Notes on Company Law

Points to Remember

1) All amendments corresponding with companies act 2013 are compiled in this summary
2) Many sections of new companies act 2013 is not notified by MCA (ministry of corporate affairs) so that sections are of old companies act 1956
3) Where ever as per companies act written that means old companies act 1956
4) For new companies act specifically mentioned …companies act 2013
5) All judgements of courts are compiled in this summary
6) All those older judgments based on old companies act 1956 which contradicts the new companies act 2013 …are not taken into consideration
7) **Comparative study of old companies act 1956 and new companies act 2013 is given**

Concept

Question1) Explain the Advantages and Disadvantages of Incorporation of a Company. (L)?

Introduction

A company, in common parlance, means a group of persons associated together for the attainment of a common end, social or economic. It has "no strictly technical or legal meaning."

According to **sec. 3 (1) (ii) of the Companies Act, 1956** a company means a company formed and registered under the Companies Act, 1956 or any of the preceding Acts. Thus, a Company comes into existence only by registration under the Act, which can be termed as incorporation.

Acording to sec 2(20) of companies act 2013 , "company" means a company incorporated under this Act or under any previous company law;

Advantages of incorporation

Incorporation offers certain advantages to a company as compared with all other kinds of business organizations. They are

1) ***Independent corporate existence***- the outstanding feature of a company is its independent corporate existence. By registration under the Companies Act, a company becomes vested with corporate personality, which is independent of, and distinct from its members. A company is a legal person. The decision of the House of Lords in ***Salomon v. Salomon & Co. Ltd. (1897 AC 22)*** is an authority on this principle:

One S incorporated a company to take over his personal business of manufacturing shoes and boots. The seven subscribers to the memorandum were all his family members, each taking only one share. The Board of Directors composed of S as managing director and his four sons. The business was transferred to the company at 40,000 pounds. S took 20,000 shares of 1 pound each n debentures worth 10,000 pounds. Within a year the company came to be wound up and the state if affairs was like this: Assets- 6,000 pounds; Liabilities- Debenture creditors-10,000 pounds, Unsecured creditors- 7,000 pounds.

It was argued on behalf of the unsecured creditors that, though the co was incorporated, it never had an independent existence. It was S himself trading under another name, but the House of Lords held Salomon & Co. Ltd. must be regarded as a separate person from S.

2) ***Limited liability***- limitation of liability is another major advantage of incorporation. The company, being a separate entity, leading its own business life, the members are not liable for its debts. The liability of members is limited by shares; each member is bound to pay the nominal value of shares held by them and his liability ends there.

3) ***Perpetual succession***- An incorporated company never dies. Members may come and go, but the company will go on forever. During the war all the members of a private company, while in general meeting, were killed by a bomb. But the company survived, not even a hydrogen bomb could have destroyed it ***(K/9 Meat Supplies (Guildford) Ltd., Re, 1966 (3) All E.R. 320)***.

4) ***Common seal***- Since a company has no physical existence, it must act through its agents and all such contracts entered into by such agents must be under the seal of the company. The common seal acts as the official seal of the company.

5) ***Transferable shares***- when joint stock companies were established the great object was that the shares should be capable of being easily transferred. Sec 82 (**as per companies act 2013 section is 44**)gives expression to this principle by providing that "the shares or other interest of any member shall be movable property, transferable in the manner provided by the articles of the company."

6) ***Separate property***- The property of an incorporated company is vested in the corporate body. The company is capable of holding and enjoying property in its own name. No members, not even all the members, can claim ownership of any asset of company's assets.

7) ***Capacity for suits***- A company can sue and be sued in its own name. The names of managerial members need not be impleaded.

8) ***Professional management***- A company is capable of attracting professional managers. It is due to the fact that being attached to the management of the company gives them the status of business or executive class.

Disadvantages of incorporation

1) ***Lifting of corporate veil***- though for all purposes of law a company is regarded as a separate entity it is sometimes necessary to look at the persons behind the corporate veil.

a) ***Determination of character***- The House of Lords in ***Daimler Co Ltd. v. Continental Tyre and Rubber Co.***, held that a company though registered in England would assume an enemy character if the persons in de facto control of the company are residents of an enemy country.

b) ***For benefit of revenue***- The separate existence of a company may be disregarded when the only purpose for which it appears to have been formed is the evasion of taxes. – ***Sir Dinshaw Maneckjee, Re / Commissioner of Income Tax v. Meenakshi Mills Ltd***.

c) ***Fraud or improper conduct***- In ***Gilford Motor Co v. Horne***, a company was restrained from acting when its principal shareholder was bound by a restraint covenant and had incorporated a company only to escape the restraint.

d) ***Agency or Trust or Government company***- The separate existence of a company may be ignored when it is being used as an agent or trustee. In ***State of UP v. Renusagar Power Co***, it was held that a power generating unit created by a company for its exclusive supply was not regarded as a separate entity for the purpose of excise.

e) ***Under statutory provisions***- The Act sometimes imposes personal liability on persons behind the veil in some instances like, where business is carried on beyond six months after the knowledge that the membership of company has gone below statutory minimum(sec 45), when contract is made by misdescribing the name of the company(sec 147), when business is carried on only to defraud creditors(sec 542).

Under New companies Act 2013--- Statutory provisions are—

1)for section 45 no new section is notified

2)for section 147 new section is 12 i.e. **Registered office of company---sub section** (*8*) If any default is made in complying with the requirements of this section, the company and every officer who is in default shall be liable to a penalty of one thousand rupees for every day during which the default continues but not exceeding one lakh rupees.

3)for section 542 ..new section is 339 ….**Liability for Fraudulent conduct of business— sub section** (*1*) If in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal, on the application of the Official Liquidator, or the Company Liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare that any person, who is or has been a director, manager, or officer of the company or any persons who were knowingly parties to the carrying on of the business in the manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Tribunal may direct:

Provided that on the hearing of an application under this sub-section, the Official Liquidator or the Company Liquidator, as the case may be, may himself give evidence or call witnesses.

(*2*) Where the Tribunal makes any such declaration, it may give such further directions as it thinks proper for the purpose of giving effect to that declaration and, in particular,—

(*a*) make provision for making the liability of any such person under the declaration a charge on any debt or obligation due from the company to him, or on any mortgage or charge or any interest in any mortgage or charge on any assets of the company held by or vested in him, or any person on his behalf, or any person claiming as assignee from or through the person liable or any person acting on his behalf;

(*b*) make such further order as may be necessary for the purpose of enforcing any charge imposed under this sub-section.

2) *Formality and expense-* Incorporation is a very expensive affair. It requires a number of formalities to be complied with both as to the formation and administration of affairs.

3) *Company not a citizen-* In ***State Trading Corporation of India v. CTO***, the SC held that a company though a legal person is not a citizen neither under the provisions of the Constitution nor under the Citizenship Act.

Q2)***Distinction between Company and Partnership.(M)?***

Ans-- The principal points of distinction between a company and a partnership are:

1) ***Legal status-*** A company is a distinct legal person. A partnership firm is not distinct from the several members who compose it.
2) ***Property-*** In partnership, the property of the firm is the property of the members comprising it. In a company, it belongs to the company and not to the members comprising it.
3) ***Mode of creation-*** A company comes into existence after registration under the Companies Act, 1956, while registration is not compulsory in case of a partnership firm.

4) ***Agents-*** Partners are the agents of the firm, but members of a firm are not its agents.

5) ***Contracts-*** A partner cannot contract with his firm, whereas a member of a company can.

6) ***Transferability of shares-*** A partner cannot transfer his share and make the transferee a member of the firm without the consent of other partners whereas a company's share can easily be transferred unless the Articles provide otherwise and the transferee becomes a member of the firm.

7) ***Liability-*** A partner's share is always unlimited whereas that of a shareholder may be limited either by shares or a guarantee**.(although limited liability partnership act is passed where in partnership concern is also limited)**

8) ***Perpetual succession-*** The death or insolvency of a shareholder or all of them does not affect the life of the company, whereas the death or insolvency of a partner dissolves the firm, unless otherwise provided.

9) ***Audit-*** A company is legally required to have its accounts audited annually by a chartered accountant, whereas the accounts of the partnership are audited at the discretion of its members**.(but firms have to conduct tax audit if turnover exceeds 1 crore)**

10) ***Number of members-*** The minimum number of partners in a firm is 2 and maximum is 20 in any business and 10 in banking business. In case of a private company the minimum number of members are 2 and maximum is 50. In case of a public company the min num of members are 7 and no max limit**.(Now even one person can form company as per companies act 2013)sec2 subsection** (*62*) "One Person Company" means a company which has only one person as a member;

11) ***Dissolution-*** a company can only be dissolved as laid down by law. A partnership firm can be dissolved at any time by an agreement.

Q3) ***When can Corporate Veil of a Company be Lifted?(L)***

Ans-- For all purposes of law a company is regarded as a separate entity from its shareholders. But sometimes it is sometimes necessary to look at the persons behind the corporate veil. The separate entity of the company is disregarded and the schemes and intentions of the persons behind are exposed to full view which is known as lifting or piercing the corporate veil. This is usually done in the following cases

1) ***<u>Determination of character</u>***- In ***Daimler Co Ltd. v. Continental Tyre and Rubber Co.***, a company was incorporated in England for the purpose of selling tyres manufactured in Germany by a German company. The German company held the bulk of the shares in the English company and all the directors of the company were Germans, resident in Germany. During the First World War the English company commenced an action to recover a trade debt. And the question was whether the company had become an enemy company and should therefore be barred from maintaining the action.

The House of Lords held that though the company was registered in England it is not a natural person with a mind or conscience. It is neither loyal nor disloyal; neither friend nor enemy. But it would assume an enemy character if the persons in de facto control of the company are residents of an enemy country.

2) ***<u>For benefit of revenue</u>***- The separate existence of a company may be disregarded when the only purpose for which it appears to have been formed is the evasion of taxes. In ***Sir DinshawManeckjee, Re***, the assessee was a wealthy man enjoying large dividend and interest income. He formed four private companies and agreed with each to hold a block of investment as an agent for it. Income received was credited in the company accounts but company handed the amount to him as pretended loan. Thus he divided his income in four parts to reduce his tax liability. The Court disregarded corporate entity as it was formed only to evade taxes.

In ***Bacha F Guzdar v. CIT, Bombay***, the SC rejected the plea of the plaintiff, a member of a tea company, who claimed that the dividend held by her in respect of her shares should be treated as agricultural income(as it was exempted from tax) and not income from manufacture and sale of tea.

3) ***<u>Fraud or improper conduct</u>***- In ***Gilford Motor Co v. Horne***, H was appointed at the managing director of the plaintiff company on the condition that he shall not solicit the customers of the company. He formed a new company which undertook solicitation of plaintiff's customers. The company was restrained by the Court.

4) ***<u>Agency or Trust or Government company</u>***- The separate existence of a company may be ignored when it is being used as an agent or trustee. In ***State of UP v. Renusagar Power Co***, it was held that a power generating unit created by a company for its exclusive supply was not regarded as a separate entity for the purpose of excise.

In ***Re R.G.Films Ltd***., an American company produced film in India technically in the name of a British company, 90% of whose share was held by the President of the American company. Board of Trade refused to register the film as the English company acted merely as the agent of the American company.

5) ***To avoid welfare legislation***- where it was found that the sole purpose of formation of new company was to use it as a device to reduce the amount to be paid by way of bonus to workmen, the SC pierced its corporate veil. –***The Workmen Employed in Associated Rubber Industries Ltd. v. The Associated Rubber Industries Ltd, Bhavnagar***.

6) ***Under statutory provisions***- The Act sometimes imposes personal liability on persons behind the veil in some instances like, where business is carried on beyond six months after the knowledge that the membership of company has gone below statutory minimum(sec 45)- ***Madanlal v. Himatlal***, when contract is made by misdescribing the name of the company(sec 147), when business is carried on only to defraud creditors(sec 542).

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sub section (*1*) If in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal, on the application of the Official Liquidator, or the Company Liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare that any person, who is or has been a director, manager, or officer of the company or any persons who were knowingly parties to the carrying on of the business in the manner aforesaid shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Tribunal may direct:
Provided that on the hearing of an application under this sub-section, the Official Liquidator or the Company Liquidator, as the case may be, may himself give evidence or call witnesses.
(*2*) Where the Tribunal makes any such declaration, it may give such further directions as it thinks proper for the purpose of giving effect to that declaration and, in particular,—
(*a*) make provision for making the liability of any such person under the declaration a charge on any debt or obligation due from the company to him, or on any mortgage or charge or any interest in any mortgage or charge on any assets of the company held by or vested in him, or any person on his behalf, or any person claiming as assignee from or through the person liable or any person acting on his behalf;
(*b*) make such further order as may be necessary for the purpose of enforcing any charge imposed under this sub-section.

Q4) ***Write a Note on Pre-incorporation Contracts.(M)?***

Ans-- Sometimes contracts are made on behalf of a company even before it is duly incorporated. These are called as pre-incorporation contracts. Two consenting parties are necessary to a contract, whereas a company before incorporation is a non-entity. Therefore, following are the effects of pre-incorporation contracts.

Company cannot be sued on pre-incorporation contracts- A company, when it comes into existence, cannot be sued on pre-incorporation contracts. In ***English and Colonial Produce Co, Re***, a solicitor on the request of promoters prepared a company's documents and spent time and money in getting it registered. But the company was not held to be bound to pay for those services and expenses.

Company cannot sue on pre-incorporation contracts- A company cannot by adoption or ratification obtain the benefit of a contract made on its behalf before the company came into existence. In ***Natal Land and Colonization Co v. Pauline Colliery Syndicate***, the promoters of a proposed company obtained an agreement from a landlord that he would grant lease of coal mining rights to the company. The company could not, after incorporation, enforce this contract.

Agents may incur personal liability- The agents who contract for a proposed company may sometimes incur personal liability. In ***Kelner v. Baxter***, the promoters of a projected hotel company purchased wine from the plaintiff on behalf of the company. The company came into being but, before paying the price went into liquidation. They were held personally liable to the plaintiff.

Ratification of a pre-incorporation contract

So far as the company is concerned it is neither bound by nor can have the benefit of a pre-incorporation contract. But this is subject to the provisions of the **Specific Relief Act, 1963.**

Section 15 of the Act provides that where the promoters of a company have made a contract before its incorporation for the purposes of the company, and if the contract is warranted by the terms of incorporation, the company may adopt and enforce it. In ***Vali Pattabhirama Rao v. Ramanuja Ginning and Rice Factory***, a promoter of a company acquired a leasehold interest for it. He held it for sometime for a partnership firm, converted the firm into a company which adopted the lease. The lessor was held bound to the company under the lease.

Section 19 of the Specific Relief Act provides that the other party can also enforce the contract if the company has adopted it after incorporation and the contract is within the terms of incorporation.

Q5)Is company a citizen?(S)

Ans-A company, though a legal person, is not a citizen. This has been the conclusion of a special bench of the Supreme Court in ***State Trading Corporation of India v. CTO (AIR 1963 SC 1811)***. The State Trading Corporation of India is incorporated as a private company under the Companies Act, 1956. All the shares are held by the President of India and two secretaries in their official capacities. The question was whether the corporation was a citizen. One of the contentions put forth on behalf of the corporation was that "if the corporate veil is pierced, one sees three persons who are admittedly the citizens of India", and, therefore, the corporation should also be regarded as a citizen.

But it was held that, "neither the provisions of the Constitution, Part II, nor of the Citizenship Act, either confer the right of citizenship on or recognize as citizen, any person other than a natural person. In striking words the Supreme Court observed,

"If all the members are citizens of India the company does not become a citizen of India any more than, if all are married the company would not be a married person."

A company can have the benefit of only such fundamental rights as guaranteed to every "person" whether a citizen or not. However, it has a nationality, domicile and residence.

The hardship caused by the above pronouncement was later modified by holding that a citizen shareholder may petition, proceeding on behalf of the company, against violation of his company's fundamental rights.

Q6)Explain the Procedure for Registration of a Company.(S)?

Ans-- Sec 33 of the Companies Act(**section 7 of Companies act 2013**) deals with registration of a company. To obtain registration an application has to be filed to the Registrar of Companies. The application must be accompanied by the following documents:

1) Memorandum of Association.

2) Articles of Association, if necessary.

3) A copy of the agreement, if any, which the company proposes to enter into with any individual for his appointment as the managing or the whole-time director or the manager.

4) A declaration that all the requirements of the Act have been complied with.

Articles are compulsory only for unlimited companies, companies limited by guarantee and private companies limited by shares(s 26). The declaration must be signed by an advocate of the SC, or of a HC, or an attorney or a pleader entitled to appear before a HC, or any proposed director, manager or secretary of the company or by a secretary or chartered accountant who is in whole time practice in India[s 33(2)].

Under **section 7** of companies act ----- **Incorporation of company**

(*1*) **There shall be filed with the Registrar within whose jurisdiction the registered office of a company is proposed to be situated, the following documents and information for registration, namely:—**

(*a*) the memorandum and articles of the company duly signed by all the subscribers to the memorandum in such manner as may be prescribed;

(*b*) a declaration in the prescribed form by an advocate, a chartered accountant, cost accountant or company secretary in practice, who is engaged in the formation of the company, and by a person named in the articles as a director, manager or secretary of the company, that all the requirements of this Act and the rules made thereunder in respect of registration and matters precedent or incidental thereto have been complied with;

(*c*) an affidavit from each of the subscribers to the memorandum and from persons named as the first directors, if any, in the articles that he is not convicted of any offence in connection with the promotion, formation or management of any company, or that he has not been found guilty of any fraud or misfeasance or of any breach of duty to any company under this Act or any previous company law during the preceding five years and that all the documents filed with the Registrar for registration of the company contain information that is correct and complete and true to the best of his knowledge and belief;

(*d*) the address for correspondence till its registered office is established;

(*e*) the particulars of name, including surname or family name, residential address, nationality and such other particulars of every subscriber to the memorandum along with proof of identity, as may be prescribed, and in the case of a subscriber being a body corporate, such particulars as may be prescribed;

(*f*) the particulars of the persons mentioned in the articles as the first directors of the company, their names, including surnames or family names, the Director Identification Number, residential address, nationality and such other particulars including proof of identity as may be prescribed; and

(*g*) the particulars of the interests of the persons mentioned in the articles as the first directors of the company in other firms or bodies corporate along with their consent to act as directors of the company in such form and manner as may be prescribed.

(*2*) The Registrar on the basis of documents and information filed under sub-section (*1*) shall register all the documents and information referred to in that subsection in the register and issue a certificate of incorporation in the prescribed form to the effect that the proposed company is incorporated under this Act.

(*3*) On and from the date mentioned in the certificate of incorporation issued under sub-section (*2*), the Registrar shall allot to the company a corporate identity number, which shall be a distinct identity for the company and which shall also be included in the certificate.
(*4*) The company shall maintain and preserve at its registered office copies of all documents and information as originally filed under sub-section (*1*) till its dissolution under this Act.
(*5*) If any person furnishes any false or incorrect particulars of any information or suppresses any material information, of which he is aware in any of the documents filed with the Registrar in relation to the registration of a company, he shall be liable for action under section 447.
(*6*) Without prejudice to the provisions of sub-section (*5*) where, at any time after the incorporation of a company, it is proved that the company has been got incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company, or by any fraudulent action, the promoters, the persons named as the first directors of the company and the persons making declaration under clause (*b*) of subsection (*1*) shall each be liable for action under section 447.
(*7*) Without prejudice to the provisions of sub-section (*6*), where a company has been got incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants,—
(*a*) pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or
(*b*) direct that liability of the members shall be unlimited; or
(*c*) direct removal of the name of the company from the register of companies; or
(*d*) pass an order for the winding up of the company; or
(*e*) pass such other orders as it may deem fit:
Provided that before making any order under this sub-section,—
(*i*) the company shall be given a reasonable opportunity of being heard in the matter; and
(*ii*) the Tribunal shall take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.

Section 12(**now section 3 of companies act 2013)**, which states the mode of forming an incorporated company, enables any seven persons (two for private company) to associate for any lawful purpose and to get themselves incorporated into a company with or without limited liability. They can do so by subscribing their names to a memorandum of association and by complying with other documents.

If the Registrar finds the documents to be satisfactory, he registers them and enters the name of the company in the Register of Companies and issues a certificate called the Certificate of Incorporation. Certificate of Incorporation brings the company into existence as a legal person. It is the conclusive evidence that all the requirements under the Act in respect of registration and matters precedent and incidental thereto have been complied with and that the association is a company authorized to be registered and duly registered under the Act.

Section 3 of companies act 2013-- **Formation of company---** (*1*) A company may be formed for any lawful purpose by—
(*a*) seven or more persons, where the company to be formed is to be a public company;
(*b*) two or more persons, where the company to be formed is to be a private company; or
(*c*) one person, where the company to be formed is to be One Person Company 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:

Provided that the memorandum of One Person Company shall indicate the name of the other person, with his prior written consent in the prescribed form, who shall, in the event of the subscriber's death or his incapacity to contract become the member of the company and the written consent of such person shall also be filed with the Registrar at the time of incorporation of the One Person Company along with its memorandum and articles:
Provided further that such other person may withdraw his consent in such manner as may be prescribed:
Provided also that the member of One Person Company may at any time change the name of such other person by giving notice in such manner as may be prescribed:
Provided also that it shall be the duty of the member of One Person Company to intimate the company the change, if any, in the name of the other person nominated by him by indicating in the memorandum or otherwise within such time and in such manner as may be prescribed, and the company shall intimate the Registrar any such change within such time and in such manner as may be prescribed:
Provided also that any such change in the name of the person shall not be deemed to be an alteration of the memorandum.
(*2*) A company formed under sub-section (*1*) may be either—
(*a*) a company limited by shares; or
(*b*) a company limited by guarantee; or
(*c*) an unlimited company.

*Q7) **Write a Note on Certificate of Incorporation (sec 34 and 35)(now section 9 of companies act 2013)(S)?***

Ans-- Certificate of Incorporation is the certificate issued by the Registrar of Companies ion registration of a company. It brings the company into existence as a legal person. It marks the birth of the company, and the date mentioned on it is conclusive, even if wrong.

Certificate of Incorporation is the conclusive evidence that all the requirements under the Act in respect of registration and matters precedent and incidental thereto have been complied with and that the association is a company authorized to be registered and duly registered under the Act(s 35). This is illustrated by the Privy Council in ***Moosa Goolam Ariff v. Ebrahim Goolam Ariff***, in which the memorandum of a company was signed by two adult members and by a guardian on behalf of the other five members, who were minors. The Registrar, however, registered the company. The plaintiff's contention that the Certificate of Incorporation should be declared void was rejected as the certificate is conclusive for all purposes.

However, the illegal objects of the company do not become legal by the issue of the certificate. The certificate is subject to judicial review where it happens to be issued to a company which on account of illegal objects should not have been registered. This is so because a company cannot be registered for illegal purposes.

Section 9 of companies act 2013 states--- **Effect of registration ----** From the date of incorporation mentioned in the certificate of incorporation, such subscribers to the memorandum and all other

persons, as may, from time to time, become members of the company, shall be a body corporate by the name contained in the memorandum, capable of exercising all the functions of an incorporated company under this Act and having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued, by the said name.
And section 35 of old act is omitted in new act. So same is to be written

Q9)Explain the Clauses of Memorandum of Association OR Explain the Importance of Memorandum of Association.(L)?

Ans--- Introduction

One of the essentials for the registration of a company is memorandum of association (sec 33)(**now section 7 of companies act 2013)(refer page 10 and 11 of notes).** It is the first step in the formation of a company. Its importance lies in the fact that it contains the fundamental clauses which have often been described as the conditions of the company's incorporation.

Memorandum of association is divided into 5 clauses:

1) Name clause
2) Registered office clause
3) Objects clause
4) Liability clause and
5) Capital clause

Name clause---The first clause states the name of the proposed company. The name of a corporation is the symbol of its personal existence. The name should not be, in the opinion of the Central Government, undesirable. Generally it is so when it is identical with or too nearly resembles the name of another company. If the company is with "limited liability" the last word of the name should be "limited" and in case of a private company "private limited". The Central Govt. may permit a company to drop the word limited from its name, if

a) If the company is formed for the promotion of arts, commerce, religion, science, charity or any other useful object.

b) The company is to apply its income in promoting its objects and prohibits the payment of dividend to its members.

The name of a company must be painted outside of every place where the company carries on business and printed on every business document and official letter of the company. Misdescription entails personal liability(s147**).(now section 12 of companies act 2013)**

<u>Registered office clause</u>---The second clause of the memorandum must specify the State in which the registered office of the company shall be situate (sec 146)(**now setion 12 of companies act**). Within 30 days of incorporation or commencement of business, whichever is earlier, the exact place where the registered office is to be located must be decided and sent to the Registrar for recording of the same.

<u>Objects clause</u>

The third clause states the objects of the proposed company. The objects clause s divided into two sub-clauses (sec 13)(**now section 4 of companies act 2013):**

a) *<u>Main objects clause</u>*: states the main objects to be pursued by the company and the objects incidental or ancillary to the main objects.

b) *<u>Other objects</u>*: states any other objects which are not included in the main objects clause.

The essence of this clause is that the investors must be informed of the objects of the company in which their money is going to be employed and the creditors must feel protected when they know the assets are being used for the authorized objects.

<u>Section 4 of companies act 2013--- Memorandum</u> -- (*1*) The memorandum of a company shall state—

(*a*) the **name of the company** with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company:

Provided that nothing in this clause shall apply to a company registered under section 8;

(*b*) the State in which the **registered office** of the company is to be situated;

(*c*) the objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof;

(*d*) the **liability of members** of the company, whether limited or unlimited, and also state,—

(*i*) in the 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; and

(*ii*) in the case of a company limited by guarantee, the amount up to which each member undertakes to contribute—

(*A*) to the assets of the company in the event of its being wound-up while he is a member or within one year after he ceases to be a member, for payment of the debts and liabilities of the company or of such debts and liabilities as may have been contracted before he ceases to be a member, as the case may be; and

(*B*) to the costs, charges and expenses of winding-up and for adjustment of the rights of the contributories among themselves;
(*e*) in the case of a company **having a share capital**,—
(*i*) the amount of share capital with which the company is to be registered and the division thereof into shares of a fixed amount and the number of shares which the subscribers to the memorandum agree to subscribe which shall not be less than one share; and
(*ii*) the number of shares each subscriber to the memorandum intends to take, indicated opposite his name;
(*f*) in the case **of One Person Company**, the name of the person who, in the event of death of the subscriber, shall become the member of the company.
(*2*) The name stated in the memorandum shall not—
(*a*) be identical with or resemble too nearly to the name of an existing company registered under this Act or any previous company law; or
(*b*) be such that its use by the company—
(*i*) will constitute an offence under any law for the time being in force; or
(*ii*) is undesirable in the opinion of the Central Government.
(*3*) Without prejudice to the provisions of sub-section (*2*), a company shall not be registered with a name which contains—
(*a*) any word or expression which is likely to give the impression that the company is in any way connected with, or having the patronage of, the Central Government, any State Government, or any local authority, corporation or body constituted by the Central Government or any State Government under any law for the time being in force; or
(*b*) such word or expression, as may be prescribed, unless the previous approval of the Central Government has been obtained for the use of any such word or expression.
(*4*) A person may make an application, in such form and manner and accompanied by such fee, as may be prescribed, to the Registrar for the reservation of a name set out in the application as—
(*a*) the name of the proposed company; or
(*b*) the name to which the company proposes to change its name.
(*5*) (*i*) Upon receipt of an application under sub-section (*4*), the Registrar may, on the basis of information and documents furnished along with the application, reserve the name for a period of sixty days from the date of the application.
(*ii*) Where after reservation of name under clause (*i*), it is found that name was applied by furnishing wrong or incorrect information, then,—
(*a*) if the company has not been incorporated, the reserved name shall be cancelled and the person making application under sub-section (*4*) shall be liable to a penalty which may extend to one lakh rupees;
(*b*) if the company has been incorporated, the Registrar may, after giving the company an opportunity of being heard—
(*i*) either direct the company to change its name within a period of three months, after passing an ordinary resolution;
(*ii*) take action for striking off the name of the company from the register of companies; or
(*iii*) make a petition for winding up of the company.
(*6*) The memorandum of a company shall be in respective forms specified in Tables A, B, C, D and E in Schedule I as may be applicable to such company.
(*7*) Any provision in the memorandum or articles, in the case of a company limited by guarantee and not having a share capital, purporting to give any person a right to participate in the divisible profits of the company otherwise than as a member, shall be void.

Liability clause---The fourth clause states the nature of liability the members incur. The clause will state whether the liability of the members shall be limited by shares or by guarantee or unlimited.

Capital clause---The last clause states the amount of capital with which the company is proposed to be registered and the kinds, number and value of shares into which the capital is to be divided.

After the Companies (Amendment) Act, 2000, the minimum paid up capital of a public company must be five lakh rupees or more and one lakh or more for a private company.

Q10)Explain the Procedure for Alteration of Memorandum of Association.(M)?

Ans-- ***Alteration of name (sec 21)(refer sec 4 of companies act 2013)***

A company may change its name at any time by passing a special resolution and with the prior approval of the Central Government. Where a company has been registered with a name which is undesirable, the same may be changed by an ordinary resolution and with the prior approval of the Central Government. In such a case the central government may also within 12 months of registration direct the company to rectify its name and the company must change the name within 3 months from the date of direction unless the time is extended. The new name would also require the prior approval of the Central Govt. The British Diabetic Society was compelled to change its name to something that would not impinge the goodwill of the British Diabetic Association ***(British Diabetic Association v. The Diabetic Society).***

When a company changes its name, the Registrar of Companies has to enter the new name in the register and a new certificate of incorporation must be issued with necessary alterations.

However, it should be noted that no approval will be required if the change consists merely addition or deletion of the word "private" consequent on the conversion of a public company into a private company or vice versa.

Effect of such change: The old name of the company will stand abolished and the new name will come into existence from the date of passing such resolution. However, it does not affect the rights and obligations of the company (sec 23).

Alteration of registered office clause (sec 17)

Shifting of registered office from one State to another is a complicated affair. For this purpose, sec 17 requires

a) A special resolution of the company.

b) The sanction of the Company Law Board.

The Board can confirm the alteration only if the shifting of the registered office from one state to another is necessary for any purposes detailed in sec 17(1).

Alteration of objects (sec 17)--A company may alter its objects with the passing of a special resolution. The confirmation of the Company Law Board is not required for this purpose. An alteration of the objects is allowed only for the purposes mentioned in sec 17(1).

Registration of alteration (sec 18)-- In case of alteration of objects, a copy of the resolution should be filed with the Registrar of Companies within one month from the date of resolution. In the case of inter-state shifting of the registered office a certified copy of the Board's order and a printed copy of the altered memorandum must be filed with the Registrar within three months of the Board's order. Within one month the Registrar will certify the registration. Alteration takes effect when it is so registered.

As per companies act 2013---

Alteration of memorandum.(section 13)--- (*1*) Save as provided in section 61, a company may, by a special resolution and after complying with the procedure specified in this section, alter the provisions of its memorandum.

(*2*) Any change in the name of a company shall be subject to the provisions of subsections (*2*) and (*3*) of section 4 and shall not have effect except with the approval of the Central Government in writing:

Provided that no such approval shall be necessary where the only change in the name of the company is the deletion therefrom, or addition thereto, of the word "Private", consequent on the conversion of any one class of companies to another class in accordance with the provisions of this Act.
(*3*) When any change in the name of a company is made under sub-section (*2*), the Registrar shall enter the new name in the register of companies in place of the old name and issue a fresh certificate of incorporation with the new name and the change in the name shall be complete and effective only on the issue of such a certificate.
(*4*) The alteration of the memorandum relating to the place of the registered office from one State to another shall not have any effect unless it is approved by the Central Government on an application in such form and manner as may be prescribed.
(*5*) The Central Government shall dispose of the application under sub-section (*4*) within a period of sixty days and before passing its order may satisfy itself that the alteration has the consent of the creditors, debenture-holders and other persons concerned with the company or that the sufficient provision has been made by the company either for the due discharge of all its debts and obligations or that adequate security has been provided for such discharge.
(*6*) Save as provided in section 64, a company shall, in relation to any alteration of its memorandum, file with the Registrar—
(*a*) the special resolution passed by the company under sub-section (*1*);
(*b*) the approval of the Central Government under sub-section (*2*), if the alteration involves any change in the name of the company.
(*7*) Where an alteration of the memorandum results in the transfer of the registered office of a company from one State to another, a certified copy of the order of the Central Government approving the alteration shall be filed by the company with the Registrar of each of the States within such time and in such manner as may be prescribed, who

shall register the same, and the Registrar of the State where the registered office is being shifted to, shall issue a fresh certificate of incorporation indicating the alteration.
(*8*) A company, which has raised money from public through prospectus and still has any unutilised amount out of the money so raised, shall not change its objects for which it raised the money through prospectus unless a special resolution is passed by the company and—
(*i*) the details, as may be prescribed, in respect of such resolution shall also be published in the newspapers (one in English and one in vernacular language) which is in circulation at the place where the registered office of the company is situated and shall also be placed on the website of the company, if any, indicating therein the justification for such change;
(*ii*) the dissenting shareholders shall be given an opportunity to exit by the promoters and shareholders having control in accordance with regulations to be specified by the Securities and Exchange Board.
(*9*) The Registrar shall register any alteration of the memorandum with respect to the objects of the company and certify the registration within a period of thirty days from the date of filing of the special resolution in accordance with clause (*a*) of sub-section (*6*) of this section.
(*10*) No alteration made under this section shall have any effect until it has been registered in accordance with the provisions of this section.
(*11*) Any alteration of the memorandum, in the case of a company limited by guarantee and not having a share capital, purporting to give any person a right to participate in the divisible profits of the company otherwise than as a member, shall be void.

Rectification of name of company.(Section 16 of companies act 2013)-- (*1*) If, through inadvertence or otherwise, a company on its first registration or on its registration by a new name, is registered by a name which,—
(*a*) in the opinion of the Central Government, is identical with or too nearly resembles the name by which a company in existence had been previously registered, whether under this Act or any previous company law, it may direct the company to change its name and the company shall change its name or new name, as the case may be, within a period of three months from the issue of such direction, after adopting an ordinary resolution for the purpose;
(*b*) on an application by a registered proprietor of a trade mark that the name is identical with or too nearly resembles to a registered trade mark of such proprietor under the Trade Marks Act, 1999, made to the Central Government within three years of incorporation or registration or change of name of the company, whether under this Act or any previous company law, in the opinion of the Central Government, is identical with or too nearly resembles to an existing trade mark, it may direct the company to change its name and the company shall change its name or new name, as the case may be, within a period of six months from the issue of such direction, after adopting an ordinary resolution for the purpose.
(*2*) Where a company changes its name or obtains a new name under sub-section (*1*), it shall within a period of fifteen days from the date of such change, give notice of the change to the Registrar along with the order of the Central Government, who shall carry out necessary changes in the certificate of incorporation and the memorandum.
(*3*) If a company makes default in complying with any direction given under sub-section (*1*), the company shall be punishable with fine of one thousand rupees for every day during which the default continues and every officer who is in default shall be punishable with fine which shall not be less than five thousand rupees but which may extend to one lakh rupees.

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Q11)Articles of Association.(L)?

Ans-- Introduction

Articles of Association is the second important document, which in case of some companies, has to be registered along with the memorandum. As per sec 26(**now section 5 of companies act 2013)**, companies which must have articles are:

1) Unlimited companies;

2) Companies limited by guarantee;

3) Private companies limited by shares.

This document contains rules, regulations and bye-laws for the general administration of the company. Schedule I of the Act sets out tables of model forms of articles for different companies.

Contents--A of A may prescribe such regulations for the company as the subscribers to the memorandum deem expedient. The Act gives the subscribers a free hand. Any stipulations as to the relation between the company and its members or members inter se may be inserted in the articles. But everything stated therein is subject to the Companies Act. Usually, articles contain provisions relating to the following matters:

1) Share capital, rights of shareholders, share certificates, payment of commission.

2) Lien on shares.

3) Call on shares.

4) Transfer of shares.

5) Transmission of shares.

6) Forfeiture of shares.

7) Conversion of shares into stock.

8) Share warrants.

9) Alteration of capital.

10) General meetings and proceedings there at.

11) Voting rights of members, voting and poll, proxies.

12) Directors, their appointment, remuneration, qualifications, powers and proceedings of Board of Directors.

13) Manager.

14) Secretary.

15) Dividends and reserves.

16) Accounts, audit and borrowing power.

17) Capitalization of profits.

18) Winding up.

Under companies act 2013 --Section 5 – Articles—sub section (*1*) The articles of a company shall contain the regulations for management of the company.
(*2*) The articles shall also contain such matters, as may be prescribed:
Provided that nothing prescribed in this sub-section shall be deemed to prevent a company from including such additional matters in its articles as may be considered necessary for its management.
(*3*) The articles may contain provisions for entrenchment to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.
(*4*) The provisions for entrenchment referred to in sub-section (*3*) 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 a special resolution in the case of a public company.
(*5*) Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed.
(*6*) The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company
(*7*) A company may adopt all or any of the regulations contained in the model articles applicable to such company.
(*8*) In case of any company, which is registered after the commencement of this Act, in so far as the registered articles of such company do not exclude or modify the regulations contained in the model articles applicable to such company, those regulations shall, so far as applicable, be the regulations of that company in the same manner and to the extent as if they were contained in the duly registered articles of the company.
(*9*) Nothing in this section shall apply to the articles of a company registered under any previous company law unless amended under this Act.

Act to override memorandum, articles, etc. (section 6)-- Save as otherwise expressly provided in this Act—
(*a*) the provisions of this Act shall have effect notwithstanding anything to the contrary contained in the memorandum or articles of a company, or in any agreement executed by it, or in any resolution passed by the company in general meeting or by its Board of Directors, whether the same be registered, executed or passed, as the case may be, before or after the commencement of this Act; and
(*b*) any provision contained in the memorandum, articles, agreement or resolution shall, to the extent to which it is repugnant to the provisions of this Act, become or be void, as the case may be.

Importance of Articles of Association

Under sec 36(**now section 10 of companies act 2013**), the memorandum and the articles when registered, shall bind the company and its members to the same extent as if it had been signed by them and had contained a covenant on their part that the memorandum and the articles shall be observed.

With respect to the above section, the importance of articles of association can be summed up as follows:

1) ***Binding on members in their relation to the company-*** the members are bound to the company by the provisions of the articles just as much as if they had all put their seals to them.

2) ***Binding on company in relation to its members-*** just as members are bound to the company, the company is bound to the members to observe and follow the articles.

3) ***Neither company, nor members bound to outsiders-*** articles bind the members to the company and company too the members but neither of them is bound to an outsider to give effect to the articles.

4) ***Binding between members inter se-*** the articles define rights and liabilities of the members. As between members inter se the articles constitute a contract between them and are also binding on each member as against the other or others. Such contract can be enforced only through the medium of the company.

Effect of memorandum and articles(section 10 of companies act 2013)—subsection (*1*) Subject to the provisions of this Act, the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed by the company and by each member, and contained covenants on its and his part to observe all the provisions of the memorandum and of the articles.
(*2*) All monies payable by any member to the company under the memorandum or articles shall be a debt due from him to the company

Q12)Difference between articles and memorandum.(S)?

Ans--

1) The memorandum contains the fundamental condition upon which alone the company is allowed to be incorporated. The articles are for the internal regulation and management of the company.

2) Memorandum defines the scope of the activities of the company, or the area beyond which the actions of the company cannot go. Articles are the rules for carrying out the objects of the company as set out in the memorandum.

3) Memorandum being the character of the company, is the supreme document. Art are subordinate to the memorandum. If any conflict between them, the memorandum prevails.

4) Every company must have its own memorandum(**now The memorandum of a company shall be in respective forms specified in Tables A, B, C, D and E in Schedule I as may be applicable to such company**). A company limited by shares need not have articles of its own. In such a case, Table A applies.(**now specified in Tables, F, G, H, I and J in Schedule I**)

5) An action of the company outside the scope of its memorandum is void and incapable of ratification. An act of the company outside the scope of its articles can be confirmed by the shareholders.

6) There are strict restrictions on its alteration. The change of name requires the prior permission of central government and change of registered office to another state requires the prior approval of the Company Law Board. Articles can be altered by a special resolution, to any extent, provided they do not conflict with the memorandum and the Companies Act.

Alteration of articles (sec 31)(now section 14 of companies act 2013)(S)

Section 31 empowers every company to alter its articles at any time with the authority of a special resolution of the company and filing copy with the Registrar. Since it is a statutory power a company will not be deprived of the power of alteration by a contract wit anyone.

The power of alteration of articles conferred by sec 31(now sec 14 of companies act 2013) is almost absolute. It is subject only to two restrictions-

It must not be in contravention with the provisions of the Act.

It is subject to the conditions contained in the memorandum of association.

The proviso to sub-section (1) says that an alteration which has the effect of converting a public company into a private company would not have any effect unless it is approved by the Central Government.

Alteration against memorandum- in ***Hutton v. Scarborough Cliff Hotel Co***, a resolution was passed in a general meeting of a company altered the articles by inserting the power to issue preference shares which did not exist in the memorandum. It was held inoperative. However, after ***Andrews v. Gas Meter Co Ltd*** this view has been changed where a company was allowed by changing articles to issue preference shares when its memorandum was silent on the point. The power of alteration of art is subject only to what is clearly prohibited by the memorandum, expressly or impliedly.

Alteration in breach of contract- a company may change its articles even if the alteration would operate as a breach of contract. If the contract is wholly dependant on the articles, the company would not be liable in damages if it commits breach by changing articles. But if the contract is independent of the articles, the co will be liable in damages if it commits breach by changing articles. Thus in ***Southern Foundries Ltd v. Shirlaw***, where a Managing Director was appointed for a term of ten years, but was removed earlier under the new articles on amalgamation with another company, the company was held liable for breach of contract.

Alteration as fraud on minority shareholders- an alteration must not constitute a fraud on the minority. It should not be an attempt to deprive the company or its minority shareholders of something that in equity belongs to them.

Alteration increasing liability of members- no alteration can require a person to purchase more shares in the company or to increase his liability in any manner except with his consent in writing.

Thus, the power of alteration should be exercised in absolute good faith in the interest of the company.

Alteration of articles.(section 14 of companies act 2013)-- (*1*) Subject to the provisions of this Act and the conditions contained in its memorandum, if any, a company may, by a special resolution, alter its articles including alterations having the effect of conversion of—
(*a*) a private company into a public company; or
(*b*) a public company into a private company:
Provided that where a company being a private company alters its articles in such a manner that they no longer include the restrictions and limitations which are required to be included in the articles of a private company under this Act, the company shall, as from the date of such alteration, cease to be a private company:
Provided further that any alteration having the effect of conversion of a public company into a private company shall not take effect except with the approval of the Tribunal which shall make such order as it may deem fit.
(*2*) Every alteration of the articles under this section and a copy of the order of the Tribunal approving the alteration as per sub-section (*1*) shall be filed with the Registrar, together with a printed copy of the altered articles, within a period of fifteen days in such manner as may be prescribed, who shall register the same.
(*3*) Any alteration of the articles registered under sub-section (*2*) shall, subject to the provisions of this Act, be valid as if it were originally in the articles.

Q13)Explain the Doctrine of Ultra-vires.(L)?

Ans--- Introduction

The object clause of the Memorandum of the company contains the object for which the company is formed. An act of the company must not be beyond the objects clause, otherwise it will be ultra vires and, therefore, void and cannot be ratified even if all the members wish to ratify it. This is called the doctrine of ultra vires.

The word 'ultra' means beyond and 'vires' means powers. Thus the expression ultra vires means an act beyond the powers. Here the expression ultra vires is used to indicate an act of the company which is beyond the powers conferred on the company by the objects clause of its memorandum.

The application of the doctrine of ultra-vires was first demonstrated by the House of Lords in ***Ashbury Railway Carriage & Railway Co. v. Riche***, where the mem of a co defined its objects: 1) to manufacture and sell railway carriages etc; 2) to carry on the business of mechanical engineers and general contractors. The company contracted with Richie to finance the construction of a railway line in Belgium and subsequently repudiated it as one beyond its powers. Richie brought an action for breach of contract. The House of Lords held that the contract was ultra vires and void. They were of the opinion that general terms like general contractors must be taken in reference to the main objects of the company which otherwise would authorize every kind of activity making the memorandum meaningless.

In the next leading case of ***Attorney General v. Great Eastern Railway Co*****,** this doctrine was made clearer. The House of Lords held that the doctrine of UV as explained in ***Ashbury case*** should be maintained but reasonably understood and applied. Thus, an act which is incidental to the objects authorized ought not to be held as UV, unless it is expressly prohibited. Thus in ***Evans v. Brunner, Mond & Co***, a chemicals manufacturing company was allowed to donate 1,00,000 pounds to universities and scientific institutions for research as this would be conducive for the progress of the company.

In India the Supreme Court has affirmed the doctrine in ***A Lakshmanaswami Mudaliar v. LIC***, where the donation made as charity was held ultra vires and the directors were held personally liable to compensate the money.

Thus an act of the company is ultra vires if it is not

a) Essential for the fulfillment of the objects stated in the memorandum;

b) Incidental or consequential to that attainment of its objects

c) Which the company is authorized to do by the Company's Act, in course of its business.

Present position

In England the doctrine of ultra vires has been restricted by the European Communities Act, 1972. Thus, as against a third person acting in good faith, the company can no longer plead that the contract was ultra-vires.

In India, the principles laid down in ***Ashbury case*** are still applied without restrictions and modifications. Thus, in India the ultra vires act is still regarded, as void and it cannot be validated by ratification.

Consequences

1) ***Injunction-*** whenever an ultra vires act has been or is about to be done, any member of the company can get an injunction to restrain the co from proceeding further.

2) ***Personal liability of the directors-*** it is the duty of the directors to see that the funds of the company are used only for legitimate business of the company. If the funds of the company are used for a purpose foreign to its memorandum, the directors will be personally liable to restore it.

3) ***Breach of warranty of authority-*** an agent who acts beyond the scope of his authority will be held personally liable. The directors of a company are its agents. If they induce an outsider to contract in a matter the company does not have power to act, they will be personally liable to him.

4) ***Ultra vires acquired property-*** if a company's money has been spent ultra vires in purchasing some property, the company's right over that property must be held secure. For that asset, though wrongfully acquired, represents corporate capital.

5) ***Ultra vires contracts-*** an ultra vires contract being void ab initio, cannot become intra vires by reason of estoppel, lapse of time, ratification, acquiescence or delay. No performance of either side can give an unlawful contract any validity or right of action upon it.

6) ***Ultra vires torts-*** a company can be made liable for an ultra vires tort committed, provided, it is shown that

a) The activity in the course of which it has been committed falls within the scope of the mem.

b) That the servant committed the tort.

Conclusion

It can be concluded that an UV act is void and cannot be ratified. It prevents the wrongful application of the company's assets likely to result in the insolvency of the company and thereby protects creditors. It also prevents directors from departing the object for which the company has been formed and, thus, puts a check over the activities of the directions. However, it has sometimes led to injustice of third parties acting in good faith.

Q14)Explain the Doctrine of Constructive Notice.(L)?

Ans-- Introduction

Every person who enters into any contract with a company will be presumed to know the contents of the memo of ass and the articles of ass. This is known as the doctrine of constructive notice.

The memorandum and the articles of association of every company are registered with the Registrar of Companies. The office of the Registrar is a public office. Hence, the memo and the articles of ass become public documents. It is therefore the duty of person dealing with a company to inspect its public documents and make sure that his contract is in conformity with their provisions.

As observed by Lord Hatherley, "…whether a person actually reads them or not, he is to be in the same position as if he had read them". Every person will be presumed to know the contents of the documents.

The practical effects of this rule can be observed in ***Kotla Venkataswamy v. Ramamurthy***- The articles of a company provided that its deeds etc should be signed by the managing director, the secretary and a working director on behalf of the co. the plaintiff accepted a deed of mortgage executed by the secretary and a working director only. The plaintiff could not claim his deed. It was held that, "notwithstanding, therefore, she may have acted in good faith and the money may have been applied for the purposes of the company, the bond is nevertheless invalid."

Another effect of this rule is that a person dealing with the company is taken not only to have read the documents but also to have understood them according to their proper meaning. Further, there is a constructive notice not merely of the memo and art, but also of all the documents, such as special resolutions and particulars of charges which are required by the Act to be registered with the Registrar. But there is no notice of documents which are filed only for the sake of record, such as returns and account.

Statutory reform of constructive notice

The 'doctrine of constructive notice' is more or less an unreal doctrine. It does not take notice of the realities of business life. People know a company through its officers and not through its documents. Section 9 of the European Communities Act, 1972 has abrogated this doctrine. These provisions are now incorporated in sec 35 of the (English) Companies Act, 1985.

Position in India

The courts in India do not seem to have taken the doctrine seriously. For example, the Calcutta High Court in ***Charnock Collieries Co Ltd. v. Bholanath***, enforced a security which was not signed in accordance with the company's articles.

Also, in *Dehra* ***Dun Mussorie Electric Tramway Co. v. Jagmandardas,*** the Allahabad High Court allowed an overdraft incurred by the managing agent of a company when under the articles the directors had no power to delegate their borrowing power.

Conclusion-- Thus, the doctrine of constructive notice seeks too protect the company against the outsider by deeming that such an outsider had the notice of the public documents of the company. However, in India the courts with a view to protect the innocent third parties acting in good faith have not relied upon the doctrine seriously.

Q15)Explain the Doctrine of Indoor Management OR

Explain the Rule laid down in Royal British Bank v. Turquand.(L)?

Ans-- Introduction

The doctrine of indoor management is an exception to the rule of constructive notice. It imposes an important limitation on the doctrine of constructive notice. According to this doctrine, a person dealing with a company is bound to read only the public documents. He will not be affected by any irregularity in the internal management of the company.

The rule of indoor management had its genesis in ***Royal British Bank v. Turquand***- The directors of the company borrowed a sum of money from the plaintiff. The company's articles provided that the directors might borrow on bonds such sums as may from time to time be authorized by a resolution passed at a general meeting of a company. The shareholders claimed that there was no such resolution authorizing the loan and, therefore, it was taken without their authority.

The company was however held bound for the loan. Once it was found that the directors could borrow subject to a resolution, the plaintiff had the right to assume that the necessary resolution must have been passed.

The rule is based on public convenience and justice and the following obvious reasons:

1. The internal procedure is not a matter of public knowledge. An outsider is presumed to know the constitution of a company, but not what may or may not have taken place within the doors that are closed to him.
2. The lot of creditors of a limited company is not a particularly happy one; it would be unhappier still if the company could escape liability by denying the authority of officials to act on its behalf.

The rule/doctrine is applied to protect persons contracting with companies from all kinds of internal irregularities. It has been applied to cover the acts of de facto directors, who have not been appointed but have only assumed office at the acquiescence of the shareholders or whose appointment is defective, or have exercised authority which could have been delegated to them under the Act but actually not delegated, or who have acted without quorum.

Exceptions to the rule

1) ***Knowledge of irregularity*** A person who has actual knowledge of the internal irregularity cannot claim the protection of this rule, because he could have taken steps

for self-protection. A person who himself is a party to the inside procedure, such as a director is deemed to know the irregularities, if any.

*T.**R Pratt (Bombay) Ltd. V. E.D. Sassoon & Co. Ltd***. - Company A lent money to Company B on a mortgage of its assets. The procedure laid down in the articles for such transactions was not complied with. The directors of the two companies were the same. Held, the lender had notice of the irregularity and hence the mortgage was not binding.

2) ***Negligence and suspicion of irregularity:*** where a person dealing with a company could discover the irregularity if he had made proper inquiries, he cannot claim the benefit of the rule of indoor management. The protection of the rule is also not available where the circumstances surrounding the contract are so suspicious as to invite inquiry, and the outsider dealing with the company does not make proper inquiry.

3) ***Forgery:*** The rule in ***Turquand's case*** does not apply where a person relies upon a document that turns out to be forged since nothing can validate forgery. In ***Ruben v. Great Fingall Ltd***, a co was not held bound by a certificate issued by tit secretary by forging the signature of two directions. However, in ***Official Liquidator v. Commr of Police***, the Madras High Court held the company liable where the Managing Director had forged the signature of two other directors.

4) ***Representation through articles:*** A person who does not have actual knowledge of the company's articles cannot claim as against the company that he was entitled to assume that a power which could have been delegated to the directors was in fact so delegated. In ***Rama Corporation v. Proved Tin and General Investment Co***, the plaintiffs contracted with the defendant co and gave a cheque under the contract. The director could have been authorized but in fact, was not. The plaintiffs had not read the articles. The director misappropriated the cheques and plaintiff sued. Held, director not liable as it was outside his authority.

Q16) Prospectus(M)?

Ans --- **Definition**

Section 2(36)-" any document described or issued as a prospectus and includes any notice, circular, advertisement, or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of any share in, or debentures of, a corporate body."

Now **section 2 (*70*) of companies act 2013** “prospectus” means any document described or issued as a prospectus and includes a red herring prospectus referred to in section 32 or shelf prospectus referred to in section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate;

In simple words, any document inviting deposits from the public or inviting offers from the public for the subscription of shares or debentures of a company is a prospectus.

Contents

“The Companies Act contains a comprehensive set of regulations intended to protect the investing public from victimization”. The intention of the Legislature in making these regulations, is “to secure the fullest disclosure of material and essential particulars and lay the same in full view of all the intending purchasers of shares”

The relevant rules and regulations are-

1. Every prospects must be dated(section 55)
2. A copy of the prospectus must be registered with the Registrar and this fact must be stated on the face of the prospectus. The Registrar can refuse to register a prospectus which does not comply with the disclosure requirements.(section 60). The prospectus must be issued within 90 days of its registration.
3. If the prospectus includes a statement purporting to be made by an expert, consent in writing of that expert must be obtained and this fact must be stated in the prospectus. (Section 58). The expert should be unconnected with the formation or management of the company. (Section 57). Section 59 provides that the expression “expert” includes an engineer, a valuer, an accountant and any other person whose profession gives authority to a statement made by him. Thus the expert becomes a party to the prospectus and liable for untrue statements, if any.
4. Section 56 requires every prospectus to disclose the matters specified in Schedule II of the Act. The information required to be disclosed refers to the objects of the company, details as to shares, managerial personnel, minimum subscription, underwriting, preliminary expenses, material contracts, etc.

5. Lastly, the "golden rule" –the public is at the mercy of the company promoters. Everything must, therefore, be stated with strict and scrupulous accuracy"

Under companies act 2013—

Public offer and private placement.(section 23 of companies act 2013)-- (*1*) A public company may issue securities—
(*a*) to public through prospectus (herein referred to as "public offer") by complying with the provisions of this Part; **or**
(*b*) through private placement by complying with the provisions of Part II of this Chapter; **or**
(*c*) through a rights issue or a bonus issue in accordance with the provisions of this Act and in case of a listed company or a company which intends to get its securities listed also with the provisions of the Securities and Exchange Board of India Act, 1992 and the rules and regulations made thereunder.
(*2*) A private company may issue securities—
(*a*) by way of rights issue or bonus issue in accordance with the provisions of this Act; or
(*b*) through private placement by complying with the provisions of Part II of this Chapter.
Explanation.—For the purposes of this Chapter, "public offer" includes initial public offer or further public offer of securities to the public by a company, or an offer for sale of securities to the public by an existing shareholder, through issue of a prospectus.

Power of Securities and Exchange Board to regulate issue and transfer of securities, etc.(section 24 of companies act 2013)-- (*1*) The provisions contained in this Chapter, Chapter IV and in section 127 shall,—
(*a*) in so far as they relate to —
(*i*) issue and transfer of securities; and
(*ii*) non-payment of dividend, by listed companies or those companies which intend to get their securities listed on any recognised stock exchange in India, except as provided under this Act, be administered by the Securities and Exchange Board by making regulations in this behalf;
(*b*) in any other case, be administered by the Central Government.
Explanation.—For the removal of doubts, it is hereby declared that all powers relating to all other matters relating to prospectus, return of allotment, redemption of preference shares and any other matter specifically provided in this Act, shall be exercised by the Central Government, the Tribunal or the Registrar, as the case may be.
(*2*) The Securities and Exchange Board shall, in respect of matters specified in subsection (*1*) and the matters delegated to it under proviso to sub-section (*1*) of section 458, exercise the powers conferred upon it under sub-sections (*1*), (*2A*), (*3*) and (*4*) of section 11, sections 11A, 11B and 11D of the Securities and Exchange Board of India Act, 1992.

Issue of application forms for securities.(section 33 of companies act 2013)-- (*1*) No form of application for the purchase of any of the securities of a company shall be issued unless such form is accompanied by an abridged prospectus:
Provided that nothing in this sub-section shall apply if it is shown that the form of application was issued—
(*a*) in connection with a *bona fide* invitation to a person to enter into an underwriting agreement with respect to such securities; or
(*b*) in relation to securities which were not offered to the public.
(*2*) A copy of the prospectus shall, on a request being made by any person before the closing of the subscription list and the offer, be furnished to him.
(*3*) If a company makes any default in complying with the provisions of this section, it shall be liable to a penalty of fifty thousand rupees for each default.

Prohibition on acceptance Of deposits from public.(section 73 of companies act 2013)-- (*1*) On and after the commencement of this Act, no company shall invite, accept or renew deposits under this Act from the public except in a manner provided under this Chapter:
Provided that nothing in this sub-section shall apply to a banking company and nonbanking financial company as defined in the Reserve Bank of India Act, 1934 and to such other company as the Central Government may, after consultation with the Reserve Bank of India, specify in this behalf.
(*2*) A company may, subject to the passing of a resolution in general meeting and subject to such rules as may be prescribed in consultation with the Reserve Bank of India, accept deposits from its members on such terms and

conditions, including the provision of security, if any, or for the repayment of such deposits with interest, as may be agreed upon between the company and its members, subject to the fulfilment of the following conditions, namely:—
(*a*) issuance of a circular to its members including therein a statement showing the financial position of the company, the credit rating obtained, the total number of depositors and the amount due towards deposits in respect of any previous deposits accepted by the company and such other particulars in such form and in such manner as may be prescribed;
(*b*) filing a copy of the circular along with such statement with the Registrar within thirty days before the date of issue of the circular;
(*c*) depositing such sum which shall not be less than fifteen per cent. of the amount of its deposits maturing during a financial year and the financial year next following, and kept in a scheduled bank in a separate bank account to be called as deposit repayment reserve account;
(*d*) providing such deposit insurance in such manner and to such extent as may be prescribed;
(*e*) certifying that the company has not committed any default in the repayment of deposits accepted either before or after the commencement of this Act or payment of interest on such deposits; and
(*f*) providing security, if any for the due repayment of the amount of deposit or the interest thereon including the creation of such charge on the property or assets of the company:
Provided that in case where a company does not secure the deposits or secures such deposits partially, then, the deposits shall be termed as ''unsecured deposits'' and shall be so quoted in every circular, form, advertisement or in any document related to invitation or acceptance of deposits.
(*3*) Every deposit accepted by a company under sub-section (*2*) shall be repaid with interest in accordance with the terms and conditions of the agreement referred to in that sub-section.
(*4*) Where a company fails to repay the deposit or part thereof or any interest thereon under sub-section (*3*), the depositor concerned may apply to the Tribunal for an order directing the company to pay the sum due or for any loss or damage incurred by him as a result of such non-payment and for such other orders as the Tribunal may deem fit.
(*5*) The deposit repayment reserve account referred to in clause (*c*) of sub-section (*2*) shall not be used by the company for any purpose other than repayment of deposits

Shelf prospectus(section 31 of companies act 2013)-- (*1*) Any class or classes of companies, as the Securities and Exchange Board may provide by regulations in this behalf, may file a shelf prospectus with the Registrar at the stage of the first offer of securities included therein which shall indicate a period not exceeding one year as the period of validity of such prospectus which shall commence from the date of opening of the first offer of securities under that prospectus, and in respect of a second or subsequent offer of such securities issued during the period of validity of that prospectus, no further prospectus is required.
(*2*) A company filing a shelf prospectus shall be required to file an information memorandum containing all material facts relating to new charges created, changes in the financial position of the company as have occurred between the first offer of securities or the previous offer of securities and the succeeding offer of securities and such other changes as may be prescribed, with the Registrar within the prescribed time, prior to the issue of a second or subsequent offer of securities under the shelf prospectus:
Provided that where a company or any other person has received applications for the allotment of securities along with advance payments of subscription before the making of any such change, the company or other person shall intimate the changes to such applicants and if they express a desire to withdraw their application, the company or other person shall refund all the monies received as subscription within fifteen days thereof.
(*3*) Where an information memorandum is filed, every time an offer of securities is made under sub-section (*2*), such memorandum together with the shelf prospectus shall be deemed to be a prospectus.
Explanation.—For the purposes of this section, the expression "shelf prospectus" means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.

Red herring prospectus.(section 32 of companies act 2013)-- (*1*) A company proposing to make an offer of securities may issue a red herring prospectus prior to the issue of a prospectus.
(*2*) A company proposing to issue a red herring prospectus under sub-section (*1*) shall file it with the Registrar at least three days prior to the opening of the subscription list and the offer.
(*3*) A red herring prospectus shall carry the same obligations as are applicable to a prospectus and any variation between the red herring prospectus and a prospectus shall be highlighted as variations in the prospectus.
(*4*) Upon the closing of the offer of securities under this section, the prospectus stating therein the total capital raised, whether by way of debt or share capital, and the closing price of the securities and any other details as are not included in the red herring prospectus shall be filed with the Registrar and the Securities and Exchange Board.

Explanation.—For the purposes of this section, the expression "red herring prospectus" means a prospectus which does not include complete particulars of the quantum or price of the securities included therein.

Q17) Prospectus- Remedies for Misrepresentation(M)?

Ans-- 1)***Rescission for misrepresentation***-the shareholder can also sue the company for rescission of the contract. Under this remedy the contract is cancelled and the money given by the shareholder refunded. Under **Section 75 of the Contract Act**, a person who lawfully rescinds a contract is entitled to compensation for any damage which he has sustained through non-fulfillment of the contract.

Loss of right of rescission

(a) ***By affirmation***-if the allottee with full knowledge of the misrepresentation upholds the contract, he cannot afterwards rescind.

(b) ***By unreasonable delay***- any man who claims to retire from a company on the ground that he was induced to become a member by misrepresentation, is bound to come at the earliest possible moment after he becomes aware of the misrepresentation." An action after 5 months was held to be too late.

(c) ***By commencement of winding up***-the right of rescission is lost on the commencement of the winding up of the company. "But where a shareholder has started active proceedings to be relieved of his shares, the passing of the winding up order during their pendency would not prevent his getting the relief."

2. ***Damages for deceit***-any person induced by a fraudulent statement in a prospectus to take shares, is entitled to sue the company for damages. He must prove the same matters in claiming damages for deceit as in claiming rescission of the contract. He cannot both retain the shares and get damages against the company. He must show that he has repudiated the shares and has not acted as a shareholder after discovering the fraud or misrepresentation.
3. ***Compensation***-Section 62(**now section 35 of companies act 2013**)-every director, promoter and every person authorizes the issue of the prospectus is liable to pay compensation to the aggrieved party for loss or damage he may have incurred by reason of any untrue statement in the prospectus.

The persons who are liable to pay compensation are

(a) directors at the time of issue of prospectus

(b) persons who have authorized themselves to be named as directors in the prospectus

(c) promoters

(d) persons who have authorized the issue of prospectus.

Civil liability for misstatements In prospectus(Section 35 of companies act 2013)-- (*1*) Where a person has subscribed for securities of a company acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the company and every person who—
(*a*) is a director of the company at the time of the issue of the prospectus;
(*b*) has authorised himself to be named and is named in the prospectus as a director of the company, or has agreed to become such director, either immediately or after an interval of time;
(*c*) is a promoter of the company;
(*d*) has authorised the issue of the prospectus; and
(*e*) is an expert referred to in sub-section (*5*) of section 26, shall, without prejudice to any punishment to which any person may be liable under section 36, be liable to pay compensation to every person who has sustained such loss or damage.
(*2*) No person shall be liable under sub-section (*1*), if he proves—
(*a*) 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; or
(*b*) that the prospectus was issued without his knowledge or consent, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent.
(*3*) Notwithstanding anything contained in this section, where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person referred to in subsection
(*1*) shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.

Punishment For fraudulently Inducing persons to invest money (section 36 of companies act 2013)- Any person who, either knowingly or recklessly makes any statement, promise or forecast which is false, deceptive or misleading, or deliberately conceals any material facts, to induce another person to enter into, or to offer to enter into,—
(*a*) any agreement for, or with a view to, acquiring, disposing of, subscribing for, or underwriting securities; or
(*b*) any agreement, the purpose or the pretended purpose of which is to secure a profit to any of the parties from the yield of securities or by reference to fluctuations in the value of securities; or
(*c*) any agreement for, or with a view to obtaining credit facilities from any bank or financial institution, shall be liable for action under section 447.

Action by affected persons.(section 37 of companies act 2013)- A suit may be filed or any other action may be taken under section 34 or section 35 or section 36 by any person, group of persons or any association of persons affected by any misleading statement or the inclusion or omission of any matter in the prospectus.

Punishment for personation For acquisition, etc., of securities.(section 38 of companies act 2013) (*1*) Any person who—
(*a*) makes or abets making of an application in a fictitious name to a company for acquiring, or subscribing for, its securities; or
(*b*) makes or abets making of multiple applications to a company in different names or in different combinations of his name or surname for acquiring or subscribing for its securities; or
(*c*) otherwise induces directly or indirectly a company to allot, or register any transfer of, securities to him, or to any other person in a fictitious name, shall be liable for action under section 447.
(*2*) The provisions of sub-section (*1*) shall be prominently reproduced in every prospectus issued by a company and in every form of application for securities.

(*3*) Where a person has been convicted under this section, the Court may also order disgorgement of gain, if any, made by, and seizure and disposal of the securities in possession of, such person.
(*4*) The amount received through disgorgement or disposal of securities under subsection
(*3*) shall be credited to the Investor Education and Protection Fund

Defences

(a) ***Withdrawal of consent***-a director, etc is not liable if he withdrew his consent before the issue of the prospectus and it was issued without his consent or authority

(b) ***Absence of consent***-where a prospectus was issued without the a directors', etc knowledge or consent, and on becoming aware of its issue, he forthwith gave reasonable public notice of that fact, he is not liable.

(c) ***Ignorance of untrue statement***-a director, etc may sometimes be ignorant of the untrue statement contained in the prospectus. If after te issue of the prospectus and before allotment there under, he on becoming aware of any untrue statement therein withdrew his consent to the prospectus and gave reasonable public notice of the withdrawal and of the reasons therefore, he is not liable.

(d) ***Reasonable ground for belief***-if a director, etc has reasonable ground to believe that the statement was true and he, in fact, believed it to be true up to the time of allotment, he is not liable.

(e) ***Statement of expert***-if the statement is a correct and fair representation or extract or copy of the statement made by an expert who is competent to make it and had given his consent and not withdrawn it, the director, etc is not liable.

Q18)Promoters.(M)?

Ans-- A promoter is a person who does the necessary preliminary work incidental to the formation of a company. It is a compendious term used for a person who undertakes, does and goes through all the necessary and incidental preliminaries, keeping in view the object, to bring into existence an incorporated company.

Chronologically, the first persons who control a company's affairs are its promoters.

Section 2(*69*) of companies act 2013"promoter" means a person—

(*a*) who has been named as such in a prospectus or is identified by the company in the annual return referred to in section 92; or
(*b*) who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or
(*c*) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act:
Provided that nothing in sub-clause (*c*) shall apply to a person who is acting merely in a professional capacity;

Functions

1. The promoter of a company decides its name and ascertains that it will be accepted by the Registrar of Companies.
2. He settles the details of the company's Memorandum and Articles, the nominations of directors, solicitors, bankers, auditors and secretary and the registered office of the company.
3. He arranges for the printing of the Memorandum and Articles, the registration of the company, the issue of prospectus, where a public issue is necessary

He is responsible for bringing the company into existence for the object which he has in view.

Quasi-trustee-a promoter is neither an agent nor a trustee of the company under incorporation but certain fiduciary duties have been imposed on him under the Companies Act, 1956.He is not an agent because there is no principal born at the time and he is not a trustee because there is no cesti que trust in existence. Hence he occupies the peculiar position of a quasi-trustee.

Fiduciary position

1. ***Not to make any profit at the expense of the company***-the promoter must not make, either directly or indirectly, any profit at the expense of the company which is being promoted. If any secret profit is made in violation of this rule, the company may, on discovering it, compel him to account for and surrender such profit.

2. ***To give benefit of negotiations to the company***-the promoter must, when once he has begun to act in the promotion of a company, give to the company the benefit of any negotiations or contracts into which he enters in respect of the company. Thus where he purchases some property for the company, he cannot rightfully sell that property to the company at a price higher than he have for it. If he does so, the company may, on discovering it, rescind the contract and recover the purchase money.
3. ***To make a full disclosure of interest or profit*-**if the promoter fails to make a full disclosure of all the relevant facts, including any profit and his personal interest I a transaction with the company, the company may sue him for damages for breach of his fiduciary duty and recover from him any secret profit made even though rescission is not asked or is impossible.
4. ***Not to make unfair use of position***-the promoter must not make an unfair or t take care to avoid any unreasonable use of his position and must take care to avoid anything which has the appearance of undue influence or fraud

   Further, a promoter cannot relive himself of his liability by making provisions to that effect in the Articles of the company.

5. ***Duty of promoter as regards prospectus***-the promoter must see, in connection with the prospectus, if any is issued, that the prospectus –

(a) contains the necessary particulars

(b) does not contain any untrue or misleading statements or does not omit any material fact.

Remuneration--- A promoter has no right to get compensation from the company for his services in promoting the company unless there is a contact to that effect. In practice, a promoter takes remuneration for his services in one of the following ways-

1. he my sell his own property at a profit to the company for cash or fully- paid shares provided he makes a disclosure to this effect
2. He may be given an option to buy a certain number of shares in the company at par.
3. He may take a commission on the shares sold
4. He may be paid a lump sum by the company.

Q19)Directors- Powers, Duties and Position.(L)?

Ans -- A company in the eyes of the law is an artificial person. It has no physical existence. It has neither soul nor a body of its own. As such, it cannot act in its own person.

The directors are the brain of a company. They occupy a pivotal position in the structure of the company. They are in fact the mainspring of the company.

Definition

Sction 2(*34*)of companies act 2013 "director" means a director appointed to the Board of a company

'Director' includes any person occupying the position of director, by whatever name called. The important factor to determine whether a person is or not a director is to refer to the nature of the office and its duties. Thus a director may be defined as a person having control over the direction, conduct, management or superintendence of the affairs of the company.

Only individuals can be directors-no body corporate, association or firm can be appointed director of a company. Only an individual can be so appointed.

Position of directors

1. ***Directors as agents*-**a company, as an artificial person, acts through directors who are elected representatives of the shareholders. They are, in the eyes of the law, agents of the company for which they act-***Ferguson v Wilson***. The general principles of the law of principal and agent regulate in most respects the relationship between the company and its directors.
2. ***Directors as servants*-**they are not servants of the company. A director may, however, become a servant in a different capacity. For example, the creator and controller of an air farming company was also working as its pilot. He died in an accident. His widow was allowed workman's compensation –***Lee v Lee's Farming Ltd.***

3. ***Directors as officers***- a director is an officer of the company. As such they are liable to certain penalties if the provisions of the Companies Act are not strictly complied with.
4. ***Director as trustees***-

(a) ***Directors as trustees of the company's money and property*** in the sense that they must account for all the company's money and property over which they exercise control.

Directors are, however, not trustees in the real sense of the world because they are not vested with the ownership of the company's property. It is only as regards some of their obligations to the company and certain powers that they are regarded as trustees of the company.

(b) ***Directors as trustees of the power entrusted to them*** in the sense that they must exercise their powers honestly and in the interest of the company and the shareholders and not in their own interest.

Trustees of the company-directors are trustees for the company and not for the third party who have made contracts with the company or for the individual shareholders.

Quasi-trustees-directors are only quasi-trustees because-

(i) they are not vested with ownership of the company's property

(ii) their functions are not the same as those of trustees

(iii) their duties of care are not as onerous as those of trustees.

Powers of directors

General Powers of the Board (Section 291of companies act 1956)(section 179 of Companies act 2013)

The powers of the Board of directors are co-extensive with those of the company. This proposition is, however, subject to two conditions:

First, the Board shall not do any act which is to be done by the company in general meeting

Second, the Board shall exercise its powers subject to the provisions contained in the Companies Act, or in the Memorandum or the Articles of the company or in any regulations made by the company in general meeting.

Powers to be exercised at Board meetings (Section 292)(section 179 of companies act 2013)

The Board of directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at the meetings of the Board, viz, the power to-

(a) make calls on shareholders in respect of money unpaid on their shares

(b) issue debentures

(c) borrow money otherwise than on debentures

(d) invest the funds of the company

(e) make loans

Powers of Board.(section 179 of companies act 2013)--- (*1*) The Board of Directors of a company shall be entitled to exercise all such powers, and to do all such acts and things, as the company is authorised to exercise and do:
Provided that in exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made thereunder, including regulations made by the company in general meeting:
Provided further that the Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting.
(*2*) No regulation made by the company in general meeting shall invalidate any prior act of the Board which would have been valid if that regulation had not been made.
(*3*) The Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board, namely:—
(*a*) to make calls on shareholders in respect of money unpaid on their shares;
(*b*) to authorise buy-back of securities under section 68;
(*c*) to issue securities, including debentures, whether in or outside India;
(*d*) to borrow monies;
(*e*) to invest the funds of the company;
(*f*) to grant loans or give guarantee or provide security in respect of loans;
(*g*) to approve financial statement and the Board's report;
(*h*) to diversify the business of the company;
(*i*) to approve amalgamation, merger or reconstruction;
(*j*) to take over a company or acquire a controlling or substantial stake in another company;
(*k*) any other matter which may be prescribed:
Provided that the Board may, by a resolution passed at a meeting, delegate to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the powers specified in clauses (*d*) to (*f*) on such conditions as it may specify:
Provided further that the acceptance by a banking company in the ordinary course of its business of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise, or the placing of monies on deposit by a banking company with another banking company on such conditions as the Board may prescribe, shall not be deemed to be a borrowing of monies or, as the case may be, a making of loans by a banking company within the meaning of this section.

Explanation I.—Nothing in clause (*d*) shall apply to borrowings by a banking company from other banking companies or from the Reserve Bank of India, the State Bank of India or any other banks established by or under any Act.
Explanation II.—In respect of dealings between a company and its bankers, the exercise by the company of the power specified in clause (*d*) shall mean the arrangement made by the company with its bankers for the borrowing of money by way of overdraft or cash credit or otherwise and not the actual day-to-day operation on overdraft, cash credit or other accounts by means of which the arrangement so made is actually availed of.
(*4*) Nothing in this section shall be deemed to affect the right of the company in general meeting to impose restrictions and conditions on the exercise by the Board of any of the powers specified in this section.

Powers to be exercised with the approval of company in general meeting

(a) sale or lease of the company's undertaking

(b) extension of the time for payment of a debt due by a director

(c) investment of compensation received on acquisition of the company's assets in securities other than trust securities

(d) borrowing of money beyond the paid-up capital of the company

(e) contributions to any charitable fund beyond 5% of the average et profits during the preceding three financial years,**(section 181 of companies act 2013).**

(f) Prohibitions And restrictions Regarding political contributions(**section 182 of companies act 2013**) the aggregate of the amount which may be so contributed by the company in any financial year shall not exceed seven and a half per cent. of its average net profits during the three immediately preceding financial years:
(g) **Power of Board and other persons to make contributions to national defence fund, etc.(section 183 of companies act 2013)-no limit fixed**
Restrictions on powers of Board.(section 180 of companies act 2013)-- (*1*) The Board of Directors of a company shall exercise the following powers only with the consent of the company by a special resolution, namely:—
(*a*) to sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company or where the company owns more than one undertaking, of the whole or substantially the whole of any of such undertakings.
Explanation.—For the purposes of this clause,—
(*i*) "undertaking" shall mean an undertaking in which the investment of the company exceeds twenty per cent. of its net worth as per the audited balance sheet of the preceding financial year or an undertaking which generates twenty per cent. of the total income of the company during the previous financial year;
(*ii*) the expression "substantially the whole of the undertaking" in any financial year shall mean twenty per cent. or more of the value of the undertaking as per the audited balance sheet of the preceding financial year;
(*b*) to invest otherwise in trust securities the amount of compensation received by it as a result of any merger or amalgamation;
(*c*) to borrow money, where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital and free reserves, apart from temporary loans obtained from the company's bankers in the ordinary course of business:
Provided that the acceptance by a banking company, in the ordinary course of its business, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise, shall not be deemed to be a borrowing of monies by the banking company within the meaning of this clause.

Explanation.—For the purposes of this clause, the expression "temporary loans" means loans repayable on demand or within six months from the date of the loan such as short-term, cash credit arrangements, the discounting of bills and the issue of other short-term loans of a seasonal character, but does not include loans raised for the purpose of financial expenditure of a capital nature
(*d*) to remit, or give time for the repayment of, any debt due from a director.
(*2*) Every special resolution passed by the company in general meeting in relation to the exercise of the powers referred to in clause (*c*) of sub-section (*1*) shall specify the total amount up to which monies may be borrowed by the Board of Directors.
(*3*) Nothing contained in clause (*a*) of sub-section (*1*) shall affect—
(*a*) the title of a buyer or other person who buys or takes on lease any property, investment or undertaking as is referred to in that clause, in good faith; or
(*b*) the sale or lease of any property of the company where the ordinary business of the company consists of, or comprises, such selling or leasing.
(*4*) Any special resolution passed by the company consenting to the transaction as is referred to in clause (*a*) of sub-section (*1*) may stipulate such conditions as may be specified in such resolution, including conditions regarding the use, disposal or investment of the sale proceeds which may result from the transactions:
Provided that this sub-section shall not be deemed to authorise the company to effect any reduction in its capital except in accordance with the provisions contained in this Act.
(*5*) No debt incurred by the company in excess of the limit imposed by clause (*c*) of sub-section (*1*) shall be valid or effectual, unless the lender proves that he advanced the loan in good faith and without knowledge that the limit imposed by that clause had been exceeded

Duties of the Directors

1. ***Fiduciary duties***-as fiduciaries, the directors must-

(a) exercise their powers honestly and bona fide for the benefit of the company as a whole; and

(b) not place themselves in a position in which there is a conflict between their duties to the company and their personal interests. They must not make any secret profit out of their position. If they do, they have to account for it to the company.

2. ***Duties of care, skill and diligence***- directors should carry out their duties with reasonable care and exercise such degree of skill and diligence as is reasonably expected of persons of their knowledge and status. He is not bound to bring any special qualifications to his office.

Standard of care-the standard of care, skill and diligence depends upon the nature of the company's business and circumstances of the case. They are various standards of the care depending upon:

(a) the type and nature of work

(b) division of powers between directors and other officers

(c) general usages and customs in that type of business; and

(d) whether directors work gratuitously or remuneratively

3. ***Duty to disclose interest*-**where a director is personally interested in a transaction of the company, he is required to disclose his interest to the board. An interested director is neither to vote on the matter of his interest nor his presence shall count for the purposes of quorum.
4. ***Duty to attend board meetings*-**the Act only says that the office of a director is automatically vacated if he fails to attend three consecutive meetings of the board or all meetings for a period of 3 months, whichever is longer. Moreover, a director's habitual absence may become evidence of negligence.
5. ***Duty not to delegate***- a director should not delegate his functions to another person. But delegation of functions may be made to the extent to which it is authorized by the Act or the constitution of the company.

Q20)Company Secretary and Secretrial audit(section 204 and 205 of companies act 2013)?

Ans-- *Section 2 (24) of companies act 2013* "company secretary" or "secretary" means a company secretary as defined in clause (*c*) of sub-section (*1*) of section 2 of the Company Secretaries Act, 1980 who is appointed by a company to perform the functions of a company secretary under this Act;

Secretarial audit for Bigger companies(section 204 of companies act 2013)- (*1*) Every listed company and a company belonging to other class of companies as may be prescribed shall annex with its Board's report made in terms of sub-section (*3*) of section 134, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed.

(*2*) It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

(*3*) The Board of Directors, in their report made in terms of sub-section (*3*) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his report under sub-section (*1*).

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

Functions of company secretary.(section 205 of companies act 2013)- (*1*) The functions of the company secretary shall include,—

(*a*) to report to the Board about compliance with the provisions of this Act, the rules made thereunder and other laws applicable to the company;

(*b*) to ensure that the company complies with the applicable secretarial standards;

(*c*) to discharge such other duties as may be prescribed.

Explanation.—For the purpose of this section, the expression "secretarial standards" means secretarial standards issued by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980 and approved by the Central Government.

(*2*) The provisions contained in section 204 and section 205 shall not affect the duties and functions of the Board of Directors, chairperson of the company, managing director or whole-time director under this Act, or any other law for the time being in force.

<u>Q21)Quorum (Section 174).(S)(section 103 of companies act 2013)?</u>

Ans-- ‘Quorum’ means the minimum number of members who must be present in order to constitute a valid meeting and transact busies thereat. The quorum is generally fixed by the Articles. If the Articles of a company do not provide for a large quorum, the following rules apply:

1.) Quorum for public company-5 members personally present

Quorum for other companies-2

For the purpose of quorum a person may be counted as 2 or more members if he holds shares in different capacities.

2. if within half an hour a quorum is not present, the meeting, if called upon the requisition of members, shall stand dissolved. In any other case, it shall stand adjourned to the same day, place and time in the next week. The Board of Directors may adjourn the meeting to be convened on any particular day, time and place to b fixed on the date of the meeting itself or at least before the commencement of the same in the next week. Where the Board of directors fails to do so, the meeting stands statutorily adjourned to the same day in the next week.

<u>The Articles may provide for a large quorum</u>-The Articles cannot provide for a quorum smaller than the statutory minimum. For the purpose of quorum, only members present in person and not proxies are to be counted.

<u>When quorum should be present-Article 49(1)</u> of Table A requires the quorum to be present at the time when the meeting proceeds to transact business. It need not be present throughout or at the time of taking vote on any resolution.

<u>Quorum for meetings(section 103 of companies act 2013)-</u> (*1*) Unless the articles of the company provide for a larger number,—
(*a*) in case of a public company,—
(*i*) five members personally present if the number of members as on the date of meeting is not more than one thousand;
(*ii*) fifteen members personally present if the number of members as on the date of meeting is more than one thousand but up to five thousand;
(*iii*) thirty members personally present if the number of members as on the date of the meeting exceeds five thousand;
(*b*) in the case of a private company, two members personally present, shall be the quorum for a meeting of the company.
(*2*) If the quorum is not present within half-an-hour from the time appointed for holding a meeting of the company—

(*a*) the meeting shall stand adjourned to the same day in the next week at the same time and place, or to such other date and such other time and place as the Board may determine; or
(*b*) the meeting, if called by requisitionists under section 100, shall stand cancelled:
Provided that in case of an adjourned meeting or of a change of day, time or place of meeting under clause (*a*), the company shall give not less than three days notice to the members either individually or by publishing an advertisement in the newspapers (one in English and one in vernacular language) which is in circulation at the place where the registered office of the company is situated.
(*3*) If at the adjourned meeting also, a quorum is not present within half-an-hour from the time appointed for holding meeting, the members present shall be the quorum

Q22)Kinds of Companies.(L)?

Ans-- Classification on the basis of liability

1. ***Companies with limited liability***

(a) ***Companies limited by shares***- where the liability of the members of a company is limited to the amount unpaid on the shares, such a company is known as a company limited by shares

(b) ***Companies limited by guarantee***- where the liability of the members of a company is limited to a fixed amount which the members undertake to contribute to the assets of the company in the event of its being wound up, the company is called a company limited b guarantee.

2. ***Unlimited companies***- A company without limited liability is known as an unlimited company. In case of such a company, every member is liable for the debts of the company.

Classification on the basis of number of members

1. ***Private company***-a private company is normally what the Americans call a 'close corporation'. According to Section 3(1)**,** a private company means a company which has a minimum paid-up capital of Rs. 1,00,000 or such higher paid-up capital as may be prescribed, and by its Articles-

(i) restricts the right to transfer its shares, if any. The restriction is meant to preserve the private character of the company

(ii) limits the number of its members to 50 not including its employee-members

(iii) prohibits any invitation to the public to subscribe for any shares in, or debentures of, the company

(iv) prohibits any invitation or acceptance of deposits from persons other than its members, directors or their relatives.

Ever private company, existing on the commencement of the Companies(Amendment)Act, 2000, with a paid-up capital of less than Rs. 1,00,000 shall, within a period of 2 years from such date of commencement, enhance its paid up capital to Rs. 1,00,000.

2. ***Public company***- A public company means a company which –

(i) has a minimum paid-up capital of Rs. 5 lakh or such higher paid-up capital, as may be prescribed

(ii) is a private company which is a subsidiary of a company which is not a private company.

Ever public company, existing on the commencement of the Companies(Amendment)Act, 2000, with a paid-up capital of less than Rs. 5,00,000 shall, within a period of 2 years from such date of commencement, enhance its paid up capital to Rs. 5,00,000.

One person company ---Section 2(*62*) of companies act 2013"One Person Company" means a company which has only one person as a member;

Classification on the basis of control

1. ***Holding company-Section 4(4)*- a company is known as the holding company of another company if is has control over that other company

Under section 2 **(46) of companies act 2013 "holding company", in relation to one or more other companies, means a company of which such companies are subsidiary companies**

2. ***Subsidiary company-Section 4(1)***—a company is known as a subsidiary of another company when control is exercised by the latter(called holding company) over the former called a subsidiary company.

Under section 2 **(*87*)of companies act 2013** "subsidiary company" or "subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company—
(*i*) controls the composition of the Board of Directors; or
(*ii*) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:
Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.
Explanatio*n.*—For the purposes of this clause,—
(*a*) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (*i*) or sub-clause (*ii*) is of another subsidiary company of the holding company;
(*b*) the composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;
(*c*) the expression "company" includes any body corporate;
(*d*) "layer" in relation to a holding company means its subsidiary or subsidiaries;

A company is deemed to be a subsidiary of another company when-

(i) where the company controls the composition of Board of Directors of the subsidiary company

(ii) where the company holds more than half the nominal value of equity share capital of another company

(iii) where a company is subsidiary of another company, which is itself is subsidiary of the controlling company.

Classification on the basis of ownership

1. ***Government company***-a Government company means any company in which not less than 51 % of the paid-up share capital is held by-

(i) the Central government

(ii) any State government or governments

(iii) partly by the Central government and partly by one or more State governments.

2. ***Non-government company***

Foreign company- it means any company incorporated outside India which has an established place of business in India. **(Section 591(1)**

Section 2 (42**) of companies act 2013 "foreign company**" means any company or body corporate incorporated outside India which—
(*a*) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
(*b*) conducts any business activity in India in any other manner.

Q23) ***Government Company.(S)?***

Ans --- A Government company means any company in which not less than 51% of the paid-up share capital is held by-

(a) the Central Government, or

(b) any State Government or Governments, or

(c) partly by the Central Government and partly by one or more State Governments.

Section 2(*45*) of companies act 2013"Government company" means any company in which not less than fiftyone per cent. 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

Example- State Trading Corporation of India

Rules applicable by Government companies

1. ***Appointment of auditor and audit reports-Section 619***-the auditor of a Government company shall be appointed or re-appointed by the Comptroller and Auditor-General of India. The Comptroller and Auditor-General shall have power to direct the manner in which the company's accounts shall be audited by the auditor. A copy of the audit reports are to be submitted to the Comptroller and Auditor-General who shall have the right to comment upon it or supplement it.

2. ***Annual report to be placed before Parliament-Section 619*-A-**where the Central Government is a member of a Government company, it shall cause an annual report on the working and affairs of the company to be prepared within 3 months of its annual meeting before which the audit report is placed. The report shall be laid before both Houses of Parliament together with a copy of the audit report.

3. ***Provisions of Section 619 to apply to certain companies***-the provisions of Section 619 shall apply to a company in which not less than 51% of the paid-up capital is held jointly by Government, Government companies and public financial corporations.

4. ***Certain provisions of the Companies Act do not apply-Section 620***-the Central Government may, by notification in the Official Gazette, direct that any of the provisions of the Companies Act(other than Sections 618, 619), specified in the notification –

(a) shall not apply to any Government company,

(b) shall apply to any Government company, with such exceptions, modifications and adaptations, as may be specified in the notification.

But under New companies act 2013 ----

Annual reports on Government companies(section 394 of companies act 2013)-- (*1*) Where the Central Government is a member of a Government company, the Central Government shall cause an annual report on the working and affairs of that company to be—
(*a*) prepared within three months of its annual general meeting before which the comments given by the Comptroller and Auditor-General of India and the audit report is placed under the proviso to sub-section (*6*) of section 143; and
(*b*) as soon as may be after such preparation, laid before both Houses of Parliament together with a copy of the audit report and comments upon or supplement to the audit report, made by the Comptroller and Auditor-General of India.
(*2*) Where in addition to the Central Government, any State Government is also a member of a Government company, that State Government shall cause a copy of the annual report prepared under sub-section (*1*) to be laid before the House or both Houses of the State Legislature together with a copy of the audit report and the comments upon or supplement to the audit report referred to in sub-section (*1*).

Annual reports where one or more State Governments(section 395 of companies act 2013)-- (*1*) Where the Central Government is not a member of a Government company, every State Government which is a member of that company, or where only one State Government is a member of the company, that State Government shall cause an annual report on the working and affairs of the company to be—
(*a*) prepared within the time specified in sub-section (*1*) of section 394; and
(*b*) as soon as may be after such preparation, laid before the House or both Houses of the State Legislature together with a copy of the audit report and comments upon or supplement to the audit report referred to in sub-section (*1*) of that section.
(*2*) The provisions of this section and section 394 shall, so far as may be, apply to a Government company in liquidation as they apply to any other Government company.

Q24)Conversion of a Private Company into a Public Company.(M)?

Ans -- A private company may become a public company by-

1. ***Conversion by default-Section 43*****-**where a default is made by a private company in complying with the essential requirements of a private company, the company ceases to enjoy the privileges and exceptions conferred on a private company. In such a case, the provisions of the Companies Act apply to it as if it were not a private company. Company Law Board may relieve the company from the consequences as aforesaid, if it is of opinion that the non-compliance was accidental or due to inadvertence or other sufficient cause.

2. ***Conversion by operation of law (deemed public company)-Section 43A*****-**a private company becomes a public company-

(a) where not less that 25% of the paid-up share capital of the private company is held by one or more bodies corporate.

(b) where the average annual turnover of the private company at ny time is not less than such amount as may be prescribed for 3 consecutive financial years.

(c) where the private company holds not less than 25% of the paid-up share capital of a public company, having a share capital.

(d) where the private company invites, accepts or renews deposits from the public.

3. ***Conversion by choice or volition-Section 44***-if a private company so alters its Articles that they do not contain the provision which make it a private company, it shall cease to be a private company as on the date of the alteration. It shall than file with the Registrar, within 30 days, either a prospectus or statement in lieu of prospectus. When this is done, the company becomes a public company

A private company which becomes a public company shall also-

(i) file a copy of the resolution altering the Articles, within 30 days of passing thereof, with the Registrar;

(ii) take steps to raise its membership to at least 7 if it is below that number on the date of conversion, and also increase the number of its directors to more than 2 if it is below that number;

(iv) alter the regulations contained in the Articles which are inconsistent with those of a public company.

These all sections are omitted in new companies act 2013

Q25)What are the Advantages of a Private Company?(M)

Ans--

1. ***Number of members***-its formation requires only 2 persons. This facilitates its harmonious functioning and makes the choice of a private company must suitable for friendly or family concerns.
2. ***Allotment before minimum subscription***-a private company can allot shares before the minimum subscription is subscribed for or paid.
3. ***Kinds of shares***-a private company may issue share capital of any kind and with such voting rights as it may think fit.
4. ***Commencement of business***-a private company can commence business immediately on incorporation without having to obtain a certificate for commencement.
5. ***Number of directors***-a private company need not have more than 2 directors. All the directors can be given permanent appointment by a single resolution.
6. ***Index of members***-a private company need not keep an index of members.
7. ***Prospectus or statement in lieu of prospectus***- a private company may allot shares without issuing a prospectus or delivering to the Registrar a statement in lieu of prospectus.
8. ***Issue of new shares***-it can issue new shares to outsiders. Section 81(**now section 62 of companies act 2013)** does not apply.
9. ***Statutory meeting and statutory report*-**a private company need not hold statutory meeting or file with the Registrar the statutory report.
10. ***Rules regarding directors***-the rules regarding directors are less stringent.

Q26)Dividends.(M)?

Ans--One of the main objects of commercial enterprises is to earn profits which are disturbed among shareholders by way of ‘dividend’. In commercial usage, ‘dividend’ is the share of the Company profits distributed among the members. Under Section 2(14A) of the Companies Act, 1956, ‘dividend’ includes any interim dividend.

Section 2(*35*)of companies act 2013 “dividend” includes any interim dividend

In ***Commr. Of Income-tax v Girdhadas & Co***, it was observed that the term 'dividend' has two meanings:

1. as applied to a company which is a going concern, it ordinarily means the portion of the profits of the company which is allocated to the holders of shares in the company
2. in the case of a winding up, it means a division of the realized assets among the creditors and contributories according to their respective rights

Rules regarding dividend

1. ***Resolution at the annual general meetings***-the dividend is declared by a company by a resolution passed at the annual general meetings. The Board of directors determines the rate of dividend. The rate determined by the Board is to be sanctioned by the members of the company in general meeting. The members may reduce the rate recommended by the Board but they cannot increase it.
2. ***Payment of dividend in proportion to paid up capital (Section 93)(now section 51 of companies act 2013)*-**a company may, if authorized by its Articles, pay dividends in proportion to the amount paid up on each share. In the absence of such a clause in the Articles, members are entitled to dividend in proportion to the nominal value of the shares and not in proportion to the amounts paid thereon.

Payment of dividend in proportion to amount paid up(section 51 of companies act 2013)- A company may, if so authorised by its articles, pay dividends in proportion to the amount paid-up on each share

3. ***Dividend to be paid only out of profits(Section 205)(now 123 of companies act 2013)*-**the dividend can be declared or paid by a company for any financial year only-

(a) out of profits of the company for that year arrived at after providing for depreciation in the manner laid down in the Act, or

(b) out of the profits of the company for any previous financial year or years arrived at after providing for depreciation and remaining undistributed, or

(c) out of both, or

(d) out of moneys provided by the Central Government or a State Government for the payment of dividend in pursuance of a guarantee given by the Governmnet

Declaration of dividend(section 123 of companies act 2013)-- (*1*) No dividend shall be declared or paid by a company for any financial year except—
(*a*) out of the profits of the company for that year arrived at after providing for depreciation in accordance with the provisions of sub-section (*2*), or out of the profits of the company for any previous financial year or years arrived at after providing for depreciation in accordance with the provisions of that sub-section and remaining undistributed, or out of both; or
(*b*) out of money provided by the Central Government or a State Government for the payment of dividend by the company in pursuance of a guarantee given by that Government:
Provided that a company may, before the declaration of any dividend in any financial year, transfer such percentage of its profits for that financial year as it may consider appropriate to the reserves of the company:
Provided further that where, owing to inadequacy or absence of profits in any financial year, any company proposes to declare dividend out of the accumulated profits earned by it in previous years and transferred by the company to the reserves, such declaration of dividend shall not be made except in accordance with such rules as may be prescribed in this behalf:
Provided also that no dividend shall be declared or paid by a company from its reserves
other than free reserves
(*2*) For the purposes of clause (*a*) of sub-section (*1*), depreciation shall be provided in accordance with the provisions of Schedule II.
(*3*) The Board of Directors of a company may declare interim dividend during any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be declared:
Provided that in case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.
(*4*) The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of such dividend.
(*5*) No dividend shall be paid by a company in respect of any share therein except to the registered shareholder of such share or to his order or to his banker and shall not be payable except in cash:
Provided that nothing in this sub-section shall be deemed to prohibit the capitalization of profits or reserves of a company for the purpose of issuing fully paid-up bonus shares or paying up any amount for the time being unpaid on any shares held by the members of the company:
Provided further that any dividend payable in cash may be paid by cheque or warrant or in any electronic mode to the shareholder entitled to the payment of the dividend.
(*6*) A company which fails to comply with the provisions of sections 73 and 74 shall not, so long as such failure continues, declare any dividend on its equity shares.

4. ***Unpaid dividend to be transferred to special dividend account-(Section 205-A(sec 124 of companies act 2013)*-** where a dividend has been declared by a company but has not been paid to or claimed by any shareholder within a period of 30 days from the date of declaration, the company shall, within 7 days from the date of expiry of the 30 days, transfer the unpaid or unclaimed dividend to a special account with any scheduled bank to be called "unpaid dividend account of….company limited/company private limited"

Unpaid Dividend Account(section 124 of companies act 2013)-- (*1*) Where a dividend has been declared by a company but has not been paid or claimed within thirty days from the date of the declaration to any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the Unpaid Dividend Account.

(*2*) The company shall, within a period of ninety days of making any transfer of an amount under sub-section (*1*) to the Unpaid Dividend Account, prepare a statement containing the names, their last known addresses and the unpaid dividend to be paid to each person and place it on the website of the company, if any, and also on any other website approved by the Central Government for this purpose, in such form, manner and other particulars as may be prescribed.

(*3*) If any default is made in transferring the total amount referred to in sub-section (*1*) or any part thereof to the Unpaid Dividend Account of the company, it shall pay, from the date of such default, interest on so much of the amount as has not been transferred to the said account, at the rate of twelve per cent. per annum and the interest accruing on such amount shall enure to the benefit of the members of the company in proportion to the amount remaining unpaid to them.

(*4*) Any person claiming to be entitled to any money transferred under sub-section (*1*) to the Unpaid Dividend Account of the company may apply to the company for payment of the money claimed.
(*5*) Any money transferred to the Unpaid Dividend Account of a company in pursuance of this section which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Fund established under sub-section (*1*) of section 125 and the company shall send a statement in the prescribed form of the details of such transfer to the authority which administers the said Fund and that authority shall issue a receipt to the company as evidence of such transfer.
(*6*) All shares in respect of which unpaid or unclaimed dividend has been transferred under sub-section (*5*) shall also be transferred by the company in the name of Investor Education and Protection Fund along with a statement containing such details as may be prescribed:
Provided that any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with such procedure and on submission of such documents as may be prescribed.
(*7*) If a company fails to comply with any of the requirements of this section, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

5. If any amount remains unpaid or unclaimed for 7 years from the date of such transfer, it should be transferred to ***"Investor Education & Protection Fund"(section 125 of companies act 2013)***
6. ***Dividend to be paid to the registered shareholder-Section 206***- the dividend shall be paid only to

(a) to the registered shareholder or to his order or to his bankers,

(b) in case a share warrant has been issued, to the bearer of such warrant or to his bankers.

Right to dividend, rights shares and bonus shares to be held in abeyance pending registration of transfer of shares(section 126 of companies act 2013)-- Where any instrument of transfer of shares has been delivered to any company for registration and the transfer of such shares has not been registered by the company, it shall, notwithstanding anything contained in any other provision of this Act,—
(*a*) transfer the dividend in relation to such shares to the Unpaid Dividend Account referred to in section 124 unless the company is authorised by the registered holder of such shares in writing to pay such dividend to the transferee specified in such instrument of transfer; and

(*b*) keep in abeyance in relation to such shares, any offer of rights shares under clause (*a*) of sub-section (*1*) of section 62 and any issue of fully paid-up bonus shares in pursuance of first proviso to sub-section (*5*) of section 123.

7. ***Penalty for defaulting directors-section 207(now section 127 of companies act 2013)***-every director, who is knowingly a party to the default, is punishable with simple imprisonment up to 3 years and liable to a fine of Rs. 1000 for every day during which such default continues ad the company shall be liable to pay interest @ 18% p.a during the period of default.

Punishment for failure to distribute dividends(section 127 of companies act 2013)- Where a dividend has been declared by a company but has not been paid or the warrant in respect thereof has not been posted within thirty days from the date of declaration to any shareholder entitled to the payment of the dividend, every director of the company shall, if he is knowingly a party to the default, be punishable with imprisonment which may extend to two years and with fine which shall not be less than one thousand rupees for every day during which such default continues and the company shall be liable to pay simple interest at the rate of eighteen per cent. per annum during the period for which such default continues:
Provided that no offence under this section shall be deemed to have been committed:—
(*a*) where the dividend could not be paid by reason of the operation of any law;
(*b*) where a shareholder has given directions to the company regarding the payment of the dividend and those directions cannot be complied with and the same has been communicated to him;
(*c*) where there is a dispute regarding the right to receive the dividend;
(*d*) where the dividend has been lawfully adjusted by the company against any sum due to it from the shareholder; or
(*e*) where, for any other reason, the failure to pay the dividend or to post the warrant within the period under this section was not due to any default on the part of the company.

Q27)Debentures.(M)?

Ans--The most usual form of borrowing by a company is by the issue of debentures. According to Section 2(12)**,** 'debenture' includes debenture stock, bonds and any other securities of a company, whether constituting a charge on the assets of the company or not. Section 2(12) however does not explain as to what a debenture really is.

'Debenture' means a document which either creates a debt or acknowledges it.-***Levy v Abercorris Slate & Slab Co.***

Section 2(*30*)of companies act 2013 "debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not;

Kinds of debentures

Classification according to negotiability

1. ***Bearer debentures/unregistered debentures***-these debentures are payable to the bearer. These are regarded as negotiable instruments and are transferable by delivery and a bona fide transferee for value is not affected by the defect in the title of the prior holder.
2. ***Registered debentures***-these are debentures which are payable to the registered holders. A holder is one whose name appears both on the debenture certificate and in the company's register of debentures.

Classification according to security

1. ***Secured debentures***-debentures which create some charge on the property of the company are known as secured debentures. The charge may be a fixed charge or floating charge.
2. ***Unsecured or naked debentures***.-debentures which do not create any charge on the assets of the company are known as unsecured debentures. The holders of these debentures like ordinary unsecured creditors may sue the company for recovery of debt.

Classification according to permanence

1. ***Redeemable debentures***-debentures are usually issued on the condition that they shall be redeemed after a certain period. Such debentures are known as redeemable debentures. They may be re-issued after redemption in accordance with the provisions of Section 121**.(now section 71 of companies act 2013**)
2. ***Irredeemable or perpetual debentures***-when debentures are irredeemable, they are called perpetual debentures.

Classification according to convertibility

1. ***Convertible debentures***-these debentures give an option to the holders to convert them into preference or equity shares at stated rates of exchange, after a certain period.
2. ***Non-convertible debentures***-these debentures do not give any option to their holders to convert them into preference or equity shares. They are to be duly paid as and when they mature.

<u>Classification according to priority</u>

1. ***First debentures***-these are the debentures which are to be repaid in priority to other debentures which may be subsequently issued.
2. ***Second debentures***-these are the debentures which are to be paid after the 'first debentures' have been redeemed.

Remedies of debenture holders

The remedies of a debenture-holder of a company vary according to whether he is secured or unsecured. An unsecured debenture-holder is in exactly the same position as an ordinary trade creditor. Like any other unsecured creditor he has two remedies-

1. He may sue for his principal and interest
2. He may, if he wishes, petition under Section 439 **(now section 272 of companies act 2013**)for the winding up of the company by the Court on the ground that the company is unable to pay its debts.

A **secured debenture-holder** has both the above remedies in addition to the following-

1. ***Debenture-holder's action***-he may sue on behalf of himself and all other debenture-holders of the same class to obtain payment and enforce his security by sale. If several debenture holders sue separately, the Court can consolidate their suits into one.

2. ***Appointment of receiver***-he may appoint a receiver if the conditions which give him power to do so are fulfilled or apply to the Court in a debenture-holders' action to appoint one.

3. ***Foreclosure***-he may apply to the Court for foreclosure of the company's right to redeem the debentures. Foreclosure is a process by which the mortgagor, failing to repay the money lent on the security of property, is compelled to forfeit his right to redeem the property.

4. ***Sale***-he may sell the property charged as security if an express power to do so is contained in the terms of issue of debentures. He may also have the property sold through trustees if such power is given by the debenture trust deed.

5. ***Proof of balance***-if the company is insolvent and his security is insufficient, he may value his security and prove for the balance. In the alternative, he may surrender his security and prove for the whole amount of his debt.

Debentures(section 71 of companies act 2013)- (*1*) A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption:
Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting.
(*2*) No company shall issue any debentures carrying any voting rights.
(*3*) Secured debentures may be issued by a company subject to such terms and conditions as may be prescribed.
(*4*) Where debentures are issued by a company under this section, the company shall create a debenture redemption reserve account out of the profits of the company available for payment of dividend and the amount credited to such account shall not be utilised by the company except for the redemption of debentures.
(*5*) No company shall issue a prospectus or make an offer or invitation to the public or to its members exceeding five hundred for the subscription of its debentures, unless the company has, before such issue or offer, appointed one or more debenture trustees and the conditions governing the appointment of such trustees shall be such as may be prescribed.
(*6*) A debenture trustee shall take steps to protect the interests of the debentureholders and redress their grievances in accordance with such rules as may be prescribed.
(*7*) Any provision contained in a trust deed for securing the issue of debentures, or in any contract with the debenture-holders secured by a trust deed, shall be void in so far as it would have the effect of exempting a trustee thereof from, or indemnifying him against, any liability for breach of trust, where he fails to show the degree of care and due diligence required of him as a trustee, having regard to the provisions of the trust deed conferring on him any power, authority or discretion:
Provided that the liability of the debenture trustee shall be subject to such exemptions as may be agreed upon by a majority of debenture-holders holding not less than threefourths in value of the total debentures at a meeting held for the purpose.
(*8*) A company shall pay interest and redeem the debentures in accordance with the terms and conditions of their issue.
(*9*) Where at any time the debenture trustee comes to a conclusion that the assets of the company are insufficient or are likely to become insufficient to discharge the principal amount as and when it becomes due, the debenture trustee may file a petition before the Tribunal and the Tribunal may, after hearing the company and any other person interested in the matter, by order, impose such restrictions on the incurring of any further liabilities by the company as the Tribunal may consider necessary in the interests of the debenture-holders.
(*10*) Where a company fails to redeem the debentures on the date of their maturity or fails to pay interest on the debentures when it is due, the Tribunal may, on the application of any or all of the debenture-holders, or debenture trustee and, after hearing the parties concerned, direct, by order, the company to redeem the debentures forthwith on payment of principal and interest due thereon.
(*11*) If any default is made in complying with the order of the Tribunal under this section, every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than two lakh rupees but which may extend to five lakh rupees, or with both.
(*12*) A contract with the company to take up and pay for any debentures of the company may be enforced by a decree for specific performance.
(*13*) The Central Government may prescribe the procedure, for securing the issue of debentures, the form of debenture trust deed, the procedure for the debenture-holders to inspect the trust deed and to obtain copies thereof, quantum of debenture redemption reserve required to be created and such other matters.

Q28) ***Floating Charge(M)?***

Ans--A floating charge is an equitable charge which is created on some class of property which is constantly changing, e.g, a charge on stock-in-trade, trade debtors, etc. The company can deal in such property in the normal course of its business until the charge becomes fixed on the happening of an event. The main idea behind floating charge is to allow the company to carry on its business in the ordinary course as if no charge had been created.

Debentures usually create a floating charge on the assets of a company.

Characteristics

In Re Yorkshire Woolcombers' Ass. Ltd-

1. it is a charge on a class of assets of the company both present and future
2. that class of assets is one which, in the ordinary course of the business of the company, is changing from time to time
3. It is contemplated by the charge that, until some steps are taken by or on behalf of those interested in the charge, the company may carry on its business in the ordinary way.

Consequences of a floating charge

The company can-

1. deal in the property on which a floating chare is created, till the charge crystallizes
2. notwithstanding the floating charge, create specific mortgages of its property having priority over the floating charge
3. sell the whole of is undertaking if that is one of its objects in the Memorandum, in spite of the floating charge on the undertaking.

Crystallization-- Crystallization gets fixed when

1. the company goes into liquidation
2. the company ceases to carry on business
3. a receiver is appointed
4. a default is made in paying the principal and/or interest and the holder of the charge brings an action to enforce his security.

Q29) What are the Kinds of Share Capital?(S)

Ans--Share capital means the capital raised by a company by the issue of shares. The capital of a company may be of two kinds-

1. ***Equity share capital-***

(i) with voting rights

(ii) with differential rights as to dividend, voting or otherwise in accordance with such rules and subject to such conditions as may be prescribed.

Shares with differential rights- it means a share that is issued with differential rights in accordance with the provisions of Section 86.(**omitted in new companies act 2013)**

2. ***Preference share capital***-it means, in the case of a company limited by shares, that part of the capital of the company which carries a preferential right as to-

(a) payment of dividend during the lifetime of the company

(b) repayment of capital on winding up

Equity share capital means, with reference to a company limited by shares, all share capital which is not preference share capital. In other words it is capital which does not carry preferential right as to-

(a) payment of dividend

(b) repayment of capital on winding up.

Called-up capital-this is that part of the issued capital which has been called up on the shares.

Paid-up capital-this is that part of the issued capital which has been paid up by the shareholders or which is credited as paid-up on the shares

Uncalled capital-this is the remainder of the issued capital which has not yet been called.

Reserve capital-this is that part of the uncalled capital of a company which can be called only in the event of its winding up.

Authorized or nominal capital-This is the nominal value of the shares which a company is authorized to issue by its Memorandum of Association.

Issued or subscribed capital-issued capital is the nominal value of the shares which are offered to the public for subscription.

Q30)Bonus shares.(S)?

Ans --'Bonus' is something given in addition to what is usually or strictly due". It comes to shareholders in addition to what they get in the form of dividend. It may also be paid-

1) in case the company has surplus cash and has no use for it, or

2) by making partly paid shares as fully paid. Normally bonus is paid to the shareholders in the form of fully paid shares free of cost. This augments the resources and earning capacity of the company.

A company may be following a conservative policy of not disturbing all the profits every year accumulate large reserves over time. If the Articles so permit, it may convert a part of these reverses into share capital by issuing fully paid bonus shares to the existing shareholders. This is called capitalization of profits.

Issue of bonus shares results in capitalization of profits and reserves of the company.

Q31)Allotment of Shares.(M)?

Ans-- The capital of company is divided into certain indivisible units of a fixed amount. These units are called shares. 'Share' means share in the share capital of a company.

A share has been defined as "an interest having a money value and made up of diverse rights specified under the Articles of Association"- ***Commr of Income Tax v Standard Vaccum Oil Co. Ltd***

A share is evidenced by a share certificate. A share certificate is issued by a company under its common seal.

Each share is to be distinguished by appropriate number **(Section 83).** Each share in a company having share capital is distinguished by its appropriate number.

General principles

An effective allotment has to comply with the requirements of the law of contract relating to acceptance of an offer.

1. ***Allotment by proper authority***-an allotment must be made by a resolution of the board of directors. "Allotment is a duty primarily falling upon the directors.", and this duty cannot be delegated except in accordance with the provisions of the articles.
2. ***Within reasonable time***-allotment must be made within a reasonable period of time, otherwise the application lapses. What is reasonable time must remain a question of fact in each case. The interval of about six months between application and allotment has been held to be reasonable. On the expiry of reasonable time Section 6 of the Contract Act applies and the application must be deemed to have been revoked.
3. ***Must be communicated***-the allotment must be communicated to the applicant. Posting of a properly addressed and stamped letter of allotment is a sufficient communication even if the letter is delayed or lost in the course of post. ***Household Fire & Carriage Accident Insurance Co. v Grant*** is the leading authority.
4. ***Absolute and unconditional***-allotment must be absolute and in accordance with the terms and conditions of the applicant, if any. Thus where a person applied for 400 shares on the condition that he would be appointed cashier of a new branch of the company. He was not bound by any allotment unless he was so appointed.

   A condition which is to operate subsequently to allotment will not affect its validity. An applicant to whom shares were allotted on the condition that he would pay for them only when the company paid dividends was held to be bound even though the company had gone into liquidation before paying any dividend.

   The applicant must promptly reject the allotment when shares have been allotted to him without his condition being fulfilled. An acquiescence on his part would amount to a waiver of the condition.

Q32)Reduction of Capital.(M)?

Ans -- The law regards the capital of a country as something sacred. The general principle of law founded on principles of public policy and rigidly enforced by Courts is that no action resulting in a reduction of capital of a company should be permitted unless the reduction is effected-

(a) under statutory authority or by forfeiture

(b) in strict accordance with the procedure, if any, laid down in that behalf in the Articles of Association. Any reduction of capital contrary to this principle is illegal and ultra vires.

<u>Reduction of capital with the consent of the court</u>

1. It may extinguish or reduce the liability on any of its shares in respect of share capital not paid-up
2. It may, either with or without extinguishing or reducing liability on any of its shares, cancel any paid-up share capital which is lost, or is unrepresented by available assets.
3. It may, either with or without extinguishing or reducing liability on any of its shares, pay off any paid-up share capital which is in excess of the wants of the company.

<u>Procedure for reduction of share capital</u>

1. ***<u>Special resolution-Section 100(now section 66 of companies act 2013)</u>***- a company shall first pass a special resolution for reduction of capital. Power to reduce capital must be granted in the Articles of the company. If the Articles do not grant such power, they may be altered by a special resolution giving such power.
2. ***<u>Application to the Court-Section 101</u>***-***<u>(now section 66 of companies act 2013)</u>***the company shall then apply to the Court by petition for an order confirming the reduction.
3. ***<u>Registration of order of Court with Registrar-Section 103(now section 66 of companies act 2013)</u>***- the order of the Court confirming the reduction shall be

produced before the Registrar and a certified copy thereof shall be filed with him for registration. With such a copy shall also be filed a minute, showing with respect to the share capital of the company as altered by the order.

Reduction of share capital(section 66 of companies act 2013)- (*1*) Subject to confirmation by the Tribunal on an application by the company, a company limited by shares or limited by guarantee and having a share capital may, by a special resolution, reduce the share capital in any manner and in particular, may—
(*a*) extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or
(*b*) either with or without extinguishing or reducing liability on any of its shares,—
(*i*) cancel any paid-up share capital which is lost or is unrepresented by available assets; or
(*ii*) pay off any paid-up share capital which is in excess of the wants of the company,
alter its memorandum by reducing the amount of its share capital and of its shares accordingly:
Provided that no such reduction shall be made if the company is in arrears in the repayment of any deposits accepted by it, either before or after the commencement of this Act, or the interest payable thereon.
(*2*) The Tribunal shall give notice of every application made to it under sub-section
(*1*) to the Central Government, Registrar and to the Securities and Exchange Board, in the case of listed companies, and the creditors of the company and shall take into consideration the representations, if any, made to it by that Government, Registrar, the Securities and Exchange Board and the creditors within a period of three months from the date of receipt of the notice:
Provided that where no representation has been received from the Central Government, Registrar, the Securities and Exchange Board or the creditors within the said period, it shall be presumed that they have no objection to the reduction.
(*3*) The Tribunal may, if it is satisfied that the debt or claim of every creditor of the company has been discharged or determined or has been secured or his consent is obtained, make an order confirming the reduction of share capital on such terms and conditions as it deems fit:
Provided that no application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such reduction is in conformity with the accounting standards specified in section 133 or any other provision of this Act and a certificate to that effect by the company's auditor has been filed with the Tribunal.
(*4*) The order of confirmation of the reduction of share capital by the Tribunal under sub-section (*3*) shall be published by the company in such manner as the Tribunal may direct.
(*5*) The company shall deliver a certified copy of the order of the Tribunal under subsection (*3*) and of a minute approved by the Tribunal showing—
(*a*) the amount of share capital;
(*b*) the number of shares into which it is to be divided;
(*c*) the amount of each share; and
(*d*) the amount, if any, at the date of registration deemed to be paid-up on each share, to the Registrar within thirty days of the receipt of the copy of the order, who shall register the same and issue a certificate to that effect.
(*6*) Nothing in this section shall apply to buy-back of its own securities by a company under section 68.
(*7*) A member of the company, past or present, shall not be liable to any call or contribution in respect of any share held by him exceeding the amount of difference, if any, between the amount paid on the share, or reduced amount, if any, which is to be deemed to have been paid thereon, as the case may be, and the amount of the share as fixed by the order of reduction.
(*8*) Where the name of any creditor entitled to object to the reduction of share capital under this section is, by reason of his ignorance of the proceedings for reduction or of their nature and effect with respect to his debt or claim, not entered on the list of creditors, and after such reduction, the company is unable, within the meaning of sub-section (*2*) of section 271, to pay the amount of his debt or claim,—
(*a*) every person, who was a member of the company on the date of the registration of the order for reduction by the Registrar, shall be liable to contribute to the payment of that debt or claim, an amount not exceeding the amount which he would have been liable to contribute if the company had commenced winding up on the day immediately before the said date; and
(*b*) if the company is wound up, the Tribunal may, on the application of any such creditor and proof of his ignorance as aforesaid, if it thinks fit, settle a list of persons so liable to contribute, and make and enforce calls and orders on the contributories settled on the list, as if they were ordinary contributories in a winding up.

(*9*) Nothing in sub-section (*8*) shall affect the rights of the contributories among themselves.
(*10*) If any officer of the company—
(*a*) knowingly conceals the name of any creditor entitled to object to the reduction;
(*b*) knowingly misrepresents the nature or amount of the debt or claim of any creditor; or
(*c*) abets or is privy to any such concealment or misrepresentation as aforesaid, he shall be liable under section 447.
(*11*) If a company fails to comply with the provisions of sub-section (*4*), it shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees.

Reduction of capital without the sanction of the Court

1. ***Forfeiture of shares***-the company may, if authorized by its Articles, forfeit shares for non-payment of calls. This results in reduction of capital if the forfeited shares are not re-issued
2. ***Surrender of shares***-the company may accept surrender of partly paid shares to save it from going through the formalities of forfeiture.
3. ***Cancellation of shares***-the company may, if so authorized by its Articles, cancel shares which have not been taken or agreed to be taken by any person and diminish the amount of its share capital by the amount of the shares so cancelled.
4. ***Purchase of the shares by the company under Section 402(b)(now under section 242 0f companies act 2013)(powers of tribunal)not yet notified by MCA***-the Court may order the purchase of the shares of any members of the company by the company.
5. ***Redemption of redeemable shares***-the company may redeem redeemable preference shares in accordance with the provisions of Section 80(**now section55 of companies act 2013)**

Buy-back of shares-a company may purchase its own shares, subject to fulfillment of conditions laid down in Section 79-A (2),purchase its**(now section 68 of companies act 2013)**

Q33)--Diffrence between transfer or transmission of shares ?

Ans--Transfer of shares

1) It is a deliberate act of the holder

2) It requires exception of an instrument of transfer

3) Stamp duty is payable on its execution

Transmission of shares

1) It results by operation of law

2) It requires an evidence showing the entitlements of the transferee

3) No stamp duty is payable in this case

Question 34) –what Is DIN number?

Ans-Section 153 to 159 of companies act 2013

Application for allotment of Director Identification Number.(section 153)-- Every individual intending to be appointed as director of a company shall make an application for allotment of Director Identification Number to the Central Government in such form and manner and along with such fees as may be prescribed.

Allotment of Director Identification Number.(section 154)-- The Central Government shall, within one month from the receipt of the application under section 153, allot a Director Identification Number to an applicant in such manner as
may be prescribed.

Prohibition to obtain more than one Director Identification Number(section 155)-- No individual, who has already been allotted a Director Identification Number under section 154, shall apply for, obtain or possess another Director Identification Number

Director to intimate Director Identification Number(section 156)- Every existing director shall, within one month of the receipt of Director Identification Number from the Central Government, intimate his Director Identification Numberto the company or all companies wherein he is a director.

Company to inform Director Identification Number to Registrar.(section 157)--- (*1*) Every company shall, within fifteen days of the receipt of intimation under section 156, furnish the Director Identification Number of all its directors to the Registrar or any other officer or authority as may be specified by the Central Government with such fees as may be prescribed or with such additional fees as may be prescribed within the time specified under section 403 and every such intimation shall be furnished in such form and manner as may be prescribed.

(*2*) If a company fails to furnish Director Identification Number under sub-section (*1*), before the expiry of the period specified under section 403 with additional fee, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

Obligation to indicate Director Identification Number(section 158)-- Every person or company, while furnishing any return, information or particulars as are required to be furnished under this Act, shall mention the Director Identification Number in such return, information or particulars in case such return, information or particulars relate to the director or contain any reference of any director

Punishment for contravention(section 159)--- If any individual or director of a company, contravenes any of the provisions of section 152, section 155 and section 156, 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 fifty thousand rupees and where the contravention is a continuing one, with a further fine which may extend to five hundred rupees for every day after the first during which the contravention continues.

Question35)—Buy back of shares ?

Ans—Sources to buy back: ***[Section 77A] of companies act 1956***
(i) Its free reserves; or
(ii) The Security premium account or
(iii) The proceeds of any shares or other specified securities.

No buy-back of any shares or specified securities salary made out of proceeds of earlier issue of the same kinds of share or specified securities.

Conditions for Buy-back
(i) The buy-back is Authorised by its Articles;
(ii) A special resolution. Provided no special resolution is necessary if :

(a) The buy-back is or less than ten percent of the total paid-up equity capital and free reserves of the company; and

(b) Such buy-back has been authroised by the board by means of a resolution passed at its meeting.
(iii) The buy-back is **upto 25%** of the total paid up capital and free reserve. However, in case of equity shares, it may be noted that it **cannot exceed 25%** of the total paid equity capital in that financial year.
(iv) The ratio of the debt owed by the company is not more than twice the capital and its free reserves after such buy-back. However the central government may prescribe a higher ratio.
(v) All the shares or other specified securities are fully paid up
(vi) The buy-back of listed securities is in accordance with the regulations made by the SEBI.
(vii) The buy-back in respect of shares not listed on recognised stock exchange is in accordance with the guidelines as may be prescribed.
(viii) Every buy-back shall be completed within twelve months form the date of passing the special resolution under clause.
The buy-back under sub-Section (1) may be –
(a) Form the exiting security holders on proportionate basis; or
(b) From the open market or
(c) From employees
(d) It shall extinguish and physically destroy the securities so bought-back within seven days of the last date of completion of buy back.
(ix) It shall not make further issue of same class of share or specified securities within six month except. Bonus issue sweat equity, stock option scheme conversion of pref. share debenture into equity share.

Prohibition for buy-back in certain circumstance ***[Section 77 B of companies act 2013]***
(i) Through any subsidiary company including its own subsidiary companies or
(ii) Through any investment company or group of investment Companies; or
(iii) If a default in repayment of deposit or interest thereon, redemption of debentures or preference shares or payment of dividend or repayment of a term loan or interest thereon.
(iv) In case it has not complied with provisions of ***Section 159, 207, 211***.

However in the following not taken to have purchased is shares when it has.
(a) Redeemed its redeemable preference shares,
(b) Forfeited its shares for non-payment of calls or
(c) Accepted a valid surrender of shares-

Power of company to purchase its Own securities(section 68 of companies act 2013)-- (*1*) Notwithstanding anything contained in this Act, but subject to the provisions of sub-section (*2*), a company may purchase its own shares or other specified securities (hereinafter referred to as buy-back) out of—
(*a*) its free reserves;
(*b*) the securities premium account; or
(*c*) the proceeds of the issue of any shares or other specified securities:
Provided that no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.
(*2*) No company shall purchase its own shares or other specified securities under sub-section (*1*), unless—
(*a*) the buy-back is authorised by its articles;
(*b*) a special resolution has been passed at a general meeting of the company authorising the buy-back:
Provided that nothing contained in this clause shall apply to a case where—
(*i*) the buy-back is, ten per cent. or less of the total paid-up equity capital and free reserves of the company; and
(*ii*) such buy-back has been authorised by the Board by means of a resolution passed at its meeting;
(*c*) the buy-back is twenty-five per cent. or less of the aggregate of paid-up capital and free reserves of the company:
Provided that in respect of the buy-back of equity shares in any financial year, the reference to twenty-five per cent. in this clause shall be construed with respect to its total paid-up equity capital in that financial year;
(*d*) the ratio of the aggregate of secured and unsecured debts owed by the company after buy-back is not more than twice the paid-up capital and its free reserves:
Provided that the Central Government may, by order, notify a higher ratio of the debt to capital and free reserves for a class or classes of companies;
(*e*) all the shares or other specified securities for buy-back are fully paid-up;
(*f*) the buy-back of the shares or other specified securities listed on any recognized stock exchange is in accordance with the regulations made by the Securities and Exchange Board in this behalf; and
(*g*) the buy-back in respect of shares or other specified securities other than those specified in clause (*f*) is in accordance with such rules as may be prescribed:
Provided that no offer of buy-back under this sub-section shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back, if any.
(*3*) The notice of the meeting at which the special resolution is proposed to be passed under clause (*b*) of sub-section (*2*) shall be accompanied by an explanatory statement stating—
(*a*) a full and complete disclosure of all material facts;
(*b*) the necessity for the buy-back;
(*c*) the class of shares or securities intended to be purchased under the buy-back;
(*d*) the amount to be invested under the buy-back; and
(*e*) the time-limit for completion of buy-back.
(*4*) Every buy-back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board under clause (*b*) of sub-section (*2*).
(*5*) The buy-back under sub-section (*1*) may be—
(*a*) from the existing shareholders or security holders on a proportionate basis;
(*b*) from the open market;
(*c*) by purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.
(*6*) Where a company proposes to buy-back its own shares or other specified securities under this section in pursuance of a special resolution under clause (*b*) of sub-section (*2*) or a resolution under item (*ii*) of the proviso thereto, it shall, before making such buy-back, file with the Registrar and the Securities and Exchange Board, a declaration of solvency signed by at least two directors of the company, one of whom shall be the managing director, if any, in such form as may be prescribed and verified by an affidavit to the effect that the Board of Directors of the company has made a full inquiry into the affairs of the company as a result of which they have formed an opinion that it is capable of meeting its liabilities and will not be rendered insolvent within a period of one year from the date of declaration adopted by the Board:
Provided that no declaration of solvency shall be filed with the Securities and Exchange Board by a company whose shares are not listed on any recognised stock exchange.
(*7*) Where a company buys back its own shares or other specified securities, it shall extinguish and physically destroy the shares or securities so bought back within seven days of the last date of completion of buy-back.

(*8*) Where a company completes a buy-back of its shares or other specified securities under this section, it shall not make a further issue of the same kind of shares or other securities including allotment of new shares under clause (*a*) of sub-section (*1*) of section 62 or other specified securities within a period of six months except by way of a bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares.
(*9*) Where a company buys back its shares or other specified securities under this section, it shall maintain a register of the shares or securities so bought, the consideration paid for the shares or securities bought back, the date of cancellation of shares or securities, the date of extinguishing and physically destroying the shares or securities and such other particulars as may be prescribed.
(*10*) A company shall, after the completion of the buy-back under this section, file with the Registrar and the Securities and Exchange Board a return containing such particulars relating to the buy-back within thirty days of such completion, as may be prescribed:
Provided that no return shall be filed with the Securities and Exchange Board by a company whose shares are not listed on any recognised stock exchange.
(*11*) If a company makes any default in complying with the provisions of this section or any regulation made by the Securities and Exchange Board, for the purposes of clause (*f*) of sub-section (*2*), the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees, or with both.
Explanation I.—For the purposes of this section and section 70, "specified securities" includes employees' stock option or other securities as may be notified by the Central Government from time to time.
***Explanation II*.—**For the purposes of this section, "free reserves" includes securities premium account.

Question36) –Winding up of companies?

Ans--A company is an artificial person created by a legal process known as incorporation. Its existence is distinct from that of the members who compose it. Therefore, events affecting individual members such as death, lunacy or insolvency etc. do not affect the existence of a company and it continues until its dissolution is brought about by any of the following methods:
1. By removal of the name of the company from the Register when it becomes a defunct company. (Sec. 248).
2. By an order of the Court, without winding up, under a scheme of arrangement as provided by Sections 241 of the Companies Act, 2013.
3. By winding up when the purpose of the company has been accomplished or may have become impossible or in the event of insolvency or liquidation of the company.

Meaning of winding up

Winding up is a term commonly associated with the ending of a company's existence. In fact, winding up' is a process by which the assets of the company are . collected and realised, its liabilities are discharged and the net surplus, if any, is distributed in accordance with the company's articles of association

Winding up Distinguished from Insolvency

Winding up of a company differs from insolvency of an individual inasmuch as a company cannot be made insolvent under the Insolvency Act. In other words, a company can never be adjudged insolvent, even though it is unable to pay its debt; it can only be wound up. The main points of difference between insolvency of an individual or a firm and winding up of a company **may be stated below**:
1. In the case of insolvency, the whole of the property of the insolvent is taken out of his hands and vests in the court under the Provincial Insolvency Act or in the Official Assignee under the Presidency Towns Act. On the other hand, in case of winding up, the property remains in the company subject to its being administered for the purposes of winding up. The legal death of the company takes place when it is formally dissolved.

2. In the case of insolvency of an individual, the administration of his property by the Official Assignee or the Official Receiver occurs only if he is declared insolvent by the court. But the assumption of director's powers by the liquidator occurs even if the company is fully solvent.

<u>Winding up [Section 270]</u>

The Companies Act, 1956 had prescribed three modes of winding up of a company, namely, (i) by Court, (ii) under Supervision of the Court, and (iii) voluntary winding up, which may be (a) Member's voluntary winding up or (b) Creditor's voluntary winding up.
However, the Companies Act, 2013 prescribes only two modes of winding up :
(i) Winding up by the Tribunal; and
(ii) Voluntary winding up.
The Act of 2013 does not acknowledge the distinction between member's voluntary Winding up and creditor's voluntary winding up.

1. Winding up by Tribunal [Section 271]
The compulsory winding up of a company which is also called winding up by the Tribunal, is initiated by an application by way of petition to the Tribunal for a winding Up order.
The circumstances under which a company may be wound up by the Tribunal are stated in Section 271 of the Companies Act, 2013. They are as follows:
(a) Inability to Pay Debts [Section 271 (a)]
A company may be ordered to be wound up if it is unable to pay its debts. The expression "unable to pay debts" has to be taken in commercial sense of being unable to meet current demands though the company may be otherwise solvent.'
Section 271 further provides that a company is deemed unable to pay its debts if a creditor for an amount exceeding one lakh rupees does not get his money within twenty-one days after it fell due, and the creditor is entitled to make a petition to the Tribunal for an order of winding up of the company. The debt must, however, be really due and not under dispute.
Thus, where a financially sound company disputed the claim on *bona fide* grounds, that was held not to be a neglect to pay and the Court (now Tribunal) refused to make an order for winding up of the company."
In ***Krishnamsetty Basav Rao* v. *Kubashi Machine Tools (P) ltd,*** the Andhra Pradesh High Court (now Tribunal) held that order of winding up besides being discretionary, has to be resorted as a last measure when it is in the interest of not only the company but also public. In the instant case, the Court (now Tribunal) declined to exercise such discretion in favour of petitioners, who had come up before the Court (now Tribunal) with ulterior motive and not in the industrial unit, and were seeking winding up of the unit.
From the foregoing analysis, it may be summed that inability to pay debts on the part of the company is usual ground for filing the petition for winding up of a company. However, every debt cannot be a ground for winding up of a company. A company may be wound up on the ground of being unable to pay its debts only when the following conditions exist:
(a) the amount of debt exceeds one lakh rupees;
(b) the sum must be definite, presently payable and there should be no *bona fide* dispute about the debt;
(c) the creditor makes a written demand of payment;
(d) the demand is signed by the creditor or his agent or legal adviser duly authorised on this behalf;
(e) the demand has been served by causing it to be delivered at the registered office by registered post or otherwise; and
f) the company must have neglected to pay the demanded sum or to secure or compound the same to the satisfaction of the creditor for three weeks.
(b) Special Resolution [Section 271 (b)]

A company may be wound up by an order of the Tribunal if a special resolution for its winding up has been passed by the company. The Tribunal is, however, not bound to order winding up simply because the company has so resolved. I The power of the Tribunal being discretionary, it may not be exercised if the winding up is opposed to the public interest or the interests of the company. It must, however, be pointed out that winding up by a special resolution is not a common occurrence because of the fact that companies generally have a very large number of shareholders and if they want the company to be wound up, they would prefer its voluntary winding up which is comparatively cheaper and less time-consuming. It is quite often noticed that companies which are in very bad financial position and confronted with the problems of income-tax or sales-tax defaults, protracted litigation with creditors and prosecution by Registrar of Companies etc., prefer compulsory winding up by the Tribunal by passing special resolution so that all these problems are passed on to the Official Liquidator and the Company's burden is considerably reduced.

(c) Where company has acted against National Interest [Section 271 (c)]

The Tribunal has power under Section 271 (c) of the Companies Act, 2013 if it is found that the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign states, public order, decency or morality.

(d) Winding up of Sick Companies [Section 271 (d)]

Where on demand by more than fifty per cent of secured creditors apply to the tribunal for winding up of the company 'with relevant evidence for its failure to offer security, or compound it, the Tribunal may pass an order for winding up of the company under Chapter XIX of the Companies Act, 2013, which relates to revival and Rehabilitation of Sick Companies.

(e)Winding up on application made by Registrar [Section 271 (e)]

If an application made by the Registrar of Companies of (ROC) or any other person authorised by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of a company have been conducted in a fraudulent manner or the company has been formed for a fraudulent or unlawful purpose or persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company may be wound up. •

(f) Default of company in filing with Registrar its financial statement etc. [Section 271 (f)]

Where the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive years, the Tribunal may order winding up the company. Where a company has not commenced its business within one year from the date of its incorporation, or has suspended its business for a whole year, it may be ordered to be wound up. The power of the Tribunal being discretionary, it will not be exercised unless there are indications that the company has no intention to commence or continue its business. If the suspension of business is due to some temporary or unavoidable reason, the Tribunal may refuse to order winding up. Again, the petition for winding up would Not be allowed if the delay in commencement or suspension or interruption of business is duly explained and the Tribunal is satisfied that the business could not be commenced or resumed for a valid reason.

The case of ***Murlidhar* v. *Bengal Steamship Co.,,*** is an illustration on this point.-- In this case, the company employed a steamer and two flats to carryon its business. These two flats were acquired by the Government during the First World War and the company could not replace them due to hike in prices. As a result of this, the company's business remained suspended for more than a year and a petition for winding up was brought against the company. The Court (now Tribunal) refused to order winding up on the ground that the suspension of business for a whole year was sufficiently accounted for and gave no indication that the company had no intention to carryon the business.

(g) 'Just and Equitable' cause

Section 271 (I) (g) of the Companies Act, 2013 provides that the Tri bunal can order winding up of a company when the Tribunal is of the opinion that it is just and equitable that the company should be wound up. It is the remedy of the last resort.? In this case, the Tribunal has wide powers and has a complete discretion to decide when it is "just and equitable" to order winding up of a company. The discretionary authority of the Tribunal even enables it to subject the exercise of legal rights to equitable considerations.

The expression, "just and equitable" is general in nature and it is undesirable to attempt to define the circumstances in which it will apply.' Thus, in ***Mohanlal Dhanjibhai Mehta* v. *Chunilal B. Mehta;"*** the Gujarat High Court expressed its unwillingness to order winding up when it was found that the majority of shareholders did not want the company to be wound up. The Court observed that the disputes of internal character such as distribution of properties of family concern, cannot be allowed to be pursued through winding up petitions. In short, the powers under this clause are to be exercised with great care and circumspection.

Referring to the 'just and equitable' clause in relation to the discretionary power of the Tribunal in ordering winding up of a company, Lord Wilberforce in ***Ebrahimi* v. *Westbourne Gallaries Ltd.* & *others...*** observed that, "the general words of the sub-section should remain general and not be reduced to the sum of particular instances." The discretion of the Tribunal under this clause is very wide and the courts have exercised this discretion on a variety of grounds which may be generalised in the following categories:

(i) Deadlock in the management of a company.-Where there is a complete deadlock in the management of the company, the Tribunal may order winding up on just and equitable ground. The case **In Re *Yenidje Tobacco Co. Ltd.,*** I is an illustration on this point.

In the instant case, two cigarette manufacturers Wand R who were trading separately, agreed to amalgamate their business by forming a private limited company of which they were the only shareholders and directors. They had equal voting rights and therefore their disputes were to be resolved by arbitration, but one of them dissented from the award. They became so hostile that they were not even on speaking terms with each other. Thus there was a complete deadlock and, therefore, the company was ordered to be wound up although its business was flourishing well

(ii) Where the company has lost its substratum.- The substratum of a company is deemed to have been lost where:

(a) subject-matter of the company is gone; or

(b) the main object for which the company was formed failed to materialise ; or

(c) it is impossible to carryon the business of the company except at a loss; or

(d) the existing and possible future assets are insufficient to meet the liabilities of the company.

The Supreme Court in ***Seth Mohan Lal* v. *Grain Chambers ltd.*** refused to order winding up of the company whose business had badly been paralysed and virtually came to a stand-still due to long drawn litigation and a part of the business was banned by the legislation. The Court held that it could not direct winding up of the company as it could always restart its business with assets it possessed.

(iii) Mismanagement & Losses.-The Tribunal is justified in ordering winding up of a company under the "just and equitable" clause where it is not possible for the company to carryon business except at losses and there are no prospects of achieving profits. J However, mere apprehension of losses on the part of shareholders is no ground for winding up under this clause.

It was held in ***Vijay Laxmi Talkies v, Kotilingeswara.*** -- that where a company is not able to payoff its debts and its amount of interest is constantly increasing and consequently it is leading towards financial crisis. and there is no possibility of improvement in its financial condition, it could be wound up by the Tribunal on just and equitable ground,

In ***Vanaspati Industries Ltd.* v. *Prabhu Dayal Hari Ram,*** the Court (now Tribunal) ordered winding up of the company on the ground that it had no reasonable hope of trading at a profit and had not enough credit in the market to pay its employees.

(iv) Oppression of minority shareholders by the majority.-It would be just and equitable on the part of the Tribunal to order winding up of a company where majority shareholders have adopted oppressive or squeezing policy towards the minority shareholders. Thus, in ***R. Sabapathy Rao* v. *Sabapathi Press ltd.*** the Court (now Tribunal) was justified in ordering winding .up on the ground of oppressive tactics adopted by the directors representing majority shareholders against the minority of shareholders. In this case, directors of' the company exerted dominating influence on the management and the managing director which was oppressive to minority of shareholders. They retained profits of the business between members of the family and did not send copy of balance sheet to the shareholders nor was the auditor's report read at the general meeting. The dividend were also not regularly paid and the rate of dividend was constantly falling. Under these circumstances, there was a just and equitable ground to order winding up of the company by the Court (Tribunal),

(v) Fraudulent or illegal purpose.-Where a company has been conceived or brought into existence fraudulently for some illegal purposes it is just and equitable to order its winding up. Thus, in ***Universal Mutual Aid* & *Poor Houses Association* v. *A.D. Thippa Naidu.*.** the main object of the company was conduct of a lottery, therefore, the mere fact that some of its objects were philanthropic was not a sufficient ground to prevent the company being wound up as it was mainly formed for an illegal purpose.

(vi) Where a private company is in essence a partnership.-Where it is proved that an incorporated private company is in substance a partnership, it may be ordered to be wound up when there is abuse of power or breach of good faith which the partner's owe to each other. The decision In **Re *American Pioneer Leather CO.,*** may be cited as an illustration. In this case, the articles of a small private company consisting of only three members two of whom were directors, provided that any member willing to withdraw would offer his interest to other members and if the members refuse to purchase the shares, he would be entitled to have the company wound up. The company was accordingly ordered to be wound up when the other members refused to purchase the shares of the petitioner.

Who may file petition for Winding up [Section 272(2)]

Section 272 (I) of the Companies Act, 2013 provides that a petition for the winding up of a company may be presented to the Tribunal by any of the following :-

(a) the company; or
(b) any creditor or creditors including any contingent or prospective creditor or creditors; or
(c) any contributory or contributories; or
(d) all or any of the above parties, whether together or separately; or
(e) the Registrar of Companies; or
(f) in a case falling under Section 224 *i.e.,* application for winding up following an investigation, by any person authorised by the Central Government in that behalf; or
(g) where a compnay is already under voluntary liquidation or under winding up by the Tribunal, and such voluntary winding up cannot be continued with due regard to the interests of the creditors or contributories or both, the petition for an order of its winding up may be presented by any of the persons mentioned above or by the Official Liquidator as provided in Section 272 of the Companies Act, 2013.

Powers of Tribunal [Section 273]

On receipt of a petition for winding up of a company under Section 272, the Tribunal may pass any of the following orders, namely :-

(I) (a) dismiss the petition with costs; or
(b) make any interim order as it deems necessary; or
(c) appoint a Provisional Liquidator of the company till the making up of a winding up order; or
(d) any other order as it thinks fit.
Any of such order shall be made by the Tribunal within 90 days from the date of presentation of the petition.

In case the Tribunal orders the appointment of a Provisional Liquidator, it has to give a notice to the company and afford a reasonable opportunity to it to make its representation before passing of such order, unless for special reasons to be recorded in writing, the Tribunal thinks it fit to dispense with such notice.!

II. VOLUNTARY WINDING UP

Voluntary winding up is different from compulsory winding up. In voluntary winding up, the members of the company may, instead of presenting a petition to the Tribunal for winding up of the company, pass a resolution in the general meeting that the company be wound up. The main advantage of a voluntary winding up is that the company and its creditors shall be left free to settle their affairs amicably without coming to the Tribunal. They may, however. apply to the Tribunal for directions or order- if necessary.

The winding up of a company by Tribunal is usually the result of hostile action by a creditor or sometimes a contributory whereas voluntary winding up is the act of company itself. Voluntary winding up may become necessary for a company when it desires to reconstruct itself by forming a new company or amalgamate its business with another company.

Resolutions for Voluntary Winding Up [Section 304]

Section 304 of the Companies Act, 2013 provides that a company may be voluntarily wound up in any of the following two manners, namely:

(a) By Ordinary Resolution

A company is voluntarily wound up by passing an ordinary resolution under Section 304 (a) in its general meeting when the period fixed for the duration of the company by the articles has expired, or an event on the occurrence of which the articles provide that the company would be dissolved, has occurred. The company can commence its voluntary winding up after an ordinary resolution to this effect has been passed in the general meeting.

(b) By Special Resolution

The articles of the company usually do not contain any provision as to the duration of the company, or the mention of an event on the happening of which the company is to be dissolved. Therefore, in absence of any such provision in the articles, a special resolution is necessary if the company decides its winding up voluntarily. For instance, if the company is unable to carry on its business because of its liabilities or it wants to reconstruct itself by forming a new company, a special resolution for its voluntary winding up would be necessary. 1 The winding up commences at the time when the special resolution has been passed by the company in its general meeting.? The date of commencement is not altered by a supervision order or a compulsory winding order subsequently being made by the Tribunal.

Publication of Resolution

After the company has passed a resolution for winding up, it must, within fourteen days of the passing of the resolution, give notice of the resolution by advertisement in the Official Gazette and also in some newspaper circulating in the district where the registered office of the company is situated.' In case of default in publication of the resolution, the company and every defaulting officer shall be punishable with a fine which may extend upto five thousand rupees for every day during where such default continues."

Effect of Voluntary Winding Up

According to Section 309 of the Companies Act, 2013 the corporate status and powers of the company shall continue until it is finally dissolved, but it must stop to carryon its business except so far as may be necessary for beneficial winding up.>
All invoices, papers, business letters etc. must contain a specific mention that-the company is being wound Up. Other effects of voluntary winding up are as follows:

1. A Company Liquidator or liquidators must be appointed to take necessary steps to effect the final dissolution of the company.'
2. The transfer of shares and any alteration in the status of members, made after the commencement of winding up, shall be void unless sanctioned by the Company Liquidator.?

3. Where the winding up is on the ground of insolvency, the employees of the company are *ipso facto* dismissed, but where the company is solvent and is being voluntarily wound up for the purpose of amalgamation, the employees are not automatically so dismissed.'
4. The powers of directors cease except with the sanction of the liquidator, creditors or committee of inspection. The directors must, however, give notice of appointment of a Company Liquidator to the Registrar in case of member's voluntary winding Up.
5. The assets of the company are used in satisfying the liabilities *pari passu* except that certain preferential debts must be paid first, and secured creditors may have recourse to their securities.

Modes of Voluntary Winding Up

The Companies Act, 2013 does not make a distinction between Member's voluntary winding and creditor's voluntary winding up which was recognized under the preceding Companies Act, 1956. The voluntary winding up, whether by the members or the creditors of the company, is covered under Sections 305 and 306 of the Companies Act, 2013 respectively.
Under the Companies Act, 1956, before resolution for voluntary winding up was passed, the company, it had to decide whether the winding up will be Member's or Creditor's. Where the directors of the company were able to make a "Declaration of Solvency", the winding up was known as Members' Voluntary Winding up. But where they were not able to do so, the winding up was said to be Creditor's winding up.5 Thus, the main distinction between these two types of voluntary winding up depended upon the solvency or otherwise of the company at the time of taking decision about winding up by passing a resolution.

Declaration of Solvency [Section 305]

Section 305 of the Companies Act, 2013 provides that where it is proposed to wind up a company voluntarily, the directors, or in case the company has more than two directors, the majority of them, may, at a meeting of the Board, make a declaration commonly known as 'Declaration of Solvency', verified by an affidavit, to the effect that they have made a full inquiry into the affairs of the company, and that it will be able to pay its debts in full from the proceeds of assets sold in voluntary winding up
The provisions applicable to members' voluntary winding up are contained in Sections 310 to 318 of the Companies Act, 2013. They are briefly as follows:

1. Appointment of Company Liquidator [Section 310]

When a declaration of solvency has been effectively made, the company in its general meeting appoints a Company Liquidator from the panel prepared by the Central Govt. for the purpose and his remuneration is fixed.> More than one Liquidators may also be appointed by the company.
On appointment as Company Liquidator, such Liquidator shall file a declaration in the presc.ibed form within seven days of the date of appointment disclosing conflicts of interest or lack of independence in respect of his appointment, if any, with the company and the creditors and such obligation shall continue throughout the term of his appointment.

2. Board's power to cease on appointment of a Liquidator [Section 313]

On appointment of the liquidator, all the powers of the Board of Directors and managing or whole time Director and Manager shall cease except for the propose of giving notice of appointment of the Company Liquidator to the Registrar.'

3. liquidator's power to sell company's business or property

Generally, the Company Liquidator sells the undertaking and all the property of the company for cash which is then distributed among the creditors and members. But sometimes he sells them for shares in another company so that members instead of receiving their capital and any surplus assets in the form of cash-money, become shareholders of that another company. This forms. the basis of reconstruction of the company during liquidation. The interests of the dissenting members, if any, can be purchased by the Liquidator at a price to be determined by agreement or by arbitration. If the Liquidator decides to purchase the shares of the dissenting shareholders, then the purchase money must be paid before the company is dissolved.

4. Powers and Duties of Company Liquidator in Voluntary winding up [Section 314]

Where the company is being wound up by the resolution passed by the members of the company, the Liquidator appointed by the company has an important role to play in various steps of such winding up. The Companies Act, 2013 has assigned him powers and duties as provided under Section 314 of the Act. These are stated as follows :-

(1) The Company Liquidator shall perform such functions and discharge such duties as may be determined from time to time by the company in case of members winding up (or creditors in case of creditors' winding up).

(2) He shall settle the list of contributories, which shall be *prima facie* evidence of the liability of the persons named therein as contributories,

(3) He shall maintain regular and proper books of account as may be prescribed and file statement of account within 30 days from the close of each quarter year with the Registrar. Any default in non-compliance with this provision will make the Company Liquidator liable to punishable with fine which may extend to five thousand rupees for every day during which the failure continues

(4) The members, creditors and officers of the Central Government may inspect such companies book of account at reasonable time.

(5) The Company Liquidator shall pay the debts of the company and shall adjust against the rights of contributories among themselves.

For non-compliance with the above provisions as contained in Section 314 of the Act, the Company Liquidator, except under item 3 mentioned above, shall be punishable with fine which may extend to ten lakh rupees.!

5. Company's General Meeting

Where the liquidation continues for more than one year, the Liquidator must call a general meeting of the company at the end of the first year and at the end of each subsequent years. He must lay before this meeting an account of his acts and dealings and progress report of winding up proceedings during the year, together with a statement giving therein the prescribed particulars relating to the proceedings of the winding up.

6. Final Meeting and Dissolution of Company [Section 318]

Section 318 of the Companies Act, 2013 provides that when the affairs of the company are fully wound up, the Company Liquidator must make an account of the winding up showing how the winding up has been conducted and the property of the company has been disposed. He must then call a general meeting by advertisement in the Official Gazette and in a local newspaper circulating in the district in which the registered office of the company is situated, specifying the time, place and object of the meeting.

The publication of meeting must be done at least one month before the date of meeting. The Liquidator must lay the account before the meeting. Within one week after the meeting, the Company Liquidator should send a copy of accounts and a return of the meeting to the Registrar and the Official Liquidator. Where no quorum was present at the meeting, he must file a return stating this fact. The Registrar of Companies must register the account and the return.

Voluntary Winding Up by Creditors

Provisions applicable to creditors' voluntary winding up are contained in **Sections 306 to 318 of the Companies Act, 2013.** Section 306 provides that the company along with the calling of its meeting at which the resolution for the voluntary winding up is to be proposed by the members, shall also cause a meeting of its creditors to be held either on the same day or on the next day. The notice of such notice shall be sent to by registered post to the creditors with a notice of the meeting of the company requiring the company to be wound up under Section 304 which describes the circumstances in which a company may be wound up voluntarily.

According to sub-section (2) of Section 306, the Board of Directors of the company shall-

(a) cause to be presented a full statement of the position of the affairs of the company together with a list of creditors of the company alongwith a copy of declaration of solvency as required under Section 305 and the estimated amount of the claims before such meeting; and
(b) appoint one of the directors to preside at the meeting. If two-thirds in the value of creditors of the company are of the opinion that:
(a) it is in the interest of all the parties that the company be wound up voluntarily, the company shal: be wound up voluntarily, or
(b) the company may not able to pay for its debts in full from the assets sold in voluntary winding up and pass a resolution in the interest of all parties that it should be wound up by the Tribunal in accordance of the provisions of the Act. In that case, it shall file an application before the Tribunal within 14 days of the passing of the resolution.
The notice of any resolution passed at the meeting of creditors in pursuance of Section 306 shall be given by the company to the Registrar of Companies (ROC) within ten days of the passing of the resolution.
The effect of such winding up will be that the company shall cease to carryon its business from the date of commencement of winding up except as far as required for the beneficial winding up of its business. However, the corporate status and corporate powers of the company under winding up shall continue until it is dissolved

Q37) Powers and Duties of the Company Liquidator?
Ans--Powers and Duties of the Company Liquidator [Section 290]
The Company Liquidator shall take into custody all the property or claims to which he appears to be entitled. The powers of the Official Liquidator can broadly be classified into three broad heads as follows:
(a) Powers which the Company Liquidator can exercise with the sanction of the Tribunal;
(b) Powers which he can exercise without such sanction; and
(c) Powers which he can exercise with the leave of the Tribunal in case of onerous contracts.
It must, however, be pointed out that the Company Liquidator is subject to the control of the Tribunal even in respect of those powers that are exercisable by him without Tribunal's sanction.'
The Supreme Court in **Industrial Financial Corporation v. Official Liquidator, High Court of Calcutta**. "observed that in case of sale of assets of a company in liquidation by Tribunal under Section 457(1) (now Section 290 (1) of the 2013 Act) the Tribunal should formulate some method, procedure and terms of sale so as to avoid negotiating the terms and conditions by the Tribunal with the party.
I. Powers exercisable with the sanction of the Tribunal
The Company Liquidator may, with the sanction of the Tribunal, exercise all or any of the following powers:
(i) to institute or defend any suit, prosecution or other legal proceeding in the name and on behalf of the company;
(ii) to carryon the business of the company so far as may be necessary for beneficial winding up of the company, but not for making profit for the company;
(iii) to sell the immovable and movable property and actionable claims of the company by public auction or private contract etc.;
(iv) to raise on the security of the assets of the company any money requisite;
(v) to do all such things as may be necessary for winding up the affairs of the company and distributing its assets
(vi) to appoint an advocate, attorney or pleader to assist him in performance of his duties.'
The Supreme Court in Narendra Kumar v. Nandi Hasbi Textile Mills & others observed that where in a sale of property of a winding up company the bid of the appellant is cancelled, he becomes entitled to refund of the whole amount as the parties are relegated to their original position even though the cancellation of the acceptance of bid may be on account of the conduct of the bidder himself. It is only on acceptance of the offer made by the bidder and the sale having been

confirmed by the Court (now Tribunal), other clauses and terms and conditions in the offer of sale would have applied. In the absence of confirmation of the sale, the appellant is entitled to the refund of the entire money.

The Supreme Court in Allahabad Bank v. Bengal Paper Mills Co. Ltd. & others' set aside the. sale of assets and properties of winding up company on the ground that valuation of properties was suspicious and the publicity of sale was also not adequate.

The Court observed that the sale had not procured the best possible price because it was conducted in undue haste. The mere fact that purchaser was allowed to take possession of properties on very next day of sale is not a ground for not setting aside the sale specially when appeals against sale were filed within limitation. Further, the fact of re-employment of 1700 workers of the company by the purchaser could not overweigh the interests of unsecured creditors.

II. Powers exercisable without the sanction of the Tribunal

There are certain powers which the Company Liquidator can exercise without the sanction of the Tribunal. These powers are contained in Section 290(1) of the Companies Act, 2013 and include the power:

(i) to execute and seal documents and deeds on behalf of the company;

(ii) to inspect the records and returns of the company or the files of the Registrar of Companies without payment of any fee;

(iii) to prove a claim in the insolvency of any contributory for any balance against his estate and receive dividends in insolvency;

(iv) to draw, accept and endorse bills of exchange, hundis and promissory notes on behalf of the company;

(v) to take out in his official name, letters of administration to any deceased contributory;

(vi) to appoint an agent to do any business which he is unable to do himself. I

The official liquidator being the principal officer of the company, may be called upon to file income tax returns on behalf of the company.'

III. Power exercisable with the leave of the Tribunal in case of onerous contracts

There may be certain assets of the company which may be worthless or an unnecessary burden on the company and the creditors and contributories far from being interested in such assets, may prefer to do away with them. For example, shares which are not fully paid, onerous covenants, unprofitable contracts or short-term leases may be a liability rather than the asset and the Company Liquidator may like to get rid of them. This is called disclaimer and it operates in the interests of creditors and contributories by disposing on such unwanted assets of the company in liquidation. The liquidator may, with the leave of the Tribunal, disclaim in writing. The right of disclaimer has to be exercised by the Company Liquidator within twelve months after the commencement of the winding up.

The effect of disclaimer is to terminate the rights, interests and liabilities of the company in respect of the property which is disclaimed, but it does not affect the rights or liabilities of any other person' except so far as is necessary to release the company from liability. **However, the right of disclaimer is subject to following two conditions, namely**:

(i) where any interested person in writing calls upon the Company Liquidator to decide whether or not he *(i.e.* liquidator) will disclaim, the power of disclaimer will be lost if the liquidator does not, within twenty eight days after receiving the application, give notice of his intention to apply to the Tribunal for leave to disclaim ; .

(ii) if in case of a contract, the power to disclaim is lost as stated above, the company is deemed to have adopted the contract.

The disclaimer does not vest the property disclaimed in any person. But where a person claiming an interest in the disclaimed property, or under a liability in respect of it, applies to the Tribunal, the Tribunal may make an order vesting the property in any person entitled to it.

Any person aggrieved by the disclaimer is deemed to be a creditor of the company and may claim compensation amount as a debt in the winding up proceeding against the company.

Duties of the Company Liquidator [Section 290]

The duties of a Company Liquidator include taking custody and charge of the property of the company in liquidation and pay the debts and distribute the balance, if any, among the contributories. Section 451(1) of the Companies Act, 1956 (Section 290 of the 2013 Act) provides that the Company Liquidator shall conduct the proceedings in winding up of the company and perform such duties in reference thereto as the Tribunal may impose**. His main duties include:**

I, Duty to take the property of the company into his custody

Soon after his appointment, a Company Liquidator or a Provisional Liquidator is required to take into his custody and control all the property, effects and actionable claims of the company in liquidation.' The property, effects and actionable claims which the Liquidator takes into his possession shall be deemed to be in custody of the Tribunal from the date of the winding up order

2.Duty to Settle List of Contributories

Section 285 of the Companies Act, 2013 empowers the Tribunal to settle the list of contributories and cause rectification of the register of members where required in pursuance of this Act. However, the Tribunal may dispense with the settlement of a list of contributories where it deems its to be unnecessary.

The Tribunal may dispense with the settlement of the list of contributories where it appears that it will not be necessary to make calls or adjust the rights of contributories.

3.Duty to admit or reject proof of debts

The Company Law requires that all the creditors must formally prove the debts owed to them by the company by means of affidavits known as "Proofs" unless the Tribunal orders the admission of debts of any creditor without such proof. A claim of debt which is barred by limitation at the commencement of the winding up cannot be lodged."

So also a debt which is founded on an illegal or immoral consideration cannot be claimed.

4.Duty to make calls [Section 296]

Section 296 of the Companies Act, 2013 provides that the Tribunal is empowered To make calls on persons who are on the list of contributories in order to enforce their Liability but this duty is delegated by the Tribunal to the Company Liquidator who is an Officer of the Tribunal. The Company Liquidator can make calls to the extent of amount necessary to satisfy the debts and liabilities of the company, and costs, charges and expenses needed for completion of the winding up process and to adjust the claims of the contributories among themselves. He can make an application supported by an affidavit, to the Tribunal for an order against any contributory for payment of money due on calls.

Where the contributory attempts to abscond or disposes off property in order to evade calls, he may be arrested and his property may be seized by the Tribunal.

5. Duty to pay Company's debts

The Company Liquidator is under a duty to payoff the debts in full where the company is solvent and the assets of the company must not be distributed among the contributories unless the company's debt is fully paid. However, where the company is insolvent, the rules for payment to the secured and unsecured creditors as contained in the law of insolvency shall be applicable.? It is only after the meeting, the costs of the winding up and paying off ordinary debts of secured creditors in full that the Company Liquidator should pay the deferred debts, namely, the money owed to members in their capacity as members by way of dividend, profit, etc

6. Duty to keep Books, Papers, Documents, etc.

The Company Liquidator is expected to maintain a number of registers and books and enter therein the minutes of proceedings of the meetings held from time to time." Any creditor or contributory can inspect such books and records on payment of prescribed fees but he is not entitled to inspect the account books

7. Duty to Report as to the progress of Liquidation

Section 348 of the Companies Act, 2013 provides that the winding up of a company could not be concluded within one year, the Company Liquidator is under a duty to file a statement in prescribed form within two months of the expiry of such year and thereafter at an interval of not more than one year, until the winding up is completed, with the winding up Tribunal. The statement must be audited by a qualified auditor of the company. A copy of the statement should simultaneously be also filed with the Registrar of Companies and to the Central Government, if the company under liquidation is a government company. A creditor or contributory of the company may inspect the statement and receive a copy or extract thereof, on payment of the prescribed fees

Where the statement referred to above relates to a Government Company in liquidation, the Company Liquidator shall forward a copy of such statement :-

(a) to the Central Government, if the Government is a' member of the Government company;

(b) to the State Government, if the State Government is a member of the company;

(c) to the Central Government and any State Government; if both the Governments are members of the Government company.

If the Company Liquidator contravenes the provisions of Section 348 of the Act (of 2013), he shall be punishable with fine which may extend to five thousand rupees for every day during which the default continues.

8. Duty to Maintain proper accounts

A Company liquidator has also to submit to the Tribunal twice a year, an account of his receipts and payments as liquidator.' The accounts must be presented in the prescribed form and. in duplicate and must be duly verified by the Company Liquidator. The Company Liquidator has to send a copy of the printed accounts to every creditor and contributory." A copy thereof is also to be filed with the Registrar of Companies.

9. Duty to Distribute the Balance to Contributories

When the liability of company to its creditors has been fully discharged, the liquidator should apply to the Court for leave to distribute surplus assets among the contributories. The distribution of surplus among the entitled contributories shall only be made when it has been duly ordered by the Tribunal'? The preference shareholders obviously will have preferential right over the equity shareholders in repayment of the capital paid up by them. The Company Liquidator should take into consideration the provisions of the memorandum and articles of the company while distributing the surplus assets.

Q38) Investigation into the Affairs of a Company (Section 213)?

Ans-- **<u>Investigation into the Affairs of a Company (Section 213)</u>**

Section 213 of the Companies Act, 2013 makes it obligatory on the part of the Central Government to appoint inspectors to investigate into the affairs of a company in **the following two circumstances**:

1. When the company has demanded such an investigation by a special resolution; and
2. Where the Tribunal, by order declare that the affairs of the company ought to be investigated by an inspector or inspectors appointed by the Central Government.

The Act, however, is silent as to who can seek an order of the Tribunal for this purpose. Perhaps this has purposely done so with a view not to circumscribe the jurisdiction of the Tribunal. The matter, is therefore, left entirely at the discretion of the Tribunal. This view finds support in the decision of the Gujarat High Court **In re Alembic Glass Industries Ltd.»**

wherein the learned Judge held that the power of the Court (now Tribunal) under Section 237(a) of the Companies Act, 1956 (now Section 213 (a) of the Companies Act, 2013) is not subject to provisions of Section 237(b) (now Section 213(b) of 2013 Act). This, however, does not mean that the Tribunal can order investigation on mere suspicion without a *prima facie* case having been made out by the petitioner against the company. The Tribunal would ordinarily not act unless there is some factual basis for ordering investigation. The person seeking order must prove before the Tribunal that he has some genuine concern in the matter. A person having no interest in the affairs of the company as a member, creditor or otherwise has no ***locus standi*** to seek the Tribunal's intervention to order investigation into a company's affairs. Thus in **V.V. Puri v. E.M.C. Steel us»** the landlord of the Company filed a petition for seeking an order of the Court for investigation under Section 237(a) of the Companies Act, 1956 (now Section 213 (a) of the Companies Act, 2013) on the ground That the had paid money to the Managing Director to induce him to vacate the premises And he misappropriated the money and that he was making use of his political contacts for promoting business. Rejecting the petition, the Court observed, "it would not be correct to read the section as authorising any man in the street to seek an order for investigation".
The relief may be available only to a person whose rights have been affected due to affairs of the company not being conducted in a proper manner. In other words, the petitioner must have approached the Tribunal *bona fide* alleging fraud, oppression, misfeasance or misconduct on the part of those who are in control of the affairs of the company.

Besides the power of the Tribunal to order investigation under Section 213(a). the Companies Act, 2013 also makes it mandatory for the Central Government to hold an investigation into the affairs of the company upon an application from-
(i) not less than one hundred members or members holding at least 1/10th of the total voting powers in case of a company having share capital; and
(ii) not less than 1/5th of the members, in case of a company without a share capital.

On receipt of such application, the Tribunal. after giving the parties an opportunity of being heard, would make an order declaring that the affairs of the company ought to be investigated by one or more inspectors.'

The Central Government, may require the applicants to deposit security," for costs of investigation' not exceeding one thousand rupees, before appointing inspectors for investigation into the affairs of the company. Where the Tribunal rejects the application, a member may apply to the Appellate Tribunal.
THe decision of the Central Government to appoint inspectors under Section 210(I) or Section 213(b) being an administrative decision. the Tribunal will not generally interfere unless *mala fide* or bad faith is proved.
Section 213 (b) provides that the Tribunal can appoint inspectors of its own motion in the following three circumstances :-
1. When there is a fraud, oppression or illegality in the conduct of its affairs by a company and the creditors or members are being adversely affected by such fraudulent dealing or the company has been formed for some unlawful purpose.
2. When the persons concerned with the formation of the company or management of its affairs have been guilty of misfeasance or misconduct towards the company or its members or creditors.
3. The members of the company have not given all the necessary information regarding the affairs which the Board had sought for, namely, information as to the commission payable to the Managing Director or the manager of the company.

Before an inspector is appointed by the Central Government under Section 237(b). the Tribunal must satisfy that there exist any of the aforesaid circumstances which warrant investigation into the affairs of the company. The opinion of the Tribunal can, however, be challenged by the company or the person aggrieved on the ground of *mala fide.* Therefore, the Tribunal should have made the order *bona fide* in good faith.'

In Barium Chemicals Ltd. V. The Company Law Board, I the affidavit filed by the Chairman of the Company Law Board (now abolished) disclosed that in the conduct of the company there was delay, bungling and faulty planning resulting into double expenditure and continuous loss to the company due to fall in the prices of the company's shares and some of the directors having resigned due to differences with the Managing Director. The Court held that the said circumstances could not by themselves suggest an intent to defraud or fraudulent management and, therefore, the order for investigation was quashed.
Mere bungling or faulty planning cannot be called misconduct or misfeasance. The Court, in this case further ruled that non-application of its mind by the Central Government to relevant circumstances is a good ground for challenging the validity of an order made by it and in such cases it is immaterial whether the impugned order is made by the Government in exercise of its administrative or *quasi-judicial* power.
"**In interpreting Section 237(b) (now Section 213 (b) of the Companies Act, 2013)** we cannot ignore the adverse effect of the investigation on the company -
We must also remember that the section in question is-an inroad on the power of the company to carryon its trade or business and thereby an infraction of the fundamental rights guaranteed to its shareholders under **Article 19(J)(g) of the Constitution of India.**
In *Jiwaji Rao Cotton Mills* v. *Company Law Board,* I the management of a company acquired the shares of its subsidiary of Rs.I0/- each at a premium of Rs.I00/- and offered them to the members in lieu of cash dividends and almost all of them opted for the shares, made a loan of huge sum to its subsidiary at 2% though commercial expediency did not justify this deal, it was held to be no ground suggesting a fraud and therefore, order of investigation was not justified and hence quashed.

Who may be appointed Inspectors [Section 215]

The Act provides that no firm, body corporate or other association shall be appointed as an inspector for investigation into the affairs of a company under Section 235 or 237 of Companies Act, 1956 (now Section 210 or 213). It, therefore, follows that only individuals can be appointed as inspectors and not any non-living entity.

Power of Inspectors [Section 217]

The inspector appointed to investigate the affairs of a company is vested with adequate powers under the Companies Act, 2013. The powers of inspectors are as follows:

1. *Power to enforce production of Documents.-Section* 217 of the Act, 2013 provides that in order to facilitate the task of the inspector, it is the duty of all officers, employees and agents incharge of the management of the company to procure and produce before the inspector any books, paper of the company which are in their custody. They
should extend to the inspector every kind of assistance in connection with the investigation which they are reasonably able to give. The Inspector may also, with the prior approval, I of the Central Government, require any body corporate, other than the body corporate whose affairs are being investigated, furnish such information or produce such books and papers before him as he may consider necessary.

2. Power to keep books in custody. - The inspector investigating into the affairs of a company may keep in his custody any books and papers produced before him, for six months and thereafter shall return the same to the company, body corporate or individual by whom the books and papers were produced. He may, however, call the books and papers again if they are needed

3. Power to examine on oath.-*The* inspector may examine any past or present Officers or any other employees or agents of the company in relation to matters connected with the affairs of the company under investigation. Where an inspector finds that a person whom he has no power to examine on oath has to be examined, he may apply to the Central Government for necessary permission.

***4. Power to Investigate affairs of related companies.-Section* 219** of the **Companies Act, 2013** provides that if the inspector considers it necessary to investigate Even the affairs of another company under the same management or in the same group, he may do so.

5. Power to seizure of documents.-*Where* an inspector has reasonable grounds to believe that relevant books and papers may be destroyed, falsified, altered or secreted ,he may make an application to Magistrate First Class and obtain an order for seizure of such books and papers.! The order may authorise him to enter the place where such books and papers are kept, to search the place and seize them. At the conclusion of the investigation, he must return these books and papers. Before returning such books and papers, the inspector may make identification marks on them or on any part of them.
6. Report by Inspector.-*On* conclusion of investigation, the inspector shall Prepare a report and submit it to the Central Government.

Q39) PREVENTION OF OPPRESSION AND MISMANAGEMENT ?

Ans--It has already been stated earlier that supremacy of the majority is the fundamental rule governing company law administration. But sometimes the majority shareholders may tend to abuse their powers to the detriment of the minority shareholders. Therefore, it becomes necessary to maintain a proper balance between the rights of majority and minority shareholders for the smooth functioning of the company.

It has also been said that the ultimate authority of the company's management vests with the general meeting which can decide certain issues by an ordinary resolution and some other issues by a special resolution. The directors of the company are elected by the shareholders and are responsible to them, their powers are regulated by the articles of association. The acts done with the consent of the majority of the company in its general meetings are deemed to have been done properly and are therefore legally valid. There are, however, certain exceptions to this general principle which are explained under **the *Foss* v. *Harbottle Rule.*** I In order to extend protection to minority interests, a positive check has been provided in Section 163 of the Companies Act, 2013 which contains provisions relating to proportional representation for the appointment of directors so that minority interests may also get proper representation in the Board of Directors. However, this check may not itself be sufficient enough to ensure adequate protection to minority shareholders in all the cases. Therefore some additional safeguards are devised under the Companies Act.? to provide relief in case of oppression and mismanagement in the affairs of the company. The ultimate object of these provisions is to protect the interests of investors and public in general.

Majority Rule – Foss v. Harbottle

Facts of the case :

2 shareholders instituted a suit against the Directors alleging that they have effected fraudulent transactions and misapplied the property of the company. The suit was dismissed.

Principles emerging out of the case:

1. Proper plaintiff is the company.
2. The affairs of the company are conducted by a majority of shareholders and their decision is binding on the company and the minority.

Criticism

Over the number of years this rule has faced a lot of criticism and hence various exceptions to this Rule have been propounded as follows.

Minority shareholders are protected by:

1. the Common Law; and
2. the provisions of the Companies Act, 1956

Protection at Common Law:

a. Where the act complained of is illegal or ultra vires the company;

b. Where the act done by the majority constitutes fraud on the minority;
c. Where a resolution is passed by a simple majority for any act, which requires special resolution for it to be effective;
d. Where the act infringes the personal rights of an individual member;
e. Where any act amounts to oppression of minority or mismanagement of the affairs of the company.

In all these cases a minority shareholder is entitled to bring an action for a declaration that the resolution complained of is void, or for an injunction to restrain the company from passing it.
All these principles have been followed in a few leading cases in India as well.

Protection under the Companies Act, 1956:
Various rights are given to minority shareholders by the Companies Act, 1956. These relate to
a. The variation of class rights (Section 107)
b. Schemes of reconstruction and amalgamation (Section 391)
c. Prevention of oppression of minority and of mismanagement under Sections 397 and 398.
d. The rights to apply to the Central Government to have the affairs of the company investigated. (Section235)
There are some other Sections of the Companies Act, which protect the minority shareholders' rights. Theseare:
1. **SEC 17 :** Consent of the Tribunal is necessary before certain acts can be validly done by a company, e.g.,an alteration of the objects of a company.
SEC 101 : Consent of the Court is necessary in case of reduction of share capital.
SEC 111 : Rights to appeal to the Central Government against the arbitrary action of the Board of Directors in refusing to register a transfer of shares.
SEC 408 : Right of the Central Government to appoint on an order from the Tribunal (C.L.B.) such number of persons as directors as considered necessary to effectively safeguard the interests of the company or its shareholders or the public interests. Such an order may be made by C.L.B. on a reference made to it by the Central Govt. or on an application of not less than 100 members of company or by such members holding not less than 1/10th of the total voting power.
SEC439: A contributory is entitled to present a petition to the Court for the winding up of the company on just and equitable grounds.
SEC517 : An arrangement between a company and its creditors may be amended, varied, confirmed or set Aside by the Court on the application of any creditor or contributory.
examples of Oppression:
A large majority of 98% wished to buy the shares held by the minority shareholders. This minority refused to sell their shares. In order to compulsorily acquire the shares of the minority, the majority shareholders altered the Articles by passing SR so as to empower the 9/10th Majority to compulsorily acquire the shares of the minority. It was held that the minority could not be compelled to sell their shares to majority. **[Brown v. British Abrasive Wheel Co.]**
The3 directors of a company used their influence to obtain a contract in their names. They held 75% of the sharecapital of the company. They passed a resolution in the GM that the Company had no interest in the contract. In such a case the court held that the resolution in the GM was void and a suit brought by even one member was tenable. **[Cook vs Deeks]**

Prevention of Oppression [Section 241]
The Companies Act, 2013 makes special provision for the prevention of oppression of any member or members and mismanagement, Before The enactment of the Companies Act, 2013 the only effective remedy against oppression was winding up order under Section 433 of the Act, 1956 (now Section 271 of Companies Act, 2013) *i.e.,* under 'just and equitable clause'. But this remedy was often worse than the disease. Therefore, the Tribunal," has been given wide powers to impose on parties whatever settlement the Tribunal," considers best and reasonable in the circumstances. Thus, if the oppressed

member or members think that winding up will not provide adequate relief, they may file a petition to the Tribunal, under Section 241 of the Companies Act, 2013. The object is to prevent an otherwise sound business concern from being wound up and make an effort to salvage it in the larger interests of the society.

In *Kanika Mukherjee* v. *Rameshwar Dayal Dubey*, I it was held that bad and inefficient management could lead to corporate collapse. Where the company is run overriding the wishes and interest of majority of shareholders involving the company into costly litigations, the management is not in the interest of the company. The powers of the Tribunal being of preventive character, are intended to remove an existing oppressive or prejudicial course of conduct in the affairs of the company. The Tribunal is not concerned with the past mismanagement except where the part project is itself as a continuing wrong and pervades the present conduct of the company's affairs

The Supreme Court in *Bhagwati Developers (P) Ltd.* v. *Peerless General Finance Investment Co. Ltd. and others,* held that where the company petition under Section 241 is filed with the consent of the other share-holders, the same must be treated as having been tiled in a representative capacity for the purpose of requirement of petitioner holding 10 per cent shares, and therefore, making an application for withdrawal by the original petitioner would not render the petition under Section 241 of the Companies Act, 2013 as non-maintainable. The other persons (i.e. the constructive parties) who provide consent to file the petition, are in fact entitled to be transposed as petitioners in such a case.

Therefore, where the original petitioner does not wish to proceed with his petition, it is not always incumbent upon the Court (Tribunal) to dismiss the petition and the Court may deal with the petition on merit without dismissing the same. Making the law on this point clear, the Apex Court observed that if the share-holder who had initially given consent to file a company petition under Section 241 to help meeting the requirement of 1/10th share-holding, transfers the shares held by him, or ceases to be a share holder, the same would not, in any way, affect the maintainability or continuity of the petition.

Meaning of Oppression

The terms 'oppression' and 'mismanagement' are not defined anywhere in the Act but for the purposes of company law, they should be used in broad generic sense and not in strict literal sense.

The Supreme Court in *Shanti Prasad Jain* v. *Kalinga Tubes ltd.»* has interpreted the term 'oppression' as follows :-

"The essence of the matters seems to be that the conduct complained of should at the lowest, involve a visible departure from the standards of fair dealing, and violation of the conditions of fair play on which every shareholder who entrusts the money to the company is entitled to rely."

Thus, a complaining member must be under a burden which is unjust and harsh or tyrannical. Therefore, it is necessary to prove a persistent unjust conduct on the part of majority shareholders and isolated acts of oppression will not normally be sufficient to justify relief;' under Section 241 of the Companies Act, 2013.

Can there be Oppression of Majority by Minority?

It would be pertinent to consider at this stage whether special remedies against oppression and mismanagement under Sections 397 and 398 (now Section 241) respectively, are available only to minority shareholders or it may extend even to the members having majority voting power. Where the court is satisfied about the acts of oppression or mismanage-ment, it may grant relief even to majority members if an application has been made by them alleging wrongful acts of the minority group.

Prevention of Mis-management

The provisions relating to prevention of mismanagement in a company are contained in Section 398 of the Companies Act, 1956 (Section 241 of 2013 Act). An application may be made under this section to the Tribunal, by any member or members of a company complaining that-

(I) the affairs of the company are being conducted in a manner prejudicial to the public interest or the company; or

(2) a material change has been introduced in the management or control of the company whereby it is likely that the affairs of the company may be conducted in a manner prejudicial to public interest or the company.

For the purposes of Section 398 (now Section 241 of Companies Act, 2013) the material change in the management or control of the company will be deemed to have taken place, if there is an alteration:
(i) in the Board of Directors; or
(ii) in the ownership of shares in the company; or
(iii) in the membership, in case the company has no share capital; or
(iv) in its manager; or
(v) in any other manner, whatsoever.
On receiving such an application, the Tribunal, shall, after taking into consideration the representation, if made, is satisfier that the affairs of the company are being conducted as complained of, or material change has taken place in the management or control of the company which is likely to be prejudicial to it, may pass any order as it thinks fit with a view to bring to an end the matters complained of in the petition.

The following points need to be particularly noted in context of relief against mismanagement as provided under Section 398 of the Companies Act, 1956 (now Section 241 of the Companies Act, 2013)
1.The relief is available to the company and not to any particular member or members.

2. There should be a present and continuing mismanagement. The charge of past mismanagement even if proved, shall not be enough to establish an existing injury to the public or the company.
3. The section enables the Tribunal to take into consideration the outside interests affected by corporate operations. Thus in ***Richardson* & *Cruddas Ltd.* v. *Haridas Mundra*.** the High Court of Calcutta refused to order the winding up of a grossly mismanaged company and appointed special officers to manage its affairs because the company was engaged in special industry necessary for the implementation of the country's Five Year Plans

Distinction between oppression and Mismanagement
In the preceding Companies Act, 1956, Section 397 of the Act dealt with relief against oppression whereas Section 398 was related to prevention of mismanagement. It is important to note that the relief available under the two sections differs in the following aspects :-
1. In case of oppression under Section 397, there should have been facts to justify the making of an order for winding up, but no such facts were necessary in case of claiming relief against mismanagement under Section 398.
2. Under Section 397, the Tribunal by its order, prevents injustice being done to the member or members in capacity of member, but under Section 398, the Tribunal makes an order to prevent injustice being done to the interests of the company as a whole.
3. The provision of Section 398 were of a preventive nature whereas under Section 397, the Tribunal sought to end the oppression complained of by the petitioner.

However, in the Companies Act, 2013, the provisions of Sections 397 and 398 of the preceding Companies Act, 1956 have been brought together under a single section *i.e.* Section 241 which provides for application to Tribunals for relief in cases of oppression.
There is no separate section for relief against mismanagement and an application against mismanagement in a company may be made to the Tribunal under the same section *i.e.*. Section 241 of the Act.

Power of the Tribunal [Section 242]

Section 242 of the Companies Act, 2013 confers wide powers on the Tribunal in respect of applications made to it under Section 241 of the Act. The Tribunal may make an order for the regulation of the conduct of the affairs of the company upon such terms and conditions as it deems just and equitable keeping in view the circumstances of the case. The ultimate object of the power conferred upon the Tribunal under Section 242 is to bring an end to the matter complained of. For example, in ***Lord Krishna Sugar Mills Ltd.* v. *Abnash Kaur*,** ..where the CLB (now Tribunal) by its order had constituted an interim Board of management for the company, held that it also had the power under Section 402 to give directions and instructions from time to time to resolve the problems of the interim Board. However, without prejudice to the generality of powers under Section 241, **the Tribunal may in exercise of its powers under Section 242 provide for** :-

I. The regulation of the conduct of the company's affairs in future.- Thus, in ***Richardson* &: *Cruddas Ltd.* v. *Haridas Mundra*.** 'while clarifying the scope of Section 242, the Tribunal held that the constitution of an Advisory Board to assist the special officer appointed by the Tribunal in managing the affairs of the company is within the competence and powers conferred under this section.

2. Acquisition of shares or interests of any members by other members or by the company.-

Thus, in ***Suresh Kumar Sanghi* v. *Supreme Motors ltd»*** where the group in actual control was given an opportunity to buyout the other at a value to be fixed by a judge. Likewise, in ***Surendra Singh Bindra* v. *Hindustan Fastners (P) Ltd.*,** I where one group of shareholders was installed in power and directors were issued for taking over the shares of the other group.

3. In case of a purchase by the company of its shares, the consequent reduction of its share capital.

4. The termination, setting aside or modification of any agreement between the company and managing director, or any other director, and the manager.

5. The termination. setting aside or modification of any agreement with any person, provided due notice has been given to him and his consent obtained.

6. Setting aside of any transfer, delivery of goods, payment, execution or other act relating to property made or done by or against the company within three months of the application which would amount to a fraudulent preference in case of an individual's insolvency. Thus, in ***Roshan Lal Agarwal* v. *Sheoram Bubna...*** the Patna High Court set aside a fraudulent preference made within three months before the date of application and held that there should be a net period of three months between the date of transfer and that of application. The Court excluded the date of transfer in computing the period of three months.

7. Any other matter which in the opinion of theTribunal is just and equitable. Thus, **in *Gajanbai* v. *Patni Transport ltd»*** the Court issued directions to the directors of the company to transfer the shares to the petitioners in accordance with the terms of the will. Again, in ***Jhambu Kumar Rauiwala* v. *Edward Mill Co.*,** *4* the Court issued directions regulating the conduct of directors.

Section 242 (7) of the Companies Act, 2013 of the Act requires that a certified copy of the order of the Tribunal altering the memorandum or articles must be filed by the company with the Registrar within thirty days of the order. Misfeasance proceedings can be commenced against the guilty officers even though the company is not being wound

The powers of the Tribunal under the provisions of Section 242 are not affected by the existence of an arbitration clause. The Tribunal may, however, at its discretion refer the matter to arbitration in terms of agreement between the parties.

Locus standi for filing petition under Section 241

The use of the legislative expression that *'any person interested in the affairs of the company'* may draw the attention of the Tribunal to a situation which warrants Tribunal's intervention, clearly suggests that the question of *locus standi* hardly arises in case of application under Section 241 for prevention of mismanagement in a company. It would, therefore, appear that the connotation *'any person interested in the affairs of the company'* has a much wider application than merely a member, creditor or liquidator of a company. Tribunal can even act *suo motu.* As pointed out in ***S.K. Gupta* v. *K.P. Jain***, "it is immaterial as to who drew the attention of the Tribunal to a situation which necessitated Board's intervention. There is no reason to circumscribe the expression 'on the application or any person interested in the affairs of the company' so as to limit it to mere creditors or members.

Right to apply under Section 241 [Section 244]

Section 244 of the Act, 2013 provides that an application complaining of rnis-mismanagement or oppression under Section 241 can be filed on behalf of members/shareholders. Although Regulation 18 requires that documents to be annexed with the petition must also include letter of consent given by supporting shareholders, but the said requirement was not deemed mandatory by the Apex Court and therefore, noncompliance with that provision of Regulation 18 will not entail dismissal of application filed under Section 241 of the Companies Act, 2013. The Court held that the requirement of consent by supporting shareholders as provided in Regulation 18 was merely directory and the petition did not deserve rejection on this technical ground alone

It may be stated that Section 242 of the Companies Act, 2013 does not empower the Tribunal to grant relief by way of prevention of apprehended mismanagement of the company due to substantial changes have taken place in the management of modern companies and the control mechanism adopted to safeguard the interests of members, share-holders and investors of companies. However, Section 245 does provide relief against mismanagement to some extent through class action by members or depositors against the company.

Valuation of Company's Assets by Registered Valuers [Section 247]

Section 247 of the Companies Act, 2013 contains a new provision providing for valuation in companies by registered valuers. Valuation in respect of any property, stocks, shares, debentures, securities, good will or any other assets or net worth of a company and its liabilities under the Companies Act, becomes necessary for various purposes. The section provides that for the purpose of valuation of company's property and assets, qualified registered valuers may be appointed by the audit committee of the company, or in its absence, by the Board of Directors.

The valuer so appointed under sub-section (I) of Section 247 shall-

(a) make an impartial, true and fair valuation of assets which may be required to be valued:

(b) exercise due diligence while functioning as a valuer;

(c) make valuation according to the prescribed rules: and

(d) not undertake valuation of any assets in which he has any direct or indirect interest.

Any contravention of the provisions of this section shall render the valuer liable to punishment with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.!

Q40) MAJORITY RULE AND RIGHTS OF MINORITY SHAREHOLDERS?

Ans--Like any other institution, a company is run by democratic process and administration of its affairs is carried on by resolution of a majority of shareholders, passed at the duly convened general meeting and at the meeting of the Board of Directors. The matters on which the members are divided are decided by the majority votes of the shareholders. Thus majority power has great importance in the working of a company and the "Tribunal will not generally intervene at the instance of shareholders in matters of internal administration, and will not interfere with the management of a company by its Board of directors so long as they are acting within the powers conferred on them under the articles of the company".

In a public limited company, the members holding paid-up equity shares have a right to vote in respect of every resolution placed before the company in its general meetings. The right of a member to vote has been recognised as *right of property* and he may exercise this right in a manner he likes according to his choice and wishes. The resolutions carrying majority support are normally binding upon the minority shareholders and consequently upon the company

Importance of Majority Rule

The decisions on routine general matters relating to internal administration of a company are taken by resolutions passed by ordinary majority at the. meeting but decision on important matters requires the approval of special majority. It therefore follows that the majority of the members enjoy the supreme authority to exercise the powers of the company and generally to control its affairs and the minority shareholders have to concede to the majority decision. This, however, may lead to a possibility that the members having majority vote may tend to be oppressive towards the minority shareholders misusing their majority strength and this may result in the mismanagement in the company. It is for this reason it has been said that "the protection of the minority shareholders within the domain of corporate activity constitutes one of the most difficult problems facing modern company law. The aim must be to strike a balance between effective control of the company and the interests of the small individual shareholders".'

Commenting on the powers of majority *vis-a-vis* minority rights, Palmer observed, "A proper balance of rights of majority and minority shareholders is essential for the smooth functioning of the company." With a view to protecting the rights of minority shareholders and safeguard the interests of investors from oppressive decisions of the majority shareholders, adequate provisions are made in the Companies Act so that those who control the affairs of the company exercise their powers according to the set principles of natural justice.' These provisions are incorporated in Sections 241 to 243 of the Companies Act, 2013.

Majority Rule – Foss v. Harbottle

Facts of the case :

2 shareholders instituted a suit against the Directors alleging that they have effected fraudulent transactions and misapplied the property of the company. The suit was dismissed.

Principles emerging out of the case:

1. Proper plaintiff is the company.
2. The affairs of the company are conducted by a majority of shareholders and their decision is binding on the company and the minority.

Criticism

Over the number of years this rule has faced a lot of criticism and hence various exceptions to this Rule have been propounded as follows.

Minority shareholders are protected by:

1. the Common Law; and
2. the provisions of the Companies Act, 1956

Protection at Common Law:

a. Where the act complained of is illegal or ultra vires the company;
b. Where the act done by the majority constitutes fraud on the minority;
c. Where a resolution is passed by a simple majority for any act, which requires special resolution for it to be effective;
d. Where the act infringes the personal rights of an individual member;

e. Where any act amounts to oppression of minority or mismanagement of the affairs of the company.
In all these cases a minority shareholder is entitled to bring an action for a declaration that the resolution complained of is void, or for an injunction to restrain the company from passing it. All these principles have been followed in a few leading cases in India as well.

In *Parashuram* v. *Tata Industrial Bank,* I it was held that unnecessary interference of the Court is likely to paralyse the working of the joint stock companies and therefore the Court should not intervene in the internal affairs of the company. In this case the minority shareholders prayed for injunction restraining the newly appointed directors and auditors from assuming their office since their appointment at the general meeting held on Ist May, 1923 was alleged to be invalid due to irregular procedure at the meeting. The Court. however, refused to intervene in the majority decision of the company taken at its duly convened general meeting

Advantages of the Majority Rule

Rule by the majority of shareholders. has been accepted as a cardinal principle of corporate management for its obvious advantages. It seeks to avoid multiplicity of frivolous suits and at the same time recognise the right of majority shareholders who provide capital to the company at the cost of risk involved in the investment. That apart, if an individual member sues a person who has caused loss to the company, and the company then ratifies that person's wrongful act at the general meeting, the legal proceedings will naturally be quite futile, for the Tribunal," would uphold the will of the majority.

Exceptions to the Rule in *Foss* v. *Harbottle* Rule

There are, however, certain exceptions to the majority supremacy rule. It extends only to cases in which the company is competent to ratify its managerial acts. There are certain cases which no majority of shareholders can approve or affirm and even a single shareholder can sue for enforcement of obligations owed to the company. He does so in the representative capacity of the company and therefore the relief goes to the company. The exceptions are :-

I. *Ultra vires acts*

In the first place, the powers of the majority of members is subject to the provisions of the company's memorandum or articles. A company, therefore, cannot legally authorise or ratify any act which, being outside the ambit of the memorandum, is *ultra vires* the company. Such acts being illegal, there can be no question of the transaction being confirmed by any majority and a shareholder is entitled to bring an action against the company and its officers in respect of such matters.

The case of *Bharat Insurance Co. Ltd.* v. *Kanhaiya Lal,* I is an illustration on this point. In this case the plaintiff was a shareholder of the Bharat Insurance Company (respondent). One of the objects of the company was, "to advance money at interest on the security of land, houses, machinery and other property situated in India " The plaintiff complained that "several investments have been made by the company without adequate security and contrary to the provisions of the memorandum". He therefore prayed for a perpetual injunction to restrain the company from making such investments. The **Court observed** that, "in all matters of internal management, the company itself is a best judge of its affairs and the Court should not interfere. But application of the assets of a company is not a matter of internal management. As the directors are acting *ultra vires* in the application of the funds of the company, a single member can maintain a suit for a declaration as to the true construction of the article in question

2. Fraud on Minority

The majority cannot be allowed to benefit itself unduly at the expense of the minority. Therefore, where the conduct of a majority of shareholders constitutes a fraud on the minority, the latter can sue the former. Thus where a special resolution seeks to discriminate between majority shareholders and minority shareholders so as to give former an advantage which the latter would be deprived of, and alteration in the articles is not *bona fide* for the benefit of the company, the Court (now Tribunal) may interfere even at the instance of a single minority shareholder."

3. Acts Requiring Special Resolution

Generally the decisions on internal affairs of the company are taken by passing ordinary resolution at the general meeting. But there are certain acts which can be done only by passing special resolution. Therefore, if the majority purports .o do any such act by passing only an ordinary resolution or without passing special resolution, in the manner required by law, any member or members can bring an action to restrain the majority.

Thus in *Dliakeswari Cotton Mills Lld.* v. *Nil kamal Chakarvartv,* I the Calcutta High Court held that where voting on a resolution takes place by show of hands, a declaration by the chairman that a resolution has or has not been passed is conclusive only if he does not find by his declaration the figures for or against the resolution. But where the chairman finds the figures and erroneously in point of law holds that resolution has been duly passed, the resolution cannot be said to have been passed according to the law and therefore liable to be set aside.

4. Infringement of Individual Membership Right ofa Shareholder

The majority-supremacy rule as laid down in *Foss v. Harbottle* has no application where an individual membership right of a shareholder is alleged to be infringed by the company *i.e.* the majority shareholders. The majority rule prevails only in respect of corporate membership right and not where any personal right of the individual member has been infringed.

Thus, for example, right to receive dividend is a corporate membership right as it cannot be exercised unless dividends are declared by the company at the general meeting. But a right to transfer the shares held in the company or right to vote i. a personal right of the individual member**. Some other examples of a member's individual rights which are statutorily recognised under Companies Act, 2013 are** :-

I. Not to have his liability increased (by taking more shares) in any way without his consent in writing (Section 13).
2. Right to use his voting right at the poll (Section 106).
3. The right to object to a compulsory transfer of shares (Section 235).
4. Right to object to appointment of two or more directors by a single resolution (Section 162).
5. Right to insist for a notice of not less than twenty one days for the annual general meeting (Section 101).
6. Right to apply to the Tribunal for calling of an annual general meeting on failure by the company to do so (Section 97).
7. Right to file a petition for a compulsory winding up of the company (Section 272).
8. Right to make representation to the Tribunal where sanction of the Tribunal is sought to a scheme of arrangement by amalgamation or reconstruction of the company (Sections 230 and 232) .

Apart from the above individual membership rights, there **are certain other individual rights of shareholders** which can be exercised with the consent of a specified number of shareholders or a specified percentage of share-holding or voting power in the company. These rights are-

I. The right to call an extraordinary general meeting on requisition by members holding not less than I/I0th paid-up share-capital in case of a company having a share-capital or I/I0th of the total voting power in case of a company not having a share-capital [Section 100 (4)].
2. The right of a dissentient shareholders to have a variation of shareholder's right cancelled by the Tribunal on requisition by members holding not less than ten percent of the issued shares of the class to which the member belongs (Section 48).
3. The right to demand a poll at a general meeting of a public company on requisition by persons having not less than 1I10th of the total voting power in respect of the resolution (Section 109).
4. The right to apply for an investigation of the affairs of the company on requisition by not less than 200 members or members holding not less than I/I0th of the total voting power in case of a company having a share-capital or not less than I/5th of the members on company's register in case of a company having no share-capital (Section 210).
5. The right to apply to the Tribunal for relief against oppression and mismanagement. This right can be exercised, in case of a company having a share-capital, by members not less than 100 or not less than I/I 0th of the total number of

members, whichever is less. In case of a company not having a share-capital, on requisition by members not less than 115th of their total number (Section 244). •

6. The right to move a resolution at an annual general meeting or for circulation of members resolution on requisition by members not less than 1/20th of the total voting power or not less than one hundred members, whichever is less (Section III).

7. The right to apply to the "tribunal for appointment of a Government director by the Central Government to prevent oppression and mismanagement (Section 242).

5. Wrongdoers in control

Occasions may arise when a wrong has been done to the company but the controlling shareholders would not permit an action to be brought against the wrongdoer.

In such cases any member can bring an action in the name of the company In ***Wallersteiner* v. *Moir (No.* 2),**I it has been held that where wrongdoers themselves control the company, an action can be brought on behalf of the company by the minority shareholders on the footing that they are its representatives to obtain redress on its behalf.

6. Oppression and Mismanagement

The principle contained in Sections 241 of the Companies Act, 2013 which relates to prevention of oppression and mismanagement in a company is also one of the exceptions to the rule in *Foss v. Harbottle.* A composite application under these sections can therefore be made alleging that the affairs of the company are being so managed as to be prejudicial to the company and also oppressive to the minority shareholders. A remedy under Section 241 is, however, only available to members who apply to Tribunal *in their capacity as members* and the matters complained of must relate to the affairs of the company.?

In *Kanika Mukherji* v. *Rameshwar Dayal Dubey,..*Justice Sinha of the High Court of Calcutta observed that relief against oppression by majority shall be available to minority shareholders provided it relates to the companies affairs but if it is directed towards a third person, it shall not be available. It was further held in this case that "inefficient management will not amount to oppression, though it may amount to mismanagement so as to come under Section 398 of the Companies Act, 1956 (now Section 241 of the 2013 Act)