[CS] CS-Executive

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CHAPTER-HEADS

CHAPTER 1

INTRODUCTION

1. COMPANY

Meaning	◆ Company is an **Association of Persons** formed for the purpose to achieve some common objects. ◆ The word 'Company' is derived from the **Latin word (Com=with or together; panis =bread),** and it originally referred to an association of persons who took their meals together.
Definition of Company- Section 2(20)	◆ Company means company formed and registered under this Act (2013) or any other previous Companies Act.

2. NATURE AND CHARACTERISTICS OF COMPANY

◆ Company has following characteristics:	
Incorporated Association	◆ A company must be incorporated or registered under the Companies Act. ◆ Minimum number required for the purpose is **7 in case of a public company and 2 in case of a private company**.
Artificial Person	◆ A company is created with the sanction of law and is not a human being. ◆ Therefore, it is called **artificial**; since it is clothed with certain rights and obligations, it is called a **person**.
Separate Legal Entity	◆ Unlike partnership, company is distinct from the persons who constitute it. ◆ On registration, the association of persons becomes **body corporate** by the name contained in the Memorandum. ◆ In the famous case of **Salomon vs. Salomon & Co. Ltd.**, it was held that a company is at law a different person from its promoters, directors and members.

	Salomon vs. Salomon & Co. Ltd.
	◆ Salomon carried on business as a leather merchant. ◆ He sold his business; for a sum of £30,000 to a company formed by him along with his wife, daughter and four sons. ◆ The purchase consideration was satisfied by allotment of 20,000 shares of £1 each and issue of debentures worth £10,000 secured by floating charge on the company's assets in favour of Mr. Salomon. ◆ All the other shareholders subscribed for one share of £1 each. Mr. Salomon was also the Managing Director of the company. ◆ The company almost immediately ran into difficulties and eventually became insolvent and winding up commenced. ◆ At the time of winding up, the total assets of the company amounted to £6,050; its liabilities were £10,000 secured by the debentures issued to Mr. Salomon and £8,000 owing to unsecured trade creditors. ◆ The unsecured sundry creditors claimed the whole of the company's assets, viz., £6,050 on the ground that the company was a mere alias or agent for Salomon. ◆ It was held that contention of the trade creditors could not be maintained, because the company being in law a person quite distinct from its members could not be regarded as an agent or trustee for Salomon. ◆ In addition, the company's assets must be applied in payment of the debentures as a secured creditor is entitled to payment out of the assets on which his debt is secured in priority to unsecured creditors.
	Lee vs. Lee Air Farming Limited
	◆ In Lee vs. Lee Air Farming Limited, a company was formed for manufacturing of aerial top-dressing. ◆ Lee, a qualified pilot, held all but one of the shares in the company and by the Articles was appointed director of the company and chief pilot. ◆ Lee was killed while piloting the company's aircraft and his widow claimed compensation for his death under the Workmen Compensation Act. ◆ The insurance company opposed the claim on the ground that Lee was not a 'worker' as the same person could not be employer and the employee. ◆ It was held that there was a valid contract of service between Lee and the company, and Lee was, therefore, a worker. Mrs. Lee is entitled to get compensation.
Limited Liability	◆ The company being a separate person, its members are not as such liable for its debts. ◆ In the case of a company limited by shares, the liability of member is **limited to the unpaid value of shares** held by them. Thus, if the shares are fully paid up, their liability will be nil. ◆ However, a company may be formed with **unlimited liability of members.** In case of unlimited liability, companies' members shall continue to be liable until each paise has been paid off. ◆ In case of **company limited by guarantee**, the liability of each member shall be determined by the guarantee amount, i.e., he shall be liable to contribute up to the amount guaranteed by him. ◆ However, in case of a **guarantee company having share capital**, the liability shall be limited to the aggregate of the amount remaining unpaid on the shares held by a member and the amount guaranteed by him.

<table>
<tr><td>Transferability of Shares</td><td colspan="2">◆ Since business is separate from its members in a company form of organization, it facilitates the transfer of members' interest.
◆ The shares of a company are transferable in the manner provided in the Articles of the company.
◆ However, in a private company, certain restrictions have to be placed on such transfer of shares but the right to transfer is not taken away absolutely.</td></tr>
<tr><td>Perpetual Existence</td><td colspan="2">◆ A company being an artificial person cannot be incapacitated by illness and it does not have an allotted span of life.
◆ The death, insolvency or retirement of its members leaves the company unaffected.
◆ Members may come and go but the company can go on forever.</td></tr>
<tr><td rowspan="3">Separate Property</td><td colspan="2">◆ Company is legal person.
◆ It holds and owns property in its own name.
◆ The property of company is not the property of shareholders.
◆ It was held in case of Macaure vs. Northern Assurance Co. Ltd., that even where a shareholder held almost entire share capital, he did not even have an insurable interest in the property of the company.</td></tr>
<tr><td colspan="2">Macaure vs. Northern Assurance Co. Ltd.</td></tr>
<tr><td colspan="2">◆ Macaure was the shareholder of a timber company. He was also a substantial creditor.
◆ He insured the company's timber considering his interest as shareholder and creditor in his own name.
◆ Timber of company was destroyed in fire and he claimed compensation.
◆ The insurance company contented that the company was not property of an individual and refused to compensate.
◆ The Court has held that the property of company is not property of individual and insurance company was not liable.</td></tr>
<tr><td rowspan="3">Common Seal</td><td>What is common seal?</td><td>◆ A company is an artificial person. Therefore, it has to work through its directors, officers and other employees.
◆ However, it can be held bound by only those documents, which bear its signature.
◆ Common seal is the official signature of a company.</td></tr>
<tr><td>Documents requiring common seal</td><td>◆ Now, common seal has been made optional.
◆ Following documents require common seal, if company has common seal:
■ Power of Attorney
■ Share Certificate
■ Share warrant.
◆ Generally, documents which require authentication by a company and contract entered into by company should be signed by any Key Managerial Personnel (KMP) or any officer authorized by board in this behalf.- Section 21</td></tr>
<tr><td>Provisions for use of common seal</td><td>◆ Authority to use common seal can be given only by board meeting. The person affixing common seal must sign the instrument.
◆ The common seal should be kept in custody of authorized person.</td></tr>
</table>

	Importance of common seal	◆ If any deed or contract is signed by director or authorized person on behalf of the company under seal it binds the company. ◆ The other party can rely on document and consider the document as authentic.
Can Sue and be Sued by Other	◆ Company may sue or be sued in its own name.	

3. COMPARISON OF COMPANY AND OTHER FORMS OF BUSINESS

Company vs. HUF	**Company**	**HUF**
	Any person can become member of company.	HUF consists family members only.
	Company is managed by its Board of Directors.	Karta manages business of HUF.
	A person cannot become member of company by birth.	A person becomes member of HUF by birth.
	Registration of company is compulsory.	Registration of HUF is not compulsory.
Company vs. Partnership	**Company**	**Partnership Firm**
	Company is an artificial legal person.	Partnership is not a legal person.
	Company has perpetual succession.	Partnership firm does not have perpetual succession.
	Registration of company is compulsory. Company is registered as per provisions of the Companies Act, 2013.	Registration of firm is option. It is guided by Indian Contract Act, 1872 and Partnership Act, 1932.
	Liability of members of company is limited by shares or by guarantee.	Liability of members is unlimited in a partnership firm.
	A member is not an agent of company or of other members.	Partner is an agent of firm and other partners.
	Member cannot bind company by his act.	Partner can bind firm by his act.
	Ordinary members cannot take part in management of a company. Only director can take part in management.	Partners can take part in management of a firm.
	Shares of a private limited company can be transferred easily.	Partner can transfer his share but the assignee does not become a partner. He is only entitled to share of profits.
	Company is separate legal entity.	Partnership is not separate legal entity.
	A single member cannot wind up a company.	A partnership may be dissolved by any partner at any time.

		◆ It cannot be sued by a member or an outsider for any debts due to it because it **cannot contract for any debt.**
	No winding up	◆ It **cannot be wound up** even under the provisions relating to winding up of unregistered companies. ◆ The profits made by an illegal association are, however, **liable to assessment to income tax. - Gopaji Co vs. C.I.T.A.**
	Always illegal	◆ The illegality of an illegal association cannot be cured by subsequent reduction in the number of its members.- **Kumar Swami Chettiar vs. M.S.M. Chinnathambi Chettiar**

PAST EXAM QUESTIONS

Q-1 **'A company is a separate person from its members'. Explain the circumstances under which the court may disregard the company's corporate personality? (CS June 2003)**

Or

What do you mean by 'lifting of corporate veil'? (CS December 2003)

Or

Explain 'lifting of corporate veil'? (CS June 2006)

Or

What is 'corporate veil'? State the circumstances when it can be lifted. (CS December, 2007)

Or

'Separate personality of a company is a special privilege. In case of dishonest or fraudulent use of this privilege, corporate veil can be lifted'. Discuss. (CS December 2008, June 2014)

Or

Write short note –Piercing through corporate veil. (CS December 2014)

Or

Explain clearly the meaning of 'lifting of corporate veil' in relation to a company incorporated under the Companies Act, 2013. Examining the judicial decisions, state whether 'corporate veil' can be lifted in the following cases: (a) Where the corporate veil has been used for improper conduct; and (b) Where the acts of a company are opposed to workmen? (CS December 2015)

Ans. Please refer paragraph no. 5

Q-2 **Explain a company as a partner. (CS December 2003)**

Ans. Any natural person capable to enter into contract or artificial person can be partner. A company being legal person can enter into contract in its own name. Therefore, company can become partner, if its object clause authorises it to enter into partnership. Company cannot enter into any business which is not supported by its object clause of MOA.

Q-3 **What are the features of a corporate form of business enterprise? (CS December 2003)**

Ans. Please refer paragraph no. 2

Q-4 **Distinguish between 'Company' and 'Partnership'. (CS June 2005, December 2013)**

Ans. Please refer paragraph no. 3

Q-5 **'Company has an independent existence apart from its members.' Comment. (CS December 2005)**

Q-23 **Comment on the following: A company can be regarded as having enemy character under certain circumstances. (CS June 2011)**

Ans. Please refer paragraph no. 5

Q-24 **The competent court of law can entertain a petition for winding up of an illegal association under company law. Comment. (CS June 2011)**

Ans. Statement is incorrect. Illegal association cannot be wound up. Please refer paragraph no. 7

Q-25 **Company law in India has been modelled on the US law. Is statement correct? (CS June 2012)**

Ans. Statement is incorrect. Company law in India is based on English law.

Q-26 **Comment the following: A shareholder who holds 99% of the share capital of a company can be held liable for the acts of the company. (CS June 2012)**

Or

Comment. A shareholder is held personally liable for the acts of the company, if he holds virtually the entire share capital of the company. (CS December 2013)

Ans. Shareholder cannot be held liable for act of company even though he is holding majority or all shares of company. Please refer paragraph no. 2

Q-27 **Common seal acts as the official signature of a company. Comment. (CS December 2013)**

Ans. Please refer paragraph no 2

Q-28 **In an annual general meeting of Amar Pvt. Ltd., all the shareholders were killed in a bomb blast. State, whether the company is still in existence. If so, how? (CS December 2014)**

Ans. Company is still in existence. Death or incapacity of members of company do not affect the existence of company. Company has perpetual succession. Please refer paragraph no. 2

Q-29 **Distinguish between 'Company' and 'limited liability partnership' (CS December 2015)**

Ans. Please refer paragraph no. 3

PRACTICE QUESTIONS

Q-1 **ABC Pvt. Ltd. Company is a Private Company having five members only. All the members of the company were going by car to Mumbai in relation to some business. An accident took place and all of them died. Answer with reasons, under the Companies Act, 2013 whether existence of the company has also come to the end?**

Hint Ans. Death of all members will not create end of company. Company has perpetual succession. Legal heirs of deceased members will be members of company.

Q-2 **Some of the creditors of M/s Get Rich Quick Ltd. have complained that the company was formed by the promoters only to defraud the creditors and circumvent the compliance of legal provisions of the Companies Act, 2013. In this context they seek your advice as to the meaning of corporate veil and when the promoters can be made personally liable for the debts of the company.**

Hint Ans. Please refer paragraph no. 5

Q-3 **F, an assessee, was a wealthy man earning huge income by way of dividend and interest. He formed three Private Companies and agreed with each to hold a block of investment as an agent for it. The dividend and interest income received by the company was handed back to F as a pretended loan. This way F divided his income into three parts in a bid to reduce his tax liability.**

Decide, for what purpose three companies were established? Whether the legal personality of all the three companies may be disregarded?

NOTE:

- This is extract of chapter and not complete chapter. It gives idea about style and you can check your level of comfort.
- This book is useful for December 2016 exam.
- Book is available at all major book stores across India and also available online at:
  - http://www.lionkart.in/single/549
  - http://www.amazon.in/Company-Law-CS-Executive-July-2016/dp/9350719991/ref=sr_1_3?ie=UTF8&qid=1471837456&sr=8-3&keywords=tejpal+sheth
- Recorded lectures of company law along with book is available at www.caclubindia.com (Approximately 45 hours)
- To know more about company law – CS Executive, uou can refer following links:
  - https://www.youtube.com/watch?v=sxFTXYjCAow
  - https://www.youtube.com/watch?v=VhUcR5qWQ54
  - https://www.youtube.com/watch?v=VN9HAiIZjKs