

Producer Companies (Sections 581A – 581ZT)

Appointment of Directors (Section 581P)

Question 1

XYZ Producer Company Limited was incorporated on 1st April, 2003. At present it has got 200 members and its board consists of 10 Directors. The Board of Directors of the company seeks your advice on the following proposals:

- (i) Appointment of one expert Director and one Additional Director by the Board for a period of four years.*
- (ii) Loan of Rs.10,000 to Mr. X, a Director of the company repayable within a period of six months.*
- (iii) Donation of Rs.10,000 to a Political Party.*

Advise the Board of Directors explaining the relevant provisions of the Companies Act, 1956.

(May, 2004)

Answer

Producer Company

Appointment of expert director or additional director: Section 581P(6), Companies Act, 1956 empowers the Board of Directors of a producer company to co-opt one or more expert directors or an additional director not exceeding one fifth of the total number of directors for such period as the Board may deem of it. But the maximum period shall not exceed the period specified in the Articles of the company (Proviso 2 to Section 581P(6)).

The number of directors proposed to be co-opted is only 2 and it does not exceed one-fifth of the total number of directors. They can hold office for the period specified by the Board provided it does not exceed the period specified in the Articles (Section 260 stipulating that the additional director can hold office only upto the date of the next annual general meeting is not applicable to a producer company). Hence the proposed appointment of one expert director and one additional director is in order.

Loan to a director: Section 581ZK empowers the Board of Directors to provide financial assistance to the members of the producer company subject to the provisions made in articles and also subject to certain conditions laid down in 581ZK(b). But any loan or advance to any director or his relative shall be granted only after the approval by the members in general meeting. (Proviso to Section 581ZK).

In view of the above, the directors must convene the general meeting and get the approval of the members before granting the proposed loan of Rs.10,000 to X, a director of the company (According to Section 581C(5) a producer company is a private limited company and there is no limit to the number of its members. Hence, Section 295 is not applicable to a producer company).

Donation to a Political Party: Producer company shall not make directly or indirectly to any political party or for any political purpose to any person any contribution or subscription or make available any facilities including personnel or material (Second proviso to Section 581ZK). As the donation to a political party is prohibited, the company cannot donate ₹.10,000 to a political party.

Option to inter-State cooperative societies to become producer companies (Section 581J)

Question 2

- (i) *The existing Inter-state Cooperative Society seeks your advice regarding the papers to be submitted to the Registrar of Companies for its registration as a Producer Company under the provisions of the Companies Act, 1956. You are required to prepare a list of such papers.*
- (ii) *A group of individuals eligible to form a Producer Company within the meaning of the Companies Act, 1956 has entrusted you with the job of preparing the Memorandum of Association of the proposed Producer Company. You are required to state the matters, which are required to be included in such Memorandum of Association.*

(November 2005)

Answer

- (i) As per Section 581J of the Companies Act, 1956, any Inter-State Co-operative Society with objects not confined to one State may make an application to the Registrar of Companies for registration as Producer Company.

The application for registration as a producer Company is to be submitted along with the following:

- (a) a copy of the special resolution, of not less than two-third of total members of Inter-State Co-operative Society, for its incorporation as a Producer Company under the Companies Act:
- (b) a statement showing:
 - (i) Names and addresses or the occupation of the directors and Chief Executive, if any, by whatever name called, of such inter-State Co-operative Society, and
 - (ii) list of members of such Inter-State Co-operative Society;

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- (c) a statement indicating that the Inter-State Co-operative Society is engaged in any one or more of the objects specified in Section 581B of the Companies Act, 1956;
 - (d) a declaration by two or more directors of the Inter-state co-operative society certifying that particulars given in the above statements are correct.
- (ii) As per Section 581F of the Companies Act, 1956, the Memorandum of Association of a Producer Company has to state the following:
 - (a) the name of the company with "Producer Company Limited" as the last words of the name of such Company;
 - (b) the State in which the registered office of the Producer Company is to situate;
 - (c) the main objects of the Producer Company confirming to the objects specified in Section 581B of the Companies Act, 1956;
 - (d) the names and addresses of the persons who have subscribed to the memorandum of Association;
 - (e) the amount of share capital with which the Producer Company is to be registered and division thereof into shares of a fixed amount;
 - (f) the names, addresses and occupations of the subscribers being producers, who shall act as the first directors in accordance with section 581J(2) of the Companies Act, 1956;
 - (g) that the liability of its members is limited;
 - (h) opposite to the subscriber's name the number of shares each subscriber takes (Each subscriber must take at least one share);
 - (i) in case the objects of the Producer Company are not confined to one State, the States to whose territories the objects extend.

Number of Directors (Section 581O)

Question 3

- (i) *An Interstate Cooperative Society has been incorporated on 1st May, 2004 as a Producer Company under the provisions of the Companies Act, 1956. Give your comments on its proposal to have 18 directors on its Board after incorporation as a Producer Company.*
- (ii) *A Producer Company wants to issue bonus shares. You are required to state the relevant provisions of the Companies Act, 1956 in this regard.*
- (iii) *What are the modes of investment, from and out of its general reserves, available to a Producer Company formed and registered under Section 581C of the Companies Act, 1956?*
(November, 2004)

Answer

- (i) As per provisions of section 581-O of the Companies Act, 1956, any Producer Company can not have more than fifteen directors. However, by way of a proviso, the said section further provides that in the case of an inter-State co-operative society which is incorporated as a Producer Company, may have more than fifteen directors for a period of one year from the date of its incorporation as a Producer Company.

In view of the above provisions of the Companies Act, 1956 the proposal to have 18 directors by the Producer Company after its incorporation as such, is a valid proposition, but since it is incorporated on 1st May, 2004, it can have more than 15 directors for one year only from the date of its incorporation

- (ii) As per provisions of section 581ZJ of the Companies act 1956, any Producer Company may, upon recommendation of the Board and passing of resolution in the general meeting, issue bonus shares by capitalisation of amounts from general reserves referred to in section 581ZI in proportion to the shares held by the Members on the date of the issue of such shares.
- (iii) As per Producer Companies (General Reserves) Rules. 2003 issued by the Department of Company Affairs, Ministry of Finance, Government of India on 7th August, 2003 a producer company formed and registered under section 581C of the Companies Act, 1956, shall make investments from and out of its general reserves in the following manner, namely:-
- (a) in approved securities, fixed deposits, units and bonds issued by the Central or State Governments or cooperative societies or scheduled bank; or
 - (b) in a co-operative bank, state co-operative bank, co-operative land development bank or central co-operative bank; or
 - (c) with any other scheduled bank; or
 - (d) in any of the securities specified in section 20 of the Indian Trusts Act, 1882; or
 - (e) in the shares or securities of any other multi-state co-operative society or any co-operative society; or
 - (f) in the shares, securities or assets of a public financial institutions specified under section 4A of the Companies Act, 1956.

Donation or subscription to Producer Companies (Section 581 ZH)

Question 4

- (i) *A two year old Producer Company registered under Section 581C of the Companies Act, 1956 wants to donate some amount. The Chief Executive of the Producer Company has approached you to advise him as to how and for what purposes the donation can be made by such company. Also state the monetary restrictions, if any, laid down in the Companies Act, 1956 on making donations by a Producer Company.*

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You are informed that as per the Profit & Loss account of the Producer Company for its last accounting year, net profit was Rs.20.00 lacs.

- (ii) *Is it obligatory for every producer company to appoint a whole time secretary under the provisions of the Companies Act, 1956?* **(May, 2005)**

Answer

- (i) As per provisions of section 581 ZH of the Companies Act, 1956, a Producer Company may, by special resolution, make donation or subscription to any institution or individual for the following purposes:-

- (a) For promoting the social and economic welfare of Producer Members or Producers or general public; or
- (b) For promoting the mutual assistance principles.

Thus as per the above stated provisions of the Companies Act, 1956, a Producer Company may make a donation by passing a special resolution and for the above mentioned purposes.

The 1st Proviso to the said section 581ZH lays down the monetary limit for making the donation by a Producer Company. According to the said proviso the aggregate amount of all such donation and subscription in any financial year shall not exceed three per cent of the net profit of the Producer Company in the financial year immediately preceding the financial year in which the donation or subscription was made.

Since the net profit of the Producer Company as per its last profit & loss account was Rs.20.00 lacs, it can make a total donation of Rs.60,000/- in this year being three percent thereof.

- (ii) Under section 581X of the Companies Act, 1956 every Producer Company having an average turnover exceeding Rs.5 crores in each of three consecutive financial years shall have a whole time secretary who is a member of ICSI.

Incorporation of Producer Companies and other matters (Section 581B to 581N)

Option to inter-State co-operative societies to become Producer Companies (Section 581J)

Question 5

The Executive Committee of an Inter-state Co-operative society decides to convert the society into a 'Producer Company' under the provisions of the Companies Act, 1956. You being a practicing Chartered Accountant are approached by the society for advice. Advise the society on the following matters:

- (i) *The steps to be taken for conversion of the society into a 'Producer Company'.*
- (ii) *Manner in which voting rights of members of Producer company after conversion may be exercised.* **(May 2006)**

Answer

Conversion of inter state cooperative society into producer company steps to be taken and manner in which voting rights of members after conversion to be exercised. [Section 581J and 581D The Companies (Amendment) Act, 2002.]

As a practicing Chartered Accountant the following advise can be given to the inter-state society which wants to get converted into a 'Producer company' under the provisions of Companies (Amendment) Act, 2002.

1. Steps to be taken for conversion (Section 581J):

Any inter-state cooperative society having objects for multiplicity for states may make an application to the Registrar for registration as producer company. Such application should be accompanied by –

- (a) A copy of the special resolution, of not less than 2/3rd of total member of Inter-State Cooperative Society, for its incorporation as a producer company.
- (b) A Statement showing : (i) names and address or the occupation of the directors and Chief Executive, if any, by whatever name called, of such inter-state cooperative society; and (ii) list of members of such inter-state cooperative society.
- (c) A statement indicating that the inter-state cooperative society is engaged in any one or more of the objects specified in Section 581B.
- (d) A declaration by two or more directors of the inter-state cooperative society certifying that particulars given in clauses (a) to (c) given above are correct.

The word "Producer Company Ltd." should form part of its name to show its identity. On compliance with the requirements of the Act, the Registrar shall, within a period of 30 days of the receipt of application, certify under his hand that the society applying for registration is registered and thereby incorporated as a producer company.

Upon registration as a producer company, the Registrar of Companies who registers the company is required to intimate the Registrar with whom the erstwhile inter-State cooperative society was earlier registered for appropriate deletion of the society from its register.

2. Manner in which voting rights of members can be exercised (Section 581Z):

Section 581Z of the Companies Act, 1956 states that subject to the provisions of sub-sections (1) and (3) of Section 581D, every member shall have one vote and in the case of equality of votes, the chairman or the person presiding shall have a casting vote except in the case of election of the chairman. As regards the voting rights it may be noted that:

1. Where individual is a member of the producer company, he has one vote irrespective of the size of his holding.

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2. Where both individuals and producer institutions are members – single vote for every member.
3. Where membership is confined to producer institutions only, in the first year of registration of the company, the voting rights shall be based on the size of the shareholding of the member institution and in the following years it will be based on participation by the respective institutions in the business of the producer company in the previous year (as may be specified in the Articles),
4. A producer company, may, if authorized by the Articles, restrict the voting rights to active members of the producer company, and
5. Casting vote can be cast by the presiding member (Chairman) in case of equality of votes on any resolution (except for election of the Chairman).

Appointment of Directors (Section 581P)

Question 6

Mr. Z an expert in modern agriculture practices is willing to lend his services as a director of M/s. Lord Krishna Cotton Producer Company Ltd. registered under Section 581C of the Companies Act, 1956. Advise Mr. Z as to how he can be appointed as a director including (1) The total number of directors that can be appointed (2) The tenure of the directors (3) The time limit within which the appointment should be made (4) the co-option of directors and (5) the voting powers of such co-opted directors **(November 2007)**

Answer

According to Section 581P of the Companies Act, 1956 the members who sign the memorandum and the articles and designated as first directors and shall given the affairs of the company until the directors are appointed at the Annual General Meeting. According to Section 581-0 every producer company shall have at least five and not more than fifteen directors. The election of directors shall be conducted within 90 days from the date of registration of the producer company. In the case of Inter-state co-operative society the election shall be held within a period of 360 days. The period of office of director shall be not less than one year and not exceeding 5 years as may be specified in the articles. The directors are normally elected and appointed by the members in the Annual General Meeting. The Board may also co-opt one or more expert directors as an additional directors. Such directors cannot exceed $\frac{1}{5}$ th of the total number of directors. The expert directors shall not have the right to vote in the election of Chairman but shall be eligible to be elected as Chairman if it is provided by the articles. The maximum period for which such experts are appointed as directors will be as provided in the articles of association and it cannot exceed 5 years. Thus Mr. Z can be appointed as expert director but he will not have any voting right in the election of chairman of the Board of Directors. Him tenure of office can be between one to five years.

Question 7

- (i) *An inter-state co-operative society has been incorporated on 1st May, 2008 as a Producer Company under the provisions of the Companies Act, 1956. Give your comments on its proposal to have 18 directors on its Board after incorporation as a Producer Company.*
- (ii) *Mr. Zameen, a member of a Producer Company, wants to transfer his shares. You are required to state as to how he can transfer his shares under the provisions of the Companies Act, 1956.*
- (iii) *A Producer Company wants to issue bonus shares. You are required to state the relevant provisions of the Companies Act, 1956 in this regard.*
- (iv) *What are the modes of investment, from and out of its general reserves, available to a Producer Company formed and registered under Section 581C of the Companies Act, 1956?*
(May 2008)

Answer

- (i) As per provisions of Section 581-O of the Companies Act, 1956, any producer Company can not have more than fifteen directors. However, by way of a proviso, the said section further provides that in the case of an inter-state cooperative society which is incorporated as a Producer Company, may have more than fifteen directors for a period of one year from the date of its incorporation as a Producer Company.

In view of the above provisions of the Companies Act, 1956 the proposal to have 18 directors by the Producer Company after its incorporation as such, is a valid proposition, but since it is incorporated on 1st May, 2008, it can have more than 15 directors for one year only from the date of its incorporation.
- (ii) According to the provisions of Section 581ZD(1) and (2) of the Companies Act, 1956, the shares of a member of a Producer Company shall not be transferable but a member of a Producer Company may after obtaining the previous approval of the Board, transfer the whole or part of his shares along with any special rights, to an active member at par value.

Based on the above provisions relating to the transfer of shares of a member in a Producer Company, Mr. Zameen has to obtain prior approval of the Board and then transfer his shares to an active member of the Producer Company at par value.
- (iii) As per provisions of Section 581ZJ of the Companies Act, 1956, any Producer Company may, upon recommendation of the Board and passing of resolution in the general meeting, issue bonus shares by capitalization of amounts from general reserves referred to in Section 581ZI in proportion to the shares held by the Members on the date of the issue of such shares.
- (iv) As per Producer Companies (General Reserves) Rules, 2003 issued by the Department of Company Affairs, Ministry of Finance, Government of India on 7th August, 2003, a

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producer company formed and registered under Section 581C of the Companies Act, 1956, shall make investments from and out of its general reserves in the following manner namely:

- (a) in approved securities, fixed deposits, units and bonds issued by the Central or State governments of cooperative societies or scheduled banks; or
- (b) in a co-operative bank, State co-operative Bank, co-operative land development bank or Central co-operative bank; or
- (c) with any other schedule bank; or
- (d) in any of the securities specified in Section 20 of the Indian Trusts Act, 1882; or
- (e) in the shares or securities of any other multi-State Co-operative society or any co-operative society; or
- (f) in the shares, securities or assets of a public financial institutions specified under Section 4A of the Companies Act, 1956 specified.

Further, Section 581ZL of the Act provides that the general reserves of any producer company shall be invested to secure the highest returns available from approved securities. A producer company may, for promotion of its objectives acquire the shares of another producer company. Again a producer company, either by itself or together with its subsidiaries may invest in the shares of any other company, other than a producer company for an amount not exceeding thirty per cent of the aggregate of its paid up capital and free reserves. Provided that a producer company may, by special resolution passed in its general meeting and with prior approval of the Central Government, invest in excess of the limits specified in the section. All investments by a producer company may be made if such investments are consistent with the objects of the producer company.

Question 8

A Producer Company wants to issue bonus shares. You are required to state the relevant provisions of the Companies Act, 1956 in this regard **(CA Final, New Course, May 2009)**

Answer

As per provisions of Section 581ZJ of the Companies Act, 1956, any Producer Company may, upon recommendation of the Board and passing of resolution in the general meeting, issue bonus shares by capitalization of amounts from general reserves referred to in Section 581ZI in proportion to the shares held by the Members on the date of the issue of such shares.

Question 9

A Producer Company has received applications from Mr.Ramanathan, a Director of the Company, and Mr.Prem, a member of the Company, for grant of loan of Rs.2,00,000 and Rs.25,000 respectively. Discuss the relevant provision of the Companies Act, 1956 as to how the applications for grant of loan will be disposed of by the Company. **(November 2009)**

Answer

Under Section 581ZK of the Companies Act, 1956, the Board of the Producer Company may, subject to the provision in the Articles of Association, provide financial assistance by way of loan and advances against such security as may be specified in its Articles of Association to any member repayable within a period exceeding three months but not exceeding seven years from the date of disbursement of such loan or advances. In the instant case, member has applied for loan of Rs.25,000. The period is not specified in the question. The Company may grant the member a loan of Rs.25,000 against such security and at such rate of interest as may be specified in the Articles. However, in the case of a director, loan of Rs.2 lakh can be granted only after its approval by the members in general meeting.

Question 10

A producer company was incorporated on 1st September, 2009. At present the paid-up share capital of the company is ₹ 10 lakhs consisting of 1,00,000 equity shares of ₹ 10 each fully paid-up held by 200 individuals and 20 producers institutions. You are required to answer the following with reference to the provisions of the Companies Act, 1956:-

- (i) *What is the time limit for holding the First Annual General Meeting and the subsequent Annual General Meetings?*
- (ii) *What is the Quorum for the Annual General Meeting?*
- (iii) *State the manner in which the voting rights of the members are determined.*
- (iv) *Is it possible to remove a member?* **(November 2010)**

Answer

Producer Companies

Annual General Meeting – The first annual general meeting of a producer company shall be held within 90 days of incorporation i.e. on or before 29th November, 2009 in this case (Sec. 581 ZA(2)). In the case of subsequent AGMs gap between two AGMs must not be more than 15 months. Registrar of Companies may extend the time for holding any AGM other than the first AGM by a period not exceeding 3 months for any special reason (581ZA(i))

Quorum Unless the articles of association of the producer company provide for a larger number, 1/4th of the total number of members of the producer company shall be the quorum for its annual general meeting. In this case the company has got 220 members. Hence the quorum is 55 (Sec. 581ZA(8))

Voting rights of members: It depends on the type of membership. Where the membership consists of individuals and producer institutions, (as in this case) voting rights should be computed on the basis of a single vote for every member (Section 581D(i))

Removal of member: No person, who has any business interest which is in conflict with business of the producer company, shall become a member of that company (Section 581D(4)). A person who has become a member of the producer company acquires any

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business interest which is on conflict with the business of the producer company, shall cease to be a member of that company and be removed as a member in accordance with the articles (Sec. 581D(5)).

Question 11

Under provisions of Companies' Act, 1956, relating to producer company, examine whether the office of director of such company shall fall vacant in the following circumstances:

- (i) *X a Director of ABC Ltd., a producer company has made a default in payment of loan taken from a company and default continues for 60 days.*
- (ii) *Z a Director of the above company could not call the Annual General Meeting for the company due to some natural calamity occurred three days before the Schedule date.*

(CA Final, New course, November 2010)

Answer

Producer Company - Vacation of Office of a Director:

1. According to provisions of Companies Act, 1956, as contained in Section 581Q, if the producer company in which a director has made a default in repayment of any advances or loans taken from any company or institution or any other person and such default continues for 90 days, the office of such director shall become vacant. In the given case the default on the part of X, the director continues for less than 90 (i.e. *only* 60 days) days, the office of director shall not fall vacant.
2. The office of director of a producer company shall become Vacant if the Annual General Meeting or extraordinary general meeting of the producer company, in which he is a director, is not called in accordance with the provisions of this Act except due to natural calamity or such other reason. In the given case since the Annual General Meeting could not be held due to some natural calamity, the office of Z, the director shall not fall vacant. This is an exception.