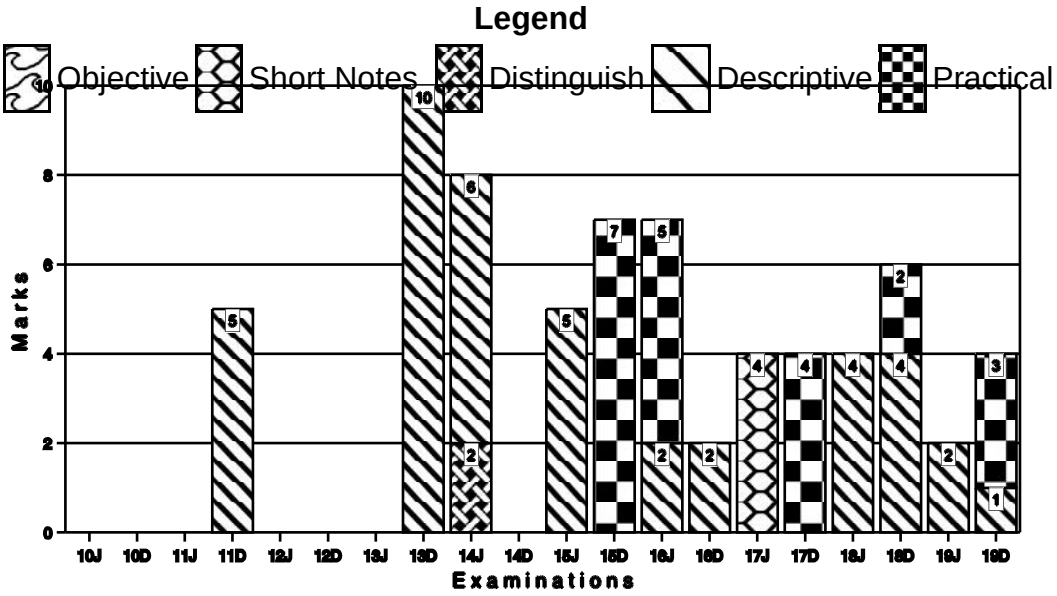
1 COMPANY FORMATION AND CONVERSION

THIS CHAPTER INCLUDES

- Incorporation of companies conversions/reconversion/re-registration.
- Nidhi Companies
- Mutual Benefit Funds and Producer Companies
- Formation of "Not-for-Profit" making companies
- Conversion of LLPs into Private Limited Companies and *vice versa*

Marks of Objective, Short Notes, Distinguish Between, Descriptive & Practical Questions



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CHAPTER AT A GLANCE

Company

A company is an association of both natural and artificial persons incorporated under the existing law of a country. A company has a separate legal entity from the persons constituting it.

Characteristics of a Company

The main characteristics of a company are corporate personality, limited liability, perpetual succession, separate property, transferability of shares, common seal, capacity to sue and be sued, contractual rights, limitation of action, separate management, termination of existence etc.

Doctrine of lifting of or piercing the corporate veil

1. Separate personality of a company is a statutory privilege and it must be used for legitimate business purposes only.
2. Where a fraudulent and dishonest use is made of the legal entity, the individuals concerned will not be allowed to take shelter behind the corporate personality.
3. The Court will break through the corporate shell and apply the principle/doctrine of what is called as “lifting of or piercing the corporate veil”.

LLP

- It is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.
- LLP can continue its existence irrespective of changes in partners.
- It is capable of entering into contracts and holding property in its own name.
- LLP is a separate legal entity, and is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP.

Corporation

An organization formed under state law for the purpose of carrying on a business enterprise is such a manner as to make the enterprise distinct from its owners.

Illegal Association

- As per Section 464 of Companies Act, no association or partnership consisting of more than such number of persons as may be prescribed shall be formed for the purpose of carrying on any business that has for its object the acquisition of gain by the association or partnership or by the individual members thereof, unless it is registered as a company under this Act or is formed under any other law for the time being in force.
- The number of persons which may be prescribed under this section shall not exceed 100. Rule 10 of Companies (Miscellaneous) Rules, 2014 prescribes 50 persons in this regard.

Types of Company

From the point of view of incorporation, companies can be classified as chartered companies, statutory companies and registered companies.

✓ Companies can be categorized as unlimited companies, companies limited by guarantee and companies limited by shares.

✓ Companies can also be classified as public companies, private companies, one person companies, small companies, associations not for profit having license under Section 8 of the Act, Government Companies, Foreign Companies, Holding Companies, Subsidiary Companies, Associate Companies, Investment Companies and Producer Companies.

Private Company

A private company has been defined under Section 2(68) of the Companies Act, 2013 as a company which has a minimum paid-up capital of ₹ 1,00,000 or such higher paid-up capital as prescribed and by its articles restricts the right to transfer its shares, limits the number of its members to two hundred

and prohibits any invitation to the public to subscribe for any securities of the company.

☞ **Amendment Made by Companies (Amendment) Act, 2015**
Provides that in clause (68), the words "of ₹1 lakh or higher paid up share capital" shall be omitted.

One Person Company

One Person Company" means a company which has only one person as a member.

"Small Company''

'Small company'' means a company, other than a public company, (i) paid-up share capital of which does not exceed ₹ 50,00,000 or such higher amount as may be prescribed which shall not be more than ₹ 5 crores; or (ii) turnover of which as per its last profit and loss account does not exceed ₹ 2 crores or such higher amount as may be prescribed which shall not be more than ₹ 20 crores.

Amendment made by Companies (Amendment) Act, 2017:

"Small Company means a company, other than a public company,—

(i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than **ten crore rupees;** and

(ii) turnover of which as **per profit and loss account for the immediately preceding financial year** does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than **one hundred crore rupees."**

Public Company

A public company is a company which (a) is not a private company (b) has a minimum paid-up share capital of ₹ 5 lakh or such higher paid-up capital, as may be prescribed.

☞ **Amendment Made by Companies (Amendment) Act, 2015:**
Provides that in clause (68), the words "of ₹5 lakhs or higher paid up share capital" shall be omitted.

Limited Company
A limited company is a company limited by shares or by guarantee. An unlimited company is a company not having any limit on the liability of its members.
Foreign Company
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.
Investment Company
Investment Company means a company whose principal business is the acquisition of shares, debentures or other securities.
Association not for profit
Section 8(1) permits the registration, under a licence granted by the Central Government, of associations not for profit with limited liability without being required to use the word “Limited’ or the words ‘Private Limited” after their names. The Central Government may grant such a license if: (a) it is intended to form a company for promoting commerce, art, science, sports, education, research, social welfare, religion, charity protection of environment or any such other object; and (b) the company prohibits payment of any dividend to its members but intends to apply its profits or other income in promotion of its objects.

Government Companies
A company in which not less than 51% 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.
Holding Company
As per Section 2 (46), holding company, in relation to one or more other companies, means a company of which such companies are subsidiary companies. Amendment made by Companies (Amendment) Act, 2017 for the purpose of this clause, the expression company includes any body corporate.
Subsidiary Company
Section 2 (87) provides that 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.
Dormant Companies
As per Section 455 (1) where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

Associate Company

As per Section 2(6), “Associate Company”, in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

Amendment made by Companies (Amendment) Act, 2017:

Section 2(6):

(a) the expression "significant influence" means control of at least twenty per cent. of total voting power, or control of or participation in business decisions under an agreement;

(b) the expression "joint venture" means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.”

Position of OPC in India under the Companies Act, 2013

As per Section 2(62) of the Companies Act, 2013, “One Person Company” means a company which has only one person as a member.

Section 3(1)(c) lays down that a company may be formed for any lawful purpose by one person, where the company to be formed is to be One Person Company that is to say, a private company. In other words, one person company is a kind of private company.

A One person company shall have a minimum of one director. Therefore, a One Person Company will be registered as a private company with one member and one director.

Procedure for incorporation of a company

(a) Application for Availability of Name of Company;
(b) Preparation of Memorandum and Articles of Association;
(c) Filing of Documents With Registrar of Companies;
(d) Declaration from the professional;
(e) Declaration from the subscribers to the Memorandum;
(f) Furnishing verification of Registered Office
(g) Filing of particulars of Subscribers
(h) Filing particulars of first directors along with their consent to act as

directors (i) **Power of Attorney :** Execution of power of attorney on a non-judicial stamp paper of a value prescribed in state stamp laws. (j) Issue of Certificate of Incorporation by Registrar.
Conclusive evidence
The certificate of incorporation is conclusive evidence that everything is in order as regards registration and that the company has come into existence from the earliest moment of the day of incorporation stated therein.
Private company to public company
Pass special resolution in general meeting File Form INC 27 with Registrar File MGT 14 for special resolution.
Public to private company
Pass Special Resolution in general meeting File Form INC 27 with Registrar Get NCLT's approval File MGT. 14 for special resolution .
Conversion of Section 8 company to any other kind
• Pass special Resolution in general meeting along with MGT 14 • Application to Regional Director in Form INC 18 (copy to be filed with Registrar) Publication of notice (INC 19) in news paper • Declaration to the effect that no dividend/ bonus is paid • NOC from the relevant regulatory authority • No failure in filing financial statement certificate from PCS/CA/CMA for conversion compliance.
Conversion of one person company to a public company or private company
• If the paid up capital of an OPC exceeds ₹ 50,00,000. Or • Its average annual turnover during the relevant period exceeds ₹ 2 crore. Then it shall cease to be entitled to continues OPC. • Minimum number of members and directors has to be increased accordingly.

Pass special Resolution in General Meeting to alter MOA & AOA Notice to Registrar within 60 days in INC 5.

Conversion of Pvt. company into one person company

Private company other than Section 8 company having paid up share capital of ₹ 50,00,000 or less or Average annual turnover during the relevant period is ₹ 2 crore or less

- Before passing resolution the company shall obtain NOC from members & creditors then pass S/R in General Meeting
- The company shall file an application in INC 6 for its Conversion
- Declaration by Directors by way of affidavit.

465(1)

Proviso to 465(1) states that provisions of Part IX A of the Companies Act, 1956 shall be applicable mutatis mutandis to a Producer Company in a manner as if the Companies Act, 1956 has not been repealed until a Special Act is enacted for Producer Companies.

'Producer'

- A 'Producer' shall mean any person engaged in any activity connected with or relatable to any primary produce.
- The amendment also seeks to provide a comprehensive meaning to primary produce which shall encompass produce of farmers, arising from agriculture (including animal husbandry, horticulture, etc.) produce of persons engaged in handloom, handicraft, any product resulting from any of the above activities or from an ancillary activity and any activity which is intended to increase the production or quality of anything referred above.

Objectives of Producer Companies

Objectives for which Producer Companies may be formed include *inter alia*,

- production, marketing,
- export of primary produce of members,
- processing, packaging of produce of its members, manufacture,
- sale of machinery etc. mainly to its members, generation and

distribution of power,
- insurance of producers/primary produce,
- rendering technical/ consultancy services,
- promoting mutual assistance,
- welfare measures and any other activity for the benefit of members.

No. of Producer

The Act provides that, any ten or more individuals, each of them being a producer or two or more producer institutions or a combination of ten or more individuals and producer institutions, desirous of forming a producer company may form an incorporated company, as such having its objects specified under this Act after complying with the requirements and the provisions of the Act in respect of registration.

Voting in Producer Companies

Unless the membership of the Producer Company consists of a Producer Institution only, every member shall have a single vote irrespective of the number of shares held. Further, every such member shall be entitled to receive a limited return and may be allotted bonus shares.

Memorandum of Association

- The Memorandum of Association is a document which sets out the constitution of the company and is the foundation on which the structure of the company stands.
- It defines as well as confines the powers of the company.
- If the company enters into contract or engages in any trade or business which is beyond the powers conferred on it by the memorandum, such a contract or the act will be *ultra vires* the company and hence void.

Clauses

Memorandum of Association consists of:

(a) Name Clause
(b) Situation Clause

(c) Object Clause
(d) Liability Clause
(e) Capital Clause
(f) Subscription Clause

Articles of Association

- Articles mean the articles of association of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this Act.
- The articles include the regulations contained in Tables F to J in Schedule I of the Act, in so far as they apply to the company.

Alter its Articles of Association

- A company has a statutory right to alter its articles of association.
- But the power to alter is subject to the provisions of the Act and to the conditions contained in the memorandum.
- Any alteration so made shall be as valid as if originally contained in the articles.

Registration of MOA/AOA

The memorandum and articles, when registered, bind the company and its members to the same extent as if they have been signed by the company and by each member to observe and be bound by all the provisions of the memorandum and of the articles.

Alteration of Memorandum of Association

(1) Name Change:
- Pass Special Resolution
- Approval of Central Government
- To delete the word “private” approval from the name, Central Government is not required in case of conversion of private company to public company.

(2) Change in Registered Office:
(a) Change within local limits:

- Pass Board Resolution and Special Resolution Notice of change to Registrar in INC 22 within 15 days of such change

(b) Change of State:
- Approval of Central Govt. In INC 23 the Approval should be registered with Registrar for Incorporation Certificate

(c) Change in jurisdiction of Registrar:
- Get confirmation by Regional Director Communication of confirmation by Regional Director to the company within 60 days.

(3) Change in Liability:
- Needs Special Resolution to be passed.
- File the same with Registrar in Form MGT 14.

(4) Change in Capital:
- alteration of capital clause to be authorised by the Articles of Association [Section 61]; Ordinary Resolution

Doctrine of constructive notice

- As per **doctrine of constructive notice**, every person dealing with the company is deemed to have a "constructive notice" of the contents of its memorandum and articles. Outsiders dealing with incorporated bodies are bound to take notice of limits imposed on the corporation by the memorandum or other documents of constitution.
- Nevertheless they are entitled to assume that the directors or other persons exercising authority on behalf of the company are doing so in accordance with the internal regulations as set out in the Memorandum and Articles of Association.

Doctrine of indoor management

- While the doctrine of constructive notice seeks to protect the company against the outsiders, the doctrine of indoor management operates to protect the outsiders against the company.
- While persons contracting with a company are presumed to know the provisions of the contents of the memorandum and articles, they are entitled to assume that the provisions of the articles have been observed by the officers of the company.

- However, there are certain exceptions to doctrine of indoor management.

Doctrine of *ultra vires*

In the case of a company whatever is not stated in the memorandum as the objects or powers is prohibited by the doctrine of *ultra vires* (The word 'ultra' means beyond and the word 'vires' means powers).

Nidhi Companies

(a) As per Section 406 of the Companies Act, 2013, 'Nidhi' means a company which has been incorporated as a Nidhi with the object of:
   1. cultivating the habit of thrift and savings amongst its members
   2. receiving deposits from, and lending to, its members only, for their mutual benefit, and
   3. which complies with such rules as are prescribed by the Central Government for regulation of such class of companies.

(b) The Central Government may, by notification, direct that any of the provisions of this Act shall not apply, or shall apply with such exceptions, modifications and adaptations as may be specified in that notification, to any Nidhi or Nidhis of any class or description as may be specified in that notification.

Requirements for Minimum Number of Members, Net Owned Fund etc.

(a) Every Nidhi shall, within a period of one year from the commencement of these rules, ensure that it has:
   1. Not less than two hundred members.
   2. Net Owned Funds of ten lakh rupees or more.
   3. Un-encumbered term deposits of not less than ten per cent of the outstanding deposits as specified in Rule 14 and
   4. Ratio of Net Owned Funds to deposits of not more than 1:20.

List of Important Forms

Form No.	Form Type	Purpose of Form as per Companies Act, 2013	Important Section	Important Rule
INC-1	e-Form	Application for reservation of Name	4(4)	8, 9
INC-2	e-Form	One Person Company - Application for incorporation	3(1), 7(1)	4,10, 12,15
INC-3	e-Form	One Person Company –Nominee Consent Form	3(1)	4(2), (3), (4), (5), (6)
INC-4	e-Form	One Person Company – Change in Member/Nominee	3(1)	4(4), (5), (6)
INC-5	e-Form	One Person Company - Intimation of exceeding threshold	–	6 (4)
INC-6	e-Form	One Person Company – Application for Conversion	18	7 (4)
INC-7	e-Form	Applicant for incorporation of Company (Other than OPC)	7(1)	10, 12, 14, 15
INC-8	Physical Form	Declaration	7(1)(b)	14
INC-9	Physical Form	Affidavit	7(1)(c)	15
INC-10	Physical Form	Form for verification of signature of subscribers	–	16 (1) (q)
INC-11	Physical Form	Certificate of Incorporation	7(2)	8
INC-12	Physical Form	Application for grant of License under Section 8	8(1), 8(5)	19, 20
INC-13	Physical Form	Memorandum of Association	–	19 (2)

INC-14	Physical Form	Declaration	7(1)(b)	19 (3) (b)
INC-15	Physical Form	Declaration	–	19 (3) (d)
INC-16	Physical Form	Licence under Section 8(1) of the Companies Act, 2013	–	20
INC-17	Physical Form	Licence under Section 8 (5) of the Companies Act, 2013	–	20
INC-18	e-Form	Application to Regional Director for conversion of Section 8 company into company of any other kind	8 (4) (ii)	21(3)
INC-19	e-Form	Notice	–	22
INC - 20	e-Form	Intimation to Registrar of revocation/surrender of license issued under Section 8	8 (4),8(6)	23
INC - 21	e-Form	Declaration prior to the commencement of business or exercising borrowing powers	11(1) (a)	24
INC - 22	e-Form	Notice of situation or change of situation of registered office	12(2), (4)	25, 27
INC - 23	e-Form	Application to the Regional Director for approval to shift the Registered Office from one state to another state or from jurisdiction of one Registrar to another Registrar within the same State	12 (5), 13(4)	28, 30
INC - 24	e-Form	Application for approval of Central Government for change of name	13 (2)	29 (2)
INC - 25	Physical Form	Certificate of Incorporation pursuant to change of name	–	29

INC - 26	Physical Form	Advertisement to be published in the newspaper for License for existing companies	–	30
INC - 27	e-Form	Conversion of public company into private company or private company into public company	14	33
INC - 28	e-Form	Notice of Order of the Court or any other competent authority	–	–

SHORT NOTES

2017 - June [8] Write short note on the following:
(a) Producer Companies **(4 marks)**
Answer:
Producer Companies:
The Companies (Amendment) Act, 2002 has introduced provisions relating to Producer Companies vide **Sections 581A to 581ZT under Part-IX A** of the **Companies Act, 1956. Section 465 of the Companies Act, 2013,** deals with the provisions relating to repeal of certain enactments and savings. However, **Section 465(1) of the Companies Act, 2013** has retained the provisions relating to Producer Companies and clarifies that these provisions shall continue to be in force in a manner as if the **Companies Act, 1956** has not been repealed until a special Act is enacted for Producer Companies.
In view of the explicit provisions contained in the **Companies Act, 2013**, the Producer Companies are continued to be governed by the **Companies Act, 1956 (Section 581A to 581ZT)** for the time being. Thus, under this topic 'Producer Companies', wherever the word 'Act' is used, it refers to the **Companies Act, 1956.**
It must be understood that the concept of Producer Companies has not taken off despite there being enough potential in view of some of the irritants like restricted tenure of directors of maximum five years. People who have for long been associated with Co-operative and other such movements in India have found that the tenure of five years is too short and would force

people out of the producer companies. The tenure should be suitably enhanced. The Government has done well to retain the old provisions of **Companies Act, 2013**, but should give a try to remove the irritants so that the movement takes off.

—— Space to write important points for revision ——

DISTINGUISH BETWEEN

2014 - June [6] (d) State the distinction between a Mandatory provision and a Directory provision. **(2 marks)**

Answer:

Distinction between a mandatory and directory provision:

- The distinction between a provision which is mandatory and one which is 'directory' is that when it 'mandatory', it must be strictly complied with, when it is 'directory', it would be sufficient that it is substantially complied with.
- Non-observance of mandatory provisions involves the consequences invalidating. But non-observance of directory provision does not entail the consequence of invalidating, whatever other consequences may occur.
- Mandatory provision has a compulsory requirements for compliance while directory provisions provide direction and are suggestive in nature, substance and compliance.

—— Space to write important points for revision ——

DESCRIPTIVE QUESTIONS

2009 - June [8] (b) "A promoter stands in a fiduciary relation towards the company, he promotes"- Explain. **(3 marks)**

Answer:

A promoter stands in a fiduciary(means faithful specially in terms of money) relation (relation requiring confidence or trust) to the company which he promotes. The promoter in such a situation:

(i) must not make, either directly or indirectly, any profit at the expenses of the company which is being promoted.
(ii) must give to the company the benefit of any negotiations or contracts into which he enters in respect of the company,
(iii) must give full disclosure of all the relevant facts, including any profit and his personal interest in a transaction with the Company.

—— Space to write important points for revision ——

2011 - Dec [6] (a) MS. SUCHANDA has entered into a transaction with GLAMOUR LTD. for a contract value of ₹ 40 lacs. The Articles of Association enjoin that contracts above ₹ 10 lacs should be approved in Board Meeting. Mr. Dhuruv, an officer of the company, produces forged documents to her, which show a resolution having been passed in a Board Meeting approving the contract. Later, the forgery comes to light. MS. Suchanda pleads that she is protected by the Doctrine of Indoor Management-Discuss.

(3 + 2 = 5 marks)

Answer:

Doctrine of Indoor Management:

- Doctrine of constructive notice is to protect the company from outsider.
- The doctrine of indoor management is to protect the outsider from the irregularity and mis-management on the part of company.
- These two doctrines *viz*. Doctrine of Constructive Notice and Doctrine of Indoor Management are opposite in nature and operation. Doctrine of Constructive Notice says that an outsider is supposed to have knowledge of MOA and AOA of the company, but as far as the internal management is concerned, he is entitled to assume that everything is in order inside the company and there is no irregularity.
- The Doctrine of Indoor Management is not available in certain cases as enumerated below:

1.	**Knowledge of irregularity**	If the person dealing with the company has prior knowledge of some irregularity, he cannot take the shelter of DOIM. Suppose A Ltd. lent some money to B Ltd. on mortgage of its assets. The procedure as detailed in AOA was not followed. The directors in both the companies were same. In this case the irregularity was in the knowledge of lender before lending, therefore the mortgage is not binding. Doctrine of Indoor Management is not available in such cases.
2.	**Negligence**	If the person has not observed due diligence on his part. If he has enough facility to find out the irregularity or flaw in the process or document by observing little care, caution or concern, he is assumed to have neglected the responsibility on his part. In such cases of negligence Doctrine of Indoor Management is not available.
3.	**Forgery**	The DOIM is not applicable where a person relies upon a document that turns out to be fake, false or forged. A company is not liable for the forgeries or falsification on the part of its officers or employees.
4.	**Acting beyond the authority**	If the officer of a company does something beyond his powers and authority with some third party, the company is not bound. This also comes under the negligence on the part of third party, it should have seen and verified whether the officer is acting within his limits.

Space to write important points for revision

2013 - Dec [1] {C} (a) A group of promoters approach you for advice regarding the formation of a guarantee company. Advise them briefly about the types of organizations for which it is suitable to form a guarantee company and the advantages that can be derived by registering a guarantee company. **(4 marks)**

Answer :

- A guarantee company is a suitable form of organisations which are created to serve some social purposes.
- Such a company is generally recommended for non profit organisations which are engaged in some social and philanthropic purposes.
- Formation of Guarantee Company is a convenient and suitable form for association such as clubs, chamber of commerce, trade associations, societies setup for carrying on charitable work etc.

The advantages of a guarantee company are:

(i) It has most of the advantages enjoyed by a limited company. It has a separate legal entity and can own property, enter into contracts, sue or be sued in regard to its contracts and transactions.

(ii) In respect of the transaction of the company, no personal liability is incurred by the members or director. Their liability arises only on winding up.

- A guarantee company is like any other limited company. It has separate legal entity.
- In a guarantee company the liability of the members is limited.
- In the case of a company having share capital, it is limited by the nominal amount of shares held by each member.
- In the case of a company not having share capital, by amounts of guarantee undertaken by the members i.e., the amounts they shall contribute for the repayment of debts of the company in the event of the company being wound up.

Space to write important points for revision

2013 - Dec [4] (b) In a limited liability partnership (LLP), what are the requirements relating to minimum and maximum number of partners, designated partners and identification numbers for the designated partners? **(4 marks)**

(d) Is it legally necessary for the every producer company to appoint a whole-time secretary under the provision of The Companies Act, 2013.

(2 marks)

Answer:

(b) Partners and designated partners in LLP

- In the case of a LLP there must be a minimum of two partners.
- There is no maximum number prescribed.
- Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.
- The term 'resident' means a person who has stayed in India for a period of not less than one hundred and eighty two days during the immediately preceding one year.
- However, in case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

- There is also the requirement that each designated partner must have a Designated Partner Identification Number DPIN.
- This would mean before making the application for registration the person proposing to act as a designated partner must have obtained the DPIN, in this regard.

(d) Section 465 of the Companies Act, 2013, provides that the Companies Act,1956 shall stand repealed. However, Section 465(1) provides that the provisions of Companies Act, 1956 shall be applicable mutatis mutandis (means same to same, in exactly similar manner) to a Producer Company. Section 581X of the Companies Act, 1956 provides that every producer company having an average turnover exceeding ₹ 5 crores in each of the three consecutive financial years shall have a whole time secretary who is a member of ICSI.

Space to write important points for revision

2014 - June [1] {C} (a) What is the effect of the registration of the Memorandum of Association of a company on

(i) the subscribers of the Memorandum;
(ii) such other persons as may from time to time become members of the company;
(iii) the company and
(iv) outsiders dealing with the company? **(4 marks)**

(e) A producer company wants to issue bonus shares. You are required to state the relevant provisions of the Companies Act, 2013 in this regard. **(2 marks)**

Answer:

(a) When the Memorandum of Association of a company has been registered, it has the following effect:-

(i) The signatories become members of the company, the entry of their names in the register of members not being legally necessary and they are bound to observe all the provisions of the memorandum.
(ii) Such other persons as may from time to time become members of the company are bound by the memorandum, as if it had been signed by them, to observe all the provisions thereof.
(iii) The company is bound to observe all the provisions of its memorandum of association, as if it had been signed by the company.
(iv) The memorandum of association of a company is a public document, and every person dealing with the company is deemed to have notice of its contents. If a person deals with a company in a way contrary to its memorandum, he must take its consequences.

(e)
- Producer Companies are still governed by the Companies Act, 1956 because Section 465(1) of the Companies Act, 2013 provides that provisions of the Companies Act, 1956 shall mutatis mutandis be applicable to the Producer Companies.
- As per provisions of Section 581ZJ of the Companies Act, 1956, any producer company may, upon recommendation of the Board and passing of Resolution in the general meeting, issue bonus shares by capitalization of amounts from General Reserves.

- Referred to in Section 581ZJ, Bonus shares should be issued in proportion to the shares held by the members on the date of issue of such shares.

Space to write important points for revision

2015 - June [1] Answer the question:

(a) Define the term 'Promoter' as contained in the Companies Act, 2013. **(3 marks)**

Answer:

The Companies Act, 2013 has introduced a new definition of Promoter in Sec. 2(69) of the Act which 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.

2015 - June [2] (c) (iv) Explain the provisions under the Companies Act for amendment of articles of association of a producer company. **(2 marks)**

Answer:

Amendment of Memorandum and Articles of Association of a Producer Company:

- A producer company may, by special resolution, (objects of a producer company), alter its objects specified in the memorandum.
- A copy of the memorandum as amended, together with a copy of the special resolution duly certified by two directors, shall be filed with the Registrar within thirty days from the date of adoption of the resolution.
- With a view to alter the memorandum so as to change the address of the producer company, from the jurisdiction of one Registrar to the jurisdiction of another Registrar, a special resolution will have to be passed and copies of the special resolution certified by two directors of the producer company shall be filed with both the Registrars, presumably

with copies of the altered memorandum within thirty days.

- Each Registrar will record the same and thereafter it will be the responsibility of the Registrar from whose jurisdiction the address (the place) has been shifted to forthwith forward to the other Registrar all the documents with him relating to the producer company concerned.
- In case the change involves shifting of the producer company from one state to another, the confirmation of the NCLT is necessary.

—— Space to write important points for revision ——

2016 - June [4] (a) (ii) Is it legally necessary for the every producer company to appoint a whole-time secretary under the provision of the Companies Act, 1956. **(2 marks)**

Answer:

Under Section 581X of the Companies Act,1956 every producer company having an average turnover exceeding ₹ 5 crores in each of three consecutive financial years shall have a whole time secretary who is a member of ICSI.

—— Space to write important points for revision ——

2016 - Dec [2] (c) (ii) Is it obligatory for every producer company to appoint a whole-time Secretary under the provisions of the Companies Act, 1956? **(2 marks)**

Answer:

Please refer 2016 - June [4] (a) (ii) on page no. 42

—— Space to write important points for revision ——

2018 - June [2] (b) The Secretary of a company issued a share certificate to 'Prem' under the company's seal with his own signature and the signature of a Director forged by him. 'Prem' borrowed money from 'Amar' on the strength of this certificate. 'Amar' wanted to realise the security and requested the company to register him as a holder of the shares. Explain whether 'Amar' will succeed in getting the share registered in his name. Explain with the help of the doctrine of 'Indoor management' in brief. **(4 marks)**

Answer:

- The doctrine of indoor management is also known as Turquand's rule. The role of doctrine of indoor management is opposed to of the role of doctrine of constructive notice.
- The doctrine of constructive notice protects company against outsiders whereas the doctrine of indoor management protects outsiders against the actions of company.
- This doctrine also is a possible safeguard against the possibility of abusing the doctrine of constructive notice.
- The person entering into a transaction with the company only needed to satisfy that his proposed transaction is not inconsistent with the articles and memorandum of the company.
- He is not bound to see the internal irregularities of the company and if there are any internal irregularities than company will be liable as the person has acted in the good faith and he did not know about the internal arrangement of the company.
- The rule is based upon obvious reason of convenience in business relations. Firstly, the articles of association and memorandum are public documents and they are open to public for inspection.
- Hence, an outsider is presumed to know the constitution of a company, but what may or may not have taken place within the doors that are closed to him.
- However, this doctrine has several exceptions one of them being forgery, rule does not apply to the transaction involving forgery or illegal transactions which are *void ab initio*.
- In the case of the forged transaction there is lack of consent.
- Here, the question of consent cannot arise as the person whose signature is forged he is not even aware of the transaction.
- However, this doctrine is not applicable where the person dealing with the company has notice of irregularity or when an instrument purporting to be enacted on behalf of the company is a forgery.
- **In the instant problem,** the doctrine of indoor management will not apply as the certificate is a forgery which does not give a good title to Prem and thereby to Amar.

  Hence, Amar will not succeed in getting the share registered in his name.

—— Space to write important points for revision ——

2018 - Dec [2] (a) (i) The common seal is a seal used by Corporation as the symbol of its incorporation and also a statutory requirement for a company. Comment. **(2 marks)**

(iii) Is it obligatory for a Producer Company to have internal audit of its accounts for financial year 2016-17? **(2 marks)**

Answer:

(i) The common seal acts as the official signature of the company. Before companies (Amendment) Act, 2015, the common seal is a seal used by corporation as the symbol of its incorporation and also a statutory requirement for a company. As a departure from this concept, the companies (Amendment) Act, 2015 has deleted the essential of having common seal compulsorily.

After this Amendment, in case a company does not have a common seal, the Authorisation shall be made by two directors or by a director and a company secretary, wherever the company has appointed a company secretary.

(iii) Yes as per Section 581ZF of the Companies Act, 1956, every producer company is required to have internal audit of its accounts carried out by a Chartered Accountant at such intervals and in such manner as may be specified in the articles.

—— Space to write important points for revision ——

2019 - June [2] (a) (i) Although Company is an artificial person, it can still own property and enter into contracts — Comment. **(2 marks)**

Answer:

It is true that Company is an artificial person as it is created by law. However, like a natural person a Company may also own property and enter into contracts. Being an artificial person, Company, enters into contracts through its Board of Directors (BOD). BOD enters into an agreement with others and indicates Company's approval through a common seal.

—— Space to write important points for revision ——

2019 - Dec [2] (c) Answer the following in a few words:

(i) Which type of Public Enterprise is established under a Special Act of the Parliament? (1 mark)

PRACTICAL QUESTIONS

2015 - Dec [1] (A) An association of 120 persons has been formed with the object of acquisition of gain. Now, due to an internal mismanagement, the said association has applied for being wound up under the provisions of the Companies Act, 2013. Advise. **(3 marks)**

Answer:

- According to Section 464 of the Companies Act, 2013, no association or partnership consisting of more than prescribed number of persons shall be formed for the purpose of carrying on any business that has for its object the acquisition of gain by the association or partnership or by the individual members thereof, unless it is registered as a company under the Companies Act, or is formed under any other law for the time being in force. Further, the prescribed number of persons shall not exceed 100.
- The association as mentioned in the question exceed the prescribed number of members i.e., it consists of 120 members and it is not registered as a company under the Companies Act, 2013.
- Where an association is formed, which has membership in excess of the number aforementioned, will be an illegal association except it is registered as company under Companies Act, 2013.
- Such a body will have no legal existence and it cannot be wound up under the Companies Act, 2013, or even as an unregistered company. Neither any member of it would be able to sue it nor would it be able to sue the member.

- Further, every member of an association or partnership carrying on business in contravention of above law, shall be punishable with fine which may extend to one lakh rupees and shall also be personally liable for all liabilities incurred in such business.

Space to write important points for revision

2015 - Dec [2] (c) (ii) Under provisions of Companies Act, 1956, relation to producer company, examine whether the office of director of such company shall fall vacant in the following circumstances:

(a) X, a Director of P.K.R. Ltd., a producer company has made a default in payment of loan taken from a company and default continues for 60 days.

(b) Z, a Director of the above company could not call the Annual General Meeting for the company due to some natural calamity which occurred three days before the schedule date. **(4 marks)**

Answer:

Producer company – Vacation of Office of a Director:

(a) According to provisions of Companies Act, 1956, as contained in Section 581Q, if the producer company in which a director has made a default in repayments of any advances or loans taken from any company or institution or any other person and such default continues for 90 days, the office of such director shall become vacant. **In the given case** the default on the part of X, the director continues for less than 90 (i.e. only 60 days) days, the office of director shall not fall vacant.

(b) The office of director of a producer company shall become vacant if the Annual General Meeting or extraordinary general meeting of the producer company, in which he is a director, is not called in accordance with the provisions of this Act except due to natural calamity or such other reason. **In the given case** since the Annual General Meeting could not be held due to some natural calamity, the office of Z, the director shall not fall vacant. This is an exception.

Space to write important points for revision

2016 - June [3] (b) The promoters of Welcome Company incorporated on 8th June, 2015 has entered into a contract with A on 10th May, 2015 for supply of goods. After incorporation, the company does not want to proceed with the contract. As a company advisor, advise the management of the company, referring to the provisions of the Companies Act, 2013.

(5 marks)

Answer:

(i) It is not only the company which is allowed, under the Specific Relief Act, to adopt and enforce its pre-incorporation claims against third parties, Section 19 of the Specific Relief Act also allows, the other party to enforce the contract against the company if (i) the company had adopted the same after incorporation, and (ii) the contract is warranted by the terms of incorporation. Contracts like preparation and printing of the memorandum, and articles, remunerating the professionals, if any, for securing the registration of the company, renting premises, hiring secretarial staff are envisaged under the Act.

(ii) Pre-incorporation contracts in general are *void ab initio*, and hence not binding on the company. However, under Section 19(e) of the Specific Relief Act, 1963, the party to the contract can enforce the contract against the company, if:

(a) The company had adopted the same after incorporation, and

(b) The contract is warranted by the terms of incorporation.

Thus, unless the company adopts the contract, the other party cannot enforce the same against the Company. There shall be no personal liability for the Promoter, if the agreement provides that:

(i) His liability shall cease once the Company adopts the agreement, and

(ii) Either party may rescind the agreement, if the Company does not adopt it within a specified time.

—— Space to write important points for revision ——

2017 - Dec [7] (c) (i) Central Government and Government of Maharashtra together hold 40% of the paid-up share capital of MN Limited. A government company also holds 20% of the paid-up share capital in MN Limited.

(ii) PQ Limited is a subsidiary but not a wholly owned subsidiary of a government company.

Examine with reference to the provisions of the Companies Act, 2013 whether MN Limited and PQ Limited can be considered as Government Company. **(4 marks)**

Answer:

(i) No, MN Limited cannot be considered as a government company because central and state governments only hold 40% of the shares in MN Limited.

(ii) Yes, PQ Limited is a government company as it is a subsidiary of government company.

—— Space to write important points for revision ——

2018 - Dec [2] (a) (ii) M/s Kaberi Mutual Benefits Nidhi Ltd. is incorporated as a Nidhi Company under the Companies Act, 2013. The Board of Directors of the company have decided to appoint Mr. Raja (a minor) as a member of the company. Referring to the applicable provisions of the Companies Act, 2013 read with rules thereunder, advise them. **(2 marks)**

Answer:

Rules 8(3) of Nidhi Rules, 2014, a minor shall not be admitted as a member of Nidhi. Although, deposit may be accepted in the name of a minor, if they are made by the natural or legal guardian who is a member of Nidhi.

Therefore, the Board of Directors of the company cannot appoint Mr. Raja (a minor) as a member of the company.

—— Space to write important points for revision ——

2019 - Dec [2] (b) (ii) Soma Nidhi Limited proposes to reappoint Mr X, a director who has completed a term of 10 consecutive years as a Director of the Nidhi.

State your views the validity of the above proposals with reference to Nidhi Rules, 2014 formulated under Companies Act, **(3 marks)**

Repeatedly Asked Questions		
No.	**Question**	**Frequency**
1	Is it legally necessary for the every producer company to appoint a whole-time secretary under the provision of the Companies Act, 1956. 16 - June [4] (a) (ii), 16 - Dec [2] (c) (ii)	2 Times

Table Showing Marks of Compulsory Questions										
Year	**15 J**	**15 D**	**16 J**	**16 D**	**17 J**	**17 D**	**18 J**	**18 D**	**19 J**	**19 D**
Descriptive										
Practical		4								
Total		4								