

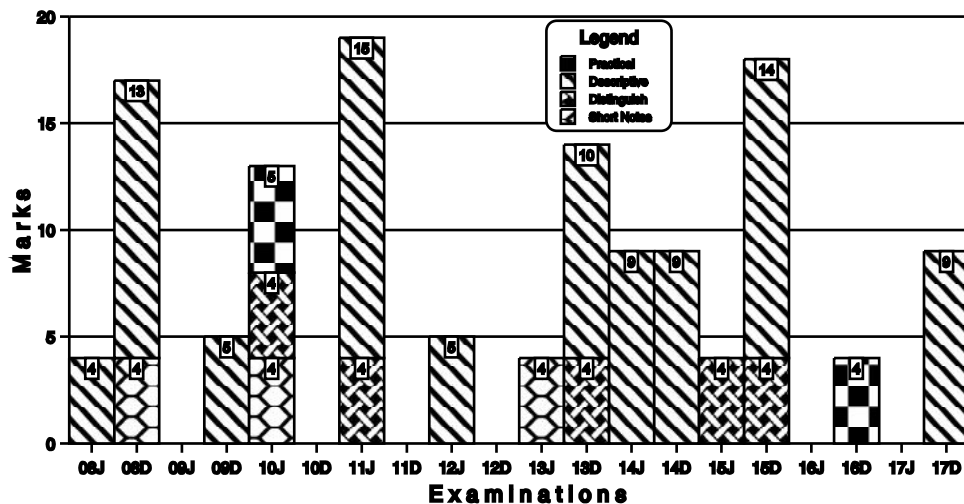
# 1

# INTRODUCTION

## THIS CHAPTER INCLUDES

- Company as a business medium
- Meaning and definition of term company
- Nature and characteristics of a company
- Historical Development of Concept of Corporate Law in India
- Development of Company Law in India and England
- Highlights of the Companies Act, 2013
- Companies vis-a-vis other Forms of business
- Concept of Corporate Personality
- Lifting of Corporate Veil
- Citizenship
- Personal liability of directors or members
- Illegal association.

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



## CHAPTER AT A GLANCE

| Topic   | Important Highlight  |
|---|--|
| <b>1. Company</b>   | 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.   |
| <b>2. Characteristics of a company</b>                          | 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.             |
| <b>3. Compared to other types of business associations</b>      | As compared to other types of business associations, an incorporated company has the advantage of corporate personality, limited liability, perpetual succession, transferable shares, separate property, capacity to sue, flexibility and autonomy.   |
| <b>4. Disadvantages and inconveniences in incorporation</b>     | There are, however, certain disadvantages and inconveniences in incorporation. Some of these disadvantages are formalities and expenses, corporate disclosures, separation of control from ownership, greater social responsibility, greater tax burden in certain cases, cumbersome winding-up procedure. |
| <b>5. Doctrine of lifting of or piercing the corporate veil</b> | (1) Sometime veil of corporate personality is used for some dishonest and fraudulent purpose in that case NCLT will look into reality and remove the corporate veil.   |

|        |  |
|--------|--|
|        | <p>In the following case the Tribunal have lifted the corporate veil.</p> <ul style="list-style-type: none"> <li>• Prevention of fraud and misconduct <b><i>[Gilford Motor Co. Vs. Horne [1933] Ch 935]</i></b></li> <li>• The company is in reality an agency or trust for someone else <b><i>[Re. F G Films Ltd. (1953) 1 All E.R. 615]</i></b></li> <li>• Protection of public policy <b><i>[Connors Vs. Connors Ltd. (1940) 4 All E.R. 179]</i></b></li> <li>• Enemy character of company <b><i>[Daimler Co. Ltd. Vs. Continental Tyre and Rubber Co. (1916) 2 A.C. 307]</i></b></li> <li>• To protect labour welfare legislation <b><i>[Workmen of Associated Rubber Industries Ltd. Vs. Associated Rubber Industries Ltd. A.I.R. 1986 SC 1]</i></b></li> <li>• Use of corporate veil for hiding criminal activities.</li> <li>• To punish for contempt of Court <b><i>[Jyoti Limited Vs. Kanwaljit Kavr Bhasin 32] (1987) DLT 198]</i></b></li> </ul> <p>(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.</p> <p>(3) The NCLT will break through the corporate shell and apply the principle/doctrine of what is called as “lifting of or piercing the corporate veil”.</p> |
| 6. LLP | <p>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.</p>  |

|                               |   |
|-------------------------------|---|
|                               | 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.   |
| <b>7. Corporation</b>         | An organization formed under state law for the purpose of carrying on a business enterprise in such a manner as to make the enterprise distinct from its owners.  |
| <b>8. Illegal association</b> | <p>As per <b>Section 464 of Companies Act</b>, 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. <b>Rule 10 of Companies (Miscellaneous) Rules, 2014</b> prescribes 50 persons in this regard.</p> <p><b>Effects of an illegal association:</b> An illegal association:</p> <ul style="list-style-type: none"> <li>(i) Cannot enter into any contract.</li> <li>(ii) Cannot sue any member, or outsider, not even if the company is subsequently registered.</li> <li>(iii) Cannot be sued by a member, or an outsider for recovery of any debts.</li> <li>(iv) Cannot be wound up by an order of the Tribunal. In fact, the Tribunal cannot entertain a petition for winding up as an unregistered</li> </ul> |

|  |  |
|--|--|
|  | <p>company, for if it did, it would be indirectly according recognition to the illegal association. <b>[Raghubar Dayal Vs. Sarafa Chamber A.I.R. 1954 All. 555]</b></p> <p>However, an illegal association is liable to be taxed. <b>[Kumara Swamy Chattiar Vs. Income Tax Officer (1957) I.T.R. 457].</b></p>   |
| <b>9. Company as a Citizen</b>         | <ul style="list-style-type: none"> <li>• The company, though a legal person, is not a citizen under the <b>Citizenship Act, 1955</b> or under the Constitution of India.</li> <li>• In <b>State Trading Corporation of India Ltd. Vs. CTO AIR 1963 SC 1811</b>, the Supreme Court held that the State Trading Corporation though a legal person, was not a citizen and can act only through natural persons.</li> </ul>                                  |
| <b>10. Nationality &amp; Residence</b> | <ul style="list-style-type: none"> <li>• Though it is established through judicial decisions that a company cannot be a citizen, yet it has nationality, domicile and residence.</li> <li>• In <b>Gasque Vs. Inland Revenue Commissioners (1940) 2 K.B. 88</b>, it was held that a limited company is capable of having a domicile and its domicile is the place of its registration and that domicile clings to it throughout its existence.</li> </ul> |

## SHORT NOTES

**2008 - Dec [5]** (b) Write short note on the following :

- (ii) The separate personality of a company is a statutory privilege and it must be used for legitimate business purposes only.

**(4 marks) [CSEM - II]**

**Answer:**

| S. No. | Heading  | Description  |
|--------|--|--|
| 1.     | <b>Authenticity of the statement</b>               | Statement is correct.  |
| 2.     | <b>Statutory Privilege for legitimate purpose</b>  | As separate personality of the company is a statutory privilege and it must be used for legitimate business purpose only.  |
| 3.     | <b>“Lifting of or piercing the corporate veil”</b> | Where a fraudulent and dishonest use is made of the legal entity, the individuals concerns will not be allowed to take shelter behind the corporate personality. The Tribunal will break through the corporate veil. |

**2010 - June [8]** Write a note on the following:

- (i) Disadvantages of corporate form of enterprise

**(4 marks) [CSEM - II]**

**Answer:**

**Disadvantages of corporate form of enterprises:**

There are certain disadvantages of a corporate form of enterprise. Some of these disadvantages are:

|            |                                 |  |
|------------|---------------------------------|--|
| <b>(a)</b> | <b>Formalities and expenses</b> | Formation of a company is coupled with difficult and detailed legal formalities and procedure involving considerable amount of time and money. |
| <b>(b)</b> | <b>Greater tax burden</b>       | In few circumstances, the tax burden on a company is more than that in comparison to other form of business organization.                      |

|     |                                      |  |
|-----|--------------------------------------|--|
| (c) | <b>Greater social responsibility</b> | Having regard to the enormous powers wielded by the companies and the impact they have on the society, the companies are called upon to show greater social responsibility in their working. |
| (d) | <b>Detailed winding up procedure</b> | Detailed procedure for winding - up of companies which is more expensive and more time consuming.  |

**2013 - June [6]** Write a note on the following:

- (v) Illegal association.

**(4 marks) [CSEM - II]**

**Answer:**

**Please refer 2008 - Dec [8] (a) on page no. 35**

**DISTINGUISH BETWEEN**

**2010 - June [6]** Distinguish between the following:

- (i) 'Company' and 'corporation'.

**(4 marks) [CSEM - II]**

**Answer:**

**Distinction between Company and Corporation.**

|    |   |   |  |
|----|---|---|--|
| 1. | Wider Concept of the Word "Corporation" | The term body corporate is much wider in concept than the word company because it includes: |  |
|    |   | (a) Companies   | Formed and registered under the <b>Companies Act, 2013</b> that is all Indian Companies. |
|    |   | (b) Foreign Companies   | Companies incorporated outside India that is foreign companies.                          |

1.8

■ **Solved Scanner CSEP M-I Paper 1 (New Syllabus)**

|  |  |  |
|--|--|--|
|  | (c) Public Financial Institution   |  |
|  | (d) Nationalized Bank  |  |
|  | (e) Corporations formed under acts of parliaments  |  |
|  | (f) Limited Liabilities Partnerships   | Registered under the Limited Liability <b>Partnership Act, 2008.</b> |
|  | As per <b>Section 2 (11) of Companies Act, 2013</b> , the term body corporate does not include : |  |
|  | (a) Co-operative Society   | Registered under any law relating to Co-operative Societies.         |
|  | (b) Any other body corporate, notified by Central Government in its official gazette             | But not being a company as defined in this Act.                      |

**2011 - June [3]** Distinguish between the following :

(i) 'Company' and 'corporation'.

**(4 marks) [CSEM - II]**

**Answer:**

**Please refer 2010 - June [6] (i) on page no. 25**

**2013 - Dec [2]** Distinguish between the following:

(a) 'Company' and 'partnership firm'.

**(4 marks)**



Answer:

| S. No. | Topic                     | Company   | Partnership Firm  |
|--------|---------------------------|---|---|
| 1      | <b>Regulating Act</b>     | A Company is regulated by the <b>Companies Act, 2013.</b>   | While a partnership is governed by the <b>Indian Partnership Act, 1932.</b>   |
| 2      | <b>Mode of Creation</b>   | Registration is compulsory in case of company.  | Whereas registration is optional in Partnership.  |
| 3      | <b>Minimum Membership</b> | Whereas the minimum number of members in a private company are two and that in case of public company are seven members.                                    | In partnership, the minimum number of partners are two.   |
| 4      | <b>Maximum Membership</b> | Maximum number of member are: <ul style="list-style-type: none"> <li>• For private company: <b>200</b></li> <li>• For Public company : Unlimited</li> </ul> | A partnership with objects of acquisition for gains cannot be formed beyond 50 numbers of partners. <b>[Section 464 read with Rule 10 of Companies (Miscellaneous) Rules, 2014]</b> |
| 5      | <b>Legal Status</b>       | A company has a separate legal personality distinct from that of its members.   | Whereas partnership is not a distinct person, it comprises of several persons who compose it.   |

1.10

■ **Solved Scanner CSEP M-I Paper 1 (New Syllabus)**

|   |                             |  |   |
|---|-----------------------------|--|---|
| 6 | <b>Liability of Members</b> | In case of company, the liability of shareholders is limited to the extent of their share capital or upto the amount of guarantee given by them. | But in case of partnership the liability of partner is unlimited. Each partner is liable to an unlimited extent for the debt incurred in the ordinary course of business. |
| 7 | <b>Transfer of Share</b>    | Shares of a Public Co. are freely transferable   | But in case of partnership, no partner can transfer his share without the consent of other partner.   |

**2015 - June [2]** Distinguish between the following :

(c) 'Limited liability partnership' and 'body corporate'.

**(4 marks)**

**Answer:**

**Limited Liability Partnership (LLP) and Body Corporate**

| Sr. No. | Basis             | Limited Liability Partnership (LLP)   | Body Corporate  |
|---------|-------------------|---|---|
| 1.      | <b>Regulation</b> | LLP is an alternative form of corporate business, not being a company, that gives the benefits of limited liability of a company and the flexibility of a partnership. LLP is covered under the <b>Limited Liability Partnership Act, 2008.</b> | While term "Body Corporate" as defined under <b>section 2(11) of Companies Act, 2013</b> includes a Company incorporated outside India but does not include:<br>(i) a co-operative society registered under any law relating to co-operative societies; and |

|    |   |   |  |
|----|---|---|--|
|    |   |   | (ii) any other body corporate (not being a company as defined in this Act), which the Central Government may, by notification, specify in this behalf. |
| 2. | <b>Incorporation as one person Company</b>  | LLP can't be incorporated by One Person.      | A body corporate may be a company incorporated by one person as One Person Company.  |
| 3. | <b>LLP as body corporate and Vice-Versa</b> | A LLP may be a body corporate.                | But the <i>vice-versa</i> may not be true.   |
| 4. | <b>Compliance Requirements</b>              | LLP will have lesser compliance requirements. | A body corporate will have more compliance requirements.   |

2015 - Dec [2] Distinguish between the following:

(a) 'Company' and 'limited liability partnership'.

(4 marks)

Answer:

| S. No. | Heading           | Description   |
|--------|-------------------|---|
| 1.     | <b>Regulation</b> | A basic difference between an LLP and a joint stock company lies in that the internal <b>governance structure</b> of a company is regulated by statute (i.e. <b>Companies Act, 2013</b> ) whereas for an LLP it would be by a contractual agreement between partners. |

|    |   |   |  |
|----|---|---|--|
| 2. | <b>Management</b>                                   | The <b>management-ownership divide</b> inherent in a company is not there in a limited liability partnership. |  |
| 3. | <b>Compliance requirements</b>                      | LLP will have lesser compliance requirements as compared to a company.  |  |
| 4. | <b>Benefit of limited liability and Flexibility</b> | (a) <b>Limited Liability</b>  | <ul style="list-style-type: none"> <li>• LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership.</li> <li>• LLP can continue its existence irrespective of changes in partners.</li> <li>• It is capable of entering into contracts and holding property in its own name.</li> <li>• LLP is a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP.</li> </ul> |
|    |   | (b) <b>Flexibility</b>  | LLP will have more flexibility as compared to a company.   |

|    |                                 |  |
|----|---------------------------------|--|
| 5. | <b>Enforcement of contracts</b> | LLP is a body corporate and a legal entity separate from its partners, having perpetual succession.  |
| 6. | <b>LLP as a business model</b>  | LLP form is a form of business model which. <ul style="list-style-type: none"> <li>(i) is organized and operates on the basis of an agreement in between partners;</li> <li>(ii) provides flexibility without imposing detailed legal and procedural requirements;</li> <li>(iii) enables professional/technical expertise and initiative to combine with financial risk taking capacity in an innovative and efficient manner.</li> </ul> |

## DESCRIPTIVE QUESTIONS

**2008 - June [6]** (b) Two companies are incorporated with the same set of shareholders. Are they same or distinct under the **Companies Act, 2013**? Discuss. **(4 marks) [CSIG - II]**

**Answer:**

|    |                              |   |   |
|----|------------------------------|---|---|
| 1. | <b>Separate Legal Entity</b> | <b>(i) Separate Corporate Personality</b> | On incorporation, a company becomes a separate legal person in the eyes of law. The company is vested with a corporate personality distinct from individuals who are its members. |
|    |                              | <b>(ii) Own Name and acts</b>             | Being a separate legal entity, it bears its own name and acts under a distinct corporate name.  |

1.14

■ **Solved Scanner CSEP M-I Paper 1 (New Syllabus)**

|           |                         |  |  |
|-----------|-------------------------|--|--|
|           |                         | <b>(iii) Owned assets</b>  | Its assets are separate and distinct from those of its members.  |
|           |                         | <b>(iv) Different person from promoters</b>  | It is also different 'person' from the members who compose it.   |
|           |                         | <b>(v) Owned properties, borrowing money etc</b>   | As such, it is capable of owning property, incurring debts, borrowing money, having a bank account, employing people, entering into contracts and suing or being sued in the same manner as an individual. |
| <b>2.</b> | <b>Conclu-<br/>sion</b> | Thus, the two companies which are incorporated with the same set of shareholders are nevertheless distinct and separate entities [ <i>Patinson v. Bindya Debi AIR 1933 Pat 196</i> ]. [ <i>Theory of Corporate veil; Saloman v. Saloman &amp; Co. Ltd.</i> ] |  |

**2008 - Dec [1] {C}** Comment on the following :

- (i) Common seal of a company will have to be affixed on all the letters and documents of the company. **(5 marks) [CSEM - II]**

**Answer:**

|     |                                      |   |
|-----|--------------------------------------|---|
| (A) | <b>Authenticity of the statement</b> | Statement is not correct.   |
| (B) | <b>Provisions of Companies Act</b>   | <ol style="list-style-type: none"> <li>1. Resolution of Board is required for affixing common seal (if any) of the company on deed and contracts.</li> <li>2. Common seal is affixed only in presence of two directors and Company Secretary or such other person as the Board may appoint for the purpose in accordance with the articles of association.</li> </ol> |

## Amendment Made by Companies (Amendment) Act, 2015

| S. No. | Section in which Amendment is made | Words to be omitted                            | Words to be substituted with  | New Provisions to be inserted in the section  |
|--------|------------------------------------|--|---|---|
| 1.     | Section 9                          | The words “and a common seal” shall be omitted | —   | —   |
| 2.     | Section 22 sub section (2)         | —  | (a) for the words “under its common seal”, the words “under its common seal, if any,” shall be substituted; | (b) <i>The following proviso shall be inserted, namely:—<br/>“Provided that in case a company does not have a common seal, the authorisation under this sub-section shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.”</i> |

1.16

■ **Solved Scanner CSEP M-I Paper 1 (New Syllabus)**

|     |                                   |  |  |   |
|-----|-----------------------------------|--|--|---|
| 3.  | Section 22<br>Subsection<br>(3)   | The words<br>“and have<br>the effect as<br>if it were<br>made under<br>its common<br>seal” shall be<br>omitted | —  | — |
| 4.  | Section<br>46, sub<br>section (1) | —  | <i>For the words<br/>“issued under<br/>the common<br/>seal of the<br/>company”, the<br/>words “issued<br/>under the<br/>common seal,<br/>if any, of the<br/>company or<br/>signed by two<br/>directors or by<br/>a director and<br/>the Company<br/>Secretary,<br/>wherever the<br/>company has<br/>appointed a<br/>C o m p a n y<br/>S e c r e t a r y”<br/>shall be<br/>substituted.</i> |   |
| (c) | Seal when<br>to be used           | ➤ The article of association of a company provide for affixing the seal of the company on documents.           |  |   |



|  |  |  |
|--|--|--|
|  |  | <p>➤ The company seal may be affixed on the following documents after authorisation from AOA &amp; Board resolution:</p> <ul style="list-style-type: none"> <li>(i) Power of attorney.</li> <li>(ii) Deed of lease</li> <li>(iii) Share certificate</li> <li>(iv) Deed of mortgage</li> <li>(v) Promissory notes</li> <li>(vi) Share Warrant etc.</li> </ul> |
|--|--|--|

**2008 - Dec [8]** (a) What do you understand by the term 'illegal association' ?  
**(8 marks) [CSEM - II]**

**Answer:**

**Illegal Association:**

|           |   |  |   |
|-----------|---|--|---|
| <b>1.</b> | <b>Provisions of Section 464 of Companies Act, 2013</b> | <b>Mandatory requirement of registration</b> | <p>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.</p> |
|-----------|---|--|---|

|    |   |  |  |
|----|---|--|--|
|    |   | <b>Exceptions</b>                                  | This section does not apply to:<br>(a) Hindu Undivided Family or<br>(b) An association or partnership formed by professionals who are governed by special Acts like LLP.   |
| 2. | <b>Rule 10 of Companies (Misc) Rules, 2014 as Notified on 1<sup>st</sup> April 2014</b> | <b>Maximum number of members</b>                   | Any unregistered association shall be treated as illegal association provided such association has more than 50 members.   |
| 3. | <b>Companies Act, 2013</b>  | <b>Maximum number of Partners</b>                  | Maximum number of partners of a partnership firm registered under Partnership Act other than LLP. should not exceed 50.  |
|    |   | <b>Limit for banking and other business</b>        | As per Companies Act, 2013, no separate limit is specified for banking and other business, earlier it was 10 in case of banking business and 20 in case of other business. |
| 4. | <b>Hindu Undivided Family Firms</b>   | <b>Limit for members in Hindu Undivided Family</b> | If two or more joint Hindu family firms carry on business together and the combined number of major members exceeds 50, then their association will become illegal.        |
|    |   | <b>Minor members of Joint families</b>             | In computing the number for illegal association, minor members of joint families are to be ignored.  |

|           |  |  |  |
|-----------|--|--|--|
|           |  | <b>Minor members on attaining majority</b> | If by reason of minor members of such joint families on attaining majority, the number of persons exceeds the statutory limit, it will become an illegal association.  |
| <b>5.</b> | <b>Effects of an Illegal Association</b> | <b>Consequences</b>                        | <ol style="list-style-type: none"> <li>1. Cannot enter into any contract.</li> <li>2. Cannot sue any member, or outsider, not even if the company is subsequently registered.</li> <li>3. Cannot be sued by a member, or an outsider for recovery of any debts.</li> <li>4. Cannot be wound up by an order of the Tribunal. In fact, the Tribunal, cannot entertain a petition for winding up as an unregistered company, for if it did, it would be indirectly according recognition to the illegal association.</li> </ol> |
| <b>6.</b> | <b>Penalty</b>                           | <b>Fine</b>                                | Every member of an illegal association shall be punishable with fine which may extend to ₹ 1 lakh and shall also be personally liable for all liabilities incurred in such business.   |

**Note:** However, an illegal association is liable to be taxed. [Kumara Swamy Chattiar Vs. Income Tax Officer (1957) I.T.R. 457].

The members of an illegal association are individually liable in respect of all acts or contracts made on behalf of the association; they cannot either individually or collectively, bring an action to enforce any contract so made, or to recover any debt due to the association. [Wilkinson Vs. Levison (1925)42 T.L.R. 97]

**2009 - Dec [1] {C}** Attempt the following :

- (v) "Common seal of a company will have to be affixed on all the letters and documents of the company." Discuss. **(5 marks) [CSIM - II]**

**Answer:**

**Please refer 2008 - Dec [1] {C} (i) on page no. 32**

**2011 - June [1] {C}** Comment on the following :

- (ii) The managing director and other directors of a company are not liable to be sued for dues against a company. **(5 marks) [CSEM - II]**
- (iii) The competent Tribunal of law can entertain a petition for winding-up of an illegal association under company law. **(5 marks) [CSEM - II]**
- (iv) A company can be regarded as having enemy character under certain circumstances. **(5 marks) [CSEM - II]**

**Answer:**

**(ii)**

|    |                                      |  |   |
|----|--------------------------------------|--|---|
| 1. | <b>Authenticity of the statement</b> | A company being a juristic person, it can sue and can be sued by others in its own name. |   |
| 2. | <b>Case Law</b>                      | <b>Abdul Haq Vs. Das Mal</b>   | If an employee was not paid his salary for several months. He may file a suit against the director of the company for the recovery of the amount of salary due to him. It is held that he will not succeed because the remedy lies against the company and not against the directors or members of the company. |

**(iii)**

|    |   |   |
|----|---|---|
| 1. | <b>No recognition to illegal association by Law</b> | The law does not recognize illegal association and therefore cannot be wound up by order of Tribunal. |
|----|---|---|

|    |                   |   |
|----|-------------------|---|
| 2. | <b>Conclusion</b> | The Tribunal cannot entertain a petition for the winding up of a company formed in contravention of <b>Companies Act, 2013.</b> |
|----|-------------------|---|

(iv)

|    |                                      |  |
|----|--------------------------------------|--|
| 1. | <b>Authenticity of the Statement</b> | The statement is correct based on a case Law - <b>Daimier Co. Ltd. vs. Continental Tyre and Rubber Co. Ltd.</b>  |
| 2. | <b>Analysis of the case law</b>      | <ul style="list-style-type: none"> <li>➤ The facts in question are similar to the facts in <b>Daimler Co. Ltd. Vs. Continental Tyre and Rubber Co. Ltd.</b> a company was incorporated in England to sell tyres manufactured by a German Company.</li> <li>➤ The bulk of the shares of the English Company were held by Germans and all the directors were Germans.</li> <li>➤ During world war, the English Company filed a suit to recover a trade debt.</li> <li>➤ It was held that the company through incorporated in England was an enemy company; and the company was not allowed to proceed with the action to recover its debts.</li> <li>➤ It was laid down that a company may assume an enemy character when persons in defacto control of its affairs are residents of an enemy country or, wherever resident, are acting under the control of enemies.</li> </ul> |

**2012 - June [1] {C}** Comment on the following:

- (ii) A shareholder who holds 99% of the share capital of a company can be held liable for the acts of the company. **(5 marks) [CSEM - II]**

Answer:

|    |   |  |
|----|---|--|
| 1. | <b>Authenticity of the statement</b>                          | The statement is not true.   |
| 2. | <b>Separate Legal Entity</b>                                  | <ul style="list-style-type: none"> <li>➤ A company is an artificial person. It is formed and registered under the Companies Act. It has distinct legal entity. Its personality is separate and distinct from its members.</li> <li>➤ The company's money and property belong to the company and not to the of members of company. Similarly, the members' personal property can not be held liable to pay the creditors of the company.</li> </ul> |
| 3. | <b>Characteristics of company</b>                             | <p>In some cases company is treated as a natural person.</p> <ul style="list-style-type: none"> <li>(a) It can make contracts.</li> <li>(b) Open a bank account.</li> <li>(c) Can sue and be sued by others.</li> <li>(d) It can also own property.</li> </ul>   |
| 4. | <b>Analysis of Case Law: Saloman Vs. Saloman Company Ltd.</b> | This point has clearly established the principle that once a company has been validly constituted under the <b>Companies Act, 2013</b> , it becomes a legal person distinct from its members and for this purpose, it is immaterial whether any member has a large or small proportion of the share capital, and whether he holds those shares beneficially or as a mere trustee.  |
| 5. | <b>Conclusion</b>   | Hence, shareholders can not be held liable for the acts of the company.  |

**2013 - Dec [1]** Comment on the following:

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

(d) Common seal acts as the official signature of a company.

**(5 marks each)**

**Answer:**

(b) *Please refer 2012 - June [1] (ii) on page no. 39*

(d)

| S. No. | Heading  | Description  |
|--------|--|--|
| 1.     | <b>Authenticity of the statement</b>           | The statement is correct.  |
| 2.     | <b>Contracts under the seal of the company</b> | <ul style="list-style-type: none"> <li>➤ On incorporation, a company acquires legal entity with perpetual succession and a common seal.</li> <li>➤ Since the company has no physical existence, it must act through its agents and all such contracts entered into by its agents must be under the seal of the company.</li> </ul>   |
| 3.     | <b>Official signature of the company</b>       | The common seal acts as the official signature of a company. The name of the company must be engraved on its common seal.  |
| 4.     | <b>Authenticity of a document</b>              | <ul style="list-style-type: none"> <li>➤ A rubber stamp of the company on a document does not make it authentic and legal unless such document bears the common seal of the company.</li> <li>➤ The Companies Act or the Articles of Association of a company may require certain instruments or documents to be executed under the common seal of the company.</li> </ul> |

|    |   |   |
|----|---|---|
| 5. | <b>Safe custody of the common seal</b>                | The person authorised to use the seal should ensure that it is kept under his personal custody and is used very carefully because any deed, instrument or a document to which seal is improperly or fraudulently affixed will involve the company in legal action and litigation. |
| 6. | <b>Deeds or contracts to be under the common seal</b> | According to the Companies Act, the following deeds and contracts are required to be under the common seal of the company:<br>➤ Power of attorney<br>➤ Share certificates<br>➤ Share warrant<br>➤ Any deed as required by articles  |
| 7. | <b>Companies Amendment Act, 2015</b>                  | As per the said amendment, the mandatory requirement of Common seal has been removed.   |

**2014 - June [1]** Comment on the following:

- (b) Common seal can be used by any employee of the company irrespective of his designation. **(5 marks)**

**Answer:**

***Please refer 2008 - Dec [1] {C} (i) on page no. 32***

**2014 - June [5]** Answer the following citing the relevant provisions of law/case law, if any:

- (c) "Separate personality of a company is a special privilege. In case of dishonest or fraudulent use of this privilege, corporate veil can be lifted". Discuss. **(4 marks)**



**Answer:**

**Doctrine of lifting of or piercing the corporate veil:**

| S. No. | Points   | Description   |  |
|--------|--|---|--|
| 1.     | <b>Meaning of lifting or piercing the corporate veil</b> | <ul style="list-style-type: none"> <li>● The separate personality of a company is a statutory privilege and it must be used for legitimate business purposes only.</li> <li>● 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.</li> <li>● The Tribunal will break through the corporate shell and apply the principle/doctrine of what is called as “lifting of or piercing the corporate veil”.</li> <li>● The Tribunal will look behind the corporate entity and take action as though no entity separate from the members existed and make the members or the controlling persons liable for debts and obligations of the company.</li> </ul> |  |
| 2.     | <b>When it is lifted</b>                                 | <b>Concerned Case Law:</b> [BSN (UK) Ltd. v. Janardan Mohandas Mohandas rajan Pillai [1996] 86 Com Cases 371 (Bom).]  | The corporate veil is lifted when in defence proceedings, such as for the evasion of tax, an entity relies on its corporate personality as a shield to cover its wrong doings. |

|    |  |  |   |
|----|--|--|---|
| 3. | Shareholders not permitted for the lifting of the veil for their purpose | <b>Concerned Case Law: Premlata Bhatia v. Union of Indian (2004) 58 CL 217 (Delhi)</b> | This was held in wherein the premises of a shop were allotted on a licence to the individual licensee. She set up a wholly owned private company and transferred the premises to that company with the Government consent. She could not remove the illegality by saying that she and her company were virtually the same person. |
|----|--|--|---|

In the following case the Tribunal have after the corporate veil.

|    |   |  |
|----|---|--|
| 1. | <b>Prevention of fraud and misconduct</b> | Where the medium of a company has been used for committing fraud or improper conduct, the Courts have lifted the veil and looked at the realities of the situation. <b>[Gilford Motor Co. Vs. Horne [1993] Ch 935]</b> |
| 2. | <b>Company acting as agent</b>            | Where the company is in reality an agency or trust for someone else and the corporate facade is used to cover up that agency or trust. <b>[Re F G Films Ltd. (1953) 1 All E.R. 615]</b>                                |
| 3. | <b>Protection of public policy</b>        | Where the doctrine conflicts with public policy, Tribunal have lifted the corporation veil for protecting the public policy. <b>[Connors Vs. Connors Ltd. (1940) 4 All E.R. 179]</b>                                   |
| 4. | <b>Enemy Character of Company</b>         | Tribunal will lift the corporate veil if the company has enemy character. <b>[Daimler Co. Ltd. Vs. Continental Tyre and Rubber Co. (1916) 2 A.C. 307]</b>  |

|    |   |  |
|----|---|--|
| 5. | <b>Evasion of taxes</b>                                     | Where the veil has been used for evasion of taxes and duties, the Tribunal upheld the piercing of the veil to look at the real transaction. <b><i>[Re. Dinshaw Maneckjee Petit A.I.R. 1927 Bombay 371]</i></b>   |
| 6. | <b>To protect labour welfare legislation</b>                | Where the purpose of company formation was to avoid the welfare legislation, the Tribunal will lift the corporate veil.<br>Where it was found that the sole purpose for the formation of new company was to use it as a device to reduce the amount to be paid by way of bonus to workman the Supreme Court upheld the piercing of the veil to look at the transaction. <b><i>[Workmen of Associated Rubber Industries Ltd. Vs. Associated Rubber Industries Ltd. A.I.R. 1986 SC1]</i></b> |
| 7. | <b>Use of corporate veil for hiding criminal activities</b> | Where the defendant used the corporate structure as a device to conceal his criminal activities (evasion of customs and excise duties), the Tribunal could lift the corporate veil and treat the assets of the company as the realizable property of the shareholder.  |

**2014 - Dec [1]** Comment with reasons on the following:

(a) Piercing through corporate veil.

**(5 marks)**

**Answer:**

**Please refer 2014 - June [5] (c) on page no. 42**

**2014 - Dec [2A] (Or)** (i) In an annual general meeting of Amar (Pvt.)Ltd., all the shareholders were killed in a bomb blast. State, whether the company is still in existence. If so, how?

**(4 marks)**

Answer:

| S. No. | Heading   | Description   |
|--------|---|---|
| 1.     | <b>Perpetual Succession</b>   | <ul style="list-style-type: none"> <li>➤ Perpetual Succession, therefore, means that the membership of a company may keep changing from time to time, but that does not affect its continuity.</li> <li>➤ A company, being a separate legal person is unaffected by death or departure of any member and remains the same entity, despite total change in the membership.</li> </ul>  |
| 2.     | <b>Death only on winding of the company</b>                               | <ul style="list-style-type: none"> <li>➤ An incorporated company never dies except when it is wound up as per law.</li> </ul>   |
| 3.     | <b>Change in membership</b>   | <ul style="list-style-type: none"> <li>➤ The membership of an incorporated company may change either because one shareholder has transferred his shares to another or his shares devolve on his legal representatives on his death or he ceases to be a member under some other provisions of the Companies Act.</li> <li>➤ Thus, perpetual succession denotes the ability of a company to maintain its existence by the constant succession of new individuals who step into the shoes of those who cease to be members of the company.</li> </ul> |
| 4.     | <b>Survival of company even after death of all the members during war</b> | <ul style="list-style-type: none"> <li>➤ A company's life is determined by the terms of its Memorandum of Association. It may be perpetual or it may continue for a specified time to carry on a task or object as laid down in the Memorandum of Association.</li> </ul>   |

**Note:**

**Professor L.C.B. Gower rightly mentions,** “Members may come and go, but the company can go on forever. During the war all the members of one private company, while in general meeting, were killed by a bomb, but the company survived - not even a hydrogen bomb could have destroyed it”.

**2015 - Dec [1]** Comment on the following:

- (a) A company incorporated under the Companies Act, 2013, being an artificial person, is not entitled to sue a natural person or to sue another company incorporated under the same Act. **(5 marks)**
- (d) A company incorporated under the Companies Act, 2013 never dies except when it is wound-up as per the law. **(5 marks)**

**Answer:**

**(a)**

| S. No. | Heading                                   | Description  |
|--------|---|--|
| 1.     | <b>Authenticity of the statement</b>      | A Company being a body corporate, can sue and be sued in its own name.   |
| 2.     | <b>Legal Framework</b>                    | <ul style="list-style-type: none"> <li>➤ To sue, means to institute legal proceedings against (a person) or to bring a suit in a Tribunal of law.</li> <li>➤ All legal proceedings against the company are to be instituted in its name.</li> <li>➤ Similarly, the company may bring an action against anyone in its own name.</li> </ul>                                  |
| 3.     | <b>Company's right to sue for damages</b> | <ul style="list-style-type: none"> <li>➤ A company's right to sue arises when some loss is caused to the company, i.e. to the property or the personality of the company. Hence, the company is entitled to sue for damages in libel or slander as the case may be [<b><i>Floating Services Ltd. vs. MV San Fransceco Dipaloo (2004) 52 SCL 762 (Guj)</i></b>].</li> </ul> |

1.30

■ **Solved Scanner CSEP M-I Paper 1 (New Syllabus)**

|    |                   |   |
|----|-------------------|---|
|    |                   | ➤ A company, as a person distinct from its members, may even sue one of its own members.  |
| 4. | <b>Conclusion</b> | Hence, a company is entitled to sue a natural person or to sue another company incorporated under the <b>Companies Act, 2013</b> in its own name. |

(d) **Please refer 2014 - Dec [2A] (Or) (i) on page no. 45**

However in case of merger, the transferor company is dissolved without winding up.

**2015 - Dec [2A] (Or)** (i) Explain clearly the meaning of 'lifting of corporate veil' in relation to a company incorporated under the Companies Act, 2013. Examining the judicial decisions, state whether 'corporate veil' can be lifted in the following cases:

- (a) Where the corporate veil has been used for improper conduct; and  
 (b) Where the acts of a company are opposed to workmen? **(4 marks)**

**Answer:**

| S. No. | Heading  | Description   |
|--------|--|---|
| 1.     | <b>Lifting of Corporate Veil under Judicial Interpretation</b> | Ever since the decision in <b>Salomon vs. Salomon &amp; Co. Ltd., (1897) A.C. 22</b> , normally Tribunal are reluctant or at least very cautious to lift the veil of corporate personality to see the real persons behind it. Nevertheless, Tribunal have found it necessary to disregard the separate personality of a company in the following situations |

|  |   |  |  |
|--|---|--|--|
|  | <b>(a) Where the corporate veil has been used for commission of fraud or improper conduct</b> | <b>Case Laws:<br/>In Jones vs. Lipman,<br/>(1962) I.W.-<br/>L.R. 832</b> | <ul style="list-style-type: none"><li>➤ In this case the court lifted the veil and looked at the realities the situation.</li><li>➤ A agreed to sell certain land to B. Pending completion of formalities of the said deal, A sold and transferred the land to a company which he had incorporated with a nominal capital of £100 and of which he and a clerk were the only shareholders and directors. This was done in order to escape a decree for specific performance in a suit brought by B. The Tribunal held that the company was the creature of A and a mask to avoid recognition and that in the eyes of equity A must complete the contract, since he had the full control of the limited company in which the property was vested, and was in a position to cause the contract in question to be fulfilled.</li></ul> |
|--|---|--|--|

(b) Where the acts of a company are opposed to workmen

The Associated Rubber Industries Ltd. Bhavnagar & another, AIR 1986 SC 1

- It has been decided in The Associated Rubber Industries Ltd. Bhavnagar & another, AIR 1986 SC 1 that where the acts of the company are opposed to workmen the corporate veil may be lifted.
- **Brief facts of the case:** In this case, a new company was created wholly by the principal company with no assets of its own except those transferred to it by the principal company with no business or income of its own except receiving dividends from share transferred to it by the principal company i.e. only for the purpose of splitting the profits into two hands and thereby reducing the obligation to pay bonus. The Supreme Court held that the new company was formed as a device to reduce the gross profits of the principal company and thereby reduce the amount to be paid by way of bonus to workmen. The amount of dividends received by the new company should, therefore be taken into account in assessing the



gross profit of the principal company. The corporate veil, therefore was lifted in this case.

**2017 - Dec [1]** Comment on the following:

(d) Three companies incorporated with the same set of shareholders are treated as same companies under the Companies Act, 2013.

**(5 marks)**

**2017 - Dec [3]** (c) One of the subscribers to Memorandum of Association of a company under process of incorporation is a foreign national residing outside India. State the provisions of Companies Act, 2013 regarding authentication of his signature and address. Will the requirement of business visa be applicable to his case if he is a person of Indian origin or overseas citizen of India?

**(4 marks)**

## PRACTICAL QUESTIONS

**2010 - June [5]** (b) Rani is a wealthy lady enjoying large dividend and interest income. She has formed three private companies and agreed with each of them to hold a block of investment as an agent for it. Income received was credited in the accounts of the company but the company handed back the amount to her as a pretended loan. This way, she divided her income in three parts in a bid to reduce her tax liability. Discuss the legality of the purpose for which the three companies were formed.

**(5 marks) [CSEM - II]**

**Answer:**

|    |                         |   |
|----|-------------------------|---|
| 1. | <b>Leading Case Law</b> | <b><i>Sir Dinshaw Maneckjee Petit, A.I.R 1927 Bombay 371.</i></b> If a company is used as a means to evade tax, the <b>Tribunal</b> may disregard the corporate veil. |
|----|-------------------------|---|

1.34

■ **Solved Scanner CSEP M-I Paper 1 (New Syllabus)**

|           |                   | <b>Analysis of the case law</b>   |
|-----------|-------------------|---|
|           |                   | <p>(A) The Supreme Court held that the <b>Tribunal</b> is entitled to lift the mask of corporate entity, if it is used for tax evasion or to circumvent tax obligations.</p> <p>(B) In such cases individual shareholders may be held liable to pay income tax.</p> <p>(C) In the given case, the facts are similar to the above mentioned case. The reason to which the companies were formed by the assessee was purely and simply as a means of avoiding tax liability and the companies were nothing more than the assessee herself.</p> <p>(D) Therefore, the <b>Tribunal</b> disregarded the corporate veil and found that the companies were formed by the assessee for the purpose of avoiding tax.</p> |
| <b>2.</b> | <b>Conclusion</b> | Hence, in view of the above case law Rani can be held liable.   |

**2016 - Dec [4]** (d) Six persons are the only members of Tab (Pvt.) Ltd. All of them went to USA on a pleasure trip by aeroplane. On the way, the plane crashed and all the six members died. Does Tab (Pvt.) Ltd. still exist? Decide. **(4 marks)**

**Answer:**

|           |                             |   |
|-----------|-----------------------------|---|
| <b>1.</b> | <b>Perpetual Succession</b> | <ul style="list-style-type: none"> <li>• An incorporated company never dies, except when it is wound up as per law.</li> <li>• A company, being a separate legal person is unaffected by death or departure of any member and it remains the same entity, despite total change in the membership.</li> <li>• A company's life is determined by the terms of its Memorandum of Association.</li> </ul> |
|-----------|-----------------------------|---|

|           |                   |  |
|-----------|-------------------|--|
|           |                   | <ul style="list-style-type: none"> <li>It may be perpetual, or it may continue for a specified time to carry on a task or object as laid down in the Memorandum of Association.</li> </ul>   |
| <b>2.</b> | <b>Conclusion</b> | The Company has perpetual succession, therefore, means that the membership of a company may keep changing from time to time, but that shall not affect its continuity. Therefore, TAB PVT. LTD. still exist despite of the death of all its members. |

| <b>Repeatedly Asked Questions</b> |  |                  |
|-----------------------------------|--|------------------|
| <b>No.</b>                        | <b>Question</b>  | <b>Frequency</b> |
| <b>1</b>                          | What is 'illegal association'?<br>08 - Dec [8] (a), 13 - June [6] (v)                    | 2 Times          |
| <b>2</b>                          | Distinguish between 'Company' and 'corporation'.<br>10 - June [6] (i), 11 - June [3] (i) | 2 Times          |