COMPANY LAW

Syllabus

Unit I

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Statute prescribed

Companies Act, 2013

Books prescribed

Avatar Singh: Company Law

Books for reference

1. Gower:Company Law
2. Mayson,French&Ryamn:Company Law
3. Palmer : Company Law

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UNIT I

INTRODUCTION

Company – Definition

The word company is derived from the Latin words 'com' and 'panis'. 'Com' means with or together and 'panis' means bread. It initially referred to an association of persons who took their meals together. In the past the merchants with the intention of taking advantage of the festive gatherings discussed their business matters. With the passage of time and evolution of man and his needs business has become an important aspect of life and has acquired more complicated and complex form and hence cannot be discussed at length in festive gatherings. The rapid growth of trade, commerce and industry in modern times has brought about a number of changes in the size of a firm. With the expansion in the scale of operation of business undertakings, enterprises organized on the basis of sole proprietorship or partnership found themselves unequal to the task of meeting all the capital requirements of the present day large scale business. Thus a new form of business organization came into existence and this is called a Joint Stock Company or simply a company or corporation. A company is a corporate body and a legal entity having status and personality distinct and separate from that of the members constituting it.

Definition under the Companies Act

Section 2(20) of the Companies Act 2013 defines company as a company incorporated under this Act or under any previous company law. This definition does not reveal the distinctive characteristics of a company. Chief Justice Marshall of USA defines company as "a person, artificial, invisible, intangible, and existing only in the contemplation of the law. Being a mere creature of law, it possesses only those properties which the character of its creation confers upon it either expressly or as incidental to its very existence." Lord Justice Lindley gives a comprehensive definition of company. According to him, "a company means an association of many persons who contribute money or money's worth to a common stock and employ it in some trade or business and who share the profit and loss arising there from. The common stock contributed is denoted in money and is the capital of the company. The persons who contribute it or to whom it belongs are members. The proportion of capital to which each member is entitled is his share. Shares are always transferable although the right to transfer them is often more or less restricted."

From the definitions it can be concluded that a company is a registered association or body corporate which is an artificial legal person, having an independent legal entity, with a perpetual succession, a common seal for its signatures, a common capital comprised of transferable shares and carrying limited liability. It is called body corporate because the persons composing it are made into one body by incorporating it according to the law and clothing it with legal personality.

The expression 'body corporate' is wider than the word 'company'. A company is one of the forms of a corporation or body corporate.

"Body corporate" as defined under section 2(11) Companies Act 2013 includes a company incorporated outside India, but does not include-

1. A cooperative society registered under any law relating to cooperative societies; and
2. Any other body corporate (not being a company as defined in this Act), which the Central Government may, by notification, specify in this behalf.

The definition of body corporate under the new Act does not as such define the term but it only provides a list of associations that are excluded from its purview. Not only the statutory definition of body corporate excludes cooperatives societies from the scope of the term body corporate but a society registered under the societies Registration Act has also been held by the Supreme Court in the case of Board of trustees v. State of Delhi, AIR 1962 SC 458 not to come within the term body corporate under the companies Act, though it is a legal person of holding property and becoming member of a company.

Under the Companies Act 1956 the definition of body corporate excluded from its scope 'a corporation sole' but the Act of 2013 has removed this exception and has come up with a new concept called one person company. (Discussed later)

CHARACTERISTICS

Once registered a company comes into existence. From the day of existence the company gets the following characteristics:

1. **CORPORATE PERSONALITY**: Through registration a company acquires a legal personality, that which is independent of, and distinct from, its members. The company's liabilities are the legal responsibility of the company and the members will not be liable for the company's debts.

2. **LIMITED LIABILITY**: One of the advantages of doing business under the corporate form of legal entity is that the liability of the members is limited. A company may be company limited by shares or a company limited by guarantee. In company limited by shares, the liability of members is limited to the unpaid value of the shares. For example if the face value of a share in a company is Rs.10 and a member has already paid Rs.7 per share, he can be called upon to pay not more than rs.3 per share during the lifetime of the company. In a company limited by guarantee, the liability of members is limited to such amount as the member may undertake to contribute to the assets of the company in the event of its being wound up.

3. **PERPETUAL SUCCESSION**: A company is a stable form of business organization. Its life does not depend upon the death, insolvency or retirement of any or all shareholders or directors. Law creates it and law alone can dissolve it. Members can come and go but the company can go on forever. Thus a company has a perpetual existence, irrespective of changes in its membership.

4. **SEPARATE PROPERTY**: As a company is a legal person distinct from its members, it is capable of owning, enjoying and disposing of property in its own name. Although its capital and assets are contributed by its shareholders, they are not the private and joint owners of its property. The company is the real person in which all its property is vested and by which it is controlled, managed and disposed of.

5. **TRANSFERABILITY OF SHARES**: in a public company the shares are easily transferable. The right to transfer shares is a statutory right and it cannot be taken away by a provision in the articles of association of the company. In case f a private company the articles shall restrict the right of members to transfer their shares in companies with the statutory definition.

6. **CAPACITY TO BE SUED AND BE SUED**: a company being a body corporate can sue and be sued in its own name. To sue means to institute legal proceeding against a person or to bring a suit in a court. All legal proceedings against a company are to be instituted in its own name. In the same way, a company may bring an action in a court of law against anyone in its own name. This is an effect of registration provided under section 9 of the Companies Act 2013 i.e. once a company is incorporated through a formal procedure provided under the Companies Act it acquires several features and advantages.

TYPES OF COMPANIES

Starting a business in India requires one to choose a type of business entity. In India one can choose from five different types of legal entities to conduct business. These include Sole Proprietorship, Partnership Firm, Limited Liability Partnership, Private Limited Company and Public Limited Company. The choice of the business entity is dependent on various factors such as taxation, owner liability, compliance burden, investment and funding and exit strategy.

Sole Proprietorship

This is the most easy business entity to establish in India. It doesn't need its own Permanent Account Number (PAN) and the PAN of the owner (Proprietor) acts as the PAN for the Sole Proprietorship firm. Registrations with various government departments are required only on a need basis. For example, if the business provides services and service tax is applicable, then registration with the service tax department is required. Same is true for other indirect taxes like VAT, Excise etc. It is not possible to transfer the ownership of a Sole Proprietorship from one person to another. Assets of such firm may be sold from one person to another. Proprietors of such firms have unlimited business liability. This means that owners personal assets can be attached to meet business liability claims.

Partnership

A partnership firm in India is governed by The Partnership Act, 1932. Two or more people can form a Partnership subject to maximum of 20 partners. A partnership deed is prepared that details the amount of capital each partner will contribute to the partnership. It also details how much profit/loss each partner will share. Working partners of the partnership are also allowed to draw a salary in accordance with The

Indian Partnership Act. A partnership is also allowed to purchase assets in its name. However the owner of such assets are the partners of the firm. A partnership may/may not be dissolved in case of death of a partner. The partnership doesn't really have its own legal standing although a separate Permanent Account Number (PAN) is allotted to the partnership. Partners of the firm have unlimited business liabilities which means their personal assets can be attached to meet business liability claims of the partnership firm. Losses incurred due to act of one partner makes the other partner also liable for payment.

A partnership firm may or may not be registered with Registrar of Firms (ROF). Registration provides some legal protection to partners in case they have differences between them. Until a partnership deed is registered with the ROF, it may not be treated as legal document. However, this does not prevent either the Partnership firm from suing someone or someone suing the partnership firm in a court of law.

Limited Liability Partnership

Limited Liability Partnership (LLP) firm is a new form of business entity established by an Act of the Parliament. LLP allows members to retain flexibility of ownership (similar to Partnership Firm) but provides a liability protection. The maximum liability of each partner in an LLP is limited to the extent of his/her investment in the firm. An LLP has its owner Permanent Account Number (PAN) and legal status. LLP also provides protection to partners for illegal or unauthorized actions taken by other partners of the LLP. A Private or Public Limited Company as well as Partnership Firms are allowed to be converted into a Limited Liability Partnership.

Private Limited Company

A Private Limited Company in India is similar to a C-Corporation in the US. Private Limited Company allows owners to subscribe to its shares by paying a share capital fees. On subscribing to shares, the owners/members become shareholders on the company. A Private Limited Company is a separate legal entity both in terms of taxation as well as liability. The personal liability of the shareholders is limited to their share capital. A private limited company can be formed by registering the company name with appropriate Registrar of Companies (ROC). Draft of Memorandum of Association and Article of Association are prepared and signed by the promoters (initial shareholders) of the company. A Private Limited Company can have between 2 to 50 members with minimum share capital of Rs 1,00,000 (one lac). To look after the day to day activities of the company, Directors are appointed by the Shareholders. Minimum two Directors must be appointed to look after the daily affairs of the company. A Private Limited Company has more compliance burden when compared to a Partnership and LLP. For example, the Board of Directors must meet every quarter and at least one annual general meeting of Shareholders and Directors must be called. Accounts of the company must be prepared in accordance with Income Tax Act as well as Companies Act. Also Companies are taxed twice if profits are to be distributed to Shareholders. Closing a Private Limited Company is a tedious process and requires many months.

One the positive side, Shareholders of a Private Limited Company can change without affecting the operational or legal standing of the company. Generally Venture Capital investors prefer to invest in

businesses that are Private Limited Company since it allows great degree of separation between ownership and operations. It also allows investors to exit the company by selling shares without being liable for company affairs.

Public Limited Company

Public Limited Company is similar to Private Limited Company with the difference being that number of shareholders of a Public Limited Company can be unlimited with a minimum seven members. It is generally very difficult to establish a public limited company. A Public Limited Company can be either listed in a stock exchange or remain unlisted. A Listed Public Limited Company allows shareholders of the company to trade its shares freely on the stock exchange. A Public Limited Company requires more public disclosures and compliance from the government as well as market regular SEBI (Securities and Exchange Board of India) including appointment of independent directors on the board, public disclosure of books of accounts, cap of salaries of Directors and CEO. Like a Private Limited Company, a Public Limited Company is also an independent legal person, its existence is not affected by the death, retirement or insolvency of any of its shareholders.

Lifting the corporate veil

The doctrine of lifting the corporate veil means ignoring the corporate nature of the body of individuals incorporated as a company. A company is a juristic person, but in reality it is a group of person who are the beneficial owners of the property of the corporate body. Being an artificial person, it (company) cannot act on its own, it can act only by natural persons. The doctrine of lifting the veil can be understood as the identification of the company with its members.

The company is equal in law, to natural person. This is one of the cornerstones of Indian Company Law and has been followed since 1897 when House of Lords handed down its decision in Saloman v. Saloman & Co.An important principle of seprate legal entity has been recognized in Saloman's case which means a company has its own legal personality, distinct from its members. It allows a company to perform juristic acts in its own name, as well as to sue and to be sued. Members and Directors enjoy protection against personal liability. Although this fundamental rule has considerable influence in Company Law across the globe, including India, it cannot be absolute and must allow some exceptions, where the court may disregard the legal personality of the company. Such exceptions as there are represent haphazard refusals by the legislature or the courts to apply logic where it is to flagrantly opposed to justice, convenience or the interest of the revenue. The veil of incorporation never means that the internal affairs of the company are completely concealed from view.

Ordinarily, corporate personality of a company is to be respected. The whole law of corporations is still based on this basic principle of corporate entity. There are umpteen instances in which the courts have upheld this principle and resisted the temptation to break through the veil. But when the benefit is misused, the court is not powerless and it can lift the veil of corporate personality to see the realities behind the veil. In doing so the court sub serves the important public interest, namely, to arrest misuse or abuse of benefit conferred by

law. InUnited States v. Milwaukee Refrigerator Co.,it was held that, "a corporation will be looked upon as a legal entity as a general rule, but when the notion of legal entity is used to defeat public convenience, justify, protect fraud or defend crime, the law will regard the corporation as an association of persons.

Meaning of the Doctrine of Lifting the Corporate Veil

Lifting the corporate veil means disregarding the corporate personality and looking behind the real person who are in the control of the company. In other words, where a fraudulent and dishonest use is made of the legal entity, the individuals concerned will not be allowed to take shelter behind the corporate personality. In this regards the court will break through the corporate veil.According to the definition of Black Law Dictionary," the piercing the corporate veil is the judicial act of imposing liability on otherwise immune corporate officers, Directors and shareholders for the corporation's wrongful acts."Aristotle said, when one talks of lifting status of an entity corporate veil, one has in mind of a process whereby the corporate is disregarded and the incorporation conferred by statute is overridden other than the corporate entity an act of the entity.

When the principle is involved, it is permissible to show that the individual hiding behind the corporation is liable to discharge the obligations ignoring the concept of corporation as a legal entity. In DDA v. Skipper Construction Co. Pvt. Ltd. The Supreme Court referred to the principle of lifting corporate veil. The concept of corporate entity was evolved to encourage and promote trade and commerce but not to commit illegalities or to defraud people. The corporate veil indisputably can be pierced when the corporate personality is found to be opposed to justice, convenience and interest of the revenue or workman or against public interest.

Origin of Doctrine of Lifting of the Corporate Veil

An incorporated company has a legal entity distinct from its members from the date of its incorporation.In England the legal personality of a company was recognized in 1867 but it was firmly established in 1897 in the case of **Saloman v. Saloman & Co. Ltd.** In this case one Salomon was a boot and shoe manufacturer. His business was in sound condition and there was a substantial surplus of assets over liabilities. He incorporated a company named Saloman & Co. Ltd for the purpose of taking over and carrying on his business. The seven subscribers to the Memorandum were Saloman, his wife, his daughter and four sons and they remained the only members of the company. Saloman and two of his sons, constituted the Board of Directors of the company. The business was transferred to the company for £ 40000. In payment Saloman took 20000 shares of £ 1 each and debentures worth £ 10,000. These debentures certified that the company owned Salomon £ 10000 and created a charge on the company's assets. One share was given to each remaining member of his family. The company went into liquidation within a year.Its assets amounting to £ 6,000 were insufficient to pay the debentures in full and the ordinary creditors received nothing. The liquidator sought to have the debentures cancelled on the ground that the company was only an agent of Salomon. The unsecured creditors, on their part contended that though the company was incorporated under the Act, the Salomon & Co. Ltd. had no independent existence and it was in fact only Salomon who was the sole person behind it, he was the managing director, the other directors being his sons were under his control. Thus, in effect the company was one man

show and its existence was contrary to the spirit and meaning of the Company Law. The Salomon and Company Ltd. was incorporated complying with all the formalities which were necessary to corporate a company having a personality separated from that of its members and since Salomon was one of its members or share holders he was under no obligation to meet liabilities of the company.

The House of Lords refused these arguments on the ground that after incorporation the Salomon and Co. Ltd. became in law a different person altogether from its members with its own rights and liabilities. So, the House of Lords has made it clear that after incorporation a company is conferred on a legal entity different from the motives or conduct of its members and promoters.

The History of English doctrine can be divided into three stages:

a) 1897-1966- This period may be called as the classical veil lifting or the early experimentation period, during which the English courts experimented with different approaches of the doctrine. The House of Lords decision in Saloman's case dominated in this period.

b) 1966-1989- This period started after the Second World War and this is the interventionist period. The rules of House of Lords in Saloman's case were changed and the veil lifting was encouraged during this period.

   In Littlewoods Mail Order Stores Ltd. v. IRC,Lord Denning stated, "the doctrine laid down in Saloman's case has to be watched very carefully. It has often been supposed to cast a veil over the personality of a limited company through which the courts cannot see. But that is not true. The courts can, and often do, pull off the mask." With of wanting of any hypothesis, the sprit of the doctrine in this period can be attributed to the most influential jurist of the twentieth century.

c) 1989- The Present- The doctrine of corporate veil lifting began to be disfavoured by the courts in this period. InWoolfsan v. Strathelyed regional council,court stated that the one situation where a corporate veil could be lifted was whether there are special circumstances indicating that the company is a 'mere facade concealing the true facts.'

But the judgement of the court of appeal in Adams Vs. Cape Industry Plc leaves only three circumstances when a corporate veil can be lifted.

i) It the court in interpreting a statute or document and the statute itself is ambiguous, which would allow the court to treat a group as a single entity.

ii) If special circumstance indicate that it is a mere facade concealing the true facts, the court may lift the veil.

iii) The third exception is an application of the agency principle. Parent companies and subsidiaries are unlikely have express agency agreements and it is even difficult to prove an implied agency. Evidence is required that day to day control was being exercised by the parent company over its subsidiaries.

Indian law

The most of the provisions of Indian company law were borrowed from English law, it more or less resembles the English law. The Salomon's case has been the authority since in the decisions of the doctrine of Indian company cases.

The Supreme Court in Tata Engineering Locomotive Co. Ltd. v. State of Bihar and others,"the corporation in law is equal to natural person and has a legal entity of its own. The entity of corporation is entirely separate from that of its shareholders; it bears its own names and has seal of its own; its assets are separate and distinct from those of its members, the liability of the members of the shareholders is limited to the capital invested by them, similarly, the creditors of the members have no right to the assets of the corporation."

In **LIC of India v. Escorts Ltd,** Justice O. Chinnapa Reddy had stressed that the corporate veil should be lifted where the associated companies are inextricably connected as to be in reality, part of one concern. After the Bhopal Gas leak disaster case, the lifting of corporate veil has been escalated. Furthermore in state of UP v. Renusagar Power Company, the Supreme Court lifted the veil and held that Hindal co, the holding company and its subsidiary, Renusagar must be treated as the own source of generation of Hindalco and on that basis, Hindalco would be liable to pay the electric duty.After the decision of Renusager case, the doctrine has been considered in several cases.

Need of the Doctrine of Lifting the Corporate Veil

The theory of lifting the corporate veil becomes necessary when unscrupulous people started using the corporate veil as an instrument to conceal fraud in company's affairs. Thus, it become compulsory for the legislature and court to evolve and to lift the corporate veil and find out the person behind the company, who are the actual beneficiaries of the corporate body.

In Andhra Pradesh State Road Transportation Case the Supreme Court pointed out that a corporation has a separate legal entity is so firmly rooted in our notions derived from common law that it is hardly necessary to deal with it elaborately.

The Philosophy Behind the Doctrine of Lifting of Corporate Veil

The concept of corporate veil is a fundamental aspect of a Company Law. This is a protective device for those who exist behind the veil. Pickering says that there are two main reasons why there are exceptions to the separate entity doctrine. Firstly, he says that a company cannot all the times and in all the circumstances be treated as an ordinary independent person, e.g. a company has no mens rea and therefore is not capable of committing a crime, unless the court lifts the veil and impose the intention of the Directors or members on the company. Secondly, if there were no exception to the separate entity rule, Directors and members would be allowed to hide behind the shield of limited liability, with potentially disastrous effects. Thus, the doctrine of lifting the corporate veil is essentially used as a flexible tool to ensure justice.

The doctrine of lifting the veil has been developed as a device to avoid the hardship of the doctrine of corporate personality. It may be understood as the identification of a company with its members. In order to protect themselves from the liabilities of the company its members often take the shelter of the corporate veils. Sometimes these corporate veils are used as a vehicle of fraud, or evasion of tax. To prevent unjust and fraudulent acts, it becomes necessary to lift the veils to look into the realities behind the legal facade and to hold the individual member of the company liable for its acts.The corporate veil has been lifted by the courts and legislatures both for the interest of equity, justice and good conscience.

Doctrine Law lifting the corporate veil as such is not given in the text of Indian Company Law but could be inferred from number of provisions.

The Companies Act, 1956

The Companies Act 1956, itself provides for circumstances, when corporate veil will be lifted and the individual members or directors will be made liable for certain transactions.

1) Reduction of Membership:

Section 45 of the Act makes the members of the company severally liable for the payment of the whole debts of the company if the membership of the company is reduced below the statutory requirements i.e. two for the private company and seven for a public company. It must be noted that this section 45 does not operate to destroy the separate personality of the company, it still remains an existing entity though there may be one or more member. However, this provision applies only to members who remain as members if the company continuous with less number for a period more than 6 months after the membership falls below the statutory limits.

2) Holding and Subsidiary Company

Section 212of the companies Act, 1956 provides that in relation to financial disclosure a true and fair view of the overall position of the group is to be presented and therefore, the parent company must present financial statements of its subsidiaries as well as its own individual statement, thereby avoiding any misleading picture given by presenting only the financial statement of the parent company.However, it would be highly misleading to construe this action alone as resulting in a lifting of the corporate veil as this provision nowhere provides for the holding company being liable for the debts of its subsidiaries. Its sole object seems to be ensured accurate information about the finances of its subsidiaries.

3) Failure to Deliver Share Certificate (Section 113)

Sub section (2) of Section 113 provides that in case a company fails to deliver the share/debenture certificate within 3 months of allotment and within 2 months of application for transfer, then the company as well as every officer of the company who is at fault shall be punishable with fine upto Rs. 5000 per day till such default continues.

The Companies Act- 2013

I. Failure to return application money (Section-39)

In the case of issue of share by a company, whether to the public or by way of rights if, minimum subscription as stated in the prospectus has not been received directors shall be personally liable to return the money with interest, in case application money is not repaid within a prescribed period.

II. Misrepresentation in prospectus (Section- 34 and 35)

In case of misrepresentation in a prospectus,every director, promoter and every other person who authorize such issue of prospectus incurs liability towards those who subscribed for shares on the faith of untrue statement.

III. Fraudulent Conduct (Section 339):

Where in the case of winding-up of a company it appears that any business of the company has been carried on with intent to defraud creditors of the company or any other person, or for any fraudulent purpose, those who are knowingly parties to such conduct of business may, if the Tribunal thinks it proper so to do, be made personally liable without any limitation as to liability for all or any debts or other liabilities of the company.

CRIMINAL LIABILITY FOR MISSTATEMENTS IN PROSPECTUS

Where a prospectus, issued, circulated or distributed, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead, every person who authorities the issue of such prospectus shall be liable under section 447.

Provided that nothing in this section shall apply to a person if he proves that such statement or omission was immaterial or that he had reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was necessary. Civil liability for misstatement in prospectus:where a person has subscribed for securities of a company acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the company and every person who-

a. is a director of the company at the time of the issue of the prospectus;

b. has authorized himself to be named and is named in the prospectus as a director of the company, or has agreed to become such director;

c. is a promoter of the company;

d. has authorized the issue of the prospectus, and

e. is an expert referred to in sub section (5) of section 26,

shall, without prejudice to any punishment to which any person may be liable under section 36, be liable to pay compensation to every person who has sustained such loss or damage. Where it is proved that a prospectus has been issued with intend to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person referred to in sub sec. (1) shall be personally responsible, without any limitation of liability, for all or any of the losses or damage that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.

Punishment for Fraudulently Inducing Persons to Invest money:-any person who, either knowing or recklessly makes any statement, promise or forecast which is false, deceptive or misleading, or deliberately conceals any material facts, to induce another person to enter into, or to offer to enter into-

a.any agreement for, or with a view to, acquiring, disposing of subscribing for or under- writing, securities, or

b.any agreement, the purpose or the pretend purpose of which is to secure a profit to any of the parities from the yield of securities or by reference to fluctuation in the value of securities; or
c.any agreement for, or with a view to, obtaining credit facilities from any bank or financial institutions, shall be liable for action under section 447.

IV. Miss description of Name:-where an officer of any company signs on behalf of company any contract, bill of exchange, cheque promissory note etc. such person shall be personally liable to the holder if the name of the company is not mentioned or not properly mentioned.

Every person shall have its name printed on hundies, promissory notes, bill of exchange and such other documents as may be prescribed.

If any default is made in complying with the requirements to this section, the company and every officer who is in defaults shall be liable to a penalty of one thousand rupees for every day during which the default continues but not exceeding one lakh rupees.

Investigation into affairs of Company:-

Where the central government is of the opinion, that it is necessary to investigate into the affairs of a company-

a. on the receipt of a report of a the Registrar or Inspector under Sec.- 208
b. on information of a special resolution passed by a company that the affairs of the company ought to be investigated; or
c. In public interest,

It may order an investigation into the affairs of the company.

Establishment of Serious fraud Investigation Office-

The central government shall, by notification, establish an office to be called the Serious Fraud Investigation Office to investigate fraud relating to a company.

Investigation of Ownership of Company-

Where it appears to the central government that there is a reason so to do, it may appoint one or more inspectors to investigate and report on matters relating to the company, and its membership for the purpose of determining the true persons-

a. who are or have been financially interested in the success or failure, whether real or apparent, of the company; or

b. Who are or have been able to control or to materially influence the policy of the company.

Liability for fraudulent conduct of business:-

If in the course of the winding up of a company, it appears that any business of the company has been carried on with intend to defraud creditors of the company or any other persons or for any fraudulent purpose, the tribunal, on the application of the official Liquidator, or the company Liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare that any person, who is or has been a director, manager, or officer of the company or any persons who were knowingly parties to the caring one of the business in the manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts. or other liabilities of company as the tribunal may direct.

Liability for ultra vires acts:-

Directors and other officers of a company will be personally liable for those acts which they have done on behalf of a company if the same are ultra vires the company.

MISCELLANEOUS LAWS:

The Income Tax Act, 1961

Under the income tax act, there are some section where the principal of lifting of the corporate veil is applied. Section 178 applies to a company in liquidation. The liquidator of any company shall be personally liable for tax due from the company and remaining unpaid if he has failed to give notice to the income tax officer having jurisdiction to assesses the company of the fact of his appointment as liquidator of the company within 30 days of his becoming such liquidator or fails to set aside amounts equal to the amounts notifies to him by the income tax officer. The Income Tax officer's notice notifying the amount to be set apart by the liquidator has to issue within three months of receipt by the income tax officer of the intimation of appointment of the liquidator. The liquidator personal liability is limited to the amount notified by the Income Tax officer under section 178 (2) if so notified. This is strictly not a case of lifting the corporate

veil but one where for non- compliance with certain provisions in the I.T. Act, the liquidator is personally held liable for the tax obligations of the company in liquidation. Sec- 179 (1) of the Income Tax Act is the one provision which fit in well with the concept of a lifting the corporate veil. It provides for personal liability of directors of a private company for the taxes due from a private company and becoming irrecoverable from the company, in respect of the income of the private company for any period during which it was a private company, unless the person who was a private company, unless the person who was a director during that period proves that the ir-recoverability cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company. This is a negative provision throwing the onus on the director to prove his non- culpability.

According to section 278, where an offence under the income Tax has been committed by a company, not only the company, but also every person who, at the time of commission of the offence was in charged of and responsible to the company for the conduct of its business will also be personally liable deeming him to be guilty of such offence unless he proves that the offence was committed without his knowledge or could not be prevented in spite of all due diligence exercised by him. This does not involve the principle of lifting the corporate veil as personal guilt of the individuals is itself proved.

Foreign Exchange Regulation Act, 1973:-

Sec- 63 of this Act deems guilty for contravention of the provisions of the Act, every person in charge of and responsible to the company for its affairs.

JUDICIAL APPROACH

The theory of piercing the corporate veil cannot be ignored in the circumstances where in fraud, oppression and misconduct, etc is required to be detected by the court. These are the situations when the court will lift the corporate veil of the company with the view to examine the actual persons who stand behind the corporate mask.The doctrine of lifting the veil is a device which is developed to avoid the hardships of the doctrine of corporate personality.

The corporate veil is said to be lifted when the court ignores the company and concerns itself directly with the members or managers. In Union of India and others v. Playworld electronics private limited and another the Supreme Court held that the legislature cannot be expected to enumerate each and every device which may be used by the members of the company to evade tax etc.

It is at the discretion of the Court whether to lift the corporate veil of the corporation or not, because it depends on the different situations, but in some circumstances it is highly desirable for the Court to lift the corporate veil. There are various situations in which the judiciary has used this doctrine.

Determination of the character of the Company:

The corporate veil has been lifted by the courts to determine the enemy character of a company in time to war. The court will lift the veil for the purposes of finding out the person who in reality control the company's affairs and if the affairs of the company are found to have been controlled by enemy aliens, it will assume enemy character.

Evasion of Tax:

The corporate device is often used as a means of avoiding forms of tax. It is very difficult for the legislature to plug all the gaps in the law and thus the judiciary has to stop it. The Courts very often resort to lifting of the veil in order to find out the true intent of the company.

Bacha F. Guzdar v. Commissioner of Income tax, Bombay,In this case, the agricultural income was exempt from tax under the income tax Act. The income of a tea company was exempt to the extent of 60% as agricultural income and 40% was taxed as income from manufacture and sale of tea. The plaintiff, a member of the tea company received certain amount as dividend in respect of shares held by her in the company. She claimed that 60% of her dividend income should be exempt from the income tax being an agricultural income. The Supreme Court rejected the argument of the plaintiff and held that although the income in the hands of the company was partly agricultural, yet the same income when received by the shareholders as dividend could not be regarded as agricultural income. .CIT v. Associate Clothiers Ltd.in this case a company was incorporated by certain assess who held all its shares. Thereafter the assess sold certain premises to the company. The question arose whether the difference between the selling price and the cost of the property should be regarded as the profits received by the assesses and therefore, taxable income because the transfer of the premises by the assesses was merely a transfer from self to self and it was not a commercial sale from person to another person, but the contention of the assesses was rejected by the Court on the ground that a company after incorporation becomes a legal person district from its shareholders and thus the sale of the premises by the assesses to the company should be regarded as a sale from one entity to another entity and the difference between the selling price and the cost of the property should be treated as the taxable income in the hands of the assesses.

Fraud or Improper Conduct:

Where the medium of a company has been used for committing fraud and improper conduct, courts have lifted the veil and looked at the realities of the situation.. InDelhi Development Authorityv. Skipper Construction Company Pvt Ltd.the DDA ad entered into a contract for construction on a piece of land. After prolonged delays and problems, the DDA had to finally order the construction company to stop the construction and hand over the land to DDA. The company inspite of a Court order to this effect, had already collected various monies from parties, agreeing to sell the space and had infact, sold the same space to more than one party in the situations. The Supreme Court stated that this was a fit case for lifting of the corporate veil and the veil must be lifted when the device of incorporation is being used for some

illegal or improper purpose. The Court thus found the individual members behind the corporate body liable for the acts that they attempts to carry on through the guise of the company.

Avoidance of Welfare Legislation:

Where it was found that the sole purpose for the formation of the new company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the supreme court uphold the piercing of the veil to look at the retranslation.

In Cases of Economic Offences:

InSantanu Ray v. Union of India,it was held that in case of economic offences a Court is entitled to lift the veil of corporate entity and pay regard to the economic realities behind the legal facade. In this case, it is alleged that the company had violated section 11(a) of the central excises and salt act, 1944. The Court held that the veil of corporate entity could be lifted by adjudicating authorities so as to determine as to which of the directors was concerned with the evasion of the excise duty by reason of fraud, concealment or willful mis-statement or suppression of facts or contravention of the provisions of the act and the rules made there under.

Agency:

According to this classification, the Courts examine whether or not the company is acting as an agent of some of its shareholders or other members of the company. In such a situations the veil may be lifted to make these persons liable for the companies acts.

InSmith Stone and knight v. Birmingham Corporation,a company required a partnership concern and registered it as a company and continued to carry on the acquired business as subsidiary company. The parent company held all the shares except five which were held in trust for the company by its directors. When the Birimingham corporation compulsorily acquired the premises for the subsidiary, the parent plaintiff corporation claimed compensation. The contention for the respondent, however was that the proper party for claiming compensation was the subsidiary and not the parent corporation as they were two separate legal entities. The Court held that the subsidiary company was nothing more than an agent of the parent company, and therefore all the acts of the subsidiary were attributable to the parent company. The subsidiary, not operating in its own behalf but on that to the parent was sufficient reason for the parent to claim compensation on behalf of the subsidiary. Thus though the separate legal entity of the subsidiary was recognised. The agency principle was applied to identify the parent company and its subsidiary.

Conclusion

This device merely seeks to strike a balance between the interest of the public and the concept of a separate personality. Thus the device is essentially used as a flexible tool to ensure justice. It would be defeat the object of the device if it were to be applied rigidly with no scope at all left for judicial discretion. There can

be no single unifying principle that underlines the decisions of the Courts. Although on ad hoc explanation may be offered by a Court which so decides, there is no principle approach to be derived from the authorities. Thus it is not possible to evolve a rational, consistent and inflexible principle which can be invoked in determining the question as to whether the veil of corporation should be lifted or not. Courts and Legislature must adopt a single set of statutory standards as to when limited liability should be disregarded. This will provide the certainty in this area of law and will allow uniformity, applying the doctrine of lifting the corporate veil.

KINDS OF COMPANIES

There are various kinds of companies: Private Company, Public Company, One Man Company and a Foreign Company. A Company can be classified on the basis of the mode of incorporation as Statutory and Registered Company, on the basis of the number of members as Private Company and Public Company and on the basis of the liability of members as Company Limited by Shares, Company Limited by Guarantee and Unlimited Company. Various other types of companies, such as Licensed Company, Family Company, Foreign Company, Government Company, Holding Company and Illegal Company are also discussed in detail in this lesson.

Companies According to Mode of Incorporation

A company may be incorporated[1] either by a charter or by a special Act of legislation or under the Companies Act 1956. If a company is incorporated by issuing a charter it is called a Chartered Company. If a Special Act of Legislation incorporates the company then it is called a Statutory Company and if it is incorporated under the Companies Act then it is called an Incorporated Company.

Chartered Company

A company when incorporated by issuing a charter by the King or the Queen it is called a Chartered Company. Some of the chartered companies are The East India Company, B.B.C. (British Broadcasting Corporation) and The Bank of England

Statutory Company

These companies are formed with the objective of carrying out businesses, which are in the interest of the nation as a whole. The Reserve Bank of India, The Unit Trust of India and Life Insurance Corporation of India are examples of statutory companies. They have been incorporated by Special Acts passed by the legislature. The Acts define the powers to be exercised by the company; therefore these Companies are not required to have a Memorandum of Association, nor do they have to use the word 'limited' as part of their name. The provisions of their respective Acts govern them. Their accounts are audited under the supervision and control of The Auditor General of India

Registered / Incorporated Company

An Incorporated Company can also be called a Registered Company. These companies are registered under the Companies Act, 1956. The registered companies can further be classified into various types. They can be classified either on the basis of the number of members or on the basis of the liability of members.

Companies on the Basis of the Number of Members

A registered company can be classified as a private company or a public company on the basis of the number of members.

Private Company

According to section 3(1) (iii), a 'private company' is a company which has a minimum paid up capital of Rs. One lakh or such higher paid up capital as may be prescribed, and by its articles of association:

1. Restricts the right of the members to transfer shares.
2. Limits the number of its members to 50. The members do not include persons who are in the employment of the company or were previously in the employment of the company.

   Prohibits inviting public to subscribe for shares or debentures.

3. Prohibits any invitation or acceptance of deposits from persons other than its members, directors or their relatives.

According to The Companies (Amendment) Act, 2000 'every private company existing on the date of commencement of this Amendment Act and having a paid up capital of less than Rs. one lakh shall, within a period of two years, increase its paid up c

Public Company

According to section 3(1) (iv), as amended by the Companies (Amendment) Act, 2000, a "public Company" means:

1. A company, which is not a private company.In other words a public company is one which:

1. Does not restrict the transfer of shares.
2. Does not limit the number of members.
3. Invites the public for the subscription of its shares and debentures.
4. Invites or accepts deposits from the public.

A company, which has a minimum paid up capital of Rs. five lakhs or such higher paid up capital as may be prescribed from time to time. According to The Companies (Amendment) Act 2000, 'every public

company existing on the date of commencement of this amendment and having a paid up capital of less than Rs. five lakh shall, within a period of two years, increase its paid up capital to Rs five lakh. In case the company fails to enhance the paid up capital to Rs. five lakh, the company shall be deemed to be a 'defunct company' under section 560 and its name shall be struck off from the register of companies maintained by the Registrar of Companies'.

A private company which is a subsidiary of a public company. By becoming the subsidiary of a public company the basic characteristic of a private company are not altered. The private company is treated as a public company in relation to the other provisions of the Act but not with reference to its basic characteristics. All the provisions in terms of section 3 (1) (iii) continue to govern the affairs of the company even though it is a subsidiary of a public company.

Illustration:

Meeta Private Limited was a subsidiary of Geet International Ltd., which was a public limited company. Seeta, who was a member of Meeta Company, held 50 shares of the company and wanted to transfer her shares to her friend Anu. Although Meeta's company, by virtue of being a subsidiary of Geet International, was a public company, its characteristics were still those of a private company. Hence Seeta could not transfer her shares to her friend Anu.

Exemptions and Privileges of a Private Company

There are certain advantages which a private company has over a public company. According to the Companies Act 1956, these advantages are called exemptions and privileges which are enjoyed by a private company. These privileges and exemptions are as follows:

1. Just two persons can form themselves into a company (section 12)
2. The Company can commence business immediately on incorporation as it does not require to obtain the certificate for the commencement of business to start business (Section 149(7)).
3. It can function with only two directors (section 252 (2)) At the time of incorporation the directors are not required to file with the Registrar of Companies, their consent in writing to act as directors and their undertaking to take up qualification shares, if any (section 266 (5)).
4. The company need not prepare and file 'prospectus' or 'statement in lieu of prospectus' with the Registrar (section 70 (3)).
5. It can proceed to allot shares without waiting for a 'minimum subscription' (section 69).
6. It need not hold a statutory meeting and file a statutory report (section 165).
7. The right of pre-emption does not apply to it. It is free to allot new issues (further shares) to outsiders and not to its existing shareholders.

8. It need not comply with the provisions and restrictions applicable to the management (directors, managing directors or managers) of a public company.

9. A life Director appointed on or before 1st April, 1952, cannot be removed by the company in a general body meeting (section 284).

10. The restrictions on inter-corporate loans and investments do not apply to it (section 372A).

11. It can keep its accounts secret. The copies of the Profit and Loss Account and the Balance Sheet filed with the Registrar are not open for inspection to a non-member (section 220).

12. It need not follow the provisions of section 171 to 186 relating to general meetings, procedure of voting etc. but can make its own regulations by its articles in these respects (section 170).

13. The quorum for a general meeting of shareholders is two persons personally present, unless provided otherwise in the articles (section 174 (1)).

15. It need not keep an index of members (section 151).

Distinction between a Private and a Public Company

There are several distinctions between a private and a public company which are given in Table

Basisof Distinction	Private Company	Public Company
Minimum number of members	Two	Seven
Maximum number of members	Fifty	No limit
Minimum number of directors	Two	Three
Transfer of shares	Restriction on transfer of shares	Shareholders can transfer shares freely without restriction
Public subscription	Prohibits invitation to the public to subscribe for any shares or debentures	Invites the public for subscription to its shares and debentures
Public deposits	Prohibits invitation or acceptance of deposits from the public	Invites deposits from the public
Commencement of business	Can commence business soon after getting the Certificate of Incorporation	Can commence business only after getting the Certificate of Commencement of Business
Prospectus	Need not prepare and file a prospectus or a statement in lieu of the prospectus	Has to prepare and file a prospectus or a statement in lieu of the prospectus
Minimum subscription	Can allot shares to the public without waiting for a minimum total amount of subscription	Can allot shares to the public only after raising a minimum total amount of subscription
Statutory meeting	Is not required to hold a statutory meeting	Is required to hold the statutory meeting after one month and before six months from the date of obtaining the certificate to commence business
Management (Managerial personnel)	Has freedom with regard to the appointment of management (managerial personnel)	Has to comply with certain provisions and restrictions relating to the appointment of the management
Managerial Remuneration	No restriction on the remuneration of the personnel	The maximum remuneration is fixed at 11 % of the annual profits
Index of members	Not required to keep an index of members	Has to keep an index of members if the number of members exceeds fifty

Conversion of a Private into a Public Company

A private company can be converted into a public company by either of the following two ways:

1. Automatically
2. Deliberately

*Automatic conversion:*A private company automatically converts into a public company, by the operation of law when it makes a default in complying with the essential statutory requirements as laid down in section 3 (1) (iii) of the Companies Act 1956. The default can be made in any one of the following circumstances:

1. The company's membership exceeds 50.
2. The company gives permission for free transfer of shares.

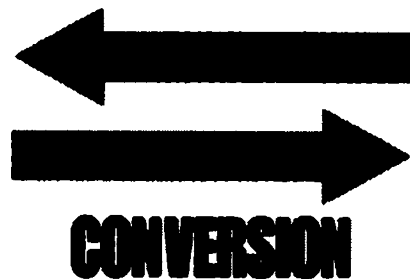


Figure: Conversion of Private into a Public Company

3. The company invites the public to subscribe to its shares or debentures.
4. The company invites or accepts deposits from the public.

The Company Law Board, if it so wishes, can relieve the company from being treated as a public company on an application made by the company or any interested person if it is of the opinion that the default was made due to an accident or some other justifiable cause.

Further, a private company which becomes a public company need not comply with any legal formality, and if the company so wishes, it can still retain the characteristics of a private company, i.e. it can continue to have only two members and two directors.

Deliberate conversion: When a private company deletes from its articles the four compulsory restrictions (as per section 3 (1) (iii)) by passing a special resolution , it becomes a public company, and within thirty days of passing the resolution, a copy of the altered articles and a copy of the prospectus or a statement in lieu of prospectus has to be filed with the Registrar. Further the company has to increase the number of its members to at least seven and the number of directors to at least three. Also it has to increase its paid up capital to at least five lakhs rupees if its existing capital is less than that and has to delete the word private from its name.

A decision reached by a majority i.e. members three times in favor than those in disfavor voting in person or by proxy at a general meeting.

Conversion of a Public into a Private Company

A public company has to pass a special resolution to alter its articles of association in order to incorporate the four restrictions imposed upon a private company

section 3 (1) (iii). A copy of the altered articles has to be filed with the Registrar of Companies within 30 days of the passing of the resolution and the sanction of the central government has to be obtained for the altered article. The company becomes a private company from the date on which the Central Government gives the order of approval of the altered articles. Within thirty days of the receipt of the approval from the Central Government, copies of the altered articles and the Central Government's letter of approval have to be filed with the Registrar.

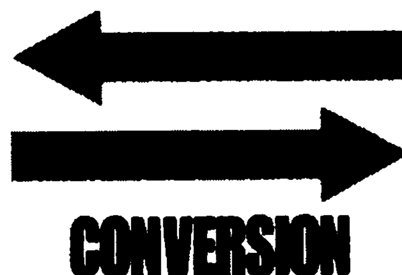


Figure: Conversion of Public into a Private Co

Further the company has to reduce its members if the total number of its members is more than fifty and has to add the word 'Private' to its existing name.

Companies on the Basis of the Liability of Members

On the basis of liability, companies can be classified into three types, as follows:

1. Company limited by shares
2. Company limited by guarantee
3. Unlimited company

Company Limited by Shares

Most of the companies in India are companies limited by shares. According to section 12(2)(a) of the Companies Act, "a company having the liability of its members limited by the memorandum, to the amount, if any, unpaid on the shares respectively held by them is termed a company limited by shares. In such companies the extent of its liability is determined by the face value of its shares. Unless the articles provide for it there is no liability on the shareholders to pay any balance amount due on the shares, except when the calls are duly made while the company is still in existence or when the company is being wound up.

Illustration

Ram Gopal purchases 50 shares of Rs.100 each of ABL Company Ltd. He pays the application money of Rs. 40 per share and the allotment money of Rs. 20 per share. The company makes the first call and Ram Gopal pays the first call money of Rs. 20 per share. In all he pays Rs 80 per share for the 50 shares held by him. Ram Gopal is not liable to pay the balance of Rs. 20 per share unless the company makes the final call. The company does not make the final call hence Ram Gopal is not liable to pay the unpaid money of Rs. 20 per share on the 50 shares held by him.

Illustration:

Ram Gopal purchases 50 shares of Rs.100 each of ABL Company Ltd. He pays the application money of Rs. 40 per share and the allotment money of Rs. 20 per share. The company makes the first call and Ram Gopal pays the first call money of Rs. 20 per share. In all he pays Rs 80 per share for the 50 shares held by him. After 25 years the company is declared insolvent and undergoes winding up. At the time of winding up Ram Gopal is liable to pay the unpaid amount on the shares held by him. Hence Ram Gopal pays Rs. 20 for each of the 50 shares held by him.

Company Limited by Guarantee

According to section 12(2)(b) "a company having liability of its members limited by the memorandum to such amount as the members may respectively undertake by the memorandum to contribute to the assets of the company in the event of its being wound up is termed a company limited by guarantee."

Figure: Company Limited by Gurant

Illustration:

Ram Gopal is a shareholder of ABL Company Ltd. He holds fully paid up shares. This means that he has already paid Rs 5000 for 50 shares of Rs. 100 each held by him. He also gives a guarantee to the company that his liability is Rs. 6000. After 40 years the company undergoes insolvency and is wound up. As per the guarantee given by Ram Gopal, he is liable to pay Rs. 1000 more to the company.

Unlimited Company

According to Section 12(2)(c) " a company having no limit on the liability of its members is an unlimited company" and according to Section 27(1) the articles of association of an unlimited company must state the number of members with which the company is to be registered, and, if the company has share capital, the amount of share capital with which the company is to be registered because an unlimited company may or may not have share capital. The members of such a company are liable to pay the whole amount of the company's debts. The creditors can enforce their claim against the company by instituting the proceedings of winding up and then the official liquidator calls upon the members to discharge the debts of the company without any limit.

Illustration:

Ram & Shyam Company is an unlimited company consisting of 10 members. Each member holds 100 fully paid up shares of Rs. 100 each. After 5 years the company goes into liquidation. The Company owes its creditors Rs. 1 Crore. At the time of winding up, irrespective of the value of shares held by the members, they together are liable to pay Rs. 1 Crore as their liability is unlimited.

Other Types of Companies

There are some other types of companies which are discussed below:

Company not for profit / Licensed Company

Section 25 of the Companies Act deals with licensed companies. Such companies obtain the license from the central government and then register themselves under the Companies Act. Such companies are formed to promote art, religion or any other social and useful purpose for the welfare of the society. They do not use their profits to pay dividends to their members; instead they apply their profits (income) to promoting the objective for which the company is formed. They enjoy certain exemptions and privileges as compared to other limited companies. For example they can exclude the words 'limited' or 'private limited' from their names. Unlike other companies they need not pay the stamp duty on the memorandum and articles of association while getting themselves registered. They may be a public or a private company and may or may not have a share capital. They need not comply with the requirement of the minimum paid up capital of Rs. one lakh for a private company and Rs. five lakh for a public company. However the central government may at anytime revoke the license of the company if it finds that the fundamental conditions for which the company has been established are not being met.

Illustration:

Five friends Ram, Ghanshyam, Raghu, Shweta and Sweety were in their final year of MBBS and had a plan of starting their own hospital. After attaining their degrees they applied to the central government to start a hospital in a rented accommodation in Delhi by the name of 'Chikitsa'. They soon got the license and thereafter registered themselves as a private limited company without adding the name private or limited to the name 'Chikitsa'.

Max India limited is a public limited company which was founded in the year 1985. It has hospitals in Delhi and its adjoining areas by the name of 'Max Medcentre' and 'Max Hospital'.

Figure: Company not for Profit

One Man Company

One man company has only a single (one) shareholder who is also the director. Such companies are not formed in India. The Companies Bill 2009 has a provision on "one man company".

Foreign Company

According to Section 591(1) of the Companies Act a foreign company is a company incorporated outside India but having a place of business in India.

The PepsiCo Company is a foreign company which was incorporated in New York, USA in the year 1898. Today it has its place of business in many countries around the globe. In India it gained entry in the year 1988 and has been doing business here since then.

Figure: Foreign Company

Government Company

According to Section 617 of the Companies Act, a Government Company is defined as "any company in which not less than 51 per cent of the paid up share capital is held by the Central Government or by the State Government or Governments or partly by the Central Government and partly by one or more State Governments and includes a company which is a subsidiary of a Government Company". As the government owns these companies, in India such companies are called public sector undertakings or a company in the public sector (government sector).

Figure: Bharat Sanchar Nigam Limited

Some of the famous government companies in India are the BSNL and the Indian Oil Corporation. BSNL or the Bharat Sanchar Nigam Limited is a telecommunication company. It is also known as India Communications Corporation Limited.

Indian Oil Corporation is an Indian Public-sector petroleum company. It is India's largest commercial enterprise.

Figure: Indian Oil Corporation

Holding Company and Subsidiary Company

When one company controls the management of another company the former is called a holding company and the latter is called a subsidiary company. A company is a subsidiary of another company if it fulfils any of the following conditions (Section 4)If the other company has a majority on the board of directors of this company.

Illustration:

Ruksar India limited, a Delhi based company, comprises five directors. Out of the five directors, three are board members of Angel Company Limited, which is a Bombay based company. Angel Company has eight directors. As the majority of the directors (three out of five) of Ruksar India Limited are also directors of the Angel Company, the former company becomes a subsidiary of the latter.

If the other company holds more than half the nominal value of this company's equity share capital.

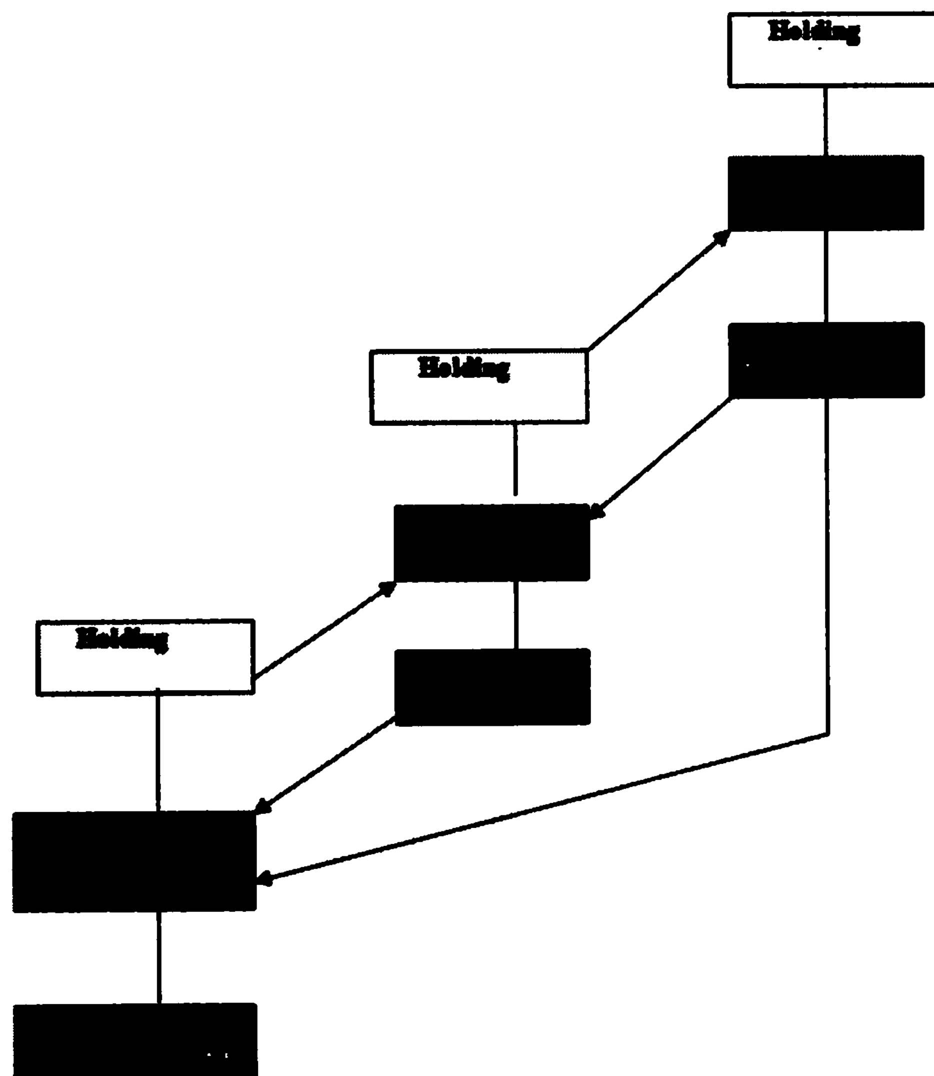
Illustration:

Ruksar India Limited, a Delhi based company has a share capital of Rs. 5,00,000 (5000 shares @ Rs.100 each). Angel Ltd which is a Bombay based company owns 3000 shares of Ruksar India Limited. As Angel owns 60% of the share capital of Ruksar India Limited, the latter is the subsidiary of Angel Company.

If this company is a subsidiary of a third company which is a subsidiary of the controlling company.

Illustration:

Ruksar, a Delhi based company, has a share capital of Rs. 5,00,000 (5000 shares @ Rs.100 each). Angel Ltd, a Bombay based company, owns 3000 shares of Ruksar Company. Angel Limited has a share capital of Rs 10,000,00 (10000 share @ Rs.100 each). Another company by the name of Spider Limited operating in Chennai holds 7000 shares of Angel Limited. Thus Spider Limited holds more than half of the nominal value of Angel Company's share capital and Angel Company owns more than half of the nominal value of Ruksar Company's share capital. Therefore Angel Company becomes the subsidiary of Spider Company and Ruksar Company becomes the subsidiary of Angel Company. As a result Ruksar Company becomes the subsidiary of Spider Company.



What is One Person Company (OPC)?

The concept of One Person Company [OPC] is a new vehicle/form of business, introduced by The Companies Act, 2013 [No.18 of 2013], thereby enabling Entrepreneur(s) carrying on the business in the Sole-Proprietor form of business to enter into a Corporate Framework.

One Person Company is a hybrid of Sole-Proprietor and Company form of business, and has been provided with concessional/relaxed requirements under the Act.

Features of One Person Company (OPC)

1. **Only One Shareholder:**

Only a natural person, who is an Indian citizen and resident in India shall be eligible to incorporate a One Person Company. *Explanation:* The term "Resident in India" means a person who has stayed in India for a period of not less than 182 days during the immediately preceding one calendar year.

2. **Nominee for the Shareholder:**

The Shareholder shall nominate another person who shall become the shareholders in case of death/incapacity of the original shareholder. Such nominee shall give his/her consent and such consent for being appointed as the Nominee for the sole Shareholder. Only a natural person, who is an Indian citizen and resident in India shall be a nominee for the sole member of a One Person Company.

3. **Director:**

Must have a minimum of One Director, the Sole Shareholder can himself be the Sole Director. The Company may have a maximum number of 15 directors.

Terms and Restrictions of OPC

1. A person shall not be eligible to incorporate more than a One Person Company or become nominee in more than one such company.
2. Minor cannot shall become member or nominee of the One Person Company or can hold share with beneficial interest.
3. An OPC cannot be incorporated or converted into a company under Section 8 of the Act. [Company not for Profit].
4. An OPC cannot carry out Non-Banking Financial Investment activities including investment in securities of any body corporate.
5. An OPC cannot convert voluntarily into any kind of company unless two years have expired from the date of incorporation of One Person Company, except threshold limit (paid up share capital) is increased beyond Rs.50 Lakhs or its average annual turnover during the relevant period exceeds Rs.2 Crores i.e., if the Paid-up capital of the Company crosses Rs.50 Lakhs or the average annual turnover during the relevant period exceeds Rs.2 Crores, then the OPC has to invariably file forms with the ROC for conversion in to a Private or Public Company, with in a period of Six Months on breaching the above threshold limits.

Steps to Incorporate One Person Company (OPC)

1. Obtain Digital Signature Certificate [DSC] for the proposed Director(s).
2. Obtain Director Identification Number [DIN] for the proposed director(s).
3. Select suitable Company Name, and make an application to the Ministry of Corporate Office for availability of name.
4. Draft Memorandum of Association and Articles of Association [MOA & AOA].
5. Sign and file various documents including MOA & AOA with the Registrar of Companies electronically.
6. Payment of Requisite fee to Ministry of Corporate Affairs and also Stamp Duty.
7. Scrutiny of documents at Registrar of Companies [ROC].
8. Receipt of Certificate of Registration/Incorporation from ROC.

UNIT II
FORMATION

Incorporation is the legal process used to form a corporate entity or company. A corporation is a separate legal entity from its owners, with its own rights and obligations. Corporations can be created in nearly all countries in the world and are usually identified as such by the use of terms such as "Inc." or "Limited" in their names.

For the purpose of formation of a company there must be a process and that involves several stages. The first stage in the process is the promotion. At this stage the idea of carrying on a business is conceived by a person called promoters. For the incorporation of company various formalities are required to be carried out. The promoters perform these function and bring the company into existence. A promoter conceptualizes the idea of a company and the purpose of its formation.

1. CONCEPT OF PROMOTER:

Before look upon the term *'Promoter'* we have to know first of all the meaning of the term *'Promotion'*. So, *'Promotion'* is a term of wide import denoting the preliminary steps taken for the purpose of registration and flotation of the company. And the persons who assume the task of promotion are called *'Promoters'*. A promoter may be individual, syndicate, association, partner or company. It is the Promoter who undertakes does and goes through all the necessary & incidental requirements keeping in view the object of proposed company in order to bringing to existence as such incorporated company.

1.1. Meaning:

So far as meaning of promoter is concerned, it means A person who involves in the promotion the company. A promoter is a person who does all necessary preliminary work, incidental to the formation or promotion of the company. To be a promoter one need not necessarily be associated with the initial formation of the company; one who subsequently helps to arrange floating of its capital will equally be regarded as a promoter.

1.2. Definition:

The expression 'promoter' has not been defined under the companies Act, although the term is used expressly in sections 2(69), 35, 39, 40, 300, and 317 of the New company Act, 2013. Even in English law, no general statutory definition of 'Promoter' is available.

As per section 2(69) of the Act, 2013 defines the term 'Promoter', it means a person-

(a). who has been named as such in a prospectus or is identified by the company in the annual return to in section 92; or

(b). who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

(c). in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act:

Provided that nothing in sub-clause (c) shall apply to a person who is acting merely in a professional capacity;

So, in other words we can defines the expression 'promoter' to mean a promoter who has a party to the preparation of prospectus or of a portion thereof containing the untrue statement, but does not include any person by reason of his acting in a professional capacity in procuring the formation of the company.

Certain attempts have been made by the Judiciary to define the term 'promoter'. Cockburn C.J., in the case of *Twycross v. Grant*, described a 'Promoter' as "one who undertakes to form a company with reference to a given project, and to set it going, and who takes the necessary steps to accomplish that purpose".

In USA, securities Exchange Commission Rule 405(a) defines a promoter as a person who, acting alone or in conjunction with other persons directly or indirectly takes the initiative in founding or organizing the business enterprise.

1.3. Types of Promoter:

"A promoter is the one who envisages an idea for setting up a particular business at a given place and carries out a variety of formalities required for starting a business." A promoter is the one who envisages an idea for setting up a particular business at a given place and carries out a variety of formalities required for starting a business. A promoter may be an individual, a firm, an association of persons or a company.

The promoters may be professional, occasional, financial or managing promoters. ***Professional promoters*** handover the company to the shareholders when the company starts. Unfortunately, such promoters are very scarce in the developing countries.

They have played an important role in many countries and helped the business community to a great extent. In U.K. Issue house, in U.S. Investment Bank and in Germany,

Joint Stock Banks have played the role of promoters very significantly.

Occasional promoters are those whose main interest is the floating of companies. They are not in promotion work on regular basis but take up promotion of some companies and then go to their earlier profession. For example, engineers, lawyers etc. may float some companies.

Financial promoters do the task of promoting the financial institutions. They generally take up this work when financial environment is favorable at the time. ***Managing*** promoters played a significant role in promoting new companies and then got their managing agency rights.

A promoter is neither an agent nor a trustee of the company as it is a non-entity before incorporation. Some legal cases have tried to spell out the standing of promoters.

FUNCTIONS OF PROMOTER

A promoter plays a very important role in the formation of a company. A promoter may be an individual, an association or a company. In their capacity as promoters, they perform the following functions in order to incorporate a company and to set it going. To originate the scheme for formation of the company:

- Promoters are generally the first persons who conceive the idea of business.
- They carry out the necessary investigation to find out whether the formation of a company is possible and profitable.
- Thereafter they organize the resources to convert the idea into a reality by forming a company or in other words we can say that it is the promoter –
- who settles the name of the company thereby ascertain the name will be acceptable by the registered of the office;
- who settles the content or details as to the Articles of the companies; (here, articles implies Articles of association & Memorandum of association),
- who nominates the directors, bankers, auditors and etc.;
- who decides the place where registered office (head office) have to be situated;
- who prepare the Memorandum of Association, Prospectus and other necessary documents and file them for incorporation.

In this sense, the promoters are the originators of the plan for the formation of a company. To secure the cooperation of the required number of persons willing to associate themselves with the project: The promoters, in accordance with whether they want to incorporate a private or public company, try to secure the co-operation of persons needed to from the company. Minimum number of members required to from a public company is seven and that for a private company the minimum number is two. Depending upon the form chosen, the promoters may decide upon the number of primary members. To seek and obtain the consent of the persons willing to act as first directors of the company: The company has a system of representative management and is managed by individuals appointed as directors. The first directors of the company are, however, generally appointed by the promoters. The promoters seek the consent of some individual whom they seem appropriate so that they agree to be the first directors of the proposed company. To settle about the name of the company: The promoters have to seek the permission of the Registrar of companies for selecting the name of the company.[x]

3. PRE-CONTRACTUAL AND POST CONTRACTUAL OBLIGATIONS WITH RESPECT TO: STATUS, DUTIES & LIABILITIES.

Legal status of promoter is concerned it is undefined. So, legal status of promoter has not been determined and specified by the statute. His position is incapable of being defined. He cannot considered as an agent, an employee and trustee of the companies. The status of the promoter is generally terminated when the board of directors has been formed and the board starts governing the company. Chronologically, the first persons who control or influence the company, and it they who take the necessary steps to incorporate it, to provide it with share and loan capital and acquire the business or property which it, to provide it with share and loan capital and acquire the business or property which it is to manage. When these things are done, they handover the control of the company to its directors, who are often themselves under a different name.

Duties:

The early companies Acts contained no provisions regarding the liabilities or duties of promoters, and even today legislation is largely silent on the subject, merely imposing liability for untrue statement in listing particulars or prospectuses to which they are parties.

There are some duties or liabilities with respect to Promoter has been also provides by the statute: The promoters have certain basic duties towards the company formed :-

- As we know that Promoters have been described to be in a fiduciary relationship (i.e., relationship of trust and confidence) with the company. This relationship of trust and confidence requires the promoter to make a full disclosure of all material facts relating to the formation of the company. He must not make any secret profit out of the promotion of the company. Secret profit is made by entering into a transaction on his own behalf and then sell to concerned property to the company at a profit without making disclosure of the profit to the company or its members. The promoter can make profits in his dealings with the company provided he discloses these profits to the company and its members. What is not permitted is making secret profits i.e. making profits without disclosing them to the company and its members.
- He must make full disclosure to the company of all relevant facts including to any profit made by him in transaction with the company.

Liabilities of promoter:

A promoter can be compelled by the company to hand over any secret profit which he has made without full disclosure to the company. The company can also sue for the rescission of the contract of sale by the promoter where the promoter has not disclosed his interest therein.

A promoter is subject to the following liabilities under the various provisions of the companies Act:

- Section 56 lays down matters to be stated and reports to be set out in the prospectus. He may be held liable for the non-compliance of the provisions of this section.

- Under section 62, a promoter is liable for any untrue statement in the prospectus to a person who has subscribed for any shares or debentures on the faith of the prospectus. Such a person may sue the promoter for compensation for any loss or damage sustained by him.

- Besides civil liability, the promoters are criminally liable under section 63 for the issue of prospectus containing untrue statements. Section 68 imposes severe penalty on promoters who make untrue and deceptive statements in a prospectus with a view to obtaining capital.

- A promoter may be liable to public examination like any other director or officer of the company if the court so directs on a liquidators report alleging fraud in the promotion or formation of the company.

- A company may proceed against a promoter on action for deceit or breach of duty under section 543, where the promoter has misapplied or retained any property of the company or is guilty of misfeasance or breach of trust in relation to the company.

So, promoter is liable to the original allottee of shares for mis-statements contained in the prospectus. It is clear that his liability does not extend to subsequent alloottees. He may also be imprisonment for a term which may extent to 2 years or may be punished with fine up to Rs. 50,000 for such untrue statements in the prospectus.

4. POSITION OF PROMOTER IN INDIA IN RELATION TO COMPANY.

Position of the promoter is fiduciary concerning the company which being the promotes his position is quasi legal. A promoter is neither a trustee nor an agent of the company which he promotes because there is no trust or principal in existence at the time of his efforts. But certain fiduciary duties, like an agent, have been imposed on him under the Companies Act. As such he is said to be in & fiduciary position (a position full of trust and confidence) towards the company and the original allottee of shares. Consequently, a promoter must make full disclosure of the relevant facts, including any profit made.

He must not make any secret profits out of the transactions he makes on behalf of the company. It is to be observed that it is not the profit made by the promoter which the law forbids, but the non-disclosure of it. If full disclosure is made to an independent Board of Directors or to the shareholders as a body (and not to a selected few), the profit is permissible. A promoter vendor cannot evade his liability of disclosure of profits by disclosing to a Board of Directors who is mere nominees of his own, or in his pay. A good illustration on the point is to be found in *Gluckstein vs. Barnes.* In this case, a syndicate of persons was formed to purchase the Olympia Company and to promote and register a company to which the Olympia property was to be resold. At that time the Olympia Company was in a bad shape. The syndicate first bought the debentures of the Olympia Company at a discount. Then they brought the Company for £ 1,40,000. Out of this money, provided by them, the debentures were repaid in full and a profit of £ 20,000 was made thereon. They promoted a new company and sold Olympia to it for £ 1,80,000. The profit of 40,000 was revealed in the, prospectus, but not the profit of £ 20,000. It was held that the profit of £ 20,000

was a secret profit made by the syndicate as promoters of the company, and they were bound to pay it to the company which was at that time in liquidation. On behalf of the syndicate it was argued that they had in fact made a proper disclosure, but it was turned down on the plea that disclosure made by them in the capacity of vendors to themselves in the capacity of directors of the purchasing company was not sufficient. The disclosure ought to be to an independent Board or to all shareholders by means of a prospectus.

4.1. Prior to incorporation of the company:

Sometimes, contracts are made on behalf of a company even before it is duly incorporated. But no contract can be bind a company even before it becomes capable of contracting by incorporations. So, a pre-incorporation contract is a contract entered into by a company before it is incorporated, which is obviously not possible. Ratification of a pre-incorporation contract is not possible since ratification acts retrospectively. A person cannot entered into a contract on behalf of a company before the company incorporated or born or came into existence. However, it may be necessary to bind an outsider with a contract before the company is incorporated. Hence, the need for pre-incorporation contract.

The true legal position in respect of pre-incorporation contracts may be discussed under the following two heads:-

- Position before 1963(i.e., before passing of Specific Relief act, 1963), and
- Position since 1963.

Position before 1963:

1. A pre-incorporation contract never binds a company since a person (legal or juristic cannot contract before his or its existence and a company before incorporation has no legal existence. Another reason is that promoters are proverbially profuse in their promises and if the corporation were to be bound by them, it would be subject to many unknown, unjust and heavy obligations).

2. Even where there is a request purported to enforce such a contract, the company cannot be found because ratification is not possible as the ostensible principal did not exist at the time the contract was made. In *re English and colonial Produce Company case*, a solicitor was engaged to prepare the necessary documents and obtain the registration of a company. He paid the registration fee and incurred the certain expenses incidental to registration. It was held in this case that the company was not liable or bound to pay for his services and expenses.

- The company is also not entitled to sue on a pre-incorporation contract. As it was held in the case of *Natal land and colonisation company v. pauline colliery syndicate* that the syndicate was not entitled to its claim as it was not in existence when the contract was made and a company cannot obtain the benefit of a pre-incorporation contract in the suit of specific performance. So, fact of this case was that the a 'N' company contracted with 'A', the nominee of the syndicate company which was not even incorporated, to grant a lease of certain coal mining rights for three years. After the syndicate was registered, it claimed the contracted lease which the company 'N' refused.

Position since 1963 (i.e., after passing of the specific relief Act, 1963):

Until the passing of the specific relief Act, 1963, in India the promoters found it very difficult to carry out the work of incorporation. Since contracts prior to incorporation were void and also could not be ratified, people hesitated to either supply any goods or services for the cause of incorporation. Promoter also felt shy of accepting personal responsibility. The specific relief Act, 1963 came as a relief to the promoters.

The specific relief Act provides under the following sections:

Section 15(h) and 19(e) of the Specific Relief Act provides as follows:

1. The contract should have been entered into by the promoter for the purpose of the company.
2. The terms of incorporation should warrant should warrant such contract.
3. The company should accept the contract after incorporation.
4. Such acceptance should be communicated to the other party to the contract.

So, preliminary contract enforced by the promoter at the prior to incorporation of the company will be treated as contract between two individuals who are in existence. Thus, the company do have no inherent right concerning ratification of those contract unless company acquiring the power as to the ratification by its memorandum as the subject-matter of contract is not contrary to the object of the company. Hence, the third party cannot sue the company, if any breach of contract has been taken place where such contract entered prior to the incorporation even they for the benefit of the company. So , question is here that the what is the position of the promoter in relation to preliminary contracts? Or in other words we can say that if the company does not execute a fresh contract incorporation and the contract is not one warranted for the purposes of incorporation of the company, what will be the legal position of the promoter who brings about such a contract? It was observed in the case of *Phonogram Limited v. Lane*, that although a contract made before a company's incorporation cannot bind the company, it is not wholly devoid of legal effect, even if all the persons who negotiated the contract are attempting to incorporate a Pop group had obtained financial assistance from a recording company. He was held personally liable to refund the amount on his project failing to materialise.

So, Promoters shall be liable to pay damages for failure to perform the promises made in the name of company and this shall be so, even where the contract expressly provides that only the company's paid up capital shall be answerable for performance as it was also held in the case of *Scot. v. Lord Ebury.*

4.2. After incorporation of the company:

After company came into existence, a company can ratify or adopt the contract, and this would bound the company and not the promoter. Under the *Specific Relief Act 1963, section 15(h) and 19(e)* promoter can shift his right and responsibility to the company, if it is warranted by the terms of incorporation. If we look on the point of remuneration for promoter concerns, then it is clear that generally the promoter is not

entitled for any kind of remuneration, salary and in any manner. However, once the company is incorporated & members of the company is improved then he may be compensated in terms of lum-sum amount. Nothing is entitled to obtained as a legal right he only be compensate on the ground of equity. If the allotment of share is taken place for promoter then automatically promoter becomes a member of the company.

4.3. Comparison between Indian and other country's laws regarding promoter's liability for pre-incorporation contract:

Although under the English Common Law, the American law and the Indian Law recognize the rule that promoter is personally liable for pre-incorporation contract, American Laws and Indian laws are much more innovative and effective to solve the problem of Pre-incorporation Contract. Whereas the English Courts still follow the principle of *Kelner v. Baxter.* Although in UK, Contracts (Rights of Third Parties) Act 1999 brought some relief, but it is not as broad as the American and Indian Laws are.

Under English Common Law, the ratification or adoption, after the incorporation, did not release the promoter from liability of pre-incorporation contract. Whereas in American Court recognize that if the after the incorporation company can ratify or adopt the contract, and this would bound the company and not the promoter. Indian Law the rule of *Kelner v Baxter* is applicable but under the *Specific Relief Act 1963, section 15(h) and 19(e)* promoter can shift his right and responsibility to the company, if it is warranted by the terms of incorporation. The principle of novation of pre-incorporation contract is applicable in above three counties, the reason behind is that, the novation replace the old contract with the new contract, so there is not problem of non-existence of company. Now after the Contracts (Rights of Third Parties) Act 1999, English laws may also allow company to become the part of pre-incorporation contract, when it acquire its legal existence.

5. CONCLUSION

In conclusion, it may be said that the word 'Promoter' is used in common parlance to denote any individual, syndicate, association, partnership or a company which takes all the necessary steps to create and set it going. The Promoter originated the scheme for the formation of the company; gets together the subscribers to the memorandum; gets memorandum and prepared articles, executed and registered; finds the bankers, brokers and legal advisors; located the first directors, settle the terms of preliminary contracts with vender and agreement with underwriters and makes arrangements for preparation, advertisement and circulation of the prospectus and arrangement of the capital. So, Promoters act as a molding format for the company and gives it a shape which can exist in the world although they cannot take anything in this regard.

MEMORANDUM OF ASSOCIATION

A Memorandum of Association (MOA) is a legal document prepared in the formation and registration process of a limited liability company to define its relationship with shareholders. The MOA is accessible to the public and describes the company's name, physical address of registered office, names of shareholders

and the distribution of shares. The MOA and the Articles of Association serve as the constitution of the company. The MOA is not applied in the U.S. but is a legal requirement for limited liability companies in European countries including the United Kingdom, France and Netherlands, as well as some Commonwealth nations.

Name Clause

The name clause requires you to state the legal and recognized name of the company. You are allowed to register a company name only if it does not bear any similarities with the name of an existing company. Your company name must end with the word "limited" because the preparation of an MOA is a legal requirement for limited liability companies only.

Registered Office Clause

The registered office clause requires you to show the physical location of the registered office of the company. You are required to keep all the company registers in this office in addition to using the office in handling all the outgoing and incoming communication correspondence. You must establish a registered office prior to commencing business activities.

Objective Clause

The objective clause requires you to summarize the main objectives for establishing the company with reference to the requirements for shareholding and use of financial resources. You also need to state ancillary objectives; that is, those objectives that are required to facilitate the achievement of the main objectives. The objectives should be free of any provisions or declarations that contravene laws or public good.

Liability Clause

The liability clause requires you to state the extent to which shareholders of the company are liable to the debt obligations of the company in the event of the company dissolving. You should show that shareholders are liable only their shareholding and/or to their commitment to contribute to the dissolution costs upon liquidation of a company limited by guarantee.

Capital Clause

The capital clause requires you to state the company's authorized share capital, the different categories of shares and the nominal value (the minimum value per share) of the shares. You are also required to list the company's assets under this clause.

Association Clause

The association clause confirms that shareholders bound by the MOA are willingly associating and forming a company. You require seven members to sign an MOA for a public company and not less than two people for a MOA of a private company. You must conduct the signing in the presence of witness who must also append his signature.

What is Ultra Vires?

The term "Ultra" means beyond and "Vires" means powers. The term, therefore, means the doing of an act, which is beyond the legal power, and authority of the company. It is considered as an act outside the scope of the object of the company.

Doctrine of Ultra Vires

The Memorandum, being the constitution of the company sets out the principal objectives, powers, scope and its area of operation, both internal and external. A company, therefore, can do anything within the scope of the powers specified in the Memorandum.

It has also an implied power to do all such things that are fairly incidental to its main objects. If the company does anything which is beyond the powers specified in the Memorandum it shall be construed as an Ultra Vires act.

Why the Doctrine?

The objective of the Doctrine of Ultra Vires is to ensure the shareholders and the creditors that the fund and assets of the company will not be used for any purpose other than those specified in the Memorandum. Especially the creditors, while dealing with the company can make themselves aware of the fact whether his transaction with the company is ultra vires or not. If it is found ultra vires, he can avoid such transaction and thereby safeguard his interest.

Effects of an Ultra Vires Act

The effects of an ultra vires act can be summed up as follows:

1. An ultra vires act will be wholly void and it will not bind the company; neither the company nor the outsider can enforce the contract.
2. Any member of the company can bring injunction against the company to prevent it from doing any ultra vires act.
3. The directors of the company will be personally liable to make good the funds used for the ultra vires acts.
4. Where a company's money has been used ultra vires to acquire some property, the right of the company over such property is held secure.
5. Since Ultra Vires contracts are treated as invalid from the outset, it cannot become Intra Vires by reason of estoppel or ratification.
6. Ultra Vires borrowing does not create the relationship of debtor and creditor. The only possible remedy in such case is in *rem* and not in *personam*.

Can an Ultra Vires Act be Ratified?

An ultra vires act cannot be ratified even by the whole body of the shareholders and make it binding on the company. In other words, even the shareholders cannot do an ultra vires act. This is the peculiar feature of this doctrine.

The principles of law on this subject were first enunciated by Lord Cairons, L.J., in Ashbury Railway Carriage & Iron Co. Ltd. V. Riche. In that case, a company was formed with the following objects:

a. to make, sell, lend or hire, railway carriages and wagons, and

b. to purchase, lease, work and sell mines, minerals and land and buildings.

The directors contracted to finance the construction of a railway line in Belgium with Mls Riche. The Court held that the contract was ultra vires the company and void, so that even the subsequent assent of the whole body of the shareholders could not ratify it.

However, later on, the House of Lords held in other cases that the doctrine of ultra vires should be applied reasonably and unless it is expressly prohibited, a company may do an act, which is important for, or incidental to attainment of its objectives.

Types of Ultra Vires Acts

There are three types of ultra vires acts. They are-

i. ultra vires the Memorandum or the company,

ii. ultra vires the Articles but intra vires the company, and

iii. ultra vires the directors but intra vires the company.

Ultra Vires the Memorandum or the Company

If the act done or contract made by the company is beyond the powers given in the objects clause of the Memorandum, it is called an act, which is ultra vires the Memorandum. The act is good to the extent of the authority of the company and bad as to the excess. But, where it cannot be separated from the authority conferred on the company by the Memorandum, the whole of the transaction shall be void. However, there is nothing in law to prevent a company from protecting its property, though it is ultra vires the company.

Ultra Vires the Articles but Intra Vires the Company

The acts done or contracts made beyond the powers given by the Articles but are within the powers of the Memorandum are called ultra vires the Articles but intra vires the company. The shareholders can ratify these acts by making an alteration in the Articles to that effect.

Ultra Vires the Directors but Intra Vires the Company

These are acts done or contracts made by the directors, which are ultra vires the directors, but intra vires the company. These acts can be ratified by the company and can make it binding.

CASE LIST

Ashbury Railway Carriage and Iron Co. vs. Riche, [1875] L. R. 7 HL 653

When an act is performed or a transaction is carried out, which, though legal in itself, is not authorised by the object clause, in the memorandum of association, such an act is null and void.

Attorney General vs. Great Eastern Railway Co., [1880] 5 AC 473 (HL)

"Whatever may fairly be regarded as incidental or consequential upon those things specified in the memorandum of association as object ought not to be held ultra vires unless expressly prohibited."

Rolled Steel Products (Holdings) Ltd v British Steel Corporation [1986] Ch 246

A company has power to do only those things which are within, or reasonably incidental to, its stated objects. If an act is capable of being in pursuance of, or incidental to, the stated objects, it could not be ultra vires and void because of the purpose or state of mind of the directors who authorised it.

Radhabari Tea Company Private Limited vs. Mridul Kumar Bhattacharjee and Other, 2009 Indlaw GUW 44

The doctrine of ultra vires provides that an action, taken by the board of directors of a company or the company itself beyond the powers conferred on the company and/or its directors by the memorandum of association of the company, is ultra vires.

White and another v South Derbyshire District Council, [2013] P.T.S.R. 536 90 (UK Case)

An ultra vires act is not necessarily void for all purposes and the law would strive to protect innocent third parties who had relied upon the apparent validity of such an act.

Note:

Under the new Companies Act, 2013 this doctrine of ultra vires gives a ground to the members and depositor(s) of the company to file an application before the Tribunal on behalf of the members or depositors for restraining the company from committing an act which is ultra vires the articles or memorandum of the company vide Section 245(1)(a) of the new Companies Act, 2013.

ARTICLES OF ASSOCIATON

Articles of Association (AOA) is the secondary document, which defines the rules and regulations made by the company for its administration and day to day management. In addition to this, the articles contain the rights, responsibilities, powers and duties of members and directors of the company. It also includes the information about the accounts and audit of the company.

Every company must have its own articles. However, a public company limited by shares can adopt Table A instead of Articles of Association. It comprises of all the necessary details regarding the internal affairs and the management of the company. It is prepared for the persons inside the company, i.e. members, employees, directors, etc. The governance of the company is done according to the rules prescribed in it. The companies can frame its articles of association as per their requirement and choice.

Key Differences Between Memorandum of Association and Articles of Association

The major differences between memorandum of association and articles of association are given as under:

1. Memorandum of Association is a document that contains all the condition which are required for the registration of the company. Articles of Association is a document that contains the rules and regulation for the administration of the company.
2. Memorandum of Association is defined in section 2 (28) while the Articles of Association is defined in section 2 (2) of the Indian Companies Act 1956.
3. Memorandum of Association is subsidiary to the Companies Act, whereas Articles of Association is subsidiary to both Memorandum of Association as well as the Act.
4. In any contradiction between the Memorandum and Articles regarding any clause, Memorandum of Association will prevail over the Articles of Association.
5. Memorandum of Association contains the information about the powers and objects of the company. Conversely, Articles of Association contain the information about the rules and regulations of the company.
6. Memorandum of Association must contain the six clauses. On the other hand, Articles of Association is framed as per the discretion of the company.
7. Memorandum of Association is obligatory to be registered with the ROC at the time of registration of Company. As opposed to Articles of Association, is not required to be filed with the registrar, although the company may file it voluntarily.
8. Memorandum of association defines the relationship between company and external party. On the contrary, articles of association govern the relationship between the company and its members and also between the members themselves.
9. When it comes to scope, the acts performed beyond the scope of memorandum are absolutely null and void. In contrast, the acts done beyond the scope of artciles can be ratified by unanimous voting of all shareholders.

Conclusion

Memorandum and Articles are the two very important documents of the company, which are to be maintained by them as they guide the company on various matters. They also help in the proper management and functioning of the company throughout its life. That is why every company is required to have its own memorandum and articles.

All the companies have its own Memorandum of Association and Articles of Association; **'Memorandum of Association'** abbreviated as MOA, is the root document of the company, which contains all the basic details about the company. **'Articles of Association'** shortly known as AOA, is also a major document which contains all the rules and regulations designed by the company. Below you can see the basic differences between the Memorandum of Association and Articles of Association.

sec 2(28) MOA

sec 2(2) AOA

Comparison Chart

Basis for Comparison	Memorandum of Association	Articles of Association
Meaning	Memorandum of Association is a document that contains all the fundamental information which are required for the incorporation of the company.	Articles of Association is a document containing all the rules and regulations that governs the company.
Defined in	Section 2 (28)	Section 2 (2)
Type of Information contained	Powers and objects of the company.	Rules of the company.
Status	It is subordinate to the Companies Act.	It is subordinate to the memorandum.
Retrospective Effect	The memorandum of association of the company cannot be amended retrospectively.	The articles of association can be amended retrospectively.
Major contents	A memorandum must contain six clauses.	The articles can be drafted as per the choice of the company.
Obligatory	Yes, for all companies.	A public company limited by shares can adopt Table A in place of articles.
Compulsory filing at The time of Registration	Required	Not required at all.
Alteration	Alteration can be done, after passing Special Resolution (SR) in Annual General Meeting (AGM) and previous approval of Central Government (CG) or Company Law Board (CLB) is required.	Alteration can be done in the Articles by passing Special Resolution (SR) at Annual General Meeting (AGM)
Relation	Defines the relation between company and outsider.	Regulates the relationship between company and its members and also between the members inter se.
Acts done beyond the scope	Absolutely void	Can be ratified by shareholders.

Doctrine of Constructive Notice

The Memorandum and Articles, on registration, assume the character of public documents. The office of the Registrar is a public office and documents registered there are open and accessible to the public at large. Therefore, every outsider dealing with the company is deemed to have notice of the contents of the Memorandum and Articles. This is known as **Constructive Notice** of Memorandum and Articles.

Under the **doctrine of 'constructive notice'**, every person dealing or proposing to enter into a contract with the company is deemed to have constructive notice of the contents of its Memorandum and Articles. Whether he actually reads them or not, it is presumed that he has read these documents and has ascertained the exact powers of the company to enter into contract, the extent to which these powers have been delegated to the directors and the limitations to such powers. He is presumed not only to have read them, but to have understood them properly. Consequently, if a person enters into a contract which is ultra vires the Memorandum, or beyond the authority of the directors conferred by the Articles, then the contract becomes invalid and he cannot enforce it, not-withstanding the fact that he acted in good faith and money was applied for the purposes of the company.

Doctrine of indoor Management

The doctrine of Indoor management, popularly known as the Turquand's rule initially arose some 150 years ago in the context of the doctrine of constructive notice. The rule of Doctrine of Indoor Management is conflicting to that of the principle of Constructive Notice. The latter seeks to protect the company against outsiders; the former operates to protect outsiders against the company. The rule of constructive notice is confined to the external position of the company and, therefore, it follows that there is no notice as to how the company's internal machinery is handled by its officers. If the contract is consistent with the public document, the person contracting will not be prejudiced by irregularities that may beset the indoor work of the company.

The Doctrine of Indoor Management lays down that persons dealing with a company having satisfied themselves that the proposed transaction is not in its nature inconsistent with the memorandum and articles, are not bound to inquire the regularity of any internal proceeding. In other words, while persons contracting with a company are presumed to know the provisions of the contents of the memorandum and articles, they are entitled to assume that the provisions of the articles, they are entitled to assume that the officers of the company have observed the provisions of the articles. It is no part of duty of any outsider to see that the company carries out its own internal regulations.

It is important to note that the notice of constructive notice can be invoked by the company and it does not operate against the company. It operates against the person who has failed to inquire but does not operate in his favour. But the doctrine of "indoor management" can be invoked by the person dealing with the company and cannot be invoked by the company.

The **doctrine of indoor management** was first propounded by Lord Hatherlyin the celebrated case *Royal British Bank vs. Turquand.* The directors of the Bank had issued a bond to Turquand. The company was empowered by its Articles to issue such bonds provided it was authorized by a resolution of the company in general meeting. In this case no such resolution had been passed. It was held that Turquand could recover the amount of bond from the company on the ground that he was entitled to assume that the necessary resolution had been passed by the company.

No benefit under the **doctrine of indoor management** can be claimed by a person under the following circumstances:

Exceptions to doctrine of indoor management

In following circumstances relief of indoor management cannot be claimed by an outsider who is dealing with the company.

1. Where the outsider had knowledge of irregularity – The rule will not apply if the person dealing with the company has slight knowledge about the lack of authority of person who is acting on behalf of the company in this situation the doctrine will not apply.

In the case of Howard v. Patent Ivory Co. , the directors cannot borrow more than 1000 pound without the consent of the company's annual general meeting. Directors borrowed 3500 pound without the consent of annual general meeting from another director who took debentures. Now as the plaintiff is director than he has the knowledge about the internal irregularity. Held- the debentures are good only for the 1000 pounds only because the plaintiff (director) has the knowledge of the internal irregularity

2. No knowledge of memorandum and articles- again, the rule cannot be invoked by a person on the ground that he don't have the knowledge of memorandum and articles and thus he did rely on them.

In the case of Rama Corporation v. Proved Tin & General Investment Co, the X who was director in the company entered into a contract with Rama Corporation while purporting to act on behalf of the company and he also took a cheque from them. The articles of the company did provide that the director may delegate their power but Rama Corporation did not have knowledge of this as they did not read the articles and memorandum of the company. Now later on it was found that company had never delegated their power to X. Held- plaintiff cannot take the remedy of the indoor management as they even don't that power could be delegated.

3. Forgery- The rule does not apply to the transaction involving forgery or illegal or transactions which are void *ab initio.* In the case of the forged transaction there is lack of consent. Here the question of consent cannot arise as the person whose signature is forged he is not even aware of the transaction.

In the case of Rouben v. Great Fingal Consolidated– Here the secretary of the company forged the signature of two of the directors and issued the certificate without the authority. The issue of certificate requires the

sign of two directors as given in the article. Held- here the holder of certificate cannot take the advantage of the doctrine as it was forged transaction which is void ab initio.

In the case of Kreditbank Cassel v. Schenkers Ltd,– a bill of exchange signed by the manger of a company with his own signature under the words stating that he signed on behalf of the company, was held to be forgery when the bill was drawn in favour of a payee to whom the manger was personally indebted. The bill in this case was held to be forged because it purported to be a different document from what it was in fact; it purported to be issued on behalf of the company in payment of its debt when in fact it was issued in payment of the manager's own debt.

4. Negligence- the doctrine of indoor management, in no way, rewards those who behave negligently. Thus, where an officer of a company does something which shall not ordinarily be within his authority, the person dealing with him must make proper enquiries and satisfy him as to the officer's authority. If he fails to make an enquiry, he is estopped from relying in the rule.

In the case of B. Anand Behari Lal v. Dinshaw & Co. (Bankers) Ltd., an accountant of a company in favour of Anand Behari. On an action brought by him for breach of contract, the court held the transfer to be void. It was observed that the power of transferring immoveable property of the company could not be considered within the apparent authority of an accountant.

5. The doctrine will not apply where the question is in regard of to the very existence of an agency.

In the case of Varkey Souriar V. Leraleeya Banking Co. Ltd the Kerala High Court held that the doctrine of Indoor management cannot apply where the question is not one as to scope of the power exercised by an apparent agent of a company but is in regard to the very existence of the agency.

6. This doctrine is also not applicable where a pre-condition is required to be fulfilled before company itself can exercise a particular power. In other words, the act done is not merely *ultra vires* the directors/ officers but *ultra vires* the company itself.

How Indian judiciary has interpreted this doctrine

In the case of Lakshmi Ratan Cotton Mills Co. Ltd, v. J. K. Jute Mitts Co. Ltd, the company of plaintiff sued defendant's company for the total amount of Rs.1,50,000. The defendant company raised the argument that no such resolution sanctioning the loan was passed by the board of director, thus it is not binding on the company.

The court held that- *"If it is found that the transaction of loan into which the creditor is entering is not barred by the charter of the company or its articles of association, and could be entered into on behalf of the company by the person negotiating it, then he is entitled to presume that all the formalities required in connection therewith have been complied with. If the transaction in question could be authorised by the passing of a resolution, such an act is a mere formality. A bona fide creditor, in the absence of any suspicious circumstances, is entitled to presume its existence. A transaction entered into by the borrowing company*

under such circumstances cannot be defeated merely on the ground that no such resolution was in fact passed. The passing of such a resolution is a mere matter of indoor or internal management and its absence, under such circumstances, cannot be used to defeat the just claim of a bona fide creditor. A creditor being an outsider or a third party and an innocent stranger is entitled to proceed on the assumption of its existence ; and is not expected to know what happens within the doors that are closed to him. Where the act is not ultra vires the statute or the company such a creditor would be entitled to assume the apparent or ostensible authority of the agent to be a real or genuine one. He could assume that such a person had the power to represent the company, and if he in fact advanced the money on such assumption, he would be protected by the doctrine of internal management."

In the case of Official Liquidator, Manasube & Co. (P.) Ltd. V. Commissioner of police,

It is expected from the person that he will read the article and memorandum when he enters into a contract with the company but it is highly unlikely that he will also check the legality, propriety and regularity of acts of directors.

In recent judgment Indian courts had broadened the scope of the doctrine. The object is still same, to protect the third party who acted in good faith with the company and is unaware of the internal management of the company.

Does the doctrine of indoor management apply to government authorities?

In the case of MRF Ltd. v. Manohar Parrikar the Supreme Court has first time analysed the doctrine of indoor management in some detail. The case is related to the public law but a reference was made to the doctrine of indoor management to draw an analogy.

In this case notification issued by State Government for granting rebate of 25 per cent in Tariff in respect of the power supply to the Low Tension and High Tension Industrial Consumers was rescinded by another Notification issued at instance of Ministry of Power – Legality of the notifications challenged on grounds that they were not issued in compliance with the requirements of Article 154 read with Article 166 of the Constitution of India and the Business Rules of the Government of state framed by the Governor. Decision taken at ministers level without submitting it to council of misters or chief minister without obtaining concurrence of finance department, and notifications issued pursuant to ministers decision, so it was held that it is not sustainable in law. A decision can be treated as the decision of the government only when decision satisfies requirements of with Rules of business framed under Art. 116(3)/77(3). Decision having financial implications, if taken by a minister without seeking concurrence of finance department as provided by with Rules of business, cannot be treated as decision of state government as a whole under article 154. So notifications issued pursuant to ministers decision so taken, are void *ab initio* and all actions consequent thereto are null and void

"Doctrine of indoor management is in direct contrast to doctrine of constructive notice which is essentially a presumption operating in favour of the company against the outsider. It prevents the outsider from

alleging that he did not know the constitution of the company rendered a particular delegation of authority ultra-vires. Doctrine of indoor management is an exception to rule of constructive notice. It imposes an important limitation on doctrine of constructive notice. According to this doctrine, persons dealing with company are entitled to presume that internal requirements prescribed in the memorandum and articles have been properly observed. Therefore, doctrine of indoor management protects outsiders dealing with the company, whereas doctrine of constructive notice protects the insiders of a company or corporation against dealings with outsiders. However, suspicion of irregularity has been widely recognized as an exception to doctrine of indoor management. Protection of doctrine is not available where the circumstance surrounding are suspicious and therefore invite inquiry.

Applying the exception to the present scenario, there is sufficient doubt with regard to conduct of power minister in issuing notifications. Therefore there is a definite suspicion of irregularity which render doctrine of indoor management inapplicable to the present case"

PROSPECTUS

Clause (70) of Section 2 of this Bill define "prospectus" means any document described or issued as a prospectus and includes a red herring prospectus referred to in section 32 or shelf prospectus referred to in section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate.

Section 26 deals with matters to be stated in prospectus.

MATTERS TO BE STATED IN PROSPECTUS (SECTION 26):

A prospectus may be issued by or behalf of a public company either with reference to its formation or subsequently, or by or on behalf of any person who is or has been engaged or interested in the formation of a public company.

Information in Prospectus:

Every prospectus shall state following information:-

i. names and addresses of the registered office of the company, company secretary, Chief Financial Officer, auditors, legal advisers, bankers, trustees, if any, underwriters and such other persons as may be prescribed;

ii. dates of the opening and closing of the issue, and declaration about the issue of allotment letters and refunds within the prescribed time;

iii. a statement by the Board of Directors about the separate bank account where all monies received out of the issue are to be transferred and disclosure of details of all monies including utilised and unutilised monies out of the previous issue in the prescribed manner;

iv. details about underwriting of the issue;

v. consent of the directors, auditors, bankers to the issue, expert's opinion, if any, and of such other persons, as may be prescribed;

vi. the authority for the issue and the details of the resolution passed there for;

vii. procedure and time schedule for allotment and issue of securities;

viii. capital structure of the company in the prescribed manner;

ix. main objects of public offer, terms of the present issue and such other particulars as may be prescribed;

x. main objects and present business of the company and its location, schedule of implementation of the project;

xi. particulars relating to—

    1. management perception of risk factors specific to the project;

    2. gestation period of the project;

    3. extent of progress made in the project;

    4. deadlines for completion of the project; and

    5. any litigation or legal action pending or taken by a Government Department or a statutory body during the last five years immediately preceding the year of the issue of prospectus against the promoter of the company;

xii. minimum subscription, amount payable by way of premium, issue of shares otherwise than on cash;

xiii. details of directors including their appointments and remuneration, and such particulars of the nature and extent of their interests in the company as may be prescribed; and

xiv. Disclosures in such manner as may be prescribed about sources of promoter's contribution.

Reports with Prospectus:

Every prospectus shall set out following reports for the purpose of financial information:

i. Reports by the auditors of the company with respect to its profits and losses and assets and liabilities and such other matters as may be prescribed;

ii. Reports relating to profits and losses for each of the five financial years immediately preceding the financial year of the issue of prospectus including such reports of its subsidiaries and in such manner as may be prescribed. Where company has not completed five financial years than such report for all financial years is required.

iii. Reports made in the prescribed manner by the auditors upon the profits and losses of the business of the company for each of the five financial years immediately preceding issue and assets and liabilities of its business on the last date to which the accounts of the business were made up, being a date not more than one hundred and eighty days before the issue of the prospectus. Where company has not completed five financial years than such report for all financial years is required.

iv. Reports about the business or transaction to which the proceeds of the securities are to be applied directly or indirectly.

Declaration of Compliance:

Every prospectus shall make a declaration about the compliance of the provisions of this Act and a statement to the effect that nothing in the prospectus is contrary to the provisions of this Act, the Securities Contracts (Regulation) Act, 1956 and the Securities and Exchange Board of India Act, 1992 and the rules and regulations made there under.

Other matters in Prospectus:

Clause (d) of Sub – section (1) of section 26 give unlimited power to central government to list other matters and set out other reports to be included in a prospectus.

Delivery of Prospectus with Registrar:

A copy of prospectus shall be delivered to the Registrar for registration signed by every person who is named as a director or proposed director of the company or by his duly authorised attorney on or before the date of its publication and only then it shall be issued by or on behalf of a company or in relation to an intended company.

Statement of an Expert:

A statement made by an expert shall be included only if expert is or was engaged or interested in the formation or promotion or management of the company and has given his written consent to the issue of the prospectus. Such consent of expert must not be withdrawn by his before the delivery of prospectus to the Registrar for registration and a statement to that effect shall be included in the prospectus.

Every prospectus issued shall state that a copy has been delivered to the Registrar and specify attached documents.

The registrar shall not register a prospectus all requirements has been complied with and the prospectus is accompanied by the consent in writing of all the person named in the prospectus.

Prospectus shall not be valid if it is issued more than ninety days after the date on which a copy thereof delivered to the Registrar.

Caution:

If a prospectus is issued in contravention of the provisions of section 26, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and every person who is knowingly a party to the issue of such prospectus shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.

VARIATION IN TERMS OF CONTRACT OR OBJECTS IN PROSPECTUS (SECTION 27):

A company may vary the terms of a contract refered in the prospectus or object for which the prospectus was issued, only under approval or authority given by way of special resolution.

The notice of such resolution to shareholders shall also be published in the newspapers (one in English and one in vernacular language) in the city where the registered office of the company is situated. These notices shall clearly indicate justification for such variation.

The shareholders who have not agreed to the proposal to vary the terms of contracts or objects referred to in the prospectus, shall be given an exit offer by promoters or controlling shareholders at exit price as determined in accordance with regulation made by the Securities and Exchange Board of India.

Requirement in Deemed Prospectus (Section 25):

Section 26 as applied by Section 25 shall have effect as if —

1. it required a prospectus to state in addition to the matters required by section 26 to be stated in a prospectus—

    i. the net amount of the consideration received or to be received by the company in respect of the securities to which the offer relates; and

    ii. the time and place at which the contract where under the said securities have been or are to be allotted may be inspected;

1. the persons making the offer were persons named in a prospectus as directors of a company.

The 'Golden Rule' for Prospectus interpretation

The Golden Rule as regards the drafting of the prospectus was laid down in the leading case *New Brunswick and Canada Railway and Land Co. v. Muggeridge*, as:

- Only true nature of the company's venture shall be disclosed;
- Strict and scrupulous accuracy shall be maintained in drafting prospectus as it invites the public to take shares on the faith of the representations contained in the prospectus;
- In addition to the mandatory information required to be given as per Part I and Part II of Schedule II of the Act, there must be voluntary disclosures of information as would reasonably constitute a fair representation of facts for the public to act upon.

UNIT III

ALLOTMENT OF SHARES

As per Section 23 of the new Companies Act, 2013, a public or private company may issue securities in any of the following manner:

Public Company

- To public through issue of Prospectus
- Private Placement
- Rights Issue or a Bonus Issue

Private Company

- Rights or Bonus Issue
- Private placement

Private Placement vis-a-vis Preferential Allotment

Section 42 of the new Companies Act, 2013 deals with private placement. Any offer of securities or invitation to subscribe to securities to 200 persons or less (excluding qualified institutional buyers and employees) in a financial year will be a 'private placement' under Section 42(2) of the Companies Act, 2013. Reading the **Rule 13 of the of Companies (Share Capital and Debentures) Rules, 2014** makes it is very clear that any preferential allotment by rights issue has to comply with private placement.

As per the amended definition of 2011, '**preferential allotment**' means allotment of shares or any other instrument convertible into shares including hybrid instruments convertible into shares on preferential basis made pursuant to the provisions of sub section(1A) of section 81 of the Companies Act, 1956. Earlier, preferential allotment envisaged a situation when a listed issuer issues shares or convertible securities, to a select group of persons in terms of provisions of Chapter XIII of SEBI (DIP) Guidelines.

Time Limit for allotment of securities:

Unlisted Public Companies (Preferential Allotment) Amendment Rules, 2011 amended the erstwhile Rules of 2003. The 2011 Rules provided that allotment of securities should be completed within **60 days** from the receipt of application money. If not so allotted, the company should **repay application money within 15 days** thereafter, failing which it should be repaid along with an interest at **12%** p.a. However, please note that these Rules applied only to unlisted public companies, and no such conditions were prescribed for private companies back then.

Time Limit for allotment of securities under the new Companies Act, 2013:

Under the new Companies Act, **Sections 62 & 42** and **Rule 13** of **Companies (Share Capital and Debentures) Rules, 2014** deals with issue of shares on **preferential basis**. Rule 13 prescribes that any such issue on preferential basis has to comply with conditions laid down in **section 42** of the Companies Act, 2013. **Section 42(6)** further provides that-

"(6) A company making an offer or invitation under this section shall allot its securities within ***sixty days*** *from the date of receipt of the application money for such securities and if the company is not able to allot the securities within that period, it shall* ***repay the application money to the subscribers within***

***fifteen days** from the date of completion of sixty days and if the company fails to repay the application money within the aforesaid period, it shall be liable to repay that money with interest at the rate of twelve per cent. per annum from the expiry of the sixtieth day:*

Provided that monies received on application under this section shall be kept in a separate bank account in a scheduled bank and shall not be utilised for any purpose other than—

(a) for adjustment against allotment of securities; or

(b) for the repayment of monies where the company is unable to allot securities."

Whether such time limitation apply to convertible instruments as well.

Explanation to Rule 13 of Companies (Share Capital and Debentures) Rules, 2014 provides that-

*"Explanation.- For the purposes of this rule, (i) the expression 'Preferential Offer' means an issue of **shares or other securities**, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities;*

*(ii) the expression, "**shares or other securities**" means **equity shares**, fully **convertible** debentures, partly **convertible** debentures or **any other securities, which would be convertible into or exchanged with equity shares at a later date.**"*

Thus, it is clear that the restriction regarding the number of days permitted **for allotment of securities,** as mentioned in Section 42(6) of the new Act will be applicable for convertible instruments as well. It is also to be noted that the provisions for private placement under Section 42 applies to the issue of "securities" and not "shares".

ECURITIES IN DEMATERIALISED FORM (SECTION 29):

Under this section;

1. Every company making public offer; and
2. Such other class or classes of companies as may be prescribed

shall issue the securities only in the dematerialised form.

When any company issue its securities in dematerialised form, provisions of the Depositories Act, 1996 and regulations made under that Act shall be applicable.

There is no bar for any other company to issue its securities in any form. Any other company may convert its securities into dematerialised form.

ALLOTMENT OF SECURITIES BY COMPANY (SECTION 39):

After public offer, any allotment shall be made only if the amount stated in the prospectus as minimum amount. The sum payable on application for the amount so stated as minimum amount has been paid to and received by the company by cheque or other instrument.

There is no clarity yet, what will be these instrument and why the term other banking channel has not been included.

The amount payable on application on every security shall not be less than five percent of he nominal amount of security or such other percentage or amount as may be specified.

If the stated minimum amount has not been subscribed and the sum payable on application is not received within a period of thirty days from the date of issue of the prospectus, all amount received shall be returned within prescribed time and in prescribed manner.

The company shall file with the Registrar of Companies a "Return of Allotment" in prescribed manner.

In case of any default, the company and its officer who is in default shall be liable to a penalty, for each default, of one thousand rupees for each day during which such default continues or one lakh rupees, whichever is less.

I do not understand why there is an upper limit on this penalty.

LISTING OF SHARES (SECTION 40):

Every company making public offer shall make an application to at least one stock exchange before making the public offer. This is duty of company to obtain permission of stock exchange or stock exchanges for the dealing of securities there.

Prospectus for the public offer shall also state the name or names of the stock exchange in which application for dealing of the securities has been made.

All money received on application from the public for subscription of the securities shall be kept in a separate bank account in a schedule bank. This money shall not be utilised for any purpose other than –

1. For adjustment against allotment of securities where the permission from the stock exchanges named in prospectus has been received; or
2. For repayment of money within the time specified by the Securities and Exchange Board, where the company is for any other reason unable to allot securities.

A company may pay commission to any person in connection with the subscription to its securities subject to such conditions as may be prescribed.

Any condition which require or bind any applicant for securities to waive compliance with any of the requirement of this section shall be void.

If a default is made in complying with the provisions of this section, the company shall be punishable with a fine which shall not be less than five lakh rupees but which may extend to fifty lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.

GLOBAL DEPOSITQRY RECEIPT (SECTION 41):

A company may, after passing a special resolution in its general meeting, issue depository receipts in any foreign country in such manner, and subject to such conditions, as may be prescribed.

Member and Shareholder

A shareholder may or may not be the member. Similarly, a number of a member may or may not be the shareholder. The given statement is very confusing because the term shareholder and member are either used synonymously as well as interchangeably by many people. some differences between member and shareholder of a company.

Comparison Chart Basis for Comparison	Member	Shareholder
Meaning	A person whose name is entered in the register of members of a company, is the registered member of the company.	The person who owns the shares of a company is known as shareholder.
Defined in	Section 2 (27)	Not defined
Share Warrant	The holder of a share warrant is not a member.	The holder of a share warrant is a shareholder.
Company	Every company must have a minimum number of members.	The company limited by shares can have shareholders.
Memorandum	The person who signs the memorandum of association with the company becomes a member.	After signing the memorandum, a person can be a shareholder only when the shares are allotted to him.

A person whose name is entered in the register of members of a company becomes a member of that company. The register includes every single detail about the member like name, address, occupation, date of becoming a member, etc. It also includes every person who holds company's shares and whose name is entered as the beneficial owners in depository records.

The liabilities of members are limited to the amount of shares held by them in the case of a company having share capital while in the case of a company limited by guarantee the liability of members is limited to the amount of guarantee given by them. But, in the case of an unlimited company the members have to contribute from his personal assets to pay the debts.

The members cannot take part in the management of the company, i.e. the management of the company is looked after by the Board of Directors. Although the right to appoint and remove the directors is in the hands of members.

How to become the member of a company

- If a person subscribes the memorandum of association of a company, he becomes a member by signing it.
- If a person becomes the beneficial owner of shares whose name is registered in the record of the depository, then also he becomes a member.
- If a person gets shares by way of transfer and the transfer is recorded by the company, along with the entry of the name of the transferee in the register of members.
- If a person gets shares by way of transmission and the transmission is recorded by the company along with the entry of the name in the register of members.
- If a person agrees to take the qualification shares of the company and pay for it then also he becomes a member of the company.

Definition of Shareholder

An individual who owns the share of a public or a private company is known as a 'Shareholder.' A subscriber of shares is not regarded as the shareholder until the shares are actually allotted to him.

The shareholders are the owners of the company, i.e. to the extent of the share capital held by them. The legal representative of the deceased member, is a shareholder, not the member, until and unless his name is recorded in the register of members of the company. Hence, it can be said that every shareholder is a member but every member, is not a shareholder.

The following are the rights of a shareholder:

- Right to transfer or sell their shares.
- Right to get the dividend.
- Right to attend the general meeting and vote.
- Right to take copies of Memorandum and Articles of Association.
- Right to receive the copy of the statutory report.

Key Differences Between Members and Shareholders

The following are the differences between members and shareholders:

1. A member is a person who subscribed the memorandum of the company. A shareholder is a person who owns the shares of the company.
2. The term member is defined under section 2 (27) of the Indian Companies Act, 1956. Conversely, the term shareholder is not defined in the Indian Companies Act, 1956.
3. The bearer of a share warrant is not a member, but the bearer of a share warrant can be a shareholder.
4. All shareholders whose name are entered in the register of members are the members. On the other hand, all members may not be the shareholders.
5. In the case of a public company, there must be a minimum of 7 members. There is no such cap on the maximum number of members. Similarly, a private company can have a minimum of 2 and maximum of 50 members. As opposed to shareholders, there is no minimum or maximum limit, in the case of a public company.

Members and Shareholders both are important persons of any company, whether it is public or a private limited company. We explained many differences between them, which makes it clear that how these two terms differentiate each other. However, a member can be a shareholder and in the same way, a shareholder can also be a member subject to certain conditions has to be fulfilled for the same.

Capital

The term capital, in general, means the amount of money invested in a business. It includes not only the money invested at the time of inception of business firm but also all the moneys invested subsequently. Capital is must for all business concerns irrespective of their nature, size or constitution, and so without adequate capital no business can survive. The failure of many business concerns is only due to the lack of sufficient capital.

Classification of Share Capital

The capital raised by the company by issuing shares is called share capital. The Companies Act uses the term capital in several senses. They are the following:

1. Authorized Capital: This is the amount of capital stated in the capital clause of Memorandum of Association. It is also known as "**Nominal Capital**" or "**Registered Capital**". The company is entitled to raise finance by the issue of shares only up to the amount of authorized capital. However, the company can increase the amount of authorized capital by altering the Memorandum suitably. The promoters generally fix the amount of nominal capital after considering both the long-term and short-term requirements of the proposed company.

2. Issued Capital: It is that part of nominal capital which is issued to the public. Companies generally do not issue all its capital at once. They issue their capital in installments and so the issued capital is generally less than the nominal capital. It never exceeds the authorized capital.

3. Subscribed Capital: It is that part of the issued capital which is taken up by the public. Sometimes, the public may not take up all the shares that are offered to the public, for subscription. In such case, the subscribed capital shall be less than the issued capital. If the public subscribes all the shares, it shall be equal to the issued capital.

4. Called up Capital: It is that part of the subscribed capital, which has been called up on shares. For example, if the face value of a share is Rs.10 and Rs.5 has been called up on each of the 10,000 shares, then the called up capital shall be Rs.50,000.

5. Paid-up Capital: It is that part of the subscribed capital which has been actually paid up by the shareholders. The amount not paid by the shareholders on the calls made is known as calls-in-arrears. The expression "Paid-up Capital" also includes the amount credited as paid up on the shares.

Uncalled Capital: It is that part of the capital, which is not called up on the shares already, issued. The shareholders continue to be liable to pay as and when the calls are made.

7. Reserve Capital: It is that part of the capital which the company has decided not to be called up except in the event of winding up of the company. Sometimes, a company may feel that the capital already paid up is sufficient for the proper conduct and smooth running of the company. In such case, it may decide not to call up a certain portion of its subscribed capital except in the event of winding up. The company law also sanctions the creation of a reserve capital otherwise known as "**Reserve Liability**".

As per law, the company is required to pass a special resolution to determine that any portion of its share capital, which has not been already called-up shall not be capable of being called-up except in the event of its winding up. If such a resolution is passed, then that portion of its share capital shall not be called-up except in that event. The purpose of this capital is to protect the interest of the creditors in the event of winding up of the company.

Kinds of Share Capital

Share capital is not a condition precedent for incorporation of a company because the Act allows registration of companies without a share capital. But for trading companies capital is essential at every stage. The term capital, in relation to a company, can be broadly divided into four kinds. They are as below:

1. Equity Capital: It consists of equity shares and denotes the capital raised by the issue of equity shares.

2. Preference Share Capital: It consists of preference shares and denotes the capital raised through the issue of preference shares.

3. Debenture Capital: It consists of debentures and denotes the money raised by the issue of debentures. The debenture is only a debt of the company and comes under the category of borrowed capital.

4. Public Deposits: Now-a-days companies like commercial banks, accept deposits from the public. The rate of interest is generally attractive.

Methods of Raising Capital

A private company cannot raise capital by the public issue of share. Only a public company can issue its shares and debentures to the public and thereby mobilise the funds. There are three methods of raising the share capital from the public. They are

1. By directly selling the shares to the public (i.e., Public Issue),
2. By entering into an underwriting contract with the underwriters, and
3. By placing shares.

The company, when it feels that the whole issue may not be subscribed by the public it may either enter into an agreement with the underwriters or place the shares, so as to ensure the sale of the whole issue of the shares.

DEBENTURE

Debenture is most important instrument and method of raising the loan capital by the company. A debenture is like a certificate of loan or a loan bond evidencing the fact that the company is liable to pay a specified amount with interest and although the money raised by the debentures becomes a part of the company's capital structure, it does not become share capital.

Section 2 (30) of the Companies Act, 2013 define inclusively debenture as "debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.

Types of Debentures

There are several types of the debentures on the basis of the terms and conditions of the issue of the debentures. Let us now proceed to discuss the different classes of debentures.

Debentures on the basis of Registration

1. Registered Debentures: The debentures which are payable to the registered debenture holders are called registered debentures. The names of the holders of these debentures with details of the number, value and type of debenture held are recorded in the register of debenture holders. Registered debentures are not negotiable instruments. Transfer of such debentures requires registration.

2. Bearer Debentures: Bearer debentures are those which are payable to the bearer.The register of debenture holders does not have the names of the debenture holder recorded. Hence they are transferable by mere delivery. Registration of transfer is not necessary. Bearer debentures are also called as Unregistered Debentures.

Debentures on the basis of Security

1. Secured Debentures: The debentures, which are secured fully or partly by a charge over the assets of the company are called secured debentures. The charge may be either a fixed charge.or a floating charge. The charge, when created should be registered with the Registrar within 30 days of its creation.

2. Unsecured Debentures: The debentures, which are not secured fully or partly by a charge over the assets of the company are called unsecured debentures. The general solvency of the company is the only security for the holders. The debenture holders are treated as only unsecured creditors.

Debentures on the basis of Redemption

1. Redeemable Debentures: The debentures, which are repayable after a certain period, are called redeemable debentures. Sometimes, they can be redeemed by the company on demand by the holders or at the discretion of the company.

2. Irredeemable Debentures: The debentures, which are not repayable during the life time of the company, are called irredeemable debentures. The company may repay the money at the time of liquidation or on the happening of a contingency or on the expiration of a longer period or when the company breaches the terms of issue of the debentures.

Debentures on the basis of Conversion

1. Convertible Debentures: The debentures, which are convertible into equity shares or preference shares at the option of the holders, after a certain period, are called convertible debentures.

2. Non-Convertible Debentures: The debentures, which are not convertible into equity shares, are called non-convertible debentures.

Debentures on the basis of Priority

1. Preferred Debentures: The debentures, which are paid first at the time of winding up, are called preferred debentures or first debentures. Thus they are just like preference shares.

2. Ordinary Debentures: Debentures, that are paid after the preferred debentures during the winding up of a company are called ordinary debentures.

Debentures on the basis of Status

1. Equitable Debentures: Debentures, that are secured by deposit of title deeds of the property with a Memorandum creating a charge, are called equitable debentures. In this case, the property is with the company.

2. Legal Debentures: The debentures, which are secured by actual transfer of the legal ownership of the property from the company to the holder, are called legal debentures.

Debentures with Pari Passu Clause

The (secured) debentures, which are discharged ratably, though issued at different dates, are called debentures with pari passu clause.

Debenture Trust Deed

When a company issues mortgage debentures, it is a common practice to secure them by means of a Trust Deed conveying the company's property to the trustees to be held in trust for the benefit of the debenture holders. The trust deed contains the conditions governing the rights of the debenture holders and the relationship between them and the company. The trustees hold the property in trust for the debenture holders and safeguard their interests.

The trustees must act diligently and honestly in the discharge of their duties. Any clause in the trust deed, which, exempts them from liability for breach of their duty as trustees, is void.

Fixed and floating charges are used to secure borrowing by a company. Such borrowing is often done under the terms of a debenture issued by the company. Charges on a company's assets must be registered at Companies House and may also need to be registered in some other way, e.g. a charge on land and buildings must also be registered at the Land Règistry.

A fixed charge is a charge or mortgage secured on particular property, e.g. land and buildings, a ship, piece of machinery, shares, intellectual property such as copyrights, patents, trade marks, etc.

A floating charge is a particular type of security, available only to companies. It is an equitable charge on (usually) all the company's assets both present and future, on terms that the company may deal with the assets in the ordinary course of business. Very occasionally the charge is over just a class of the company's assets, such as its stock.

The floating charge is useful for many companies, allowing them to borrow even though they have no specific assets, such as freehold premises, which they can use as security. A floating charge allows all the company's assets, such as stock in trade, plant and machinery, vehicles, etc., to be charged.

The special nature of the floating charge is that the company can continue to use the assets and can buy and sell them in the ordinary course of business. It can thus trade with its stock and sell and replace plant and machinery, etc. without needing fresh consent from the mortgagee. The charge is said to float over the assets charged, rather than fixing on any of them specifically. This continues until the charge 'crystallizes', which occurs when the debenture specifies. This will include any failure to meet the terms of the loan (non-payment, etc.), or if the company goes into liquidation, ceases to trade, etc.

When the charge chrysalizes it fixes on the assets then owned by the company, catching any assets acquired up to that date, but missing any which have already been disposed of. If the charge was created before 15th. September 2003 the debenture-holder is then entitled to appoint an administrative receiver, whose job is to collect the assets charged to pay off the loan. This is what is usually meant when a company goes into receivership. If the charge was created after that date, the debenture-holder may appoint an administrator.

Most borrowing comes from the High Street banks, whose standard practice is to take an all-monies debenture, secured by fixed charges on any assets the company may have which will carry a fixed charge, and a floating charge on all other assets. This is the best security which can be created over the assets of any particular company. The bank may require other security from the directors and may want their personal guarantees.

Basis for Comparison	Fixed Charge	Floating Charge
Meaning	Fixed charge refers to a charge that can be ascertained with a specific asset, while creating it.	Floating charge refers to a charge that is created on the assets of circulatory nature.
Nature	Static	Dynamic
Registration of charge	Voluntary	Compulsory
What is it?	A legal charge.	An equitable charge.
Preference	First	Second
Asset type	Non-Current Asset	Current Asset
Dealing in asset	The company has no right to deal with the property, but subject to certain exceptions.	The company can use or deal with asset, until crystallization.

Definition of Fixed Charge

Fixed Charge is defined as a lien or mortgage created over specific and identifiable fixed assets like land & building, plant & machinery, intangibles i.e. trademark, goodwill, copyright, patent and so on against the loan. The charge covers all those assets that are not sold by the company normally. It is created to secure the repayment of the debt.

In this type of arrangement, the unique feature is that after the creation of charge the lender has full control over the collateral asset and the company (borrower) is left over with the possession of the asset. Therefore, if the company wants to sell, transfer or dispose off the asset, then either previous approval of the lender is to be taken, or it has to discharge all the dues first.

Definition of Floating Charge

The lien or mortgage which is not particular to any asset of the company is known as Floating Charge. The charge is dynamic in nature in which the quantity and value of asset changes periodically. It is used as a mechanism to secure the repayment of a loan. It covers the assets like stock, debtors, vehicles not covered under fixed charge and so on.

In this type of arrangement the company (borrower) has the right to sell, transfer or dispose off the asset, in the ordinary course of business. Hence, no prior permission of the lender is required and also there is no obligation to pay off the dues first.

The conversion of floating charge into fixed charge is known as crystallization, as a result of it, the security is no more floating security. It occurs when:

- The company is about to wind up.
- The company ceases to exist in future.
- The court appoints the receiver.
- The company defaulted on payment, and the lender has taken action against it to recover the debts.

Key Differences Between Fixed Charge and Floating Charge

The following are the major differences between fixed charge and floating charge:

1. The charge that can be easily identified with a certain asset is known as Fixed Charge. The charge which is created on assets that changes periodically is Floating Charge.
2. Fixed Charge is specific in nature. Unlike floating charge which is dynamic.
3. Registration of movable assets is voluntary, in the case of fixed charge. Conversely, when there is a floating charge, the registration is compulsory irrespective of the asset type.
4. The fixed charge is a legal charge while the floating charge is an impartial one.
5. Fixed Charge is given preference over floating charge.
6. The fixed charge covers those assets that are specific, ascertainable and existing during the creation of the charge. On the other hand floating charge, covers present or future asset.
7. When the asset is covered under fixed charge, the company cannot deal with the asset until and unless the charge holder agrees for so. However, in the case of floating charge the company can deal with the asset until the charge is converted to fixed charge.

Fixed Charge is created on fixed asset, no matter if they are tangible or intangible. Unlike Floating Charge, which covers the current assets of the company, which varies from time to time. Moreover, when the borrower defaults in the payment of outstanding debt, the floating charge becomes fixed charge.

DIVIDEND

The word "Dividend" has origin from the Latin word "Dividendum". It means a thing to be divided. Dividend means the portion of the profit received by the shareholders from the company's net profit, which is legally available for distribution among the members. Therefore, dividend is a return on the share capital subscribed for and paid to its shareholders by a company. Dividend defined under section 2(35) of the Companies Act, 2013, includes any interim dividend. Dividend: As per Section 2(35) of Companies Act, 2013 defines the term as including any interim dividend.

- Dividend is basically the share of profit distributed among shareholders.
- Ordinary meaning of dividend is a share of profits, whether at a fixed rate or otherwise, allocated to holders of shares in a company.
- Dividend can be paid on Equity or preference shares both.
- The word "Dividend" has origin from the Latin word "Dividendum". It means a thing to be divided.

Section under CA 2013	Section under CA 1956	Matters dealt with
2(35)	2(14A)	Definition of Dividend
51	93	Payment of dividend in proportion to amount paid up.
91	154	Declaration of book closure/Record date and publication of notice of record date/book closur
123	205	Payment of dividend-sources, conditions, transfer of profits to reserve, etc.
123(5)	205, 205A(3)	Dividend shall be paid to registered shareholders and beneficial owners under CSDL/NSDL Opening of a separate bank account for making payment of dividend and deposit the amount of dividend into the account within a period of 5 days of its declaration
126(6)	205	Restriction on payment of dividend on equity shares on failure to comply with Deposits
124	205A	Unpaid dividend to be transferred to special dividend account.
126	206A	Right of dividend, etc. — When to be kept in abeyance.
127	207	Payment of dividend must be made within 30 days of its declaration and penalty for failure to pay dividend within prescribed time limit.

Types of dividend: There are following types of dividend:—

a. Interim dividend; and

b. Final dividend

c. Preference share Dividend

Meaning of Final dividend:

Dividend is said to be a final dividend if it is declared at the annual general meeting of the company. Final dividend once declared becomes a debt enforceable against the company.

Source for payment of Dividend: Dividend can be paid out of Followings mentioned below: Section-123 (1)(a)

i. Profit of the current year after providing of the depreciation; or

ii. Profit of the previous financial year or years after providing for depreciation for previous years; or

iii. Out of the money provided by Central or State Government for payment of dividend in pursuance of guarantee given by that, if any.

In terms of the provisions of section 123 of the Act, no company can pay dividend in any year without charging depreciation in the profit and loss account for the current year and that there is no balance of un provided depreciation of any earlier year or years.

Depreciation shall be provided in accordance with the provisions of Schedule II to the Companies Act, 2013.

It refers to profits after tax.

Term 'Profit'- Profit can be either revenue profit or Capital profits or both. Thus, dividend can't be paid by revaluation of assets, as the surplus has not been actually realized.

For the purpose of prohibition of payment of dividend out of capital, capital means capital according to the Act and not the goods or things on which capital is laid out. [Lubbock v British Bank of South America (1892) 2 Ch. 198 (CA)]

Transfer portion of profit in reserve:

Before declaration of dividend, a company may transfer a portion from the profit to the reserves of the company. The company is free to decide the percentage for such transfer to the reserve.

It's not mandatory to transfer the amount. Earlier in Companies Act, 1956 it was Compulsory to transfer the amount in reserve while declaration of dividend. But the same is on the discretion of the Company in Companies Act, 2013.

Companies are free to transfer such percentage of its profits for that financial year as it may consider appropriate to the reserves. {First Proviso to Section 123(1) of the Companies Act, 2013}.

The reserve shall, at the discretion of the Board, be applicable for any purpose to which the profits of the company may be properly applied, including provision for meeting contingencies or for equalizing dividends. {As per Clause 82 (i) of Model Articles of Company Limited by shares as Contained in Table-F of Schedule-I of the 2013 Act}.

Declaration of Dividend:

Notice of Dividend:

{As per Clause 87 of Model Articles of Company Limited by shares as Contained in Table-F of Schedule-I of the 2013 Act} Notice of dividend declared shall be given to the persons entitled to share in it.

Process for declaration of Dividend:

{As per Clause 80 of Model Articles of Company Limited by shares as Contained in Table-F of Schedule-I of the 2013 Act}

i. Company in Board Meeting may decide the amount of dividend which they want to recommend in General Meeting.

ii. Company will mention the resolution for Dividend in the Notice of General Meeting.

iii. Company will hold the General Meeting:

  a. Declaration of Dividend is Ordinary Business.

  b. Ordinary Resolution for declaration of dividend will be passed in the General Meeting.

iv. Once dividend is declared, it must be paid within 30 days.

Note:

i. Dividend declared in General Meeting can't exceed the dividend recommended by the Board.

ii. Dividend declared in General Meeting by member can be less than the dividend recommended by the Board.

iii. Dividend paid in General Meeting is Final Dividend.

In the matter of payment of dividend or not in any financial year irrespective of the profit earned by a company in the financial year is left to the discretion of the Board to recommend or not to recommend dividend for any year. If the Board does not recommend any dividend, the company in general meeting cannot consider and approve any dividend for payment. The company in general meeting cannot also

Increase the rate of dividend recommended by the Board.

In Maharani Lalita Rajya Lakshmi v Indian Motor Co. (Hazaribagh) Ltd. (1962) 32 Comp Cas 207, the Division Bench of the Calcutta High Court rejected the grievance of the shareholders by observing thus: "It is then argued that the board of directors controlled by the managing agents has not been properly declaring dividends. In fact what is said in paragraph 21 of the petition is that dividend which is much below the actual profit earned by the company has been declared. I fail to see how this is an act of oppression to any member or members within the meaning of section 397 of the Companies Act, 1956 (Now section 241of the Companies Act, 2013). The board of directors has a discretion to declare dividend and the rate of such dividend. There is no company law that I know which obliges a board of directors to use up all its profits by declaring dividend. No company law lays down that all profits must be declared and exhausted in paying dividends. Surely, failure to do so could not be a ground for an application for oppression under section 397 of the Companies Act. Besides, that will also not be a ground for winding up a company as indicated by Lord Blanesburgh in the observation quoted above in the Privy Council decision of Ripon Press and Sugar Mill Co. Ltd. v Gopal Chetty." The decision has been followed by the Single Judge of Calcutta High Court, in the case of Jaladhar Chakraborty & Ors. v Power Tools & Appliances Co. Ltd. (1994) 79 Comp Cas 505.

Since the director's recommendation of dividend is only a proposal, it can be withdrawn by the Board before it is included in the notice for the annual general meeting. –

Where a dividend is approved by the shareholders at the annual general meeting, it becomes a debt against the company and it is deemed to be receivable by the members only in the year at which the members declared the dividend and not at the time when the dividend was recommended by the Board. [Tarajan Tea Co. (P) Ltd. v CIT (1994) 13 CLA 75 (Gau); Hanuman Prasad Gupta v Hiralal (1970) 40 Comp Cas 1058 (SC); Upendra Kumar Joshi v Manik Lal Chatterjee (1982) 52 Comp Cas 177 (Pat)]

Interim Dividend: {As per Clause 81 of Model Articles of Company Limited by shares as Contained in Table-F of Schedule-I of the 2013 Act}

i. Interim dividend can only be declared by board of Directors.

ii. Generally paid in the middle of the year if Board of directors fined that profitability of the Company.

iii. Board of Directors can declare dividend out of surplus in profit and loss account at the beginning of the year or profit during the year.

In case of Company incurred losses in current financial year:

If the company has incurred loss during the current financial year upto the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends by the company during the immediately preceding three financial year-Section 123(3).

Note:

i. Interim dividend is really a mod of keeping shareholder happy and keeping good image of Company in stock market.

ii. All legal provisions applicable on final dividend equally apply on interim dividend.

Condition common for Both Final Dividend and Interim Dividend:

i. Deposit of Amount of declared dividend in separate Bank Account.

ii. Payment of dividend within 30 days of declaration.

iii. Transfer of unpaid dividend in special account.

iv. Interest for late payment

v. Transfer of Investor protection Fund after Seven year.

vi. Penalty for nonpayment etc.

HOW TO DECIDE THE SHAREHOLDERS TO WHOM DIVIDEND WILL BE GIVEN:

Unlisted Companies (Include unlisted Public and Private Limited Company):

i. It is not necessary to close register.

ii. There are few transfers in these Companies.

iii. General Meeting can decide the 'Cut off' date or could be date of General Meeting.

In case of the annual dividend, the persons who are members as on the date of the annual general meeting will be eligible to receive the dividend as the dividend is approved by the members on the day when annual general meeting is held.

Listed companies are required to inform the Stock Exchange 1 [atleast 7 working days] in advance of closing the Register of members for payment of dividend declared at the annual general meeting for determining the names of shareholders entitled to dividend.

7. Whether shareholder can give director to the Company to pay his dividend to any third person?

Section 123(5) provides that no dividend shall be paid by a company in respect of any shares therein except to the

i. Registered holders of such shares or

ii. To his order to any person or

iii. To his Bankers

So it is clear that on the director of the register shareholder company can pay dividend to any third person.

8. In case of Transfer of shares, shares are still not registered on the name of the transferee then who will be entitled to receive the dividend on the point of view of the Company?

Merely because a person may have purchased or been in receipt of shares, in the absence of the shares being registered in his name in the books of account of the company, such a person is not entitled to receive the dividend, unless the shares lodged for transfer. The dividend has to be paid by the company in the name of the registered shareholders and it is the registered shareholders alone who claim dividend under section 27 of the Securities Contracts (Regulation) Act, 1956. [CIT v Aatur Holdings Pvt. Ltd. (2008) 146 Comp Cas 152 (Bom)]

Section 126 provides that where valid transfer deed has been lodged which has not been registered by the company, it shall withhold payment of the dividend on such shares till the shares are registered. This section does not apparently apply to a transfer, which has been refused. But where the rejection is on account of reasons like difference in signature, insufficient stamp, etc., it will be desirable for the company to wait and keep in abeyance the dividend till the irregularity is removed to enable the company to register the transfer and pay the dividend to the transferee.

In Nagarajan (S.V.) v Lakshmi Vilas Bank Ltd. (1997) 90 Comp Cas 392 (CLB): (1997) 26 CLA 308 (CLB), it was held that when a person comes with a petition as an aggrieved person all that is required to be seen is whether he has any such prima facie ground for seeking rectification and so long as he had such prima facie ground, he can come as an aggrieved person.

In such cases, the company shall transfer the dividend to the Unpaid Dividend account referred in section 124, unless the company has authorised by the registered holder of such shares in writing to pay such dividend to the transferee specified in such instrument of transfer.

9. In case of joint share holder who will be entitled to receive dividend?

In the case of Joint Holdings, the dividend shall be paid to the person whose name is registered first in the books. It may be noted that the person whose name is named first in the application for shares is entered first in the Register of members. There will be no objection to send the dividend to any other joint holder, if a request is made to the company signed by all the joint holders.

In other words:

i. In case of Joint shareholders, the cheque or warrant of dividend should be sent to the holder first named in the register of members.

ii. If the joint holders direct in writing the cheque or dividend can be send to another person as directed by the join shareholders { Regulation 85(i) of Model Articles Table- F as per the 2013 Act.}

10. In case of shares held in electronic mode, who will be entitled to receive dividend?

In case if the shares are held in electronic mode, the dividend will be paid to the beneficiaries whose names as may be provided by the CDSL/NSDL to the Company or its registrar on the record date or date of book closure as the case may be.

Mode of Payment of Dividend:

There are following Modes of Payment of Dividend: [Section- 123(5)]

a. Cash

b. Cheque

c. Dividend Warrant

d. In any electronic Manner.

Note:

i. Dividend should be paid by cheque or warrant sent through post to the registered address of the shareholder.

ii. Dividend can't be paid in 'KIND' e.g. in form of Gifts, Goods or Bonus Shares.

iii. Payment of dividend to another person as per order of the shareholder is permissible. This is also providing in {Regulation 85(ii) of Model Articles Table- F as per the 2013 Act.}

Issue of Shares with Differential Right:

If share with differential right have been issued, dividend will be declared and paid on the basis of terms of issue. {Regulation 83(iii) of Model AOA Table-F of the Act, 2013}.

A company which has default under Section 73 and 74 related to deposit and repayment of deposit or interest thereon may not declare dividend.

A company cannot declare dividend if the company fails to comply with acceptance of deposits and repayment of deposits accepted prior to the commencement of this Act. (Section 73 & 74 of Companies Act 2013.

Free Reserve:

No dividend shall be paid from its reserves other than free reserves. The term "Free Reserves" is defined under Section 2 (43) of the Company Act 2013. Free reserve means such reserve which, as per the latest audited balance sheet of a Company, are available for distribution of profit.

Punishment for Failure to Distribute Dividend (SECTION 127):

Where a dividend has been declared by a company but has not been paid or the warrant in respect thereof has not been posted within thirty days from the date of declaration to any shareholder entitled to the payment of the dividend, every director of the company shall, if he is knowingly a party to the default, be punishable with imprisonment which may extend to two years and with fine which shall not be less than one thousand rupees for every day during which such default continues and the company shall be liable to pay simple interest at the rate of eighteen percent per annum during the period for which such default continues.

No offence under this section shall be deemed to have been committed:—

(a) Where the dividend could not be paid by reason of the operation of any law;

(b) Where a shareholder has given directions to the company regarding the payment of the dividend and those directions cannot be complied with and the same has been communicated to him;

(c) Where there is a dispute regarding the right to receive the dividend;

(d) Where the dividend has been lawfully adjusted by the company against any sum due to it from the shareholder; or

(e) Where, for any other reason, the failure to pay the dividend or to post the warrant within the period under this section was not due to any default on the part of the company.

Some Important Points to be kept in Mind:

i. Declaration of dividend and amount to be transferred to reserve is responsibility of the Board.

ii. Bona fide decision of Board in respect of dividend can't be challenged.

iii. The dividend should be declared unconditional and must be paid within 30 days.

iv. Dividend on equity shares can be distributed only after dividend on preference shares is declared.

v. The amount of the dividend, including interim dividend, shall be deposited in a schedule bank in separate account within 5 days from the date of declaration of such dividend.

UNIT IV

CORPORATE GOVERNANCE

DEFINITION: DIRECTOR

Companies Act 2013 defines '**DIRECTOR**'. A director means a director appointed to the Board of a company. [s. 2(34)]

Interpretation:

- A Director is a person who is appointed by the board members unanimously with the help of poll.
- He has the responsibility for determining and implementing the company's policy.
- A company director need not be a shareholder or an employee and he may hold only the office of a director under the provisions of the Act.
- Directors derive their powers from the board resolutions
- Unlike shareholders, the directors cannot participate in proxy
- Unlike employees, they cannot absolve themselves of their responsibility for the delegated duties.

The '**BOARD OF DIRECTORS**'or '**BOARD**', in relation to a company means the collective body of directors of the company. [s.2(1)(10)]

There are mainly two kinds of Directors of a company;

1. Executive Director (includes Managing Director, Whole-time Director);
2. Non-Executive Director (includes Independent Director, Nominee Director)

AGE LIMITS FOR DIRECTORSHIP

To be a Director (of any kind) a person must have attended the age of majority in order to enter into contracts. Schedule v of the Act has put a mandatory condition that the Managing Director/ Whole-time Director / Manager to be appointed must have completed the age of 21 years(earlier under the 1956 Act it was 25 years) and has not attained the age of 70 years.

A person can be appointed as the Managing Director/ Whole-time Director/ Manager even if he has attained the age of 70 years by taking shareholders' approval by passing of a special resolution in a general meeting. Then the approval of the central government will not be required further.

In a listed company the age of Independent Director should not be less than 21 years of age – as per the Listing Agreement.

NATIONALITY OF A DIRECTOR

No nationality specific restrictions under the Act as to the appointment of the Directors.

A COMPANY CANNOT BECOME DIRECTOR I N ANOTHER COMPANY

According to section 149 of the Act, only individuals shall be appointed as Directors. Hence, no body corporate, association or firm shall be an appointed director of a company.

DISQUALIFIED PERSON CANNOT BE A DIRECTOR

A person disqualified to be appointed/ reappointed as a Director under section 164 of the Act cannot be appointed as a director of a company.

LEGAL POSITION OF DIRECTORS

Directors have been described as a company's 'directing mind and will'. They are the human agents of a company tasked with its management. Although the office they hold also resembles that of a trustee or a managing partner, directors remain creatures of statute, occupying a position 'peculiar to themselves'.

The position that the directors occupy in a corporate enterprise is a complicated one. They are professional men hired by the company to direct its affairs. Yet they are not the servants of the company. They are rather the officers of the company.

Moriarty v. Regent's Garage Co, *(1921)1KB 423*

Lush J, " A director is not a servant of any master. He cannot be described as the servant of the company or of anyone"

McCardie J, "A director is, in fact, a director or controller of the company's affairs. He is not a servant".

Lee v. Lee Air Farming Ltd. *1961 AC12*

Held: A director may, however, work as an employee in a different capacity.

In this case, the principal controller and director of a company was also working as its pilot. Following his death while acting as a pilot, his widow recovered compensation from the Workmen's Compensation Act.

However, this principle will not apply where no proof of employment apart from being a director is available.

Imperial Hydropathic hotel Co Blackpool v. Hampson *(1882)LR 23Ch D 1*

Bowen LJ," Directors are described sometimes as agents, sometimes as trustees and sometimes as managing partners. But each of these expressions is not used as exhaustive of their powers and responsibilities.

Coal Mining Co, re, *(1878)10 Ch D 451-52*

Jessel MR," Directors have sometimes been called trustees or commercial trustees and sometimes they have been called managing partners. It does not matter what name they are called as long as their true position is understood, which is that they are really commercial men managing a trading concern for the benefit of themselves and of all other shareholders in int"

DIRECTOR AS AGENT

The success of the company depends to a very large extent, upon the competence and integrity of its directors. As the company's agents, directors can bind the company with valid contracts entered into with third-parties such as buyers, lenders, and suppliers.

It was recognised as early as 1866 in ***Ferguson v. Wilson*** *(1866)LR 2 Ch 67*, that directors are in the eyes of the law, agents of the company. The court said:

" The company has no person; it can act only through its directors and the case is as regards to those directors, merely the ordinary case of Principal and Agent.

Therefore, the general principles of agency govern the relations of directors with the company and of persons dealing with the company through its directors. Where the directors contract in the name and on behalf of the company, it is the company which is liable on it and not the directors.

The position of directors as agents is superior to that of ordinary agents and hence, they are more than agents. An ordinary agent derives his authority from his principal but the directors as agents derives their authority not only from the principal which is the company by virtue of its Articles but they also derive their authority from the Act itself. Such Act cannot be overridden.

Kuriakose v. PKV Group Industries*(2002)111 Comp Cas 826*

A director was held to be not personally liable in a suit against a private chit fund company. Attachment of the property of the managing director was held to be not permissible.

PC Agarwala v. Payment of wages inspector *(2005) 8 SCC 104*

It was held that overdue wages could not be recovered from the director. There is no such liability unless there is a specific statutory provision to that effect.

NOTICE TO AGENT AMOUNTS TO NOTICE TO THE PRINCIPAL:

Just as notice to the agent in the course of business amounts to notice to the principal so it is true for directors in relation to the company.(1) But notice to the director will amount to a notice to the company only if the director is, like an agent, bound in the course of his duty to receive the notice and to communicate it to the company.

Hampshire Co, Re, *(1896) 2Ch 743*

Where one person is an officer of two companies, his personal knowledge is not necessarily the knowledge of both the companies unless he is under a duty to receive the notice and to communicate it to the other.

DUTY TO DISCLOSE PERSONAL INTEREST:

Like agents, directors have to disclose their personal interest, if any, in any transaction of the company.

Directors are the agents of an institution and not of its individual members, except when the relationship arises due to special facts of the case. The company can be held liable for the malice contended by its directors.

Ray Cylinders and & Containers v. Hindustan General Industries Ltd.

(2001)103 Comp Cas 161

In this case, permission granted to file a suit against a company was not allowed to be treated as permission against directors as well.

Indian Overseas Bank v. RM Mktg (P) Ltd *AIR 2002 Del 344*

It was held; For a loan taken by a company, the directors, who had not given any personal guarantee to the creditor could not be made liable merely because they were directors.

DIRECTOR AS EMPLOYEE

In the normal course, a director is elected by the shareholders in general meeting, and once he is so elected, he enjoys well-defined rights and powers under the Act or the Articles of association. Even the shareholders who elect them cannot interfere with their rights or powers except under certain circumstances. An employee

appointed by the company under a contract of service is a servant of the company. He does not enjoy any powers other than those vested in him by the employer, who can always direct his actions and interfere in his work.

In Lee Behrens & Co., Re, *[1961] 31 Comp. Cas. 143 (SC)*

In this case, it was held that there is nothing in law to prevent a director from accepting employment under the company under a special contract which he may enter into with the company.

Therefore, where a director accepts employment under the company under a separate contract of service, in addition to the directorship, he is also treated as an employee or servant of the company. He shall, in such a case, be entitled to remuneration and other benefits admissible to employees, in addition to his remune-ration as Director.

Directors are also treated as officers of the company for certain matters and are made liable along with the manager, secretary, etc. for the purpose of marking them as 'officers in default' for certain penalties for failure to comply with the provisions of the Act.

- **DIRECTOR AS "OFFICER":**

"officer" includes any director, manager or key managerial personnel or any person in accordance with whose directions or instructions the Board of Directors or any one or more of the directors is or are accustomed to act.

- **DIRECTOR AS "KEY MANAGERIAL PERSONAL"(KMP)**

In relation to a company, KMP includes;

(i) the Chief Executive Officer or the managing director or the manager;

(ii) the company secretary;

(iii) the whole-time director;

(iv) the Chief Financial Officer; and

(v) such other officer as may be prescribed;

- **DIRECTOR AS "OFFICER IN DEFAULT"**

It means an "Officer who is in default". For the purpose of any provision in this Act which says that an officer of the company who is in default shall be liable to any penalty or punishment by way of imprisonment, fine or otherwise, means any of the following officers of a company, namely;

(i) whole-time director; (ii) key managerial personnel; (iii) where there is no key managerial personnel, such director or directors as specified by the Board in this behalf and who has or have given his or their consent in writing to the Board to such specification, or all the directors, if no director is so specified; (iv) any person who, under the immediate authority of the Board or any key managerial personnel, is charged with any responsibility including maintenance, filing or distribution of accounts or records, authorises, actively participates in, knowingly permits, or knowingly fails to take active steps to prevent, any default; (v) any person in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act, other than a person who gives advice to the Board in a professional capacity;

http://taxguru.in/company-law/roles-responsibilities-directors-companies-act-2013.html (seen on 7.3.2016)

(vi) every director, in respect of a contravention of any of the provisions of this Act, who is aware of such contravention by virtue of the receipt by him of any proceedings of the Board or participation in such proceedings without objecting to the same, or where such contravention had taken place with his consent or connivance; (vii) in respect of the issue or transfer of any shares of a company, the share transfer agents, registrars and merchant bankers to the issue or transfer.

VI.DIRECTOR AS TRUSTEE:

Directors are trustees of the company's money and property. They safeguard them and use them for and on behalf of the company. According to Law of Trust, a Trustee holds legal ownership of the trust property of which the equitable ownership lies with the **cestui que trust (beneficiary)**. From this point of view directors are not full-fledged trustees.

A trustee can make contracts in respect of the trust property in his own name but the directors cannot do so. They can make such contracts under the common seal of the company. The company is the legal owner. In the Companies Act, the duties and rights of a trust are not defined as they are defined in the Law of Trust.

The directors are not trustees of a debt due to a company or for the company's creditors. The directors are hence quasi-trustees.

Directors are trustees of the company's money, properties and must account for all the money over which they exercise control and shall refund any money improperly paid away and shall exercise their powers honestly in the interest of the company and all the shareholders and not for their own interests.(1)

Ramaswamy Iyer v. Brahamayya & Co *(1996)1 Comp LJ 107*

The Madras High Court held; " The directors of a company are trustees for the company and with reference to their power of applying funds of the company and for misuse of the power they could be rendered liable as trustees and on their death, the cause of action survives against their legal representatives".

DIRECTORS HOLD A FIDUCIARY POSITION:

Directors, like trustees, occupy a fiduciary position. Almost all the powers of directors are powers in trust. The power to make calls, to forfeit shares, to issue further capital, the general powers of management and the powers to accept or refuse a transfer of shares are all powers in trust which have to be exercised in good faith for the benefit of the company as a whole.

The position of directors is fiduciary in nature with power delegated to them by the members. The directors should act in good faith. The directors do not hold any fiduciary relationship with individual members of the company. This principle was laid down in 1902 in ***Percival v. Wright*** *(1902)2 Ch 421*and holds good as a basic principle;

The court held: There is no fiduciary duty towards individual shareholders.

This principle was **reiterated** in ***Peskin v. Anderson*** *(2000) 2 BCLC*

The decision was **overruled** in ***Coleman v. Myers*** *(1977)2 NZLR 225*

Held; The court will not impose a fiduciary duty automatically upon directors when they enter into transactions with the company's shareholders. The court imposed a fiduciary duty due to the special circumstance of this case which is as follows;

There were face-to-face negotiations which the members who relied upon the directors to disclose all material circumstances and the directors had a high degree of inside knowledge and the directors actively promoted the scheme and advised the shareholders to accept.

A director is a trustee of an institution and not merely an attorney of the investor.

CURRENT SCENARIO:

Now there is a statutory obligation to disclose any profit to the shareholders along with the offer by which their shares are proposed to be acquired. Section 30-32 of the Companies Act 2013.

The modern company should not simply function as an economic machine designed to churn out profits for its shareholders, but as an institution which owes social responsibilities to a wide circle of interests.

Hence, the directors have to consider the interests of labour, consumers, the general public and the State. Public responsibility of a company means to take into account the outside interests affected by corporate operations.

To the extent the directors are bound to consult the outside interests, they become trustees of such interests.

VII. DIRECTOR AS MANAGING PARTNER

Viewing a company as a large partnership, directors are being charged with the responsibility of managing the affairs. The other shareholders are virtually dormant partners. By virtue of the various provisions in the Memorandum and Articles, the directors enjoy vast powers of management and act as the supreme policy and decision making body.

VIII. DIRECTORS AS ORGANS OF CORPORATE BODY

In earlier times it became difficult to hold a company to its responsibilities in view of the artificial nature of its personality. The company could not be held responsible for any wrong involving mental element. But today the range of corporate responsibilities almost corresponds with that of an individual by saying that they are a corporation. This transformation has been brought under the influence of the organic theory of corporate life.

Gopal Khaitan v. State AIR1969 Cal132

Talukdar J, " A theory which treats certain officials as organs of the company, for whose action the company is to be held liable just as a natural person is for the action of his limbs".

Thus, the modern directors are something more than mere agents or trustees. The Board is also correctly recognised to be a primary organ of the company.

Lennard's Carrying Co Ltd. v. Asiatic Petroleum Co Ltd *1915 AC 705*

In this case, the ship owner was an incorporated company and the loss has taken place due to the negligence of the managing director. The company was sued for the loss and its chief defence was that the company, being an artificial person, was incapable of committing "actual fault".

Lord HALDANE said "A corporation is an abstraction. It has no mind of its own any more than it has a body of its own. The company's acting and directing must be sought in the person of somebody who for some purpose may be called an agent, but who is actually the directing mind and the will of the corporation. That person may be the Board of directors itself.

Based on the principle of **respondent superior**, the company is responsible for the action of somebody, whose very action is the action of the company itself.

But the courts have not attempted to define the persons whose acts or intentions are to be considered the acts or intentions of the company. It has been suggested that it would include the company's governing body, directors, managing director or general manager or other persons having authority from the Board of directors to conduct the company's business.

For certain purposes, even the secretary has been recognised as an essential organ. In

Panorama Developments (Guildford) Ltd v. Fidelis Furnishing Fabrics Ltd *(1971)2 QB71*
A company was held liable for the hire of taxis engaged by the secretary for his personal purposes while operating from the office of the company. **Lord Denning MR** said "A modern secretary is not a mere clerk but an officer of the company with extensive duties and responsibilities and has authority to sign contracts connected with the administrative side of a company's affairs and has the ostensible authority to enter into a wide range of contracts.

This decision has materially altered the position of a secretary since the 19th century.

IX. LIABILITY OF DIRECTORS

PERSONAL LIABILITY OF WORKING ORGAN

QUESTION: When a **tort** or some other **wrong** occurs in the working processes of the company, the question is whether the responsibility for it is to be attributed to the company or it is to be borne by the director alone?

Principle laid down in;

C Evans & Sons Ltd v. Spritebrand Ltd *1985BCLC 10546*

Held; "A director of a company is not automatically identified with his company for the Purpose of the law of tort, however small the company may be and, however powerful his control over its affairs. In every

case where it is sought to make him liable for his company's torts, it is necessary to examine with care what part he played personally in regard to the act or acts complained of ".

Trevor Ivory Ltd v. Anderson *(1992)2NZ LR 5177*

In this case, the director of a one-man company gave advice through the company, to a client for spraying of an insecticide around fruit trees. The advice was so negligent that fruit trees perished along with their parasites. The Court did not hold the director personally liable. He had made it clear that he was trading through the company and the company was the legal contracting party to be charged with liability.

Fairline Shipping Corpn v. Adamson *1976QB180*

In this case, the director became personally liable for loss of perishable goods from the storage provided by his one-person company. The liability hinged on a letter written by the managing director to the plaintiffs on his own note paper rather than that of the company, an act which the court thought displayed an assumption to personal duty to care.

LIABILITY FOR BOUNCING OF CHEQUES:

A company would be liable to be prosecuted for the bouncing of a cheque if it was issued in the authority of the company.

Unico Trading and chit Funds (India) (P) Ltd v. Zahoor Hassan *(1991)71Comp Cas 270(Kant)*

In this case, a complaint was alleged that the cheque was issued by a director who was in charge of and responsible for the day to day administration of the affairs of the company. It was held that the director was not liable.

LIABILITY OF NON-EXECUTIVE / INDEPENDENT DIRECTORS

An independent director and a non-executive director not being promoter or key managerial personnel shall be held liable only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

LIABILITY AS "OFFICER"

SECTION 66 (REDUCTION OF CAPITAL)

If any officer of the company—

(a) Knowingly conceals the name of any creditor entitled to object to the reduction; (b) Knowingly misrepresents the nature or amount of the debt or claim of any creditor;

or (c) Abets or is privy to any such concealment or misrepresentation as aforesaid, he shall be liable under section 447.

SECTION 105 (PROXIES)

If for the purpose of any meeting of a company, invitations to appoint as proxy a person or one of a number of persons specified in the invitations are issued at the company's expense to any member entitled to have a notice of the meeting sent to him and to vote thereat by proxy, every officer of the company who knowingly issues the invitations as aforesaid or wilfully authorises or permits their issue shall be punishable with fine which may extend to one lakh rupees.

Provided that an officer shall not be punishable under this sub-section by reason only of the issue to a member at his request in writing of a form of appointment naming the proxy, or of a list of persons willing to act as proxies, if the form or list is available on request in writing to every member entitled to vote at the meeting by proxy.

SECTION 173 (MEETING OF BOARD)

Every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of twenty-five thousand rupees.

SECTION 204 (SECRETARIAL AUDIT)

If a company or any officer of the company or the company secretary in practice contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

SECTION 207 (CONDUCT OF INSPECTION AND ENQUIRY)

If any director or officer of the company disobeys the direction issued by the Registrar or the inspector under this section, the director or the officer shall be punishable with imprisonment which may extend to one year and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company.

SECTION 212 (INSPECTION BY SFIO)

On receipt of the investigation report, the Central Government may, after examination of the report (and after taking such legal advice, as it may think fit), direct the Serious Fraud Investigation Office to initiate prosecution against the company and its officers or employees, who are or have been in employment of the company or any other person directly or indirectly connected with the affairs.

Notwithstanding anything contained in this Act or in any other law for the time being in force, the investigation report filed with the Special Court for framing of charges shall be deemed to be a report filed by a police officer under section 173 of the Code of Criminal Procedure, 1973 of the company.

SECTION 274 (DIRECTIONS FOR FILING STATEMENT OF AFFAIRS – WINDING UP BY TRIBUNAL)

If any director or officer of the company contravenes the provisions of this section, the director or the officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.

LIABILITY AS "OFFICER IN DEFAULT"

- Directors are liable as officers in default under all sections where specific penalty is provided for each officer in default.
- Where no specific penalty is provided under the Act, they are liable under Section 450.

LIABILITY FOR "FRAUD"

"Fraud" in relation to affairs of a company or any body corporate includes any act omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss;

Any person who is found to be guilty of fraud, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud.

PERSONAL LIABILITY

Directors can be made personally liable in the following situations;

- When the directors enter into contract in their own name.
- When they enter into contracts on behalf of company but fails to use "LTD. Or PVT LTD."
- When directors exceed their powers
- The Board of Directors should act as an agent of the company and not of a single director. Therefore a single director cannot enter into a contract on behalf of company unless the Board of Directors authorise.

SECTION 35 – CIVIL LIABILITY FOR MIS-STATEMENT IN PROSPECTUS

Where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person concerned shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.

SECTION 75 – DAMAGES FOR FRAUD-FAILURE TO REPAY DEPOSIT

Where a company fails to repay the deposit or part thereof or any interest thereon referred to in section 74 within the time specified in sub-section *(1) of that section* or such further time as may be allowed by the Tribunal under sub-section*(2) of that section* and it is proved that the deposits had been accepted with intent to defraud the depositors or for any fraudulent purpose, every officer of the company who was responsible for the acceptance of such deposit shall, without prejudice to the provisions contained in subsection *(3)* of that section and liability under section 447, be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by the depositors.

SECTION 339 – LIABILITY FOR FRAUDULENT CONDUCT OF BUSINESS

If in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal, on the application of the Official Liquidator, or the Company Liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare that any person, who is or has been a director, manager, or officer of the company or any persons who were knowingly parties to the carrying on of the business in the manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Tribunal may direct.

Thus the Act has introduced significant changes in the provisions with respect to directors. The penalties for contravention under different sections have been increased from a minimum of Rs. 010,000 to a minimum of Rs. 50,000 to bring in more accountability. The Act has introduced high levels of responsibility and introduced high standards for directors so that they are accountable to the shareholders for their action and personally liable for any damage caused by them. But the effectiveness of these provisions will depend only on how strictly they are enforced.

INDEPENDENT DIRECTORS

The companies Act 2013 has introduced the concept of independent directors for listed companies and extended it even to prescribed public unlisted companies. The criterion for independent directors is more stringent than in listing agreement. Further now the independent directors are requires to be appointed from a data bank maintained for that purpose. The Act seeks to define the role and duties of independent director in schedule IV.

Qualifications of independent directors

Independent director needs to possess following qualifications at the time of his appointment and during the term of his appointment:

- He should possess qualifications of a director and should not be otherwise disqualified to be appointed as a director.
- He is not a managing director or whole time director or nominee director.
- He is a person of integrity and possesses relevant expertise and experience in the opinion of the Board.

- He is not a promoter of the company or its holding, subsidiary or associate company.
- He has never been a promoter of the company or its holding, subsidiary or associate company.
- He is not related to promoters or directors in the company, its holding, subsidiary or associate company.
- He has no pecuniary relationship with the company, its holding, subsidiary or associate, or their promoters, or directors.
- He had no pecuniary relationship with the company, its holding, subsidiary or associate company, r their promoters, or directors, during the two immediately preceding financial years or during the current financial year.
- None of his relatives has or had pecuniary relationship or transaction with the company, its holding, subsidiary or associate company, or their promoters, or directors, amounting to two per cent, or more of its gross turnover or total income or Rs 50 lakh or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year.
- He or his relative does not hold and has never held the position of a key managerial personnel or is or has been employee of the company or has been or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed.
- He or his relative is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of –
  a. A firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary or associate company; or
  b. Any legal or a consulting firm that has had any transaction with the company, its holding, subsidiary or associate company amounting to ten per cent or more of the gross turnover of such firm.
- He or his relative holds together with his relatives two percent or more of the total voting power of the company.
- He or his relative is not a chief executive or director, by whatever name called, of any non profit organisation that receives twenty five percent or more of its receipts from the company, any of its promoters, directors or its holding, subsidiary or associate company or that holds two per cent or more of the total voting power of the company.
- More qualification can be specified by the Central Government and those will have to be complied with.

CORPORATE SOCIAL RESPONSIBILITY

Corporate social responsibility is nowadays considered to be the most important part of business. Philip Koller as well as Naney Lee specify CSR as a "determination to raise community health by means of discretionary company techniques with management and business resources." CSR is a term for the actual requirements associated with entrepreneurs to help constantly abide by procedures to procure selections as well as to take up these relationships that are relating to help phrases from the ambitions as well as values your modern society. The concept of CSR rests on the ideology of give and take. Companies take resources etc from the society. By performing the task of CSR activities the companies are giving something back to the society.

Indian Companies Act 2013 has introduced several new provisions which change the face of Indian corporate business. One such important provision is CSR. The Minstry of Corporate Affairs has recently notified section 135 and schedule VII of the companies Act as well as the provisions of Corporate Social Responsibility Policy Rules 2014 which has come into effect from April 2014.

Section 135 of the companies Act provides the threshold limit for applicability of the CSR to the company that is

b) Net worth of the company to be Rs 500 crore or more;

c) Turn over of the company to be Rs 1000 crore or more;

d) Net profit of the company to be Rs 500 crore or more.

Further as per the CSR Rules, the provisions of CSR are not only applicable to Indian companies, but also applicable to branch and project offices of a foreign company in India.

Every qualifiying company requires spending of at least 2% of its average net profit for the immediately preceding 3 financial year on CSR activities. Further, the qualifying company will be required to constitute a committee of the Board of Directors consisting of 3 or more directors. The CSR committee shall formulate and recommend to the board a policy which shall indicate the activities to be undertaken in corporate social responsibility policy; recommend the amount of expenditure to be incurred on the activities referred and monitor CSR policy of the company. The Board shall take into account the recommendations made by the CSR committee and approve the CSR policy of the company.

The term CSR has been defined under the CSR Rules which includes but is not limited to

1. Projects or programs relating to activities specified in the schedule; or

2. Projects or programs relating to activities undertaken by the board in pursuance of the recommendations of the CSR committee as per the declared CSR policy subject to the conditions that such policy covers subjects enumerated in the schedule.

The definition of CSR assumes significance as it allows companies to engage in projects or programs relating to activities enlisted under the schedule. Flexibility is also provided to the companies by allowing

them to choose their preferred corporate social responsibility engagements that are in conformity with the CSR policy. However in determining CSR to be undertaken preference would be given to local areas and the areas around where the company operates. TATA, TESCO, AMBUJA Cements are some of the companies which are engaging in CSR activities.

INSIDER TRADNG

Corporate governance and insider trading are opposed to each other as they are contradictory in nature. They are contradictory in the sense that the former curbs transparency to the share holders of the corporate entity while the latter promotes the same. Hence it is regarded as a menace to corporate governance.

Generally in a company meetings are held to ensure that the shareholders come together once in a year to ensure and review the working of the company. The information released in the Annual Report and Annual General Meeting relate to the performance of the company and hence play a valuable role in shaping the minds of the existing and prospective shareholders. The general public and shareholders get knowledge of this information only during the Annual General Meeting or when the company announces it in a press conference, etc. however persons in the company itself or otherwise concerned to the company are in possession of such information before it actually made public. This knowledge of this unpublished price sensitive information in hands of persons connected to the companies puts them in an advantageous position over others who lack it. Such information can be used to make gains by buying shares at a cheaper rate anticipating that it might rise. Similarly it can be used to insulate themselves against losses by selling shares before the prices fall down. Such transaction entered into by persons having access to any unpublished price sensitive information is called insider trading. Such trading s not based on a level playing field and can prove detrimental to the interests of the shareholders of the company. Consequently SEBI [The Securities and Exchange Board of India] banned insider trading and laid down the SEBI (prohibition of Insider Trading) Regulations 1992.

According to the above said regulation an insider is, "Any person who, is or was connected with the company or is deemed to have been connected with the company, and who is reasonably expected to have access, by virtue of such connection, to unpublished price sensitive information i respect of securities of the company or who has received or has had access to such unpublished price sensitive information."

SEBI (prohibition of Insider Trading) Regulations 2015 has come into force with effect from 15th May 2015 after having been gazetted on 15th Jan 2015.it replaces the regulations of 1992 which was amended in the year 2002. The regulation of 2015 is with the same name and style with 2015 substitution of 1992.

The companies Act 2013 is partially in force certain provisions of the Companies Act 1956 are still in force.

Section 195 of the Companies Act 2013 provides for prohibition of insider trading of securities. Prior to this provision there was no provision regarding insider trading under the Companies Act 1956.

Definitions under the new Act:

Regulation 2(g) defines Insider as

1. A connected person.
2. In possession of or having access to unpublished price sensitive information.

Regulation 2(i) defines Trading as

"Trading to mean and include subscribing buying, selling or dealing or agreeing to subscribe, buy, sell, deal in any securities and trade shall be construed accordingly."

Section 2(I) defines unpublished price sensitive information

"Any information relating to a company or its securities, directly or indirectly that is not generally available which upon becoming generally available is likely to materially affect the price of the securities and shall, ordinarily including but not restricted to, information relating to the following:

1. Financial results.
2. Dividends.
3. Change in capital structure
4. Mergers, demergers, acquisitions de listings disposals and expansion of business and such other transaction.
5. Changes in key managerial personnel.
6. Material events in accordance with the listing agreement.

Hindustan Lever Ltd. V. SEBI, Rakesh Aggarwal v. SEBI, Dilip Pendse v. SEBI, Securities Exchange Commission v. Rajat Gupta, are some of the land mark decisions regarding insider trading.

AUDITORS

There are tremendous changes in new Companies Act 2013 with subject to auditors as compared to the old Act. The new Act intends to improve corporate governance and to further strength regulations. The onus and responsibilities of auditors becomes cumbersome and lots of responsibilities are imposed under the new Act and Rules.

POWERS AND DUTIES OF AUDITORS (SECTION 143)

Powers:

1) **Right to Access**

Every auditor of a company shall have right to access at all time to book of accounts and vouchers of the company. The auditor shall be entitled to require from officers of the company such information and

explanation as he may consider necessary for performance of his duties. There is an inclusive list of matter for which auditor shall seek information and explanation. This list helps auditors to take special care on serious issues. Those issues are:

1. Proper security for loan and advances.
2. Transaction by back entries.
3. Sale of assets in securities in loss.
4. Loan and advances made shown as deposits.
5. Personal expenses charged to revenue account.
6. Cash received for share allotted for cash

2) **Right to Remuneration** (section 142)

The remuneration of the auditor of a company shall be fixed in its general meeting or in such manner as may be determined therein. It must include the expenses, if any, incurred by the auditor in connection with the audit of the company and any facilities extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company.

3) **Auditor to sign Audit Reports** (section 145)

The auditor of the company shall sign the auditors reports or sign or certify any other documents of the company and financial transactions or matters, which have any adverse effect on the functioning of the company mentoned in the auditors report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

4) **Auditor in General Meeting** (section 146)

All notice of and communications relating to any general meeting have to be forwarded to the auditor of the company. The auditor has either himself or through authorised representations who should also be qualified as an auditor has to attend any general meeting and is to be heard at it on any part of the business which concerns him as an auditor.

DUTIES

1) Make Report

The auditor shall make a report to the members of the company on accounts examined by him on every financial statements.

The auditor report shall also state:

a. Whether he has sought and obtained all the necessary information and explanations.

b. Whether proper books of accounts have been kept.

c. Whether company's balance sheet and profit and loss account are in agreement with books of accounts and returns.

2) Audit Report of Government Company

The auditor of the government company will be appointed by the Comptroller and Auditor General of India and such auditor shall act according to the directions given by them. He must submit a report to them which should include the action taken by him and impact on account and financial statement of the company. The Comptroller and Audit General of India shall within 60 days of receipt of the report have right to

a. Conduct a supplementary audit and

b. Comment upon or supplement such audit report.

The comptroller and audit general of India may cause test audit to be conducted of the accounts of such company.

3) Liable to pay Damages

As per section 245 the depository and members of the company have right to file an application before the tribunal if they are of the opinion that the management or conduct of the affairs of the company being conducted in a manner prejudicial to the interests of the company. They also have right to claim damages or compensation from the auditor including audit firm of the company for any improper or misleading statement of particulars made in his audit report or for any fraudulent unlawful or wrongful act or conduct.

4) Branch Audit

Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company, or by any other person qualified for appointment as an auditor of the company. The branch auditor of the company who shall deal with it in his report is necessary.

5) Auditing Standards

Every auditor shall comply with the auditing standards. The central government shall notify these standards in consultation with national Financial reporting Authority. The government may also notify that auditors report shall include a statement on such matters as notified.

6) Fraud Reporting

If an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the central government within such time and in such manner as may be prescribed.

7) Winding up

As per section 305 at the time of voluntary winding up of a company it is a mandatory requirement that auditor should attach the copy of the audits of the company.

Auditor not to render certain services (section 144)

Mandatory requirement of approval for permissible services by Board of Directors or the audit committee as the case may be. Auditor is not allowed to render the following services either directly or indirectly to the company, its holding or subsidiary company:

a. Accounting and book keeping services.

b. Internal Audit.

c. Design and implementation of any financial information system.

d. Actuarial services.

e. Investment advisory services.

f. Investment banking services.

g. Rendering of outsourced financial services.

h. Management services.

i. Any other services as may be prescribed.

j. Compliance to be ensured before closure of first financial year after enactment of 2013 Act prohibited.

k. Terms such as investment advisory services, management services and investment banking services are not defined. This may give rise to diverse practices.

l. Restrictions apply to the audit client and its parent and subsidiary company, whether the parent and / or subsidiary company is located within or outside India.

m. Restriction under section 144 of the Act does not apply to sister concerns of audit clients and investor/ investees of audit clients.

n. In case the same auditor audits both parent and subsidiary company and proposes permissible services to the subsidiary company, the Board or audit committee approval is required from subsidiary company only and not the parent company.

OPPRESSION AND MISMANAGEMENT

Minority shareholders protection has always been the concern of company law in different parts of the world. The phrase minority protective means remedies evolved to safeguard a minority of company members from the abuse of the majority rule. There are various ways in which the law protects minority interests. Minority shareholders should be protected from abusive actions by, or in the interest of, controlling shareholders acting either directly or indirectly, and should have effective means of redressal.

The Companies Act 2013 has retained the remedy of oppression and mismanagement. This is a remedy for protecting the minority investors. A member and government can apply for oppression and mismanagement. The remedy of oppression and mismanagement can be applied for if the following conditions are satisfied:

a. Oppression: An application can be made if the affairs are conducted in a manner prejudicial to the interests of the public or the company or it is otherwise oppressive to the members.

b. Mismanagement: An application can also be made when there is a material change in the management or control of the company, which makes it likely that the affairs of the company will be conducted n a manner prejudicial to its interests or its members or any class of members. However if such change is for the benefit or interest of certain creditor or members then it will not be considered as mismanagement.

Eligibility Criteria:

The criteria for company having share capital

- Hundred members or one tenth of the total number of its members whichever is less, or
- Any member or members holding not less than one tenth of the issued share capital of the company.

The criteria for company not having share capital

- One fifth of the total number of its members:

A representative suit can also be filed by a member or members with the written consent from other members.

If the Tribunal considers a case to be deserving it can waive or relax the eligibility criteria for the benefits of the members. The Tribunal is given complete freedom to bring an end to the oppression and mismanagement. Certain powers that can be exercised are enumerated below. They are categorised as existing power which were specified in the old Act and new powers which are inserted in this Act:

Existing Powers

- The regulation of conduct of affairs of the company in future.
- The purchase of shares or interests of any members of the company by other members thereof or by the company and reduction of capital if the shares are acquired by the company.
- The termination, setting aside or modification, of any agreement, between the company and its MD/ Director / Manager.
- The setting aside of any transfer, delivery of goods, payment, execution or other act relating to property made or done by or against the company within three months before the date of the application under this section, which would, if made or done by or against an individual, be deemed in his insolvency to be a fraudulent preference.

New / Modified Powers

- The termination, setting aside or modification of any agreement between the company and any person other than MD/ Director / Manager. This can be done after obtaining the consent of the party concerned. Earlier for termination, the consent of the other party was not required.
- Restrictions o the transfer or allotment of the shares of the company.
- Removal of the MD/ manager/ Director of the company.
- Recovery of undue gains made by any MD/ manager/ Director during the period of his appointment. Determine the manner in which the amount said so recovered shall be utilised.

Rationale

When the Satyam Fraud was unveiled, the Central Government approached the Company Law Board claiming relief in the case of oppression and mismanagement. They sought several reliefs many of which were granted by CLB. However, in the hindsight it seems that CLB was not empowered by the Act to grant these reliefs. The examples of such reliefs granted in that case are as follows:

- Suspension of the entire board of the Satyam and removal of the auditor.
- Empowering the Central Government to nominate a new Board.
- Conferring immunity of the nominees of the Board.
- Restraining the judicial forums from taking any action against the government nominees for wrongs committed by them.
- Introduction of a strategic partner by making a preferential allotment without the consent of the shareholders of Satyam.

The Tribunal is given wide powers to pass orders in cases of fraud such as Satyam. The additional powers enumerated in the section, though not exhaustive, ensure that the scope of powers of Tribunal at least as regards those matters shall not be questioned in the higher forums.

Rule in *Foss v. Harbottle*

For over a century, the rule that was followed in England was that the courts were not justified in interfering with the matters of a company. This was first expounded by the court in Foss v Harbottle, in which the cardinal rule which was laid down is reproduced as below:

"On the first point it is only necessary to refer to the clauses of the Act to shew that, whilst the supreme governing body, the proprietors at a special general meeting assembled, retain the power of exercising the functions conferred upon them by the Act of Incorporation, it cannot be competent to individual corporators to sue in the manner proposed by the Plaintiffs on the present record. This in effect purports to be a suit by cestui que trusts complaining of a fraud committed or alleged to have been committed by persons in a fiduciary character. The complaint is that those trustees have sold lands to themselves, ostensibly for the

benefit of the cestui que trusts. The proposition I have advanced is that, although the Act should prove to be voidable, the cestui que trusts may elect to confirm it. Now, who are the cestui que trusts in this case? The corporation, in a sense, is undoubtedly the cestui que trust; but the majority of the proprietors at a special general meeting assembled, independently of any general rules of law upon the subject, by the very terms of the incorporation in the present case, has power to bind the whole body, and every individual corporator must be taken to have come into the corporation upon the terms of being liable to be so bound. How then can this Court act in a suit constituted as this is, if it is to be assumed, for the purposes of the argument, that the powers of the body of the proprietors are still in existence, and may lawfully be exercised for a purpose like that I have suggested? Whilst the Court may be declaring the acts complained of to be void at the suit of the present Plaintiffs, who in fact may be the only proprietors who disapprove of them, the governing body of proprietors may defeat the decree by lawfully resolving upon the confirmation of the very acts which are the subject of the suit. The very fact that the governing body of proprietors assembled at the special general meeting may so bind even a reluctant minority is decisive to shew that the frame of this suit cannot be sustained whilst that body retains its functions..."

In substance, the "majority rule principle" states that if the alleged wrong can be confirmed or ratified by a simple majority of members in a general meeting then the court will not interfere, *cadit quaestio.*

This rule could be justified on two grounds – firstly that the corporation in itself constitutes a legal personality and therefore any injuries caused to the corporation by the majority shareholders should be remedied by the corporation itself and not any individual member.This is known as the 'corporation principle' – "the proper plaintiff in an action in respect of a wrong alleged to have done to a company or association of persons is prima facie the company or association itself." Secondly there is a "partnership doctrine" which was held by the equity courts in the early 19th century that the affairs between one partner and another were out of bounds for the courts except in cases of dissolving the partnership.

Exceptions

The majority rule had certain exceptions to it, thus affording remedy to individual members in common law:

1. Where the act complained is illegal or ultra vires the company;
2. Where the act done by the majority inflicts fraud on the minority;
3. Where a resolution is passed by a simple majority for any act which specifically requires a resolution by special majority;
4. Infringement of individual rights of a member;

The rule in Foss is very notorious when it comes to the administration of justice and fairness. It allows the majority to perpetuate anything and everything on the minority shareholders in a company by virtue of its deceptive simplicity. The majority cannot complain about any wrong on the corporation itself or internal improprieties. Such a bottleneck approach is in absolute dissonance with the basic notion of shareholding i.e. every shareholder has an interest in the company by virtue of his share in the capital and it is the duty of the management to protect this interest.

Shift from The Rule

Since Indian company law (S. 397) has been borrowed essentials from English law (S. 210 English CA 1948), it is imperative that we look at some of the landmark decisions in England.

"210. (1) Any member of a company who complains that the affairs of the company are being conducted in a manner oppressive to some part of the members (including himself) or, in a case falling within [s. 169(3)], the Board of Trade, may make an application to the court by petition for an order under this section.

(2) If on any such petition the court is of opinion—

(a) that the company's affairs are being conducted as aforesaid; and

(b) that to wind up the company would unfairly prejudice that part of the members, but otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up;

the court may, with a view to bringing to an end the matters complained of, make such order as it thinks fit, whether for regulating the conduct of the company's affairs in future, or for the purchase of the shares of any members of the company by other members of the company or by the company and, in the case of a purchase by the company, for the reduction accordingly of the company's capital, or otherwise."

While there is no consistent link in the various judgements it can be safely said that the English Courts have abandoned their traditionally conservative approach towards allowing such petitions by giving the provisions a wider interpretation, thereby increasing the access to justice. The first case is the landmark judgement of *Scottish Co-operative Wholesale Society Ltd. v. Meyer*[ix] where it was held that recourse to Section 210, was possible when it was shown that the company was suffering damage and that remedy under the section was not barred in case of minor oppression. This judgment significantly increased the scope of the recourse available by watering down the requirement of proving that the company must be wound up. As per Lord Denning:

"The object of the remedy is to bring 'to an end the matters complained of' that is, the oppression, and this can be done even though the business of the company has been brought to a standstill. If a remedy is available when the oppression is so moderate that it only inflicts wounds on the company, whilst leaving it active, so, also, it should be available when the oppression is so great as to put the company out of action altogether. Even though the oppressor by his oppression brings down the whole edifice – destroying the value of his own shares with those of everyone else – the injured shareholders have, I think, a remedy under Section 210."

However the decision of the Court has to be balanced against the decision subsequently in In *Re H. R. Harmer Ltd.*, where the Court increased the standard of oppression, thereby limiting the availability of the recourse to members:

"This indicates that the oppression complained of must be complained of by a member of the company and must be oppression of some part of the members (including himself) in their or his capacity as members or a member of the company as such. Secondly, it is to be noted that the section does not purport to apply to every case in which the facts would justify the making of a winding up order under the 'just and equitable' rule, but only to those cases of that character which have in them the requisite element of oppression. Thirdly, the phrase 'the affairs of the company are being conducted' suggests, prima facie, a continuing process and is wide enough to cover oppression by anyone who is taking part in the conduct of the affairs of the company, whether de facto or de jure. Fourthly, the section gives no guidance as to the meaning of the word 'oppressive', although it does, as already mentioned, indicate that the victim or victims of the oppressive conduct must be a member or members of the company as such. Prima facie, therefore, the word 'oppressive' must be given its ordinary sense and the question must be whether in that sense the conduct complained of is oppressive to a member or members as such. Inasmuch as in the present case it is not in dispute that the facts would justify a winding up order under the 'just and equitable' rule and it is recognised that such an order would unfairly prejudice the complaining members, this would appear to be, in effect, the only question in issue."

Statutory Remedies

Section 994 CA 2006 provides that:

A member of a company may apply to the court by petition for an order...on the ground

(a) that the company's affairs are being or have been conducted in a manner which is unfairly prejudicial to the interests of its members generally or of some part of its members (including at least himself), or

(b) that any actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial.

Section 996 confers on the court a broad discretion in terms of the remedies available. The petitioners generally seek an order requiring the respondents, commonly the majority shareholders, to purchase their shares (s 996(2)(e) CA 2006).

The petitioner must establish that the company's affairs are being or have been conducted in a manner that is unfairly prejudicial to his interests as a member. Simply remaining as a shareholder even after prejudice to his interests is not conduct relating to company's affairs.[xii] Although the petitioner must be a shareholder in order to bring the action, the requirement that his interests in the capacity of a "member" must have been unfairly prejudiced has not been restrictively construed in the interest of justice; which is in juxtaposition with S. 210 of the 1948 Act wherein this restrictive approach was adopted by the courts. However, S. 994 does not confer arbitrary power upon the judges to administer justice. Indeed, Lord Wilberforce had recognised in Ebrahimi that the starting point for the court was always to look to the agreement between

the parties, for example as contained in the articles. It is upon the petitioner to establish in each case that the conduct in question is both prejudicial (in the sense of causing prejudice or harm) to the relevant interests and also unfair. Such conduct is not confined to any particular class of persons. The conduct is not confined to a specific group. In Re HR Harmer Ltd, Jenkins LJ noted that the definition is "wide enough to cover oppression by anyone who is taking part in the conduct of the affairs of the company whether de facto or de jure." Therefore, it can cover the actions of directors, a controlling shareholder, and persons with de facto control of the company, a class of shareholders, or conduct of a related company.

Indian Corporate Legal Scenario

Old Companies Act

The primary provision in the Companies Act 1956 was S. 397, which was as mentioned earlier, modelled in the likeliness of S. 210 of the English Companies Act 1948. The section is as produced below:

"397. Application to Company Law Board for relief in cases of oppression.

(1) Any members of a company who complain that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members (including any one or more of themselves) may apply to the Company Law Board for an order under this section, provided such members have a right so to apply in virtue of section 399.

(2) If, on any application under sub- section (1), the Company Law Board is of opinion-

(a) that the company's affairs are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members; and

(b) that to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding- up order on the ground that it was just and equitable that the company should be wound up; the Company Law Board may with a view to bringing to an end the matters complained of, make such order as it thinks fit."

The section prescribes criteria for maintainability of application for relief in cases of oppression. The impugned act should be prejudicial to the interest of the company or oppressive upon a member or group of members; or the act may be prejudicial to general "public interest". It is also the burden of the applicant to satisfy before the Board that winding up the company would "unfairly prejudice" him or the class he is representing; but otherwise the facts prima facie would justify that the company be wound up on just and equitable grounds. The right to apply is given to members as specified in the definition of "minority". Both conditions under this section should subsist in order to entail relief from the Board. Where there are no allegations to support a winding up, a petition u/s 397 cannot be entertained.

In Killick Nixon Ltd v Bank of India, it was held that no personal prejudice need be caused to the applicant. The cause of action is that the affairs of the company were conducted in a manner which was prejudicial and oppressive to the interests of the members or the public interest. Thus, oppression of other members can also be a locus standi for filing a petition under this section.

The expression "public interest" renders a wide ambit to this section. An action for oppression, thus, could be justified even when a member or group of members is not affected at all by the impugned acts of the majority but the brunt thereof is suffered by some third party. In cases of companies the concept of public interest takes it out of the conventional sphere of merely being a going concern in which only shareholders are interested. The stakeholder theory is endorsed by emphasising upon the idea that a company works for the public good and welfare of the society at large, and anyone who is reasonably connected to the company and impacted by its actions can be said to have a "stake" in its actions.

Definition of "oppression"

The definition of oppression in India has been adopted from the words of Lord Keith in *Scottish Co-operative Ltd v Meyer*, in Needle Industries (India) Ltd v Needle Industries Newey (India) Ltd and it runs as below:

"Oppression under s 210 may take various forms. It suggests to my mind...a lack of probity and fair dealing in the affairs of the company to the prejudice of some portion of its members. The section confers a wider power on the Court to deal with such a situation in an equitable manner..."

However, inefficient management would not fall into the category of oppression even if the impact thereof is oppressive upon some members.

Scope of requirements of the law

In *Shant Prasad Jain v Kalinga Tubes Ltd*, the Supreme Court has thus expressed the position on the requirements demanded by s 397:

"It is not enough to show that there must be a just and equitable cause for winding up the company though that must be shown as a preliminary to the application of section 397. It must further be shown that the conduct of the majority shareholders was oppressive to the minority as members and this requires that events have to be considered not in isolation but as part of a consecutive story... There must be continuous acts on the part of the majority shareholders, continuing upto the date of petition, showing that the affairs of the company were being conducted in a manner oppressive to some part of the members. The conduct must be burdensome, harsh and wrongful and mere lack of confidence between the majority and minority shareholders would not be enough unless the lack of confidence springs from oppression of a minority by a majority in the management of the company's affairs and such oppression must involve atleast an element of lack of probity and fair dealing to a member in the matter of his proprietary rights as a shareholder."

Thus in substance, an application for oppression is not very easy to maintain for the applicant before a court in India. This ratio of the Supreme Court has enlarged the onus lying upon the applicant in such cases. The requirement of continuous acts is one which has been inserted into the gamut of s 397 by virtue of this case law. Thus an unwise, inefficient or careless conduct of a Director or the Board of Directors cannot give rise to a claim for relief u/s 397. However, if circumstances indicate that even though an oppressive act is not per se continuous its effect is, the courts can interfere. The requirement that the act must prejudice the member(s) in the capacity of members is also strictly enforced, unlike the English counterpart in s 994 CA 2006.

New Companies Act

Ss. 241 and 242 are the relevant provisions that give the power to an individual member or a group of members to apply for relief in case of oppressive practices. The major portion of these sections is similar to that of S. 397 and 402 of the Companies Act 1956.

The only difference is that of S. 241 (1) (b), which provides an additional ground for filing application for oppression:

(b) the material change, not being a change brought about by, or in the interests of, any creditors, including debenture holders or any class of shareholders of the company, has taken place in the management or control of the company, whether by an alteration in the Board of Directors, or manager, or in the ownership of the company's shares, or if it has no share capital, in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests or its members or any class of members

Thus this clause allows the minority a pre-emptive remedy, i.e. they can prevent any change in the original composition and structure of the company if there is reason to believe that such change will lead to an injury to their interests. Also, the term "fraud" has been specifically defined to include any act, omission, concealment of any fact or abuse of position committed with intent to deceive, to gain undue advantage from, or to injure the interests of the company or its shareholders or its creditors or any other person.

Conclusion

Indian law provides for the empowerment of every shareholder of the company, including the minority shareholders. The minority shareholders were specifically granted powers under the Companies Act 1956 to challenge the decisions of majority shareholders and also to convey their opinion on the management and working of the company.

Apart from the deadlock or risks of litigation created by the minority block, there can be cases where the majority wants to do away with the minority shareholders in entirety in order to obtain an administrative stronghold. Thus the concept of minority "squeeze outs", which are well recognized in the legal frameworks of many jurisdictions, becomes relevant.

A squeeze out refers to a device by which the controlling block effectively acquires the shares held by the minority shareholders in a company. S. 395 of the 1956 Act directly deals with this concept. It provides for compulsory acquisition of shares by the majority shareholders in certain circumstances. The shareholders who dissented from this acquisition had the right to file their objections before the Court. Unless the court orders otherwise, the acquirer will be entitled to acquire the shares of the transferor company (including the minority). However, no corresponding rules were framed and thus wide discretionary powers fell into the lap of the Courts. Further, the section did not contain any guidelines for valuation of shares for purposes of the acquisition offer.

UNIT - V

WINDING UP

MODES OF WINDING - UP (SECTION 270):

The winding up of a company may be either –

1. by the Tribunal; or
2. Voluntary.

CIRCUMSTANCES FOR WINDING UP BY TRIBUNAL (SECTION 271):

A company may be wound up by the Tribunal on a petition filed under Section 272 of the Act.

The company may be wound up by Tribunal –

1. If the company is unable to pay its debts;
2. If the company has resolved by special resolution that the company be wound up by the Tribunal;
3. If the company has acted against the interests of the sovereignty and integrity of India, its security of the State, friendly relations with foreign States, public order, decency or morality;
4. If the Tribunal has ordered the winding up of the company under Chapter XIX i.e. in case of a sick company;
5. If, on application by the Registrar or the Government, the Tribunal is of the opinion that the affairs of the company has been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up;
6. If the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or
7. If the Tribunal is of the opinion that it is just and equitable to wind up the company.

Unable to Pay Debt (sub – section 2 of Section 271):

A company shall be deemed to be unable to pay its debts –

a) If the company has to pay the sum within twenty – one days after the receipt of demand or to provide adequate security or re – structure or compound the debt to the reasonable satisfaction of the creditor. The demand may be served:

    i. A creditor by assignment or otherwise,

    ii. to whom company is indebted for an amount exceeding one lakh rupees then due,

    iii. by causing it to be delivered at its registered officer, by registered post or otherwise,

    iv. a demand requiring the company to pay the amount so due.

b) If any execution or other process issued on a decree or order of any court or tribunal in favour of a creditor of the company is returned unsatisfied in whole or in part; or

c) If it is proved to the satisfaction of the Tribunal that the company is unable to pay its debt, and the Tribunal has taken into account the contingent and prospective liabilities of the company while determining this.

PETITION FOR WINDING UP (SECTION 272):

A petition to the Tribunal for the winding up of a company shall be presented by –

a) The company;

b) Any creditor or creditors, including any contingent or prospective creditor or creditors;

c) Any contributory or contributories;

d) All or any of the person in above clauses (a), (b) and (c) together;

e) The Registrar;

f) Any person authorised by the Central Government in that behalf; or

g) In case the company has acted against the interests of the sovereignty and integrity of India, its security of the State, friendly relations with foreign States, public order, decency or morality , by the Central Government or State Government.

A secured creditor, debenture holder and debenture trustee shall be deemed to be creditor for this Section.

A contributory shall be entitled to present a petition for winding up of a company, whether –

i. He hold fully paid – up shares, or.

ii. The company have no asserts at all

iii. The company have no surplus assets left for distribution among shareholders.

The Shares in respect of which, a person is contributory or contributories were—

i. originally allotted to them, or

ii. have been held by him and registered in his name for at least six months during the eighteen months immediately before commencement of the winding up, or

iii. have devolved on him through the death of a former holder.

The Registrar shall not be entitle to present a petition for winding up on the grounds specified in clauses (b), (d) or (g) of sub – section of Section 271. the Registrar shall not present a petition on the ground that the company is unable to pay its debts unless it appears to him either from the financial condition of the company as disclosed in its balance sheet or from the report of an inspector appointed under section 210 that the company is unable to pay its debts. The Registrar shall obtain the previous sanction of the Central Government to the presentation of a petition. The Central Government shall not accord its sanction unless the company has been given a reasonable opportunity of making representations.

A petition presented by the company for winding up before the Tribunal shall be admitted only if accompanied by a statement of affairs in such form and in such manner as may be prescribed.

Before a petition for winding up of a company presented by a contingent or prospective creditor is admitted, the leave of the Tribunal shall be obtained for the admission of the petition and such leave shall not be granted, unless in the opinion of the Tribunal there is a prima facie case for the winding up of the company and until such security for costs has been given as the Tribunal thinks reasonable.

A copy of the petition made under this section shall also be filed with the Registrar and the Registrar shall, without prejudice to any other provisions, submit his views to the Tribunal within sixty days of receipt of such petition.

POWERS OF TRIBUNAL (SECTION 273):

The Tribunal, on receipt of a petition for winding up, may pass any of the following orders, namely—

1. dismiss it, with or without costs;
2. make any interim order as it think fit;
3. appoint a provisional liquidator of the company till the making of a winding up order;
4. make an order for the winding up of the company with or without cost; or
5. any other order as it think fit.

The Tribunal shall make the order within ninety days from the date of presentation of the petition.

Before appointing a provisional liquidator, the Tribunal shall give notice to the company and afford a reasonable opportunity to it to make its representations. However, for special reasons to be recorded in writing, the Tribunal may dispense with such notice.

The Tribunal shall not refuse to make a winding up order on the ground only that the assets of the company have been mortgaged for an amount equal to or in excess of those assets, or that the company has no assets.

Where a petition is presented on the ground that it is just and equitable that the company should be wound up, the Tribunal may refuse to make an order of winding up, if it is of the opinion that some other remedy is available to the petitioners and that they are acting unreasonably in seeking to have the company wound up instead of pursuing the other remedy.

DIRECTIONS FOR FILING STATEMENT OF AFFAIRS (SECTION 274):

Where a petition for winding up is filed before the Tribunal by any person other than the company, the Tribunal shall, if satisfied that a prima facie case for winding up of the company is made out, by an order direct the company to file its objections along with a statement of its affairs within thirty days of the order.

The Tribunal may allow a further period of thirty days in a situation of contingency or special circumstances.

The Tribunal may direct the petitioner to deposit such security for costs as it may consider reasonable as a precondition to issue directions to the company.

A company, which fails to file the statement of affairs, shall forfeit the right to oppose the petition and such directors and officers of the company as found responsible for such non-compliance, shall be liable for punishment.

The directors and other officers of the company, in respect of which an order for winding up is passed by the Tribunal, shall submit at the cost of the company, the books of account of the company completed and audited up to the date of the order to liquidator within a period of thirty days of such order.

If any director or officer of the company contravenes the provisions of this section, the director or the officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both. The complaint may be filed in this behalf before the Special Court by Registrar, provisional liquidator, Company Liquidator or any person authorised by the Tribunal.

CIRCUMSTANCES IN WHICH COMPANY MAY BE WOUND UP VOLUNTARILY (SECTION 304):

A company may be wound up voluntarily,—

1. if the company in general meeting passes a resolution requiring the company to be wound up voluntarily:

1. as a result of the expiry of the period for its duration fixed by its articles, or

2. on the occurrence of any event in respect of which the articles provide that the company should be dissolved; or

3. the company passes a special resolution that the company be wound up voluntarily.

DECLARATION OF SOLVENCY (SECTION 305):

In case of a proposed voluntary winding up, majority of its directors but not less than two directors, shall at a Board meeting make a declaration verified by an affidavit that they have made full inquiry into the affairs of the company and they have formed an opinion that the company has no debt or whether it will be able to pay its debts in full from the procddes f assets sold in voluntary winding up.

Conditions for Declaration of Solvency:

This declaration shall have effect only if:

(a) it is made within five weeks immediately preceding the date of the passing of the resolution for winding up the company and it is delivered to the Registrar for registration before that date;

(b) it contains a declaration that the company is not being wound up to defraud any person or persons;

(c) it is accompanied by a copy of the report of the auditors of the company prepared in accordance with the provisions of this Act, on the profit and loss account of the company for the period commencing from the date up to which the last such account was prepared and ending with the latest practicable date immediately before the making of the declaration and the balance sheet of the company made out as on that date which would also contain a statement of the assets and liabilities of the company on that date; and

(d) where there are any assets of the company, it is accompanied by a report of the valuation of the assets of the company prepared by a registered valuer.

Unreasonable Declaration:

Where the company is wound up in pursuance of a resolution passed within a period of five weeks after the making of the declaration, but its debts are not paid or provided for in full, it shall be presumed, until the contrary is shown, that the director or directors did not have reasonable grounds for his or their opinion while making declaration of solvency.

Punishment for wrong declaration:

Any director of a company making a declaration under this section without having reasonable grounds for the opinion that the company will be able to pay its debts in full from the proceeds of assets sold in voluntary winding up shall be punishable with imprisonment for a term which shall not be less than three years but which may extend to five years or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.

MEETING OF CREDITORS (SECTION 306):

The company shall along with the calling of meeting of the company at which the resolution for the voluntary winding up is to be proposed, cause a meetings of its creditors either on same day or on the next day. The company shall cause a notice of the meeting to be sent by registered post to the creditors with the notice of the meeting of the company.

The Board of Directors of the company shall—

a) cause to be presented a full statement of the position of the affairs of the company together with a list of creditors of the company, if any, copy of declaration under section 305 and the estimated amount of the claims before such meeting; and

b) appoint one of the directors to preside at the meeting.

Where two-thirds in value of creditors of the company are of the opinion that—

(a) it is in the interest of all parties that the company be wound up voluntarily, the company shall be wound up voluntarily; or

(b) the company may not be able to pay for its debts in full from the proceeds of assets sold in voluntary winding up and pass a resolution that it shall be in the interest of all parties if the company is wound up by the Tribunal, the company shall within fourteen days thereafter file an application before the Tribunal.

The notice of any resolution passed at the meeting of creditors shall be given by the company to the Registrar within ten days of the passing thereof.

If a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to two lakh rupees and the director of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than fifty thousand rupees but which may extend to two lakh rupees, or with both.

PUBLICATION OF RESOLUTION TO WIND UP VOLUNTARILY (SECTION 307):

Where a company has passed a resolution for voluntary winding up and a resolution by creditors is passed, it shall within fourteen days of the passing of the resolution give notice of the resolution by advertisement in the Official Gazette and also in a newspaper which is in circulation in the district where the registered office or the principal office of the company is situate.

If a company contravenes, the company and every officer of the company who is in default shall be punishable with fine which may extend to five thousand rupees for every day during which such default continues.

COMMENCEMENT OF VOLUNTARY WINDING UP (SECTION 308):

A voluntary winding up shall be deemed to commence on the date of passing of the resolution for voluntary winding up under section 304.

EFFECT OF VOLUNTARY WINDING UP (SECTION 309):

In the case of a voluntary winding up, the company shall from the commencement of the winding up cease to carry on its business except as far as required for the beneficial winding up of its business. The corporate state and corporate powers of the company shall continue until it is dissolved.

POWER AND DUTIES OF COMPANY LIQUIDATORS (SECTION 290):

The Company Liquidator, in a winding up of a company by the Tribunal, shall have the power—

(a) to carry on the business of the company so far as may be necessary for the beneficial winding up of the company;

(b) to do all acts and to execute, in the name and on behalf of the company, all deeds, receipts and other documents, and for that purpose, to use, when necessary, the company's seal;

(c) to sell the immovable and movable property and actionable claims of the company by public auction or private contract, with power to transfer such property to any person or body corporate, or to sell the same in parcels;

(d) to sell the whole of the undertaking of the company as a going concern;

(e) to raise any money required on the security of the assets of the company;

(f) to institute or defend any suit, prosecution or other legal proceeding, civil or criminal, in the name and on behalf of the company;

(g) to invite and settle claim of creditors, employees or any other claimant and distribute sale proceeds in accordance with priorities established under this Act;

(h) to inspect the records and returns of the company on the files of the Registrar or any other authority;

(i) to prove rank and claim in the insolvency of any contributory for any balance against his estate, and to receive dividends in the insolvency, in respect of that balance, as a separate debt due from the insolvent, and rateably with the other separate creditors;

(j) to draw, accept, make and endorse any negotiable instruments including cheque, bill of exchange, hundi or promissory note in the name and on behalf of the company, with the same effect with respect to the liability of the company as if such instruments had been drawn, accepted, made or endorsed by or on behalf of the company in the course of its business;

(k) to take out, in his official name, letters of administration to any deceased contributory, and to do in his official name any other act necessary for obtaining payment of any money due from a contributory or his estate which cannot be conveniently done in the name of the company, and in all such cases, the money due shall, for the purpose of enabling the Company Liquidator to take out the letters of administration or recover the money, be deemed to be due to the Company Liquidator himself;

(l) to obtain any professional assistance from any person or appoint any professional, in discharge of his duties, obligations and responsibilities and for protection of the assets of the company, appoint an agent to do any business which the Company Liquidator is unable to do himself;

(m) to take all such actions, steps, or to sign, execute and verify any paper, deed, document, application, petition, affidavit, bond or instrument as may be necessary,—

(i) for winding up of the company;

(ii) for distribution of assets;

(iii) in discharge of his duties and obligations and functions as Company Liquidator; and

(n) to apply to the Tribunal for such orders or directions as may be necessary for the winding up of the company.

The exercise of powers by the Company Liquidator shall be subject to the overall control of the Tribunal.

The Company Liquidator shall perform such other duties as the Tribunal may specify in this behalf.

PROVISION FOR PROFESSIONAL ASSISTANCE TO COMPANY LIQUIDATOR (SECTION 291):

The Company Liquidator may, with the sanction of the Tribunal, appoint one or more chartered accountants or company secretaries or cost accountants or legal practitioners or such other professionals on such terms and conditions, as may be necessary, to assist him in the performance of his duties and functions under this Act.

Any person appointed under this section shall disclose forthwith to the Tribunal any conflict of interest or lack of independence in respect of his appointment.

EXERCISE AND CONTROL OF COMPANY LIQUIDATOR'S POWERS (SECTION 292):

In the administration of the assets of the company and the distribution thereof among its creditors, the Company Liquidator shall have regard to any directions which may be given by the resolution of the creditors or contributories at any general meeting or by the advisory committee.

Any directions given by the creditors or contributories at any general meeting shall, in case of conflict, be deemed to override any directions given by the advisory committee.

The Company Liquidator—

(a) may summon meetings of the creditors or contributories, whenever he thinks fit, for the purpose of ascertaining their wishes; and

(b) shall summon such meetings at such times, as the creditors or contributories, as the case may be, may, by resolution, direct, or whenever requested in writing to do so by not less than one-tenth in value of the creditors or contributories, as the case may be.

Any person aggrieved by any act or decision of the Company Liquidator may apply to the Tribunal, and the Tribunal may confirm, reverse or modify the act or decision complained of and make such further order as it thinks just and proper in the circumstances.

BOOKS TO BE KEPT BY COMPANY LIQUIDATOR (SECTION 293):

The Company Liquidator shall keep proper books in which he shall cause entries or minutes to be made of proceedings at meetings and of such other matters as may be prescribed.

Any creditor or contributory may, subject to the control of the Tribunal, inspect any such books, personally or through his agent.

AUDIT OF COMPANY LIQUIDATORS ACCOUNTS (SECTION 294):

The Company Liquidator shall maintain proper and regular books of account including accounts of receipts and payments made by him.

The Company Liquidator shall, at such times as may be prescribed but not less than twice in each year during his tenure of office, present to the Tribunal an account of the receipts and payments as liquidator in duplicate, which shall be verified by a declaration.

The Tribunal shall cause the accounts to be audited and for the purpose of the audit, the Company Liquidator shall furnish to the Tribunal with such vouchers and information as the Tribunal may require, and the Tribunal may, at any time, require the production of, and inspect, any books of account kept by the Company Liquidator.

When the accounts of the company have been audited, one copy thereof shall be filed by the Company Liquidator with the Tribunal, and the other copy shall be delivered to the Registrar which shall be open to inspection by any creditor, contributory or person interested.

Where an account relates to a Government company, the Company Liquidator shall forward a copy thereof—

(a) to the Central Government, if that Government is a member of the Government company; or

(b) to any State Government, if that Government is a member of the Government company; or

(c) to the Central Government and any State Government, if both the Governments are members of the Government company.

The Company Liquidator shall cause the accounts when audited, or a summary thereof, to be printed, and shall send a printed copy of the accounts or summary thereof by post to every creditor and every contributory. The Tribunal may dispense with the compliance of this provision.

REVIVAL AND REHABLTATION OF SICK COMPANIES

SCHEME OF REVIVAL AND REHABILITATION (SECTION 261):

The company administrator shall prepare or cause to be prepared a scheme of revival and rehabilitation of the sick company after considering the draft scheme filed along with the application under Section 254.

The scheme may provide any one or more of following measures, namely –

i. the financial reconstruction of the sick company;

ii. the proper management of the sick company by any change in, or by taking over, the management of such company;

iii. the amalgamation of –

    1. the sick company with any other company; or

    2. any other company with the sick company;

iv. takeover of a part or whole of my asset or business of the sick company;

v. the sale or release of a part or whole of any asset or business of the sick company;

vi. the rationalisation of managerial personnel, supervisory staff and workmen in accordance with law;

vii. such other appropriate preventive, ameliorative and remedial measures;

viii. repayment or rescheduling or restructuring of the debts or obligations of the sick company to any of its creditors or class of creditors;

ix. such incidental, consequential or supplemental measures as may be necessary or expedient in connection with or for the purpose of the measures specified in above clauses.

SANCTION OF SCHEME (SECTION 262):

The scheme prepared by the company administrator shall be place before the creditors of the company in a meeting for their approval within the period sixty days from his appointment. This period of sixty days may be extended up to one hundred twenty days.

Approval in Meetings:

The company administrator shall separate meetings of secured and unsecured creditors. If the scheme is approved by (a) unsecured creditors representing one – forth in value of the amount owed by the company and (b) secured creditors representing three – forth in value of the amount outstanding against financial assistance disbursed to the company; the company administrator shall submit the Tribunal for sanctioning the scheme.

Where the scheme relates to amalgamation of the sick company with any other company, the scheme shall also be approved by a special resolution in general meetings by shareholders of both companies. Only after this approval, the scheme shall be proceeded with.

Examination by Tribunal:

The scheme prepared by the company administrator shall be examined by the Tribunal. If, there is any modification, the Tribunal shall send the draft to the sick company and the company administrator. In case of amalgamation, the scheme shall also be sent to other company under the amalgamation. The Tribunal may publish or cause to be published the draft scheme in brief in daily newspapers for suggestions and objections.

The complete draft scheme shall be kept at the place where registered office of the company is situated or at a place mentioned in the advertisement.

In light of suggestions and objections received, the Tribunal may make such modifications as it may consider necessary. The sick company, company administrator, amalgamating company, and any shareholder or creditor or employee of these companies may submit suggestions and objections.

Approved Scheme:

After satisfying that the scheme had been validly approved, the Tribunal shall within sixty days from the receipt of the scheme, pass an order sanctioning such scheme. Yes, this is practically a challenge for all parties concerned.

The sanction accorded by the Tribunal shall be conclusive evidence that all the requirements of the scheme relating to the reconstruction or amalgamation or any other measure specified therein have been complied with. A copy of the sanctioned scheme certified in writing by an officer of the Tribunal to be a true copy thereof shall in all legal proceedings be admitted as evidence.

A copy of the sanctioned scheme shall be filed with the Registrar by the sick company within a period of thirty days from the date of receipt of a copy thereof.

Properties and Liabilities:

Where a sanctioned scheme provides for the transfer of any property or liability of the sick company to any other company or person or where the scheme provides for the transfer of any property or liability of any other company or person in favour of the sick company, then, by virtue of, and to the extent provided in, the scheme, on and from the date of coming into operation of the sanctioned scheme or any provision thereof, the property shall be transferred to, and vest in, and the liability shall become the liability of, such other company or person or, as the case may be, the sick company.

Review of Scheme:

The Tribunal may review any sanctioned scheme and make such modifications, as it may deem fit, or may by order in writing direct company administrator, to prepare a fresh scheme providing for such measures as the company administrator may consider necessary.

WINDING UP OF COMPANY ON REPORT OF COMPANY ADMINISTRATOR (SECTION 265):

If the scheme is not approved by the creditors, the company administrator shall submit a report to the Tribunal within fifteen days and the Tribunal shall order for winding up of the sick company and conduct the proceeding with the provision of Chapter XX of the Companies Act, 2013.

SCHEME TO BE BINDING (SECTION 263):

On and from the date of the coming into operation of the sanctioned scheme, the scheme shall be binding on the sick company, transferee company or such other company and also on employees, shareholders, creditors and guarantors of said companies.

IMPLEMENTATION OF SCHEME (SECTION 265):

The Tribunal shall, for the purpose of effective implementation of the scheme, have power to enforce, modify or terminate any contract or agreement or any obligation pursuant to such agreement or contract entered into by the company with any other person.

The tribunal may by order in writing authorise the company administrator to implement a sanctioned scheme till its successful implementation. The Tribunal may require company administrator to file period reports on implementation of the sanctioned scheme.

Where the whole or substantial assets of the understanding of the sick company are sold under a sanctioned scheme, the sale proceeds shall be applied towards implementation of the scheme in a manner as directed by the Tribunal. The debtors and creditors shall have the power to scrutinise and make appeal for review of the value before final order of fixing value.

Where it is difficult to implement the scheme for any reason or the scheme fails due to non – implementation of obligations under the scheme by the parties concerned, the company administrator may make an application before the Tribunal for (a) modification of the scheme or (b) to declare the scheme as failed and that the company may be wound up. Where there is no company administrator; the company, secured creditors or transferee company may make the application.

The Tribunal shall pass an order within thirty days of presentation of the application with the consent of secured creditors holding three – fourths in value of secured credit.

304 → Voluntary winding up
305 → Declaration of [illegible]
3[illegible] → Meeting of [illegible]

[illegible] MANASA

[illegible]

[illegible]

SURYA

NIRANJANA