

Share Qualification (Sections 270 – 273)

Time within which share qualification is to be obtained and maximum amount thereof (Section 270)

Question 1

Mr. A has been appointed as a director in a Public Limited Company? Referring to the provisions of the Companies Act, 1956 state:

- (a) *Whether the director should possess any share qualification?*
- (b) *If so what is the number of share(s), which he should acquire and at what value?*
- (c) *Whether the articles of the company can insist on the director for compulsory acquiring of share qualification?*

Answer

It is that number of shares which a shareholder must hold in order to be eligible for election as a director. The Companies Act, 1956 does not prescribe for any share qualification for a director. However, Regulation 66 of Table A provides that the qualification for being a director of a company is the holding of at least one share in the company. The articles of a company usually prescribe for such qualifications so that a director has a personal interest in the company. In the event of such a provision by the articles, it becomes incumbent on the part of every director to hold qualification shares and if does not hold them at the time of his appointment as director, he must acquire them within two months after his appointment as director. *Any provision, made in the articles of the company requiring a person proposed for directorship to hold qualification shares either before appointment or within a third shorter than two months after his appointment will be void. The nominal value of qualification shares must not exceed ₹5,000 and if the nominal value of each share is ₹5,000 or more than the number of shares prescribed, as qualification will be only one. It is, of course, not necessary for any company to insist upon the holding of shares for the purpose of qualification for directors.* For the purpose of share qualification, the bearer of a share warrant is not deemed to be the holder of the shares mentioned in the warrant (Section 270). A Director acting without qualification shares is punishable with fine, which may extend to ₹ 500/- for every day during which he continues as director (Section 272). The provisions relating to the share qualification of a director do not apply to a private company, unless it is subsidiary of a public company (Section 273) nor do they apply to directors appointed by the Central Government under Section 408.

Question 2

Discuss the validity of the arguments of the Director in the following cases:

7.2 Corporate and Allied Laws

In the General Meeting of X Ltd., held on 2.5.2000, Mr. A was appointed as a Director. On that day, he was not holding any equity shares in X Ltd. As per the Articles of Association of X LTD, the share qualification is the holding of 500 equity shares. On 15.6.2000 Mr. A applied for 1,000 equity shares in X Ltd and the shares were allotted on 10.7.2000. Mr. A claims that he was holding the qualification shares within the time specified in Companies Act. (November, 2000)

Answer

Under Section 270 of the Companies Act, 1956, the director must obtain qualification shares within two months from the date of appointment. In this case, he was appointed on 2.5.2000 and therefore he must obtain qualification shares on or before 2nd July, 2000 but the shares were allotted on 10th July, 2000. Only after the date of allotment, he was looking those shares and not on the date of application. Therefore, the argument of A is not correct.

Question 3

- (i) *The Articles of Association of MKP Limited incorporated with an Authorised Share Capital of Rs.50 crores divided into 5 crore Equity Share of Rs.10 each contained the following clause:*

"The qualification of a director shall be the holding of at least 1,000 Equity Shares in the Company and such a director, if not already so qualified shall have to obtain his qualification within a period of 30 days from the date of his appointment as a director."

Examine the validity of the above clause in the light of the provisions of the Companies Act, 1956.

- (ii) *Redraft the above clause which would conform to the provisions of the Companies Act, 1956. (November, 2004, CA Final, New Course, June 2009)*

Answer

- (i) The subject matter of the question is covered by the provisions of section 270 of the Companies Act, 1956. The Companies Act, 1956 does not provide for any qualification for becoming a director of any company. According to the said section, any person appointed as a director is required to obtain the qualification if it is so provided by the Articles of Association of the company.

The said section states that in case the Articles of Association of a company provides for the qualification of a director, then such a director is required to obtain the requisite qualification within a period of two months from the date of his appointment as a director. The section further states that any clause in the Articles of Association requiring the director to obtain the qualification shares within a shorter time than two months shall be void.

The said section also puts a maximum limit on the qualification that can be prescribed by the Articles of Association. Such maximum limit being shares with nominal value not exceeding Rs.5,000 or in a case where the nominal value of one shares exceeds ₹ 5,000 then the qualification share shall be maximum one share.

Based on the provisions of section 270 of the Companies Act, 1956 as explained above, the clause in the Articles of Association as given in the question is void since it stipulates the obtaining of the qualification shares within a period of 30 days which is shorter than two months. Moreover the clause also violates the maximum limit of share qualification by prescribing the same to be 1,000 shares of Rs.10 each totaling Rs.10,000 which is more than the limit of ₹ 5,000 as prescribed in the said section.

- (ii) The clause to be included in the Articles of Association regarding qualification of directors conforming to the provisions of the Companies Act, 1956 may be as follows:

“The qualification of a director shall be the holding of shares with a nominal value not exceeding Rs.5,000 or one share with a nominal value of Rs.5,000, and such a director if not already so qualified shall have to obtain his qualification within a period of two months from the date of his appointment as a director.”

Question 4

X, who does not hold any shares in his name is appointed as Director in JAM Company on 1st April, 2010. His wife holds 10,000 Equity Shares in the company in her name singly. Certain members of the company objects to X' appointment on the ground that since he does not hold any shares in his own name, his appointment is violative of the provisions of the Companies' Act, 1956. Articles of the Company are silent on the issue of holding any shares by a Director.

Examine the provisions of the Act and decide

- (i) *Whether contention of the members is tenable?*
- (ii) *Whether X wife's shareholding in the company can be the ground for 'X' continuation as a director in the company?*
- (iii) *What would be your answer in case 'X' is one of the subscribers of the Memorandum of Association?*

(CA Final, New Course, November 2010)

Answer

The Companies Act, 1956 does not impose any share qualification on the directors. Therefore, unless the company's articles contain a provision to that effect, a director need not be a shareholder. However, the articles usually provide for a minimum share qualification. As per Regulation 66 of Table A, a director must hold at least one share in a company. Where a share qualification is fixed by the articles of a public company or a private company which is a subsidiary of a public company, Section 270 provides that:

- (i) each director must take his qualification shares within two months after his appointment;
- (ii) the nominal value of the qualification shares must not exceed ₹ 5,000 after his appointment
- (iii) share warrants will not count for purposes of share qualification.

7.4 Corporate and Allied Laws

If a director fails to obtain his qualification shares within two months, he vacates office automatically on the expiry of two months after the date of his appointment. However, the subscribers to the Memorandum, as per provisions of the Act and/or Articles are deemed to be the first directors of the company. They need not hold qualification shares, unless the Articles so require.

Examining the above provisions of the Act, following shall be the answers to the questions asked:

- (i) Contention of members shall not be tenable, for the reasons stated above (i.e. provisions of the Act).
- (ii) His wife's holding of shares shall not be the qualification for the director. If the Articles are silent, the director need not hold any shares. Articles may provide that directors need not hold any qualification shares.
- (iii) If he is one of the subscribers to the memorandum, he need not hold the Qualification shares. However, as a subscriber to a Memorandum he has to take at least a share and that share entitles him to qualify as a director. Therefore, he can continue as a director in the given case.

Penalty (Section 272)

Question 5

Mr. Busybody has been appointed as a Director of ACE Automobiles Limited on 2nd April, 2002. The articles of association of the company provide that the qualification of a director shall be holding of at least 10 shares in the company. Mr. Busybody applied for 10 equity shares of the company on 31st May, 2002. But the shares were allotted only at the Board meeting held on 19th August, 2002. Examine with reference to the relevant provisions of the Companies Act, 1956 whether Mr. Busybody has complied with the requirements relating to qualification shares. If not, what are the consequences? **(May, 2003)**

Answer

The Companies Act, 1956 does not provide for any share qualification of any director. But Regulation 66 of Table A provides that a Director must hold at least one share in the company. Usually the Articles of a company provides for holding qualification share by a Director. Where a share qualification has been prescribed in the Articles of a company which is a public company or a private company which is a subsidiary of a public company, the provisions of section 270 regarding holding of share qualification by a Director shall apply whereby such director must take his qualification share within 2 months after his appointment.

If a person acts as a director without acquiring the qualification share in accordance with the provisions of section 270, he shall be punishable with fine which may extend to Rs.500/- for every day during which he continues to act as a director (Section 272). Moreover a director who fails to hold qualification shares is liable to vacate his office. (Section 283(i)(a).

In this case, Mr. Busybody was appointed as Director of ACE Automobiles Ltd on 2nd April,

2002. He applied for shares of the company on 31st May, 2002 which was allotted only at the Board Meeting held on 19th August 2002. Unless the shares applied for by Mr. Busybody has been allotted in his favour it cannot be said that he held the shares before expiry of 2 months from the date of his appointment. Therefore Mr. Busybody must vacate his office of director.

Question 6

The articles of association of DEF Ltd. mentioned in it that Mr. X and Mr. Y will act as directors of the company from the date of incorporation. The company was incorporated on 2nd January, 2007. The articles also provided that the directors will have to obtain qualification shares within one month from the date of appointment as director. Mr. X purchased the shares of the company on 28th February, 2007 and Mr. Y purchased on 28th March, 2007 thus violating the provisions contained in the articles. Having regard to the provisions of the companies Act. Examine the validity of the appointments of Mr. X and Mr. Y as directors.
(November 2007)

Answer

Without prejudice to the restrictions imposed by section 266, it shall be the duty of every director who is required by the articles of the company to hold a specified share qualification and whom is not already qualified in that respect, to obtain his qualification within two months after his appointment as director [Section 270(1)]

So it becomes incumbent on the part of every director to hold qualification share within the time specified and if he does not held the same at the time of his appointment as director he must acquire them within two months after his appointment as director. Any provision made in the articles of the company requiring a person proposed for directorship to hold qualification share either before appointment or within a shorter than two month after his appointment will be void.

Here the provision in the articles of association to hold shares within one month shall be void. Keeping the above provision in consideration the appointment of Mr. X will be valid as he acquired the share before the expiry of two months. As far the appointment of Mr. Y is concerned he has failed to acquire the share within two-month period. As per section of 283(1)(a) the office of director shall become vacant if he fails to obtain the shares within the time specified in section 270(1) therefore Mr. Y shall have to vacate his office. Here the date of incorporation is taken as the date of appointment.

Question 7

The Articles of Association of Sunrise Ltd. provide that the qualification of a director shall be holding of at least 10 shares in the company. Mr. Rao has been appointed as a director in the said meeting on 1st May, 2008. Mr. Rao applied for 10 equity shares of the company on 30th July, 2008. The said shares were allotted to him on 20th August, 2008 when the Board meeting was held.

7.6 Corporate and Allied Laws

Discuss the relevant provisions of the Companies Act, 1956 in the matter of share qualification requirements and the consequences of non-compliance thereof. Also state whether Mr. Rao has complied with the requirements in this regard. **(November 2008)**

Answer

The Companies Act, 1956 does not provide for any share qualification of any director but Regulation 66 of Table 'A' provides that a director must hold at least one share in the company. Usually, the articles of the company provide for holding qualification shares by a director. Where a share qualification has been prescribed in the Articles of a company which is a public company or a private company which is a subsidiary of a public company, the provisions of Section 270 of the Companies Act, 1956 is applicable where under a director must take his qualification shares within 2 months after his appointment. Any provision in the articles of the company shall be void in so far as it requires a person to hold the qualification shares before his appointment as a director or to obtain them within a shorter time than two months after his appointment as such. The nominal value of the qualification shares shall not exceed Rs.5000/- or the nominal value of one share where it exceed Rs.5000/.

A person acting as a director without acquiring qualification shares is punishable under Section 272 of the said Act. Moreover, a director who fails to hold qualification shares is also liable to vacate his office under Section 283 of the Companies Act, 1956.

In the instant case Mr. Rao was appointed as Director of Sunrise Limited on 1st may 2008. He applied for shares of the company on 30th July 2008 which were allotted only at the Board meeting held on 20th August 2008. It can not therefore be said that he held the shares before expiry of 2 months from the date of his appointment. In view of this Mr. Rao must vacate his office as director as provided in Section 283(1)(a).