1.1 INTRODUCTION

The Companies Act of 1956 sets down rules for the establishment of both public and private companies. The most commonly used corporate form is the limited company, unlimited companies being relatively uncommon.
1.2 MEANING OF COMPANY

In common usage, ‘Company’ means an association of persons associated for some common purpose. The common object may be business, charity, research etc. The persons are united for achieving a common objective, normally, for earning profits, which are shared by the investors.

Definition of Company: Section 3 (1) (i) of the Companies Act, 1956 defines a company as:

“A company registered and formed under this Act or an existing company.”

The above definition does not give clear description about the company. The definition provided by Haney gives a better view about the essential elements of a company. According to Haney,

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

The characteristics of the company give a better picture about the essential elements mentioned in the above definition. Let us discuss those characteristics that describe the company, comprehensively.

1.3 CHARACTERISTICS OR ESSENTIAL FEATURES OF A COMPANY

1. Registration: A company is to be compulsorily registered under the Companies Act.
2. Artificial Person: A company is an artificial person. “Company is an artificial person, invisible, intangible and existing only in the eyes of law.” It is created under the law, not itself a human being. It is called a person as it is clothed with certain rights and obligations.
3. Separate Legal Entity: A company can enter into contracts with its directors, its shareholders and outsiders. It functions through its board of directors. A company is a distinct person, with its own independent identity.

One Man Company: When a single person holds almost all the shares of the company, it is called ‘One Man Company’. Such a company has a legal personality, if it complies with the necessary requirements of registration (Solomon Vs A. Solomon & Co. Ltd.). Such companies may be public or private companies. Usually, they are private companies.

Solomon Vs A. Solomon & Co. Ltd.: In Solomon Vs A. Solomon & Co. Ltd. (1897) AC 22, it has been held that in common law, a company is a ‘legal person or has a legal entity separate from its members and is capable of surviving beyond the lives of its members.’

In this case, one Solomon was a shoe manufacturer. He incorporated a company named Solomon and Co. Ltd. He took over the entire business of a running concern. Solomon and the
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seven subscribers to the memorandum were he and his family members. Solomon and his two sons were the Directors of the Company. The business of the company was transferred for £30,000. Solomon took 20,000 share of 1 £ each and debentures worth 10,000 in consideration.

The Company went into liquidation, within a year. On winding up, the unsecured creditors contended that the company was not having independent existence as Solomon was the Managing Director of the company and the entire company was under his control. They further contended that Solomon was holding majority of the shares and therefore, the company was merely a sham. Their contention was that the limited firm was only a guise to conceal the real identity of the persons who own. However, it was held that Solomon and Co. Ltd. fulfilled all the requirements of the legislature. Further, it was held that the company cannot be equated with the members comprising it. The company was not the agent of Solomon. It was therefore, treated as a company, distinct and independent corporation.

A company has, therefore, a separate legal existence, and is altogether a different person even from its directors and members.

Corporate Veil: On incorporation, a company assumes a separate personality of its own, called the ‘Corporate veil’. On incorporation, the veil is drawn between the company and its members. The advantages of the incorporation – separate entity – were allowed only to those who make an honest use of the ‘company’.

Lifting Corporate Veil: There may be circumstances in which the privileges of ‘separate entity, may be misused. In such cases, the court, may disregard the corporate veil.

Ignoring separate entity or overlooking corporate personality is known as the phenomenon of lifting corporate veil’. Lifting corporate veil is an exception to the decision in Solomon’s case.

In the case of dishonest and fraudulent use of the facility of corporation, the law lifts the corporate veil and identifies the persons who are behind the scene and responsible for the perpetration of the fraud. (Life Insurance Corporation of India Vs. Escorts Ltd. (1986).

Overlooking the corporate personality or separate entity is known as “the phenomenon of lifting the corporate veil.”

4. Common Seal: Common seal is the signature of the company. As company is an artificial person, it is not bestowed with the body of a human being. The company has a separate legal existence through its common seal. The use of common seal is provided in the articles of association of the company.

5. Separate Property: A company can open a bank account in its name. It can exercise the entire powers incidental to the attainment of the objects of the company. A company can enter into contracts, through its board of directors. Shareholders are not, in the eyes of the law, part owners of the company.

6. Company to Sue and be Sued: A company can sue and be sued in its name. The company’s right to sue arises as and when some loss is caused to the company. In case of breach of performance by any third party, the company can sue the third party in its name.


1.4 TYPES OF COMPANIES

Companies can be classified into three categories, based on their mode of incorporation.

(1) **Chartered Companies:** A chartered company is created under a charter, granted by the king or queen in exercise of the powers vested in the crown. A chartered company is regulated by its charter. For example, the East India Company has come into existence by the grant of Royal charter. The Companies Act is not applicable to them. Since independence, chartered companies have no place in India.

(2) **Statutory Companies:** These are the companies incorporated under a Special Act, passed by the Central or State Legislatures. Statutory companies are like Reserve Bank of India, Life Insurance Corporation of India, Food Corporation of India or State Bank of India, which are created by the special acts of parliament or legislature. The statutory bodies are governed by the Act under which they are constituted or formed. Companies Act is not totally applicable to statutory companies. The provisions of Companies Act are applicable only to the extent they are not inconsistent with the provisions of the Special Act. They do not have either Memorandum or Articles of Association. The word “Limited” is not a part of their name.

(3) **Registered Companies:** Apart from statutory government owned concerns, the most prevalent form of large business enterprises is a company, incorporated with limited liability. Companies limited by guarantee and unlimited companies are relatively uncommon.

A company can be a public or a private company and could have limited or unlimited liability. A company can be limited by shares or guarantee.

**A) Company Limited by Shares**

In the case of company limited by shares, the personal liability of a member is limited to the face value of the share or amount unpaid on the share, whichever is lower.

(i) **Private Companies**

A private company is defined under Section 3 (i) (iii) under the Act. It has the following characteristics:

- **Right to Transfer:** The right to transfer shares is restricted.
- **Number of Shares:** The maximum number of its shareholders is limited to 50 (excluding employees) and the minimum number of shares is 2.
- **Invitation to Public:** No offer can be made to the public to subscribe for its shares and debentures.
- **Regulation:** Private companies are relatively less regulated than public companies as they deal with relatively smaller amounts of public money.

**Deemed Public Company:** The concept of deemed public companies was introduced in the Companies Act to check the misuse of private companies. A private company is deemed to become a public company in the following situations:
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- When 25 percent or more of the private company’s paid-up capital is held by one or more public company.
- The private company holds 25 percent or more of the paid-up share capital of a public company.
- The private company accepts or renews deposits from the public.
- The private company’s average annual turnover is not less than Rs. 10 crores during the relevant period of three years.

The above provisions of Section 43(A) shall not apply on or after 31st December, 2000. Deemed concept of a public company on account of the above four factors is abolished.

(ii) Public Companies

A public company is defined as one which is not a private company. In other words, to a public company the restrictions of a private company do not apply.

(B) Company Limited by Guarantee

In the case of company limited by guarantee, the personal liability is limited by a pre-decided nominated amount. This guaranteed amount is fixed by the members and specified in the memorandum of association, which they respectively undertake to pay, in the event of the winding up of the company. The guaranteed amount can be called upon by the company only at the time of winding up, if the liabilities exceed its assets.

(C) Unlimited Company

In the case of an unlimited company, the liability of its members is unlimited. Its members are liable to contribute to the debts of the company in proportion of their respective interests.

(4) Foreign Companies: A foreign company is a company incorporated outside India and under the law of that country. Foreign investors can enter into the business in India either as a foreign company in the form of a liaison office/representative office, a project office and a branch office. It has to register with Registrar of Companies (ROC), New Delhi, within 30 days of setting up a place of business in India or as an Indian company in the form of a Joint Venture and wholly owned subsidiary. For opening of the foreign company, specific approval of Reserve Bank of India is also required. The foreign company must conspicuously exhibit on the outside of every office or business the name of the company, whether it is a public company or a private company and where incorporated.

Where 50% of the paid up of share capital of the foreign company is held by Indian citizens and/or companies incorporated in India, the foreign company is treated as an Indian company with respect to its Indian business. This is designed to protect the interests of the Indian citizens and Indian companies as substantial portion of their share capital is raised from them.
1.5 FORMATION OF COMPANY

The whole process of formation of a company is divided into four steps for convenience.

A. Promotion of Company
B. Incorporation or Registration of Company
C. Floatation of Company
D. Commencement of Business
1.6 PROMOTION OF COMPANY

Promoter: Promoter is a person who initiates the process of formation of company. He undertakes to form a company with reference to a given project and takes the necessary steps to accomplish the purpose. Promoter assumes responsibility for all the matters relating to the formation of the company.

The term “Promotion” refers to the process of by which a company is ‘incorporated’ or brought into existence.

Fiduciary Position of Promoter

The promoter takes the necessary steps for the registration and floatation of the company. A promoter occupies a fiduciary position [Relationship of trust and confidence] with the company and the persons whom he induces to be the shareholders of the company. On account of this relationship, the promoter has to make a full disclosure of all material facts relating to the formation of the company. A promoter is not forbidden from making a profit in the formation of the company, but the profit is not to be secret.

“A promoter is neither the trustee nor the agent of the company, he promotes.” Reason is neither a company has been formed nor a principal is in existence. In the absence of the principal, an agent cannot represent the principal. Similarly, the beneficiary has not yet born for the trustee to act. Yet, the responsibility of an agent and trustee is placed upon the promoter. Consequently, a promoter must act honestly and must not make money, directly or indirectly, at the expense of the company. He has to account and give to the company, whatever money is secretly received by him.

Remuneration to Promoter: Promoter gets remuneration for the work he does in the form of a lump sum. One of the usual ways of getting remuneration is sale of one’s own property to the company, at an inflated price. He must disclose all the facts relating to the property to an independent and competent Board of Directors. If he sells the property to the company, without making a disclosure, the company may rescind the contract. The promoter may be required to pay back the price he has received from the company. Where rescission is not possible, the promoter may be required to pay damages to the company to the extent of the undisclosed profits.

Where remuneration is paid to the promoter, it must be disclosed in the prospectus, if paid within two years preceding the date of issue of prospectus.

1.7 INCORPORATION OR REGISTRATION OF COMPANY

For a public company, the minimum number of members is seven, while it is two in the case of a private company. The promoter has to gather the required number for subscribing to the Memorandum of Association.
The following are the steps for the incorporation of a company:

1. **Application for Availability of Name:** A company cannot be registered in the name of an existing company. It also cannot be registered in a name, which is undesirable in the opinion of the Central Government. Therefore, it is necessary for the promoters to find out the availability of the name of the company from the Registrar of Companies. The first step in the formation of a company is the approval of the name by the Registrar of Companies (ROC) in the State/Union Territory in which the company is to be registered. This approval is provided subject to certain conditions. For instance, there should not be an existing company by the same name. Further, the last words in the name are required to be “Private Ltd.” in the case of a private company and “Limited” in the case of a Public Company.

**Finalisation of name:** The application for approval of name should mention at least four suitable names of the proposed company, in order of preference. The ROC, generally, informs the applicant within seven days from the date of submission of the application, whether or not any of the names applied for is available. Once a name is approved, it is valid for a period of six months, within which time Memorandum of Association and Articles of Association together with miscellaneous documents should be filed. If one is unable to do so, an application may be made for renewal of name, by paying additional fees. After obtaining the name approval, it normally takes approximately two to three weeks to incorporate a company, depending on where the company is registered.

2. **Filing of Documents:** The following three documents are required to be filed with the Registrar of Companies of the State in which the registered office of the company is to be situated:
   
   (i) Memorandum of Association,
   
   (ii) Articles of Association, and
   
   (iii) Agreement with the company for the proposed appointment of the managing director, whole-time director or manager.

   The above documents (i) and (ii) are required to be signed by the seven persons in the case of the public company and two persons in the case of private company.

3. **Payment of Stamp Duty and Filing Fee:** The company has to pay the necessary stamp duty and filing fee, according to the authorized share capital of the company.

4. **Declaration of Compliance of Act and Rules:** A declaration that the requirements of the Act and the rules framed there under have been complied. This declaration is to be signed by an advocate of the Supreme Court or High Court or attorney or a pleader having the right to appear before High Court. Alternatively, this declaration can be signed by a Company Secretary or Chartered Accountant in whole time-practice, who is engaged in the formation of a company or a person named in the articles as a director. This declaration is also to be filed with the Registrar of Companies, where the registered office of the company would be located. - Section 33(2).
5. **Additional Requirement, in Case of a Public Company:** The following further requirements are to be complied with:

(i) A list of persons who have consented to act as directors.

(ii) Written consent of the directors to act in that capacity.

(iii) An undertaking by the directors to take up and pay for the qualification shares.

6. **Certificate of Incorporation or Registration:** If the Registrar is satisfied that the requirements under the Act for the purpose of registration of a company have been complied with, he shall register the company and issue a certification of incorporation, under his hand and seal.

### 1.8 ADVANTAGES OF CERTIFICATE OF INCORPORATION

1. **Corporate Existence:** After certificate of incorporation, company obtains independent existence. The company enjoys a distinct legal personality. It becomes capable of functioning, independently, as a corporate individual, distinct from its members.

2. **Liability:** The liability of the members is limited to the extent of the nominal amount of the shares subscribed. In the case of a company limited by guarantee, the liability of the member is limited to the amount guaranteed by him.

   The liability of partners in a partnership firm is unlimited. However, the liability of the members in a limited company is limited to the face value of the shares held by him. In case, the face value of a share is Rs. 10 and an individual holds 100 shares, his total liability, at any time, is only Rs. 1,000. If he has already paid, Rs. 400, his balance liability is limited to Rs. 600 only. Even, in the event of winding up of the company and the company does not have sufficient assets to pay the total liabilities, still, the individual member cannot be called upon to pay beyond Rs. 600 as he has already paid Rs. 400. In case, the member has paid the total amount of his liability Rs. 1,000, he has no further liability to the company, at all. The novel idea of limited liability has encouraged the people to invest in a company, with limited liability, unlike in a partnership firm.

3. **Transferability of Shares:** Shares in a company can be transferred easily, without the consent of other members of the company.

   The greatest advantage of company is transferability of shares, unlike in a partnership firm. In a partnership firm, without the consent of the other partners, a partner cannot transfer his share to others. A member can transfer his shareholding, without the consent of the other members, in the manner provided by the Articles Association of the company. However, there are certain restrictions on the transferability of shares, in a private limited company. Certain restrictions can be imposed in a private limited company, but not in a public limited company about the transferability of shares.

   **In a public limited company, Articles of Association states the procedure to be followed, but cannot impose any restriction in respect of transferability of shares.**
4. **Perpetual Existence and Succession:** A company incorporated never dies. The members of the company change with the transfer of shares. The death or insolvency of the members does not affect the corporate existence of the company. Only on winding up of the company, it ceases to exist.

Prof. Grover in his book on Modern Company Law says that “A company continues to exist even if all the members are dead. 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 destroy it.”

5. **Members and the Company:** A company enjoys separate legal entity. So, it can enter into contracts with its members and sue them in the ordinary way.

6. **Separate Property:** Capital of the company is contributed by its members. However, company owns the assets in its name and the members do not have any ownership right on the property of the company.

7. **Capacity to Sue and be Sued:** A company being a body corporate, it can sue and be sued in its own name.

### 1.9 EFFECT OF CERTIFICATE OF INCORPORATION

The certification of incorporation is conclusive evidence about registration and compliance of all the legal requirements. Date of certificate of incorporation is date of birth of a company.

Once a company is registered, the certificate of incorporation cannot be challenged, though there may be irregularities prior to registration.

A company obtains separate legal existence only after it is registered under the Companies Act. By virtue of this legal existence, the company comes into being as a separate person, distinct from the persons who form it. The company becomes a body corporate, with perpetual succession. Once company is registered, the only method to end it is through the process of winding up. **The certificate of incorporation cannot be cancelled by the Registrar of Companies, even if irregular.**

### 1.10 FLOATATION OF COMPANY

Once the Certificate of Incorporation is received, it means the company is registered. Then the next step is to raise the required finances for running the company. The company is ready for floatation.
Floatation means raising the required finances for commencing and carrying on the business, satisfactorily.

In other words, the company can go ahead, with raising capital sufficient to commence the business and carry on it, satisfactorily.

**Prospectus & ‘Statement in lieu of Prospectus’**: A private company is prohibited from raising funds from the public. It can arrange the capital, privately, from its friends and relatives. In the case of public companies, it has the option to raise the funds from the public or through private sources, without raising funds from the public. In case, it decides to invite the public to subscribe to its capital, the public limited company has to issue prospectus. In case, the funds are arranged privately, the public company has to file a ‘Statement in lieu of Prospectus’ with the Registrar of Companies.

### 1.11 CERTIFICATE OF COMMENCEMENT OF BUSINESS

A public company, having share capital, cannot commence the business, without obtaining the certificate of commencement of business. The certificate of commencement of business can be obtained, only after completing the floatation process. In other words, a public limited company has to file either prospectus or statement in lieu of prospectus and comply with the required legal requirements, relating to the capital requirements. Thereafter only, Certificate of Commencement of Business is issued by ROC.

A Public Company, having share capital, cannot commence the business, without obtaining the Certificate of Commencement of Business.

However, a private limited company can commence the business, without obtaining the ‘Certificate of Commencement of Business’. There is no need for a private company to obtain Certificate of Commencement of Business. After obtaining the Certificate of Incorporation, it can immediately commence business. It is the privilege a private limited company enjoys.

### 1.12 MEMORANDUM OF ASSOCIATION

**Public Documents**: Memorandum of Association and Articles of Association are public documents. Any one who deals with the company are presumed to be aware of the contents of those documents.

Memorandum of Association is a document, which contains the fundamental conditions regarding constitution, objects or activities and powers of the company. It is a charter of the company. It is a principal document without which a company cannot be registered. It is a life-giving document.
Memorandum of Association is a document based on which the relations of the company is governed with outsides and members of the company.

**Purposes:** Memorandum of Association serves the following purposes:

(A) It contains the fundamental conditions on which the company is formed.

(B) It sets the boundaries of the company.

Lord Macmillan has rightly observed that the purpose of Memorandum of Association is to enable the shareholders, creditors and those who deal with the company to know the permitted range of the enterprise. *(Egyptian Salt and Soda Co. Ltd. Vs Port Said Salt Association Ltd. -1931).*

### 1.13 CONTENTS OF MEMORANDUM OF ASSOCIATION

According to Section 13 of the Act, the Memorandum of Association of every company should contain the following contents:

(A) **Name Clause:** Once the name of the company is approved and registered by the Registrar of Companies, the name of the company must be painted or affixed outside of every office or place of business. The name and address of registered office of the company has to be mentioned in letter-heads, business letters, notices and common seal of the company.

(B) **Registered Office:** Every company must have a registered office from the date of commencement of business, or 30th day of the incorporation date, whichever is earlier. All the notices have to be sent to this address.

(C) **Objects Clause:** The objects clause of the company indicates the sphere of activities and powers of the company.

*The purpose of the objects clause is two-fold:*

(i) To inform the members and creditors of the company in what kind of business their capital and funds may be used, and

(ii) To inform the persons dealing with the company what its powers are.

The objects are divided into two parts. Now, it is compulsory to specify in clear terms the main and other objects of the company.

(i) **The Main objects** to be pursed by the company on its incorporation and the ancillary objects incidental to the attainment of the main objects. The ancillary objects must have reasonable proximity or connection with the main objects.

(ii) **Other objects:** These are the objects which are not included in the above.

A company is prohibited from commencing any new business, though stated in the other objects, without passing the special resolution passed in the general meeting.
**Doctrine of Ultra Vires**

‘Ultra’ means ‘beyond’. ‘Vires’ means ‘powers’. So, the term “Ultra vires” means ‘beyond the powers of the Company’. A company exists only to carry on the objects which are expressly stated in the objects clause. It means the company can perform those objects only. It can also do such acts, which are incidental or consequential to the specific objects of the company. A trading company has implied power to borrow and this power need not be stated, separately.

This doctrine has been first explained in the leading case of *Ashbury Railway Carriage Co. Ltd. Vs Riche* LR HL 653 (1875). The object of the company as contained in the Memorandum of Association has been “to make, sell or lend on hire, railway carriages and wagons of all kinds .... to carry on the business of mechanical engineers and contractors. The directors of the company, however, have contracted for financing the construction of a railway line in Belgium. The company has endorsed the act of directors by passing a special resolution in the general meeting. However, the contract has been held to be ultra vires of the objects of the company because the word ‘general contractors’ does not authorize the company to make contract of every description. The doctrine has been confirmed by the Supreme Court in *Lakshmana Sami Mudaliar Vs LIC of India* 1963 AIR Sc 1185.

An act done outside the express or implied objects is *ultra vires*. The *ultra vires* acts are null and void *ab initio*.

The object of the ultra vires doctrine is to protect the interests of the investors and creditors by ensuring that the company does not invest or utilize the money in those acts, which is not contemplated by the shareholders or creditors of the company.

**Effect of Ultra Vires Acts**

1. **Void ab initio:** These acts are void from the beginning.
2. **Injunction:** A member of the company can bring an injunction (order of the court refraining to do) against the company to prevent from proceeding with the ultra vires act.
3. **Personal Liability of Directors:** The directors of the company may be personally held liable to outsiders for those *ultra vires* acts. This is made on the ground of breach of warranty or authority.
4. **No Ratification:** If an act is *ultra vires* the company, it does not create legal relationship. It is violation of the law and diversion of the assets of the company to purposes, not contemplated by the members and creditors of the company. As it is an act outside the powers of the company, even the whole body of shareholders cannot ratify it and make it binding on the company.
5. **Company Can Neither Sue or be Sued:** The company cannot sue the contracting party. Equally, the contracting party cannot sue the company.
**Various Types of Ultra Vires Acts:** It is necessary to distinguish the acts, outside the powers of the company and Board of Directors.

Acts beyond the scope of Memorandum of Association cannot be ratified by the company, even by the total body of the shareholders as they are outside the powers of the company. However, if the acts are only beyond the powers of the directors, but within the powers of the company, those acts can be ratified by the company.

(D) **Capital Clause:** In the case of a company having a share capital, the capital clause has to state the nominal or authorized capital of the company. The nominal capital is divided into different classes of shares. The capital clause has to state the values of the different classes of shares such as equity share capital and preference share capital and their division into shares of a fixed amount.

In the case of a company limited by guarantee, the amount promised by each member to be contributed by them in the event of winding up of the company, is to be mentioned.

(E) **Liability Clause:** The liability of the members is limited to the extent of the shares subscribed by the members of the company, in the case of a company having share capital. It means no member can be called upon to pay more than the nominal value of the shares held by him or the amount remaining unpaid. In case the shares are fully paid, the liability is nil.

In the case of a company by guarantee, the liability is limited to the extent of guarantee given by the members. This can be called only when the liabilities exceed the assets of the company.

(F) **Subscription or Association Clause:** In the case of a public company, at least, there must be seven subscribers although two are sufficient in the case of a private company. All the subscribers must sign the Memorandum of Association. Each subscriber must take at least one share in a company. Normally, the declaration of association reads like this “We, the several persons whose names, addresses and occupations are subscribed, are desirous of being formed into a company in pursuance of the Memorandum of Association and respectively agree to take the number of shares in the capital of the company, set opposite of our respective names.”

After incorporation, no subscriber can withdraw his name on any ground whatsoever.

### 1.14 ARTICLES OF ASSOCIATION

**Articles of Association:**

Articles of Association lays down the rules and regulations framed for the purpose of its internal management of the affairs of the company.

They facilitate the way for carrying out the objects, specified in the Memorandum of Association.

**Relationship between Memorandum of Association and Articles of Association**

1. **Ranking:** Articles of Association is subordinate and controlled by the Memorandum of Association.
2. **Subordinate:** The Articles of Association are subordinate to Memorandum of Association. Articles of Association cannot contain any provision which is inconsistent with the Memorandum of Association. Articles of Association may the supplement the Memorandum of Association.

3. **Scope:** The Memorandum of Association lays down the scope or powers of the company, while the Articles of Association govern the way in which the objects of the company can be carried out. As regards the contents, Articles of Association resembles a partnership deed.

**Adoption of Table A:** A public company limited by shares may have its own Articles of Association. In the absence of its own Articles of Association, the company can adopt Table A. In other words, preparation of Articles of Association is not compulsory. Even if Table A is adopted, if the company’s Articles of Association is silent on any matter, provisions of Table A would be applicable.

**Contents of Articles of Association:** Some of the contents of Articles of Association are here under:

(i) Allotment of shares
(ii) Procedure for Transfer of Shares
(iii) Powers of Directors
(iv) Forfeiture of shares
(v) Common seal of the company
(vi) Accounts and audit
(vii) Voting rights and proxies

The Articles of Association spells out the way the affairs of the company would be conducted.

### 1.15 ALTERATION OF MEMORANDUM OF ASSOCIATION AND ARTICLES OF ASSOCIATION

Alteration of Memorandum of Association is much difficult and strictly regulated. Articles of Association can be easily altered by passing a special resolution in the general meeting.

**Check Your Understanding**

*State whether the following statements are True or False*

1. A company is a distinct person, with its own independent identity.
2. The liability of the members in a company is unlimited, similar to a partnership firm.
3. The greatest advantage of company is transferability of shares, unlike in a partnership firm.
4. Common seal is the signature of the company.
5. In the eyes of law, shareholders of the company are part owners.
6. The term “Promotion” refers to the process of by which a company is ‘incorporated’ or brought into existence.

7. A promoter is both a trustee and agent of the company, before and after formation of the company.

8. In the case of company limited by shares, the personal liability of members is limited to the amount unpaid on their shares, at any time.

9. The Companies Act is totally applicable to statutory companies.

10. ‘One Man Company’ is not a company registered under the Act.

11. The person who assumes the task of promotion of the company is called ‘Promoter’.

12. Promoters occupy a fiduciary relationship, relationship of trust and confidence, with the company.

13. For a public company, the minimum number of members is two, while it is seven in the case of a private company.

14. A company obtains separate legal existence only after it is registered under the Companies Act.

15. Articles of Association can be altered, while Memorandum of Association cannot be altered at all.

16. “One Man Company” means a limited company with only one member as its shareholder.

17. Once a company is registered, the certificate of incorporation cannot be challenged, though there may be irregularities prior to registration.

18. Floatation means raising the required finances for commencing and carrying on the business, satisfactorily.

19. A private company is allowed to raise funds from the public.

20. A public limited company enjoys the privilege of commencing the business, without obtaining the ‘Certificate of Commencement of Business’.

21. The objects clause in the Memorandum of Association of the company indicates the sphere of activities and powers of the company.

22. An act done outside the express or implied objects of the company is *ultra vires*.

23. Even after the shares are fully paid, the liability of the member continues to remain to the face value of the shares held by him.

24. Articles of Association are the regulations or bye-laws, which govern the internal management and conduct of the company.

25. The Companies Act is applicable only to public companies, but not to private companies.

26. The directors of the company may be personally held liable to outsiders for the *ultra vires* acts, beyond the scope of the powers contained in Memorandum of Association.

27. The Memorandum of Association lays down the scope or powers of the company, while the Articles of Association govern the way in which the objects of the company can be carried out.

28. The certificate of incorporation can be cancelled by the Registrar of Companies, when the certificate is found irregular.
29. The ancillary objects stated in the Memorandum of Association need not have reasonable proximity or connection with the main objects.

30. The object of the ultra vires doctrine is to protect the interests of the investors and creditors by ensuring that the company does not invest or utilize the money in unauthorised acts, not contemplated by the shareholders or creditors of the company.

31. Acts which are within the powers of the company, but beyond the powers of the directors, can be ratified by the company.

32. It is necessary for every public company to have its own Articles of Association.

33. Articles of Association does not constitute a contract between the company and an outsider.

Answers:

31. True 32. False 33. True

Pick up the Right Answer

Q.1 The person who initiates the process of formation of company is known is:
   (a) Director.
   (b) Shareholder.
   (c) Promoter.
   (d) Registrar.

Q.2 Company may start its business in the following circumstances:
   (a) When it is registered, in case of a public company.
   (b) On presentation of an application for registration on requisite form.
   (c) When the private limited company obtains certificate of incorporation.
   (d) When Memorandum of Association of the company is presented before the Registrar of Companies.

Q.3 The company may appoint the following as director:
   (a) An individual.
   (b) A body corporate.
   (c) An association of individuals.
   (d) A partnership firm.
Q. 4 Company is a:
   (a) Natural person.
   (b) Artificial person.
   (c) Natural and artificial person.
   (d) None of the above.

Q. 5 Based on the following document, the relations of the company is governed with outsiders and members of the company:
   (a) Articles of Association
   (b) Prospectus
   (c) Memorandum of Association
   (d) Statement in lieu of Prospectus

Q. 6 This document is called as the charter of the company.
   (a) Articles of Association
   (b) Prospectus
   (c) Memorandum of Association
   (d) Statement in lieu of Prospectus

Q. 7 The Companies Act is applicable to the following categories of companies:
   (a) Statutory companies
   (b) Companies registered under the Companies Act
   (c) Partnership firms
   (d) Chartered Companies

Q. 8 The following document lays down the rules and regulations for internal management of the company:
   (a) Articles of Association
   (b) Prospectus
   (c) Memorandum of Association
   (d) Statement in lieu of Prospectus

Q. 9 Floatation of Company means
   (a) raising required finances at the initial starting and carrying on business, satisfactorily.
   (b) registration of a company.
   (c) running business efficiently and profitably.
   (d) situation before winding up of the company.
Q. 10 This form of business enjoys corporate form
(a) limited company,
(b) unlimited company
(c) partnership firm
(d) proprietorship concern

Q. 11 Name the company which is not a statutory company from the following:
(a) Reserve Bank of India
(b) Life Insurance Corporation of India
(c) Food Corporation of India
(d) HDFC

Q. 12 Articles of Association lays down
(a) relationship between company and outsiders.
(b) rules and regulations for internal management of the company.
(c) relationship between company and employees.
(d) relationship between company and shareholders of the company.

Q. 13 If there is any contradiction between Memorandum of Association and Articles of Association, the following document prevails.
(a) Memorandum of Association.
(b) Articles of Association
(c) Both (a) and (b)
(d) Company cannot perform that act.

Q. 14 Memorandum of Association is
(a) a public document
(b) a private document
(c) a confidential document
(d) none

Q. 15 When Articles of Association of a public company, limited by shares, is silent on any matter, then
(a) company cannot do any act on that matter.
(b) company cannot do till its Articles of Association is altered.
(c) Table A is applicable to that extent.
(d) provision of Memorandum of Association is applicable on that matter.
Discuss Legal Implications

(A) Memorandum of Association of a public company has been signed by six majors and a guardian of a minor. The Certificate of Incorporation has been issued by the Registrar of Joint Stock Companies, without noticing the defect. Is the Certificate of Incorporation valid? Can the Registrar of Joint Stock Companies cancel the certificate, once the irregularity is found out? Does it make any difference if only one adult has forged the signatures of the rest of four members?

Answer: In the case of a public company, the signatories to the Memorandum of Association should be seven. In the relevant case, seven members have signed, but out of seven one is a minor. Minor has been signed by the guardian. Minor is incompetent to enter into a contract. Any contract with a minor is void. But, the Certificate of Incorporation has been issued by the Registrar of Joint Stock Companies. With the issue of Certificate of Incorporation, the company has been formed. The date of the certificate is the date of birth of the company.

According to Section 35 of Companies Act, once the Certificate of Incorporation is issued, it is a conclusive proof that the requirements of the Companies Act have been complied with, in full. The regularity of the certificate cannot be questioned. (Moosa Goolam Ariff Vs Goolam Ariff ILR(1913) 40 CAL PC)

Registrar of Joint Stock Companies has no authority to cancel the certificate. Winding up of the company is the normal way for the closure of the company.

Any irregularity such as forgery does not affect the validity of the Certificate of Incorporation.

(B) A promoter has approached Registrar of Joint Stock Companies to register a new company with the name “New Bata Ltd.” to carry on shoe manufacturing activity. Can the company secure the approval for the name requested? Would the Registrar of Companies be justified in disallowing the proposed name?

Answer: No company is allowed to be registered in the name of any existing company or with such a misleading name which would confuse the public that the new company is connected to the existing company. Here, the proposed name “New Bata Ltd.” is also engaged in the shoe manufacturing activity, similar to the existing company “Bata Ltd.” This would naturally create misleading impression and confusion that the proposed company is connected with the existing company. So, Registrar of Companies would be justified in disallowing the new proposed name.

(C) The Articles of Association has contained a clause that A should be the Financial Advisor of the company for a period of five years and he should not be removed for misconduct. Vinod acted as Financial Advisor for a period of two years. Later, the company has removed him. Vinod sues the company for damages. Decide.
**Formation and Incorporation of Companies**

**Answer:** Vinod cannot succeed because the Articles of Association does not constitute a contract between the company and an outsider. Moreover, the right has been conferred on Vinod other than as a member. The leading case on this matter is *Eley Vs Positive Life Assurance Co.* (1876) 1 Ex. Div. 88 and *Mothey Krishna Rao Vs Grandhi Anjaneyulu* (AIR 1954) Madras 113.

**Descriptive Questions**

1. Define ‘Company’. Write the essential features of a company. (1.2 and 1.3)

2. “Company is an artificial person, invisible, intangible and existing only in the eyes of law.” Explain. (1.2 and 1.3)

3. “A company has a separate legal existence, and is altogether a different person from its directors and members.” –Discuss. (1.2 and 1.3)

4. Discuss the facts and principles of law laid down in Soloman Vs Soloman. (1.2 and 1.3)

5. Discuss the concept of ‘One man Company’. (1.2 and 1.3)

6. State the principles of law laid down in “Solomon Vs. Solomon and Co. Ltd. What are the exceptions to the decision in Solomon’s case? (1.3)

7. Define company and describe the different types of companies. (1.2 and 1.4)

8. Who is a promoter? “A promoter is neither the trustee nor the agent of the company, he promotes.” Discuss. Can a promoter be paid remuneration? (1.6)

9. Explain the term “Company”. Discuss the various steps involved in Formation of Company. (1.2, 1.5, 1.6, 1.7, 1.10 and 1.11)

10. Write the advantages of Incorporation of Company. What is the effect on incorporation of a company? (1.7, 1.8 and 1.9)

11. Discuss the importance and contents of Memorandum of Association and Articles of Association. (1.2, 1.12 and 1.13)

12. What are the clauses to be stated in the Memorandum of Association? (1.2, 1.12 and 1.13)

13. “The Memorandum of Association is the fundamental law or charter defining the objects and limiting the powers of the company.” Explain. (1.2, 1.12 and 1.13)

14. Explain the doctrine of ‘Ultra Vires’. What are the effects of the ultra vires transaction? Can a company ratify such transactions? (1.13 –Point C)

15. Write short notes on:
   (A) One-man company (1.3)
   (B) Corporate veil (1.3)
   (C) Ultra vires of Memorandum of Association (1.13 –C)
   (D) Common seal (1.3 –Point 4)
   (E) Commencement of business (1.11)