

# COMPANY LAW AND SECRETARIAL PRACTICE – I

## UNIT-I

### MEANING OF COMPANY:

The term “company” refers to a body corporate. In other words, it is a body incorporated in accordance with the provisions of a specified Act. It is viewed to be a person created by law – a jurisdical person. Its legal entity is distinct from its members and independent of even its promoters who give birth to it.

### DEFINITION COMPANY.

According to **Haney’s** definition, this brings out all its essentials. He observes, “A company is an incorporated association; it is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal.”

According to sec 3 (1) (i) of Indian companies Act, a company is one “formed and registered under this Act or an existing company”

According to **Justice Cave** “A corporation is a legal person just as much as an individual, but with no physical existence”

### SALIENT FEATURES COMPANY:

#### **Separate legal entity**

A company is a person created by law. It means that it comes into existence only by complying with all formalities prescribed under the Companies Act, 1956. It enjoys a separate personality of its own, different from the members composing it. This enables a company to enter into valid contracts with others including its members and deal with the property in any way it likes. It can sue others in its own name and be sued in its own name by others including its members.

#### **Perpetual Succession- Continuity of Life**

“Members may come and go but the company can go on forever” (Lord Gower). This is because company’s existence does not depend upon the existence of even promoters who were instrumental in its formation. Neither change in the membership of the company nor the death of its members has any impact on the continuity of its life.

### **Common Seal**

Though the separate personality of the company is legally recognised, it needs human agency to act. Obviously it cannot sign. Any contract entered into by a company, to be valid, must bear the official seal of the company.

### **Limited Liability**

The liability of the members of a company is generally limited to the value of shares. When once the full value of the shares is paid up, there is no more liability for the shareholders. The feature of limited liability attracts a large number of investors to subscribe to the shares of the company.

### **Easy Transferability of Shares**

In the case of public limited companies, their fully paid shares can be transferred to others without any difficulty. However, in the case of private limited companies, the right to transfer the shares is subject to certain restrictions.

## **MERITS OF THE COMPANY**

The distinctive features of a joint stock company are in fact its merits. They make this form of organisation very popular and better fitted for starting large-sized business ventures.

### **Stability (Perpetual Life)**

While certain contingencies such as death, insanity or insolvency of partners lead to the dissolution of partnership, they do not have any effect on the continued existence of a company. The company enjoys perpetual succession despite change in its membership or change in its Board of directors. Large sized enterprises which take a long time to reach profit earning stage can be started only as company form of organisations which ensures long life.

### **Limited Liability**

The liability of a member of a joint stock company is limited to the amount remaining unpaid on his shares. Once the full value of the shares is paid, a shareholder will not be called upon to contribute anything further even if the assets are inadequate to meet business debts. In view of this feature of limited liability, people come forward readily to invest in the shares of joint stock companies. Thus the savings of the community which lie scattered can be easily mobilised for financing business enterprises.

### **Easy and Speedy Transferability of Shares**

The fully paid up shares of a public limited company can be easily transferred from one person to another by following the procedure prescribed by the Companies Act, 1956. This facility is another attraction for the investing public to subscribe to the shares of the company.

### **Professionalization of Management**

In a company form of organisation there is complete divorce between ownership and management. Though shareholders are the real owners, they do not have any right to manage its affairs. Management of a company is entrusted to a Board of Directors elected by the shareholders from among themselves. The Board can secure the services of experts in various fields of production and management.

### **Economies of large scale**

In view of the suitability of the company form of organisation for undertaking large sized industries, it can reap all the advantages of economies of large scale operation. Further there is scope for tremendous growth through expansion of its activities as rising of capital is not a problem for sound companies.

### **Better credit**

A company enjoys greater public confidence and reputation in the capital market as its functioning is subject to many legal restrictions with a view to protecting the interest of all the shareholders. In view of these merits joint stock form of organisation is very popular and is preferred to other forms especially for setting up large sized industrial undertakings.

## **DEMERITS OF THE COMPANY:**

### **Complicated legal formalities**

The legal formalities to be complied with at the time of forming a company are complicated and difficult. Even after incorporation, its functioning is subject to severe restrictions. A number of documents have to be filed with the Registrar of joint stock companies from time to time and every failure in this regard invites penalties.

### **Heavy cost of Floating a company**

At the promotion and incorporation stage itself, the company has to get the services of specialised professionals. Many documents are to be drafted and printed. Further, huge expenditure is to be incurred for publicising the issue of prospectus, inviting the public to subscribe to the shares of the company. Cost of merchant bankers to whom the entire issue of shares is entrusted, also adds considerably to the cost of raising capital.

### **Separation of Ownership and Control**

Though divorce of ownership and control is an advantageous feature of a company form of organisation, it also acts as a setback in that the shareholders are not entitled to participate directly in its management. Their interest may not be well taken furthering their own selfish motives, and thereby harming the larger interest of the company and the shareholders.

### **Fraudulent Promoters**

Unscrupulous promoters may mobilise large capital through attractively designed prospectus, swindle the money and disappear, despite the stringent legal restrictions. Shareholders lose their entire money. Such companies, known as ‘fly by night companies’ are a threat to a healthy capital market.

### **Oligarchic Management**

In theory, the management of a company is democratic, as it is in the hands of the Board of Directors who are elected by the shareholders from among themselves. However, in reality it proves to be a case of oligarchy. Due to the apathy and ignorance of a vast number of shareholders and because of their being widely scattered throughout the length and breadth of the country, a very few shareholders tend to get themselves elected as directors and manage the affairs of a company. Since the voting strength depends on the number of shares, the power is concentrated in a few hands. Also the shareholders attending the meeting are far less. They do not have any voice in the management and the general meetings prove to be only a farce.

## **LIFTING OF THE CORPORATE VEIL:**



The Corporate Veil Theory is a legal concept which separates the identity of the company from its members. Hence, the members are shielded from the liabilities arising out of the company's actions.

Therefore, if the company incurs debts or contravenes any laws, then the members are not liable for those errors and enjoy corporate insulation. In simpler words, the shareholders are protected from the acts of the company.

### **Corporate Veil Theory**

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### **Piercing the Corporate Veil**

Scenarios under which the Courts consider piercing or lifting the corporate veil are as below,

#### **1. To Determine the Character of the Company**

There are cases where the Courts need to understand if the company is an enemy or friend. In such cases, the Courts adopt the test of control. The Courts usually avoid piercing the corporate veil, unless the public interest is in jeopardy. However, to ascertain if a company is an enemy company, the Court might choose to do so.

## **2. To Protect Revenue or Tax**

In matters concerning evasion or circumvention of taxes, duties, etc., the Court might disregard the corporate entity.

Imagine a company that is used to evade tax. In such cases, piercing the corporate veil allows the Court to understand the real owner of the income of the company and make the said person liable for legitimate taxes.

## **3.If trying to avoid a Legal Obligation**

Sometimes the members of a company can create another company subsidiary company to avoid certain legal obligations. In such cases, piercing the corporate veil allows the Courts to understand the real transactions.

Imagine a company liable to share 20 percent of its profits with its employees as a bonus. This is a legal obligation. To avoid this, the company opens a wholly owned subsidiary company and transfers its investment holdings to it.

The new company formed has no assets of its own and no business income either. It is completely dependent on the principal company.

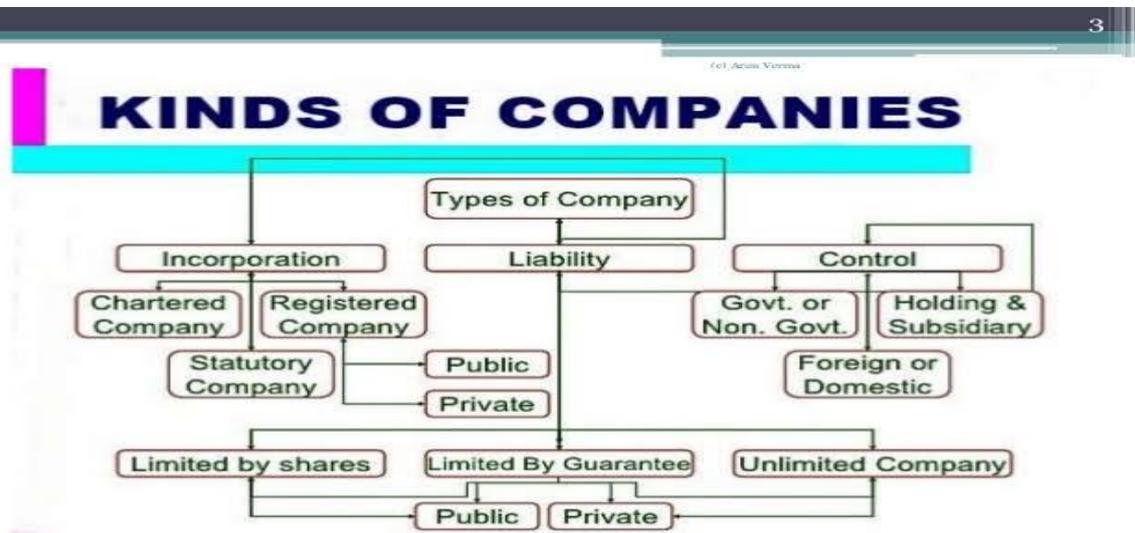
## **4. Forming Subsidiaries to act as Agents**

Sometimes, the basis of the formation of a company is to act as an agent or trustee of its members or of another company. In such cases, the company loses its individuality in favour of its principal. Also, the principal is liable for the acts of such a company.

## **5. A company formed for fraud or improper conduct or to defeat the law**

In cases where a company is formed for some illegal or improper purposes like defeating the law, the Courts might decide to lift or pierce the corporate veil.

## KINDS OF COMPANY:



Joint Stock Companies can be classified on the basis of incorporation, nature of liability, extent of public interest, ownership, nationality etc. Let us examine briefly the different kinds of companies.

### **ON THE BASIS OF INCORPORATION:**

Any company is to be incorporated under an Act. The provision of the particular Act under which it is established governs its working. Companies of this kind are of three types. They are:

#### **Chartered Companies**

Companies established as a result of a charter granted by the King or Queen of a country is known as chartered companies. The charter issued, governs their functioning. **Examples:** East India Company and Bank of England. The provisions of the Companies Act are not applicable to them. In India, such companies do not exist now.

#### **Statutory Companies**

Companies established by Special Acts of Parliament or State Legislatures are called statutory companies. The special Acts under which they are established regulate their functioning. Reserve Bank of India, Life Insurance Corporation of India etc. is of this type.

## **Registered Companies**

Companies which are registered under The Companies Act, 1956 are called registered companies. A vast majority of companies we come across belong to this category. Tata Motors Limited, Satyam Computer Services Ltd, EID Parry Ltd, etc belong to this category.

### **ON THE BASIS OF LIABILITIES:**

On the basis of the extent of liabilities of the shareholders such companies are divided into three categories.

#### **Companies Limited by Shares**

Here the maximum liability of a shareholder is limited to the amount unpaid on the shares held. Once he pays the full value of shares, he has no further liability. A vast majority of companies in India are of this type.

#### **Companies Limited by Guarantee**

In a company limited by guarantee the liability of a shareholder is limited to the amount he has voluntarily undertaken to contribute to meet any deficiency at the time of its winding up. Such a company may or may not have a share capital. If it has a share capital a member's liability is limited to the amount remaining unpaid on his shares plus the amount guaranteed by him. This type of company is started with the object of promoting science, arts, sports, charity, etc. It is clear that its objective is not profit earning. It gets subscription from its members and donations and endowments from philanthropists.

#### **Unlimited Companies**

The liability of the members of unlimited companies is unlimited. In other words, their liability extends to their private properties also in the event of winding up. Unlimited companies are almost non-existent.

## **COMPANIES ON THE BASIS OF NATIONALITY:**

They are of two types viz domestic companies and foreign companies.

### **Domestic Company**

Companies registered under the Companies Act, 1956 or under earlier Acts are considered domestic companies.

### **Foreign Company**

Foreign company means a company incorporated outside India but having a place of business in India. It has to furnish to the authorities the full address of the registered or principal office of the company or a list of its directors or names and addresses of the residents in India authorized to receive notices, documents, etc.

## **ON THE BASIS OF OWNERSHIP:**

They are of three types viz holding company, subsidiary company and Government Company.

### **Holding and Subsidiary Companies**

A company becomes a holding company of another

- i) If it can appoint or remove all or majority of the directors of the latter company or
- ii) If it holds more than 50% of the equity share capital of the latter or
- iii) If it can exercise more than 50% of the total voting power of the latter.

The other company which is so controlled is called subsidiary company.

### **Government Companies**

A Government company is one in which not less than 51% of the paid up capital is held by the Central Government or by any one or more State Governments or partly by the Central Governments and partly by one or more State Governments. Examples: Bharat Heavy Electricals Limited, Steel Authority of India Limited, etc A subsidiary of a Government company is also treated as a Government company. A Government company also enjoys a separate corporate existence. It should not be identified with the Government and its employees are not Government employees.

## ON THE BASIS OF NUMBER OF MEMBERS:

### Public Limited Companies

The public is invited to subscribe to the shares of the company usually by issuing a prospectus. Shares are easily transferable. Minimum number of person is seven and there is no limit to the maximum number of shareholders. The name must end with the word 'limited'.

### Private Limited Companies

A private limited company is a company which has a minimum paid up capital of rupees 1, 00,000 or such higher paid up capital, as may be prescribed. The Articles of Association may prescribe the following.

- i. Restricts the right to transfer the shares, if any.
- ii. Limits the number of its members to 200 not including its present or past employee- members
- iii. Prohibits any invitation to the public to subscribe to any shares in or debentures of the company. The name of the company must end with the words "Private Limited".

## DIFFERENCES BETWEEN A PRIVATE LIMITED COMPANY AND A PUBLIC LIMITED COMPANY

S.No	Basis of Differences	Private Limited Companies	Public Limited Companies
1	Number of Members	In the case of a private limited company, the minimum number of members is two while the maximum is not to exceed 200 ( excluding its employee members whether past or present)	As for the public limited company while the minimum number of members is 7, the maximum is unlimited

2	Name	The words " Private Limited" must be added at the end of the name of the private limited company	The name of a public limited company must end with the word "Limited "
3	Articles of Association	A private limited company has to file the Articles of Association of its own with the Registrar of companies	A Public limited company can have either its own Articles or can adopt model set of articles as provided in Table A of the companies Act.
4	Minimum Subscription	The question of minimum subscription does not arise in the case of a private limited company	A public limited company has to collect minimum subscription as specified in the prospectus, i.e. minimum of 90 % of the Shares issued by the company
5	Allotment of Shares	Conditions to be satisfied before allotment of shares do not apply to a private limited company	In the case of public limited companies only after collecting minimum subscription and after allotting shares to existing shareholders, allotment to new applicants can begin
6	Directors	A private limited company must have at least two directors. They need not retire by rotation. One can act as a director in any number of private limited companies	In the case of a public limited company, it should have at least three directors. They are subject to retirement by rotation. A person can act as a director for a maximum of 15 companies
7	Statutory Meeting	A Private limited company need not hold any statutory meeting	A public limited company should hold it within six months from the date of the commencement of business.

<b>8</b>	Quorum	The minimum number of members to be present in a meeting so as to constitute a valid meeting is two in a private company	Whereas it is five in a public limited company
<b>9</b>	Managerial Remuneration	In a private limited company, no limit has been placed on managerial remuneration	In a public limited company, the overall managerial remuneration shall not exceed 11 % of the net profits. However, if there is no profit in any year, or if the profits are inadequate, such remuneration shall not exceed the limits prescribed in the act.
<b>10</b>	Issue of Prospectus	A private company is prohibited from issuing prospectus.	A public limited company can issue prospectus.
<b>11</b>	Transfer of shares	There is restriction on the transfer of shares in this company	Shares of public company are freely transferable
<b>12</b>	Issue of subsequent shares	Rights issue does not arise	Public company's new shares are offered first to the existing shareholders
<b>13</b>	Issue of share warrants	A private company cannot issue share warrant	It can issue share warrants
<b>14</b>	Retirement of directors	In a private company a director is not required to retire at the age of sixty five years.	Public company directors have to retire at the age of sixty five years.

## **OVERVIEW OF COMPANY ACT 1956:**

The Companies Act, 1956 constitutes the Company Law in India. It came into force with effect from 1<sup>st</sup> April, 1956. It is a consolidating Act which presents the whole body of the company law in a complete form and repeals earlier Companies Act and subsequent amendments. It contains 658 sections and XV schedules and numerous forms.

## **MAIN OBJECTIVES OF COMPANY ACT 1956:**

1. To protect the interest of shareholders.
2. To safeguard interest of creditors.
3. To help the development of companies in India on healthy lines.
4. To help the attainment of ultimate ends of the social and economic policy of the government.
5. To equip the government with necessary powers to intervene directly into affairs of a company in public interest.

## **SPECIAL FEATURES OF COMPANIES ACT 1956:**

1. It provides more stringent provisions relating to the company promoters and company management.
2. It provides elaborate provisions relating to the form and contents of a prospectus, maintenance of accounts by companies, reduction of share capital, etc.
3. This Act recognizes the institution of 'Government Companies' (in which government holds at least 51% share capital) and makes special provisions for them.
4. The Act also provides measures calculated to disintegrate the concentration of economic power and wealth which affect the public interest adversely.
5. It gives extensive powers to the Central Government and the Company Law Board to intervene directly in affairs of a company in public interest, in recognition of the fact that a public company should be regarded as a national asset and not as something of exclusive concern to the shareholders or the directors.

## **COMPANY LAW BOARD (CLB)**

With a view to ensuring greater efficiency, cohesion and despatch in the day-to-day administration of the Companies Act, an administrative authority, namely, the Board of Company Law Administration (popularly known as the Company Law Board) was set up in February 1964, by Central Government, in accordance with Section 10F. The CLB is to exercise and discharge such powers and functions of the Central Government under this Act or any other law as may be conferred on it by the Central Government, by notification in the Official Gazette under the provisions of this Act or that other law.

Under the provision of Companies (Amendment) Act, 1988, the powers and functions of CLB have been enlarged. The new Board is quasi-judicial body. It has been vested with considerable powers and functions. Some of these are judicial while others are administrative in nature. The Board has the power to regulate its own procedure and act in its own discretion. The Board would be guided by the principles of natural justice in the conduct of its business.

The new CLB, as reconstituted on 31<sup>st</sup> May, 1991, has framed the CLB Regulations, 1991, for regulating the proceedings before it. The government has also prescribed the fee making an application to the Company Law Board vide CLB (Fees on Application and Petitions) Rules, 1991.

The CLB is to consist of such number of members, not exceeding 9, as the Central Government may appoint by notification in the Official Gazette, and one of such member shall be appointed as its Chairman. The members of the CLB shall possess such qualifications and experience as may be prescribed. They may be appointed for such period, not exceeding 3 years, as may be specified in the notification.

## **APPEAL AGAINST THE ORDERS OF THE CLB**

Section 10F, provides that an aggrieved person may file an appeal against any decision or order of the CLB before the High Court, within 60 days from the date of communication thereof, on any question of law. The said period of 60 days may be extended by the Court to a further period up to 60 days on justifiable grounds. The order or decision of the Board on any question of fact will be final and will not be appealable. The High Court to which an appeal against the decision of CLB would lie.

## **OVERVIEW COMPANY SECRETARIES ACT 1980:**

**Short title, extent and commencement .-** (1) This Act may be called The Company Secretaries Act, 1980.

- It extends to the whole of India.
- It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint.

**Incorporation of the Institute.-** (1) All persons whose names are entered in the Register of the dissolved company immediately before the commencement of this Act and all persons who may hereafter have their names entered in the Register to be maintained under this Act, so long as they continue to have their names borne on the Register to be maintained under this Act, are hereby constituted a body corporate by the name of the Institute of Company Secretaries of India and all such persons shall be known as members of the Institute.

**Entry of names in the Register.-**(1) Any of the following persons shall be entitled to have his name entered in the Register, namely:—

- (a) any person who immediately before the commencement of this Act was an Associate or a Fellow (including an Honorary Fellow) of the dissolved company;
- (b) any person who is a holder of the Diploma in Company Secretaryship awarded by the Government of India;
- (c) any person who has passed the examinations conducted by the dissolved company and has completed training either as specified by the dissolved company or as prescribed by the Council, except any such person who is not a permanent resident of India;

**Associates and Fellows.-** (1) The members of the Institute shall be divided into two classes designated respectively as Associates and Fellows.

(2) Any person other than a person to whom the provisions of sub-section (4) apply shall, on his name being entered in the Register, be deemed to have become an Associate and as long as his name remains so entered, shall be entitled to use the letters "A.C.S." after his name to indicate that he is an Associate.

(3) A person, being an Associate who has been in continuous practice in India as a Company Secretary for at least five years and a person who has been an Associate for a continuous period of not less than five years and who possesses such qualifications or practical experience as the Council may prescribe with a view to ensuring that he has experience equivalent to the experience normally acquired as a result of continuous practice for a period of five years as a Company Secretary shall, on payment of such fees, as may be determined, by notification, by the Council, which shall not exceed rupees five thousand, and on application made and granted in the prescribed manner, be entered in the Register as a Fellow:

**Certificate of practice.**- (1) No member of the Institute shall be entitled practise, whether in India or elsewhere, unless he has obtained from the Council a certificate of practice. A member who desires to be entitled to practise shall make an application in such form and pay such annual fee, for his certificate as may be determined, by notification, by the Council, which shall not exceed rupees three thousand, and such fee shall be payable on or before the 1st day of April in each year : Provided that the Council may with the prior approval of the Central Government, determine the fee exceeding rupees three thousand, which shall not in any case exceed rupees six thousand.

**Members to be known as Company Secretaries.**- Every member of the Institute in practice shall, and any other member may, use the designation of a Company Secretary and no member using such designation shall use any other description, whether in addition thereto or in substitution therefor : Provided that nothing in this section shall be deemed to prohibit any such member from adding any other description or letters to his name, if entitled thereto, to indicate membership of such other institute whether in India or elsewhere as may be recognised in this behalf by the Council, or any other qualification that he may possess, or to prohibit a firm, all the partners of which are members of the Institute and in practice, from being known by its firm name as Company Secretaries.

**Constitution of the Council of the Institute .-**(1) There shall be a Council of the Institute for the management of the affairs of the Institute and for discharging the functions assigned to it by or under this Act. The Council shall be composed of the following persons, namely:--

- (a) not more than fifteen persons elected by the members of the Institute, from amongst the Fellows of the Institute chosen in such manner and from such regional constituencies as may be specified: Provided that a Fellow of the Institute, who has been found guilty of any professional or other misconduct and whose name is removed from the Register or has been awarded penalty of fine, shall not be eligible to contest the election,

**Settlement of disputes regarding election.-**In case of any dispute regarding any election under clause (a) of sub-section (2) of section 9, the aggrieved person may make an application within thirty days from the date of declaration of the result of election to the Secretary of the Institute, who shall forward the same to the Central Government.

**Establishment of Tribunal.-**(1) On receipt of any application under section 10A, the Central Government shall, by notification, establish a Tribunal consisting of a Presiding Officer and two other Members to decide such dispute and the decision of such Tribunal shall be final.

**Functions of Council.-**(1) The Institute shall function under the overall control, guidance and supervision of the Council and the duty of carrying out the provisions of this Act shall be vested in the Council.

(2) In particular, and without prejudice to the generality of the foregoing powers, the duties of the Council shall include-

- (a) To approve academic courses and their contents;
- (b) The prescribing of fees for the examination of candidates for enrolment;
- (c) The prescribing of qualifications for entry in the Register;
- (d) The recognition of foreign qualifications and training for purposes of enrolment;
- (e) The prescribing of guidelines for granting or refusal of certificates of practice under this Act;
- (f) The levy of fees from members, examinees and other persons;
- (g) The regulation and maintenance of the status and standard of professional qualifications of members of the Institute;
- (h) The carrying out, by granting financial assistance to persons other than members of the

Council or in any other manner, of research in such matters of interest to Company Secretaries as may be prescribed;

- (i) To enable functioning of the Director (Discipline), the Board of Discipline, the
  - (ii) Disciplinary Committee and the Appellate Authority constituted under the provisions of this Act;
- (j) To enable functioning of the Quality Review Board;
- (k) Consideration of the recommendations of the Quality Review Board made under clause of section 29B and details of action taken thereon in its annual report; and
- (l) To ensure the functioning of the Institute in accordance with the provisions of this Act and in performance of other statutory duties as may be entrusted to the Institute from time to time.

## **References**

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3. Secretarial Practice - M C Kuchhal – Vikas Publishers.
4. Company Law - Dr. S.R. Myneni - Asia Law House Publishers.
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6. Company Law and Secretarial Practice – N.D.Kapoor – Sultan chand& Sons Publications.

## Questions

### **Two marks question:**

1. What is company?
2. Define company.
3. What is Holding Company?
4. What is Government Company?

### **Five Marks question:**

1. What is the Salient Features Company?
2. What is the Merits of the Company?
3. What are the Demerits of the Company?
4. Discuss the overview of company's act 1956.

### **Ten marks question**

1. What the different between public company and private company?
2. Discuss the kinds of company.
3. Discuss the overview of company secretaries' act 1980.