

As per Revised Syllabus of Mumbai University for B.Com.,  
Semester IV w.e.f. June 2017 onwards

**Academic Year 2018-19**



# **BUSINESS LAW - II**

Dr. Chandar H. Rohra

**Himalaya Publishing House**

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As per Revised Syllabus of Mumbai University for B.Com. - Semester IV

w.e.f. June, 2017 onwards

Academic Year 2018-2019

**Dr. Chandar H. Rohra**

*B.Com., LL.M., MFM, NET, SET, Ph.D. in Law,*

HOD, Business Law Dept.,

RKT College of Arts, Science and Commerce,

Ulhasnagar - 421003, Dist. Thane.

Former Coordinator and Lecturer,

Nari Gursahani Law College,

Smt. CHM College Campus,

Ulhasnagar - 421003, Dist. Thane.



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New Delhi - 110 002. Phone: 011-23270392, 23278631; Fax: 011-23256286
- Nagpur** : Kundanlal Chandak Industrial Estate, Ghat Road, Nagpur - 440 018.  
Phone: 0712-2738731, 3296733; Telefax: 0712-2721216
- Bengaluru** : Plot No. 91-33, 2nd Main Road, Seshadripuram, Behind Nataraja Theatre,  
Bengaluru - 560 020. Phone: 080-41138821;  
Mobile: 09379847017, 09379847005
- Hyderabad** : No. 3-4-184, Lingampally, Besides Raghavendra Swamy Matham,  
Kachiguda, Hyderabad - 500 027. Phone: 040-27560041, 27550139
- Chennai** : New No. 48/2, Old No. 28/2, Ground Floor, Sarangapani Street, T. Nagar,  
Chennai - 600 012. Mobile: 09380460419
- Pune** : "Laksha" Apartment, First Floor, No. 527, Mehunpura,  
Shaniwarpath (Near Prabhat Theatre), Pune - 411 030.  
Phone: 020-24496323, 24496333; Mobile: 09370579333
- Lucknow** : House No. 731, Shekhupura Colony, Near B.D. Convent School, Aliganj,  
Lucknow - 226 022. Phone: 0522-4012353; Mobile: 09307501549
- Ahmedabad** : 114, "SHAIL", 1st Floor, Opp. Madhu Sudan House, C.G. Road, Navrang  
Pura, Ahmedabad - 380 009. Phone: 079-26560126; Mobile: 09377088847
- Ernakulam** : 39/176 (New No. 60/251), 1st Floor, Karikkamuri Road, Ernakulam,  
Kochi - 682 011. Phone: 0484-2378012, 2378016; Mobile: 09387122121
- Bhubaneswar** : Plot No. 214/1342, Budheswari Colony, Behind Durga Mandap,  
Bhubaneswar - 751 006. Phone: 0674-2575129; Mobile: 09338746007
- Kolkata** : 108/4, Beliaghata Main Road, Near ID Hospital, Opp. SBI Bank,  
Kolkata - 700 010. Phone: 033-32449649; Mobile: 07439040301
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## DEDICATION



**Dedicated to my  
parents, wife and guru  
who have been the  
source of my  
inspiration at every  
moment of life**

## PREFACE

I am very much glad to present this Edition of my Business Law textbook for Semester IV for the S.Y.B.Com. students.

This book is prepared keeping in mind the requirements of the students of Semester IV, S.Y.B.Com. for External examination as per the Revised Syllabus w.e.f. June 2017. Keeping in mind the examination, several problems, case studies on each topic are discussed and explained.

This paper for External examination is divided into five modules.

In the First Module – Indian Companies Act, 2013 (Part – I), topic wise Provisions of Incorporation, classification, MOA, AOA and its alteration, Prospectus of companies, Doctrine of Constructive notice, Doctrine of Indoor management with relative case laws and explanations are provided.

Module Two is Indian Companies Act, 2013 (Part – II) with provisions relating to Members, Directors meetings with its relative provisions.

Module Three is about Indian Partnership Act, 1932 and LLP 2008. It consists of concept of partnership, types, Relationship of partners, distinguish with other forms of business and Dissolution of partnership. The LLP Act, 2008 will make us understand about concept of LLP, Liability of Partners and Firm, In corporation, Conversion and Dissolution. To make it understandable effectively, efforts are put by giving several easy illustrations and case studies.

Module Four is about Consumer Protection Act, 1986 and Competition Act, 2002. It says about Consumer, Dispute, Complaint, Defects, Deficiency, Redressal Agencies and its Mechanisim. The Competition Act, 2002 narrates about Competition policies, Abuse of Dominant position, Competition Commission in India etc.

Module Five consists of Intellectual Property Right (IPR). It deals with its Nature, Concept. Provision relating to Trademark, Patents, Copyrights which are discussed with the required Explanation, Illustrations and Case laws.

After reference of required books and papers, provisions of law are defined and explained in a simplified method for easy understanding of the students. An effort is made to eliminate unnecessary details with concentration to the syllabus. It will help the pupils to understand the role of law in their contemporary course.

December, 2018

**Dr. Chandar H. Rohra**

## ACKNOWLEDGEMENTS

The credit for bringing about this edition goes to the my fellow students from different faculties for their encouragement and good response to Semester-III textbook.

However, no book can be brought out without the support of trustworthy persons and the necessary resources.

My thanks to colleagues from mine and other colleges for their support and help in bringing out this edition.

My gratefulness to my family and friends for their inalienable support.

Last but not the least my gratitude to the publisher for the continued support and cooperation.

**Dr. Chandar H. Rohra**

# SYLLABUS

Academic Year 2018-2019

As per Revised Syllabus of Mumbai University for B.Com. - Semester IV  
w.e.f. June, 2017 onwards

Core Course (CC)

Business Law - II

Sr. No.	Modules	No. of Lectures
1.	Indian Companies Act, 2013 (Part – I)	12
2.	Indian Companies Act, 2013 (Part – II)	12
3.	Indian Partnership Act, 1932 and Limited Liability Partnership (LLP) Act, 2008	12
4.	Consumer Protection Act 1986 and Competition Act, 2002	12
5.	Intellectual Property Rights	12
<b>Total</b>		<b>60</b>

## MODULE – I: INDIAN COMPANIES ACT – 2013 (Part – I)

- ▶▶ Company – Concept, Features, Role of Promoters (S.2(69) S. 92), Duties and Liabilities of the Promoter, Effects of Pre-incorporation Contracts, Consequences of Non-registration, and Lifting of Corporate Veil.
- ▶▶ Classification of Companies, Distinction between Private Company and Public Company, Advantages and Disadvantages of Private Company and Public Company, Procedure for Incorporation of Company.
- ▶▶ Memorandum of Association (MOA) and Article of Association (AOA) – Concept, Clauses of MOA, AOA – Contents, Doctrine of Constructive Notice, Doctrine of Ultra Vires, Doctrine of Indoor Management.
- ▶▶ Prospectus – Concept, Kinds, Contents, Private Placement.

## MODULE – II: INDIAN COMPANIES ACT – 2013 (Part II)

- ▶▶ Member of a Company – Concept, Who can become a Member?, Modes of Acquiring Membership, Cessation of Membership, Rights and Liabilities of Members.
- ▶▶ Director – Qualifications and Disqualifications, Classification, Director Identification Number (DIN), Legal Position of Directors.
- ▶▶ Meetings – Types, Legal Provisions of Statutory Meeting, Annual General Meeting, Extraordinary Meeting, Board Meetings.

**MODULE – III: INDIAN PARTNERSHIP ACT, 1932 AND  
LIMITED LIABILITY PARTNERSHIP (LLP) ACT, 2008**

- ▶▶ Partnership – Contents, Essentials, True Test of Partnership, Partnership Deed, Types of Partnerships, Rights and Duties of Partners, Distinguish between Partnership and Hindu Undivided Family (HUF)
- ▶▶ Dissolution – Concept, Modes of Dissolution, Consequences of Dissolution.
- ▶▶ Limited Liability Partnership (LLP) Act, 2008 – Concept, Characteristics, Advantages and Disadvantages, Procedure for Incorporation.
- ▶▶ Extent of LLP – Conversion of LLP, Mutual Rights and Duties of Partners, Winding up of LLP, Distinction between LLP and Partnership.

**MODULE – IV: CONSUMER PROTECTION ACT, 1986 AND COMPETITION ACT, 2002.**

- ▶▶ Consumer Protection Act – Concept, Objects, Reasons for Enacting the Consumer Protection Act, Definition of Consumer, Consumer Dispute, Complaint, Complainant, Defect, Deficiency, Consumer Dispute, Unfair Trade Practices, Goods and Services.
- ▶▶ Consumer Protection Councils and Redressal Agencies – District, State and National.
- ▶▶ Competition Act, 2002 – Concept, Salient Features, Objectives and Advantages.
- ▶▶ Abuse of Dominant Position, Competition Commission of India, Anti-competition Agreements.

**MODULE – V: INTELLECTUAL PROPERTY RIGHTS**

- ▶▶ Intellectual Property Right (IPR) – Concept, Nature, Introduction and Background of IPR in India.
- ▶▶ IPR Relating to Patents – Concepts of Invention and Discovery, Comparison (S2 (j)), Concepts of Patents, General Principles Applicable to Working of Patented Inventions, Term of Patent, Infringement of Patent Rights and Remedies. (Ss.104-115).
- ▶▶ IPR Relating to Copyrights – Concept of Copyright (Ss. 14, 16, 54,) Concept of Author and Authorized Acts, (S.2) Ownership of Copyright (S.17), Duration or term of Copyright. (Ss.22-27), Original Work and Fair use, Rights of Copyright Holder, Infringement of Copyrights & Remedies. (Ss. 51, 52).
- ▶▶ IPR Relating to Trademarks – Concept, Functions of Trademarks, Types, Trademarks that cannot be Registered, Registration of Trademarks and Rights of the Proprietor of Trademarks, Procedure for Registration of Trademarks, Infringement of Trademarks and Remedies.



# QUESTION PAPER PATTERN

## Semester End Examination

**Total Marks : 100**

**Duration : 3 hours**

**N.B (1) All Questions are Compulsory.**

**(2) Attempt any two questions from each.**

**Q.1 Attempt any two of the following: (Module I)**

- (a) (10 Marks)
- (b) (10 Marks)
- (c) (10 Marks)
- (d) (10 Marks)

**Q.2 Attempt any two of the following: (Module II)**

- (a) (10 Marks)
- (b) (10 Marks)
- (c) (10 Marks)
- (d) (10 Marks)

**Q.3 Attempt any two of the following: (Module III)**

- (a) (10 Marks)
- (b) (10 Marks)
- (c) (10 Marks)
- (d) (10 Marks)

**Q.4 Attempt any two of the following: (Module IV)**

- (a) (10 Marks)
- (b) (10 Marks)
- (c) (10 Marks)
- (d) (10 Marks)

**Q.5 Attempt any two of the following: (Module V)**

- (a) (10 Marks)
- (b) (10 Marks)
- (c) (10 Marks)
- (d) (10 Marks)

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# Introduction to Law

Sometimes it seems as though we cannot do anything in today's world without consulting an attorney. Over the past few decades, law has crept and clawed its way further into our daily lives. Law, in one form or another, permeates modern society, including business environment, which is subject to numerous laws and regulations at all levels of government – local, state, federal, and in limited circumstances, international. Consequently, today's business-persons benefit themselves and their organizations by acquiring a basic, working knowledge of the law.

Learning the basics of business law includes not only learning some substantive law but also how to spot issues for consideration. In fact, such **“issue-spotting”** may be the more important of the two. In the business world, we may not always know what the substantive law is but if we can spot the issue (hopefully before it becomes a problem), we will be able to raise it with the appropriate persons within the organization, with outside counsel, or find the answer ourselves.

## What is Law?

Many legal scholars have tried to answer the essential, but difficult question, ‘what is law?’ In his 1881 book *The Common Law*, US Supreme Court Justice Oliver Wendell Holmes stated that “the Law embodies the story of a nation's development through many centuries and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics.” Accordingly, because the law is not math, a precise definition may be unattainable.

According to *A Dictionary of Basic Legal Terms*, law is “the regime that orders human activities and relations through systematic application of the force of politically organized society, or through social pressure, backed by force, in such a society.” This definition of law, while true, is too abstract and long for our needs. We should therefore think of law in more basic terms as rules that govern and guide actions and relations among and between persons, organizations, and governments. This is the short and easily understandable definition that we will use.

‘Law’ in simple terms means ‘rules’. It is a very wide term and includes different sets of rules regulating external human actions and conduct of individuals in their dealings with other individuals and with the government.

In simple words, the term ‘Law’ denotes ‘rules of conduct enforced by the State’. Legally, a set of rules alone is not sufficient, unless:

- ▶▶ it is enforced by the State;
- ▶▶ the State to enforce law is a Sovereign State;

- ▶▶ it receives due recognition;
- ▶▶ it attempts to achieve some sort of security and uniformity in its application.

Rules which have the above characteristics are called 'law'. Law includes all the rules and principles which regulate our relations with other individuals and with the State.

## Definition of Law

Austin has defined law in the following words: "A law is a rule of conduct imposed and enforced by the Sovereign".

Salmond defined Law as "the body of principles recognized and applied by the State in the administration of justice".

Holland defined law as "rule of external human actions enforced by Sovereign Political Authority".

## Purposes and Functions of Law

Law serves many purposes and functions in society. Four principal purposes and functions are **establishing standards, maintaining order, resolving disputes** and **protecting liberties and rights**.

1. **Establishing Standards:** Law is a guidepost for minimally acceptable behavior in society. Some activities, for instance, are crimes because society (through a legislative body) has determined that it will not tolerate certain behaviors that injure or damage persons or their property. For example, under a typical state law, it is a crime to cause physical injury to another person without justification – doing so generally constitutes the crime of assault.
2. **Maintaining Order:** This is an offshoot of establishing standards. Some semblance of order is necessary in a civil society and is therefore reflected in the law. The law – when enforced – provides order consistent with society's guidelines.
3. **Resolving Disputes:** Disputes are unavoidable in a society made of persons with different needs, wants, values, and views. Law provides a formal means for resolving disputes – the court system.
4. **Protecting Liberties and Rights:** The constitution provides for various liberties and rights. A purpose and function of the law is to protect these various liberties and rights from violations or unreasonable intrusions by persons, organizations, or government. *For example*, subject to certain exceptions, the First Amendment to the Constitution prohibits the government from making a law that prohibits the freedom of speech. Someone who believes that his free speech rights have been prohibited by the government may pursue a remedy by bringing a case in the courts.

You have probably realized that law may serve more than one principal function and there are obviously more principal functions than the four that we have identified.

## Sources of Indian Law

The following are the sources of Indian Law:

1. **English Law:** The English Law is the principal source of Indian Law. English law originates from the following sources:



- (a) **Maritime usages or Law of Merchant:** During the 14<sup>th</sup> and 15<sup>th</sup> centuries, maritime law based on customs and usages came to be recognized as the primary basis of English Mercantile Law.
  - (b) **English Common Law:** English Common Law was based on justice, equity and good conscience, which were developed on the customs, usages and traditions prevalent from centuries. Common Law was found to be inadequate as it was unwritten and its principles were applied whenever subsequent disputes of similar nature arose.
  - (c) **Roman Law:** When customs and usages did not exist, Roman Laws were applied.
  - (d) **Rules of Equity:** Where common law was harsh and oppressive, Judges applied rules of justice in their decisions, which became precedents. Rules of Equity were the codification of these rules of justice in the form of precedents. Rules of Equity and Common Law were applied simultaneously.
  - (e) **Statutes of British Parliament:** British Parliament enacted laws which were enforced by the Courts. British Statutes override the rules of Common Law and rules of equity.
  - (f) **English Judicial Decisions:** Judicial decisions or British Common Law or precedents form a very important source of law today. Decisions in future cases with similar facts are based on already decided cases.
2. **Indian Statutes:** The Central and State Legislatures enact laws in India, which are applied by the Courts in India. Prior to 1872, English Courts used to apply personal law of the parties to the suit. In 1872, the Indian Contract Act was passed, which is one of the oldest enactments in India. The Indian Contract Act is based on English Common Law Rules.
  3. **Judicial decisions:** Interpretation of statutes by Judges and their application depending on the facts of each case, meting out justice to the aggrieved parties has today formed a very important source of law. Where Indian Statutes, customs or usages are silent, courts apply law based on English judgments, which came to be recognized as an important basis of law in our country. Application of judicial decisions in previous cases to subsequent similar cases forms a very important source of law today.
  4. **Customs and usages:** Customs and usages in practice for a long time, in the absence of any statutory rules or which are not opposed to any statutory rules, are binding on the parties to the contract. Customs and usages should be ancient, reasonable and constant. Customs when accepted by the Court and incorporated in a judicial decision become a legal custom.

## What is Business Law?

**Business law**, also called **commercial law** or **mercantile law**, is the body of rules, whether by convention, agreement or national or international legislation, governing the dealings between persons in commercial matters.

Business law falls into two distinctive areas:

1. The regulation of commercial entities by the laws of company, partnership, agency, and bankruptcy and
2. The regulation of commercial transactions by the laws of Contract, Sale of Goods Act, Negotiable Instrument Act and related fields.

In civil-law countries, company law consists of statute law; in common-law countries, it consists partly of the ordinary rules of common law and equity and partly statute law. Two fundamental, legal concepts underlie the whole of company law: the concept of legal personality and the theory of limited liability. Nearly all statutory rules are intended to protect either creditors or investors. That's all elaborated in company laws.

Business law touches everyday lives through every contractual dealing undertaken. A contract, usually in the form of a commercial bargain involving some form of exchange of goods or services for a price, is a legally binding agreement made by two or more persons, enforceable by the courts. As such, they may be written or oral, and to be binding, the following must exist: an offer and unqualified acceptance thereof, intention to create legal relations, valuable consideration, and genuine consent (i.e., an absence of fraud). The terms must be legal, certain, and possible of performance.

Contractual relations, as the cornerstone of all commercial transactions, have resulted in the development of specific bodies of law within the scope of business law regulating:

1. sale of goods – i.e., implied terms and conditions, the effects of performance, and breach of such contracts and remedies available to the parties;
2. the carriage of goods, including both national and international rules governing insurance, bills of lading, charter parties, and arbitrations;
3. consumer credit agreements; and
4. labour relations determining contractual rights and obligations between employers and employees and the regulation of trade unions.

The corporate laws, Intellectual Property laws, coupled with high standards of governance and transparency plays key roles in shaping corporate business structure.

Business law, on national and international levels, is continually evolving with new areas of law developing in relation to consumer protection, competition, computers and the Internet.



## *Module*

### **I**

# **Indian Companies Act, 2013 (Part - I)**

## **Evolution of Company**

The Indian Companies Act, like many other laws, have been framed on the lines of the common law. In the year 1850, the Joint Stock Companies Act was passed. This was the first Indian legislation relating to companies. This was followed by the 1882 Act, which remained in force till 1912. Following this, the Indian Companies Act, 1913 was passed. The Act was aimed at improving the earlier law, and meeting the requirements of the then prevailing world. However, this Act was replaced by the Act of 1936.

With the Second World War, followed by the partition of the country and India becoming a sovereign, democratic country, revamping the law was necessitated. The GOI under the Chairmanship; of Shri. H.C. Bhabh, a Company Law Commission was set up to revise the Companies Act, 1913, to safeguard the interest of the investors and the public. On the recommendations of this committee, the Companies Act, 1956 was enacted. This Act of 1956 was in operation for over five decades.

Since the formation of the 1956 Act, the Act has undergone amendments for over two dozen times, each time trying to improvise the law to meet the needs of the hour.

The major committees set up from time-to-time for the purpose of revision of the Companies Act, 1956 were :

- ▶▶ Sachar Committee,
- ▶▶ Eradi Committee,
- ▶▶ Naresh Chander Committee and
- ▶▶ Dr. J.J. Irani Committee.

On the basis of the reports of the first three committees, major amendments to the Act took place in 1988, 2002 and 2003.

However, with the change in stakeholders' expectations, manifold increase in a number of companies, lessons from bad corporate governance, etc., it became necessary to revamp the Act of 1956. This resulted in a bill being introduced in 2008, which lapsed in 2009 due to the dissolution of Lok Sabha. Again a Bill was introduced in Lok Sabha in 2011, which was amended and Companies Bill 2012 was passed by Lok Sabha on 18<sup>th</sup> December, 2012 and by the Rajya Sabha on 8<sup>th</sup> August,

2013 and the Presidential assent was given on 29<sup>th</sup> August, 2013. The new 2013 Act is more rule based, thus the substantial form will be in the form of Rules. However, the implementation of the Act, 2013 shall be made operational in phases.

The Companies Act, 1956 comprised of 13 Parts, 658 Sections and 15 Schedules, while the Companies Act, 2013 comprises of 29 Chapters, 470 Sections and 7 Schedules, 98 Sections became operative with immediate effect, while 183 Sections came into effect from 1<sup>st</sup> April, 2014.

The changes in the Act in recent years have elaborated implications that are set to significantly change the manner in which the corporates shall operate in India.



# 1

# Concept, Features and Incorporation of Companies

## Chapter Outline

- 1.1 Characteristics of a Company or Advantages of Incorporation
- 1.2 Disadvantages of Incorporation
- 1.3 Lifting the Corporate Veil
- 1.4 Formation of a Company
- 1.5 Electronic Filing of Documents
- 1.6 Consequences of Non-registration
- 1.7 Case Studies
- 1.8 Questions

The word 'Company' is an amalgamation of two Latin words, 'com' meaning 'with or together' and 'panies' meaning 'bread'. Occasionally, it referred to a group of persons who took their meals together. A company is also called a 'corporate' meaning 'body' in English. A company is nothing but a group of persons who have come together or who have contributed money for some common purpose and who have incorporated themselves into a distinct legal entity in the form of a company for that purpose. Under Halsbury's Laws of England, the term 'company' has been defined as 'a collection of many individuals united into one body under special domination, having perpetual succession under an artificial form and tested by the policies of law with the capacity of acting in several respect as an individual, particularly for taking and granting of property, for contracting obligation and for suing and being sued for enjoying privileges and immunities in common and exercising a variety of political rights, more or less extensive, according to the design of its institution or the powers upon it, either at the time of its creation or at any subsequent period of its existence'.

Thus, a company is a juristic person having a separate legal entity, distinct from the members who constitute it, capable of rights and duties of its own and endorsed with the potential of perpetual succession.

**Section 2(20) defines Company: "company means a company incorporated under this Act or under any previous company law".**

**Section 3(1)(i) of the Act, 1956 defines a company as: “a company formed and registered under this Act or an existing company”. An ‘existing company’ means a company formed and registered under any of the previous company law.**

Act, 2013	Act, 1956
Section 2(20) defines a company Section 2(67) defines a previous company Section 2(68) defines a private company Section 2(71) defines a public company <b>Note:</b> The word ‘existing company’ is replaced by ‘previous company’. Also, various sub-sections deal with the definition of a previous company, private and public company.	Section 3(i) defines a company Section 3(ii) defines an existing company Section 3(iii) defines a private company Section 3(iv) defines a public company The word ‘existing company is used’ and the same section under various clauses deal with the definition of an existing company, private and public company.

This definition seemed inadequate, as it was difficult to comprehend the real nature of the company. In order to know the nature of a company, one needs to refer to the definition of L.H. Haney, who defined company as:

“incorporated association, which is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal”.

## 1.1 Characteristics of a Company or Advantages of Incorporation

As the characteristics are unique to the company and also formed to overcome the drawbacks of partnership, they are also called as advantages of incorporation. Following are the characteristics:



**Fig. 1.1**

### 1. Incorporated Association:

A company must be incorporated (registered) under the Companies Act. In other words, it is the registration of the association that creates a company.

A company can be formed as:

- (a) Company limited by shares; or
- (b) Company limited by guarantee; or
- (c) Unlimited company.

Any of the above types of companies may be a private company or a public company. Under the Act, 2013, a special type of private company, One Person Company (OPC) can also be formed.

The minimum and maximum number of members/shareholders varies:

Types of Company	Minimum Number	Maximum Number
One Person Company	1 and (1 nominee)	NA
Private	2	200
Public	7	unlimited

Fig. 1.2

(Under Act, 1956, One Person Company was not mentioned. Also, the maximum number in case of a private company was 50.)

### 2. Artificial Legal Person:

The company on registration is given more or less the same status of an individual. But as the company is an entity created by law, it is called an artificial legal person. Thus, the company has the right to acquire and dispose of the property, to enter into a contract with third parties in its own name and to sue and be sued in its own name.

Though a company is treated as an artificial person, it is not a citizen and cannot enjoy the rights under the Constitution of India and Citizenship Act (State Trading Corporation of India v/s C.T.O. (1963) S.C.T. 705).

### 3. Independent Corporate Personality:

A company on registration has a separate identity of its own, which is different and distinct from the members who constitute it. The creditors of the company can recover their money only from the

company and the property of the company. Creditors cannot sue individual members. Similarly, company is not in any way liable for the individual debts of its members. The property of the company is to be used for the benefit of the company and not for the personal benefit of the shareholders. On the same grounds, a member cannot claim any ownership rights in the assets of the company, either individually or jointly during the existence of the company or in the winding up. At the same time, the members of the company can enter into contracts with the company in the same manner as any other individual can. The separate legal entity of the company is also registered by the Income Tax Act. Where a company is required to pay Income-tax on the profits and when these profits are distributed to shareholders in the form of a dividend, the shareholders have to pay income-tax on their dividend of income. This proves that a company and its shareholders are two separate entities. This principle of independent corporate personality was laid down in the famous case of *Salomon v. Salomon and Co. Ltd.*

Mr. Salomon was carrying on shoe manufacturing business on proprietorship basis. He sold his business to a company *Salomon & Co. Ltd.* for Euro 30,000. Salomon received consideration in the form of shares for Euro 20,000 of Euro 1 each and for Euro 10,000 he got debentures. The company had seven members, consisting of Mr. Salomon, Mrs. Salomon, four sons and a daughter. All the other members of the company other than Mr. Salomon had only 1 share each. After some time the company had to be wound up on account of financial difficulties. The assets realized were Euro 6,000, while the liabilities were Euro 10,000 to Salomon as a secured creditor and Euro 7,000 to outsiders who were unsecured creditors. The creditors claimed priority over Salomon (secured creditor) on the ground, Salomon and *Salomon & Co.* were one and the same. It was however, observed that “the company, on incorporation, has a different personality, different from the subscribers.” Therefore, the identity of the subscribers is immaterial. Hence, Mr. Salomon was paid first as he was a secured creditor.

The principle established in Salomon’s case has also been applied in *Lee V. Lee’s Airforming Ltd.* (1961) A.C. held 1995 shares out of the 3000 shares in *Lee’s Air Forming Ltd.* He voted himself the Managing Director and also became Chief Pilot of the company on a salary. He died in an air crash while working for the company. His wife was granted compensation for the death of her husband in the course of employment. Court held that Lee was a separate person from the company he formed, and compensation was due to the widow. Thus, the rule of corporate personality was applied.

#### **4. Liability:**

The company, being a separate person, is the owner of its assets and bound by its liabilities. The liability of the shareholders/members depends on the nature of the liability. Where the company is limited by shares, the liability of the shareholder is up to the value of shares held by him. In case of a company limited by guarantee, the liability of its members would be to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up. While in case of unlimited liability company. A company would be a company not having any limit on the liability of its members.

However, in most cases, the liability of the member is limited to contribution to the assets of the company up to the face value of the shares held by him.

#### **5. Perpetual Succession:**

A company enjoys perpetual existence. It would not cease to exist even if all its members die. It is created by law and can be put to an end only by the process of law. Prof. Grover in his book “*Modern Company Law*” stated even a hydrogen bomb cannot destroy a company.



### 6. Hold and Dispose of Property:

A company can hold and dispose of property in its own name. Property of the company cannot be treated as members' property and *vice versa*.

### 7. Transferability of Shares:

The shares are easily transferable subject to certain conditions. However, between a public and private company, it is easier in the former when compared to the latter.

### 8. Common Seal:

A company is an artificial person, with no physical existence. It acts through the directors. The directors act on behalf of the company and enter into contracts by affixing company's common seal. The common seal of a company is its official signature.

### 9. May Sue and be Sued:

A company having its own independent existence, can sue in its name, to enforce any of its statutory or contractual rights and be sued in its name by others, if it commits a breach of contract or fails to discharge its duties.

**Illustration:** An employee not getting salary may sue the company itself and not the directors. Similarly, if an employee has to be sued, the company and not the director shall sue.

## 1.2 Disadvantages of Incorporation

1. **Excessive formalities and expenses:** Incorporating a company is both cumbersome and expensive. The formalities to be complied with the registration are many. Running the company also requires a lot of formalities to be followed, as well as funds.
2. **Corporate veil:** The company by its separate corporate personality is accountable for its action. In fact, there is an invisible veil between the company and the members. The company acts through human agency, yet it alone is accountable. This is a major drawback of incorporation. (Details are dealt in a separate sub-topic).
3. **Company is not a citizen:** Although a company is called an artificial legal person, enjoying many rights and being subject to many duties, yet it is not treated as a citizen. (*State Trading Corporation v. CTO AIR 1963 S.C. 1811*). Thus, a company does not enjoy all rights guaranteed to a natural person.

### Disadvantages of the Company Form of Organisation

Though company form has many advantages, there are some disadvantages too –

4. **High cost of formation:** Formation of a company requires many formalities and involves costs, like printing of memorandum and articles of association, stamp duty, filing fees, etc. On the other hand, the formation of a partnership is very easy. In fact, even the registration of a partnership firm is not mandatory.
5. **High cost of running the organization:** Accounts of the company have to be audited yearly. Meeting of shareholders have to be arranged yearly and meeting of Board of Directors have to be organized at least four times in a year. Elaborate records of members, directors, etc., have to be maintained. Annual return has to be filed. But in case of partnership, there are very few formalities required.

- 6. Winding Up of the Company:** Winding up of the company is a very long and costly affair. It is a time-consuming process. Whereas closing a partnership business is comparatively very easy and fast.

Though there are disadvantages, the advantages far outweigh the disadvantages. Therefore, all businesses of any considerable size are always formed as a company.

### 1.3 Lifting the Corporate Veil

The main advantage of incorporation from which all others follow is the separate legal entity. Though a company has a distinct personality apart from its members, but in reality, the business of the artificial person (company) is always carried on by and for the benefit of individuals. In the ultimate analysis, some individuals are the real beneficiaries of the corporate advantage. It may, therefore, happen that the corporate personality of the company is used to commit frauds or improper or illegal acts. Since an artificial person is not capable of doing anything improper, illegal or fraudulent, the veil of the corporate personality might have to be unveiled, to identify the persons who are really guilty. This is known as 'lifting the corporate veil'.

"Thus where the law disregards the corporate entity and pays regard instead to the individual members behind the legal mask, it is known as lifting the veil of corporate personality". (Gower's The Principles of Modern Company Law).

The circumstances under which the courts may lift the corporate veil may broadly be grouped under the following heads:

- I. Under statutory provisions,
- II. Under judicial interpretations.

#### I. Under Statutory Provisions:

The veil of corporate personality may be lifted in the following cases as per express provisions of the Companies Act.

- 1. Reduction of membership below statutory minimum:** If, at any time, the number of members of a company is reduced below the statutory minimum, i.e., below 7 in the case of public company or below 2 in case of a private company and the company carries on business for 6 months while the number is so reduced, every person who is the member of the company at the time the company so carries on business after those 6 months and is aware of the fact, shall be severally liable for the payment of company's debts, contracted during that time.

Thus, the law pierces the 'corporate veil' and makes persons behind the company personally liable, and the privilege of limited liability of shareholders is lost.

- 2. Misrepresentation in the Prospectus and or Fraud:** In case of misrepresentation in the prospectus, every director, promoter and every other person, who authorizes such issue of the prospectus, is liable to the person who have subscribed for shares on the faith of such untrue statement.

Any person thus guilty may be punished with imprisonment of not less than 6 months and up to 10 years and fine which shall not be less than the amount involved in fraud and up to three times the amount involved in the fraud. (Refer Section 34 and Section 447).

[Under Section 63 of the Act, 1956 the criminal liability imposed on every person liable for the untrue statement was imprisonment up to 2 years or fine up to fifty thousand rupees or both.)

3. **Failure to return application money:** If the company fails to receive minimum subscription within 120 days after the date of, first issue of the prospectus, it must refund the entire application money within next 15 days, failing which it shall have to refund the same with interest @6%.

SEBI Guidelines have brought in some changes in the above law and can be read as:

“If the company fails to receive minimum subscription on the closure of the issue, if the issue is not underwritten and within 60 days closure of issue, it must refund the entire application money within next 8 days failing which it shall have to refund the same with interest @15% per annum.”

4. **Failure to deliver share certificate, etc. within stipulated time period:** Where a company fails to deliver the share or debenture stipulated within 3 months of allotment or within 2 months of application for transfer, then the company, as well as every officer of the company who is at fault, shall be punishable with fine up to INR 5000/- per day till such default continues.
5. **Mis-description of name:** Where an officer of a company signs on behalf of the company any contract, bill of exchange, hundi, cheque, promissory note or order for money, such person shall be personally liable to the holder if the name of the company is either not mentioned, or is not properly mentioned.
6. **Holding Subsidiary Company:** A holding company is required to disclose to its members the account of its subsidiaries. It provides that every holding company shall attach to its balance sheet, copies of the balance sheet, profit and loss account, Director's report and Auditor's report, etc. in respect of each of its subsidiary company. It amounts to lifting the corporate veil, because in the eyes of law a subsidiary is a separate legal person and through this mechanism, their identity is known.
7. **For facilitating the task of an inspector to investigate the affairs of the company:** An inspector may be appointed for alleged mismanagement or oppressive policy towards its members. The inspector may also investigate into the affairs of another related company in the same management or group.
8. **For investigation of ownership of company:** The Central Government may, in order to ascertain the persons who are financially interested and also control decision making, appoint one or more inspectors for investigation and reporting on the membership of the company.
9. **Fraudulent conduct:** In the case of winding up of a company, if appears that any business of the company has been carried on with intent to defraud creditors of the company or any other person, or for any fraudulent purpose, those person who are knowingly parties to such conduct of business may, if the court thinks it proper, be made personally liable without any limitation as to liability for all or any debts or other liabilities of the company. Liability under this section may be imposed only if it is proved that the business of the company has been carried on with a view to defraud the creditors (Re, Augustus Bannett & sans Ltd. (1986) B. CLC 170).

10. **Liability for ultra-vires acts:** Directors and other officers of a company will be personally liable for all those acts, which have been done on behalf of the company, if the same are ultra-vires the company.
11. **Liability under other statutes:** The Directors and other officers of the company may be held personally liable under the provision of other statutes, e.g., for the recovery of tax arrears of a private company while being wound up, every director, during the tenure for which arrears is due, shall be jointly or severally liable for the tax under the Income Tax Act. In a similar manner, under the Foreign Exchange Management Act, 1999, the directors and other officers may be proceeded against individually or jointly for violations of the Act.

## II. Under Judicial Interpretations:

There may be various circumstances under which the court may feel compelled to lift the corporate veil in its judicial pronouncements. Following are some of the indicative cases to get an idea as to the kind of circumstances under which the façade of corporate personality will be removed or the persons behind the corporate entity identified and penalised, if necessary.

1. **Protection of revenue:** In *Sir Dinshaw Maneckjee Petit, Re* AIR 1927 Born 371, the assessee was a millionaire earning huge income by way of dividend and interest. He formed four private companies and transferred his investments to each of these companies in exchange for their shares. The dividends and interest income received by the company was handed back to Sir Dinshaw as a pretended loan. Held that the company was formed by the assessee only as a means of avoiding tax and company was nothing more than assessee himself.
2. **Prevention of fraud or improper conduct:** 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. A very important case in the point is *Gilford Motor Company v. Horne* (1933) 1 CH935. In this case, 'Horne' had been employed by the company under an agreement that he shall be solicit the customers of the company or compete with it for a certain period of time after leaving its employment. After ceasing to be employed by the plaintiff, Horne formed a company which carried on a competing business and allotted whole of its shares to his wife and an employee of the company, who were appointed to be its directors. It was held that since the defendant (Horne) in fact controlled the company, its formation was a mere 'cloak or sham' to enable him to break his agreement with the plaintiff. Accordingly, an injunction was issued against him and against the company he had formed restraining them from soliciting the plaintiff's customers.  
(Refer S. 447)
3. **Determination of the enemy character of a company:** Since a company is an artificial person, it cannot be an enemy or a friend. However, during war, it may become necessary to lift the corporate veil and see the persons behind as to whether they are our enemies or friends. It is because, though a company enjoys a distinct legal entity, its affairs are essentially run by individuals. In *Daimler Company Ltd. v. Continental Tyre and Rubber Co. (Great Britain) Ltd.* (1916) 2 AC 307, a company was incorporated in London for the purpose of selling tyres manufactured in Germany by a German company. Its majority shareholders and all the directors were Germans. On declaration of war between England and Germany in 1914, held that since both the decision making bodies, namely the Board of Directors and the general body of shareholders were controlled by Germans, the company

was a German company and thus, an enemy company. Accordingly, the suit filed by the company to recover a trade debt was dismissed on the ground that such payment would amount to travelling with the enemy.

4. **In case of economic offences:** In case of economic offences, the court is entitled to lift the veil of the corporate and pay regard to the economic realities behind the legal façade. *Santanu Ray v. Union of India* (1989) 65 Com p. CFas. 196 (Delhi).
5. **Where a company is used to avoid welfare legislation:** Where the sole purpose for the formation of the new company was to use it as a device to avoid the implementation of labour welfare measures, the Supreme Court ordered the piercing of the corporate veil to look at the real transaction. *Workmen of Associated Rubber industry Ltd. v. Associated Rubber Industry Ltd.* (1986) 59 Lone) G.S. 134.
6. **To punish for contempt of court:** The corporate veil may be lifted in the event of disobeying the orders of the court. *Jyoti Limited v. Kanwaljit Kaur Bhasin* (1987) 62 Comp. Cas-626 (Delhi).

## 1.4 Formation of a Company

A company is a creation of law. Thus, it may be created as a One Person Company or private company or a public company. Further, these companies can be created as a company limited by shares or limited by guarantee or as an unlimited company.

Formation of a company involves two stages, namely –

- I. Promoters and pre-incorporation contracts.
- II. Registration.

### I. Promoters and Pre-Incorporation Contracts

Promoters are persons who undertake to form a company and take steps to accomplish that purpose. As they take responsibility in forming the company, they stand in a fiduciary relation to the company they float.

S. 2(69) of Companies Act, 2013 defines promoter as:

**“Promoter means a person:**

1. 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
2. who has control over the affairs of the company, directly or indirectly, whether as a shareholder, director or otherwise; or
3. in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act;
4. Provided that nothing in sub-clause (3) shall apply to a person who is acting merely in a professional capacity”.

Promoters in ordinary parlance means a person who is responsible for the formation of a company, does all preliminary work for registration of a company.

Further, according to SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, “promoter” includes (i) the person or persons who are in control of the issuer; (ii) the person or

persons who are instrumental in the formulation of a plan or programme pursuant to which specified securities are offered to public; (iii) the person or persons named in the offer document as promoters.

Thus, a promoter is a person named in the prospectus or annual returns who has control over the company and on the advice the Board of Directors is accustomed to act. However, a person acting in a professional capacity is not a promoter. Promoters stand in a fiduciary relation to the company they float.

### **Functions of Promoter**

A promoter plays a very important role in the formation of a company. A promoter may be an individual, an association or a company. In their capacity as promoters, they perform the following functions in order to incorporate a company.

1. Promoters are generally the first persons who conceive the idea of business.
2. Promoters carry out the necessary investigation to find out whether the formation of a company is possible and profitable.
3. Promoters organize the resources to convert the idea into a reality by forming a company.
4. Promoters select the name of the company and thereby ascertain that the name shall be acceptable by the register of the office.
5. Promoters prepare the MOA and AOA of the proposed company.
6. Promoters nominate the first directors, bankers, auditors, etc.
7. Promoters select the place where registered office (head office) has to be situated.
8. Promoters are responsible for incorporation of the company.

In this sense, the promoters are the persons behind the incorporation of the company.

### **Duties and Liabilities of the Promoter**

1. Promoter stands in a fiduciary relation to the company he floats, thus he cannot make a secret profit.
2. A promoter who fails to give true and proper information in the statement annexed to the general meeting may be required to compensate the company to the extent of the benefit received by him. In case of default in complying with above provisions, every promoter, director, manager or other key managerial personnel who is in default shall be punishable with fine which may extend to INR 50,000 or five times the amount of benefit accruing to the promoter, director, manager or other key managerial personnel or any of his relatives, whichever is more (Section 102).
3. Under Section 7(6), a promoter may be held liable for fraud if he is found guilty of any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company.
4. Where the required information or documents are not furnished in the prospectus under Section 26 of the Act, 2013, the promoter/s may be held liable for the non-compliance.
5. For misstatement in the prospectus, the company and certain persons, including a promoter of the company shall, without prejudice to any punishment to which any person may be liable under Section 36, be liable to pay compensation to every person who has sustained such loss or damage.
6. If a company makes an offer or accepts monies in contravention of the provisions of private placement, as stated in Section 42, the company, its promoters and directors shall be liable

for a penalty, which may extend to the amount involved in the offer or invitation or INR 2,00,00,000/-, whichever is higher, and the company shall also refund all monies to subscribers within a period of thirty days of the order imposing the penalty [Section 42(10)].

### **Rights of the Promoter**

These rights are subject to the agreements:

1. Right to remuneration.
2. Right to profit on transactions entered with the company, subject to complete disclosure of the details to the company and members.
3. Subject to full disclosure, a promoter has right to sell his property and acquire fully paid-up shares.
4. Right to buy further shares in the company.
5. Commission on shares sold.
6. The articles of the company may provide for fixed sum to be paid by the company to the promoter. However, such provision has no a legal effect and the promoter cannot sue to enforce it. But if the company makes such payment, it cannot recover it back.

The contracts which the promoters enter into for floating the company are called pre-incorporation contracts.

### **Effects of Pre-incorporation Contracts**

1. Pre-incorporation contracts are not binding on the company after the incorporation, because the company was not in existence at the time the contract was entered.
2. Pre-incorporation contracts are not binding on the third party as well.
3. The promoters become personally liable.

Because of these hurdles, promoters were reluctant to enter into contracts and floating of company was not possible.

The difficulties posed by the company's inability to ratify a preliminary contract has to a very large extent been overcome by Section 15(h) and Section 19(e) of the Specific Relief Act, 1963. Under these sections, a company can sue and be sued, provided the contract specifically falls within the object clause.

**Section 15(h):** Sometimes the promoters of a public company have made a contract before its incorporation, for the purpose of the company. In such cases, the company may enforce the if it is 'warranted by the terms of incorporation'. The words 'warranted by the terms of incorporation' means within the scope of the company's objects as stated in the memorandum of association.

**Section 19(e):** The other party may also enforce the contract against the company if the company has adopted the contract after incorporation and it is within the terms of the incorporation.

## **II. Registration/Incorporation**

1. **Number of Persons:** In case of a private company, minimum 2 persons are necessary, with a minimum capital of INR 1,00,000; 7 persons in case of a public company with a minimum capital of INR 5,00,000 and 1 person in case of a One Person Company [Section 3(1)].
2. **Name of the Company:** The promoters have the duty to select the name of the proposed company. They are required to give a list of 6 preferred names in the order of preference.

Form INC-1 needs to be filed along with prescribed fee of INR 1000. After approval of name, ROC will issue a name availability letter. Under Section 4(5), the name will be valid for a period of 60 days from the date on which the application of reservation was made.

- 3. First Directors of the company:** The names of the first directors need to be mentioned. Minimum of 2 directors in case of a private company, 3 in case of a public company and 1 director in case of One Person Company [Section 149(1)(a) and Rule 17 of the Companies (Incorporation) Rules, 2014]. ‘Director Identification Number (DIN) has to be obtained by the directors of the company before commencing the procedure for incorporation of a company. DIN is issued by the Ministry of Corporate Affairs. As Ministry of Corporate Affairs accepts electronic submission of forms on its website, Digital Signature Certificate (DSC) is mandatory for all users.
- 4. Preparation of Memorandum and Articles of Association:** Both these documents, namely the Memorandum and Articles of Association need to be prepared by the subscribers. The former deals with the aims and objects of the company, while the latter deals with the rules and regulations. Memorandum of Association is to be prepared in accordance with Section 4(6) and Tables A-E as prescribed in Schedule 1 and Articles of Association in accordance with Section 5(6) and Tables F-J as prescribed in Schedule 1.
- 5. Declaration from Professionals:** Section 7(1)(b) requires filing of a declaration in the prescribed form by an advocate or a chartered accountant or cost accountant or company secretary in practice, who is engaged in the formation of the company and by a person named in the articles as a director, manager or secretary of the company. The declaration shall state that all the requirements of the Act and the Rules made thereunder in respect of registration and matters precedent or incidental thereto have been complied with [Refer Section 7(1)(b), Rule 14 of the Companies (Incorporation) Rules and INC. 8].
- 6. Filing of Affidavit:** An affidavit needs to be filed by the subscribers to the Memorandum and from persons named as the first directors, if any, in the articles that he is not convicted of any offence in connection with the promotion, formation or management of any company or that he has not been found guilty of any fraud or misfeasance or of any breach of duty to any company under this Act or any previous company law during the preceding five years. Further, the affidavit should contain that the information is correct, complete and true to the best of his knowledge and belief [Refer Section 7(1)(c), Rule 15 of The Companies (Incorporation) Rules 2014].
- 7. Payment of Fees and Stamp Duty:** After filing the documents, ROC fees and stamp duty has to be paid electronically. The amount of fees and stamp duty is based on the authorised capital of the company.
- 8. Issue of Certificate of Incorporation:** The Registrar of Companies after scrutinising the documents submitted, if found to be in order, shall grant a ‘Certificate of Incorporation’ [Form No. INC 11].

As per Section 2(68) and Section 2(71), the requirement of having a minimum paid-up share capital of INR 1 lakh for a private company and INR 5 lakhs for a public company has been done away with Companies Amendments.

Under Section 11, before commencement of business or exercising any borrowing powers, the director of a company having share capital was required to file with the Registrar of Companies a declaration that every subscriber to the Memorandum has paid the value of shares committed by



him/her and that the paid-up share capital of the company is not less than the amount prescribed has now been done away with Companies Amendments.

**Note:** The following documents need to be submitted to the ROC for incorporation.

1. Memorandum of Association and Articles of Association.
2. Form No. 1 – This is a declaration to be executed on a non-judicial stamp paper of INR 20 by one of the directors of the proposed company or other specified persons, such as Attorneys or Advocates, etc., stating that all the requirements of the incorporation have been complied with.
3. Form No. 18 – This is a form to be filed by one of the directors of the company informing the ROC detailing the registered office of the proposed company.
4. Form No. 29 – This is a consent form obtained from all the proposed directors of the proposed company to act as directors of the proposed company. (Not required in case of private company).
5. Form No. 32 – This is a form stating the fact of appointment of the proposed directors on the board of directors from the date of incorporation of the proposed company and is signed by one of the proposed directors.
6. Power of Attorney signed by all the subscribers of MOA authorizing one of the subscribers or any other person to act on their behalf for the purpose of incorporation and accepting the certificate of incorporation.

From the date of incorporation mentioned in the certificate of incorporation, such subscribers to the memorandum and all other persons, as may from time to time, become members of the company, shall be a body corporate by the name contained in the memorandum, capable of exercising all the functions of an incorporated company under the Act and having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued, by the said name.

**Punishment for incorporating a company by furnishing false or incorrect information [Section 7(7)]:** The Tribunal may, on an application made to it, on being satisfied that the situation so warrants:

1. pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or
2. direct that liability of the members shall be unlimited; or
3. direct removal of the name of the company from the register of companies; or
4. pass an order for the winding up of the company; or
5. pass such other orders as it may deem fit.

As per the Companies (Incorporation) Amendment Rules 2015, E-Form, INC - 29 has been introduced. This is a single application for reservation of name, incorporation of a new company and/or for allotment of DIN. This fast tracks the procedure for incorporation of the company.

## **Incorporation of Companies with Charitable Objects**

These companies are incorporated under Section 8 only for the promotion of commerce, arts, science, sports, education, research, social welfare, charity and protection of the environment or any such objects. Such companies can only be registered as a private company and they enjoy all the

privileges and are subject to all the obligations of a private company. The procedure for registration of such companies is similar to that of the registration of a private company. The only other requirement being annual income, income and expenditure for 3 years together with the source of income and the objects of expenditure needs to be furnished.

## Incorporation of a One Person Company

Incorporation of an OPC is a new concept under the new Act. Again, an OPC can be incorporated as a private company. The procedure is similar to that of incorporation of a private company with some special requirements. Those requirements are the company should have a capital of 1 lakh, only one natural person who is an Indian citizen and a resident of India for less than 182 days immediately preceding the calendar year can form an OPC. The nominee too should only be a natural person.

Act, 2013	Act, 1956
Permits reservation of 6 preferred names in the order of merit.	No such provision.
Under this Act, within 60 days, documents for incorporation to be filed.	No provision.
Affidavit to be filed by every subscriber to MOA and every first director named in AOA to the effect that he has not been convicted of any specified offences during the last 5 years.	Certificate of Incorporation was conclusive proof of incorporation. No provision for Corporate Identity Number.
Corporate Identity Number to be granted on incorporation. All companies to file AOA.	Section 26 only unlimited companies, guarantee companies and private companies limited by shares to file AOA.
Certificate of commencement of business dispensed with.	Certificate of commencement of business is necessary for public companies.

## 1.5 Electronic Filing of Documents

**Section 398: Provisions relating to filing of applications documents, inspection, etc. in electronic form.**

1. Notwithstanding anything to the contrary contained in this Act, and without prejudiced to the provisions contained in section 6 of the Information Technology Act, 2000 (21 of 2000), the Central Government may make rules so as to require from such date as may be prescribed in the rules that-
  - (a) **Application and documents to be filed in electronic form:** Such applications, balance sheet, prospectus, return, declaration memorandum, articles, particulars of charges, or any other particulars or document as may be required to be filed or delivered under this Act or the rules made thereunder, shall be filed in the electronic form and authenticated in such manner as may be prescribed.
  - (b) **Notices, communications – to be served in electronic form:** Such document, notice, any communication or intimation, as may be required to be served or delivered under this Act, shall be filed in the electronic form and authenticated in such manner as may be prescribed.

- (c) **Registrar to maintain the documents in electronic form:** Such applications, balance sheet, prospectus, return, register, memorandum, articles, particulars of charges, or any other particulars or document and return filed under this Act or rules made thereunder shall be maintained by the Registrar in the electronic form and registered or authenticated, as the case may be, in such manner as may be prescribed.
- (d) **Documents available for inspection in electronic form:** Such inspection of the memorandum, articles, register, index, balance sheet, return or any other particulars or document maintained in the electronic form, as is otherwise available for inspection under this Act or the rules made thereunder, may be made by any person through the electronic form, in such manner as may be prescribed.
- (e) **Fees and charges under the Act shall be paid through electronic form:** Such fees, charges or other sums payable under this Act or the rules made thereunder shall be paid through the electronic form and in such manner as may be prescribed.
- (f) **Registrar shall exercise his power under the Act in electronic form, e.g., alteration of memorandum, issue of certificate of incorporation:** The Registrar shall register change of registered office, alteration of memorandum or articles, prospectus, issue certificate of incorporation, register such document, issue such certificate, record the notice, receive such communication as may be required to be registered or issued or recorded or received, as the case may be, under this Act or the rules made thereunder or perform duties or discharge functions or exercise powers under this Act or the rules made thereunder (or do any which is by this Act) directed to be performed or discharged or exercised or done by the Registrar in the electronic form in such manner as may be prescribed.

**Explanation:** For the removal of doubts, it is hereby clarified that the rules made under this section shall not relate to the imposition of fines or other pecuniary penalties or demand or payment of fees or contravention of any of the provisions of this Act or punishment therefore.

2. **Framing of the scheme for use of electronic form by Central Government:** The Central Government may, by notification, frame a scheme to carry out the provisions of sub-section (1) through the electronic form.

#### **Section 399: Inspection, Production and Evidence of Documents kept by Registrar**

- (a) **Inspection of documents kept by Registrar on payment of fees:** Any person may inspect, by electronic means, any documents kept by the Registrar in accordance with the rules made, being documents filed or registered by him in pursuance of this Act, or making a record of any fact required or authorised to be recorded or registered in pursuance of this Act, on payment for each inspection of such fees as may be prescribed.
- (b) **Documents to be certified by the Registrar on payment of advance fees:** Any person may require a certificate of the incorporation of any company, or a copy or extract of any other document or any part of any other document to be certified by the Registrar, on payment in advance of such fees as may be prescribed.

**The rights conferred by this sub-section shall be exercisable –**

- i. in relation to documents delivered to the Registrar with a prospectus in pursuance of section 26, only during the fourteen days beginning with the date of publication of the prospectus; and at other times, only with the permission of the Central Government; and

- ii. in relation to documents so delivered in pursuance of clause (b) of sub-section (1) of section 388, only during the fourteen days beginning with the date of the prospectus; and at other times, only with the permission of the Central Government.
- (c) **Documents issued with the statement that it is issued with the leave of the court or tribunal:** No process for compelling the production of any document kept by the Registrar shall issue from any court or the Tribunal except with the leave of that court or the Tribunal and any such process, if issued, shall bear thereon a statement that it is issued with the leave of the court or the Tribunal.
- (d) **Such documents are admissible in evidence as the original documents:** A copy of, or extract from, any document kept and registered at any of the offices for the registration of companies under this Act, certified to be a true copy by the Registrar (whose official position it shall not be necessary to prove), shall, in all legal proceedings, be **admissible in evidence as of equal validity with the original document.**

**Section 400: Electronic form to be exclusive, alternative or in addition to physical form**

The Central Government may also provide in the rules made under section 398 and section 399 that the electronic form for the purpose specified in these sections shall be **exclusive**, or in the **alternative** or in **addition to the physical form.**

**Section 401: Provisions of Value-Added Services through Electronic Form**

The Central Government may provide such value-added services through the electronic form and levy such fee thereon as may be prescribed.

**Section 402: Application of Provisions of Information Technology Act, 2000**

All the provisions of the Information Technology Act, 2000 (21 of 2000) relating to the electronic records, including the manner and format in which the electronic records shall be filed, in so far as they are not inconsistent with this Act, shall apply in relation to the records in electronic form specified under section 398.

**Section 403: Fee for Filing, etc.**

1. Any document, required to be submitted, filed, registered or recorded, or any fact, or information, required or authorised to be registered under this Act, shall be submitted, filed, registered or recorded **within the time specified** in the relevant provision **on payment of such free** as may be prescribed.

Any document, fact or information may be submitted, filed, registered or recorded, after the time specified in relevant provision for such submission, filing, registering or recording, within a period of **two hundred and seventy days** from the date by which it should have been submitted, filed, registered or recorded as the case may be, **on payment of such additional fee.**

Any such document, fact or information may, without prejudice to any other legal action or liability under the Act, be also submitted, filed, registered or recorded, after the first time specified in the first provision on payment of fee and additional fee specified under this section.

2. **On failing to submit the documents within a specified time company will be liable for the penalty or punishment:** Where a company fails or commits any default to submit, file, register or record any document, fact or information under sub-section (1) before the expiry of the period specified in the first provision to that sub-section with additional fee, the company and the officers of the company who are in default, shall, without prejudice to the

liability for payment of fee and additional fee, be liable for the **penalty or punishment provided under this Act for such failure or default.**

#### **Section 404: Fees, etc. to be credited into Public Account**

All fees, charge and other sums received by any Registrar, Additional, Joint, Deputy or Assistant Registrar or any other officer of the Central Government in pursuance of any provision of this Act shall be paid into the public account of India in the Reserve Bank of India.

## 1.6 Consequences of Non-Registration

The following are the consequences of non-registration:

1. The association shall be an illegal association.
2. Every member of the association becomes personally liable.
3. The association cannot contract debts.
4. The association cannot be ranked as a creditor.
5. The association cannot be wound up.
6. Finally, no suit can be filed for the partition of the assets or dissolution.

## 1.7 Case Studies

### **1. Can a company become an enemy?**

**Ans:** If the persons who are controlling the affairs of the company are from an enemy nation and try to carry out activities which are contrary to the nations benefit, the company can acquire an enemy character [Daimler Co. Ltd. vs. Continental Tyre and Rubber Co. Ltd. (1916) 2 A. C. 307].

### **2. The number of members in a Public Company falls below 7 and the company carries on business.**

**Ans:** After six months period, every person who is a member during that time is severally liable for the whole of the debt contracted during that time.

### **3. All the members of the company were dead due to an explosion of an atom bomb. Does the existence of a company come to an end?**

**Ans:** Company exists beyond the lives of its members. A company has perpetual succession.

### **4. Deepak, a promoter of a company, entered into a contract for the benefit and formation of the company. After registration can company ratify such a contract of a promoter?**

**Ans:** There can be no valid ratification of a contract which is entered into by the promoters for the benefit of the company as at that back-date company was a non-entity, i.e., not in existence. Promoter becomes personally liable for such a contract.

### **5. Who is the owner of the company's capital and assets – Company, Directors, Members or Shareholders?**

**Ans:** Company being a legal/artificial person, capable of owning, enjoying and depositing of its capital and assets in the manner company likes. Shareholders and Directors are not the owners of companies property and assets.

**6. Mr. Sachin is holding shares of Reliance Co. He wishes to transfer his shares. Can he do so?**

**Ans:** Shares of a company are freely and easily transferable, unlike interests in a partnership firm, where the partner has to obtain the consent of existing partners for transfer of interest in the partnership. Any person who wants to transfer his shares can sell the it in market and transferee becomes the new member and shareholder of the company.

**7. Five persons were the only members of a Private Limited Co. While travelling together all the five persons who were the members of the company died in a plane crash. Does the company cease to exist?**

**Ans:** No, company has perpetual succession, i.e., continuous existence beyond the lives of the persons who form the company.

**8. An association of 12 members start a banking business without being registered as a company. The association wanted to file a suit against the outsider. Can they do so?**

**Ans:** Any association of persons carrying on banking business with more than 10 persons is considered an illegal association. The disability of illegal association is that it cannot sue an outsider.

**9. Company is a legal person. Whether company is a citizen of India?**

**Ans:** No, neither the provisions of the Constitution, Part II, nor the Citizenship Act confer the right of citizenship on a company. Any person other than the natural person cannot be the citizen of India.

**10. When an officer of a company commits a mistake in writing the name and registered address of company on any official documents, whether the firm becomes liable?**

**Ans:** The officer becomes personally liable for such an act to the third party due to the mistake.

**11. Six friends jointly bought a piece of land. Later on, they promoted a company and sold the property at a huge profit to the company. Can the company recover the profits from the promoters?**

**Ans:** No.

**12. A public company was floated by 6 members. One member forged the signature of the 7<sup>th</sup> member. What is the position of the association?**

**Ans:** Illegal association/Private Company.

**13. A private company was floated by Jignesh with his son. The company gave a huge amount as loan to Jignesh. In reality, the company was formed to evade taxes. Can Jignesh be held liable in his individual capacity? How?**

**Ans:** Yes. Exception under lifting of corporate veil.

**14. Sagar entered into a contract to supply an ice manufacturing machine to a proposed ice manufacturing company. The company after its incorporation adopted the contract. Some shareholders, challenged on the ground, that acceptance is invalid as the contract was entered before incorporation. Justify.**

**Ans:** Valid Contract.

15. **Mr. Salim entered into a contract to supply an ice manufacturing machine, to a proposed ice manufacturing company. The company after its incorporation adopted the contract. Some shareholders challenged on the ground, that acceptance is invalid as the contract was entered before incorporation. Justify.**

**Ans:** Shareholders cannot challenge valid adoption.

## 1.8 Questions

1. Define a company. What are the advantages and disadvantages of incorporation?
2. Explain the doctrine of 'corporate veil'. Under what circumstances can the veil be lifted?
3. What do you understand by 'promoter' of a company? Explain his position *vis-à-vis* the company he floats.
4. Explain the meaning of 'pre-incorporation contracts'. Is the company bound by such contracts? Discuss.
5. What is the procedure for registering an association as a company?
6. Discuss the concept of Corporate Personality in the light of the decision given in the Salomon v.s. Salomon and Co. Ltd.
7. Write Short note on:
  - (a) Pre-incorporation contracts.
  - (b) Certificate of Incorporation.
  - (c) Promoters.

