Indian Companies Act, 1956

Meaning and Nature of Companies

A Company implies an association of persons for some common objects or purpose.

As per sec. 3(1)(i), A company means a Company formed and registered under this Act or under any existing Act. Actually , the term company is not defined in sec.3(1)(i), it simply emphasize the formation and registration of a company.

The meaning of Company can be better understood by its Characteristics/Advantages.:-

1.) **Separate legal Entity:-** means a company is separate person in the eyes of Law different from its members and shareholders. Thus, a member cannot be held liable for the company's acts even if he holds substantial part of company's share capital. *(Solomon v/s Solomon and Co. Ltd.)*
2.) **Artificial Person:-** Not a natural person but given some rights and Duties
3.) **Limited Liability of members :-** Either Limited by Shares or Limited by Guarantee.
4.) **Common Seal:-** Official signature of Companies. Every company must have a common seal with its name engraved on it.
5.) **Perpetual Succession or Continous Existence:-** Not effected by incoming and outgoing of members. The company remains the same entity inspite of change in total shareholders.
6.) **Separate property:-** Can purchase and sale properties in its own name. All the property in the name of the company is a separate property which is controlled, managed and disposed of by the company inits own name.
7.) **Transferability of Shares:-** Freely transferable and can be purchased and sold in open market.
8.) **Company may sue and be sued in it own name:-** Company can file suits against others in its own name and others can also file suit against the company.

Disadvantages of Company:-

Company form of organization is however, not an unmixed blessing. Following are the Disadvantages:-

1.) Companies formation requires many formalities and expensive
2.) Company is not a citizen and cannot have benefit of fundamental Rights
3.) Company's Social responsibility is greater
4.) Company's members cannot have effective Control
5.) Company's Tax burden is heavy
6.) Company's winding up is expensive and time consuming

Lifting of Corporate Veil ***means Ignoring Separate Legal Entity Concept***. The advantages of incorporation are allowed to be enjoyed by only those who wants to make an honest use of the company. In this doctrine, the company and its members are taken as single persons not different from each other.

The circumstance under which Court may lift the corporate veil may broadly be Classified under 2 categories:-

A.) Under Statutory Provisions:-

1.) Reduction of members below minimum (Sec.45) i.e. below 2 in case of Pvt. Co. and 7 in case of Public Co.
2.) Misrepresentation in Prospectus. (Sec. 62 & 63)
3.) Failure to Return Application Money, within 130 days after the issue of prospectus. (Sec. 69)
4.) Misdescreption of Names. (Sec. 147)
5.) Group Accounts of Holding – Subsidiary Company. (Sec. 212)
6.) For facilitating the task of an inspector appointed under Sec. 235 or 237 to investigate the affairs of Company
7.) For investigation of ownership of Company (Sec. 247)
8.) Fradulent Control (Sec. 542)
9.) Liability for Ultra Vires Act i.e. acts done beyond the power of the company.

B.) Under Judicial Interpretation:

1.) Protection of Revenue i.e where the medium of body corporate is used to evade taxes
2.) Where it is used to commit fraud and improper conduct
3.) For Determination of enemy character of the company
4.) Where Subsidiaries are formed to act as mere agent of Holding Company
5.) Where Company act as agent of Shareholders
6.) Where a Company is used to avoid welfare legislation
7.) Where Company is used for some illegal or improper purpose
8.) Where Company is mere sham or cloak

Kinds of Companies

Basically there two types of Companies:-
Public Company and Private Company
Meaning of Private Company:- According to Sec3(1)(iii),a private Co. is a company having
Paid Up Share Capital of minimum Rs. 1 lac, and restricts the no. of members to 50 and also restricts the general public to subscribe its shares. Also it cannot accept deposit from general public but can accept deposits from members and directors.
The no. of Debenture holders can be more than 50. Limit is for No. of shareholders only. Minimum No. of shareholders is 2. Also , it has to use the words ' Pvt.Ltd.' at the end of its name.
Meaning of Public Co.:- According to Sec. 3(1)(iv), a company which is not a Private Co. is public Co.
Having minimum paid up capital of Rs. 5 lacs. Also a private Co. , which is subsidiary of a Co. which is not a private Co.
Minimum No. of shareholders is 7. Also , it has to use the words ' Public. Ltd. or Ltd.' at the end of its name.

Statutory Companies:- Companies created by special Act of parliament and is accordingly governed by the statue creating it. However, the provisions of Companies Act apply to them, in so far they are not inconsistent with the same.

Government Company:- A Company in which 51% or more of Share Capital is held by either Central Govt. or State Govt. or by Both.

Classification on Basis of Liability
Co. Limited by Share Capital:- means a Co. in which Shareholders have Limited Liability to the extent of unpaid amount on share, if called up by Co., the Liability of members can be called upon any time during the existence of Company and also in case of Winding Up.
Co. Limited by Guarantee:- A Company having Liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of Company in the event of its being wound up.
Unlimited Company:- A company having no limit on the Liability of its members. It may or may not have share Capital. The AoA of the company must state the no. of members with which it is registered or the amount of share capital , if any, with which it is registered.

Associations Not for Profit
An "Associations Not for Profit" is an association which is formed not for making profits but for promoting commerce, art, science, religion , charity or any other useful social purpose. Such an association may or may not be registered under Companies Act. However, Sec.25 permits the registration under a license granted by Central Govt. without being required to use the words "limited " or "Pvt. Ltd." At the end of their names. The conditions to be fulfilled for the same are:

1.) Intention is to promote commerce, art, science, religion , charity or any other useful social purpose
2.) It prohibits the payment of Dividend to any of its members but intends to apply the same for the promotion of its objects.

It may be noted that a partnership firm may become a member of such Company. However, on dissolution of firm , its membership will come to an end.

Public Financial Institutions(PFI)

Certain institutions have been specified as PFI under Sec.4A, namely ICICI, IFCI Ltd., IDBI, UTI, LIC, IDFC. Central govt. has been further empowered to notify any other institution as a PFI provided it has been constituted by Central Govt.

Holding and Subsidiary Company

Holding Co. is one which has control over another Company. And the Company on which Control is exercised is Subsidiary Co. A Co is a Holding Co . if :-

1.) It Control the composition of Board of Directors ,means, it has the powers to appoint or remove all or majority of the directors of the Company
2.) Holding more than 50% of share Capital of another Co.
3.) Subsidiary of another Subsidiary Co. i.e. Fellow Subsidiary.

Conversion of Public Co. into Pvt. Co.

A public Co. may become a private Co. by altering its AoA by passing a special resolution, so as to include in it the statutory restrictions which are necessary for private Companies. After alteration of AoA the Company must comply with the following restrictions:-

1.) Approval of Central Govt. must be obtained for the conversion.
2.) On Approval, a printed copy must be filed with RoC within one month of the approval.
3.) A copy of Special resolution altering AoA must also be filed with RoC within 30 days of such alteration.

Then the name of Company must be changed so as to include words "Pvt. Ltd."

Conversion of Private Co. into Public Co.

It can be converted in 3 ways:-

1.) Conversion by Default (Sec.43)

If the default is made in complying with the essential requirements of private company, then the company is treated as public Company. However, The CLB may grant relief if it is satisfied that the failure to comply with the conditions was not intentional and also satisfied that on any other ground, it is just and equitable to grant the relief.

2.) Conversion by Operation of Law or Deemed public Companies (Sec.43A)

Circumstances in which Private Companies are treated as Deemed Public Companies:-

a.) A Public Company holding 25% or more of the paid up share Capital of a private Co.
b.) A private Company holding 25% or more of the paid up share Capital of a Public Co.
c.) Annual turnover of a Private Company for the 3 consecutive years becomes 25 crores or more.
d.) A private Company accepting deposits from Public.

3.) Conversion by Choice (Sec. 44)

It may do so by passing a special resolution deleting from its AoA the statutory restrictions essential for the private Company. It must also comply with the following formalities:-

a.) A prospectus or 'statement in lieu of prospectus' must be filed with RoC within 30 days.
b.) A copy of special resolution altering the AoA must be filed with RoC within 30 days.
c.) All other requirements of Companies Act must be complied with.

Formation of a Company

There are 3 stages in formation of a company:-

1.) Promotion of a Company
2.) Registration and incorporation of a Company
3.) Commencement of Business

Promotion of a Company

It refers to all those steps which are taken from the time of having an idea of starting a company to take the time of the actual starting of Company's business. The person who thinks of forming a Company and take necessary steps are known as promoters or company promoters.

Registration and Incorporation of a Company

A company comes into existence when it is registered under Companies Act. For registration of public Co., 7 or more persons are required and for Pvt. Co., 2 or more are required.

A Company is got registered by filing an application with the RoC of the area in which registered office of Co. is situated. Before the registration, it is advisable to take the approval of proposed name from RoC. After approval is granted , application should be filed along with following documents:-

1.) The Memorandum of Association
2.) The Articles of Association
3.) The agreement which the Company proposes to enter into with any individual for appointment as Company's managing Director, or whole time directors or managers
4.) A written consent of such directors to act as directors of the company
5.) A written undertaking by such directors to take and pay for their qualification shares, if any
6.) A list of persons who have agreed to become first directors of company
7.) The declaration that all the requirements of Companies Act relating to registration have been complied with.

Certificate of Incorporation (CoI)

It is issued by the RoC. The legal effects of Certificate of Incorporation are as:-

1.) The Co. comes into existence and becomes separate legal entity.
2.) The company's life starts from the date of CoI
3.) The Co. acquires perpetual succession
4.) The MoA and AoA becomes binding upon Company
5.) The liability of members become limited

The CoI is the conclusive evidence of registration of a company. Its validity cannot be disputed on any ground whatsoever. (Sec.35)

Commencement of Business

After receiving CoI , the company becomes entitled to commence its business.

There is some difference in this regard in case of Public and Private Co. A private Co. can commence its business right after receiving CoI., but a public company can commence its business only after receiving 'certificate to commence business'. Before obtaining such certificate the public companies has to comply with following provisions:-

1.) Public Co. which issues prospectus

a.) The shares payable in cash must have been allotted upto the amount of minimum subscription
b.) The directors must have been paid the application and allotment money on their qualification shares
c.) Any money is not liable to become refundable due to failure to get permission to deal on the stock exchange
d.) A statutory declaration about compliance with all the above requirements duly signed and verified by director or Company secretary

2.) **Public Co. which does not issue prospectus**

a.) A statement in lieu of prospectus must be filed with RoC

b.) The directors must have been paid the application and allotment money on their qualification shares

c.) A statutory declaration about compliance with all the above requirements duly signed and verified by director or Company secretary.

Promoters

As_such promoters has not been defined in the act anywhere, but in the normal sense , promoters are the persons who come together to form a company with some object. They take necessary steps to carry that object into operation. The term promoter is not the term of law but of business usefully summing up in a single word a number of business operations familiar to the commercial world by which a company is generally bought into existence. (Sec.62).

Position /Legal status of a Promoter

1.) They are not the agents of the company
2.) They are not the trustees of the company
3.) They stand in fiduciary relationship within the company and to its shareholders
4.) They should not make an unfair or unreasonable use of their position.

They have in their hands the creation and moulding of a company. They have the power of defining how, and when and in what shape and under what supervision, it shall start into existence and begins to act as trading corporation.

Duties of the Promoters

1.) To disclose all material facts relating to the promotion of the company
2.) To disclose all the profits
3.) All the material facts relating to the purchase of assets should be disclosed
4.) He is not allowed to derive a profit from the sale of its own property , to the company, unless all facts are disclosed
5.) To see that there is no untrue statements n prospectus or statement in lieu of prospectus.

Rights of the Promoters

1.) Right to receive preliminary expenses
2.) Right to receive remuneration, only if there is contract for the same.
3.) Right to receive proportional amount from their co-promoters

Pre-incorporation Contracts i.e. contracts entered into by promoters before incorporation of the company.
These contracts are not binding on company because before incorporation co. does not becomes separate legal entity, as a result it is not competent to enter a contract. Thus the co. can neither be made liable for these contracts nor they can take benefit of these contracts. However, the above principal is subject to the provisions of Special Relief Act, 1963. The relevant provisions are:-

1.) The co. may enforce such contracts if it is 'warranted by the terms of incorporation'. The words 'warranted by the terms of incorporation' means within the scope of company's objects as stated in its MoA. Moreover, the contract must also be for the purpose of Co.
2.) The other party may also enforce the contract if the company has adopted contract after incorporation and within its terms of incorporation.

It may be noted that any contract which do not fall within the company's terms of incorporation, can be made liable to promoters personally.

Memorandum of Association (MoA)

As per Sec.2(28) Memorandum means MoA of a company as originally framed and altered from time to time in pursuance of any provisions of company laws or this act. This definition does not give any idea as to what memorandum really is.
Actually, MoA is a document o great importance in relation to proposed company. It contains the objects for which company is formed and therefore identifies the possible scope of its operations beyond which its action cannot go. It defines as well as confines the power of company. Thus, memorandum is the charter and defines the limitation of the power of a company.

Clauses or contents of MoA

There are 6 clauses in the MoA:-

1.) Name Clause:-

This clause requires a company to state its name. A company to establish its identity must have a name. But no company should be registered by name which in the opinion of central govt. too is undesirable and identical with or which nearly resembles the name of an existing company. Every public Co. must use the word 'limited' after its name and private co. must use the words "private Limited" after its name. It may be noticed that once the company's name is selected and registered it must be made known to the general public.

2.) The Registered Office Clause:-

It is a clause which sates the name of State where the registered office of the company is located. The 2 reasons for the importance of this clause are:-

a.) It ascertains the domicile and nationality of company.

b.) It is a place where various registers relating to the company are kept and to which all the messages and notices must be sent.

The notice of registered office should be given within 30 days from the date of incorporation, to the RoC.

3.) Objects Clause:-

The most important clause of MoA, contains the objects with which the proposed company is to be formed. This clause is divided into 2 sub-clauses namely:-

a.) **Main objects Clause:-** This will state the main objects of the company which are to be pursued by it on its incorporation.

b.) **Other objects Clause:-** It contains those objects which have not been mentioned in the above clause.

The subscribers to the Memorandum are free to choose any lawful objects for their company.

4.) The Liability Clause:-

It is a clause , which states the nature of liability of its members. In case of a company, limited by shares, the liability extends only to the amount unpaid on the shares taken. In case of company limited by guarantee, the members are liable only to the extent of the amount undertaken to be contributed by them to the assets of the company in the event of its being winding up.

5.) Capital Clause:-

It is a clause which states the amount of share capital with which the company is registered. And the number of shares into which the capital is divided and the amount of each share. It states the limit beyond which company cannot go.

6.) Association or Subscription Clause:-

This clause contains the name of persons who sign the MoA and states that they are willing to form themselves into a company. These persons are called as subscribers. The statutory requirements regarding memorandum subscription are:-

a.) It must be signed by each subscriber in the presence of at least one witness.

b.) Each subscriber at least take one share

c.) Each subscriber must write opposite his name the number of shares he takes

Each subscriber to the MoA should pay for the shares he has taken.

Alteration in Memorandum

As per Sec.16, MoA cant be altered except in certain cases. Following are the circumstances:-

1.) **Change of Name:-**

Sec.21 provides that the name of a company can be changed at any time by passing a special resolution at a general meeting of a company and with the written approval of Central Govt. However, no approval of Central Govt. is necessary if the change involves only addition or deletion of word private Ltd.

Procedure:- The application for the name change is required to be made to RoC in form no.1A along with the prescribed fees to ascertain availability of name. the period of validity of the name so allowed is six months.

The change must be communicated to the RoC by filling form no. 23 along with a written copy of the resolution within 30 days of the passing thereof. The change in name shall be sanctioned by roC in the light of guidelines prescribed by the Central Govt. in this behalf.

Change by ordinary resolution:- If through inadvertence or otherwise, a company on its first registration or on registration by a new name has been registerd with a name which in opinion of Central govt. , is identical with or too closely resembles with a name of an existing company, the company may change its name by passing an ordinary resolution and by obtaining the prior approval of the Central Govt.

The registrar will enter the new name on the register in place of old one and issue a fresh CoI.

2.) **Alteration of Registered Office Clause:-**

The change of registered office may include :-

a.) from one place to another in same city or town

b.) from one town to another town in the same state

c.) from one state to another state

Procedure:-

i) A special resolution is to be passed. An advertisement should be given by the co. in the newspaper for the declaration of the change proposed to be made and also a notice to the State Govt. All the shareholders should be informed about this change.

ii) Alteration from one state to another is effective only if it is confirmed by CLB on proper satisfaction about the fact that the notice for such change has been delivered to every person who has interest in the company.And the opinion of creditors has been obtaioned or their debts or claims have been discharged.

iii) An order confirming the alteration must be given by the CLB on such terms and conditions as it thinks fit

iv) A regard is given by CLB to the rights and interest of the members and creditors of the company

v) A certified copy of the order of CLB confirming the alteration must be filed with the RoC within 3 months from the date of order along with the rpinted copy of memorandum

vi) The certificate will be conclusive evidence that all the requirements of the Act have been fulfilled

vii) All the records of the company shall be transferred to the RoC of the state in which the company's registered office is transferred

viii) The alteration become void and inoperative , if the order is not filed within 3 months

Alteration of Object Clause:-

Sec.17 of the companies Act empowers a company to alter its articles by passing a special resolution. A company may change its object clause in so far as it is necessary for any of the following purposes given below:-

i) To carry on its business more economically or more efficiently

ii) To attain its main purpose by new or improved means.

iii) To enlarge or change the local area of its operation.

iv) To carry on some business which under existing circumstances may be conveniently or advantageously combined with the business of the company.

v) To restrict or abandon any of the object specified in the memorandum.

vi) To sell or dispose of the whole or any part of the undertaking to the company.

vii) To amalgamate with any other company or body of persons.

Procedure

To alter the objects of the company, a special resolution is to be passed at a general meeting.

A printed or a typewritten copy of a special resolution is required to be filed with the registrar of companies within 30 days of the passing thereof.

The registrar will register the documents and issue within one month, a certificate which will be conclusive evidence that everything required has been done.

If the required documents are not filed within the specified time. The alteration will at the completion of such period , become void and inoperative.

Alteration of Liability Clause:-

The liability of a member of a company cannot be increased unless the members agrees in writing. The consent of the member may, however, be given either before or after the alteration. Increase in liability may be by way of subscribing for more shares than the number held by him at the date on which the alteration is made or in any other manner.

Alteration of Capital Clause:-

The Company can alter its capital only if it is so authorized by its AoA. Certain alterations in the capital clause may be made by passing an ordinary resolution, and certain by a special resolution.

By ordinary resolution:-

i) Increase of share capital by issue of new shares
ii) Consolidation or sub-division of existing shares into shares of larger or smaller amount.
iii) Conversion of fully paid up shares into stock and vice versa
iv) Cancellation of unissued shares

By special resolution:- Reduction of share capital, it can be made after obtaining permission from court.

Doctrine of Ultra Vires

The Company Act requires that memorandum of the company should include the object clause. The company must bind itself to work within the framework of those objects as stated in MoA. The activities which are not expressely or impliedly authorized by MoA are ultra vires the company.

Ultra vires is the combination of 2 words. 'Ultra' means beyond and 'vires' means power. An act will be ultra vires when it is performed which though legal in itself ,is not permitted by the objects clause in the MoA . These type of acts are void and they cannot be accepted even by unanimous resolution of all the shareholders.

Ultra vires acts may be categorized as :-

1.) **Acts Ultra vires the directors:-** These acts are out of the scope of directors of the company. They are not totally void or inoperative. They can be accepted by the shareholders in general meeting.
2.) **Acts Ultra vires the AoA of the company:-** The acts will be ultra vires if they are beyond the powers given to it by its AoA. They are also not void or inoperative. They can be accepted by the shareholders in general meeting.
3.) **Acts Ultra vires the MoA of the company:-** They are wholly void, inoperative and cannot be accepted even by unanimous resolution of all the shareholders.

Implication of ultra vires acts

The effects of the ultravires transactions are discussed under the following heads:

1.) **Injuction :** in case a company is going to undertake an ultravires act, any member of the company can get an order of injuction from the court to restrain the company for, going ahead with the ultra-vires acts.
2.) **Personal liability of the director :** it is one of the duties of directors to see that the corporate money is used for the legitimate business of the company and not otherwise. The directors shall be personally liable to make good the amount, if any capital is unlawfully disbursed. If the person receiving the money known that he is receiving the payment of an ultra vires act, then he should return the money back to the directors.

3.) **Void-ab initio :** the ultra vires acts by nature are null and void and the company is not bound by these acts. The company cannot sue or be sued upon such acts.
4.) **Ultra-vires acquired property :** a company can protect its property acquired by the ultra-vires expenditure. For example, in case where the company's telephone wires were cut and it had no power in the memorandum to put up the wires, it was held entitled to recover the damages for injury.
5.) **Ultra-vires borrowings:-** If a person lends money to a company and the company has no borrowing powers or had already crossed the limits or borrowing is for the purpose which is ultra vires , then the contract will be declared void.

Exceptions:-
1.) If any act is ultra vires the directors but within the objects of the company, the co. ca accept it
2.) If the act is ultra vires the AoA but within the objects of the company, the AoA may be altered to include the act.
3.) If the act is ultra vires the company but it has done in good faith for the benefit of a company, the person will be freed from its liability
4.) If the co. has taken ultra vires loan and uses it to pay intra vires debts , the co. will be liable not the director. The outsiders can sue the co.

Articles of Association(AoA)

As per sec.2(2) of Companies Act, Articles means the AoA of a company as originally framed and altered from time to time in pursuance of any provisions of any previous company laws or this act. The AoA are the rules and regulations of the company framed for the purpose of internal management of its affairs.

The AoA of the company are subordinate to and are controlled by the MoA. The articles are framed mainly for carrying out the aims and objects of the MoA.

They accept the memorandum as charter of incorporation ad so accepting it the articles proceed to define the dut ies, rights and powers of the governing body.

Companies required to file the AoA:- Following companies are required to file AoA with the RoC.:-
1.) Companies limited by guarantee
2.) Unlimited Companies
3.) Private companies limited by shares.

It is however not obligatory for the public company limited by shares. A public co. may either frame its aAoA or adopt the rules and regulations contained in Table A.

Contents of AoA:-
1.) Exclusion wholly or in part of Table A.
2.) Adoption of preliminary contracts
3.) Number and value of the shares
4.) Allotment of the shares
5.) Call on shares
6.) Lien on shares
7.) Transfer and transmission of shares
8.) Forfeiture of shares
9.) Alteration of capital
10.) Share certificate
11.) Conversion of Shares into stocks
12.) Voting rights and proxies

13.) Meetings
14.) Directors and their appointments
15.) Borrowing powers
16.) Dividend and reserves
17.) Accounts and audit
18.) Winding up.

Procedure for alteration of Articles:-

1.) According to the provisions of companies Act and to the conditions contained in its memorandum, a company may by passing a special resolution alter or add to its articles.
2.) The company must file with the RoC a copy of special resolution within one month from the date of its passing.
3.) The altered articles will bind the member in the same form as the original articles.

Limitations to Alteration of AoA:- The alteration will be valid until they fall in any one of the following categories:-

1.) The alteration must not authorize anything expressly or impliedly forbidden by company law.
2.) The alteration must not extend or modify the memorandum
3.) The alteration must not contain anything illegal
4.) The alteration must not be inconsistent with any alteration made by CLB.
5.) The alteration must be bonafide for the benefit of the Company as a whole
6.) The alteration must not make articles unalterable as it is regarded as bad in law
7.) Retrospective operation of Articles
8.) The alteration must not constitute a fraud on minority by a majority
9.) An alteration of AoA to effect a conversion of a public company into a private company cannot be made without the approval of Central Govt.
10.) There cannot be alteration of articles so as to compel an existing member take or subscribe for more shares or in any way extend liability to contribute to share capital , unless he gives his consent in writing.
11.) A company cannot justify breach of contract with third partiesor avoid a contractual liability by altering articles.

Difference between AoA and MoA

Basis	*MoA*	*AoA*
Meaning	It is the charter of the company and defines the scope of its activities	It is a document which regulates the internal management of the company. these are the rules and regulations made by the company carrying out the objects or purposes.
Relationship	It defines the relationship of company with outside world	It deals with the rights of the members of the company inter se and also establishes the relationship of the company with the members
Types of Documents	Supreme Document	Subordinate to the MoA
Alteration	Cannot be altered except in the manner and to the extent provided by the Act	Can be altered by Special resolution
Provisions if not followed	Becomes ultra vires the company and cannot be ratified even by	Anything done against the provisions of articles but intra vires

	whole body shareholders	the MoA can be ratified

Binding force of MoA and AoA

The legal effects of these documents may be discussed under following heads:-

1.) **These are binding on members in their relation to the company:-** A company can sue its members for the enforcement of the provisions of these documents. The members may also be restrained through court from committing the breach of the provisions of these documents.
2.) **These are binding on company in relation to its members:-** A member can sue the company for the enforcement of the provisions of these documents. The company can also be restrained through court from committing the breach of the provisions of these documents.
3.) **These are impliedly binding on the members in their relation to one another:-** The members of the company, among themselves, are also bound by the provisions of the MoA and AoA.It may however be noted that MoA and AoA do not create any express contract between the members of the company. they are bound on the basis of implied contract.
4.) **These are not binding on the company and its members in their relation to outsiders:-** The AoA creates no contract between the company and outsiders. An outsider, therefore cannot take advantage of the provisions contained in the AoA.

Constructive Notice of MoA and AoA

The term constructive notice means the presumption of notice in certain circumstance. We know that the MoA and AoA are registered with RoC. The office of Registrar is public office. Therefore on registration , these documents become public documents. They are open for public inspection in the RoC office. It is therefore duty of every person dealing with the company to inspect these documents and make sure that his contract with the companyis in accordance with the provisions of these documents. He will be presumed to have read all the documents and to know their contents. The kind of presumed knowledge of these documents is called as constructive notce. If any person enters with the company for any contract which is contrary to the provisions of MoA and AoA, he will not get any right under such contract.

Doctrine of Indoor Management

This doctrine is an exception to the rule of constructive notice. As per the doctrine, the persons dealing with the company have right to assume that as far as the internal proceedings of the company are concerned everything has been done properly. It is necessary to read the registered documents and to see that the proposed dealing is not inconsistent therewith. They are not required to do anything more as per the regularity of internal proceeding.

This doctrine is based on the concept that all things are presumed to have done rightly. The doctrine seeks to protect the outsiders against the company.

Exceptions:-

1.) **Knowledge of irregularity:-** If the person dealing with the company has knowledge of irregularity in internal management.
2.) **Acts void ab initio and forgery:-** The doctrine is applicable to only those irregularities which otherwise might affect the genuine transaction. It does not apply to forgery done by its members.
3.) **No Knowledge:-** a person having no knowledge of Articles cannot ask for protection under indoor management.
4.) **Negligence:-** If the irregularities are discovered by the person dealing with the company on making of proper inquiries , he cannot claim the advantage of rule of indoor management. No protection of the rule is possible where the circumstances surrounding the contracts are so suspicious so as to invite enquiry and the outsider dealing with the company does not make proper inquiry.

5.) **Act outside the scope of apparent authority:-** If an officer of a company enters into a contract which is beyond the scope of his authority, the company is not bound.

Share and Share Capital

Meaning of Share:-

The capital of a company is divided into number of indivisible units of a fixed amount. These units are known as shares. As per sec.2(46), a share is a share in the share capital of a company, and includes stock except where a distinction between stock and share is expressed or implied.

A share not only represent an interest of a shareholder in a company , it carries with it certain rights and liabilities while the company is a going concern or while the company is being wound up.

Meaning of stock:- It can be defined as the aggregate of fully paid up shares of a member merged into one fund of equal value.

Kinds of shares:-

There are 2 types of shares:-

1.) Preference shares
2.) Equity shares

1.) **Preference Shares:-**(Sec.85) Preference share capital means part of the share capital of the company which fulfills both the following requirements:-

a.) During the life of a company, it must be assured of dividend on priority basis i.e. it should get preference on dividend payment.

b.) On the winding up of a company it must carry a preferential right to be paid.

The holder of preference shares have a right to vote on any resolution of the company directly affecting their rights.

Types of preference shares:-

i) Participating or non- participating:- Participating are those shares which get along with preferential dividend right to share or participate in the surplus profits along with equity shareholders . Also in the event of winding up , if there remains any surplus , then they get additional share in the surplus of the company.

ii) Cumulative and non- cumulative:- In cumulative preference share, dividend is cumulated each year till it is finally paid. The dividend becomes payable in the future years if not paid in past. But non- cumulative ,if dividend is not paid in any year , it does not becomes payable in the coming years rather it lapses in the same year.

iii) Reedemable and irredeemable shares:- Subject to authority in AoA, a public ltd. Company may issue redeemable preference shares to be redeemed either at a fixed rate or after a certain period of time during the life time of a company provided the company complies with the certain conditions as contained in sec. 80:-

a) The AoA must provide for the issue of such shares
b) Redemption can be only out of profits available for dividends or out of the proceeds of fresh issue of capital made for this purpose.
c) If premium is payable , it can be paid only out of profits of the company or out of the company's security premium account.
d) No such shares can be redeemed unless they are fully paid
e) Where the shares are redeemed otherwise than the proceeds of fresh issue, a sum equal to the nominal amount of shares redeemed shall be transferred out of divisible profits to the Capital Redemption Reserve Account.

It should be noted that companies Act prohibits the issue of any preference share which is irredeemable or is redeemable after the expiry of 20 years from the date of its issue.

iv) Convertible or Non-convertible preference shares:- Convertible are those which can be converted into equity shares within a certain period, or otherwise non- convertible.

2.) **Equity shares:-** Those shares which are not preference shares. They do not enjoy any preferential rights in the matter of dividend payment or repayment of capital. After satisfying the rights of preference shares, the equity shares shall be entitled to share in the remaining amount of distributable net profits of the company. The dividend on these shares is not fixed and vary from year to year depending on the amount of profits available , on recommendation of board of directors. Equity shareholders have right to vote on every resolution placed in the meeting.

Raising of Share Capital/Issue of Shares

Issue of Shares may be made in 3 ways:-

1.) **By private placement of shares:-** A company can raise its capital by placing the shares privately and without inviting the public for subscription of its shares. In this kind of arrangement, a broker or underwriter finds person who wish to buy the shares. He act merely as an agent and his function is to simply procure the buyers. Since no public offer is made, there is no need to issue prospectus. But a statement in lieu of prospectus is required to be filed with RoC at least 3 days before making allotment of such shares.
2.) **By an offer of Sale:-** Under this arrangement, the company allots or agree to allot the shares at a certain price to a financial institution or an Issue House for sale to the public. The issue house publishes a document called an offer for sale, with an application form attached, offering to the public shares for sale. This document is deemed to be a prospectus.
3.) **By inviting public through prospectus:-** The company invites offers from the general public to subscribe for the shares of the company through prospectus. An investor expected to study the prospectus and if convinced about the prospectus, may apply for the shares.

Allotment of Shares:-

Offer for shares are made on application forms supplied by the company. when an application is accepted, it amounts to an allotment.

General principles regarding allotment:-

1.) **Allotment by proper authority :-** i.e. by BOD or committee appointed by BOD.
2.) **Allotment against application only:-** No oral request will be accepted, only written application.
3.) **Allotment not to be in contravention of any other law:-** the issue will be invalid and void
4.) **Reasonable time:-** question of fact in each case
5.) **Communication:-** Allotment is just like any other contract. So, proper communication must be there to the allotee
6.) **Absolute and unconditional:-** that is must be made on same terms as stated in application.

Statutory provisions regarding allotment:-

1.) **Registration of prospectus:-** that is filing of prospectus to RoC for registration on or before the date of its publication. It should be signed by every person who is named therein as director or proposed director of the company
2.) **Application money:-** Application money should not be less than 5% of the nominal value of shares. As per SEBI , application money should not be less than 25% of the nominal value of shares. And it should be such that minimum total amount payable on shares is within the range of 5000-7000.
3.) **Monies to be kept deposited in separate bank account:-** until the certificate to commence business has been received or in case of co. who has already received the certificate, until the entire amount payable on the application for shares.
4.) **Minimum subscription:-** A public ltd. Company cannot make any allotment of shares until:-
a.) the amount stated in the prospectus as minimum amount has been subscribed.
b.) The sum payable on application for such amount has been paid to and received by the Company
5.) **Statement in lieu of prospectus:-** A company having a share capital, which does not issue prospectus or which has issued such a prospectus but not proceeded to allot shares offered to the public, shall not allot any of the shares unless at least 3 days before the first allotment of the shares , there has been delivered to the RoC for registration of statement in lieu of prospectus.

6.) **Opening of the subscription list:-** Begin on 5th day or later after the day on which prospectus is issued to the general public.

7.) **Closing of the subscription list:-** As per SEBI guidelines:-

For infrastructure Co.:- Min. 3 days and max. 21 days
For other companies:- Min. 3 days and max. 10 days

8.) **Permission to deal on stock exchange:-** Sec.73 requires that every company intending to offer shares to the public for subscription by the issue of prospectus shall, before such issue, make an application to anyone or more recognized stock exchange for permission for the shares to be dealt on that exchange.

9.) **Basis of allotment:-** It shall be on proportionate basis within the specified categories, rounded off to the nearest integer. Minimum allotment will be equal to the minimum application size as fixed and disclosed by the issuer.

10.) **Over-subscription:-** All monies in excess of application monies on shares allotted shall be repaid within 8 days from the day the company become liable to pay.

Effect of Irregular Allotment

S.No.	Nature of Irregularity	Effect on allotment	Liability of Company/director
1	Copy of prospectus not delivered to the RoC	Valid	Co. and every person knowing party to the issue of such prospectus shall be punishable with fine which may extend to RS.50000.
2	Application money being less than 5% of the face value	Voidable	a.)Director if willfully done:- liable for damages to the co. and allotee b.)Co. and every officer of the co. shall be punishable with fine which may extend to Rs.5000.
3	Minimum subscription not received	Voidable	a.) the entire money shall be repaid within 10 days. If not then directors shall repay with interest @6% p.a. b.) Director if willfully done:- liable for damages to the co. and allotee
4	Application money not kept deposited with scheduled bank	Voidable	a.) Director if willfully done:- liable for damages to the co. and allotee b.) Every promoter, director or other person who is knowingly responsible for such contravention shall be punishable with fine which may extend to Rs. 50000.
5	A statement in lieu of prospectus not delivered to RoC	Voidable	a.)Director if willfully done:- liable for damages to the co. and allotee b.) Company and every director responsible will be fined upto Rs. 10000
6	Time limit as to opening of subscription list is not observed	Valid	Co. and every officer of the co. who is in default shall be punishable with fine which may extend to Rs.50000.
7	Condition as to listing of share on RSE not observed	Void	If permission is not granted or refused within 10 weeks from the date of closing of the subscription list, the entire money received shall be paid within 8 days & if not then directors must repay with interest @ 15% p.a.

Underwriting Commission

As per SEBI guidelines, underwriting is an agreement with or without consideration to subscribe to the securities of a body corporate when the existing shareholders of such body corporate or the public do not subscribe to the securities offered by them.

Underwriting commission

Sec.76 allows payment of Underwriting commission subject to following conditions:

(i) the payment of the commission is authorized by the articles;

(ii) the commission paid or agreed to be paid does not exceed in the case of shares, 5% of the price at which the shares are issued and in the case of debentures, 2.5% of the price at which the debentures are issued.

(iii) the amount or rate per cent. of the commission paid or agreed to be paid is –
in the case of shares or debentures offered to the public for subscription, disclosed in the prospectus;
and in the case of shares or debentures not offered to the public for subscription, disclosed in the statement
in lieu of prospectus, and filed before the payment of the commission with the Registrar

(iv) the number of shares or debentures which persons have agreed for a commission to subscribe absolutely or
conditionally is disclosed in the manner as provided in (iii).

(v) a copy of the contract for the payment of the commission is delivered to the Registrar at the time of delivery
of the prospectus or the statement in lieu of prospectus for registration.

(vi) no commission shall be paid under clause (a) of sub-section (1) to any person on shares or debentures which
are not offered to the public for subscription:

But where a person has subscribed or agreed to subscribe under clause (a) of sub-section (1) for any shares in, or debentures of, the company and before the issue of the prospectus or statement in lieu thereof any other person or persons has or have subscribed for any or all of those shares or debentures and that fact together with the aggregate amount of commission payable under this section in respect of such subscription is disclosed in such prospectus or statement, then, the company may pay commission to the first-mentioned person in respect of such subscription.

Issue of Securities at premium

A company may issue securities at premium if it is able to sale it at a price above the par value or face value. Neither Act nor CLB put any restriction on such issue. The rate of premium will be decided by BoD. However, the Act imposes conditions regarding utilization of the premium amount so collected.

As per Sec.78(2), the premium can be utilized for:-

(a) in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares;

(b) in writing off the preliminary expenses of the company;

(c) in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company; or

(d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company.

Issue of Securities at discount

If the buyer of share is required to pay less than the company face value of share, it is called as issue at discount.

It is regulated by Sec.79 which puts certain conditions on such issue:-

1.) A company may issue at a discount shares in the company of a class already issued

2.) The issue of the shares at a discount is authorised by a resolution passed by the company in general meeting, and sanctioned by the CLB.

3.) The resolution specifies the maximum rate of discount (10%) at which the shares are to be issued. But no such resolution shall be sanctioned by the CLB if the maximum rate of discount specified in the resolution exceeds ten per cent., unless that Board is of opinion that a higher percentage of discount may be allowed in the special circumstances of the case;

4.) Not less than one year has at the date of the issue elapsed since the date on which the company was entitled to commence business; and

5.) The shares to be issued at a discount are issued within two months after the date on which the issue is sanctioned by the CLB or within such extended time as the CLB may allow.
6.) Every prospectus relating to the issue of the shares shall contain particulars of the discount allowed on the issue of the shares or exact amount of discount as has not been written off till the date of the issue of the prospectus. If default is made in complying with this sub-section, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to 500 Rs.

Issue of Sweat Equity Shares

It means equity shares issued by the company to employees or directors at a discount or for consideration other than cash. These may be issued for providing know- how or making available intellectual property rights or value additions.
Sec. 79A allows companies to issue subject to following conditions:
1.) A company may issue sweat equity shares of a class already issued
2.) It must be authorized by special resolution
3.) The resolution must specify the number of shares, cmp, consideration, if any, and the class of directors or employees to whom it is issued
4.) Not less than one year has at the date of the issue elapsed since the date on which the company was entitled to commence business; and
5.) If the shares are listed then SEBI regulations should be followed. And if not listed then as per the guidelines as may be prescribed.

Right Issue or further issue of capital

As per sec.81, if the issue of share capital is being made after completion of 2 years from the date of incorporation of the company or after the expiry of one year from the date of its first allotment of shares, then the shares to be issued are to be offered to the existing equity shareholders. This further allotment will increase the subscribed capital.
Further, after the expiry of said period, the new shares of the company may be offered to the persons other than the existing equity shareholders in following circumstances:-

1.) If the company passes a special resolution authorizing the BoD to allot shares to outsiders.
2.) If an ordinary resolution is passed and approval of Central Govt. is obtained.
3.) If any of the shareholder decline to accept the right issue, in that case the BoD may place shares in such a way as they think most beneficial to the company.
4.) Where the convertible debentures are issued by the company, the same may be converted into equity shares and the shares can be further allotted to equity shareholders.
5.) If the company has taken any loan from Central Govt. by issuing debentures and otherwise the govt. may if in public interest change such debentures or loan into shares in the company and the shares can be further allotted.
6.) Where the existing shareholder renounce his right for the shares offered to him to any other person, who may not be the existing equity shareholder.

Buy Back of Shares

The provisions regulating buy back of shares are contained in Section 77A, 77AA and 77B of the Companies Act,1956.

Resources of Buy Back

A Company can purchase its own shares from
(i) free reserves; Where a company purchases its own shares out of free reserves, then a sum equal to the

nominal value of the share so purchased shall be transferred to the capital redemption reserve and details of such transfer shall be disclosed in the balance-sheet or
(ii) securities premium account; or
(iii) proceeds of any shares or other specified securities. **A Company cannot buyback its shares or other specified securities out of the proceeds of an earlier issue of the same kind of shares or specified securities.**

<u>Conditions of Buy Back</u>
(a) The buy-back is authorized by the Articles of association of the Company;

(b) A special resolution has been passed in the general meeting of the company authorizing the buy-back. In the case of a listed company, this approval is required by means of a postal ballot. Also, the shares for buy back should be free from lock in period/non transferability. The buy back can be made by a Board resolution If the quantity of buyback is or less than ten percent of the paid up capital and free reserves;

(c) The buy-back is of less than twenty-five per cent of the total paid-up capital and fee reserves of the company and that the buy-back of equity shares in any financial year shall not exceed twenty-five per cent of its total paid-up equity capital in that financial year;

(d) The ratio of the debt owed by the company is not more than twice the capital and its free reserves after such buy-back;

(e) There has been no default in any of the following
i. in repayment of deposit or interest payable thereon,
ii. redemption of debentures, or preference shares or
iii. payment of dividend, if declared, to all shareholders within the stipulated time of 30 days from the date of declaration of dividend or
iv. repayment of any term loan or interest payable thereon to any financial institution or bank;

(f) There has been no default in complying with the provisions of filing of Annual Return, Payment of Dividend, and form and contents of Annual Accounts;

(g) All the shares or other specified securities for buy-back are fully paid-up;

(h) The buy-back of the shares or other specified securities listed on any recognized stock exchange shall be in accordance with the regulations made by the Securities and Exchange Board of India in this behalf; and

(i) The buy-back in respect of shares or other specified securities of private and closely held companies is in accordance with the guidelines as may be prescribed.

<u>Disclosures in the explanatory statement</u>
The notice of the meeting at which special resolution is proposed to be passed 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 security 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

<u>Sources from where the shares will be purchased</u>
The securities can be bought back from
(a) existing security-holders on a proportionate basis;
Buyback of shares may be made by a tender offer through a letter of offer from the holders of shares of the

company or
(b) the open market through
(i). book building process;
(ii) stock exchanges or
(c) odd lots, that is to say, where the lot of securities of a public company, whose shares are listed on a recognized stock exchange, is smaller than such marketable lot, as may be specified by the stock exchange; or
(d) purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.

Filing of Declaration of solvency

After the passing of resolution but before making buy-back, file with the Registrar and the Securities and Exchange Board of India a declaration of solvency in form 4A. The declaration must be verified by an affidavit to the effect that the Board 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 of the date of declaration adopted by the Board, and signed by at least two directors of the company, one of whom shall be the managing director, if any:
No declaration of solvency shall be filed with the Securities and Exchange Board of India by a company whose shares are not listed on any recognized stock exchange.

Issue of further shares after Buy back

Every buy-back shall be completed within twelve months from the date of passing the special resolution or Board resolution as the case may be.
A company which has bought back any security cannot make any issue of the same kind of securities in any manner whether by way of public issue, rights issue up to six months from the date of completion of buy back.

Prohibition of Buy Back

A company shall not directly or indirectly purchase its own shares or other specified securities -
(a) through any subsidiary company including its own subsidiary companies; or
(b) through any investment company or group of investment companies; or