**Chapter** A1

Company Law

# Structure

**A1.1. Introduction to Companies and Types of Companies**

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**A1.3. Documents: Prospectus,** **Memorandum of Association (MoA) and** **Articles of Association (AoA)**

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# Learning Objectives

* To know about companies and types of companies
* To understand the meaning of the term ‘corporate veil’ and its exceptions
* To understand the process of incorporation of a company
* To know about memorandum of association (MoA), articles of association (AoA) and prospectus
* To know about meetings and types of meetings
* To know about the management of company: Directors and KMP
* To know about the share capital and its types
* To know about the process of winding up of companies

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# A1.1. Introduction to Companies and Types of Companies

The company law in India is the cherished child of its English parents. Our various Companies Acts have been modelled on the English Acts. Following the enactment of the Joint Stock Companies Act, 1844, in England, the first Companies Act was passed in India in 1850. The Indian Companies Act, 1866; the Indian Companies Act, 1882; the Companies Act, 1913; and the Companies Act, 1956, were later passed in India. Every Company Act introduced new concepts. Like in the amending Act of 1857, there was no concept of limited liability, which is now a fundamental concept of the companies’ law. The Companies Act, 2013, received the assent of the president on 29 August 2013 and was notified in the Gazette of India on 30 August 2013. The Companies Act, 2013, introduced new concepts supporting enhanced disclosure, accountability, better board governance, better facilitation of business and so on. It includes associate companies, one-person companies, small companies, dormant companies, independent director, women director, resident director, special court, secretarial standards, secretarial audit, class action, registered valuers, rotation of auditors, vigil mechanism, corporate social responsibility, e-voting and so on.

## A1.1.1. Meaning and Definition of a Company

The word ‘company’ is derived from the Latin word (*com* = with or together; *panis* = bread), and it originally referred to as an association of persons who eat their meals together. In the leisurely past, merchants used to take advantage of festive gatherings, to discuss business matters. Nowadays, a company, a form of organization, has assumed great importance. When merchants form their business relations, they form a company. In popular parlance, a company or firm denotes an association of like-minded persons formed for the purpose of carrying on some business or undertaking. A company under the law is a corporate body and a legal person having status and personality distinct and separate from the members constituting it.

It is called a 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 word ‘corporation’ is derived from the Latin term *corpus*, which means ‘body’. Accordingly, ‘corporation’ is a legal person created by a process other than natural birth. As a legal person, a corporate is capable of enjoying many rights and incurring many liabilities of a natural person.

An incorporated company owes its existence either to a special Act of Parliament or to the company law. Public corporations, such as Life Insurance Corporation of India and State Bank of India (SBI), have been brought into existence through special Acts of Parliament, whereas companies such as Tata Steel Ltd and Reliance Industries Ltd have been formed under the company law, that is, the Companies Act, 1956, which is replaced by the Companies Act, 2013. In the legal sense, a company is an association of both natural and artificial persons and is incorporated under the existing law of a country.

In terms of the Companies Act, 2013, a ‘company’ means a company incorporated under this Act or under any previous company law (Section 2(20)).

In common law, a company is a ‘legal person’ or ‘legal entity’ separate from and capable of surviving beyond the lives of its members. A company is rather a legal device for the attainment of the social and economic end. It is, therefore, a combined political, social, economic and legal institution. Lord Justice Lindley has defined a company as ‘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 so contributed is denoted in money and is the capital of the company. The persons who contributed in it or form it, or to whom it belongs, are members. The proportion of capital stock to which each member has contributed entitled is his “share”. The shares are always transferable although the right to transfer them may be restricted.’

## A1.1.2. Nature and Characteristics of a Company

1. **Corporate personality:** A company incorporated under the Act is vested with a corporate personality so it bears its own name, acts under the name, may have a seal of its own and its assets are separate and distinct from those of its members. It is a different ‘person’ from the members who compose it. Therefore, it is capable of owning property, incurring debts, borrowing money, having a bank account, employing people, entering into contracts and suing or being sued in the same manner as an individual. Its shareholders are its notional owners and do not own anything in it except ownership of shares issued, and they can be its creditors simultaneously. A shareholder cannot be held liable for the acts of the company even if he holds virtually the entire share capital. The **case of Salomon vs Salomon and Co. Ltd, (1897) A.C. 22,** has clearly established the principle that once a company has been validly constituted under the Companies Act, it becomes a legal person distinct from its members; and for this purpose, it is immaterial whether any member holds a large or small proportion of the shares, and whether he holds those shares as beneficially or as a mere trustee. In the case, Salomon had, for some years, carried on a prosperous business as a leather merchant and boot manufacturer. He formed a limited company consisting of himself, his wife, his daughter and his four sons as the shareholders, all of whom subscribed to one share each so that the actual cash paid as capital was £7. Salomon sold his business (which was perfectly solvent at that time) to the company formed by him for the sum of £38,782. The company’s nominal capital was £40,000 in £1 shares. In part, payment of the purchased money for the business sold to the company and debentures of the amount of £10,000 secured by a floating charge on the company’s assets were issued to Salomon, who also applied for and received an allotment of 20,000 (£1 per share) fully paid shares. The remaining amount of £8,782 was paid to Salomon in cash. Salomon was the managing director, and two of his sons were other directors. The company soon ran into difficulties and the debenture holders appointed a receiver and the company went into liquidation. The total assets of the company amounted to £6,050, its liabilities were £10,000 secured by debentures, £8,000 owing to unsecured trade creditors, who claimed the whole of the company’s assets, namely £6,050, on the ground that, as the company was a mere ‘alias’ or agent for Salomon, they were entitled to payment of their debts in priority to debentures. They further pleaded that Salomon, as a principal beneficiary, was ultimately responsible for the debts incurred by his agent or trustee on his behalf. Their Lordships of the House of Lords observed that the company is a different person altogether from the subscribers of the memorandum; and though it may be that after incorporation the business is precisely the same as before, the same persons are managers, and the same hands receive the profits, the company is not, in law, their agent or trustee. The statute enacts nothing as to the extent or degree of interest, which may be held by each of the seven or as to the proportion of interest or influence possessed by one or majority of the shareholders over others. There is nothing in the Act requiring that the subscribers to the memorandum should be independent or unconnected, or that they or any of them should take a substantial interest in the undertakings, or that they should have a mind or will of their own, or that there should be anything like a balance of power in the constitution of the company.
2. **Company as an artificial person:** A company is an artificial person created by the law. It is not a human being, but it acts through human beings. It is considered as a legal person who can enter into contracts, possess properties in its name, sue and can be sued by others and so on. It is called an artificial person since it is invisible, intangible, existing only in the contemplation of the law. It is capable of enjoying rights and being subject to duties.
3. **Company is not a citizen:** The company, though a legal person, is not a citizen under the Citizenship Act, 1955, or the Constitution of India. In State Trading Corporation of India Ltd vs The Commercial Tax Officer (CTO; AIR 1963, SC 1811), the Supreme Court held that the State Trading Corporation, though a legal person, was not a citizen and can act only through natural persons. Nevertheless, it is to be noted that certain fundamental rights enshrined in the constitution for protection of a ‘person’, for example, right to equality (Article 14) and so on are also available to the company.
4. **Company has nationality and residence:** Though it is established through judicial decisions that a company cannot be a citizen, it has nationality, domicile and residence. In Gasque vs Inland Revenue Commissioners, (1940) 2 KB 88, Lord J. Macnaghten held that a limited company is capable of having a domicile and its domicile is the place of its registration and that domicile clings to it throughout its existence. He observed that it was suggested that a body corporate has no domicile. It is quite true that a body corporate cannot have a domicile in the same sense as an individual. But by analogy with a natural person, the attributes of residence, domicile and nationality can be given to a body corporate.
5. **Limited liability:** ‘The privilege of limited liability for business debts is one of the principal advantages of doing business under the corporate form of organization.’ The company, being a separate person, is the owner of its assets and bound by its liabilities. The liability of a member as shareholder extends to the contribution to the capital of the company up to the nominal value of the shares held and not paid by him. This means that the liability of a member is limited. For example, if A holds shares of the total nominal value of `1,000 and has already paid `500 (or 50% of the value) as part payment at the time of allotment, he cannot be called upon to pay more than `500, which is the remaining amount unpaid on his shares. If he holds fully paid shares, he has no further liability to pay even if the company is declared insolvent. In the case of a company limited by guarantee, the liability of members is limited to a specified amount of the guarantee mentioned in the memorandum.
6. **Perpetual succession:** An incorporated company never dies, except when it is wound up as per the law. A company, being a separate legal person, is unaffected by the death or departure of any member and it remains the same entity, despite a total change in the membership. Perpetual succession means that the membership of a company may keep changing from time to time, but that shall not affect its continuity. The membership of an incorporated company may change either because one shareholder has sold/transferred his shares to another or his shares devolve on his legal representatives on his death or he ceases to be a member under some other provisions of the Companies Act. Thus, perpetual succession denotes the ability of a company to maintain its existence by the succession of new individuals who step into the shoes of those who cease to be members of the company.
7. **Separate property:** A company, being a legal person and entirely distinct from its members, is capable of owning, enjoying and disposing of a property in its name. The company is the real person in which all its property is vested and by which it is controlled, managed and disposed of. Their Lordships of the Madras High Court in R. F. Perumal vs H. John Deavin, (AIR 1960, Mad 43) held that ‘no member can claim himself to be the owner of the company’s property during its existence or in its winding-up’. A member does not even have an insurable interest in the property of the company. In the case of **Mrs Bacha F. Guzdar vs The Commissioner of Income Tax, Bombay (AIR 1955, SC 74),** the Supreme Court held that though the income of a tea company is entitled to be exempted from income tax up to 60 per cent, being partly agricultural, the same income when received by a shareholder in the form of dividend cannot be regarded as agricultural income for the assessment of income tax.
8. **Transferability of shares:** The capital of a company is divided into parts, called shares. The shares are said to be a movable property and are freely transferable, subject to certain conditions, so that no shareholder is permanently or necessarily wedded to a company. When the joint-stock companies were established, the object was that their shares should be capable of being easily transferred. Section 44 of the Companies Act, 2013, enunciates the principle by providing that the shares held by the members are movable property and can be transferred from one person to another in the manner provided by the articles. If the articles do not provide anything for the transfer of shares and the regulations contained in Table ‘F’ in Schedule I to the Companies Act, 2013, are also expressly excluded, the transfer of shares will be governed by the general law relating to the transfer of movable property.
9. **Capacity to sue and be sued:** A company, being a body corporate, can sue and be sued in its name. ‘To sue’ means to institute legal proceedings against (a person) or to bring a suit in a court of law. All legal proceedings against the company are to be instituted in its name. Similarly, the company may bring an action against anyone in its own name. A company’s right to sue arises when some loss is caused to the company, that is, to the property or the personality of the company. Hence, the company is entitled to sue for damages in libel or slander, as the case may be (Floating Services Ltd vs MV San Fransceco Dipalola [2004] 52 SCL 762 [Guj]). A company as a person and distinct from its members may even sue one of its own members.
10. **Contractual rights:** A company, being a legal entity different from its members, can enter into contracts for the conduct of the business in its own name. A shareholder cannot enforce a contract made by his company; he is neither a party to the contract nor entitled to the benefit derived from of it, as a company is not a trustee for its shareholders. Likewise, a shareholder cannot be sued on contracts made by his company. The distinction between a company and its members is not confined to the rules of privity but permeates the whole law of contract. Thus, if a director fails to disclose a breach of his duties towards his company, and in consequence, a shareholder is induced to enter into a contract with the director on behalf of the company which he would not have entered into had there been disclosure, the shareholder cannot rescind the contract.
11. **Limitation of action:** A company cannot go beyond the power stated in its memorandum of association (MoA). The MoA of a company regulates the powers and fixes the objects of the company and provides the edifice upon which the entire structure of the company rests. The actions and objects of the company are limited within the scope of its MoA. In order to enable it to carry out its actions without such restrictions and limitations in most cases, sufficient powers are granted in the MoA. But once the powers have been laid down, it cannot go beyond such powers unless the MoA itself altered prior to doing so.
12. **Separate management:** The members may derive profits without being burdened with the management of the company. They do not have effective and intimate control over its working, and they elect their representatives as directors on the board of directors of the company to conduct corporate functions through managerial personnel employed by them. In other words, the company is administered and managed by its managerial personnel.
13. **Voluntary association for profit:** A company is a voluntary association for profit. It is formed for the accomplishment of some stated goals, and the profit gained is divided among its shareholders or saved for the future expansion of the company. Only a Section 8 company can be formed with no profit motive.
14. **Termination of existence:** A company, being an artificial juridical person, does not die a natural death. It is created by law, carries on its affairs according to the law throughout its life and ultimately is effaced by the law. Generally, the existence of a company is terminated by means of winding up. However, to avoid winding up, sometimes companies adopt strategies such as reorganization, reconstruction and amalgamation.

# Distinction between a Partnership Firm and a Company

The principal points of distinction between a partnership firm and a company are as follows:

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| **Partnership Firm** | **Company** |
| A partnership firm is not distinct from the several persons who form the partnership. | A company is a distinct legal person. |
| In a partnership, the property of the firm is the property of the individuals comprising it. | In a company, the property belongs to the company and not to the individuals who are its members. |
| Creditors of a partnership firm are the creditors of individual partners, and a decree against the firm can be executed against the partners jointly and severally. | The creditors of a company can proceed only against the company and not against its members. |
| Partners are the agents of the firm. A partner can dispose of the property and incur liabilities as long as he acts in the course of the firm’s business. | Members of a company are not its agents. A member of a company cannot dispose of the property and incur liabilities in the course of the company’s business. |
| A partner cannot contract with his firm. | A member can contract with his company. |
| A partner cannot transfer his share and make the transferee a member of the firm without the consent of the other partners. | A company’s share can ordinarily be transferred. |
| A partner’s liability is always unlimited. | The liability of the shareholder may be limited either by shares or a guarantee. |
| The death or insolvency of a partner dissolves the firm, unless otherwise provided. | A company has perpetual succession, that is, the death or insolvency of a shareholder or all of them does not affect the life of the company. |
| The accounts of a firm are audited at the discretion of the partners. | A company is required to have its accounts audited annually by a chartered accountant. |
| A partnership firm is the result of an agreement and can be dissolved at any time by agreement among the partners. | A company, being a creation of law, can only be dissolved as laid down by law. |

# Distinction between a Limited Liability Partnership (LLP) and a Company

An LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership. An LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name. An LLP, as a separate legal entity, is liable to the full extent of its assets but the liability of the partners is limited to their agreed contribution in the LLP.

Further, no partner is liable on account of the independent or unauthorized actions of other partners, thus, individual partners are shielded from joint liability created by another partner’s wrongful business decisions or misconduct. An LLP is a body corporate and a legal entity separate from its partners, having perpetual succession**.** AnLLP form is a form of business model which: (a) is organized and operates on the basis of an agreement,(b) provides flexibility without imposing detailed legal and procedural requirements and (c) enables professional/technical expertise and initiative to combine with financial risk-taking capacity in an innovative and efficient manner.

A basic difference between an LLP and a company lies in the internal governance structure of a company which is regulated by statute (i.e., the Companies Act); whereas for an LLP, it would be by a contractual agreement between partners.

The management–ownership division inherent in a company is not there in an LLP. An LLP has more flexibility and lesser compliance requirements as compared to a company.

## A1.1.3. Doctrine of Lifting of or Piercing the Corporate Veil

A company is a person created by law, having a distinct entity. This principle is referred to as the veil of incorporation. However, if the veil is used as a mask of fraud, then the court will lift the veil and look at the persons behind the company. The separate personality of a company is a statutory privilege, and it must be used for legitimate business purposes only. If the legal entity is misused for committing fraud or improper conduct, the individuals concerned will not be allowed to take shelter behind the corporate personality. The court will break through the corporate shell and apply the principle/doctrine of what is called as ‘lifting of or piercing the corporate veil’. The court will look behind the corporate entity and take action as though no entity separate from the members existed and make the members or the controlling persons liable for debts and obligations of the company. The corporate veil can be lifted under following circumstances:

1. **Statutory recognition of lifting of corporate veil:** The Companies Act, 2013, itself contains some provisions (Sections 7(7), 251(1) and 339) which lift the corporate veil to reach the real forces of action. Section 7(7) deals with punishment for the incorporation of a company by furnishing false information; Section 251(1) deals with liability for making a fraudulent application for removal of the name of the company from the register of companies and Section 339 deals with liability for fraudulent conduct of business during the course of winding up.
2. **Lifting of corporate veil under judicial interpretation:** Lifting of or piercing the corporate veil means ignoring the separate identity of a company. Disregarding the corporate personality and looking behind the real persons who are in the control of the company. These cases are given below:
3. **The enemy character of a company:** In the case ofDaimler Co. Ltd vs Continental Tyre and Rubber Co. Ltd, the German company (Continental Tyre and Rubber Co. Ltd) incorporated in England for the purpose of selling tyres made in Germany. During the First World War, the English company (Daimler Co. Ltd) started recovering its debts. Court held this as trading with an enemy.
4. **Prevention of fraud or improper conduct:** In the case of Gilford Motor Co. Ltd vs Horne, Horne a former employee of Gilford Motor was subject to not solicit its customers. Horne incorporated a company to solicited customers of Gilford Motor. The court passed an injunction order.
5. **Protection of revenue.** In the case ofSir Dinshaw Maneckjee Petit vs CIT, Dinshaw Maneckjee was enjoying large profit and income in the form of interest and dividend. He formed four new private companies and transferred interest income to each of them. The dividends and interest income received by the company were returned to Dinshaw Maneckjee in the form of a pretended loan. Maneckjee and all the four companies were treated as one.
6. **Avoidance of welfare legislation:** In the case of **workmen employed in Associated Rubber Industries Ltd,** a subsidiary company was formed wholly owned by the holding company only to receive dividends from shares transferred. Court held that the new company was formed to reduce the bonus to workmen.
7. **A company acting as an agent of the shareholders:** In the case of F. G. Films Ltd, an American company produced a film in India in the name of a British company. The sensor board refused to register the film as a British film.
8. **Subsidiary acting as an agent:** Inthe case of **Merchandise Transport Ltd vs British Transport Commission,** as the transport company would not get licences on its own name, it formed a subsidiary company. Court held that both are same, and the application for licences was rejected.
9. **Experience of directors is the experience of the company:** In the case ofProgressive Aluminium Ltd vs Registrar of Companies (ROCs), the prospectus of Progressive Aluminium Ltd stated that the company has vast experience. In fact, only directors of the company had vast experience. It was held that the experience of the directors is the experience of the company.
10. **To protect the public policy:**
11. **In quasi-criminal cases:**

## A1.1.4. Types of Companies

There are the following types of companies:

 **One-person company:** The 2013 Act introduces a new type of entity ‘one-person company’ (OPC). An OPC means a company with only one person as to its member (Section 3(1)).

* **Small company:** A small company has been defined as a company, other than a public company. The paid-up share capital of which does not exceed `50 lakh or such higher amount as may be prescribed which shall not be more than `10 crores; and turnover of which as per profit and loss account for the immediately preceding financial year does not exceed `2 crore or such higher amount as may be prescribed which shall not be more than `100 crores. It is providedthat nothing in this clause shall apply to a holding company or a subsidiary company, a company registered under Section 8 or a company or body corporate governed by any special Act.
* **Dormant company:** A company formed and registered under the Companies Act, 2013, for a future project or to hold an asset or intellectual property and has no significant accounting transaction; such a company or an inactive company may make an application to the ROCs for obtaining the status of a dormant company (Section 455).
* **Nidhi company:** A nidhi company means a company which has been incorporated as a nidhi with the object of cultivating the habit of thrift and savings amongst its members, receiving deposits from and lending to its members only, for their mutual benefit, and which complies with the rules prescribed by the central government for regulation of such class of companies (Section 406).
* **A company** **limited by shares**: A company limited by shares means 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.
* **Unlimited company**: An unlimited company means a company not having any limit on the liability of its members. The liability of each member extends to the whole amount of the company’s liabilities. It may or may not have a share capital. Articles must state the amount of the share capital and the amount of each share. Unlimited liability of members is towards creditors only, not towards the company. It may alter or reduce its share capital without any restriction.
* **Private company**: A private company means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, restricts the right to transfer its shares; except in case of OPC, it limits the number of its members to 200. It is provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member. It is provided further that persons who are in the employment of the company; and persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased, shall not be included in the number of members and prohibits any invitation to the public to subscribe for any securities of the company.
* **Public company:** A public company means a company which is not a private company and has a minimum paid-up share capital, as may be prescribed. It is provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.
* **Holding company:** A holding company, in relation to one or more other companies, means a company of which such companies are subsidiary companies.
* **Subsidiary company**: A subsidiary company or a ‘subsidiary’, in relation to any other company (that is to say the holding company), means a company in which the holding company controls the composition of the board of directors or exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies.
* **Associate company**: An associate company, in relation to another company, is a company in which other company has a significant influence, but which is not a subsidiary of the company having such influence and includes a joint venture company. For the purpose of this clause, the expression ‘significant influence’ means control of at least 20 per cent of the total voting power, or control of or participation in business decisions under an agreement; the expression ‘joint venture’ means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.
* **Body corporate** **or** **corporation:** This includes a company incorporated outside India, but does not include a co-operative society registered under any law relating to co-operative societies, and any other body corporate, which the central government may, by notification, specify in this behalf.
* **Foreign company:** A foreign company means any company or body corporate incorporated outside India which has a place of business in India whether by itself or through an agent, either physically or through electronic mode, and conducts any business activity in India in any other manner.
* **Listed company:** A listed company is a company which has any of its securities listed on any recognized stock exchange.
* **Government company:** It means any company in which 51 per cent or more of the paid-up share capital is held by the central government or by any state government, or partly by the central government and partly by one or more state government(s) and includes a company which is a subsidiary company of such a government company.
* **Banking company:** It means a banking company as defined in clause (c) of Section 5 of the Banking Regulation Act, 1949.
* **Financial institution**: This includes a scheduled bank and any other financial institution defined or notified under the Reserve Bank of India Act, 1934.

## A1.1.5. Association Not-for-profit or Non-profit-oriented Companies (Section 8)

Section 8 provides registration of a non-profit-oriented company with the central government’s permission. It must be registered with limited liability without using ‘Limited’ or ‘Private Limited’. It can be registered for conditions for grant of licence for promoting commerce, art, religion and so on. It prohibits payment of any dividend. The licence is subject to other conditions as thought fit by the central government. It cannot alter its objects clause in MoA without the approval of the central government. The central government may also grant an exemption for other provisions and revoke if the objects clause changed without the approval of the central government. On revocation, the registrar shall add the word ‘Limited’ or ‘Private Limited’. Before a licence is revoked, the central government shall give an opportunity of being heard to such a company.

**Advantages of Section 8 companies are** that they do not need to pay stamp duty. A partnership firm can be a member. The company secretary does not need to be a qualified company secretary. It may hold its annual general meeting (AGM) on a public holiday. For any meeting, four days’ notice is sufficient. The books of accounts need to be preserved for four years only. It need not have the minimum paid capital.

# A1.2. Formation and Incorporation of Companies

Section 3(1) states that a company may be formed for any lawful purpose. If the company to be formed is to be a public company then it is to be formed by seven or more persons. If the company to be formed is to be a private company, then it is to be formed by two or more persons. And a company may be formed by one person, where the company to be formed is to be an OPC, that is to say, a private company by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of registration. There are the following stages of formation of the company:

* 1. Promoter and promotion of company
	2. Preparation of documents such as MoA, articles of association (AoA) and prospectus
	3. Declaration form
	4. Filing application along with requisite fee with ROC

## A1.2.1 Promotion and Incorporation of a Company

A promoter means a person named as such in a prospectus or is identified by the company in the annual return and has control over the affairs of the company, directly or indirectly, whether as a shareholder, director or otherwise; or in accordance with whose advice, directions or instructions, the board of directors of the company is accustomed to act. Not in professional capacity.

**Fiduciary position of a promoter:** Until a company gets incorporated, a promoter stands in a fiduciary capacity. The term ‘fiduciary’ means a position of trust. If we discuss the legal position of a promoter, then he is neither an agent nor a trustee as the company is not in existence. The duties of a promoter are given below:

1. Not to make any profit at the expense of the company.
2. To give the benefit of negotiations to the company.
3. To make full disclosure of interest or profit: If the promoter fails to make the disclosure, the company may sue for damages and recover the secret profit made. Law does not prohibit. If full disclosure is made, the profit is permissible.
4. Not to make unfair use of position.

**Remuneration of a promoter:** A promoter has no right if there is no express contract for remuneration. If there is an express contract, the remuneration can be received in one of the following ways:

1. Sell the property at a profit provided that he has to make a disclosure of it
2. Option to buy shares at a lesser price
3. Commission on the shares sold
4. Fixed sum

**Remedies available to the company against the promoter:** If the promoter fails to disclose any secret profits made by him, then the members who join the company on his offer may:

1. Cancel the contract
2. Retain the property and pay not more than what the promoter actually paid for the purchase of it
3. Claim damages for violation of the duty of disclosure

**Pre**-**incorporation contracts:** These are the contracts entered by promoters on behalf of a company before its existence. According to the law, there must be two parties to a contract. But before incorporation, a company is not a legal entity. Hence, the contract never binds a company. If the company cannot ratify the contract, the only option is to enter into a new contract. In the case of adoption of the contract, it will not create a contract between the company and the other person. The principle of constructive notice provides that person entering into a contract is presumed to have knowledge of MoA and AoA. A person entering into a pre-incorporation contract with the promoters does this at his own risk. Section 70 of the Indian Contract Act, 1872 clearly states that where a person lawfully does anything for another person without intending to do gratuitously compensation must be paid for enjoyment of benefits. The promoters are personally liable. But the exception is if the company adopts the contract, the promoter’s liability shall cease, and if not, either party may rescind the contract.

## A1.2.2. Procedure for Incorporation

The procedure for incorporation of company is given below:

**The name of a company:** The first step is to get the name for the proposed company. The basicrequirement for the reservation of the name of the company is to make an application to the ROC for the reservation of a name with three names in order of preferences. The name applied should not be same or similar to any existing company or any prohibited name. The ROC reserves the name for a period of 60 days from the date of the application. Where after the reservation of name, it is found that the name was applied by furnishing wrong information, then, if the company has not been incorporated, the reserved name shall be cancelled or if the company has been incorporated, the ROC may either direct to change or strike off the name or make a petition for winding up of the company.

After getting the name approved, file the documents with the fee. The registrar issues the certificate of incorporation on registration and shall allot a corporate identity number (CIN) from date of incorporation. The company shall maintain and preserve at its registered office copies of all documents till its dissolution. If a company is incorporated by furnishing false information or suppressing facts, then it shall be liable for action and the tribunal may pass such orders for the regulation of the management for liability of the members as unlimited or removal of the name or pass the winding-up order for the company.

### A1.2.2.1. Documents To Be Filed with Registrar at the Time of Registration

For the registration of the company, the following are the documents need to be submitted with the ROC for registration:

1. The MoA and AoA duly signed by all the subscribers and the prospectus of the company.
2. A declaration that all the requirements of this Act and the rules complied with.
3. The affidavit from each of the subscribers/first directors that he is not convicted of any offence in connection with the promotion and so on. He has not been found guilty of any fraud or misfeasance and all the documents filed with the registrar are correct and complete.
4. Address for correspondence with the company.
5. Particulars of every subscriber to MoA.
6. Particulars of the first directors of the company.
7. particulars of the interests of the persons mentioned in the articles as the first directors.
8. Duly filled application for registration of the company along with the prescribed fee.

### A1.2.2.2. Effect of Registration of a Company

From the date of incorporation, the subscribers to the MoA become members of the company. It shall be a body corporate. The company is capable of exercising all the functions of an incorporated company. It has perpetual succession and a common seal. It shall have the power to acquire, hold and dispose of property and so on in its own name. It becomes a legal person separate from the incorporators and binding contract between the company and its members. A shareholder, who buys shares, does not buy any interest in the property of the company. Merely because a company purchases all the shares of another company, and it will not put an end to the corporate character of another company. Being a juristic person, a company has separate and distinct existence from its members.

**Time of issue of certificate of securities:** Under Section 56(4), every company, unless prohibited by any provision of law or any order of any court, tribunal or other authority must deliver the certificates of all the securities allotted, transferred or transmitted within a period of two months from the date of incorporation, in the case of subscribers to the memorandum; within a period of two months from the date of allotment, in the case of any allotment of any of its shares; within a period of one month from the date of receipt by the company of the instrument of transfer, or as the case may be, of the intimation of transmission, in the case of a transfer or transmission of securities and within a period of six months from the date of allotment, in the case of any allotment of a debenture. However, where the securities are dealt within a depository, the company shall intimate the details of allotment of securities to depository immediately on allotment of such securities. Where any default is made in complying with the above provisions, the company shall be punishable with fine which shall not be less than `25,000 but which may extend to `5 lakhs, and every officer of the company who is in default shall be punishable with fine which shall not be less than `10,000 but which may extend to `100,000.

# A1.3. Documents: Prospectus, MoA and AoA

## A1.3.1. Prospectus

**Meaning of prospectus:** Any document described or issued as a prospectus includes a red-herring prospectus or shelf prospectus 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. A document called will have three important conditions are invitation to the public in written form, made by or on behalf of the company and application constitutes an offer by the subscriber on its acceptance by the company binding contract comes into existence. The prospectus helps the investors to decide whether or not they should subscribe to securities as information in the prospectus is vital, and any misstatements may result in huge losses.

**Different modes of issue of securities by a company:** There are the following modes of issue of securities by a company:

1. **Public company:**
2. Through prospectus in public offer or private placement
3. Through a rights issue or a bonus issue
4. Public offer includes initial public offering (IPO) or further public offer (FPO) or an offer for sale
5. **Private company:**
6. By way of rights issue or bonus issue
7. By private placement

 **Private placement:** Private placement means any offer to a select group of persons through the issue of a private placement offer letter and by fulfilment of the conditions specified. The offer shall be made maximum to 50 persons or such higher number as may be prescribed, in a financial year. It does not include qualified institutional buyers and employees stock options. The offer is treated as a ‘public offer’ if offer/invitation made to more than 50 or such higher prescribed number of persons or on non-compliance of conditions of the private placement.

**Procedure for private placement:** It is applicable for private and public companies. The following are the conditions through which an invitation can be made:

1. A company may make private placement through issue of a private placement offer letter.
2. The offer shall be made maximum to 50 persons or such higher as may be prescribed, in a financial year.
3. No fresh offer or invitation shall be made unless the allotments have been completed, or invitation has been withdrawn or abandoned by the company.
4. All monies shall be paid by cheque or demand draft or other banking channels not by cash.
5. A company shall allot its securities within 60 days from the date of receipt of the application money.
6. Monies received shall be kept in a separate bank account and shall be utilized only for adjustment against allotment of securities or the repayment of monies if unable to allot securities.
7. Offers shall be made only to persons whose names are recorded by the company prior to the invitation complete information about such offer shall be filed with the registrar within 30 days.
8. A company shall not publish any advertisements or utilize any media to inform large public about such offer.
9. The company shall file with the registrar a return of allotment.

**Penalties:** Default in allotment of securities:

1. If the securities are not allotted within 60 days, the company shall repay the application money within 15 days.
2. The company shall be liable to repay that money with interest at the rate of 12 per cent per annum after the completion of 60 days.

The company, promoters and directors shall be liable to pay a penalty up to the amount involved in the offer or invitation or `2 crores, whichever is higher. The company shall also refund the amount within a period of 30 days of the order.

**Limitations on private placement as per the rules:**

1. It should be previously approved by a special resolution (SR), for each of the offers or invitations.
2. The explanatory statement shall disclose the basis or justification for the price.
3. For non-convertible debentures, the SR is sufficient only once in a year for all the offers.
4. Limit of not more than 200 persons in the aggregate in a financial year excluding QIB and employees stock options ESOPs.
5. The value of such offer or invitation per person shall be with an investment size of not less than `20,000 of face value of the securities.
6. Payment to be made for subscription shall be made from the bank account of the person subscribing and the company shall keep the record of the same.

**When prospectus is not required to be issued:**

1. Bona fide invitation to a person to enter into an underwriting agreement
2. Private placement
3. Rights issue or a bonus issue
4. Issue of shares or debentures which are in all respects uniform with shares or debentures previously issued
5. Sweat equity shares
6. Employees Stock Option Scheme

### A1.3.1.1. Requirements as to Registration of Prospectus

**1. Deliver to ROC (Section 26(4) of the Companies Act, 2013):** No prospectus shall be issued by or on behalf of a company or in relation to an intended company unless on or before the date of its publication, a copy has been delivered to the registrar for registration. The same shall be signed by every person who is named therein as a director or proposed director of the company or by his duly authorized attorney.

**2. Prospectus to state the delivery of copy and documents to the registrar (Section 26(6) of the Companies Act, 2013):** Every prospectus issued shall, on the face of it, state that a copy has been delivered for registration to the registrar, and specify any documents required to be attached to the copy so delivered or refer to statements included in the prospectus which specify these documents.

**3. No registration of prospectus (Section 26(7) of the Companies Act, 2013):** The registrar shall not register a prospectus unless the requirements of this section with respect to its registration are complied with, and the prospectus is accompanied by the consent in writing of all the persons named in the prospectus.

**4. Consent of expert (Section 26(5) of the Companies Act, 2013):** If the prospectus includes a statement made by an expert, it shall also include consent in writing of that expert. It should also state that the consent given has not been withdrawn before delivery of the prospectus to the registrar. The expert should not be a person who is connected with the formation or management of the company.

**5. The time period for the issue of a prospectus (Section 26(8) of the Companies Act, 2013):** No prospectus shall be valid if it is issued more than 90 days after the date on which a copy thereof is delivered to the registrar.

**6. Approval by various agencies:** As per SEBI (issue of capital and disclosure requirements) regulations, the draft prospectus has to be approved by various agencies before it is filed with ROC such as all the lead managers to the issue (who must be authorized by SEBI). Each of the stock exchange where the shares are listed or proposed to be listed, lead financial institution underwriting the issue (if applicable, authorized by SEBI).

**7. Vetting by SEBI:** The draft prospectus is vetted by SEBI to ensure adequacy of disclosures. However, vetting by SEBI does not amount to approval of prospectus. SEBI does not take any responsibility for the correctness of the statements made or opinions expressed in the prospectus.

**8. Penalty (Section 26(9) of the Companies Act, 2013):** The penalty for contravention of this section is that a company shall be liable with fine varying from `50,000 to `3 lakh, and every person shall be punishable with imprisonment up to three years or fine varying from `50,000 to `3 lakh or with both.

### A1.3.1.2. Contents of a Prospectus

A prospectus shall be dated and signed and shall have the following information:

1. Names and addresses of registered office and the other persons (such as company secretary and so on)
2. Dates of opening and closing of the issue
3. Details of a separate bank account
4. Details of the underwriters and the amount underwritten by them
5. Consent of directors, auditors, bankers to the issue, expert’s
6. Authority for the issue and resolution details
7. Procedure and time schedule for allotment
8. Capital structure of the company
9. Main objects of public offer
10. Main objects and present business of the company
11. Other particulars relating to management view of risk factors, gestation period, extent of progress, deadlines for completion and any litigation or legal action pending
12. Minimum subscription
13. Details of directors

**Every prospectus sets out the reports** which include the reports by the auditors of the company, reports relating to profits and losses for each of the five financial years and reports about the business or transaction to which the proceeds are to be applied.

**Procedure for variation in terms of contract or objects in prospectus:**

1. A company shall pass SR (in case of listed company through postal ballot).

2. Notice shall also be published in the newspapers indicating clear reason for such variation.

3. The dissenting shareholders shall be given an exit offer by promoters or controlling shareholders.

**An offer of sale of shares:** The members of a company may propose in consultation with the board to offer their holdings. An offer of sale document shall be deemed to be a prospectus and all laws and rules shall apply. The members shall collectively authorize the company whose shares are offered for sale to the public, and they shall reimburse the company all expenses incurred by it.

**Issue of securities in dematerialized form:** In case of public offer, every company making public offer and such other class or classes of public companies prescribed shall issue the securities only in dematerialized form. In case of other companies, the securities shall be converted into dematerialized form.

**Abridged prospectus:** It means a memorandum containing salient features of a prospectus specified by the SEBI. Every form of application issued shall be accompanied by an abridged prospectus. The objective of an abridged prospectus is to reduce the cost of issue. A copy of the prospectus shall be furnished to any person on demand. A company shall be liable to a penalty of `50,000 for each default. However, the exception is when company entered into an underwriting agreement with respect to such securities, or securities are not offered to the public.

**Powers of SEBI to regulate issue and transfer of securities and so on:**

1. According to Section 127, the provisions relating to prospectus, allotment, share capital and debenture by listed companies, companies which intend to get listed, shall be administered by SEBI.

2. Powers relating to all other matters shall be exercised by central government (Ministry of Corporate Affairs [MCA]), the tribunal or the registrar.

### A1.3.1.3. Misstatement or Misleading Statement in Prospectus or Golden Rule for Prospectus

In case, any prospectus has any misleading or misstatement in it, in the form and context or by some omission of material matter, it presents the whole picture of the company. It must disclose all the material facts truly, honestly and accurately. All facts influencing decisions must be disclosed. No fact should be omitted. Any misstatement or omission may lead to criminal and civil liability. The persons who invested in the company, based on misstatement or omission or by such action, may file the suit for damages or take any other action under Section 34, 35 or 36.

**Remedies available to a person deceived by a false and misleading prospectus:**

1. **Remedies against the company as per general law of contracts:** Rescission of the contract is based on the utmost good faith, voidable at the option of the aggrieved party. A subscriber can file a suit against the company to rescind the contract. The following conditions must be followed:
2. The misstatement should be a material fact
3. They should be induced to take the shares
4. The shareholder should have relied on the statement
5. The omission must be misleading
6. Those acting on behalf of the company must have acted fraudulently and authorized to act on its behalf
7. Suffered a loss or damage
8. The proceeding for rescission was started as soon as the allottee came to know the fact
9. **Damages for deceit:**
10. The allottee may recover damages from the company for any loss he may have suffered if he was induced to take shares based on a fraudulent misrepresentation of material facts.
11. The allottee cannot, however, both retain the shares and get damages against the company.

**Liabilities for misstatements in prospectus**

1. **Criminal liability for misstatements in prospectus:** The misstatement in prospectus means any misleading statement in the form or context in which it is included, and certain material matter included or omitted to mislead.
2. Punishment for the misstatement: Every person who authorizes the issue shall be liable to imprisonment for minimum 6 months and up to 10 years and a fine of an amount not less than the amount involved in the fraud which may extend up to 3 times of the amount.
3. Where the fraud involves public interest, the imprisonment shall not be less than 3 years.
4. An exception to criminal punishment is when a person proves that the statement or omission was immaterial or that he had reasonable grounds to believe that it was true.
5. **Civil liability for misstatements in prospectus:** Where the person has subscribed on the prospectus, which is misleading and has sustained any loss, persons liable for the misstatement include the director who authorized himself to be named in the prospectus as a director, the promoter who authorized the issue of the prospectus and the expert. The punishment is that every person shall be liable to pay compensation to every person who has sustained such loss or damage and for fraudulently inducing persons to invest money. However, the exception to civil punishment is if the person proves that, having consented to become a director of the company, he withdrew his consent before the issue of the prospectus and that it was issued without his authority or consent and that it was issued without his knowledge or consent, and on becoming aware its issue, he gave the public notice.

**An expert and his liabilities:** An expert includes an engineer, a valuer, a chartered accountant, a company secretary, a cost accountant and any other person who has the power or authority to issue a certificate. He must be unconnected with the formation or management of the company. A report is included subject to given his written consent and not withdrawn before delivery to ROC and statement appears in the prospectus that he has not withdrawn the same. An expert will be liable for civil liability for misstatements in prospectus. The expert shall not be liable if he has given his consent and he withdraws before delivery for registration, or if the prospectus was issued without his knowledge and gave a reasonable public notice. He is liable in the capacity of an expert and not for any other statement. He has no criminal liability.

* **Persons who fraudulently induces persons:** Persons who fraudulently induce persons to invest money by making a statement which is false, deceptive and so on to enter into any agreement for acquiring, disposing of, subscribing for or underwriting securities or any agreement, the purpose of which is to secure a profit to any of the parties, any agreement for obtaining credit facilities from any bank or financial institution shall be punishable for fraud.
* **Personation for acquisition of securities:** Any person who makes an application in a fictitious name for securities, multiple applications to a company in different names or induces company to allot or register any transfer to him or any other in a fictitious name shall be liable for action under the Companies Act. The amount received through disgorgement or disposal of securities shall be credited to the Investor Education and Protection Fund.

**Deemed prospectus:** The deemed prospectus is issued when an offer for sale to the public was made within six months after the allotment or agreement to allot or the whole consideration had not been received by the company when offer to the public was made. The effect of deemed prospectus includes all the enactments and rules of law which shall be applied on the company. Liability in respect of misstatement in the prospectus shall apply to the deemed prospectus. Deemed that the persons by whom the offer to the public is made as directors.

**Contents of a deemed prospectus**: It shall contain matters as specified in the Companies Act, 2013, the net consideration received or to be received by the company, the time and place for inspection of contract. The deemed prospectus shall be signed by directors of the company, and in case of a company or firm, it shall be signed by not less than one-half of the partners in the firm.

**Shelf prospectus:** ‘Shelf prospectus’ means a prospectus under which one or more issues are made over a certain period without the issue of a further prospectus. It shall commence from the date of opening of the first offer of securities under that prospectus. No further issue of the prospectus is required for a period of one year. It applies to a class or classes of companies, as the SEBI may provide. Filing of shelf prospectus is required at the stage of the first offer, and no further prospectus is required at the second or subsequent offer.

**Filing of information memorandum with the registrar:** Prior to every subsequent offer, information memorandum shall be filed with ROC, which shall contain the details of new charges created, changes in the financial position and such other changes as may be prescribed. If any changes have been made in the shelf prospectus, the company shall intimate to the person who paid money in advance and if he desires to withdraw within 15 days, the company shall refund all the monies received:

**Prospectus = Information memorandum + Shelf prospectus**

**Red-herring prospectus:** It means a prospectus which does not include complete particulars of the quantum or price. A company may issue a red-herring prospectus prior to the issue of a prospectus. The company shall file it with the registrar at least 3 days prior to the opening of the subscription list and the offer. A red-herring prospectus shall carry the same obligations of a prospectus, and any variation between the red-herring prospectus and a prospectus shall be highlighted as variations in the prospectus. Upon the closing of the offer of securities, the prospectus shall be filed with the registrar and the SEBI, which shall state the total capital raised, closing price and any other details which have not been included.

## A1.3.2. Memorandum of Association (MoA)

**Memorandum of Association:** MoA is the charter (constitution) of a company. It is the main document of a company and no company can be incorporated without MoA. It not only defines what a company can do but also what it cannot do. The main object of the MoA is that the shareholders/loan providers can know the purpose for which the funds are going to be used and person dealing can know whether the contractual relation is within its objects. It shall be on the prescribed form as provided in the Companies Act, 2013. The MoA shall be divided into paragraphs and numbered consecutively, signed and at least one witness attest the signature of the subscribers.

### A1.3.2.1. Contents of MoA

There are six clauses in MoA. These are discussed in detailed below:

**Name clause:** The name shall not be identical with the name of an existing company. It shall not be undesirable in the opinion of the central government. The name shall not give the impression that the company is connected with, or having the patronage of the central government, state government or not prohibited by the Emblems and Names (Prevention of Improper Use) Act. Every company shall paint or affix its name and the address of its registered office. It shall have its name engraved in legible characters on its seal. It will have its name printed on Hundies, promissory notes, bills of exchange and so on. An injunction will be given if an identical name is adopted. An existing company can apply to the CG for stopping the new company from using such a name. A company should end with the word ‘limited’ in case of a public company and the words ‘private limited’ in case of a private company. Application for name approval is to be made in INC-1 to indicate the name of the company as private or public.There should beno use of the name that will constitute an offence, no undesirable name as specified in Rule 8 of the Companies (incorporation) Rules andno identical name that resembles the name of an existing company.

**In case of an OPC**: The words ‘one-person company’ shall be mentioned in brackets below. Now all the companies are allotted CIN in addition to the name.

**Registered office/situation clause/location clause:** Every company shall furnish to the registrar of the registered office within a period of 30 days of its incorporation. The registered office is significant that a company shall not commence business unless it has a registered office. A company shall, on and from the 15th day of its incorporation, have a registered office for receiving all communications and notices. The nationality of a company is determined by the place of its registered office. It determines the jurisdiction of the court. The company shall paint or affix its name and address of its registered office at every place in which its business is carried on. It shall get its name, address and CIN printed on all its business letters, billheads and so on. This specifies the state in which the registered office is situated. Form INC-22 is filed and the registrar to be intimated about the details of registered office within 30 days of incorporation or 15 days of the change, if any, as the case may be.

**Objects clause:** It is the most important clause in MoA. It sets the boundary for a company to operate. It cannot undertake any activity which is not specified in the MoA. Members/creditors can know the purpose to which their money can be applied. Persons dealing with the company can know the extent of the company’s powers from it. The company may choose any object. However, the company should not be illegal or against the public interest, for example, gambling. It cannot be against the Act. It shall have objects and matters necessary for progress, powers (e.g., borrowing powers) of a company. Any provision contained in any of the abovementioned document shall be void, to the extent to which it is inconsistent to the provisions of this Act. Memorandum to state the object of the company proposed to be incorporated. The bifurcation of main, ancillary and other objects as required under the Companies Act, 1956, has been dispensed within the Companies Act, 2013.

**Liability clause:** It explains the liability of each member of the company in case of winding up. It states the limits to the liability of the members. In case the company is limited by shares, the liability of a shareholder will be the unpaid amount of the share. In case the company is limited by guarantee, without share capital, the liability of the shareholder will be the amount guaranteed by him. In case the company is limited by guarantee having a share capital, the liability of the shareholder will be the amount guaranteed by him and the unpaid value of the share. In the case of an unlimited company, the liability clause is not mandatory, and the absence of this clause means liability is unlimited. This states that the liability of the members is limited or unlimited. In case of a company limited by shares, that liability of its members is limited to the amount unpaid, if any, on the shares held by them (including premium if any) as against the Companies Act, 1956; wherein, it was limited to the amount unpaid on the face value of the share.

**Capital clause:** The capital clause states that a company shall have the authorized capital and the number and nominal value of shares. The number of shares agreed to subscribe (minimum one share). In case of an OPC, the name of the nominee, the promoters will decide the amount of subscription, stamp duty and registration fee which is payable on the basis of authorized capital. There is no maximum limit to the amount. However, the company with no share capital is not required to have the capital clause. This must state the amount of the capital with which the company is registered. The shares into which the capital is divided must be of a fixed amount and the number of shares which the subscribers to the memorandum agree to subscribe the subscribers to which shall not be less than one share. The capital is variously described as ‘nominal’ or ‘authorized’.

**Association/subscription clause:** The MoA shall be signed by at least two and seven subscribers in case of private and public companies respectively. Each signature shall be attested by at least one witness. Every subscriber is deemed to be a member. A subscriber cannot repudiate his liability on the ground of misrepresentation in the prospectus. Subscribers agree to subscribe to the prescribed number of shares stated against their name in the memorandum. The statutory requirements regarding subscription of the memorandum are: (a) each subscriber must take at least one share and (b) each subscriber agree to take the number of shares set opposite to his name.

### A1.3.2.2. Alteration of MoA

The MoA is a document which sets out the constitution of the company and is the foundation on which the structure of the company stands. It defines as well as confines the powers of the company. If the company enters into a contract or engages in any trade or business which is beyond the powers conferred on it by the memorandum, such a contract or the act will be ultra vires and hence void. However, the Companies Act, 2013, shall override the provisions in the memorandum of a company, if the latter contains anything contrary to the provisions in the Act. The alteration means and includes the making of additions, omissions and substitutions in the existing points of the MoA and different clauses of it. The MoA of a company may be altered by changing its name, altering the state in which the registered office is situated or its objects, altering or reorganizing its share capital, reducing its capital or making the liability of the directors unlimited. The procedure for making any alteration will require passing the special resolution and complying with the procedure specified in the Act. The alteration procedure for each clause is given below:

1. **Alteration of ‘name clause’:** Any company which wants to alter its name needs to pass SR in general meeting, and the approval of the central government is required. In order to delete the word ‘private’, approval from central government is not required in case of conversion of a private company to a public company. The copy of altered MoA, special resolution and copy of the approval of the central government shall be filed with the RoC within the prescribed time.
2. **Alteration of ‘registered office clause’ of MoA:** The alteration in the registered office clause can be in different ways such as change within local limits, change in the jurisdiction of registrar and change of state. The procedure for alteration under different conditions is given below:
3. **Change within the same city, town or village:** The company needs to pass board resolution and SR in the general meeting of the company. The notice of change has to be submitted to the registrar on form INC-22 within 15 days of such change.
4. **From one state to another state**: The company needs to get an approval of the central government in INC-23. The central government must satisfy that the alteration has the consent of the creditors, debenture holders and so on or adequate security has been provided for such discharge. The approval should be registered with the registrar for incorporation certificate. The order of the central government shall be filed with the registrar of each of the states. RoC shall issue a fresh certificate of incorporation indicating the alteration.
5. **From one city, town or village to another involves a change in the jurisdiction of ROC:** The company shall pass an SR and to get confirmation by the regional director to the company within 30 days. The company should file the confirmation with the registrar within 60 days. The RoC must certify within 30 days and the certificate shall be the conclusive evidence.
6. **Alteration of ‘objects’ clause:** The procedure for alteration in the object clause is by passing an SR in the general meeting and filing a copy of an SR with the registrar within a period of 30 days. Such resolution shall also be published in the newspapers and shall also be placed on the website, and the dissenting shareholders shall be given an opportunity to exit.
7. **Alteration of ‘liability clause’:** The alteration in the liability clause of the memorandum can be done by passing the SR and filing with the RoC. It does not affect any debts, liabilities and so on incurred before alteration. The unlimited company should provide for reserve share capital on conversion into limited company. In case, a company increases the nominal amount of its share capital then it provides a specified portion which shall be called only at the time of winding up.
8. **Alteration of ‘capital clause’ of MoA:** Section 61 provides that in case of alteration of capital clause is authorized by AoA, then by passing the ordinary resolution, capital can be altered. If the division or consolidation in the capital and if the voting per cent gets affected, then a confirmation from the tribunal is mandatory. The company shall notify the alterations made and a copy of resolutions passed shall be filed with the registrar within 30 days. The registrar shall record the notice and make alterations required. The alteration in the capital clause includes increasing its authorized capital, consolidating existing shares, converting fully paid-up shares into stock, sub-dividing its shares and cancelling shares which have not been taken.

## A1.3.3. Articles of Association (AoA)

Articles mean the AoA of a company as originally framed or as altered from time to time in pursuance of any previous company law or the Companies Act. It also includes the regulations contained in Tables F–J in Schedule 1 of this Act, in so far as they apply to the company. The memorandum and articles, when registered, bind the company and its members to the same extent as if they have been signed by the company and by each member to observe and be bound by all the provisions of the memorandum and articles. The memorandum lays down the scope and powers of the company and the articles govern the ways in which the objects of the company are to be carried out and can be framed and altered by the members.

### A1.3.3.1. Articles of Association of a Company

The AoA of a company is its rules and regulations, which are framed to manage its internal affairs. The AoA has a significant position in the company functioning and documentation because articles provide the manner in which the objects are to be carried out. It is a business document which regulates the domestic management of a company and bye-laws of the company. The AoA are the rules, regulations and bye-laws for governing the internal affairs of the company. They may be described as the internal regulation of the company governing its management and embodying the powers of the directors and officers of the company as well as the powers of the shareholders. They lay down the mode and the manner in which the business of the company is to be conducted. In framing the AoA, care must be taken to see that regulations framed do not go beyond the powers of the company itself as contemplated by the MoA nor should they violate any of the requirements of the Companies Act itself. All clauses in the articles ultra vires the memorandum or the Act shall be null and void. The AoA is to be printed, divided into paragraphs, serially numbered and signed by each subscriber to memorandum with the address, description and occupation. Each subscriber shall sign in the presence of at least one witness who shall attest the signatures and also mention his own address and occupation.

### A1.3.3.2. Contents and Model of AoA

Articles generally contain provision relating to the following matters: (a) the exclusion, whole or in part of Table A, (b) share capital different classes of shares of shareholders and variations of these rights, (c) execution or adoption of preliminary agreements, if any, (d) allotment of shares, (e) lien on shares, (f) calls on shares, (g**)** forfeiture of shares, (h) issue of share certificates, (i) issue of share warrants, (j) transfer of shares, (k) transmission of shares, (l) alteration of share capital, (m) borrowing power of the company, (n) rules regarding meetings, (o) voting rights of members, (p) notice to members, (q) dividends and reserves, (r) accounts and audit, (s) arbitration provision, if any, (t) directors, their appointment and remuneration, (u) the appointment and reappointment of the managing director, manager and secretary, (v) fixing limits of the number of directors, (w) payment of interest out of capital, (x) common seal and (y) winding up.

**Main points in content:**

1. Articles contain the regulations for the management of the company.
2. The articles may contain provisions for entrenchment, to protect something, and entrenchment shall only be made either on formation of a company or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by an SR in the case of a public company.
3. In case, a company does not have its AoA, or they are silent on any provision, then the company may adopt all or any of the regulations contained in the model articles given in Companies Act, 2013.

### A1.3.3.3. Alteration of the AoA and Its Limitations

A company has a statutory right to alter its AoA. But the power to alter is subject to the provisions of the Act and to the conditions contained in the memorandum. Any alteration so made shall be as valid as it originally contained in the articles.

The alteration in the AoA can be done in the following manner:

1. The company need to pass an SR in the general meeting to give effect to the changes in the AoA.

2. Alteration to include conversion of private company into a public company vice versa

3. Where a private company removes restrictions, from the date of such alteration cease to be a private company.

4. Conversion of a public company to private requires the approval of the tribunal (CG for time being).

5. Shall file with the registrar copy of the altered articles within 15 days.

6. Altered articles are valid as if it were originally contained in the articles.

7. Every alteration made in articles of a company shall be noted in every copy of the articles.

8. A company cannot deprive itself of these powers (Andrews vs Gas Meter Co.).

### A1.3.3.4. Limitations to Alteration

There are the following limitations for making the alteration in AoA:

* The alteration must not exceed the powers given by MoA.
* It must not be against any provisions of the Companies Act.
* It must not be against any provisions of any other law.
* The alteration shall not be illegal or opposed to the public interest.
* It must be for the benefit of the company as a whole.
* The alteration must not be against an order of the court.
* The articles should not be in fraud on minority.
* For converting a public into a private company, the approval of the CG is necessary.

**Difference between MoA and AoA**

1. The MoA explains that companyobject clause states the purposes for which the company has been established, whereas the AoA states the manner in which the objects are to be carried out.

2.The MoA contains 6 clauses. The AoA contains many rules and regulations.

3.TheMoA is the most important document equivalent to the ‘constitution’ whereas the AoA is equivalent to the ‘bye-laws’.

4. It is provided that the objects which are ultra vires of the MoA are fully void and cannot be ratified. However, ultra vires of the articles, but within MoA, can be confirmed by the shareholders of the company.

5. The MoA cannot include any clause contrary to the provisions of the Companies Act. Whereas the AoA cannot include any clause contrary to the provisions of the Act and the MoA.

### A1.3.3.5. Binding Effects of the MoA and the AoA

The MoA and AoA have binding effect on the company, members and person dealing with the company. These effect can be explained as below:

**1. Between the members and the company**: The MoA and AoA constitute a contract between the members and the company and members are bound to the company under a statutory contract. In the case of Borland’s Trustee vs Steel bros & Co. Ltd, the AoA states member’s shares should be sold only to another member. The trustee was bound by articles, as shares were purchased in terms of AoA of the company.

**2. Between the company and the members**: One of the opinions is that it binds in the same way as its members are and another opinion is that the company is not wholly bound. It is bound to the extent to prevent any breach of the article as to rights of a member.

**3. Between the members inter se:** There is no express agreement yet each and every member of the company is bound by the memorandum and the articles. The articles can’t regulate the rights arising out of commercial contract.

**4. Between the company and the outsiders:** TheMoA and AoA do not constitute a contract between the company and outsiders. Neither the company nor the members are bound by the articles to outsiders.

## A1.3.4. Doctrine of Constructive Notice

The doctrine of constructive notice explains that the MoA and AoA are public documents, and it is presumed that the person dealing with the company has read the documents. The person dealing cannot argue that he is not aware of the provisions of the documents. It operates in favour of the company and against the person who failed to enquire. In the case of Kotla Venkataswamy vs Ramamurthy’s case, articles require deeds signed by the managing director, secretary and director. The plaintiff accepted the deed of mortgage signed by the secretary and a working director only. It was held that the plaintiff could not claim anything under this deed.

## A1.3.5. Doctrine of Indoor Management (or) Turquand Rule

This doctrine is an exception to the doctrine of constructive notice. The person presumed to have read the MoA and AoA, and to see that the proposed dealing is not inconsistent therewith, but they need not do more. They can presume that all this was done regularly Royal British Bank vs Turquand, directors were authorized to borrow on bonds by obtaining approval of shareholders. The directors issued a bond to ‘T’ without such approval. It was held that ‘T’ could sue the company on the strength of the bond.

**Conditions for applicability of the doctrine of indoor management:**

* 1. The person dealing with the company must have the knowledge of the MoA and AoA.
	2. The person dealing with the company must not have the knowledge of irregularity.
	3. The person dealing with the company must not be put upon an enquiry.
	4. There must be some procedural or internal irregularity.
	5. There must not be any ultra vires act of illegality.

**Exceptions of the doctrine of indoor management:**

* 1. Acts done in the name of the company are void ab initio.
	2. Cannot apply to forgery which must be regarded as a nullity.
	3. If an officer of a company makes a contract with a third party and if such act of the officer falls outside his ordinary authority.
	4. The person dealing with the company acted negligently.

## A1.3.6. Doctrine of Ultra Vires and Its Effects

The MoA is considered to be the constitution of the company. It sets out the internal and external scope and area of the company’s operation along with its objectives, powers and scope. A company is authorized to do only that much which is within the scope of the powers provided to it by the memorandum. A company can also do anything which is incidental to the main objects provided by the memorandum. Anything which is beyond the objects authorized by the memorandum is an ultra-vires act. The doctrine of ultra vires first time originated in the classic case of Ashbury Railway Carriage and Iron Co. Ltd vs Riche ([1878] LR 7 HL 653) which was decided by the House of Lords. In this case, the company and M/s Riche entered into a contract where the company agreed to finance the construction of a railway line. Later on, directors repudiated the contract on the ground of its being ultra vires of the memorandum of the company. Riche filed a suit demanding damages from the company. According to Riche, the words ‘general contracts’ in the objects clause of the company meant any kind of contract. Thus, according to Riche, the company had all the powers and authority to enter and perform such kind of contracts. Later, the majority of the shareholders of the company ratified the contract. However, directors of the company still refused to perform the contract as according to them the act was ultra vires and the shareholders of the company cannot ratify any ultra-vires act.

When the matter went to the House of Lords, it was held that the contract was ultra vires of the memorandum of the company, and thus, null and void. The term ‘general contracts’ was interpreted in connection with preceding words mechanical engineers, and it was held that here this term only meant any such contracts as related to mechanical engineers and not to include every kind of contract. They also stated that even if every shareholder of the company would have ratified this act, then also it had been null and void as it was ultra vires of the memorandum of the company. The memorandum of the company cannot be amended retrospectively, and any ultra-vires act cannot be ratified.

**Purpose of the doctrine of ultra vires:** This doctrine assures the creditors and the shareholders of the company that the funds of the company will be utilized only for the purpose specified in the memorandum of the company. In this manner, the investors of the company can get assured that their money will not be utilized for a purpose which is not specified at the time of investment. If the assets of the company are wrongfully applied, then it may result in the insolvency of the company, which in turn means that creditors of the company will not be paid. This doctrine helps to prevent such kind of situation. This doctrine draws a clear line beyond which directors of the company are not authorized to act. It puts a check on the activities of the directors and prevents them from departing from the objective of the company.

**Difference between ultra-vires and an illegal act:** An ultra-vires act is entirely different from an illegal act. People often mistakenly use them as a synonym to each other while they are not. Anything which is beyond the objectives of the company as specified in the memorandum of the company is ultra-vires. However, anything which is an offence or draws civil liabilities or is prohibited by law is illegal. Anything which is ultra vires, may or may not be illegal, but both of such acts are void ab initio.

**The doctrine of ultra vires in the Companies Act, 2013:** Section 4 (1)(c) of the Companies Act, 2013, states that all the objects for which incorporation of the company is proposed and any other matter which is considered necessary in its furtherance should be stated in the memorandum of the company. Whereas Section 245 (1)(b) of the Act provides to the members and depositors a right to file an application before the tribunal if they have reason to believe that the conduct of the affairs of the company is conducted in a manner which is prejudicial to the interest of the company or its members or depositors, to restrain the company from committing anything which can be considered as a breach of the provisions of the company’s memorandum or articles.

### The basic principles regarding the doctrine:

1. Shareholders cannot ratify an ultra-vires transaction or act even if they wish to do so.

2. Where one party has entirely performed his part of the contract, reliance on the defence of the ultra vires was usually precluded in the doctrine of estoppel.

3. Where both the parties have entirely performed the contract, then it cannot be attacked on the basis of this doctrine.

4. Any of the parties can raise the defence of ultra vires.

5. If a contract has been partially performed but the performance was insufficient to bring the doctrine of estoppel into the action, a suit can be brought for the recovery of the benefits conferred.

6. If an agent of the corporation commits any default or tort within the scope of his employment, the company cannot defend it from its consequences by saying that the act was ultra vires.

## Exceptions to the doctrine:

1. Any act which is done irregularly, but otherwise it is intra vires of the company, can be validated by the shareholders of the company by giving their consent.

2. Any act which is outside the authority of the directors of the company but otherwise it is intra vires of the company can be ratified by the shareholder of the company.

3. If the company acquires property in a manner which is ultra vires of the contract, the right of the company over such property will still be secured.

4. Any incidental or consequential effect of the ultra-vires act will not be invalid unless the Companies Act expressly prohibits it.

5. If any act is deemed to be within the authority of the company by the Company’s Act, then they will not be considered as ultra vires even if they are not expressly stated in the memorandum.

6. The AoA can be altered with retrospective effect to validate an act which is ultra vires of the articles.

## Types of Ultra-vires Acts and When an Ultra-vires Act Can Be Ratified

## The ultra-vires Acts can be generally of four types:

* Acts which are ultra vires to the Companies Act.
* Acts which are ultra vires to the memorandum of the company.
* Acts which are ultra vires to the articles of the company but intra vires of the company.
* Acts which are ultra vires to the directors of the company but intra vires of the company.

**Acts which are ultra vires to the Companies Act:** Any act or contract which is entered by the company which is ultra vires to the Companies Act is void ab initio, even if the memorandum or articles of the company authorized it. Such act cannot be ratified in any situation. Similarly, some acts are deemed to be intra vires for the company even if they are not mentioned in the memorandum or articles because the Companies Act authorizes them.

**Acts which are ultra vires to the memorandum of the company:** An act is called ultra vires to the memorandum of the company if it is done beyond the powers provided by the memorandum to the company. If a part of the act or contract is within the authority provided by the memorandum and remaining part is beyond the authority, then both the parts can be separated. Then only that part which is beyond the powers is considered as ultra vires, and the part which is within the authority is considered as intra vires. However, if they cannot be separated then the whole contract or act will be considered as ultra vires and hence void. Such acts cannot be ratified even by shareholders as they are void ab initio.

**Acts which are ultra vires to the articles but intra vires to the memorandum:** All the acts or contracts which are made or done beyond the powers provided by the articles but are within the powers and authority given by the memorandum are called ultra vires to the articles but intra vires to the memorandum. Such acts and contracts can be ratified by the shareholders (even retrospectively) by making alterations in the articles to that effect.

**Acts which are ultra vires to the articles but intra vires to the memorandum:** All the acts or contracts which are made or done beyond the powers provided by the articles but are within the powers and authority given by the memorandum are called ultra vires to the articles but intra vires to the memorandum. Such acts and contracts can be ratified by the shareholders (even retrospectively) by making alterations in the articles to that effect.

## Effects of Ultra-vires Transactions (the Doctrine of Ultra Vires)

1. **Void ab initio:** The ultra vires acts are null and void ab initio. These acts are not binding on the company. Neither the company can sue, nor it can be sued for such acts (Ashbury Railway Carriage and Iron Company vs Riche).

2. Estoppel or ratification cannot convert an ultra-vires act into an intra-vires act.

3. **Injunction:** When there is a possibility that company has taken or is about to undertake an ultra-vires act, the members can restrain it from doing so by getting an injunction from the court—Attorney General vs Gr. Eastern Rly. Co., ([1880] 5 AC 473).

4. **Personal liability of the directors**: The directors have a duty to ensure that all corporate capital of the company is used for a legitimate purpose only. If such funds are diverted for a purpose which is not authorized by the memorandum of the company, it will attract personal liability for the directors.

**Criminal liability:** Criminal action can also be taken in case of a deliberate misapplication or fraud. However, there is a small line between an act which is ultra vires to the directors and acts which are ultra vires to the memorandum. If the company has authority to do anything as per the memorandum of the company, then an act which is done by the directors beyond their powers can also be ratified by the shareholders, but not otherwise. If any property is purchased with the money of the company, then the company will have full rights and authority over such property even if it is purchased in an ultra-vires manner.

## Effects of an Act Which Is Ultra Vires—On Borrowings

Any borrowing which is made by an act which is ultra vires will be void ab initio. It will not bind the company, and the outsiders cannot get them enforced in a court. The members of the company have power and right to prevent the company from making such ultra-vires borrowings by bringing injunctions against the company. If the borrowed funds of the company are used for any ultra-vires purpose, then directors of the company will be personally liable to make good such act. If the company acquires any property from such funds, the company will have full right to such property. No estoppel or ratification can convert an ultra-vires borrowings into an intra-vires borrowings, as such acts are void from the very beginning. As no debtor and creditor relationship is created in ultra-vires borrowings only a remedy in rem and not *in personam* is available.

# A1.4. Directors

A company is an artificial person in the eyes of law which is incorporated to do certain things which are given in the MoA of the company. It cannot function of its own, in order to enable a company to achieve its objects as enshrined in the objects clause of its MoA, it has necessarily to depend upon some agency, known as the board of directors. The board of directors of a company is a nucleus, selected according to the procedure prescribed in the Companies Act and the AoA. The members of the board of directors are known as directors, who unless especially authorized by the board of directors of the company, do not possess any power of the management of the affairs of the company. Acting collectively as a board of directors, they can exercise all the powers of the company except those which are prescribed by the Act to be specifically exercised by the company in the general meeting. The directors formulate policies and establish organizational setup for implementing those policies and to achieve the objectives contained in the memorandum, muster resources for achieving the company objectives and control, guide, direct and manage the affairs of the company.

## A1.4.1. Definition of Director and Maximum and Minimum Number of Directors

Section 2(34) of the Act prescribed that a ‘director’ means a director appointed to the board of a company. Section 2(10) defined that the ‘board of directors’ or the ‘board’, in relation to a company, means the collective body of the directors of the company. The term ‘board of directors’ means a body duly constituted to direct, control and supervise the affairs of a company. As per Section 149, the board of directors of every company shall consist of individual only. Thus, no body corporate, association or firm shall be appointed as the director. Section 166 of Companies Act, 2013, prohibits the assignment of office of director to any other person. Any assignment of office made by a director shall be void.

**Minimum/maximum number of directors in a company:** Section 149(1) requires that every public company shall have minimum three directors and two in the case of a private company, and one director in the case of an OPC. A company can appoint a maximum of 15 directors. A company may appoint more than 15 directors after passing an SR in the general meeting and the approval of the central government is not required. The restriction of the maximum number of directors shall not apply to Section 8 of the Companies Act.

**The number of directorships (Section 165):** A person cannot hold more than 20 directorships, including any alternate directorship. However, a person cannot be a director of more than 10 public companies or subsidiary company of a public company. Alternate directorship shall also be included while calculating the directorship of 20 companies. Section 8 company will not be counted for the purpose of the maximum number of directorship. If a person accepts an appointment as a director in contravention of this, he shall be punished with fine which shall not be less than `5,000 but which may extend to `25,000 for every day after the first day during which the contravention continues.

**Indian resident director:** Section 149 (3) provide that every company shall have at least one director who stays in India for a total period of not less than 182 days during the financial year. In the case of a newly incorporated company, the requirement shall apply at the end of the financial year in which it is incorporated.

**Woman director:** Section 149 (1) provides that every listed company, every public company having paid-up share capital of `100 crores or more; or turnover of `300 crores or more shall appoint at least one woman director. The paid-up share capital or turnover, as the case may be, as on the last date of the latest audited financial statements shall be taken into account. A company, which has been incorporated under the Act and is covered under provisions of section 149 shall comply with within a period of six months from the date of its incorporation. However, any intermittent vacancy of a woman director shall be filled up by the board at the earliest but not later than immediate next board meeting or three months from the date of such vacancy whichever is later.

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| **Director elected by small shareholders:** According to Section 151, every listed company may have one director elected by such small shareholders as explained under this Act. ‘Small shareholder’ means a shareholder holding shares of nominal value of not more than `20,000 or such other sum as may be prescribed.  |

**A1.4.2. Appointment of directors:** Section 152 provides that first directors of companies are named in their articles and the number of directors and names of the first directors shall be determined in writing by the subscribers of the memorandum or a majority of them. If they are not so named in the articles of a company, then subscribers to the memorandum who are individuals shall be deemed to be the first directors of the company until the directors are duly appointed. In the case of an OPC, an individual being a member shall be deemed to be its first director until the director(s) are duly appointed by the member in accordance with the provisions of Section 152. Section 152 (1) is applicable to all companies, whether public or private. The other provisions for the appointment of directors are:

1. Every director shall be appointed by the company in the general meeting unless the Act requires or specifies any other manner of the appointment of the directors.

2. Director identification number (DIN) is compulsory for the appointment of director of a company.

3. Every person proposed to be appointed as a director shall furnish his DIN and a declaration that he is not disqualified to become a director under the Act.

4. A person appointed as a director shall on or before the appointment give his consent to hold the office of director in physical form DIR–2, that is, the consent to act as a director of a company.

5. Company shall file Form DIR–12 along with the form DIR–2 as an attachment within 30 days of the appointment of a director and necessary fee.

6. The consent to act as director and intimation to the registrar is not required in case of section 8 company and where the appointment of such director is done by the central or state government, as the case may be.

**A1.4.2.1. Retirement by rotation:** Section 152 provides that the AoA provides for retirement of all the directors. If there is no provision in the article, then not less than two-thirds of the total number of directors of a public company shall be persons whose period of office is liable to determination by retirement by rotation and eligible to be reappointed at annual general meeting. ‘Total number of directors’ shall not include independent directors appointed on the board of a company. Nominee directors appointed by a financial institution or by the central government under Section 408 shall not be included in the ‘total number of directors’. At the AGM of a public company, one-third of the retiring directors are liable to retire by rotation shall retire from office in the order of their appointment as director in case appointed on same date, then on the basis of agreement among themselves or to be chosen by lot. The directors in the government companies are not liable to retire by rotation.

1. **Vacancy in case of retiring director:** At the AGM at which a director retires by rotation, the company may fill up the vacancy by appointing the retiring director or some other person thereto. If the vacancy of the retiring director is not so filled-up, the meeting shall stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a holiday, at the same time and place. If at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless a resolution for the re-appointment of such director has been put to the meeting and lost or expressed his unwillingness to be so re-appointed, or not qualified or disqualified for appointment, The appointment of directors to be voted individually is applicable to the case.

**Punishment:** If any individual or director of a company contravenes any of the provisions of Section 152, such individual or director of the company shall be punishable with imprisonment for a term which may extend to six months or with fine which may extend to `50,000 and where the contravention is a continuing one, with a further fine which may extend to `500 for every day after the first day during which the contravention continues.

### A1.4.2.2. Appointment of Additional Director

Section 161 provides that the board of directors can appoint additional directors if they are empowered by the AoA. Regulation 66 of Table F authorizes the board to appoint the additional directors. The number of directors and additional directors together shall not at any time exceed maximum strength fixed for the Board by the articles. Such additional directors hold office only up to the date of next annual general meeting; or last date on which the AGM should have been held, whichever is earlier. If default is made in holding AGM, the additional director shall vacate his office on the last day on which the AGM ought to hold. A person who fails to get appointed as a director in a general meeting cannot be appointed as Additional Director. Section 161 (1) of the Act applies to all companies, whether public or private.

### A1.4.2.3. Appointment of Alternate Director

Section 161 (2) empowers the board if so authorized by its articles or by a resolution passed by the company in general meeting, to appoint a director to act in the absence of an original director during his absence for a period of not less than three months from India. If it is proposed to appoint an alternate director to an independent director, it must be ensured that the proposed appointee also satisfies the criteria of independence as per Section 149 (6) of the Act. There is no condition that an alternate director shall be appointed only by passing a resolution at a board meeting. Therefore, an alternate director can be appointed by passing a resolution by circulation. If the original director ceases to be a director by reason of death or vacation of office under Section 167, the alternate director shall immediately cease to hold his office. The alternate director shall vacate his office when the original director in whose place he has been appointed returns to India.

# A1.8. Key Terms

**Annual General Meeting (Section 96):** AGM is an important annual event where members get an opportunity to discuss the activities of the company. Section 96 provides that every company, other than an OPC is required to hold an annual general meeting every year.

**Articles of Association:** Articles means the AoA of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this act. It also includes the regulations contained in Tables F–J in Schedule 1 of this Act, in so far as they apply to the company.

**Abridged prospectus:** It means a memorandum containing such salient features specified by the SEBI. Every form of application issued shall be accompanied by an abridged prospectus. The objective of abridged prospectus is to reduce the cost of issue. A copy of the prospectus shall be furnished to any person on demand.

**Adjournment:** Adjournment means to defer or suspend the meeting to a future time, either at an appointed date or indefinitely or as decided by the members present at the scheduled meeting.

**Corporate veil:** A company is a person created by law, having a distinct entity. This principles referred as veil of incorporation. However, If the veil is used as a mask of fraud, then the courts will lift the veil and look at the persons behind the company.

**Special resolution (SR):** A resolution is an SR when it is intended to be passed as an SR. The votes cast in favour of such resolution by members who, are required to be not less than three times the number of the votes, if any, cast against the resolution by members so entitled and voting.

**General meeting:** Meeting of the members of the company with the board of directors. This may be extraordinary general meeting (EGM) or AGM.

**Share capital:** Funds raised by issuing shares in return for cash or other considerations. The amount of share capital a company can change over time because each time a business sells new shares to the public in exchange for cash, the amount of share capital will increase. Share capital can be composed of both common and preferred shares.

**Redemption of shares:** Where a company issues shares on terms stating that they can be bought back by the company. Not all shares can be redeemed, only those stated to be redeemable when they were issued. The payment for the shares must generally come from reserves of profit so that the capital of the company is preserved.

**Sweat equity shares:** Sweat equity shares mean equity shares issued by a company to its employees or directors at a discount or for consideration, other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

**Rights issue:** Rights issue is an issue of capital to be offered to the existing shareholders of the company through a letter of offer.

**Bonus shares:** When a company is prosperous and accumulates large distributable profits, it converts these accumulated profits into capital and divides the capital among the existing members in proportion to their entitlements. The members do not have to pay any amount for such shares. A company may, if its Articles provide, capitalize its profits by issuing fully paid bonus shares.

**Dormant company:** Where a company is formed and registered under the Companies Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed, for obtaining the status of a dormant company.

**One-person company (OPC):** ‘One-person company’ means a company which has only one person as a member.

**Small company:** A small company means a company, other than a public company, paid-up share capital of which does not exceed `50 lakh or such higher amount as may be prescribed which shall not be more than `10 crores, and turnover of which as per profit and loss account for the immediately preceding financial year does not exceed `2 crore or such higher amount as may be prescribed which shall not be more than one `100 crore rupees.

**Private company:** It means a company having a minimum paid-up share capital as may be prescribed, and which by its articles, restricts the right to transfer its shares, except in case of an OPC, limits the number of its members to two hundred. It is provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member.

**Public Company:** It means a company which is not a private company and has a minimum paid-up share capital, as may be prescribed. It is provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.

**Holding company:** A holding company, in relation to one or more other companies, means a company of which such companies are subsidiary companies.

**Subsidiary company:** A subsidiary company , in relation to any other company (that is to say the holding company), means a company in which the holding company which controls the composition of the board of directors; or exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies.

**Associate company:** in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

**Body corporate:** Itincludes a company incorporated outside India but does not include a cooperative society registered under any law relating to co-operative societies; and any other body corporate, which the central government may, by notification, specify in this behalf.

**Foreign company:** It means any company or body corporate incorporated outside India which has a place of business in India whether by itself or through an agent, physically or through electronic mode; and conducts any business activity in India in any other manner.

**Listed company:** It means a company which has any of its securities listed on any recognized stock exchange.

**Government company:** It means any company in which not less than fifty-one percent of the paid-up share capital is held by the central government, or by any 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 company of such a Government company.

**Banking company:** It means a banking company as defined in clause (c) of Section 5 of the Banking Regulation Act, 1949.

**Financial institution:** It includes a scheduled bank, and any other financial institution defined or notified under the Reserve Bank of India Act, 1934.

**Prospectus:** Any document described or issued as prospectus and includes a red-herring prospectus or shelf prospectus 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.

**Memorandum of association (MoA):** The MoA is the charter (constitution) of the company. It is the main document of the company and no company can be incorporated without the MoA. It not only defines what a company can do and but also what it cannot do.

**Director:** A ‘director’ means a director appointed to the board of a company.

**Extraordinary general meeting (EGM):** There are so many matters relating to the business of a company, which requires approval or consent of members in general meeting. It is always not possible for consideration of such matters to wait until the next AGM.

**Class meetings:** The meetings of members of a company fall into two broad divisions, namely the general meetings and class meetings. Class meetings are meeting of shareholders, holding a particular class of share which is held to pass resolution which will bind only the members of the class concerned.

**Ordinary resolution:** A resolution shall be an ordinary resolution if the notice required under this Act has been duly given and it is required to be passed by the votes cast, whether on a show of hands, or electronically or on a poll, as the case may be, in favour of the resolution, including the casting vote, if any, of the chairman, by members who, being entitled so to do, vote in person, or where proxies are allowed, by proxy or by postal ballot, exceed the votes, if any, cast against the resolution by members, so entitled and voting.

**Proxy:** Proxymeans an instrument in writing authorizing another person to attend on behalf of member. Every member entitled to attend, and vote meeting are entitled to appoint a proxy. In case of company having no share capital cannot not apply for proxy unless articles provide otherwise.

**Minutes:** These are written record of business transacted at a meeting and contain a fair and correct summary of the proceedings. Section 118 provide that preparation of the minutes of the proceedings of meetings: every company shall cause minutes of the proceedings of every general meeting, resolution passed by postal ballot and meeting of its board of directors or committee to be prepared and signed within 30 days of the conclusion. Minutes shall contain a fair and correct summary of the proceedings there at.

**Winding up:** Winding up of a company is a process by which the life of a company is brought to an end and its property administered for the benefit of its members and creditors.

# A1.9. Text Questions

1.What is a company? Explain the features of a company.

2. Explain different types of companies and differentiate between a public and private company.

3. What do you understand by the corporate veil and the exceptions of it?

4. What is the process of incorporation of a company and is certificate of incorporation the conclusive evidence of incorporation?

5. Who is a promoter? Discuss his position and his liabilities.

6. What is a prospectus? Explain its contents and golden rule of prospectus.

7. What is an MoA? Explain the different clauses of it.

8. What is the procedure for alteration in different clauses of an MoA?

9. What is an AoA and its contents? Explain the procedure of alteration in an AoA.

10. What do you understand by the term director? How is he appointed?

11. What are the qualifications and disqualifications of a director?

12. You are required to explain the circumstances when a director has to vacate his office.

13. What are the provisions of BOD meetings?

14. What is AGM? Explain the procedure for holding it.

15. Explain EGM and the procedure for holding it.

16. Explain agenda, special and ordinary resolution, proxy and minutes of meetings.

17. What is winding up of a company and is it different from dissolution?

18. What are the types of winding of company? Explain winding up by the tribunal?

19. Who is a liquidator? Explain his powers and duties.

20. What is a share capital and explain the issue of shares on premium and discount.

# A1.10. Further Readings

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