REGULATORY FRAME WORK FOR COMPANIES

B.Com.

IV SEMESTER

CORE COURSE

(2011 Admission)

UNIVERSITY OF CALICUT

SCHOOL OF DISTANCE EDUCATION

CALICUT UNIVERSITY P.O., MALAPPURAM, KERALA, INDIA - 673 635

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STUDY MATERIAL

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CORE COURSE

REGULATORY FRAME WORK FOR COMPANIES

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MODULE I

COMPANIES ACT 1956

The first Companies Act was passed in India in 1850 immediately following the enactment of the Joint Stock Companies Act 1844 in England. In 1913, a comprehensive and consolidating enactment was passed based, mainly, on the English Act of 1908 with some additional provisions to meet the peculiar conditions of our country. Thus came into force the Indian Companies Act of 1913.

THE COMPANIES ACT OF 1956

With a view to enable the organization and management of companies, to develop trade and industry for faster economic development, Companies Act of 1956 came into force on 1st April 1956. This act is based on the recommendations of the company law committee (Bhabha committee) which submitted its report in 1952.

MAIN FEATURES OF THE COMPANIES ACT OF 1956

- Full and fair disclosure of various matters in the prospectus.
- Detailed information of the financial affairs of a company to be disclosed in its accounts.
- Provision for intervention and investigation by the government into the affairs of a company.
- Restriction on the powers of managing agents and other managerial personnel.
- Enforcement of proper performance of their duties by company management.
- Protection of minority share holders.

The companies Act 1956 has been amended several times to include different provision in the Act. Some of the important amendments have been in the years 1960, 1962, 1963, 1965, 1966, 1969, 1977, 1985, 1988, 1996, 2000, 2002, 2006.

ADMINISTRATIVE AUTHORITIES UNDRE THE COMPANIES ACT

The important administrative authorities under the companies Act in the present setup are:

1) The Central Government.
2) National Company Law Tribunal.
3) National Company Law Appellate Tribunal.
4) Registrars.
5) Official Liquidators.
6) Security Exchange Board of India

COMPANIES

Company is a voluntary association of persons formed to carry on some business for profit or to promote art, science, education or some charitable purpose.

A vast majority of companies in India are corporations incorporated by registration under Companies Act 1956. According to section 3 (1) (*i*) of the Companies Act 1956, a company means , "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 companies laws."

CHARACTERISTICS OF A COMPANY

The main characteristics of a company are:

1. Incorporated association. A company is created when it is registered under the Companies Act. It comes into being from the date mentioned in the certificate of incorporation. It may be noted in this connection that Section 11 provides that an association of more than ten persons carrying on business in banking or an association or more than twenty persons carrying on any other type of business must be registered under the Companies Act and is deemed to be an illegal association, if it is not so registered.

2. Artificial legal person. A company is an artificial person. Negatively speaking, it is not a natural person. It exists in the eyes of the law and cannot act on its own. It has to act through a board of directors elected by shareholders. But for many purposes, a company is a legal person like a natural person. It has the right to acquire and dispose of the property, to enter into contract with third parties in its own name, and can sue and be sued in its own name. It should be noted that though a company does not possess fundamental rights, yet it is person in the eyes of law. It can enter into contracts with its Directors, its members, and outsiders.

3. Separate Legal Entity: A company has a legal distinct entity and is independent of its members. The creditors of the company can recover their money only from the company and the property of the company. They cannot sue individual members. Similarly, the 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 its 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.

4. Perpetual Existence. A company is a stable form of business organization. Its life does not depend upon the death, insolvency or retirement of any or all shareholder(s) or director (s). Law creates it and law alone can dissolve it. Members may come and go but the company can go on forever. Thus, a company has a perpetual existence, irrespective of changes in its membership.

5. Common Seal. As was pointed out earlier, a company being an artificial person has no body similar to natural person and as such it cannot sign documents for itself. It acts through natural person who are called its directors. But having a legal personality, it can be bound by only those documents which bear its signature. Therefore, the law has provided for the use of common seal, with the name of the company engraved on it, as a substitute for its signature. Any document bearing the common seal of the company will be legally binding on the company.

6. Limited Liability: A company may be company limited by shares or a company limited by guarantee. In company limited by shares, the liability of members is limited to the unpaid value of the shares. For example, if the face value of a share in a company is Rs. 10 and a member has already paid Rs. 7 per share, he can be called upon to pay not more than Rs. 3 per share during the lifetime of the company. In a company limited by guarantee the liability of members is limited to such amount as the member may undertake to contribute to the assets of the company in the event of its being wound up.

7. Transferable Shares. In a public company, the shares are freely transferable. The right to transfer shares is a statutory right and it cannot be taken away by a provision in the articles. However, the articles shall prescribe the manner in which such transfer of shares will be made and it may also contain bonafide and reasonable restrictions on the right of members to transfer their shares. But absolute restrictions on the rights of members to transfer their shares shall be ultra vires. However, in the case of a private company, the articles shall restrict the right of member to transfer their shares in companies with its statutory definition. In order to make the right to transfer shares more effective, the shareholder can apply to the Central Government in case of refusal by the company to register a transfer of shares.

8. Separate Property: As a company is a legal person distinct from its members, it is capable of owning, enjoying and disposing of property in its own name. Although its capital and assets are contributed by its shareholders, they are not the private and joint owners of its property. The company is the real person in which all its property is vested and by which it is controlled, managed and disposed of.

9. Delegated Management: A joint stock company is an autonomous, self governing and self-controlling organization. Since it has a large number of members, all of them cannot take part in the management of the affairs of the company. Actual control and management is, therefore, delegated by the shareholders to their elected representatives, know as directors. They look after the day-to-day working of the company. Moreover, since shareholders, by majority of votes, decide the general policy of the company, the management of the company is carried on democratic lines. Majority decision and centralized management compulsorily bring about unity of action.

10. Legal Restrictions: The formation working and winding up of company are strictly governed by laws, rules and regulations.

11. Share Capital: A company mobilizes its capital by selling its shares. Those persons who buy shares become its shareholders and thereby become members in it.

'A Company is not a citizen'. Comment

A company is a legal person like a natural person. It has the right to acquire and dispose of the property, to enter into contract with third parties in its own name, and can sue and be sued in its own name.

However, it is not a citizen as it cannot enjoy the rights under the Constitution of India or Citizenship Act. In State Trading Corporation of India v C.T.O (1963 SCJ 705), it was held that neither the provisions of the Constitution nor the Citizenship Act apply to it. It should be noted that though a company does not possess fundamental rights, yet it is person in the eyes of law. It can enter into contracts with its Directors, its members, and outsiders. Justice Hidayatullah once remarked that if all the members are citizens of India, the company does not become a citizen of India.

'A Company is a legal person'. Comment

A company has a legal distinct entity and is independent of its members. The creditors of the company can recover their money only from the company and the property of the company. They cannot sue individual members. Similarly, the 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 its 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.

Separate legal entity of the company is also recognized by the Income Tax Act. Where a company is required to pay Income-tax on its profits and when these profits are distributed to shareholders in the form of dividend, the shareholders have to pay income-tax on their dividend of income. This proves that a company that a company and its shareholders are two separate entities. The characteristic of separate corporate personality of a company was also emphasized by Chief Justice Marshall of USA when he defined a company "as a person, artificial, invisible, intangible and existing only in the eyes of the law. Being a mere creation of law, it possesses only those properties which the charter of its creation confers upon it either expressly or as accident to its very existence". [Trustees of Darmouth College v woodward (1819) 17 US 518)]

Company and Partnership

	Company	**Partnership**
1**. Mode of creation**	By Registration by Statute.	By Agreement
2. **Legal Statute**	Legal entity distinct from members, perpetual succession.	Firm and partners are not separate;no separate entity; uncertain life
3. **Liability**	Limited liability of members	Unlimited joint and several liability of partners

4. **Authority**	Divorce between Right to share ownership and Management. Representative management,	Common and management ownership and Implied authority.
5. **Transfer**	Public Co.-freely of shares transferable; Transferee gets all the rights of the transferor	Ordinarily no right of transfer of share by a partner-limited rights of transferee
6. **Number of Members**	Private Co-Minimum 2 and Maximum 50 public Co. Minimum7 and Maximum unlimited.	Minimum 2 Maximum 20.
7. **Resources**	Large and unlimited resources	Personal resources of partners are limited.
8. **General**	Memorandum defines powers and confines the scope of the company. So also alteration is difficult.	Easy to change the agreement and the powers of the partners.
9. **Legal formalities**	Statutory books, Audit, Publication Registration, compulsory.	No legal formalities Registration, no audit, filing, etc. lots of legal no publication of accounts etc.
10. **Dissolution**	Only according to the provisions of law- usually by an order of notice, by court. Death of a share-holder does not affect the existence of a company	Dissolution by agreement by the court Death of a partner may mean dissolution of partnership

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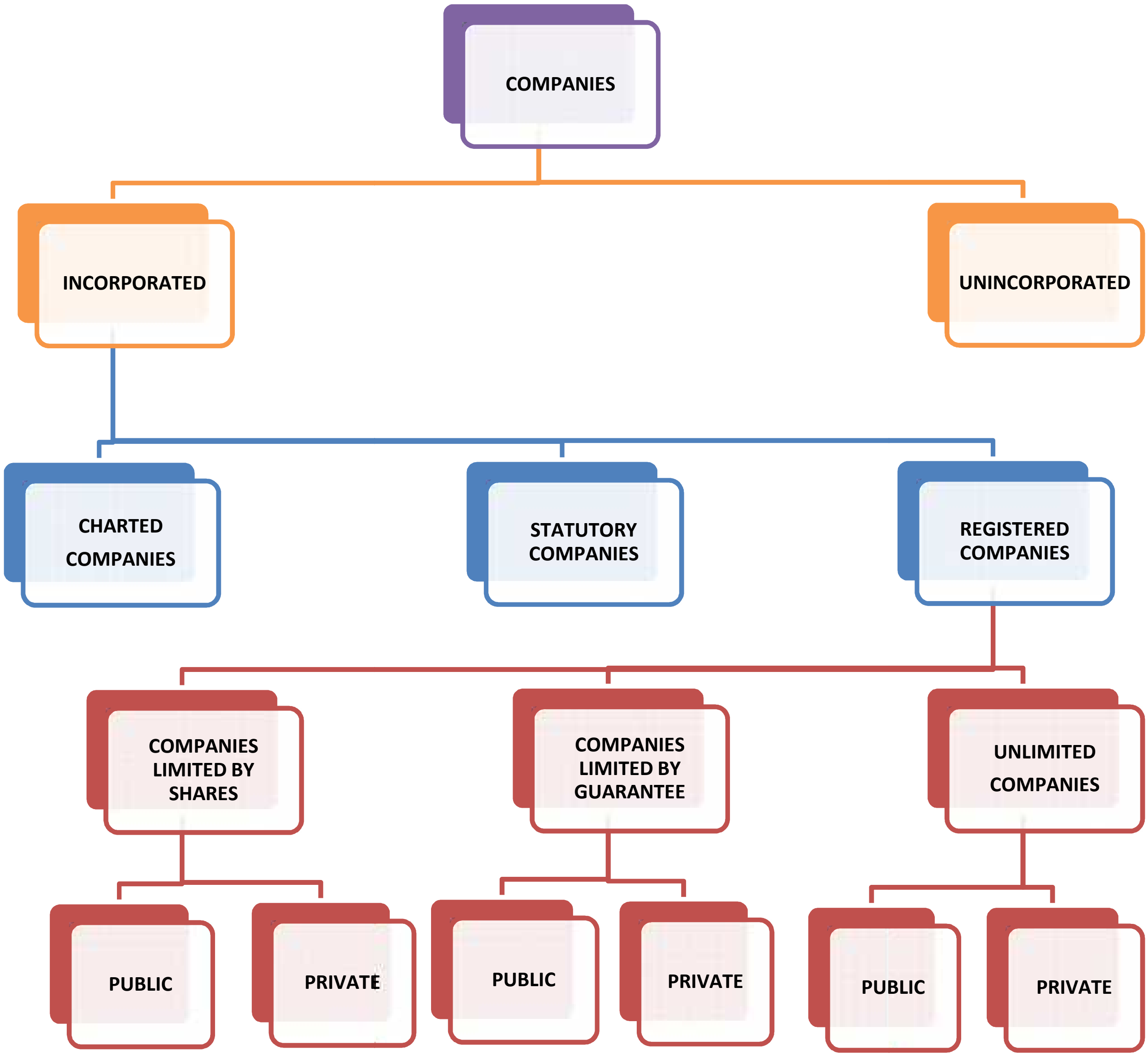
KINDS OF COMPANIES



Joint Stock Company can be of various types. The following are the important types of company:

1. Classification of Companies by Mode of Incorporation

Depending on the mode of incorporation, there are three classes of joint stock companies.

A. Chartered companies. These are incorporated under a special charter by a monarch. The powers and nature of business of a chartered company are defined by the charter which incorporates it. A chartered company has wide powers. It can deal with its property and bind itself to any contracts that any ordinary person can. In case the company deviates from its business as prescribed by the charted, the Sovereign can annul the latter and close the company. Such companies do not exist in India.

B. Statutory Companies. These companies are incorporated by a Special Act passed by the Central or State legislature. Reserve Bank of India, State Bank of India, Industrial Finance Corporation, Unit Trust of India, State Trading corporation and Life Insurance Corporation are some of the examples of statutory companies. Such companies do not have any memorandum or articles of association. They derive their powers from the Acts constituting them and enjoy certain powers that companies incorporated under the Companies Act have. Alternations in the powers of such companies can be brought about by legislative amendments. These companies are generally formed to meet social needs and not for the purpose of earning profits.

C. Registered or incorporated companies: - These are formed under the Companies Act, 1956 or under the Companies Act passed earlier to this. Such companies come into existence only when they are registered under the Act and a certificate of incorporation has been issued by the Registrar of Companies. This is the most popular mode of incorporating a company. Registered companies may further be divided into three categories of the following.

i) Companies limited by Shares: - These types of companies have a share capital and the liability of each member or the company is limited by the Memorandum to the extent of face value of share subscribed by him. In other words, during the existence of the company or in the event of winding up, a member can be called upon to pay the amount remaining unpaid on the shares subscribed by him. Such a company is called company limited by shares. A company limited by shares may be a public company or a private company. These are the most popular types of companies.

ii) Companies Limited by Guarantee: - These types of companies may or may not have a share capital. Each member promises to pay a fixed sum of money specified in the Memorandum in the event of liquidation of the company for payment of the debts and liabilities of the company [Sec 13(3)] This amount promised by him is called 'Guarantee'. The Articles of Association of the company state the number of member with which the company is to be registered [Sec 27 (2)]. Such a company is called a company limited by guarantee. The amount of guarantee of each member is in the nature of reserve capital. This amount cannot be called upon except in the event of winding up of a company. Non-trading or non-profit companies formed to promote culture, art, science, religion, commerce, charity, sports etc. are generally formed as companies limited by guarantee.

iii) Unlimited Companies: Section 12 gives choice to the promoters to form acompany with or without limited liability. A company not having any limit on the liability of its members is called an 'unlimited company' [Sec 12(c)]. An unlimited company may or may not have a share capital. If it has a share capital it may be a public company or a private company. If the company has a share capital, the article shall state the amount of share capital with which the company is to be registered [Sec 27 (1)] The articles of an unlimited company shall state the number of member with which the company is to be registered.

II. On the Basis of Number of Members

On the basis of number of members, a company may be:

(1) Private Company, and (2) Public Company.

A. Private Company

According to Sec. 3(1) (iii) of the Indian Companies Act, 1956, a private company is that company which by its articles of association :

i) limits the number of its members to fifty, excluding employees who are members or ex-employees who were and continue to be members;
ii) restricts the right of transfer of shares, if any;
iii) prohibits any invitation to the public to subscribe for any shares or debentures of the company.

Where two or more persons hold share jointly, they are treated as a single member. According to Sec 12 of the Companies Act, the minimum number of members to form a private company is two. A private company must use the word "Pvt" after its name.

CHARACTERISTICS OR FEATURES OF A PRIVATE COMPANY

The main features of a private of a private company are as follows:

- A private company restricts the right of transfer of its shares. The shares of a private company are not as freely transferable as those of public companies.
- It limits the number of its members to fifty. The minimum number of members to form a private company is two.
- A private company cannot invite the public to subscribe for its capital or shares of debentures. It has to make its own private arrangement.

B. PUBLIC COMPANY

According to Section 3 (1) (iv) of Indian Companies Act. 1956 "A public company which is not a Private Company", If we explain the definition of Indian Companies Act. 1956 in regard to the public company, we note the following :

i) The articles do not restrict the transfer of shares of the company
ii) It imposes no restriction no restriction on the maximum number of the members on the company.
iii) It invites the general public to purchase the shares and debentures of the companies

DIFFERENCES BETWEEN A PUBLIC COMPANY AND A PRIVATE COMPANY

1. Minimum number: The minimum number of persons required to form a public company is 7. It is 2 in case of a private company.

2. Maximum number: There is no restriction on maximum number of members in a public company, whereas the maximum number cannot exceed 50 in a private company.

3. Number of directors. A public company must have at least 3 directors whereas a private company must have at least 2 directors (Sec. 252)

4. Restriction on appointment of directors. In the case of a public company, the directors must file with the Register consent to act as directors or sign an undertaking for their qualification shares. The directors or a private company need not do so (Sec 266)

5. Restriction on invitation to subscribe for shares. A public company invites the general public to subscribe for shares. A public company invites the general public to subscribe for the shares or the debentures of the company. A private company by its Articles prohibits invitation to public to subscribe for its shares.

6. Name of the Company: In a private company, the words “Private Limited” shall be added at the end of its name.

7. Public subscription: A private company cannot invite the public to purchase its shares or debentures. A public company may do so.

8. Issue of prospectus: Unlike a public company a private company is not expected to issue a prospectus or file a statement in lieu of prospectus with the Registrar before allotting shares.

9. Transferability of Shares. In a public company, the shares are freely transferable (Sec. 82). In a private company the right to transfer shares is restricted by Articles.

10. Special Privileges. A private company enjoys some special privileges. A public company enjoys no such privileges.

11. Quorum. If the Articles of a company do not provide for a larger quorum 5 members personally present in the case of a public company are quorum for a meeting of the company. It is 2 in the case of a private company (Sec. 174)

12. Managerial remuneration. Total managerial remuneration in a public company cannot exceed 11 per cent of the net profits (Sec. 198). No such restriction applies to a private company.

13. Commencement of business. A private company may commence its business immediately after obtaining a certificate of incorporation. A public company cannot commence its business until it is granted a “Certificate of Commencement of business”.

SPECIAL PRIVILEGES OF A PRIVATE COMPANY

Unlike a private a public company is subject to a number of regulations and restrictions as per the requirements of Companies Act, 1956. It is done to safeguard the interests of investors/shareholders of the public company. These privileges can be studied as follows :

a) Special privileges of all companies.

The following privileges are available to every private company, including a private company which is subsidiary of a public company or deemed to be a public company:

1. A private company may be formed with only two persons as member. Sec.12(1)]
2. It may commence allotment of shares even before the minimum subscription is subscribed for or paid (Sec. 69).
3. It is not required to either issue a prospectus to the public of file statement in lieu of a prospectus. (Sec 70 (3)]
4. Restrictions imposed on public companies regarding further issue of capital do not apply on private companies. [Sec 81 (3)]
5. Provisions of Sections 114 and 115 relating to share warrants shall not apply to it. (Sec. 14)
6. It need not keep an index of members. (Sec. 115)
7. It can commence its business after obtaining a certificate of incorporation. A certificate of commencement of business is not required. [Sec. 149 (7)]
8. It need not hold statutory meeting or file a statutory report [Sec. 165 (10)]
9. Unless the articles provide for a larger number, only two persons personally present shall form the quorum in case of a private company, while at least five member personally present form the quorum in case of a public company (Sec. 174).
10. A director is not required to file consent to act as such with the Registrar. Similarly, the provisions of the Act regarding undertaking to take up qualification shares and pay for them are not applicable to directors of a private companies [Sec. 266 (5) (b)]
11. Provisions in Section 284 regarding removal of directors by the company in general meeting shall not apply to a life director appointed by a private company on or before 1st April 1952 [Sec. 284 (1)]
12. In case of a private company, poll can be demanded by one member if not more than seven members are present, and by two member if not more than seven member are present. In case of a public company, poll can be demanded by persons having not less than one-tenth of the total voting power in respect of the resolution or holding shares on which an aggregate sum of not less than fifty thousand rupees has been paid-up (Sec. 179).
13. It need not have more than two directors, while a public company must have at least three directors (Sec. 252)

b) Privileges available to an independent private company:

An independent private company is one which is not a subsidiary of a public company. The following special privileges and exemptions are available to an independent private company.

1. It may give financial assistance for purchase of or subscription for shares in the company itself.
2. It need not, like a public company, offer rights shares to the equity shareholders of the company.
3. The provisions of Sec. 85 to 90 as to kinds of share capital, new issues of share capital, voting, issue of shares with disproportionate rights, and termination of disproportionately excessive rights, do not apply to an independent private company.
4. A transfer or transferee of shares in an independent private company has no right of appeal to the Central Government against refusal by the company to register a transfer of its shares.
5. Sections 171 to 186 relating to general meeting are not applicable to an independent private company if it makes its own provisions by the Articles. Some provisions of these Sections are, however made expressly applicable.
6. Many provisions relating to directors of a public company are not applicable to an independent private company, e.g.
    a) it need not have more than 2 directors.
    b) The provisions relating to the appointment, retirement, reappointment, etc. of directors who are to retire by rotation and the procedure relating, there to are not applicable to it.
    c) The provisions requiring the giving of 14 days' notice by new candidates seeking election as directors, as also provisions requiring the Central Government's sanction for increasing the number of directors by amending the Articles or otherwise beyond the maximum fixed in the Articles, are not applicable to it.
    d) The provisions relating to the manner of filing up casual vacancies among directors and the duration of the period of office of directors and the requirements that the appointment of directors should be voted on individually and that the consent of each candidate for directorship should be filed with the Registrar, do not apply to it.
    e) The provisions requiring the holding of a share qualification by directors and fixing the time within which such qualification is to be acquired and filing with the Registrar of a declaration of share qualification by each director are also not applicable to it.

f) It may, by its Articles, Provide special disqualifications for appointment of directors.

g) It may provide special grounds for vacation of office of a director.

h) Sec. 295 prohibiting loans to directors does not apply to it.

i) An interested director may participate or vote in Board's proceedings relating to his concern of interest in any contract of arrangement.

7. The restrictions as to the number of companies of which a person may be appointed managing director and the prohibition of such appointment for more than 5 years at a time, do not apply to it

8. The provisions prohibiting the subscribing for, or purchasing of, shares or debentures of other companies in the same group do not apply to it.

9. The provisions of Section 409 conferring power on the Central Government to present change in the Board of directors of a company where in the opinion of the Central Government such change will be prejudicial to the interest of the company, do not apply to it.

WHEN A PRIVATE COMPANY BECOMES A PUBLIC COMPANY

A private company shall become a public company in following cases:

i) **By default**: When it fails to comply with the essential requirements of a private company provided under Section 3 (1) (iii) Default in complying with the said three provisions shall disentitle a private company to enjoy certain privileges (Sec. 43).

ii) A private company which is a **subsidiary** of another public company shall be deemed to be a public company.

iii) **By provisions of law -** Section 43-A.

Section 43-A

a) Where not less than 25% of the paid-up share capital of a private company is held by one or more bodies" corporate such a private company shall become a public company from the data in which such 25% is held by body corporate [Sec. 43-A (1)]

b) Where the average annual turnover of a private company is not less than Rs. 10 crores during the relevant period, such a private company shall become a public company after the expiry of the period of three months from the last day of the relevant period when the accounts show the said average annual turnover [Sec. 43 A (1 A)].

c) When a private company holds not less than 25% of the paid up share capital of a public company the private company shall become a public company from the date on which the private company holds such 25% [Sec. 43A (IB)].

d) Where a private company accepts, after an invitation is made by an advertisement of receiving deposits from the public other than its members, directors or their relatives, such private company shall become a public company [Sec. 43A (IC)].

iv) By Conversion : When the private company converts itself into a public company by altering its Articles in such a manner that they no longer include essential requirements of a private company under Section 3 (1) (iii). On the data of such alternations, it shall cease to be private company. It shall comply with the procedure of converting itself into a public company [Sec. 44]. The Articles of Association of such a public company may continue to have the three restrictions and may continue to have two directors and less than seven members.

Within 3 months of such a conversion. Registrar of Companies shall be intimated. The Registrar shall delete the word 'Private' before the words 'Limited' in the name of the company and shall also make necessary alternations in the certificate of incorporation.

III. On the basis of Control

On the basis of control, a company may be classified into :

1. Holding companies, and
2. Subsidiary Company

1. Holding Company [Sec. 4(4)].

A company is known as the holding company of another company if it has control over the other company. According to Sec 4(4) a company is deemed to be the holding company of another if, but only if that other is its subsidiary.

A company may become a holding company of another company in either of the following three ways :-

a) By holding more than fifty per cent of the normal value of issued equity capital of the company; or

b) By holding more than fifty per cent of its voting rights; or

c) By securing to itself the right to appoint, the majority of the directors of the other company , directly or indirectly.

The other company in such a case is known as a "Subsidiary company". Though the two companies remain separate legal entities, yet the affairs of both the companies are managed and controlled by the holding company. A holding company may have any number of subsidiaries. The annual accounts of the holding company are required to disclose full information about the subsidiaries.

2. Subsidiary Company. [Sec. 4 (I)].

A company is known as a subsidiary of another company when its control is exercised by the latter (called holding company) over the former called a subsidiary company. Where a company (company S) is subsidiary of another company (say Company H), the former (Company S) becomes the subsidiary of the controlling company (company H).

IV. On the basis of Ownership of companies

a) Government Companies. A Company of which not less than 51% of the paid up capital is held by the Central Government of by State Government or Government singly or jointly is known as a Government Company. It includes a company subsidiary to a government company. The share capital of a government company may be wholly or partly owned by the government, but it would not make it the agent of the government . eg. Bharat Heavy Electricals Ltd. Hindustan Machine Tools Ltd. etc.

b) Non-Government Companies. All other companies, except the Government Companies, are called non-government companies. They do not satisfy the characteristics of a government company as given above.

V. On the basis of Nationality of the Company

a) Indian Companies : These companies are registered in India under the Companies Act. 1956 and have their registered office in India. Nationality of the members in their case is immaterial.

b) Foreign Companies : It means any company incorporated outside India which has an established place of business in India [Sec. 591 (I)]. A company has an established place of business in India if it has a specified place at which it carries on business such as an office, store house or other premises with some visible indication premises. Section 592 to 602 of Companies Act, 1956 contain provisions applicable to foreign companies functioning in India.

MODULE II

PROMOTION AND INCORPORATION OF COMPANIES

INTRODUCTION

We know that a company is a separate legal entity which is formed and registered under the Companies Act. After deciding about the formation of the company like (a) which business they should start, (b) whether they should form a new company or take over he business of some existing company, (c) if new company is to be started, whether they should start a private company or pubic company, (d) what should be the capital of the company etc. the desirous persons take necessary steps, and the company is actually formed. Thereafter, they start their business. Thus, there are various stage in the formation of a company from thinking of starting a business to the actual starting of the business.

INCORPORATION OF COMPANIES

Company is an artificial person created by following a legal procedure. Before a company is formed, a lot of preliminary work is to be performed which can be divided into four distinct stages :

- Promotion;
- Incorporation or Registration;
- Capital subscription; and
- Commencement of business.

However, a private company can start business as soon as it obtains the certificate of incorporation. It needs to go through first two stages only. The reason is that a private company cannot invite public to subscribe to its share capital. But a public company having a share capital, has to pass through all the four stages mentioned above before it can commence business or exercise any borrowing powers (Section 149).

These four stages are discussed as follow :

1. PROMOTION

The term ‘promotion’ is a term of business and not of law. It is frequently used in business. Gerstenberg has defined promotion as “the discovery of business opportunities and the subsequent organization of funds, property and managerial ability into a business concern for the purpose of making profits there from.” First of all the idea of carrying on a business is conceived by promoters. Promoters are persons engaged in, one or the other way; in the formation of a company. Next, the promoters make detailed study to assess the feasibility of the business idea and the amount of financial and other resources required. When the promoters are satisfied about practicability of the business idea, they take necessary steps for assembling the business elements and making provision of the funds required to launch the business enterprise. Law does not require any qualification for the promoters. The promoters stand in a fiduciary position towards the company about to be formed. From the fiduciary position of promoters, the following important results follow:

1. A promoter cannot be allowed to make any secret profits. If any secret profit is made in violation of this rule, the company may, on discovering it, compel the promoter to account for and surrender such profit.
2. The promoter is not allowed to derive a profit from the sale of his own property to the company unless all material facts are disclosed. If he contracts to sell his own property to the company without making a full disclosure, the company may either rescind the sale or affirm the contract and recover the profit made out of it by the promoter.
3. The promoter must not make an unfair or unreasonable use of his position and must take care to avoid anything which has the appearance of undue influence or fraud.

Promoter's Remuneration

A promoter has no right to get compensation from the company for his services in promoting it unless the company, after its incorporation, enters into a contract with him for this purpose. If allowed, remuneration may be paid in cash or partly in cash partly in shares and debentures of the company.

Promoter's Liability

If a promoter does not disclose any profit made out of a transaction to which the company is a party, then the company may sue the promoter and recover the undisclosed profit with interest Otherwise, the company may set aside the transaction i.e., it may restore the property to promoter and recover its money.

Besides, Section 62 (1) holds the promoter liable to pay compensation to every person who subscribes for any share or debentures on the faith of the prospectus for any loss or damage sustained by reason of any untrue statement included in it. Section 62 also provides certain grounds on which a promoter can avoid his liability. Similarly Section 63 provides for criminal liability for misstatement in the prospectus and a promoter may also become liable under this section.

Promoter's Contracts

Preliminary contracts are contracts made on behalf of a company yet to be incorporated. Following are some of the effects of such contracts;

1. The company, when it comes into existence, is not bound by any contract made on its behalf before its incorporation. A company has no status prior to its incorporation.
2. The company cannot ratify a pre-incorporation contract and hold the other party liable. Like the company, the other party to the contract is also not bound by such a contract.

3. The agents of a proposed company may sometimes incur personal liability under a contract made on behalf of the company yet to be formed.

II INCORPORATION

This is the second stage of the company formation. It is the registration that brings a company into existence. A company is legally constituted on being duly registered under the Act and after the issue of Certificate of Incorporation by the Registrar of Companies. For the incorporation of a company the promoters take the following preparatory steps:

i) To find out from the Registrar of companies whether the name by which the new company is to be started is available or not. To take approval of the name, an application has to be made in the prescribed form along with requisite fee;
ii) To get a letter of Intent under Industries (Development and Regulation) Act, 1951, if the company's business comes within the purview of the Act.
iii) To get necessary documents i.e. Memorandum and Articles of Association prepared and printed.
iv) to prepare preliminary contracts and a prospectus or statement in lieu of a prospectus.

Registration of a company is obtained by filing an application with the Registrar of Companies of the State in which the registered office of the company is to be situated.

The application should be accompanied by the following documents:

1. Memorandum of association properly stamped, duly signed by the signatories of the memorandum and witnessed.
2. Articles of Association, if necessary.
3. A copy of the agreement, if any, which the company proposes to enter into with any individual for his appointment as managing or whole-time director or manager.
4. A written consent of the directors to act in that capacity, if necessary.
5. A statutory declaration stating that all the legal requirements of the Act prior to incorporation have been complied with.

The Registrar will scrutinize these documents. If the Registrar finds the document to be satisfactory, he registers them and enters the name of the company in the Register of Companies and issues a certificate called the certificate of incorporation (Section 34). The certificate of incorporation is the birth certificate of a company. The company comes into existence from the date mentioned in the certificate of incorporation and the date appearing in it is conclusive, even if wrong. Further, the certificate is 'conclusive evidence that all the requirements of this Act in respect of registration and matters precedent and related thereto have been fulfilled and that the association is a company authorized to be registered and duly registered under this Act.

III CAPITAL SUBSCRIPTION

A private company can start business immediately after the grant of certificate of incorporation but public limited company has to further go through 'capital subscription stage' and 'commencement of business stage'. In the capital subscription stage, the company makes necessary arrangements for raising the capital of the company.

If the capital has to be raised through a public offer of shares, the directors of the public company will first file a copy of the prospectus with the Registrar of Companies. On the scheduled date the prospectus will be issued to the public. Investors are required to forward their applications for shares along with application money to the company's bankers mentioned in the prospectus. The bankers will then forward all applications to the company and the directors will consider the allotment of shares. If the subscribed capital is at least equal to 90 percent of the capital issue, and other requirements of a valid allotment are fulfilled the directors pass a formal resolution of allotment. However, if the company does not receive applications which can cover the minimum subscription within 120 days of the issue of prospectus, no allotment can be made and all money received will be refunded. If a public company having share capital decides to make private placement of shares, then, instead of a 'prospectus' it has to file with the Registrar of Companies a 'statement in lieu of prospectus' at least three days before the directors proceed to pass the first share allotment resolution. The contents of a prospectus and a statement in lieu of a prospectus are almost alike.

IV COMMENCEMENT OF BUSINESS

A private company can commence business immediately after the grant of certificate of incorporation, but a public limited company will have to undergo some more formalities before it can start business. The certificate for commencement of business is issued by Registrar of Companies, subject to the following conditions.

1. Shares payable in cash must have been allotted upto the amount of minimum subscription
2. Every director of the company had paid the company in cash application and allotment money on his shares in the same proportion as others.
3. No money should have become refundable for failure to obtain permission for shares or debentures to be dealt in any recognized stock exchange.
4. A declaration duly verified by one of directors or the secretary that the above requirements have been complied with which is filed with the Registrar.

The certificate to commence business granted by the Registrar is a conclusive evidence of the fact that the company has complied with all legal formalities and it is legally entitled to commence business. It may also be noted that the court has the power to wind up a company, if it fails to commence business within a year of its incorporation [Sec. 433 (3)]

MEMORANDUM OF ASSOCIATION AND ARTICLES OF ASSOCIATION

MEMORANDUM OF ASSOCIATION

The formation of a public company involves preparation and filing of several essential documents. Two of basic documents are :

1. Memorandum of Association
2. Articles of Association

The preparation of Memorandum of Association is the first step in the formation of a company. It is the main document of the company which defines its objects and lays down the fundamental conditions upon which alone the company is allowed to be formed. It is the charter of the company. It governs the relationship of the company with the outside world and defines the scope of its activities. Its purpose is to enable shareholders, creditors and those who deal with the company to know what exactly is its permitted range of activities. It enables these parties to know the purpose, for which their money is going to be used by the company and the nature and extent of risk they are undertaking in making investment. Memorandum of Association enable the parties dealing with the company to know with certainty as whether the contractual relation to which they intend to enter with the company is within the objects of the company.

FORM OF MEMORANDUM (SEC. 14)

Companies Act has given four forms of Memorandum of Association in Schedule I. These are as follows :

Table B Memorandum of a company limited by shares

Table C Memorandum of a company limited by guarantee and not having a share capital

Table D Memorandum of company limited by guarantee and having share capital.

Table E Memorandum of an unlimited company

Every company is required to adopt one of these forms or any other form as near there to as circumstances admit.

PRINTING AND SIGNING OF MEMORANDUM (SEC. 15).

The memorandum of Association of a company shall be (a) printed, (b) divided into paragraphs numbered consecutively, and (c) signed by prescribed number of subscribers (7 or more in the case of public company, two or more in the case of private company respectively). Each subscriber must sign for his/her name, address, description and occupation in the presence of at least one witness who shall attest the signature and shall likewise add his address, description and occupation, if any.

CONTENTS OF MEMORANDUM

1. Name clause

Promoters of the company have to make an application to the registrar of Companies for the availability of name. The company can adopt any name if :

i) There is no other company registered under the same or under an identical name;

ii) The name should not be considered undesirable and prohibited by the Central Government (Sec. 20). A name which misrepresents the public is prohibited by the Government under the Emblems & Names (Prevention of Improper use) Act, 1950 for example, Indian National Flag, name pictorial representation of Mahatma Gandhi and the Prime Minister of India, name and emblems of the U.N.O., and W.H.O., the official seal and Emblems of the Central Government and State Governments.

Where the name of the company closely resembles the name of the company already registered, the Court may direct the change of the name of the company.

iii) Once the name has been approved and the company has been registered, then

a) the name of the company with registered office shall be affixed on outside of the business premises;

b) if the liability of the members is limited the words "Limited" or "Private Limited" as the case may be, shall be added to the name; [Sec 13(1) (1)]:

Omission of the word 'Limited' makes the name incorrect. Where the word "Limited" forms part of a company's name, omission of this word shall make the name incorrect. If the company makes a contract without the use of the word "Limited", the officers of the company who make the contract would be deemed to be personally liable [Atkins & Co v Wardle, (1889) 61 LT 23] The omission to use the word 'Limited' as part of the name of a company must have been deliberate and not merely accidental.

(c) the name and address of the registered office shall be mentioned in all letterheads, business letters, notices and Common Seal of the Company, etc. (Sec.147).

Name of a company is the symbol of its personal existence. The name should be properly and correctly mentioned. The Central Government may allow a company to drop the word "Limited" from its name.

2. Registered Office Clause

Memorandum of Association must state the name of the State in which the registered office of the company is to be situated. It will fix up the domicile of the company. Further, every company must have a registered office either from the day it begins to carry on business or within 30 days of its incorporation, whichever is earlier, to which all communications and notices may be addressed. Registered Office of a company is the place of its residence for the purpose of delivering or addressing any communication, service of any notice or process of court of law and for determining question of jurisdiction of courts in any action against the company. It is also the place for keeping statutory books of the company.

Notice of the situation of the registered office and every change shall be given to the Registrar within 30 days after the date of incorporation of the company or after the date of change. If default is made in complying with these requirements, the company and every officer of the company who is default shall be punishable with fine which may extend to Rs. 50 per during which the default continues.

3. Object Clause

This is the most important clause in the memorandum because it not only shows the object or objects for which the company is formed but also determines the extent of the powers which the company can exercise in order to achieve the object or objects. Stating the objects of the company in the Memorandum of Association is not a mere legal technicality but it is a necessity of great practical importance. It is essential that the public who purchase its shares should know clearly what are the objects for which they are paying.

In the case of companies which were in existence immediately before the commencement of the Companies (Amendment) Act. 1965, the object clause has simply to state the objects of the company. But in the case of a company to be registered after be amendment, the objects clause must state separately.

i) Main Objects: This sub-clause has to state the main objects to be pursued by the company on its incorporation and objects incidental or ancillary to the attainment of main objects.

ii) Other objects: This sub-clause shall state other objects which are not included in the above clause.

Further, in case of a non-trading company, whose objects are not confined to one state, the objects clause must mention specifically the States to whose territories the objects extend. (Sec. 13)

A company, which has a main object together with a number of subsidiary objects, cannot continue to pursue the subsidiary objects after the main object has come to an end.

While drafting the objects clause of a company the following points should be kept in mind.

- ✓ The objects of the company must not be illegal, e.g. to carry on lottery business.
- ✓ The objects of the company must not be against the provisions of the Companies Act such as buying its own shares (Sec. 77), declaring dividend out of capital etc.
- ✓ The objects must not be against public, e.g. to carry on trade with an enemy country.
- ✓ The objects must be stated clearly and definitely. An ambiguous statement like “Company may take up any work which it deems profitable” is meaningless.
- ✓ The objects must be quite elaborate also. Note only the main objects but the subsidiary or incidental objects too should be stated.

The narrower the objects expressed in the memorandum, the less is the subscriber's risk, but the wider such objects the greater is the security of those who transact business with the company.

4. Capital Clause

In case of a company having a share capital unless the company is an unlimited company, Memorandum shall also state the amount of share capital with which the company is to be registered and division thereof into shares of a fixed amount [Sec. 13(4)]. The capital with which the company is registered is called the authorized or nominal share capital. The nominal capital is divided into classes of shares and their values are mentioned in the clause. The amount of nominal or authorized capital of the company would be normally, that which shall be required for the attainment of the main objects of the company.

In case of companies limited by guarantee, the amount promised by each member to be contributed by them in case of the winding up of the company is to be mentioned. No subscriber to the memorandum shall take less than one share. Each subscriber of the Memorandum shall write against his name the number of shares he takes.

5. Liability Clause

In the case of company limited by shares or by guarantee, Memorandum of Association must have a clause to the effect that the liability of the members is limited. It implies that a shareholder cannot be called upon to pay any time amount more then the unpaid portion on the shares held by him. He will no more be liable if once he has paid the full nominal value of the share.

The Memorandum of Association of a company limited by guarantee must further state that each member undertakes to contribute to the assets of the company if wound up, while he is a member or within one year after he ceased to be so, towards the debts and liabilities of the company as well as the costs and expenses of winding up and for the adjustment of the rights of the contributories among themselves not exceeding a specified amount.

Any alteration in the memorandum of association compelling a member to take up more shares, or which increases his liability, would be null and void. (Sec 38). If a company carries on business for more than 6 months while the number of members is less than seven in the case of public company, and less than two in case of a private company, each member aware of this fact, is liable for all the debts contracted by the company after the period of 6 months has elapsed. (Sec. 45).

6. Association or Subscription Clause

In this clause, the subscribers declare that they desire to be formed into a company and agree to take shares stated against their names. No subscriber will take less than one share. The memorandum has to be subscribed to by at least seven persons in the case of a public company and by at least two persons in the case of a private company. The signature of each subscriber must be attested by at least one witness who cannot be any of the subscribers. Each subscriber and his witness shall add his address, description and occupation, if any. This clause generally runs in this form : “we, the several person whose names and addresses are subscribed, are desirous of being formed into a company in pursuance of the number of shares in the capital of the company, set opposite of our respective name”. After registration, no subscriber to the memorandum can withdraw his subscription on any ground.

ALTERATION OF MEMORANDUM OF ASSOCIATION

Alteration of Memorandum of association involves compliance with detailed formalities and prescribed procedure. Alternations to the extent necessary for simple and fair working of the company would be permitted. Alterations should not be prejudicial to the members or creditors of the company and should not have the effect of increasing the liability of the members and the creditors.

Contents of the Memorandum of association can be altered as under:

1. Change of name

A company may change its name by special resolution and with the approval of the Central Government signified in writing . However, no such approval shall be required where the only change in the name of the company is the addition there to or the deletion there from, of the word “Private”, consequent on the conversion of a public company into a private company or of a private company into a public company. (Sec. 21)

Within 30 days passing of the resolution, a copy of the order of the Central Government’s approval shall also be field with the Registrar within 3 months of the order. The Registrar shall enter the new name in the Register of Companies in place of the former name and shall issue a fresh certificate of incorporation with the necessary alterations. The change of name shall be complete and effective only on the issue of such certificate. The Registrar shall also make the necessary alteration in the company’s memorandum of association (Sec. 23)

2. Change of Registered Office

This may involve :

a) Change of registered office from one place to another place in the same city, town or village. In this case, a notices is to be give within 30 days after the date of change to the Registrar who shall record the same.

b) Change of registered office from one town to another town in the same State. In this case, a special resolution is required to be passed at a general meeting of the shareholders and a copy of it is to be filed with the Registrar within 30 days.

   The within 30 days of the removal of the office. A notice has to be given to the Registrar of the new location of the office.

c) Change of Registered Office from one State to another State to another State. Section 17 of the Act deals with the change of place of registered office form one State to another State. According to it, a company may alter the provision of its memorandum so as to change the place of its registered office from one State to another State for certain purposes referred to in Sec 17(1) of the Act.

3. Alteration of the Object Clause

The Company may alter its objects on any of the grounds (I) to (vii) mentioned in Section 17 of the Act. The alteration shall be effective only after it is approved by special resolution of the members in general meeting with the Companies Amendment Act, 1996, for alteration of the objects clause in Memorandum of Associations sanction of Central Government is dispensed with.

LIMITS OF ALTERATION OF THE OBJECT CLAUSE

The limits imposed upon the power of alteration are substantive and procedural.

i) to enable the company to carry on its business more economically or more effectively;

ii) to enable the company to attain its main purpose by new or improved means;

iii) to enlarge or change the local area of the company's operation;

iv) to carry on some business which under existing circumstances may conveniently or advantageously be combined with the business of the company;

iv) to restrict or abandon any of the objects specified in the memorandum

v) to sell or dispose of the whole, or any part of the undertaking of the company;

vi) to amalgamate with any other company or body of persons.

Alterations in the objects is to be confined within the above limits for otherwise alteration in excess of the above limitations shall be void. A company shall file with the registrar a special resolution within one month from the date of such resolution together with a printed copy of the memorandum as altered. Registrar shall register the same and certify the registration. [Sec. 18].

4. Alteration of Capital Clause

The procedure for the alteration of share capital and the power to make such alteration are generally provided in the Articles of Association If the procedure and power are not given in the Articles of Associational, the company must change the articles of association by passing a special resolution. If the alteration is authorized by the Articles, the following changes in share capital may take place :

1. Alteration of share capital [Section 94-95]
2. Reduction of capital [Section 100-105]
3. Reserve share capital or reserve liability [Section 99]
4. Variation of the rights of shareholders [Section 106-107]
5. Reorganization of capital [Section 390-391]

5. Alteration of Liability Clause

Ordinarily the liability clause cannot be altered so as to make the liability of members unlimited. Section 38 states that the liability of the members cannot be increased without their consent. It lays down that a member cannot by changing the memorandum or articles, be made to take more shares or to pay more the shares already taken unless he agrees to do so in writing either before or after the change.

A company, if authorized by its Articles, may alter its memorandum to make the liability of its directors or manager unlimited by passing a special resolution. This rule applies to future appointees only. Such alteration will not effect the existing directors and manager unless they have accorded their consent in writing. [Section 323]. Section 32 provides that a company registered as unlimited may register under this Act as a limited company. The registration of an unlimited company as a limited company under this section shall not affect any debts, liabilities, obligations or contracts incurred or entered into by the company before such registration.

ARTICLES OF ASSOCIATION

Every company is required to file Articles of Association along with the Memorandum of Association with the Registrar at the time of its registration. Companies Act defines 'Articles as Articles of Association of a company as originally framed or as altered from time to time in pursuance of any previous companies Acts.

They also include, so far as they apply to the company, those in the Table A in Schedule I annexed to the Act or corresponding provisions in earlier Acts. Articles of Association are the rules, regulations and bye-laws for governing the internal affairs of the company. They may be described as the internal regulation of the company governing its management and embodying the powers of the directors and officers of the company as well as the powers of the shareholders. They lay down the mode and the manner in which the business of the company is to be conducted.

In framing Articles of Association care must be taken to see that regulations framed do not go beyond the powers of the company itself as contemplated by the Memorandum of Association nor should they be such as would violate any of the requirements of the companies Act, itself. All clauses in the Articles ultra vires the Memorandum or the Act shall be null and void.

Article of Association are to be printed, divided into paragraphs, serially numbered and signed by each subscriber to Memorandum with the address, description and occupation. Each subscriber shall sign in the presence of at least one witness who shall attest the signatures and also mention his own address and occupation.

CONTENTS OF ARTICLES OF ASSOCIATION

Articles generally contain provision relating to the following matters;

(1) The exclusion, whole or in part of Table A;

(2) Share capital different classes of shares of shareholders and variations of these rights

(3) Execution or adoption of preliminary agreements, if any;

(4) Allotment of shares;

(5) lien on shares

(6) calls on shares;

(7) forfeiture of shares;

(8) issue of share certificates;

(9) issue of share warrants;

(10) transfer of shares;

(11) transmission of shares;

(12) alteration of share capital;

(13) borrowing power of the company;

(14) rules regarding meetings;

(15) voting rights of members;

(16) notice to members;

(17) dividends and reserves;

(18) accounts and audit;

(19) arbitration provision, if any;

(20) directors, their appointment and remuneration;

(21) the appointment and reappointment of the managing director, manager and secretary;

(22) fixing limits of the number of directors

(23) payment of interest out of capital;

(24) common seal; and

(25) winding up.

MODEL FORM OF ARTICLES

Different model forms of memorandum of association and Articles of Association of various types of companies are specified in Schedule I to the Act. The schedule is divided into following tables.

- Table A deals with regulations for management of a company limited by shares.
- Table B contains a model form of Memorandum of Association of a company limited by shares.
- Table C gives model forms of Memorandum and Articles of Association of a company limited by guarantee and not having a share capital.

- Table D gives model forms of Memorandum and Articles of Association of a company limited by guarantee and having a share capital. The Articles of such a company contain in addition to the information about the number of members with which the company proposes to be registered, all other provisions of Table A.
- Table E contains the model forms of memorandum and Articles of Association of an unlimited company.

A Public Company may have its own Article of Association. If it does not have its own Articles, it may adopt Table A given in Schedule I to the Act. Adoption and application of Table A (Section 28). There are 3 alternative forms in which a public company may adopt Articles:

1. It may adopt Table A in full
2. It may wholly exclude Table A, and set out its own Articles in full
3. It may frame its own Articles and adopt part of Table A.

In other words, unless the Articles of a public company expressly exclude any or all provisions of Table A shall automatically apply to it.

ALTERATION OF ARTICLES

Section 31 grant power to every company to alter its articles whenever it desires by passing a special resolution and filing a copy of altered Articles with the Registrar. An alteration is not invalid simply because it changes the company's constitution. Alteration of articles is much easier than memorandum as it can be altered by special resolution. However, there are various limitations under the Companies Act to the powers of the shareholders to alter the articles.

In case of conversion of a public company into a private company, alteration in the articles would only be effective after approval of the Central Government [Section 31]. The power are now vested with the Registrar of Companies. Alteration of the articles shall not violate provisions of the Memorandum. It must be made bonafide the benefit of the company. All clauses in the articles ultra vires the Memorandum shall be null and void, and the articles shall be held inoperative. Alteration must not contain anything illegal and shall not constitute fraud on the minority. Alteration in the articles increasing the liability of the members can be done only with the consent of the members. The Court may even restrain an alteration where is likely to cause a damage which cannot be adequately compensated in terms of money.

Similarly, a company cannot by altering articles, justify a breach of contract. Any alteration so made shall be valid as if originally contained in the articles. Where a special resolution has been passed altering the articles or an alteration has been approved by the Central Government where required, a printed copy of the articles so altered shall be filed by the company with the Registrar of Companies within one month of the date of the passing of special resolution.

DISTINCTION BETWEEN ARTICLES OF ASSOCIATION AND MEMORANDUM OF ASSOCIATION

The difference between memorandum of association and articles of association is as under:

Memorandum of Association	Articles of Association
1. It is character of company indicating nature of business & capital. It also defines the company's relationship with outside world	1. They are the regulation for the internal management of the company and are subsidiary to the memorandum.
2. It defines the scope of the activities of the company, the area beyond which the actions of the company cannot go.	2. They are the rules for or carrying out the objects of the company as set out in the Memorandum.
3. It, being the charter of the company, is the supreme document.	3. They are subordinate to the Memorandum.
4. Any act of the company which is ultra vires the Memorandum is wholly void and cannot be ratified even by the whole body of shareholders.	4. Any act of the company which is ultra vires the articles can be confirmed by the shareholders if it is intra vires the memorandum.
5. Every company must have its own Memorandum	5. A company limited by Shares need not have Articles of its own. In such A case, Table A Applies.
6. There are strict restrictions on its alteration. Some of the conditions of incorporation contained in it cannot be altered except with the sanction of the Central Government.	6. They can be altered by a special resolution, to any extent, provided they do not conflict with the Memorandum and the Companies Act.

DOCTRINE OF THE ULTRA-VIRES

Any transaction which is outside the scope of the powers specified in the objects clause of the MA and are not reasonable incidentally or necessary to the attainment of objects is ultra-vires the company and therefore void. No rights and liabilities on the part of the company arise out of such transactions and it is a nullity even if every member agrees to it.

Consequences of an ultra vires transaction :-

1. The company cannot sue any person for enforcement of any of its rights.
2. No person can sue the company for enforcement of its rights.
3. The directors of the company may be held personally liable to outsiders for an ultra vires

However, the doctrine of ultra-vires does not apply in the following cases :-

1. If an act is ultra-vires of powers the directors but intra-vires of company, the company is liable.
2. If an act is ultra-vires the articles of the company but it is intra-vires of the memorandum, the articles can be altered to rectify the error.
3. If an act is within the powers of the company but is irregularly done, consent of the shareholders will validate it.
4. Where there is ultra-vires borrowing by the company or it obtains deliver of the property under an ultra-vires contract, then the third party has no claim against the company on the basis of the loan but he has right to follow his money or property if it exist as it is and obtain an injunction from the Court restraining the company from parting with it provided that he intervenes before is money spent on or the identity of the property is lost.
5. The lender of the money to a company under the ultra-vires contract has a right to make director personally liable.

PROSPECTUS

INTRODUCTION

The promoters of a public company will have to take steps to raise the necessary capital for the company, after having obtained the Certificate of Incorporation. A public company may invite the public to subscribe to its shares or debentures. Prospectuses are to be issued for this purpose. To issue a prospectus is very essential for a public company. If the promoters of the company are confident of raising the required capital privately from their friend or relatives, they need not issue a prospectus. In such a case, a statement in lieu of prospectus must be filed with the Registrar. A private company is not allowed to issue a prospectus since it cannot invite the general public to subscribe to its shares and debentures. It is not required to file a statement in lieu of prospectus.

DEFINITION OF PROSPECTUS

Section 2(36) defines a prospectus an “any document described as issued as a prospectus and includes any notice, circular, advertisement or other document inviting deposits from the public or inviting orders from the public for the subscription or purchase of any share in, or debentures of, a body corporate”. In simple words, a prospectus may be defined as an invitation to the public to subscribe to a company’s shares or debentures.

The word “Prospectus” means a document which invites deposits from the public or invites offers from the public to buy shares or debentures of the company.

A document will be treated as a prospectus only when it invites offers from a public. According to Section 67 the term “public” is defined as, “It includes any section of the public, whether selected as members or debenture holders of the company concerned or as clients of the person issuing the prospectus or in any other manner”. It further provides that no offer of invitation shall be treated as mode to the public if, (i) the same is not calculated to result in the shares or debentures becoming available other than those receiving the offer or invitation; (ii) it appears to be a domestic concern of the person making and receiving the offer or invitation. Where directors make an offer to a few of their friends, relatives or customers by sending them a copy of the prospectus marked “not for publication” it is not considered an offer to the public.

Any document to be called a prospectus must have the following ingredients :

I. There must be an invitation offering to the public;
II. The invitation must be or on behalf of the company or in relation to an intended company;
III. The invitation must be to subscribe or purchase.
IV. The invitation must relate to shares or debentures.

OBJECTS OF PROSPECTUS

The main objects of a prospectus are as follows:

1. To bring to the notice of public that a new company has been formed.
2. To preserve an authentic record of the terms of allotment on which the public have been invited to but its shares or debentures.
3. The secure that the directors of the company accept responsibility of the statement in the prospectus.

REQUIREMENTS REGARDING ISSUE OF PROSPECTUS

The relevant requirements regarding issue of prospectus are given below:

1. Issue after Incorporation

Section 55 of the Act permits the issue of prospectus in relation to an intended company. A prospectus may be issued by or on behalf of the company.

- ✓ by a person interested or engaged in the formation company or
- ✓ through an offer for sale by a person to whom the company has allotted shares.

2. Dating of Prospectus

A prospectus issued by a company shall be dated and that date shall be taken as the date of publication of the prospectus (Section 55). Date of issue of the prospectus may be different from the date of publication.

3. Registration of Prospectus

A copy of every prospectus must be delivered to the Registrar for registration before it is issued to the public. Registration must be made on or before the date of its publication. The copy sent for registration must be signed by every person who is named in the prospectus as a director or proposed director of the company or by his agent authorized in writing. Where the prospectus is issued in more than one language, a copy of it as issued in each language should be delivered to the registrar. This copy must be accompanied with the following documents:

- ✓ If the report of an expert is to be published, his written consent to such publication;
- ✓ a copy of every contract relating to the appointment and remuneration of managerial personnel;
- ✓ a copy of every material contract unless it is entered in the ordinary course of business or two years before the date of the issue of prospectus;
- ✓ a written statement relating to adjustments; if any, made by the auditors or accountants in their reports relating to profits and losses, assets and liabilities or the rates of dividends, etc.; and
- ✓ written consent of auditors, legal advisers, attorney, solicitor, banker or broker of the company to act in that capacity.

A copy of the prospectus along with specific documents must been filed with the Registrar. The prospectus must be issued within ninety days of its registration. A prospectus issued after the said period shall be deemed to be a prospectus, a copy of which has not been delivered to the Registrar for registration. The company and every person who is knowingly a party to the issue of prospectus without registration shall be punishable with fine which may extend to five thousand rupees (Section 60).

4. Expert to be unconnected with the Formation of the Company

A prospectus must not include a statement purporting to be made by an expert such as an engineer, valuer, accountant etc. unless the expert is a person who has never been engaged or interested in the formation or promotion as in the management of the company (Section 57).

A statement of an expert cannot be included in the prospectus without his written consent and this fact should be mentioned in the prospectus. Further, this consent should not be withdrawn before delivery of the prospectus for registration Section (58).

5. Terms of the contract not to be varied

The terms of any contract stated in the prospectus or statement in lieu of prospectus cannot be varied after registration of the prospectus except with the approval of the members in the general meeting (Section 61).

6. Application Forms to be accompanied with the Copy of Prospectus

Every form of application for subscribing the shares or debentures of a company shall not be issued unless it is accompanied by a copy of prospectus except when it is issued in connection with a bona fide invitation to a person to enter into an underwriting agreement with respect to shares or debentures or in relation to shares or debentures which were not offered to the public [(Section 56(3)].

Section 56(5) provides that the prospectus need not contain all the details required by the Act where the offer is made to exiting members or debenture holders of the company or if such shares or debentures are in all respect uniform with shares or debentures already issued and quoted on a recognize stock exchange.

7. Personation for Acquisition etc. of Shares

The provision, consequences of applying for shares in fictitious names to be prominently displayed must be reproduced in every prospectus and every application form issued by the company to any person. A person who makes in a fictitious name to a company for acquiring shares or subscribing any shares or subscribing any shares shall be liable to imprisonment which may extend to five years similarly, a person who induces a company to allot any shares or to register any transfer of shares in a fictitious name is also liable to the same punishment. [Section 68(a)].

8. Contents as per Schedule II

Every prospectus must disclose the matters as required in Schedule II of the Act. It is to be noted that if any condition binding on the applicant for shares or debentures in a company to waive compliance with any requirements of the Act as to disclosure in the prospectus or purporting to affect him with notice of any contract, document or matter not specifically referred to in the prospectus shall be void [Section 56(2)]. If a prospectus is issued without a copy thereof, the necessary documents or the consent of the experts the company and every person, who is knowingly a part to the issue of the prospectus, shall be punishable with fine which may extend to Rs. 5,000/-.

CONTENTS OF PROSPECTUS

We know that a prospectus is issued to the public to purchase the shares or debentures of the company. Every person wants to invest his money in some sound undertaking. The soundness of a company can be known from the prospectus of a company. Thus, the prospectus must disclose the true nature of company's activities which enable the public to decide whether or not to invest money in the company. In fact, the public invest money in the company on the faith of the representation contained in the prospectus. Therefore, everything should be stated with strict accuracy, and the complete and true position of the company should be disclosed to the public.

Section 56 lays down that every prospectus issued

(a) by or on behalf of a company, or

(b) by on behalf of any person engaged or interested in the formation of a company, shall :

1. State the matters specified in Part I of Schedule II, and.

2. Set out the reports specified in Part II or Schedule II both Part I and II shall have effect subject to the provisions contained in Part III of that Schedule II.

Part I of Schedule II

1. The main objects of the company with names, descriptions, occupations and addresses of the signatories to the Memorandum of association, and number of shares subscriber by them.
2. The number and classes of shares, and the nature and extent of the interests of the shareholders in the property and profits of the company.
3. The number of redeemable preference shares intended to be issued with particulars as regards their redemption.
4. The number of shares fixed by the articles of company as the qualification of a director.
5. The names, addresses, description and occupation of directors, managing director or manager or any of those proposed person.
6. Any provisions in the articles or any contract relating to appointment, remuneration and compensation for loss of office of directors, managing director or manager.
7. The amount of minimum subscription.
8. The time of the opening of the subscription list cannot be earlier than the beginning of the fifth day after the publication of prospectus.
9. Amount payable on application and allotment on each share shall be stated. If any allotment was previously made within two preceding years, the details of the shares allotted and the amount; if any, paid thereon.
10. Particulars about any option or preferential right to be given to any person to subscribe for shares or debentures of the company.
11. The number, description and amount of shares and debentures which, within the last two years, have been issued or agreed to be issued as fully or partly paid up than in cash.
12. The amount paid or payable as a premium, if any, on such share issued within two years preceding the date of the prospectus or is to be issued stating the necessary particulars.
13. The names of the underwriters of shares or debentures, if any, and the opinion of the directors that the resources of the underwriters are sufficient to discharge their obligations.
14. The names or addresses description and occupations of the vendors from whom the property has been purchased or is to be purchased, and the amount paid or payable in cash, shares or debentures respectively.

15. The amount of underwriting commission paid within two preceding years or payable to any person for subscribing or procuring subscription for any shares or debentures of the company.
16. Any benefit given to any promoter or officer in preceding two years and the consideration for giving of the benefit.
17. Particulars as to the date, parties and general nature of every contract appointing or fixing the remuneration of managing director or manager, whenever entered into.
18. Particulars of every material contract not entered into in the ordinary course of business carried on or intended to be carried on by the company or a contract entered into more than two years before the date of the prospectus.
19. Names and addresses of the auditors of the company.
20. Full particulars of the nature and extent of interested of the directors or promoter in the promotion of the company or in the property acquired by the company within two years of the issue of the prospectus.
21. If the share capital of the company is divided into different classes of shares, the rights of voting at meeting of the company and the rights in respect of capital and the dividends attached to several classes of shares respectively.
22. Where the articles of the company impose any restriction upon the members of the company in respect of the rights to attend, speak or vote at meetings of the company or the rights to transfer shares or on the directors of the company in respect of their powers of management, the nature and extent of these restrictions.
23. Where the company carries on business, the length of time during which it has been carried on. If the company proposes to acquire a business which has been carried on for less than three years, the length of time during which the business had been conducted.
24. If any reserves or profits of the company or any of its subsidiaries have been capitalized, particulars of the capitalization and particulars of the surplus arising from any revaluation on the assets of the company.
25. A reasonable time and place at which copies of all balance sheets and profits and loss accounts, if any, on which the report of the auditors under part II below is based, may be inspected.

Part II of Schedule II

I. General Information

1. Names and address of the Company Secretary, Legal Adviser, Lead Managers, Co-managers, Auditors, Bankers to the company. Bankers to the issue and Brokers to the issue.
2. Consent of Directors, Auditors, Solicitors/Advocates, Managers to issue, Registrar of Issue, Bankers to the company, Bankers to the issue and Experts.

3. Expert's opinion obtained, if any.
4. Change, if any, in directors and auditors during the last 3 years, and reasons thereof.
5. Authority for the issue and details of resolution passed for the issue.
6. Procedure and time schedule for allotment and issue of certificates.

II. Financial Information

1. Report by the Auditors

A report by the auditors of the company as regards

(a) its profits and losses and assets and liabilities of the company and

(b) the rates of dividend, if paid by the company during the preceding 5 financial years.

If no accounts have been made up in respect of any part of the period of 5 years ending on a date 3 months before the issue of the prospectus, the report shall, in addition, deal with either the combined profits and losses and assets and liabilities of its subsidiaries or each of the subsidiary, so far as they concern the members of the company.

2. Reports by the Accountants

(a) A report by the accountants on the profits or losses of the business for the preceding 5 financial years, and on the assets and liabilities of the business on a date which shall not be more than 120 days before the date of the issue of the prospectus. This report is required to be given, if the proceeds of the issue of the shares or debentures are to be applied directly on the purchase of any business.

(b) A similar report on the account of a body corporate by an accountant if the proceeds of the issue are to be applied in the purchase of shares of a body corporate so that body corporate becomes a subsidiary of the acquiring company.

(c) Principal terms of loans and assets charged as security.

3. Statutory and other Information

Statutory and other information minimum subscription, underwriting commission and brokerage; date of allotment, closing date, date of refund, option to subscribe, material contracts and inspection of documents, etc. are required to set out in the prospectus.

Part III of Schedule II

Part III of the schedule consists of provisions applying to Part I and II of the said schedule.

A. Every person shall, for the purpose of this schedule, be deemed to be a vendor who has entered into any contract, absolute or conditional, for the sale or purchase of any property to be acquired by the company, in any case where

(a) the purchase money is not fully paid at the date of the issue of the prospectus

(b) the purchase money is to be paid or satisfied, wholly or in part, out of the proceeds of the issue offered for subscription by the prospectus;

(c) the contract depends for its validity or fulfillment on the result of that issue.

B. In the case of a company which has been carrying on business for less than 5 financial years, reference to 5 financial years means reference to that number of financial years for which business has been carried on.

C. Reasonable time and place at which copies of all balance sheets and profit and loss accounts on which the report of the auditors is based, and material contracts and other documents may be respected. “Term year” wherever used herein earlier means financial year.

DECLARATION

That all the relevant provision of the Companies Act, 1956 and the guide lines issued by the Government have been complied with and no statement made in the prospectus is contrary to the provisions of the Companies Act, 1956 and rules there under. The prospectus shall be dated and signed by the directors.

STATEMENT BY EXPERTS

1. Experts to be unconnected with formation or management of company (Section 57). Where a prospectus includes a statement made by an expert, he shall not be engaged or interested in the formation, promotion or management of the company. The expression ‘expert’ includes an engineer, accountant, a valor and, any other person whose profession gives authority to a statement made by him.
2. Expert’s consent to issue of prospectus containing statement by him (Section 58). A prospectus including a statement made by an expert shall not be issued, unless
   (a) he has given his written consent to be issued of the prospectus with the statement included in the form and context in which it is included and;
   (b) Statement that he has given and has not withdrawn his consent as aforesaid appears in a prospectus. A wholesome rule intended to protect intending investors by making the expert a party to the issue of the prospectus and making him liable for untrue statements (Section 58). Penalty [Section 59 (1)], if any, prospectus is issued in contravention of Section 57 or 58, the company, and every person who is knowingly a party to the issue thereof, shall be punishable with fine which may extent to Rs. 5,000/-

MIS-STATEMENT IN THE PROSPECTUS

A prospectus is an invitation to the public to subscribe to the shares or debentures of a company. Every person authorizing the issue of prospectus has a primary responsibility to seed that the prospectus contains the true state of affairs of the company and does not give any fraudulent picture to the public. People invest in the company on the basis of the information published in the prospectus. They have to be safeguarded against all wrongs or false statements in prospectus. Prospectus must give a full, accurate and a fair picture of material facts without concealing or omitting any relevant fact. This is known as the ‘Golden Rule’ for framing prospectus.

The statements which do not qualify to the particulars mentioned in the prospectus or any information is intentionally and willfully concealed by the directors of the company, would be considered as mis-statement. Thus, the term 'venture statement' as 'mis-statement' is used in a broader sense. It includes not only false statements which produce a impression of actual facts. Concealment of a material fact also comes within the category of misstatement. A statement included in a prospectus shall be deemed to be untrue, if

• The statement is misleading in the form and context in which it is included; and

• the omission from a prospectus of any matter is calculated to mislead (Section 65).

If there is any misstatement of a material fact in a prospectus as if the prospectus is wanting in any material fact, this may arise-

1. Civil Liability

2. Criminal Liability

1. Civil Liability

A person who has induced to subscribe for shares (or debentures) on the faith of a misleading prospects has remedies against the company, directors, promoters, and experts. Every person who is a director and promoter of the company, and who has authorized the issue of the prospectus [Section (2)].

a) Compensation The above persons shall be liable to pay compensation to every person who subscribes for any shares or debentures for any loss or damage sustained by him by reason of any untrue statement included therein [Section 62(1)].

b) Recession of the Contract for Misrepresentation Avoiding the contract is recession. Any person can apply to the court for recession of the contract if the statements on which he has taken the shares are false or caused by misrepresentation whether innocent or fraudulent.

The contract can be rescinded if the following conditions are satisfied:

1) The statement must b a material misrepresentation of fact
2) It must have induced the shareholder to take the shares.
3) The deceived shareholder is an allottee and he must have relied on the statement in the prospectus.
4) The omission of material fact must be misleading before recession is granted.
5) The proceedings for recession must be started as soon as the allottee comes to know of a misleading statement.

c) Damages for Deceit as Fraud Any person induced to invest in the company by fraudulent statement in a prospectus can sue the company and person responsible for damages. The share should be first surrendered to company before the company is used for damages. Fraud occurs when any statement is made without belief in the truth or carelessly. A statement made with knowledge that it is false, will constitute fraud or deceit.

d) Liability for non-compliance A director or other person responsible shall be liable for damage for noncompliance with or contravention of any of the matters to be stated and reports to be set out in the prospectus as provided [by Section 56(41)].

e) Damages for Fraud under General Law Any person responsible for the issue of prospectus may be held liable under the general law or under the Act for misstatements or fraud.

f) Penalty for Contravening Section 57 & 58 If any prospectus is issued is contravention of Section 57, (experts to be unconnected with formation or management of company), or Section 58 (expert's consent to issue of prospectus containing statement by him) the company and every person who is knowingly party to the issue thereof, shall be punishable with fine which may extend to Rs. 5,000/-.

g) Penalty for issuing the Prospectus without Registration If a prospectus is issued without a copy of thereof being delivered to the Registrar, the company and every person who is knowingly a party to the issue of the prospectus shall be punishable with fine which may extent to Rs 5,000 [Section 60(5)].

DEFENCE AGAINST CIVIL LIABILITY

Every person made liable to pay compensation for any loss or damages may escape such liability by proving that :

I. Having consented to become a director of the company, he withdrew his consent before the issue of the prospectus and that it was issued without his authority or consent.

II. The prospectus was issued without his knowledge or consent and that on becoming aware of its issue he forth with gave reasonable public notice that it was issued without his knowledge or consent.

III. After the issue of prospectus, and before allotment there under he, on becoming aware of any untrue statement therein withdrew his consent to the prospectus and gave reasonable public notice of the withdrawal.

IV. If a director, etc., has reasonable ground to believe that the statement was true and he, in fact, believed it to be true up to the time of allotment, he is not liable. But it is not enough for a director to say that he was honest, he has to show that his honest belief was based on reasonable grounds.

V. If statement is a correct and fair representation or extract or copy of the statement made by an expert who is competent to make it and had given his consent and had not withdrawn it, the director, etc., is not liable. Likewise, if the statement is a correct and fair representation or extract or copy of an official document or is based on the authority of an official person, no liability attaches to the director etc.

2. Criminal Liability

Every person who authorized the issue of prospectus shall be punishable for untrue statement with imprisonment for a term which may extend to 2 years or with fine which may extend to Rs. 5,000/- or with both [Section 63(1)].

Penalty for Fraudulently inducing Persons to Invest Money [Section 68]

Any person who either knowingly or recklessly makes any statement, promises or forecast which is false, deceptive or misleading or by any dishonest concealment of material facts, induces or attempts to induce another person to enter into;

- Any agreement with a view to acquiring, disposing of, subscribing for, or underwriting shares or debentures;
- An agreement to secure to any of the parties from the yield of shares or debentures; or by reference to fluctuation in the value of shares or debentures; shall be punishable for a term which may extend to 5 years of with fine which may extend to Rs. 10,000/- or with both.

Defence against Criminal Liability

Any person made criminally liable can escape the same as proving that

- The statement was true [Section 63(i)]. Statement was immaterial; or
- He had a reasonable ground to believe and did upto the time of the issue of prospectus that the statement was true [Section 63(i)].

STATEMENT IN LIEU OF PROSPECTUS (SECTION 70)

A company having a share capital which does not issue a prospectus or which has issued a prospectus but has not proceeded to allot any of the shares offered to the public for subscription, shall not allot any of its shares or debentures, unless at least three days before the allotment of shares or debentures, this has been delivered to the Registrar for registration a 'statement in lieu of prospectus' signed by every person who is named therein as a director or a proposed director of the company or by his agent authorized in writing, in the form and containing the particulars set out in Part I of Schedule III and setting out the reports specified in Part II of Schedule III subject to the provisions contained in Part III of that Schedule (Section 70).

A private company on becoming a public company shall deliver to the Registrar a statement in lieu of prospectus in the form containing the particulars specified in Part I of Schedule IV with report set out in Part II of Schedule IV subject to the provisions contained in Part III of that Schedule [Section 44(2)(b)]. If the company acts in contravention of the provisions, the company and every director who is at fault shall be punishable with fine which may extent to Rs. 1,000/-. If the 'statement in lieu of prospectus' include any untrue statement, any person who authorized the delivery of the statement in lieu of prospectus shall be, punishable with imprisonment up to two years or with fine which may extent to Rs. 5,000/- or with both. He can avoid liability if he proves either that the statement was immaterial or that he had reasonable ground to believe that the statement was immaterial or that he had reasonable ground to believe that the statement was true. The civil and criminal liability for mis-statements or misrepresentations is the same as in the case of a prospectus [Section 70(5)].

MINIMUM SUBSCRIPTION (SECTION 69)

When shares are offered to the public the amount of minimum subscription has to be mentioned in the prospectus. It means the amount which, in the opinion of the directors, is enough to meet the purchase price of any property, preliminary expenses and working capital. No allotment shall be made until atleast so much amount has been subscribed for. If the minimum subscription has not been received within 120 days, of the issue of the prospectus, the money received from the applicants must be repaid without interest. If the money is not paid back within 130 days, the directors become personally liable to pay it with interest, unless they can show that default was not due to any negligence or misconduct or their part.

COMMENCEMENT OF BUSINESS

A private company can commence business immediately on its incorporation. A public company has to, however, comply with certain additional formalities before it can commence its business. This can be grouped under the following three heads.

1. Public Company Issuing a Prospectus

No public company having a share capital and issuing a prospectus inviting the public to subscribe for its shares, shall commence business or borrow unless it has obtained ‘certificate of commencement of business’ from the Registrar of Companies. The certificate of commencement of business will be issued after the following formalities are complied with -

a) At least minimum subscription has been raised;

b) every director of the company has paid to the company, on each of the shares taken by him or agree to be taken by him the amount payable by him on application and allotment of the shares;

c) Obtain or apply for permission for dealing of the shares or debentures on the recognized stock exchange so that no money is repayable to application for an shares of debentures offered for public subscription by reason of any failure to apply for, or to obtain stock exchange permission;

d) A duly verified declaration has been filed with the Registrar by one of the director or the secretary or of the secretary in whole time practice that the above provisions have been complied with [Section 149(1)].

2. Public Company Not Issuing a Prospectus

Where a company having a share capital has not issued a prospectus inviting the public subscribe for its shares, it can commence business or exercise any borrowing powers if the following conditions are fulfilled:

- A statement in lieu of prospectus has been filled in the Registrar.
- Every director of the company has paid to the company, on each of the shares taken or contracted to be taken by him for cash, the application and allotment money.
- There has been filed with the Registrar a duly verified declaration by one of the directors or the secretary, a secretary in whole time practice, in the prescribed form, that the above provisions have been complied with.

When the company fulfils the above conditions, the Registrar shall certify that it is entitled to commerce business and that the certificate shall be conclusive evidence that the company is so entitled [Section 149(3)]. Any contract made by a public company after incorporation but before the date on which it is entitled to commence business shall be provisional only and shall not be binding on the company until the certificates is obtained [Section 149(4)]. Thus where goods are supplied to the company which never become entitled to commence business not one can sue the company for the price of goods supplied to it.

3. Failure to Commence business

It may also be noted that the court has the power to wind up a company, if it does not commence its business within a year of its incorporation [Section 433(3)].

MODULE III
SHARE CAPITAL AND SHARES

SHARE CAPITAL

The term 'share capital' refers to the amount of capital raised (or to be raised) by a company through the issue of shares. It generally means the money subscribed pursuit to memorandum of association of the company.

FEATURES OF SHARE CAPITAL

The main features of share capitals are

1. Share capital can be raised only by companies limited by shares and registered with share capital
2. Share capital can be raised by a company either at the time of its formation for starting its operations or later on for further expansion.
3. Share capitals (except in the case of redeemable preference share), one raised, cannot be returned by the company to the shareholders as long as it continues to exist, It can be returned only at time of the winding up of the company.

CLASSES TYPES OR KINDS OF SHARE CAPITAL:

The various kinds or sub-divisions of share capital are:

1. Authorised Capital, Registered Capital or Nominal Capital:

Authorised capital is the sum stated in the capital clause of the memorandum of association as the capital of a company. It is the maximum amount of share capital, which the company is authorized by its memorandum of association to raise through the issue of shares. It is called authorized capital, because it is the capital, which a company is authorized to raise from the public. It is called registered capital, because it is the capital with which a company is registered. It is also called nominal capital, because it is not the real or actual capital of a company. A company has this capital only in name. Further, it is the total nominal value of the shares, which a company can Issue.

2. Issued Capital:

A company, usually, does not need the whole of the authorized capital in the beginning. It needs only a part of the authorized capital. So, in the beginning, it, usually, issues only a part of the authorized capital to the public for subscription. That part of the authorized capital to the public for subscription. The part of the authorized capital which is issued or offered, for the time being, to the public for subscription is, usually, called the issued capital.

3. **Subscribed Capital:**

   There is no guarantee that the entire capital issued by a company to the public for subscription will be subscribed or taken up by the public. The public may subscribe in full or in part. That part of the issued capital, which is subscribed or taken up by the public, is called subscribed capital.

4. **Called-up Capital:**

   Generally, a company does not need the entire face value of the shares subscribed by the public immediately. So, it calls or demands only a part of the nominal value of the shares subscribed or taken up by the public immediately and collects the balance later, as and when necessary, by making further calls. That part of the subscribed capital, which has been called up or demanded by the company is called called-up capital.

5. **Paid -up Capital:**

   There is no guarantee that all the subscribers pay the full amount called up or demanded from them. In fact, in many cases, some of the subscribers do no pay the full amount called up from them. That means, often, only a part of the called-up capital may be paid by the subscribers or shareholders. That part of the called-up capital, which has been actually paid, by the subscribers or shareholders is called paid-up capital.

SHARES

A share is the interest of a shareholder in the company, measured by a sum of money for the purpose of liability in the first place, and of interest in the second, but also consisting of other rights given by the articles. A share can be defined as, "a share is a fractional part of the capital of a company which forms the basis of certain rights of a member of the company as well as his liabilities vis-à-vis (i.e., as against) the company"

According to Section 2(46) of the Companies Act 1956, “ A share is a share in the share capital of a company and includes stocks except where a distinction between stock and share is expressed or implied “

FEATURES OF SHARES:

The main features of shares are.

i. A share is not a sum of money. It is only an interest or right, measured in .a sum of money, to participate in the profits of the company during its life and in the assets of the company when it is wound up.

ii. A share is given a face or nominal value, and is paid for in money or money's worth.

iii. The person who holds the share or shares of a company is called a shareholder or member of the company.

iv. The title of a member to a sharp is evidenced by the share certificate issued by the company under its Common seal.

v. Each share in a company having share capital is distinguished by its specific or appropriate number.

KINDS OR TYPES OF SHARES

A company issue different types of shares in order to satisfy the requirements of different classes of investors and to collect more capital. A public company can issue only two types of shares, viz., (1) Preference Shares. (2) Equity Shares.

1. PREFERENCE SHARES.

Meaning of Preference shares:

Preference shares are shares, which have preferential rights (i.e., first priority or preference over other kinds of shares) in respect of payment of dividend during the existence of the company, and also in respect of repayment or refund of share capital in the event of the winding up of the company. In fact, it is because of their preferential rights in respect of the payment of dividend and repayment of capital that these shares are 1 mown as preference shares.

Types of Preference Shares:

1. **Cumulative Preference Shares:** The holders of cumulative preference share are entitled to receive a fixed percentage of dividend before anything is given, tot other classes of shareholders. Apart from this right, in the case of these shares, if the company has no profits or inadequate profits in any year to declare dividend, the arrears of dividend would accumulate and become payable out of the future profits before anything is given to other classes of shareholders.
2. **Non-Cumulative Preference Shares:** Non-Cumulative preference shares are entitled to a fixed rate of dividend in the first instance (i,e., before anything is given to other types of shareholders). But they are entitled to receive the fixed percentage of dividend in the first instance only for the year or years when the company earns sufficient profits and dividend is declared. In case the company has no or inadequate profits in any year to declare dividend, then, the arrears of dividend do not accumulate and become payable out of future profits in the case of these shares.
3. **Participating Preference Share:** The holders of these shares, in addition to a fixed percentage of dividend, are also entitled to participate in the surplus profits of the company along with the equity shareholders. Only if there is a specific or special provision in the articles of association of the company giving the holders of these shares special rights to participate in the surplus profits. They are also entitled to participate in surplus assets of the company on its winding up.
4. **Non-Participating Preference Share:** The holders of non-participating preference shares will get only a fixed rate of dividend, of course, in the first instance (i.e., before any dividend is paid to equity shareholders). But they are not entitled to participate in the surplus profits of the company.

5. **<u>Convertible Preference Shares:</u>** The holders of convertible preference shares are given the rights to convert their shares into equity shares later on (i.e., after a certain period).
6. **<u>Non-Convertible Preference Share:</u>** The holders of non-convertible preference share are not given the right to convert their shares into equity shares later on.
7. **<u>Redeemable Preference Shares:</u>** Redeemable preference shares are those preference shares, which can be redeemed (i.e., returned or paid back) even during the existence of the company. These shares can be redeemed as per the terms of issue either at a definite date after the expiry of a stipulated (fixed) period or at the option of the company, i.e., whenever the company wants, after giving proper notice.

Redeemable preference shares can, be redeemed by a company. But their redemption is subject to the conditions

a) The articles of association of the company should provide for the issue and redemption of these shares.

b) Only fully paid shares can be redeemed. Partly paid shares cannot be redeemed.

c) They can be redeemed only out of the profits of the company which would be otherwise available for dividend (i.e., out of the divisible profits of the company) or out of the proceeds of fresh issue of shares made for the purpose of redemption.

d) Any premium paid on their redemption must be paid out of the profits of the company or out of the company's share premium account.

8. **<u>Irredeemable Preference Shares:</u>** Irredeemable preference shares are those preference Share, which are not (i.e. refundable) until the company is wound up. By virtue of the Companies Amendment Act 1988 a company shall not issue irredeemable preference shares or preference shares redeemable after the expiry of a period of 20 years from the date of issue.

Merits of Preference shares

i) The payment of dividend to preference shares is not a legal obligation. So the company can postpone the dividend payment and it can enjoy financial flexibility.

ii) Issue of preference shares does not create any charge against the assets of the company.

iii) The promoters of the company can retain control over the company by issuing preference shares, since the preference shareholders have only limited voting rights.

iv) In the case of redeemable preference shares, there is the advantage that the amount can be repaid as soon as the company is in possession of funds flowing out of profits.

v) Preference shares are entitled to a fixed rate of dividend and the company many declare higher rates of dividend for the equity shareholders by trading on equity and enhance market value.

vi) If the assets of the company are not of high value, debenture holders will not accept them as collateral securities. Hence the company prefers to tap market with preference shares.

vii) The public deposit of companies in excess of the maximum limit stipulated by the Reserve Bank can be liquidated by issuing preference shares.

viii) Preference shares are particularly useful for those investors who want higher rate of return with comparatively Lower risk.

ix) Preference shares add to the equity base of the company and they strengthen the financial position of it Additional equity base increases the ability of the company to borrow in future.

x) Preference shares have variety and diversity, unlike equity shares, Companies have thus flexibility in choice.

Demerits of Preference Shares

i) Usually preference shares carry higher rate of dividend than the rate of interest on debentures.

ii) Compared to debt capital, preference share capital is a very expensive source of financing because the dividend paid to preference shareholders is not, unlike debt interest, a tax-deductible expense.

iii) In the case of cumulative preference shares, arrears of dividend accumulate. It is a permanent burden on the profits of the company.

iv) From the investors point of view, preference shares may be disadvantageous because they do not carry voting rights. Their interest may be damaged by a equity shareholders in whose hands the control is vested.

v) Preference shares have to attraction. Not even 1% of total corporate capital is raised in this form.

vi) Instead of combining the benefits of equity and debt, preference share capital, perhaps combines the banes of equity and debt.

2. EQUITY SHARES.

Equity shares are those, which are not preference shares. In other words, these are shares, which do not enjoy any preferential right either in respect of payment of dividend or in respect of the repayment of capital at the time of the winding up of the company. These shares are knows as equity shares, as they are the 'ownership shares' conferring the ownership of the company on the holders of these shares, i.e., the holders of these shares are the real owners of the company.

DIFFERENCES BETWEEN PREFERENCE SHARES AND EQUITY SHARE:

There are many differences between preferences shares and equity shares. The main differences between them are:

1. Generally, the face value of preference shares is relatively higher than that of equity shares.
2. Preference shares have priority over equity shares in the payment of dividend as will in the repayment of capital in the event of the winding up of the company.
3. The rate of dividend on preference shares remains fixed from year to year. But the rate of dividend on equity shares varies from year to year depending upon the amount of profits available for distribution.
4. The rate of dividend on preference shares, in generally, fixed by the articles of association. But the rate of dividend on equity shares is dependent on the discretion of the board of directors.
5. Preference shares cannot participate in the surplus profits and in the surplus assets in the event of the winding up to the company. Even the participating preference shares can participate in the surplus profits and in surplus assets only if there is a specific provision to that effect in the surplus profits and in surplus assets always.
6. Except those preference shares which are issued as non-cumulative, all preference shares are cumulative. That means, preference shares can get the arrears of dividend. But equity shares cannot get the arrears of dividend.
7. As the rate of dividend on preference shares is fixed or stable, the market value of preference shares remains more or less stable. On the other hand, as the rate of dividend on equity shares fluctuate from year to year, the market value of equity shares fluctuates greatly from year to year.
8. Preference shares, i.e., redeemable preference shares, are redeemable during the existence of the company. But equity shares are not redeemable during the life of the company.
9. Preference shares have limited voting rights. They have voting rights only on those matters, which directly affect their interests. On the other hand, equity shares have full voting rights. They can vote on any matter, which may come up before the company.
10. As there is steady dividend like rent, preference shares capital is considered as rentier capital. On the other hand, as there is much risk in equity shares, equity share capital is considered as risk capital.
11. As there is not much risk in preference shares, preference shares appeal to cautious investors who do not want to assume risks. On the other hand, equity shares appeal to adventurous investors who are prepared to assume risks.

12. The holders of preference shares do not have much control over the management of the company. On the other hand, the holders of equity shares have much control over the management of the company.

EMPLOYEES STOCK OPTION SCHEME

Employee Stock Option Plans (ESOPs) & **Employee Stock Purchase Schemes** (ESPSs) are employee benefit plans, which makes the employee of the company owners of stock in that company.

Stock options are the instruments that are offered to employees, allowing them to buy a certain number of shares in the company at a specific price. This price could either be lower than the current market-price of scrip-in which case their gains are immediate-or the same, whereupon future jumps in the share-price will show up as profits for them. There has to be a gap between the announcement of the ESOP and its coming into effect. You also have the freedom to specify how many shares an employee gets, which employees get them, and when the ownership is actually transferred.

ESOPs & ESPSs are unique employee ***benefit plans*** and are fast replacing cash incentives as a method to reward and retain employees.

The spirit of ESOP is that it would give the employees a share in the wealth of the company and infuse a sense of ownership & thence loyalty. This helps retaining talented and skilled employees, especially in today's scenario when the employee turnover and churn is high. It also improve the productivity and performance of the Employees.

Grant of ESOPs is a ***two-way*** mechanism. Employees receive stock from the promoter, as a kind of an incentive. And the incentive is on account of their good work and loyalty towards the company.

Presently ESOPs is in vogue with knowledge driven industries like software, where the major input going into the success of a company are the "intellectual inputs" provided by the skilled labour, and there exists shortage of such skilled labour and high turnover.

Different terms used in an ESOP

Grant date - The date on which the company grants an option to its employee.

Option price - The price at which such shares in a scheme are offered. It is also known as the 'strike price' or 'grant price'. Normally such option price would be below the market value/ fair value of the shares on the date of grant.

Vesting date - An ESOP would provide for a date on which an option is vested with employees and time frame over which the stock option would vest with employees ('Vesting period').

Exercise period - The employees would be given a time period, called exercise period, within which they are required to exercise the option. The date on which employees exercise this option is known as 'exercise date'.

There are two ways in which a company can set up an ESOP.

(a) Create a Trust (Special Purpose Vehicle) - Depending on the number of options to be given to the employees, the company will issue shares or options to the trust. The trust would need funds to buy these shares. For this, the company can either give soft loans from its own funds or the trust can raise loans through other sources to meet its financial requirement. The company can act as a guarantee to the lender to the trust. With the funds so raised, the trust then acquires shares/options required. The trust repays its loans as and when the employees purchase the options offered and when they exercise their options by paying the exercise price.

(b) Give options directly to employees - The selection of the employees can be based on performance of the employee, indicated by the annual performance appraisal, minimum period of service, present and potential contribution of the employees, and such other factors deemed to be relevant for the success of the company. Number of options per employee can be determined taking into consideration, the grade, level, years of service, salary, etc. These selections would entirely depend upon the objective of the company for setting up the ESOP.

The real advantage of ESOPs is that, the exercise price remains fixed over the term of the option. So, the employee would exercise his option when the market price of the shares goes substantially high and he would gain on the difference between the market price and exercise price.

DIFFERENT TYPES OF ESOPs

ESOP can be a one-time plan or an ongoing scheme depending upon the objectives that the company wants to achieve. ESOPs can be in the form of ESOS (Employee Stock Option Schemes), ESPP (Employee Stock Purchase Plans), Compensation Plans, Incentive Plans, SAR/Phantom ESOPs etc.

Employee Stock Option Scheme (ESOS) - Under this scheme, the company grants an option to its employees to acquire shares at a future date at a pre-determined price. Eligible employees are free to acquire shares on vesting within the exercise period. Employees are free to dispose of the shares subject to lock-in-period if any. Generally exercise price is lower than the prevalent market price.

Employee Stock Purchase Plan (ESPP) - This is generally used in listed companies, wherein the employees are given the right to acquire shares of the company immediately, not at a future date as in ESOS, at a price lower than the prevailing market price. Shares issued by listed companies under ESPP will be subject to lock-in-period, as a result, the employee cannot sell the shares and/or the employee has to continue with the employer for a certain number of years.

Share Appreciation Rights (SAR)/ Phantom Shares - Under this scheme, no shares are offered or allotted to the employee. The employee is given the appreciation in the value of shares between two specified dates as an incentive or performance bonus, that is linked to the performance of the company as a whole, as reflected in its share value.

Issue of stock options requires approval of shareholders by way of a special resolution as per section 81(1 a). This is not applicable for private companies who can issue stock options without shareholder approval but approval by the board of directors.

BOOK BUILDING

SEBI guidelines treat book building as an alternative method of pricing that portion of the issue, which is reserved for institutional and corporate investors. It is basically a capital issuance process used in Initial Public Offer (IPO) Book building is the process by which a market attempts to discover price and quantity. By price discovery, we are referring to how a share value might be found that best reacts a broad market's desire to hold shares of a stock. By quantity discovery. (a relatively unrecognized function of a marketplace), we are referring to how orders on both sides of the market may be revealed and turned into trades Both price and quantity discovery can start with a pre-opening, order accumulation procedure that culminates with a call auction, and then continues through the early stages of the continuous market Price discovery is a complex process in an environment characterized by either asymmetric information and/or investor expectations that are divergent. Quantity discovery, on the other hand, is a complex process that operates in an environment where investors come to the market to buy and sell shares because their security valuations differ (i.e., they have divergent expectations) but where participants do not fully reveal their trading desires because they fear their trades will be executed at inferior prices due to adverse market impact (including that attributable to front running) and/or poor market timing. Thus, the complexity of quantity discovery is an inherent and critical component of the book building problem.

As per the SEBI guidelines "Book Building is a process undertaken by which a demand for the securities proposed to be issued by a body corporate is elicited and built up and the price for such securities is assessed for the determination of the quantum of such securities to be issued by means of a notice, circular, advertisement, document or information memoranda or offer document "

The book building is done through the following processes

1. The company, which wants to issue shares, approached a merchant banker and informs him the number of shares the company wishes to issue and other material information related with it.
2. The merchant banker invites his known institutional investors to bid for the company's share. The intentional investors are asked to disclose the total number of shares they will buy at different prices. After finalizing price, securities are allocated to the highest bid price.
3. The company has the choice to cancel the issue if the bid price is too low.
4. The trading starts on the next day itself

ALLOTMENT OF SHARES

In response to public offer, by providing all details of the company in the prospectus, the company receives the applications for shares along with application money either at the registered office of the company or by the banker. Application legally, is an offer by a prospective shareholder to a company to take shares. Allotment is the acceptance of the offer by the company. Allotment is a binding contract between the company and the prospective shareholders.

The rules and regulations with regard to the allotment are as follows

1. General principles regarding allotment
2. Statutory restrictions on allotment.

1. General principles regarding allotment

With regard to the allotment of shares the following general principles should be observed in addition to the provisions of the Companies Act.

1. Alloted by Proper authority

Allotment should be made by proper authority, Ie, the board of Directors of the company or a committee authorized to allot shares on behalf of the Board. An allotment made without proper authority will be invalid.

2.Allotment against application only

No valid allotment can be made on an oral request. Section 41 provides that for becoming a member, a person should agree in writing. Thus no allotment can be made without a written application for allotment.

3. Reasonable time

Allotment must be made within a reasonable period of time, otherwise, the application lapses. Reasonable time is a question of facts depending on circumstances of the case. With regard to reasonable time section 6 of the Contract Act becomes applicable.

4. Communication

As per the Contract Act, for a legal offer and acceptance communication is essential. The allotment is an acceptance and be communicated to the applicant.

5. Absolute and unconditional

The allotment must be absolute and unconditional, that means it must be made on the same terms as stated in the application. The legal rules regarding offer and acceptance is applicable in allotment also.

II. Statutory restrictions on allotment of shares

So far as the private companies are concerned, the Act does not lay down any restrictions as to the allotment of shares. But the Act has laid down certain restrictions regarding the allotment of shares by public companies.

When no public offer is made: Where a public company does not offer its shares to the public but arranges the capital privately, the company cannot proceed with the allotment unless it files with the Registrar of Companies at least three days before the first allotment, a statement in lieu of prospectus. If the allotment is made in contravention to this provision, it will be termed as 'irregular allotment' and it shall be voidable at the option of the allottee. In addition to this, every officer of the company, who is a party to such allotment shall be punishable with fine which may extent to Rs. 1,000.

When an Offer is made to the Public: Where a company offers to shares to the public:

i) a **prospectus** must be issued and a copy of the same should be filed with the Registrar. The company cannot allot the shares immediately after issuing the prospectus. No allotment can be made until the beginning of the fifth day from the date of issue of prospectus. The fifth day is to be counted from the date of issue of prospectus was published or was otherwise notified to the public. The beginning of the fifth day is known as **'the time of the opening of the subscription lists'**. The object of this provision is to enable the public to go through the prospectus and to decide whether to apply for the shares. The Companies Act, however, does not specifically provide for the time of closing the subscription list. It means that the company may keep the subscription list open for any length of time it wants. According to stock exchange regulations where the shares are listed on any stock exchange, the subscription list must be kept open for at least three days, In such cases, the prospectus usually mentions the time of closing of the subscription lists.

ii) Minimum subscription: No company can proceed to allot shares to the public until the minimum subscription (which is usually 90% of the issue amount) has been subscribed, and the sum payable on applications for it has been received by the company in cash. **If the company does not receive the minimum subscription of 90% of the issue amount, the entire subscription will be refunded to the applicants within 90 days from the date of closure of the issue**. If there is a delay in refund of such amount by more than ten days, the company is liable to pay interest at the rate of 15% per annum for the delayed period.

iii) Application money: It is the amount which is payable on each share alongwith the application for purchase of shares. The amount payable on application on each **-** share shall not be less than **5** per cent of the nominal amount of the share.

iv) Application money to be deposited in a scheduled bank: All the money received from applicants must be deposited in a scheduled bank and it shall remain there until the certificate to commence business is received.

v) Allotment of shares to dealt in on stock exchange. According to Section 73(1) of the Companies Act, every company intending to offer shares to the public for subscription by the issue of a prospectus shall, before such issue, make an. application to one or more recognized stock exchanges for permission for the shares to be dealt with in the stock exchange. Thus, now it is made compulsory that the shares must be listed on a recognized exchange. The prospectus must state the name of the stock exchange or each of such exchanges where the application has been 'made. If the permission has not been granted before the expiry of ten weeks from the date of closing of the subscription lists, the company must immediately pay the money received from the applicants**.** If it is not repaid within eight days the directors shall be liable *to* repay it with interest at such rate**,** which should not be less than four per cent and more than fifteen per cent per annum. However a director may escape liability if he can prove that there was no negligence or misconduct on his part.

IRREGULAR ALLOTMENT AND ITS CONSEQUENCES

An allotment of shares shall be termed irregular if it is made without fulfilling the conditions precedent to a regular allotment. The allotment of shares will irregular in the following cases:

1) Where an allotment is made without receiving the minimum subscription.
2) Where an allotment is made without receiving at-least five per cent of the nominal value of shares as application money.
3) Where an allotment is made without depositing the application money in a Scheduled bank.
4) In the case of a company which does not invite public to subscribe its shares, if the allotment is made without filing with the Registrar the 'Statement in lieu of prospectus' at least three days before the first allotment of shares.
5) Where the company fails to apply for listing of its shares in one or more recognized stock exchanges before the tenth day after the first issue of prospectus or where such permission has been applied for before that day but the permission has not been granted by the stock exchange before the expiry of ten weeks from the date of the closing of the subscription list.
6) Where the allotment is made before the expiry of the fifth day after the date of issue of the prospectus.

Consequences of an irregular allotment are as follows:

i) Voidable at the option of the allottee: In the first four cases discussed above the allotment is voidable at the option of the allottee. But this right should be exercised by the allottee within two months after the holding of the statutory meeting by the company or where the company is not required to hold a statutory meeting or where the allotment is made after the holding of the statutory meeting, within two months after the date of allotment. It is not necessary that the allottee must commence legal proceedings within the said period, what is required is that he must give a notice to the company of his intention to avoid the allotment. The option to avoid the allotment can be exercised even after the company has gone into liquidation and is in the course of liquidation.

ii) Fine: Where time limit regarding the opening of the subscription list is not observed, the allotment remains valid but the company and every officer who is in default are liable to a fine upto Rs. 5.000 each.

iii) Allotment is void: In the fifth case discussed above if the application for listing of shares has not been made or such a request for permission of shares to be dealt in the stock exchange has not been granted within the prescribed time, tll allotment shall be void. In this case the money must be returned within eight days**,** failing which the directors are liable to pay it with interest at such rate which shall not be less than 4 percent and not more than 15 per cent as may be prescribed, having regard to the length of the period of delay in making repayment.

iy) Director's liability: The directors of the company who are responsible for irregular allotment, are liable to compensate the company and the allottee for any loss, damages or cost suffered or incurred by them.

ALLOTMENT PROCEDURE

The directors of the company take decision regarding allotment. Allotment is an act of the directors by accepting the offer of an applicant to purchase the shares of the company. The decision is taken after complying with the provisions of the Act by passing a resolution at the board meeting

LETTER OF REGRET

These letters are sent to those applicants to whom shares have not been allotted. Such a letter will contain the regret of the directors for their inability to allot shares. A cheque also will be enclosed with the letter for the refund of the application money.

SPLITTING OF ALLOTMENT

When a large block of shares has been allotted to a single person, the company at his request split or divide the original allotment letter into a number of small allotment letters. This facility is usually enjoyed by speculators of shares who are interested to sell part of their holdings. When an application is received for splitting the allotment, the secretary records it in the split allotment sheet and necessary remarks are made in the application and allotment list.

RENUNCIATION OF ALLOTMENT

To renounce means to give up. An allottee is permitted under the Act to give up the right over shares allotted to him either wholly or partly and transfer allotment made to him to some other person. This is known as renunciation of allotment. The right of renunciation is exercised by an allottee when he is not in a position to retain the shares to himself,. The right of renunciation is approved by the Act unless the Articles of a company expressely provide to the contrary.

Secretary’s duty in connection with the allotment of shares

The duties of a company secretary in connection with share application and allotment are as follows;-

- Before the Board of Directors proceeds to allot shares, the secretary should see that statutory conditions for application, issue and allotment are complied with
- As and when the application for shares and the banker’s list are received form the bankers, the secretary should see that the applications are scrutinized and sorted out carefully.
- He should number the applications serially and enter the details of applications in the application and allotment sheet.

- He should consult the stock exchange and obtain the instruction, if the shares are listed in the stock exchange.
- If the issue is over subscribed, the secretary should see that a sub committee of the directors is appointed to consider and report on the method or the basis to be adapted for the allotment of shares.
- He should arrange for the dispatch of allotment letters and letters of regret to the parties concerned as per the instructions of the Board.
- He should make arrangements with the company's bank for renouncing the allotment money.
- He should make necessary arrangements in splitting the allotment and renouncing the allotment.
- He should make the necessary entries in the register of members and take steps to issue share certificates.
- He should also file a return to allotment with the Registrar of companies within 30 days of the allotment of shares.

UNDERWRITING

Underwriting is an act of guarantee by an organization for the sale of certain minimum amount of shares and debentures issued by a public limited company.

According to the Companies Act, when a person agrees to take up the shares specified in the underwriting agreement, when the public or others have failed to subscribe for them, it is called underwriting agreement. For this purpose, the underwriter who guarantees for the sale of shares is given a commission. When the public to whom the shares of issue fail to subscribe, it is the underwriter who has to subscribe up to the limit he has agreed. Later on, when the market improves he may off load the shares by selling them to the public. Thus, the underwriter makes a promise to get the underwritten issue subscribed, either by him or by others.

UNDERWRITING COMMISSION

The consideration for the work done by the underwriter is known as underwriting commission. Section 76 permits the payment of underwriting commission subject to the compliance of the following conditions:-

1. It should be authorized by the Articles of the company.
2. The commission payable should not exceed 5% in case of share and 21/2 % in the case of debentures.
3. Underwriting commission may be paid in cash or kind
4. Underwriting commission shall be disclosed in the prospectus or statement in lieu of prospectus as the case may be.

5. Details of shares undertaken are also disclosed in the prospectus or statemtn in lieu of prospectus.
6. A copy of contract relating to the payment of the commission should be delivered to the Registrar.

BROKERAGE

Broker is a person connecting a purchaser and a seller. In the process of subscribing shares to the public, company appoints brokers. Brokerage is the reward for the work. It is the reward paid to the middlemen who brings about a bargain between the seller and a purchase of shares or debentures. Brokerage is different from the underwriting commission. Underwriters are laible for the under subscription of shares, but there is no such liability for brokers.

ISSUE OF SHARES OR TERMS OF ISSUE OF SHARES :

ISSUE OF SHARES AT PAR

When shares are issued by a company to the public at a price equal to their face value (i.e., the price written on the face of the share certificates), they are said to be issued at par. For example, if shares of the face value of Rs.10 each are issued by a company to the public at Rs.10 each, the shares are said to be issued at par.

ISSUE OF SHARES AT A PREMIUM (SECTION 78)

When a company finds at there is a great demand for its shares, it may issue shares at a premium. Issue of shares at a premium means the issue of shares by a company at a price higher than the face value of the shares. (The difference between the issue price, i.e., the price at which the shares are issued, and the face value of the shares is called share premium) for example, when shares of the face value of Rs.10 each are issued at a price of Rs.12 per share, the shares are said to be issued at a premium.

The expression premium is not defined in the Act. It means the value of any advantage measurable in terms of money. The Act does not stipulate any condition or restrictions regulating the issue of shares by a company at a premium. However, the Act does impose conditions regarding the utilization of the amount of premium. A sum equal to the aggregate amount or value of the premium shall be transferred to "The securities Premium Account. The Securities Premium Account shall be treated as paid up capital for the purpose of reduction of capital. However, the share premium may be utilized for the following purposes:-

1. To issue fully paid bonus shares to the members
2. To write off preliminary expenses of the company.
3. To write off expenses or commissions paid or discounts allowed on an issue of shares or debentures.
4. To provide for the premium payable on redemption of any redeemable preference shares or debentures.

Even when shares are issued at a premium for consideration other than cash, a sum equal to the amount of the premium must be transferred to the securities premium account.

ISSUE OF SHARES AT A DISCOUNT SECTION (79)

When a company wants to raise further capital at a time when its shares are not demanded, and so, quoted in the market below par, it may issue shares at a discount.

Issue of shares at a discount means the issue of shares at a price less than the face value of the shares. (The differences between the face value and the issue price of the shares are the discount allowed on the shares. The discount allowed is a capital loss to the company.). For instance, when shares of the face value of Rs.10 each are issued at Rs.9 each, the shares are said to be issued at a discount.

Section (79) of the Companies Act lays down that a company may issue shares at a discount, if the following conditions are satisfied.

- ✓ The issue of shares at discount must be of a class of shares already issued.
- ✓ At least one year have lapsed at the date of the issue from the date of commencement of business by the company.
- ✓ The issue is authorized by a resolution (ordinary) in the general meeting which must state the maximum rate of discount.
- ✓ The resolution shall specify the maximum rate of discount which shall not exceed 10%
- ✓ The resolution shall sanctioned by the Central Government. The Central Government may allow a higher percentage in special circumstances.
- ✓ Shares are issued within two months of the date on which the issue is sanctioned by the Central Government or within such extended time as the Central Government may allow
- ✓ The prospectus relating to the issue shall contain particulars of discount allowed on the issue of shares.

Advantages of Equity Share Capital

i) Equity share capita] constitutes the ’corpus’ of the company. It is the ‘heart’ to the business.

ii) It represents permanent capital. Hence, there is no problem of refunding the capita]. It is repayable only in the event of company's winding up and that too only after the claims of preference shareholders have been met in full.

iii) Equity share capital does not involve any fixed obligation for payment of dividend. Payment of dividend to equity shareholders depends on the availability of profit and the discretion of the Board of Directors.

iv) Equity shares do not create any charge on the assets of the company and the assets may be used as security for further financing.

v) Equity capital is the risk-bearing capital, unlike debt capital which is risk-burdening.

vi) Equity share capital strengthens the credit worthiness and borrowing or debt capacity of the company. In general, other things being equal, the larger the equity base, the higher the ability of the company to secure debt capital.

vii) Equity capital market is now expanding and the global capital market can be accessed.

Disadvantages of Equity Shares Capital

i) Cost of issue of equity shares is high as the limited group of risk-seeking investors need to be attracted and targeted. Equity share attract only those classes of investors who can take risk. Conservative and cautious investors do not to subscribe for equity issues, Su underwriting commission, brokerage costs and other issue expense are high for equity capital, raising up issue cost.

ii) The cost of servicing equity capital is generally higher than the companies' issuing preference shares or debenture since on account of higher n the expectation of the equity shareholders is also high as compared preference shares or debentures.

iii) Equity dividend is payable from post-tax earnings. Unlike intent paid on debt capital, dividend is not deductible as an expense from, profit for taxation purposes. Hence cost of equity is high: Sometimes, dividend tax is paid, further rising cost of equity share capital.

iv) The issuing of equity capital causes dilution of control of the equity holders.

v) In times of depression dividends on equity shares reach low which leads to drastic fall in their market values.

vi) Excessive reliance on financing through equity shares reduces the capacity of the company to trade on equity. The excessive use of equity shares is likely to result in over capitalization of the company.

SEBI Guidelines for Public issue

SEBI provides guidelines for public issues. They are:

- ✓ Prospectus has to be attached with every application.
- ✓ A company has to highlight the risk factors, in the prospectus.
- ✓ Objectives of the issue and cost of project should be mentioned in the prospectus.
- ✓ Company’s management, past history and present business of the firm should be highlighted in the prospectus.
- ✓ Justification for premium, in case of premium issue.
- ✓ Subscription list for public issue should be kept open for minimum three days and a maximum of 10 working days.

- ✓ The collection Centers should be at least 30
- ✓ Collection centers are not to collect application money in cash
- ✓ The quantum of issue shall not exceed the amount specified in the prospectus
- ✓ A Compliance request in the prescribed form should be submitted to SEBI within 45 days from the date of closure of issue.
- ✓ Minimum number of shares for which application shall be allowed to be made has been fixed at 200 shares of the face value of Rs.10 each
- ✓ The allotment have to been made in multiple of 100 shares of Rs.10 each.
- ✓ If minimum subscription of 90% has not been received, the entire amount is to be refunded to investors within 120 days
- ✓ The capital issue shall be fully paid within 120 days.
- ✓ The underwriting has been made mandatory
- ✓ The gap between the closure dates of various issues that is, rights and public issue shall not exceed 30 days.

Sweat equity:

- ✓ 1. Issue of sweat equity shares is governed by the provisions of S. 79A of the Companies Act. Explanation II to the said Section defines the expression 'sweat equity shares' to mean equity shares issued by the company to employees or directors at a discount or for consideration other than cash for providing the know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called. It is, therefore, necessary for the issue of sweat equity shares that the concerned employee either provides the know-how, intellectual property rights or other value additions to the company.
- ✓ 2. In terms of the said Section, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are satisfied :
- ✓ (a) such issue is authorised by a special resolution of the company in the general meeting;
- ✓ (b) such resolution specifies the number of shares, current market price, consideration, if any, and the class or classes of the directors or employees to whom such shares are to be issued;
- ✓ (c) such issue is after expiry of one year from the date on which the company was entitled to commence business; and
- ✓ (d) in the case of an unlisted company, such shares are issued in accordance with the prescribed guidelines.
- ✓ 3. The guidelines referred to in S. 79A are the Rules issued by the Central Government, which need to be followed by unlisted companies. The Rules *inter alia* provide the procedure to be followed by a company issuing sweat equity shares for

consideration other than cash. Rule 9 of the Rules provides that where a company proposes to issue sweat equity shares for consideration other than cash, it shall comply with the following :

- ✓ (a) the valuation of the intellectual property or of the know-how provided or other value addition to consideration at which sweat equity capital is issued, shall be carried out by a valuer;
- ✓ (b) the valuer shall consult such experts, as he may deem fit, having regard to the nature of the industry and the nature of the property or the value addition;
- ✓ (c) the valuer shall submit a valuation report to the company giving justification for the valuation;
- ✓ (d) a copy of the valuation report of the valuer must be sent to the shareholders with the notice of the general meeting;
- ✓ (e) the company shall give justification for issue of sweat equity shares for consideration other than cash, which shall form part of the notice sent for the general meeting; and
- ✓ (i) the sweat equity shares are issued to any director or manager;
- ✓ (ii) they are issued for non-cash consideration, which does not take the form of an asset which can be carried to the balance sheet of the company, in accordance with the relevant accounting standards.
- ✓ 4. Rule 8 of the Rules prescribes that the issue of sweat equity shares to employees and directors shall be at a fair price calculated by an independent valuer.

RIGHTS SHARES

If a public company issues additional or further shares at any time after the expiry of two years of its formation or one year of the first allotment of shares, which ever is earlier, such additional shares must be offered to the existing equity shareholders of the company in proportion to the capital paid up on their shares, such shares are called rights shares. Such shares are called rights shares, as the existing equity shareholders are given preferential rights (i.e., first preference) in the allotment of such shares.

The right of existing equity shareholders to be offered new shares before they are offered to the public is called shareholders' right of preemption.

OBJECT OF RIGHT ISSUES:

The object of rights issue is that there should be an equitable distribution of shares among the existing equity shareholders and the proportion of holding of shares by the existing equity shareholders should not be affected by the issue of the additional shares.

BONUS SHARES

Bonus shares are shares issued by a company out of its accumulated reserves or profits to the existing equity share holders either as fully paid shares or partly paid shares free of cost.

DIFFERENCES BETWEEN BONUS SHARES AND RIGHTS SHARES:

1. Bonus shares are issued to the existing members (i.e. free of costs. But rights shares are issued to the existing member for money.
2. Bonus shares can be issued by a company only when it has sufficient. Accumulated reserves or profits. But the issue of rights shares is not at all related to the availability of accumulated reserves or profits.
3. The purpose of bonus issue is to bring the issued capital of the company in line with the true worth of the undertaking so that the net profit of the company may not appear to be excessively high as compared to its paid -up capital. But the purpose of rights issue is to raise additional share capital for the company.
4. For the issue of bonus shares, the permission of the controller of capital issues is necessary; whatever may be the amount of issue of bonus shares. On the other hand, for the issue of right shares, the permission of the controller of capital issues is necessary only when the issue exceeds Rs.1 crore in a period of 12 months.
5. For the issue of bonus shares, sanction of the shareholders is necessary always. But for the issue of rights shares, the sanction of the shareholders is necessary only when the rights issue involves increase in the authorized capital. ,

CALLS ON SHARES

When shares are issued, the terms of issue may specify the installment by which the issue price shall be payable. A member of a company is bound to pay the nominal amount of share which he has purchased. As noted earlier section 69 provides that not less than five percent of the nominal value of share can be called by way of application money and another sum at allotment. The balance may be payable as and when called for. The power to make call is exercised by the Board in the meeting by means of a resolution. The Board, making a call, must observe the provision of the articles, otherwise the call will be invalid and the shareholder is not bound to pay.

Essentials of a Valid call

- In making a call, care must be taken that
    a. The directors making it are duly appointed and duly qualified
    b. The meeting of the Board of Directors has been duly convened
    c. The proper quorum is present
    d. The resolution making the call is duly passed
    e. A proper entry is made in the minutes
- Call on shares of same class must be made on uniform basis
- Call is to be made in the interest of the company

NOTICE OF CALL

A call must be made by serving upon members a notice of payment in accordance with the provision of section 53. It should be a formal notice, not a demand or request for payment. Every share-holder is under a statutory obligation to pay the full amount of his shares.

CALLS IN ADVANCE

Calls–in–Advance: According to sec.92 of the Companies Act, a Company may if so authorized by its articles, accept from a shareholder either the whole or part of the amount remaining unpaid on any shares held by them, as Calls in advance. No dividend is paid on such calls in advance. However, interest has to be paid on such calls in advance

The money paid in advance cannot ordinarily be repaid to the shareholder, except in the event of winding up.

1.9 SURRENDER OF SHARES : A shareholder who is not able to pay the call money may surrender its shares to the company. The company cancels such surrender shares. Surrender is a voluntary act on the part of the shareholder, whereas Forfeiture is a compulsory act on part of the company. The effect of both surrender & Forfeiture is the same, i.e. cancellation of the shares. The company can accept surrender of shares if permitted by its Articles of Association. The accounting treatment in respect of surrender of shares is same as that of Forfeiture of Shares.

FORFEITURE OF SHARES

When shares are allotted to an applicant, it becomes a contract between the shareholder & the company. The shareholder is bound to contribute to the capital and the premium if any of the company to the extent of the shares he has agreed to take. as & when the Directors make the calls. If the fails to pay the calls then his shares may be forfeiture by the directors if authorised by the Articles of Association of the company. The Forfeiture can be only for non-payment of calls on shares and not for any other reasons. When the directors forfeiture the shares the person looses his membership in the company as well as the amount already paid by him towards the share capital and premium. His name is removed from the register of members. The directors must observe strictly all the legal formalities required by the Articles of Association before forfeiting the shares.

PROCEDURE OF FORFEITURE OF SHARES

The authority to forfeit shares is given to the Board of Directors in Articles of Association of the company. The Board of Directors has to give at least fourteen days notice to the defaulting members calling upon them to pay outstanding amount with or without interest as the case may be before the specified date. The notice must also state that if the shareholders fail to remit the amount mentioned therein within the stipulated period, their shares will be forfeited. If they still fail to pay the amount within the specified period of time, the Board of Directors of the company may decide to forfeit such shares by passing a resolution. The decision regarding the forfeiture of shares should be communicated to the concerned allottees and should be asked to return the allotment letters and share certificates of the forfeited shares to the company.

RE-ISSUE OF FORFEITED SHARES

Shares are forfeited because only a part of the due amount of such shares is received and the balance remains unpaid. On forfeiture the membership of the original allottee is cancelled. He/she cannot be asked to make payment of the remaining amount. Such shares become the property of the company. Therefore company may sell these shares. Such sale of shares is called 'reissue of shares'. Thus reissue of shares means issue of forfeited shares.

Once the Board of directors has forfeited the shares, the defaulting share holder is asked to return the share certificate which is cancelled thereafter. The board of directors passes a resolution allotting the forfeited shares to the new purchaser/purchasers of such shares.

In case of reissue of shares neither a prospectus is issued nor any offer is otherwise made to the general public. Though the amount of such shares may be called in more than one installment but usually the entire amount is called in one installment i.e. lump sum.

The board of directors of the company while reissuing the shares decides the price of reissue. These shares can be reissued at par, at premium or at discount. Generally, these shares are reissued at a discount i.e. at a price which is less than its nominal value. The amount of discount allowed at the time of reissue in no case should be more than the amount forfeited on such shares.

DIFFERENCE BETWEEN FORFEITURE AND SURRENDER OF SHARES

- Forfeiture of shares is a compulsory action taken by a company as a last resort to recover the calls on arrears. But surrender of share is a voluntary act done by a shareholder either to avoid forfeiture of shares or to exchange his share for new shares
- For forfeiture the company takes the initiative. But in surrender , share holder takes the initiative.
- Complicated procedures are required for forfeiture, while surrender requires easy procedures.
- There can not be forfeiture of fully paid shares, as there is no outstanding call on such shares. But there can be surrender of fully paid shares in exchange of new issues.

STOCK

Stock can be defined as, "stock is a bundle of fully paid shares put together for convenience". In other words, it is the aggregate of fully-paid shares of a company consolidated or put together for the purpose of facilitating its division and transfer in fraction of any denomination or amount.(i.e., for helping the stock holders to sub-divide and transfer their stocks in fractions or parts of any amount, even odd amount).

FEATURES OF STOCK:

The main features of stock are:

- A stock is the consolidated amount of fully-paid shares. In other words, it is the capital which consists of fully-paid shares put together for convenience.
- There cannot be an original issue of stocks by a company. Only fully paid shares can be converted into stock.
- A stock may be split up and transferred by the holders in fraction of any denomination or amount.
- Stocks are not divided into uniform or equal denomination.
- Stocks do no bear distinctive numbers.
- The title of the holders of stocks is represented by stock certificates issued to them. The holders of stock are also the members of a company.
- The stock holders enjoy the same rights and privileges which are enjoyed by the shareholders
- Stock can be reconverted into shares of any denomination.

ADVANTAGES OF STOCK HOLDERS AND THE COMPANY

Stocks are advantageous to the stockholders and the company

The main advantages of stocks to the stockholders are

1. A stock holders can enjoy all the rights and privileges enjoyed by a shareholder
2. Besides enjoying the rights and privileges of a shareholder, a stock holder has an additional advantage. That is, he can split up or divide and transfer his stock in fractions of any amount, even in odd amount.
3. Stock denotes that the company has recognized the fact that the holder of stock has paid the complete or full payment due from him to the company this recognition will help the stockholder to transfer his stock easily,

The main advantage of the stock to the company is that, as the stocks are not numbered, the company need not keep a detailed record of stocks transferred.

DIFFERENCES BETWEEN SHARES AND STOCK:

Shares differ from stocks' in many respects. The main differences between shares arid stocks are:

1. Shares may be fully or partly paid. But stocks are always fully paid.
2. Shares have distinctive numbers, whereas stocks do not have distinctive numbers.
3. A share has nominal value, whereas a stock has no nominal value.
4. Shares are always of equal denominations or values. But stocks can be of various denominations or values.

5. Shares can be issued not only by limited companies having share capital, but also by unlimited companies. But stocks can be issued only by limited companies having share capital.
6. Shares can be issued by a company originally. But stocks cannot be issued by a company originally. But the stocks cannot be issued by a company originally. Only fully paid shares can be converted into stock later on.
7. Consent of the shareholders is not necessary for the issue of shares. But the consent of the shareholders is necessary for the issue of stocks.
8. Shares can be transferred only in round numbers. They cannot be transferred in fraction. But stocks can be transferred in fraction.
9. Registration of share capital with the registrar of companies is necessary before the issue of shares. But stocks can be issuer by just giving a notice of conversion with the registrar of companies.
10. The holder of shares is a member of the company. But the holders of stocks is not necessarily a member of the company.

SHARE CERTIFICATE:

A share certificate is a document issued by a company under its common seal specifying the number of shares held by a member and the amount paid on each share and evidencing the title of the member to those shares. It is a prima facie evidence of the title of a member of the shares specified therein.

CONTENTS OF A SHARE CERTIFICATE:

A share certificate must contain the name and the registered office of the company. It must bear the common seal of the company. It must contain the signatures of at least two directors who are authorized to sign and also the counter signature of the secretary of the company.

In addition to the above, it must contain the following particulars:

1. Name and address of the member
2. Share certificate no.
3. Number and class of shares.
4. Distinctive numbers of the shares included in the certificate.
5. Face value of the amount paid on each share.
6. Date of issue of the share certificate.
7. A revenue stamp.

SHARE WARRANTS OR SHARE WARRANT PER BEARER OR SHARE WARRANTS TO BEARER

A share warrant is a document issued by a public limited company under its common seal to its shareholders in respect of fully paid shares, stating that the bearer of the instrument (i.e., the share warrant) is entitled to the shares mentioned therein. In short, it is bearer document of title to the shares issued by a public limited company to its shareholders.

ADVANTAGES OF SHARE WARRANTS:

Share warrants have certain advantages. They are:

1. Share warrants are bearer instruments. So, they are transferable by mere delivery.
2. A share warrant is regarded as a negotiable instrument under mercantile custom and usage.
3. Share warrants are very helpful in securing loans from banks or other financial institutions.

LIMITATION OF SHARE HOLDERS:

1. There is the risk of loss of ownership of shares represented by a share warrant. As a share warrant is transferable by mere delivery , in case of loss of a share warrant, the finder of the share warrant becomes its owner
2. Heavy stamp duty is payable (n share warrants. On account of these serious limitations, share warrants are not popular.

DIFFERENCES BETWEEN A SHARE CERTIFICATE AND SHARE WARRANT:

They are many differences between a share certificate and a share warrant. They are

1. Share certificates can be issued by public companies as well as private companies. But share warrants can be issued only by public companies limited by shares.
2. Share Certificates can be issued for fully-paid as well as partly paid shares, whereas share warrants can be issued only for fully paid shares.
3. No authorization by the articles of association is necessary for the issue of shares certificates. But share warrants cannot be issued by a company unless their issue is authorized by the articles of association.
4. No sanction or approval of the Central Government is necessary for the issue of shares certificates, whereas the approval of the Central Government s necessary for the issue of share warrants.
5. Shares represented by a share certificate are considered as qualification shares for the directorship of a company. But the shares represented by a share warrant are not considered as qualification shares for the directorship of a company.
6. The stamp duty payable on the issued of share certificates is just nominal, whereas the stamp duty payable on the issued of share warrants is heavy

7. The name of the bolder of a share certificate appears in the register of members. But the name of the holder of a share warrant does not appear in the register of members.
8. A share certificate is not a negotiable instrument, whereas a share warrant is considered as a negotiable instrument under mercantile usage and custom.
9. A share certificate can be issued originally. But a share warrant cannot be issued originally. Only share certificates can be converted into share warrants later on.
10. A share certificate is only a prima facie evidence of the title of the holder to the shares specified therein. On the other hand, a share warrant is a conclusive evidence of the title of the holder to the shares specified therein, provided he is a bonafide holder for value.

SECRETARY'S DUTIES IN CONNECTION WITH THE ISSUE OF SHARE WARRANTS:

- He should make sure that the articles of the company provide for the issue of the share warrants.
- On the receipt of the application for the issue of share warrants, he should check up whether the application is accompanied by the relevant share certificates. He should issue a lodgment ticket to the applicant acknowledging the receipt of the share certificate for the issue of share warrants.
- He should convene a board meeting for the approval of the issue of share warrants.
- He should also make the necessary arrangements for the issue of share warrants.
- On the receipt of the Central Government's approval, he should proceed with the work of preparation of the share warrants. He should get them sealed and signed by the directors and counter-signed by him self.
- He should see that a circular is issued to the applicants asking them tot take delivery of the share warrants in exchanges for the lodgments tickets.
- After the issue or delivery of the share warrants, he should see that the names of such shareholders are struck off from the register of members, and the necessary particulars regarding the issue of share warrants are entered in the remarks column of the register for the members. He must also see that the names of the shareholders to whom share warrants are issued are entered in a separate register called The Register of Share Warrant Holders.
- He should see that the unused share warrant forms are kept in safe custody so as to prevend their misuse.

TRANSFER AND TRANSMISSION OF SHARES

TRANSFER OF SHARES:

When a registered shareholder passed on the property or interest in his shares by sale or otherwise (say) by gift) to another person voluntarily) there is said to be transfer of shares. So, transfer of shares refers to the passing on of the property or interest in the shares by a registered shareholder to some other person voluntarily for a valuable consideration.

The instrument of transfer of any share in the Company shall be executed by or on behalf of both the transferor and the transferee. The transferor shall be deemed to remain a holder of the share until the name of the transferee is entered in the register of members in respect thereof.

Subject to the provisions of section 108 of the Act, the shares in the Company shall be transferred through the Prescribed Form under Companies (Central Govt.'s) General Rules & Forms, 1956, unless the shares are in dematerialized form.

(1) The Shares of the Company may be transferred by any Member to another Member of the Company. However, shares of the Company shall not be transferred to a person who is not its Member at the time of such transfer, so long as any Member or any person selected by the Directors in the interest of the Company, is willing to purchase the shares at a fair value.

(2) Except where the transfer is made pursuant to Article 36 (1), hereof, every Member or other person who intends to transfer the shares (herein after referred to as the "Vendor") shall give in writing (herein after referred to as the "Transfer Notice") to the Company that he desires to transfer the same. Such notice should constitute the Board his agent for the sale of the said Shares in one or more lots at the discretion of the Board to Members of the Company. The transfer notice shall not be revocable except with the sanction of the Board.

(3) The fair price shall be that price as may be agreed upon by the Vendor and the Board, or in default of such agreement at a price which the Auditor of the Company for the time being shall certify by writing under his hand to be in his opinion the fair selling value thereof as between a willing vendor and a willing purchaser.

(4) Upon the price being ascertained as aforesaid the Board shall forthwith give notice to all the Members of the Company of the number and price of the Shares to be sold and invite each of them to state in writing within twenty one (21) days from the date of notice whether he is willing to purchase any, and if so, what maximum number, of the said Shares.

(5) At the expiration of the said twenty one (21) days, the Board may allocate the said Shares to or amongst the Member or Members who shall have expressed his or their willingness to purchase in proportion to the number of Shares already held by them respectively, provided that no Member shall be obliged to take more than the said maximum number of Shares so notified by him. Upon such allocation being made the Vendor shall be bound on payment of the said price to transfer the Shares to the purchaser or purchasers thereof and if he defaults in doing so, the Board may receive and give a good discharge for the purchase money on behalf of the Vendor and enter the name of the purchaser in the register as holder by transfer of the Shares so purchased by him.

(6) Any Share may be transferred by a Member to any of his lineal descendants, father, brother, wife or husband of such Member and the restriction in these Articles shall not apply to any transfer authorized by these Articles provided that it is proved to the satisfaction of the Board that the transfer bonafide falls within one of these exceptions and provided that also it does not have the effect of increasing the membership of the Company beyond fifty, or does not, in the opinion of the Board, violate any provision of Law.

(7) Notwithstanding anything contained to the contrary in the preceding Articles any Share or Shares may be transferred to any person not a Member, with the previous unanimous consent in writing of all the Members for the time being of the Company expressly waiving the rights, privileges and the restrictions imposed for the transfer of Shares in these Articles.

POWER TO DIRECTORS TO REJECT TRANSFER

a) Where in the articles no clause for reject the transfer

In such a case the shareholder may freely transfer his shares and may carry the direction to register the transfer

b) Where the articles have Provision

If the articles contain a clause empowering the director to reject the transfer they can do so. But the refusal must be guided by sound principles and must be in the interest of the company and subject to the rules of the Securities Contract (Regulation) Act 1956.

The appeal against the decision goes to [Tribunal]. The [Tribunal] set aside the decision of the directors in refusing to register the transfer.

1. Where the director have not acted bonafide and in the interest of the company.
2. The reason for refusal is not sufficient.

CERTIFICATION OF TRANSFER – SECTION 112

Where a Shareholder desires to sell away some of the shares represented by a share certificate or to sell them to different buyers, the problem of single share certificate arise. To overcome this problem, a practice has grown up whereby the transferor lodges the certificate and transfer form with the company with a request to certify the transfer. The company responds by endorsing a statement to the effect that a share certificate covering those transfers has been lodged with the company.

The certification by a company of any instrument of transfer of shares in, or debentures of, the company, shall be taken as a representation by the company to any person acting on the faith of the certification that there have been produced to the company such documents as on the face of them show a prima facie title to the shares or debentures in the transferor named in the instrument of transfer, but not as a representation that the transferor has any title to the shares or debentures. The company cancels the old certificates and sends a "Certification of transfer" for the shares transferred.

Where any person acts on the faith of an erroneous certification made by a company negligently, the company shall be under the same liability to him as if the certification had been made fraudulently.

FORGED TRANSFER

An instrument of transfer which is not signed by the true owner of shares, but is signed by some other person as the true owner is called a forged transfer. In other words, an instrument of transfer which contains the forged signature of the transferor is called a forged transfer.

A forged transfer is a nullity and it does not confer any legal title upon the transferee If the company has issued a share certificate to the transferee on a forged transfer, and an innocent buyer accept it, he can claim damages from the company on the ground that he acted on the share certificate of the company.

BLANK TRANSFER

When an instrument of transfer duly completed and signed by the transferor, but the name, address and signature of the transferee left blank, is delivered by the transferor to the transferee along with the relevant share certificate, there is said to be a blank transfer. A blank transfer is so called, because the name, address and signature of the transferee are left blank in the transfer form.

Here the document can be freely transferred as the share is a negotiable instrument. The process of purchase and sale can be repeated any number of times.If the ultimate buyer wants to retain it, he can fill his name and date and get it registered in the company’s book. And in such case the first seller is treated as the transferor.

TRANSMISSION OF SHARES:

Transmission of shares refers to the passing of property in shares by the operation of law, and not by sale by the original owner, on the happening such events as death, insolvency or lunacy of a shareholder, to his legal representative.

(1) On the death of a member, the survivor or survivors where the member was a joint holder, and his legal representatives where he was a sole holder, shall be the only persons recognized by the Company as having any title to his interest in the shares.

(2) Any person becoming entitled to a share in consequence of the death or insolvency of a member may, upon such evidence being produced as may from time to time properly be required by the Board and subject as hereinafter provided, elect, either-

    (a) To be registered himself as holder of the share; or

    (b) To make such transfer of the share as the deceased or insolvent member could have made.

(3) The Board shall, in either case, have the same right to decline or suspend registration as it would have had, if the deceased or insolvent member had transferred the share before his death or insolvency.

(4) If the person so becoming entitled shall elect to be registered as holder of the share himself, he shall deliver or send to the Company a notice in writing signed by him stating his intention along with evidence as may be required by the Board.

(5) If the person aforesaid elects to transfer the share, he shall testify his election by executing a transfer in respect of the share.

(5) All the limitations, restrictions and provisions of these regulations relating to the right to transfer and the registration of transfers of shares shall be applicable to any such notice of transfer as aforesaid as if the death or insolvency of the member had not occurred and the notice of transfer were a transfer signed by that member.

DIFFERENCES BETWEEN TRANSFER OF SHARES AND TRANSMISSION OF SHARES:

The main points of distinction between transfer of shares and transmission of share are:

1. Transfer of shares is the result of a voluntary and deliberate act of the holder of shares, whereas transmission of shares is the result of the operation of law.
2. Transfer of shares is a common or general method of passing of property in the shares from one person to another. But transmission of shares takes place only under certain special circumstances, such as the death, lunacy or insolvency of a shareholder.
3. As the transfer of shares is a voluntary act of the parties, there must be adequate and valid consideration for the transfer of shares. On the other hand, as the transmission of shares is the result of the operation of law, the question of consideration does not arise in the case of the transmission of shares.
4. As the transfer of shares take place for valid consideration, stamp duty is payable in case of Transfer of shares. (The stamp duty is payable on the market value of the shares transferred). But as the transmission of shares take place without any consideration, no stamp duty is payable in the case of transmission of shares.
5. For the transfer of shares, an instrument of transfer is required to be executed by the transferor in favour of the transferee. On the other hand, for the transmission of shares, there is no need for an instrument of transfer. Share are transmitted to the legal representative on his producing mere proof of his title to the shares transmitted.
6. In the case of transfer of shares, as soon as the transfer is complete, the liability of the transferor ceases completely. But in the case of transmission of shares, the shares transmitted continue to be subject to the liability of the original holder to the company.

LIEN ON SHARES

COMPANY'S LIEN OVER PARTLY PAID SHARES

If a shareholder has not fully paid the allotment price of any share or owes money to the Company, the Company has a lien over all shares registered for that shareholder alone (except fully paid shares). This lien is for the amount outstanding, even if it is not immediately payable. This lien takes priority over all other rights in the share and extends to dividends payable on the share. However, the directors can decide that a share is completely or partly exempt from this clause.

COMPANY MAY SELL PARTLY PAID SHARES

The directors may sell any shares over which the Company has a lien if all of the following conditions are met:

- The money owing in respect of the lien is payable immediately.
- The Company gives a notice to the registered holder, or the person entitled to the share, demanding immediate payment.
- The money is not paid within 14 days after that notice is given.

The company's right of lien is lost when

- The shareholder pledges his share to a third party as security for a loan and the company has notice of it.
- The company registers the transfer of shares which was subject to lien by the company.

DEMATTING OF SHARES

Dematerialization (Commonly known as 'Demat') signifies conversion of a share certificate from its present physical form to electronic form for the same number of holding.

It offers scope for paperless trading through state-of-the-art technology, whereby share transactions and transfers are processed electronically without involving any share certificate or transfer deed after the share certificates have been converted from physical form to electronic form. It attempts to avoid the time consuming and complex process of getting shares transferred in the name of buyers as well its inherent problems of bad deliveries, delay in processing/fraudulent interception in postal transit, etc.

Dematerialization of shares is optional and an investor can still hold shares in physical form. **However, he/she has to demats the shares if he/she wishes to sell the same through the Stock Exchanges.** Similarly, if an investor purchases shares, he/she will get delivery of the shares in demat form only.

The Depositories Act 1996 has been enacted to regulate the matters related and incidental to the operation of Depositories and demat operations. Two Depositories are in operation –

- National Securities Depository Limited (NSDL) and Central Depository Services Limited (CDSL).

OPERATION IN DEPOSITORY SYSTEM

The operations in the Depository System involve the participation of a Depository, Depository Participants, Company/Registrars and Investors. The company is also called the Issuer.

A **Depository** (NSDL and CDSL) is an organization where the securities on an investor are held in electronic form, through Depository participants.

A **Depository Participant** is the agent of the Depository and is the medium through which the shares are held in the electronic form. They are also the representatives of the investor, providing the link between the investor and the company through the Depository.

In both systems, the transfer of funds or securities happens without the actual handling of funds or securities. Both the banks and the Depository are accountable for safe keeping of funds and securities respectively.

PROCEDURE FOR DEMATTING OF SHARES

First, you will have to open an account with a Depository Participant (DP) and get a unique Client ID number. Thereafter, you will have to fill up a Dematerialization Request Form (DRF) provided by the DP and surrender the physical shares, which you want to be dematted to the DP.

The DP upon receipt of the shares and the DRF will send an electronic request to the company's registrar and share transfer agent through the Depository for confirmation of demat. Each request will bear a unique transaction number.

The DP will simultaneously surrender the DRF and the shares to the company's registrar and share transfer agent with a covering letter requesting the registrar and share transfer agent of the company to confirm demat. The company's registrar and share transfer agent after necessary verification of the documents received from the DP will confirm demat to the Depository.

This confirmation will be passed on from the Depository to the DP, which holds your account. After receiving this confirmation from the Depository, the DP will credit the account with the shares so dematerialized. The DP will hold the shares in the dematerialized form thereafter on your behalf. And you will become beneficial owner of these dematerialized shares.

CONVERSION OF DEMATTED SHARES INTO PHYSICAL FORM

If you are holding shares in electronic form, you still have the option to convert your holding in physical form by submitting a Rematerialization Request Form (RRF) through your DP in the same manner as Dematerialization. Upon receipt of such request from your DP, the company will issue share certificates for the number of shares so rematerialized.

TRANSFER UNDER DEPOSITORY SYSTEM

In case of fresh issue, at the time of initial offer, the investor would indicate his choice in application form, if he opts to hold the security in the depository mode.

Whenever shares held by the Depository are to be transferred by one beneficial owner to another person who has also availed himself of the services of a depository, the transferor will inform the DP, who in turn, informs the Depository.

The Depository makes appropriate book entries in its records to effect the transfer and thus in the process, deletes the name of the transferor and enters the name of the transferee. It may thus be observed that for transferring shared held under the depository system no transfer deed is required and the legal formalities regarding transfer of shares under section 108 of the companies Act are dispensed with.

MODULE IV
MANAGEMENT OF COMPANIES

A company is an artificial person created by law. Thus a company is not a natural person and yet it acts as a natural person through the persons who conducts his business, and they are known as directors of the company. The directors of the company are collectively known as board of Directors or the Board. The Board of directors entrust the day to day management of the company to a chief executive, who may be managing director or manager by delegating necessary powers. So the chief executive looks after the day to day managerial functions of the company, with or without whole time director or directors. As per the companies [Amendment] Act, 2000, the following are the managerial persons of a company.

1. Directors
2. Whole time Director
3. Managing Director or Manager

DIRECTORS DUTIES AND RESPONSIBILITIES

DIRECTORS

The Companies Act says that the term ‘Director’ includes ‘any person occupying the position of Director regardless of title’. The definition of ‘Director’ includes ‘any person occupying the position of a Director, by whatever name called’.

Directors of the company may therefore be trustees, governors, managers, officers etc., they will have the legal status of a director if that is their function. A person who has ‘Director’ in his job title may, even if he does not perform the function of a director within the organisation, may be held liable as a director.

QUALIFICATION OF A DIRECTOR

General Qualifications:

1. Director should possess a variety of knowledge and experiences while being a professional with an ethical mind.
2. Director should fully understand his obligations and practices with a commitment to create long-term values to the business and shareholders.
3. Director should have enough time to perform his duties effectively.
4. Director should be able to assess himself and is ready to notify the Board of Directors upon change or if there is anything that prevents him from performing his job effectively.

Dis-qualification of Directors (Section 274)

1. A person shall not be capable of being appointed as a director of a company, if,

a. he has been found to be of unsound mind by a court of competent jurisdiction and the findings is in force,

b. he is an undercharged insolvent

c. he has applied to be adjudicated as an insolvent and his application is pending

d. he has been convicted by a court of any offence involving moral turpitude and sentenced in respect thereof to imprisonment for not less than six months, and a period of five years has not elapsed from the date of expiry of sentence;

e. he has not paid any call in respect of shares, of the company held by him, whether alone or jointly with others, and six months have elapsed from the last day fixed for the payment of the call'

f. an order disqualifying him for appointment as director has been passed by a court in pursuance of section 203 and is in force, unless the leave of the court has been obtained for his appointment in pursuance of that section , or

g. such person is already a director of a public company which

(i) has not filed the annual accounts and annual returns for any continuous three financial years commencing on and after the first day of April. 1999 or

(ii) has failed to repay its deposit or interest thereon due date or redeem its debentures on due date to pay dividend and such failure continues for one year or more.

LEGAL POSITION OF DIRECTORS

It is difficult to define the exact legal position of the director of a company. The companies Act makes no effort to define their position. They have at various times be described by judges as agents. In the words of Bowen. L.J. " Directors are described sometimes as agents, sometimes as trustees and sometimes as managing directors . But each of these expressions is used not as exhaustive of their powers and responsibilities, but as indicating useful points of view from which they may for the moment and for the particular purpose to be considered "

DIRECTORS AS AGENTS

Sec 182.of the Indian Contract Act, 1872 says that "An 'agent' is a person employed to do an act for another or to represent another in dealings with third person. The person for whom such act is done, or who is so represented, is called the principal"

Where one employs another to do an act for him or to represent him in dealings with third parties, the person so employed is called an agent. In the theory of the English law, the agent is a connecting line between the principal & third parties. He is an intermediary who has the power to create legal relationships between the principal and the third parties.

Sec. 2(13) of the Companies Act, 1956 defines that "'director' includes any person occupying the position of a director by whatever name called"

Director is an individual lawfully appointed to the Board of Directors of a company which is duly constituted to direct, control and supervise the activities and affairs of a company. Directors of a company are in the eye of law agents of the company for which they act and the general principles of the law of principal and agent regulate in most respects the relationship of the company and its directors. (Somayazula vs. Hope Prodhome & Co. (1963) 2 An W.R. 112.) The test of agency is whether the person is purporting to enter into transaction on behalf of the principal or not. In order to constitute an agency, it is not necessary to have a formal agreement.

A director of a company is not necessarily the agent of the company or of its shareholder, but the true position of the directors of a company may that be of agents for the company with powers and duties of carrying on the whole of its business, subject to the restrictions imposed by the Articles of Association. A Director or a managing director may not be a servant of the company; he may be an agent of the company for carrying on its business. What he is in fact will depend on the facts and circumstances of each case. Generally speaking, neither the board of directors nor an individual director is, as such, an agent of the company, or the corporation, or its members. Under modern legislation, all powers of management, except those expressly reserved to the shareholders in general meeting, are vested in the board of directors, who have powers to appoint officers who are subject to the supervision and control of the board. Members of the board resemble agents in that they act on behalf of others, and are fiduciaries owing to the duties of loyalty and care. However, these duties are owed to the corporate body itself rather than to the shareholders. An individual director, as such, has still less resemblance to an agent than has the board as a body. Even when he acts as member of the board, he does not act as an agent, but as one of the group which supervises the activities of the corporation. However, he may be appointed an agent of the incorporated body.

He is to enter into relations on behalf of his principal with third persons. He acts at his discretion and judgment but within the limits of his authority.

As a company is an artificial person and can only contract through its agents, the normal mode of signing is to use the words "on behalf of" so and so company before the signature of the agent signing, and if an agent so signs, no personal liability will attach to him. Directors are agents of the company to the extent of the authority delegated to them. Hence, where directors make a contract in the name of, or purporting to bind the company, it is the company- the principal- which is liable on it and not the directors. The directors are not personally liable unless it appears that they took personal liability.

Directors are not personally liable under a contract which is lawful and which they have made in the proper exercise of their authority. Directors purchased goods for their company and agreed with the supplier to allot him debentures for the price. Before the debentures could be issued, the company went into liquidation. The supplier was held not liable to make the directors personally liable under the contract.

In another case, where its directors cum majority shareholder appointed an accountant for the company and he subsequently acting as a director removed the accountant, he was held not liable to compensate the accountant because he had acted only as an officer of the company but he was liable for the accountant's costs and expenses of litigation. This is because the litigation was solely due to his conduct in acting in a highhanded manner

While negotiating a contract for his company, a director should make it clear to the other party that the contract will be entered into by the company and not by the director personally. If he does not do this and the other party believes that he is contracting with the director or agent and not the company, the contract they conclude will be a personal one and he will be personally liable for the fulfillment of the promises made.

DIRECTORS AS TRUSTEES

In the non-profit world, “directors” and “trustees” are often used interchangeably; intended to refer to the group of individuals responsible for the management of the activities and affairs of the corporation (e.g., “board of directors,” “board of trustees,” “board of governors”). Most state non-profit laws provide a common structure from which these individuals (whether directors, trustees, or governors) may carry out those responsibilities.

- ✓ “Trustee” may have a separate meaning under state law (e.g., as a person, association, corporation, or other entity holding property for, or solicited for, any charitable purpose such as a trustee of a charitable trust). Many states have charitable trust acts or similar laws, separate and distinct from non-profit corporation acts.
- ✓ The fiduciary standards of a trustee under most charitable trust laws are often interpreted as holding the trustee to a higher standard of conduct than that applicable to the director of a non-profit corporation (e.g., liability for acts of simple negligence, as opposed to gross negligence). Furthermore, trustees of charitable trusts are held to an absolute duty of loyalty to the trust and are prohibited from engaging in any self-dealing. Directors of non-profit corporations have a more relaxed duty in this regard and may participate in conflict-of-interest and similar transactions with proper board approval.
- ✓ Most state non-profit laws are “corporate law based” as opposed to “trust law based,” meaning they are derived from the principles of business corporation law (and the state business corporation law statute), which applies the title “director.”

Simply referring to a board member as a “trustee” as opposed to a “director” should not, in and of itself, automatically convert the duties of board members to the higher trust law standard. Yet, the concern is that by referring to governing board members as “trustees,” as opposed to “directors,” the non-profit corporation may unintentionally be increasing the board’s exposure to trust law arguments. This would especially be the case in states where there exists a potential for application of charitable trust laws to non-profit corporations.

This approach is consistent with many state non-profit corporate law statutes, which use the title "director" rather than "trustee." Furthermore, some states (e.g., Ohio) have made the decision to change by statute how non-profit board members are referred, from "trustee" to "director." Indeed, in these states, the persons responsible for conducting the affairs of the non-profit corporation are regarded by the law as "directors," irrespective of the name (e.g., "trustee") by which they may be referred in the non-profit's organizational documents.

To some, the title "trustee" suggests an aura of greater sophistication and more charitable focus than the title "director," given the latter title's close association with business corporation law. Yet this is not really a fair distinction. Because most state non-profit laws are corporate based, it is more appropriate to refer to governing board members as "directors"—and without any of the unnecessary baggage attributed to charitable trust principles. So, my vote is always for "director" rather

DIRECTORS AS MANAGING PARTNERS

Directors are elected representatives of the shareholders and therefore they are in a position as managing partners.

In addition to that, they themselves are the shareholders of the company, this also makes them partners with other shareholders. They do almost all the functions of the company in the capacity of its proprietor

But they are not the managing partners of the company in full sense. Because, if they are the managing partners, why are they not authorized to bind other directors and shareholders by their acts and why do they compulsorily retire.

DIRECTORS AS EMPLOYEES

Although directors are agent of the company, they are not employees or servants to the company. Hence they cannot claim their remunerations as a preferential creditor in the event of winding up of a company under section 530 of the Companies Act 1956.

But where any director, besides being a director, is also in the service or employment of the company such as secretary, manager or otherwise, he will be treated as an employee. He will be entitled to the remuneration and other benefits of the employee in addition to his rights as a director to sitting fee etc..

APPOINTMENT AND REMOVAL OF DIRECTORS

APPOINTMENT OF DIRECTORS

The directors are the brain of a company. They occupy a very important position in the structure of the company. Only individuals can be appointed as directors. Legally, no firm or association or company can be appointed as directors. Any individual who is not disqualified under section 274 of the Companies Act may be appointed as a director of a company.

The directors may be appointed in any one of the following ways.

A. Appointment of first directors

1.By articles of the company

2.By the subscribers to the memorandum of association

B. Appointment of first directors

The first directors are generally nominated by the promoters of the company, and their names are mentioned in the articles of association of the company. If the first directors are not nominated by the promoters of the company, the subscribers to the memorandum, who are individuals, shall be deemed to be the first directors of the company, subject to the regulations of the company's articles. They shall held office until directors are duly appointed in the first annual general meeting [Section 254]

A person shall not be capable of being appointed as director of a company by the articles unless before the registration of articles he has signed and filed with the Registrar a consent in writing to act as such a director and to take up and pay for the qualification shares [Section 266(1)]

According to the provisions of section 254, the subscribers to the memorandum who are individuals will be deemed to be directors , if any subject to the regulations provided in the Articles.

In the case of a public company, a list of persons who are the first directors of the company along with their written consent should be delivered to the Registrar of companies with the necessary documents required for the registration of the company.

APPOINTMENT OF SUBSEQUENT DIRECTORS

The subsequent directors of a company are appointed in any of the following ways:-

1. By the company in annual general meeting (Section 255)

Except for the first directors, the subsequent directors are appointed by the company in the general meeting. In case of a public company or a subsidiary thereof, unless the article provide for the retirement of all directors at every annual general meeting, at least 2/3 of the total number of directors shall be liable to retire by rotation.

PROCEDURES FOR THE APPOINTMENT, ELECTION AND REMOVAL OF DIRECTORS

There are formal, considered and transparent procedures for nominating candidates to stand for election as directors. The process of evaluating the skills and composition of the Board is ongoing and is kept under regular review in order to ensure that appropriate plans for succession to the Board are in place for smooth Board refreshment, and that the Board retains its effectiveness at all times. Directors are subject to re-election/re-appointment at regular intervals.

APPOINTMENT AND ELECTION OF DIRECTORS

Election of directors at the annual general meetings – According to the Articles, at every annual general meeting, the shareholders entitled to vote for the election of directors must, by unanimous resolution, elect or appoint, a Board consisting of the number of directors for the time being set under the Articles. All the directors cease to hold office immediately before such election or appointment, but are eligible for re-election or re-appointment. If the shareholders fail to elect or appoint the directors at the annual general meetings, each director then in office continues to hold office until the earlier of: (1) the date on which his or her successor is elected or appointed; and (2) the date on which he or she otherwise ceases to hold office under the the Articles.

Directors may fill casual vacancies and appoint additional directors – Any casual vacancy in the Board may be filled by the Directors. The Directors may also appoint one or more additional directors between the annual general meetings, but the number of additional directors must not at any time exceed one-third of the number of the current Directors.

Shareholders may fill vacancies – The shareholders may elect or appoint Directors to fill any vacancies on the Board if the Company has no directors or fewer directors in office than the number set pursuant to the Articles as quorum of directors.

Nominating committee – The Nominating Committee is mandated to review the size and composition of the Board at least annually, and to identify individuals qualified to become Board members and make recommendations to the Board for the appointment or election of Director nominees.

Information on the director candidates – To enable shareholders to make an informed decision on their election at a general meeting, the names of all candidates submitted for election or re-election as a director together with his/her biographical details as set out in Rule 13.51(2) of the Listing Rules (including other directorships held in listed public companies in the past 3 years and other major appointments) shall be set out in a circular to be sent to shareholders prior to the meeting.

REMOVAL OF DIRECTORS

Removal of director by shareholders – Shareholders may remove any director before the expiration of his or her term of office by special resolution. In that event, the shareholders may elect, or appoint by ordinary resolution, a director to fill the resulting vacancy. If the shareholders do not elect or appoint a director to fill the resulting vacancy contemporaneously with the removal, then the directors may appoint or the shareholders may elect, or appoint by ordinary resolution, a director to fill that vacancy.

Removal of director by directors – The directors may remove any director before the expiration of his or her term of office if the director is convicted of an indictable offence, or if the director ceases to be qualified to act as a director of a company and does not promptly resign, and the directors may appoint a director to fill the resulting vacancy.

Section 252 provides that every public company (other than a public company which has become such by virtue of Section 43-A) must have at least 3 directors and every private company must have at least 2 directors. Subject to the minimum number of directors a company should have, the articles of a company may prescribe the maximum and the minimum number of directors for its board of directors. A company in a general meeting may by ordinary resolution increase or reduce the number of its directors within the limits fixed in that behalf by its article. A public company or a private company which is a subsidiary of a public company cannot increase the number of directors beyond the permissible maximum under its articles without the approval of the central government. However, no approval of the central government is required if such permissible maximum is twelve or less than twelve, and the increase in the number of its directors does not exceed twelve.

Appointment of Directors:

Director may be appointed in the following ways:

1. By the articles as regards first directors.
2. By the company in general meeting.
3. By the directors,
4. By third parties
5. By the principle of proportional representation
6. By the central government

1. First directors:

The first directors are usually named in the articles. The articles may also provide that both the number and the names of the first directors shall be determined in writing by the subscribers to the memorandum or a majority of them. Where the articles are silent regarding the appointment of directors, the subscribers of the memorandum who are individuals shall be deemed to be the first directors of the company. They shall hold office until the directors are appointed at the first annual general meeting.

2. Appointment by company:

Appointment of subsequent directors is made at every annual general meeting of the company. Section 255 provides that not less than two-thirds of the total number of directors of a public company must be appointed by the company in general meeting. These directors must be subject to retirement by rotation. The remaining directors of such a company and the directors generally of a purely private company must also be appointed by the company in general meeting. In other words, not more than one-third of the total number of directors can act as non-retiring directors i.e not subject to retirement by rotation.

At every subsequent annual general meeting one-third of the directors of a public company are liable to retire by rotation. If the number is not three or a multiple of three, then the number nearest to one-third must retire from office. The directors to retire by rotation at every annual general meeting must be those who have been longest in office since their last appointment. As between person who become directors on the same day, those who are to retire will, subject to any agreement among themselves, be determined by lot.

At the annual general meeting at which a director retires, the company may fill up the vacancy by appointing the retiring director or some other person thereto. If the place of the retiring director is not so filled, and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned. If at the adjourned meeting also the vacancy is not filled, and the meeting has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting unless:

1. At the meeting or at the previous meeting a resolution for the re-appointment of such director has been put to the meeting and lost;
2. He has by a notice in writing, addressed to the company or its board, expressed his unwillingness to be re-appointed;
3. He is not qualified or disqualified for appointment;
4. A special or ordinary resolution is necessary for his appointment or re-appointment.

A person other than a retiring director is also eligible for appointment to the office of director subject to his necessary qualification. A notice in writing signifying his candidature must be left at the office of the company at least fourteen days before the date of the meeting. The notice may be given either by the candidate himself or by his proposer. The company shall inform the members at least seven days before the meeting about the candidature. It is not necessary for the company to serve individual notices upon the members if the company advertises such candidature not less than seven days before the meeting, in at least two newspapers. One of the newspapers must be in English language and the other in the regional language of the place where the registered office of the company is located.

These provisions do not apply to a private company, unless it is a subsidiary of a public company.

A person who is being proposed as a candidate for the office of a director must sign and file with the company his consent in writing to act as a director if appointed. This requirement does not apply to a director retiring by rotating.

Appointment of directors of a public company must be voted individually by separate ordinary resolutions.

3. Appointment by Directors:

The directors are empowered to appoint

i) Additional directors.

ii) Alternate directors.

iii) Directors filling casual vacancy.

ADDITIONAL DIRECTORS:

The board of directors may appoint additional directors from time to time. The number of directors and additional directors must not exceed the maximum strength fixed for the board by the articles. The additional directors shall hold office only up to the date of the next annual general meeting.

ALTERNATE DIRECTORS:

The board of directors may appoint an alternate director if authorized by the articles or by a resolution of the company in general meeting. An alternate director acts in the place of a director who is absent for more than three months from the state in which board meetings are held. He cannot hold office for a period longer than that permissible to the original director in whose place he has been appointed. He must vacate office on the return of the original director.

CASUAL VACANCY:

Where the office of any director appointed by the company in general meeting is vacated before the expiry of his term, the directors may fill up the vacancy at a meeting of the board. The director so appoint will hold office till the end of the term of the director in whose place he is appointed. These provisions are applicable only to a public company and a private company which is a subsidiary of the public company.

4. Appointment by third parties:

The articles may gives right to debenture-holders, financial corporations or banking companies who have advanced loans to the company to nominate director on the board of the company. The number of directors so nominated should not exceed one-third of the total strength of the board. They are not liable to retire by rotation.

5. Appointment by proportional representation:

The articles of a company may provide that the appointment of not less than2/3 of the total number of director of a public company shall be according to the principle of proportional representation, either by the single transferable vote or by a system of cumulative voting or otherwise. Such appointments shall be made once in three years and interim casual vacancies may be filled up according to section 262.

6. Appointment by the central government:

According to section 408 of the companies act, the central government has the power to appoint directors for the purpose of prevention of oppression and mismanagement. It provides that the central government may appoint such number of directors on the board of the company as it may think fit to effectively safeguard the interest of the company, its shareholders, or public interest. Such an appointment shall be for a period not exceeding three years, and shall be made on the application of not less than 100 member or members holding not less than $1/10^{th}$ of the voting power of the company. Such directors will not be required to hold any qualification shares, not they shall be liable to retire by rotation.

RESTRICTION ON APPOINTMENT OF DIRECTORS:

A person shall not be capable of being appointed a director by the articles or named as a director or proposed director of the company or intended company in a prospectus or statement in lieu of prospectus unless he or his agent in writing has signed and filed with the registrar consent in writing to act as such director and has:

(a) Signed the memorandum for his qualification shares; or

(b) Taken his qualification shares from the company and paid or agreed to pay for them; or

(c) Signed and filed with the registrar an undertaking in writing to take from the company his qualification shares and pay for them; or

(d) Field with the registrar an affidavit that his qualification share, if any, are registered in his name.

The provisions of section 266 do not apply to a private company.

Central Government Act Section 284 in the Companies Act, 1956 284. Removal of directors. (1) A company may, by ordinary resolution, remove a director (not being a director appointed by the Central Government in pursuance of section 408) before the expiry of his period of office: Provided that this sub- section shall not, in the case of a private company, authorize the removal of a director holding office for life on the 1st day of April, 1952 , whether or not he is subject to retirement under an age limit by virtue of the articles or otherwise: Provided further that nothing contained in this sub- section shall apply where the company has availed itself of the option given to it under section 265 to appoint not less than two- thirds of the total number of directors according to the principle of proportional re- presentation.

(2) Special notice shall be required of any resolution to remove a director under this section, or to appoint somebody instead of a director so removed at the meeting at which he is removed.

(3) On receipt of notice of a resolution to remove a director under this section, the company shall forthwith send a copy thereof director concerned, and the director (whether or not he is a member of the company) shall- be entitled to be heard on the resolution at the meeting.

(4) Where notice is given of a resolution to remove a director under this section and the director concerned makes with respect thereto representations in writing to the company (not exceeding a reasonable length) and requests their notification to members of the company, the company shall, unless the representations are received by it too late for it to do so,- (a) in any notice of the resolution given to members of the company state the fact of the representations having been made; and (b) send a copy of the representations to every member of the company to whom notice of the meeting is sent (whether before or after receipt of the representations by the company); and if a copy of the representations is not sent as aforesaid because they were received too late or because of the company' s default, the director may (without prejudice to his right to be heard orally) require that the representations shall be read out at the meeting: Provided that copies of the representations need not be sent representations need not be read out at the meeting if, on the application either of the company or of any other person who claims to be aggrieved, the 1[Company Law Board] is satisfied that the right conferred by this sub- section are being abused to secure needless publicity for defamatory matter; and 1[Company Law Board] may order

the company' s costs on the application to be paid in whole or in part by the director notwithstanding that he is not a party to it.

(5) A vacancy created by the removal of a director under this section may, if he had been appointed by the company in general meeting or by the Board in pursuance of section 262, be filled by the appointment of another director in his stead by the meeting at which he is removed, provided special notice of the intended appointment has been given under sub- section (2). A director so appointed shall hold office until the date up to which his predecessor would have held office if he had not been removed as aforesaid.

(6) If the vacancy is not filled under sub- section (5), it may be filled as a casual vacancy in accordance with the provisions, so far as they may be applicable, of section 262, and all the provisions of that section shall apply accordingly: Provided that the director who was removed from office shall not be re- appointed as a director by the Board of directors.

(7) Nothing in this section shall be taken- (a) as depriving a person removed there under of any compensation or damages payable to him in respect of the termination of his appointment as director or of any appointment terminating with that as director; or (b) as derogating from any power to remove a director which may exist apart from this section. Meetings of Board

REMOVAL OF DIRECTORS

(1) A company may, by ordinary resolution, remove a director (not being a director appointed by the Central Government in pursuance of section 408) before the expiry of his period of office: Provided that this sub- section shall not, in the case of a private company, authorize the removal of a director holding office for life on the 1st day of April, 1952 , whether or not he is subject to retirement under an age limit by virtue of the articles or otherwise: Provided further that nothing contained in this sub- section shall apply where the company has availed itself of the option given to it under section 265 to appoint not less than two- thirds of the total number of directors according to the principle of proportional re- presentation.

(2) Special notice shall be required of any resolution to remove a director under this section, or to appoint somebody instead of a director so removed at the meeting at which he is removed.

(3) On receipt of notice of a resolution to remove a director under this section, the company shall forthwith send a copy thereof to the director concerned, and the director (whether or not he is a member of the company) shall- be entitled to be heard on the resolution at the meeting.

(4) Where notice is given of a resolution to remove a director under this section and the director concerned makes with respect thereto representations in writing to the company (not exceeding a reasonable length) and requests their notification to members of the company, the company shall, unless the representations are received by it too late for it to do so,-

(a) in any notice of the resolution given to members of the company state the fact of the representations having been made; and

(b) send a copy of the representations to every member of the company to whom notice of the meeting is sent (whether before or after receipt of the representations by the company); and if a copy of the representations is not sent as aforesaid because they were received too late or because of the company' s default, the director may (without prejudice to his right to be heard orally) require that the representations shall be read out at the meeting: Provided that copies of the representations need not be sent out and the representations need not be read out at the meeting if, on the application either of the company or of any other person who claims to be aggrieved, the 1[Company Law Board] is satisfied that the right conferred by this sub- section are being abused to secure needless publicity for defamatory matter; and 1[Company Law Board] may order the company' s costs on the application to be paid in whole or in part by the director notwithstanding that he is not a party to it.

(5) A vacancy created by the removal of a director under this section may, if he had been appointed by the company in general meeting or by the Board in pursuance of section 262, be filled by the appointment of another director in his stead by the meeting at which he is removed, provided special notice of the intended appointment has been given under sub-section (2). A director so appointed shall hold office until the date up to which his predecessor would have held office if he had not been removed as aforesaid.

(6) If the vacancy is not filled under sub- section (5), it may be filled as a casual vacancy in accordance with the provisions, so far as they may be applicable, of section 262, and all the provisions of that section shall apply accordingly: Provided that the director who was removed from office shall not be re- appointed as a director by the Board of directors.

(7) Nothing in this section shall be taken-

(a) as depriving a person removed there under of any compensation or damages payable to him in respect of the termination of his appointment as director or of any appointment terminating with that as director; or

(b) as derogating from any power to remove a director which may exist apart from this section.

POWERS OF DIRECTORS

The directors powers are normally set out in the articles. The shareholders cannot control the way in which the Board of Directors act provided its actions are within the powers given to the Board. Section 291 of Companies Act, 1956 provides for general powers of the Board of directors. It mandates that the Board is entitled to exercise all such powers and do all such acts and things, subject to the provisions of the Companies Act, as the company is authorized to exercise and do. However, the Board shall not exercise any power and do any act or things which is required whether by the Act or by the memorandum or articles of the company or otherwise to be exercised or done by the company in general meeting.

POWER OF THE INDIVIDUAL DIRECTORS

Unless the Act or the articles otherwise provide, the decisions of the Board are required to be the majority decisions only. Individual directors do not have any general powers. They shall have only such powers as are vested in them by the Memorandum and Articles. Section 292(1) of the Companies Act, 1956 provides that the Board of directors of a company shall exercise the following powers on behalf of the company and it shall do so only by means of resolution passed at meeting of the Board:

(a) the power to make calls on shareholders in respect of money unpaid on their shares; (aa)the power to authorize the buy-back referred to in the first proviso to clause (b) of sub-section (2) of section 77A;

(b) the power to issue debentures;

(c) the power to borrow moneys otherwise than on debentures;

(d) the power to invest funds of the company; and

(e) the power to make loan.

DUTIES

1. Statutory Duties:

(A) To file return of allotment: Section 75 of the Companies Act, 1956 requires a company to file with the Registrar, within a period of 30 days, a return of the allotments stating the specified particulars. Failure to file such return shall make the directors liable as .officer in default.. A fine up to Rs. 5000/- per day till the default continues may be levied.

(B) Not to issue irredeemable preference share or shares or share redeemable after 20 years: Section 80, as amended by Amendment Act, 1996, forbids a company to issue irredeemable preference shares or preference shares redeemable beyond 20 years. Directors making any such issue may be held liable as .officer in default. And may be subject to fine up to Rs. 10,000/-.

(C) To disclose interest (Section 299-300): In respect of contracts with director, Section 299 casts an obligation on a director to disclose the nature of his concern or interest (direct or indirect), if any, at a meeting of the Board of directors. The said Section provides that in case of a proposed contract or arrangement, the required disclosure shall be made at the meeting of the Board at which the question of entering into the contract or agreement is first taken into consideration. In the case of any other contract or arrangement, the disclosure shall be made at the first meeting of the Board held after the director become interested in the contract or arrangement. Every director who fails to comply with the aforesaid requirements as to disclosure of concern or interest shall be punishable with fine, which may extend to Rs. 50,000/-.

(D) To disclose receipt from transfer of property (sec. 319): Any money received by the directors from the transferee in connection with the transfer of the company's property or undertaking must be disclosed to the members of the company and approved by the company in general meeting. Otherwise, the amount shall be held by the directors in trust for the company. This money may be in the nature of compensation for loss of office but in essence may be on account of transfer of control of the company. But if it is bona fide payment of damages for the breach of contract, then it is protected by sec. 321(3). Even no director other than the managing director or whole time director can receive any such payment from the company itself.

(E) To disclose receipt of compensation from transferee of shares (Sec.320): If the loss of office results from the transfer (under certain conditions) of all or any of the shares of the company, its directors would not receive any compensation from the transferee unless the same has been approved by the company in general meeting before the transfer takes place. If the approval is not sought or the proposal is not approved, any money received by the directors shall be held in trust for the shareholders, who have sold their shares. Any such director, who fails to take reasonable steps as aforesaid, shall be punishable with fine, which may extend up to Rs. 2500/-.

(F) Duty to attend Board meetings: A number of powers of the company are exercised by the Board of directors in their meetings held from time to time. Although a director may not be able to attend all the meetings but if he fails to attend three consecutive meetings or all meetings for a period of three months whichever is longer, without permission of the Board, his office shall automatically fall vacant [Section 283(1)(g)].

(G) To convene statutory, Annual General meeting (AGM) and also extraordinary general meetings [Section 165,166 &169]

(H) To prepare and place at the AGM along with the balance sheet and profit & loss account a report on the company's affairs including the report of the Board of Directors (Section 173, 210 & 217).

(I) To authenticate and approve annual financial statement (Section 215).

(J) To appoint first auditor of the company (Section 224).

(K) To appoint cost auditor of the company (Section 233B).

(L) To make a declaration of solvency in the case of Members. voluntary winding up (Section 488).

2. General Duties:

(A) Duty of good faith: The directors must act in the best interest of the company. Interest of the company implies the interest of the present and future members of the company on the footing that company would be continued as going concern.

(B) Duty of care: A director must display care in performance of work assigned to him. He is, however, not expected to display an extraordinary care but that much care which a man of ordinary prudence would take in his own case. Any provision in the company's Articles or in any agreement that excludes the liability of the directors for negligence, default, misfeasance, breach of duty or breach of trust, is void. The company cannot even indemnify the directors against such liability.

(C) Duty not to delegate: Director being an agent is bound by the maxim .delegatus non potest delegate which means a delegatee cannot further delegate. Thus, a director must perform his functions personally. However, he may delegate his in certain conditions.

LIABILITES

1. Liability to the company:

(A) **Breach of fiduciary duty:** where a director acts dishonestly to the interest of the company, he will be held liable for breach of fiduciary duty. Most of the powers of directors are .powers in trust. and therefore, should be exercised in the interest of the company and not in the interest of the directors or any section of members.

(B) **Ultra vires acts:** Directors are supposed to act within the parameters of the provisions of the Companies Act, Memorandum and Articles of Association, since these lay down the limits to the activities of the company and consequently to the powers of the Board of directors. Further, the powers of the directors may be limited in terms of specific restrictions contained in the Articles of Association. The directors shall be held personally liable for acts beyond the aforesaid limits, being ultra vires the company or the directors.

(C) **Negligence:** As long as the directors act within their powers with reasonable skill and care as expected of them as prudent businessman, they discharge their duties to the company. But where they fail to exercise reasonable care, skill and diligence, they shall be deemed to have acted negligently in discharge of their duties and consequently shall be liable for any loss or damage resulting there from.

(D) **Mala fide acts:** Directors are the trustee for the moneys and property of the company handled by them, as well as exercise of the powers vested in them. If they dishonestly or in a mala fide manner, exercise their powers and perform their duties, they will be liable for breach of trust and may be required to make good the loss or damage suffered by the company by reason of such mala fide acts. They are also accountable to the company for any secret profits they might have made in course of performance of duties on behalf of the company. Directors can also be held liable for their acts of .misfeasance. i.e., misconduct or willful misuse of powers.

LIABILITY TO THIRD PARTIES

LIABILITY UNDER THE COMPANIES ACT:

(A) Prospectus: Failure to state any particulars as per the requirement of the section 56 and Schedule II of the act or mis-statement of facts in prospectus renders a director personally liable for damages to the third party. Section 62 provides that a director shall be liable to pay compensation to every person who subscribes for any shares or debentures on the faith of the prospectus for any loss or damage he may have sustained by reason of any untrue or misleading statement included therein.

(B) With regard to allotment: Directors may also incur personal liability for:

(a) Irregular allotment, i.e., allotment before minimum subscription is received (Section 69), or without filing a copy of the statement in lieu of prospectus (Section 70) - [Section 71(3)] - Under section 71(3), if any director of a company knowing contravenes or willfully authorizes or permits the contravention of any of the provisions of section 69 or 70 with respect to all allotment, he shall be liable to compensate the company and the allottee respectively for any loss, damages or costs which the company or the allottee may have sustained or incurred thereby.

(b) For failure to repay application monies in case of minimum subscription having not been received within 120 days of the opening of the issue: Under section 69(5) read with SEBI guidelines, in case moneys are not repaid within 130 days from the date of the issue of the prospectus, the directors of the company shall be jointly and severally liable to repay that money with interest at the rate of 6 % per annum on the expiry of 130th day. However, a director shall not be liable if he proves that the default in repayment of money was not due to any misconduct or negligence on his part.

(c) Failure to repay application monies when application for listing of securities are not made or is refused: Under section 73(2) . where the permission for listing of the shares of the company has not been applied or such permission having been applied for, has not been granted, the company shall forthwith repay without interest all monies received from the applicants in pursuance of the prospectus, and, if any such money is not repaid within eight days after the company becomes liable to repay, the company and every director of the company who is an officer in default shall, on and from the expiry of the eighth day, be jointly and severely liable to repay that money with interest at such rate, not less than four per cent and not more than fifteen per cent, as may be prescribed, having regard to the length of the period of delay in making the repayment of such money.

(C) Unlimited liability: Directors will also be held personally liable to the third parties where their liability is made unlimited in pursuance of section 322(i.e., vide Memorandum) or section 323(i.e., vide alterations of Memorandum by passing special resolution). By virtue of section 322, the Memorandum of a company may make the liability of any or all directors, or manager unlimited. In that case, the directors, manager and the member who proposes a person for appointment as director or manager must add to the proposal for appointment as a statement that the liability of the person holding the office will be unlimited. Notice in writing to the effect that the liability of the person will be unlimited must be given to him by the following or one of the following person, namely: the promoters, the directors, manager and officers of the company before he accept the appointment.

Further, in case of limited liability Company, the company may, if authorized by the articles, by passing resolution alter its Memorandum so as to render the liability of its directors or of any director or manager unlimited. But the alteration making the liability of director or directors or manager unlimited will be effective only if the concerned officer consents to his liability being made unlimited. This alteration also, unless specifically consented to by any or all directors will not have any effect until expiry of the current term of office.

(D) Fraudulent trading: Directors may also be made personally liable for the debts or liabilities of a company by an order of the court under section 542. Such an order shall be made by the court where the directors have been found guilty of fraudulent trading. Section 542(1), in this regard, provides that if in the course of the winding up of a company, it 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, the court, on the application of the Official Liquidator, or the liquidator or any creditor or contributory of the company may if it thinks it proper so to do, declare that any persons who were knowingly parties to the carrying on business in the manner aforesaid shall be personally responsible without any limitation of liability, for all or any of the debts or other liabilities of the company as the court may direct.

Further, section 542(3) provides that every person who was knowingly a party to the carrying on of the business in the manner aforesaid, shall be punishable with imprisonment for a term which may extend to two years, or with fine which may extend to fifty thousand rupees, or with both.

1. Liability for breach of warranty:

Directors are supposed to function within the scope of their authority. Thus, where they transact any business in resect of matters, ultra vires the company or ultra vires the articles, they may be proceeded against personally for any loss sustained by any third party.

2. Liability for breach of statutory duties:

The Companies Act, 1956 imposes numerous statutory duties on the directors under various sections of the Act. Default in compliance of these duties attract penal consequences. The various statutory penalties which directors may incur by reason of non-compliance with the requirements of Companies Act are referred to in their appropriate places.

3. Liability for acts of co-directors:

A director is the agent of the company except for matters to be dealt with by the company in general meeting and not of the other members of the Board. Accordingly, nothing done by the Board can impose liability on a director who did not participate in the Board's action or did not know about it. To incur liability he must either be a party to the wrongful act or later consent to it. Thus, the absence of a director from meeting of the Board does not make him liable for the fraudulent act of a co-director on the ground that he ought to have discovered the fraud.

4. Criminal liability:

Apart from the civil liability under that Act or under the common law, directors of a company may also incur criminal liability. Some of the provisions of the Companies Act, which make directors criminally liable, are as follows:

(i) Section 44(4) . filing of prospectus or statement in lieu of prospectus containing untrue statement. Penalty . Two years imprisonment or / and fine up to Rs. 50000.

(ii) Section 58A(5) . failure to repay deposits within the prescribed time limit as specified under sub sections (3) and (4) of section 58A. Penalty . Up to five years imprisonment and fine.

(iii) Section 58A(6) - Accepting deposits or inviting deposits in excess of the prescribed limits. Penalty . up to five years imprisonment and fine.

(iv) Section 63 - Issuing a prospectus containing untrue statement. Penalty. Imprisonment up to two years or/ and fine up to Rs. 50000.

(v) Section 68 - Knowingly making a false, deceptive or misleading statement and there by inducing persons to invest money. Penalty . Imprisonment up to five years or/ and fine up to Rs. 1,00,000.

(vi) Section 73 . Failure to repay excess application money. Penalty . Default in repayment of application money and interest is punishable with fine up to Rs.50000 but if repayment is not made within six months from the expiry of eight day, also with imprisonment for a term up to one year.

(vii) Section 84(3) . Fraudulently renewing a share certificate or issuing a duplicate share certificate. Penalty . Imprisonment up to six months or/ and fine up to Rs.1,00, 000.

(viii) Section 105 . Concealing name of creditor or misrepresenting the nature and the amount of the debt or claim of any creditor. Penalty . Imprisonment up to one year or/ and fine or both.

(ix) Section 202(1) . Undischarged insolvent acting as director. Penalty. Imprisonment up to two years or/ and fine up to Rs. 50000.

(x) Section 207 . Default in distributing dividends. Penalty . Simple imprisonment up to three years and fine up to Rs. 1000 for every day during which the default continues.

(xi) Section 209A . Failure to assist Registrar or any officer so authorized by Central Government in inspection of books of account, etc., of the company. Penalty . Imprisonment for a term not exceeding one year and fine to be not less than Rs. 50000.

(xii) Section 210(5) . Failure to lay balance sheet, profit & loss account, etc., at the annual general meeting. Penalty . Imprisonment up to six months or/ and fine up to Rs. 10000.

(xiii) Section 211(8) . Failure to comply with section 211 regarding form of balance sheet and matters to be stated therein and the content and disclosures to be made in the profit and loss account. Penalty. imprisonment up to six months or/ and fine up to Rs. 10000.

(xiv) Section 217(5) . Failure to attach to balance sheet a report of the Board of directors. Penalty. Imprisonment up to six months or / and fine up to Rs.20000.

(xv) Section 221(4) . Failure to supply information to auditors. Penalty. Imprisonment upto six months or / and fine up to Rs. 50000.

(xvi) Section 233B(11) . Audit of cost account of the company -Default in complying with the requirements of the section. Penalty . Imprisonment for a term that may extent to three years or with fine which may go up to Rs. 50000 or with both.

(xvii) Section 250(9) . Failure to honour restrictions upon shares and debentures imposed by the CLB. Penalty . Imprisonment up to six months or / and fine up to Rs. 50000.

(xviii) Section 293A(5) . Contribution to political party or for political purpose in contravention of section 293A. Penalty . Imprisonment up to three years and fine.

(xix) Section 295(4) . Grant of loan to directors without obtaining previous approval of the Central Government. Penalty . Simple imprisonment up to six months or fine up to Rs. 50000.

(xx) Section 299(4) . Failure to disclose interest in a contract or arrangement. Penalty . Fine which may extend to Rs. 50000.

(xxi) Section 308(3) . Failure to disclose shareholdings. Penalty . Imprisonment up to two years or / and fine up to Rs. 50000.

(xxii) Section 371 . Giving loans to other bodies corporate in excess of the limit prescribed under section 370. Penalty . Fine up to Rs. 50000 or simple imprisonment upto six months.

(xxiii) Section 407 . Any person, whose agreement has been terminated or set aside under section 402, knowingly acts as a managing or other director before expiry of a period of five years from the date of termination, without approval of the CLB, attracts criminal liability. Penalty . Imprisonment up to one year or / fine up to Rs. 50000 [Section 407(2)].

(xxiv) Section 488(3) . False declaration of company’s solvency. Penalty Imprisonment upto six months or / and fine up to Rs. 50000.

(xxv) Section 209(8) . Non-compliance with the requirement of maintenance of proper books of account. Penalty . fine not less than Rs. 50000 and also with imprisonment not exceeding one year for each offence committed.

RESTRICTIONS ON DIRECTORS

1. **Age :**A person who has reached the age of 65 cannot become director unless approved by ordinary resolution
2. **Number of directorship:** A person cannot become director in more than 15 companies at one time.
3. **Assignment of office:** A director cannot assign or transfer his office in favour of anyone else
4. **Office of profit:** A director cannot hold any office of profit except with the previous consent of the company accorded by special resolution
5. **Disclosure of interest (section299):** If a director is having interest in any contract entered into or to be entered into on behalf of the company, he is bound to disclose his interest through a notice to the board of directors.
6. **Loan (section 295):** No director shall obtain any loan from the company without the previous approval of the central government.

MANAGING DIRECTOR

According to section 2 (26) of the Act, the Managing director is a director who by virtue of an agreement with the company or of a resolution passed in the general meeting or by board of directors, by virtue of a memorandum of articles is "entrusted with substantial powers of the management which would not otherwise be exercisable by him".

DISQUALIFICATIONS OF A MANAGING DIRECTOR (SEC. 267).

No company can employ, a person as its managing director who

(a) Is an undischarged insolvent, or has at any time been adjusted an insolvent.

(b) Suspends, or has at any time suspended, payment to his creditors, or makes, or has any time made, a composition with them or

(c) Is, or has at any time been, convicted by a court of an offence involving moral turpitude.

APPOINTMENT OF MANAGING DIRECTOR

Companies having a paid up share capital of Rs.5 crores shall have a managing or whole time director or manager. Various provisions in the Act in connection with the appointment of the Managing director; (sec. 269(1)).

The rules relating to the appointment or reappointment of Managing or Whole- Time Directors cannot be amended without the approval of the Central Government. (sec.268).

RESTRICTIONS ON APPOINTMENT OF MANAGING DIRECTORS

(1) No company shall appoint an individual as its Managing Director for a term exceeding five years at a time.

(2) Whereat the commencement of this Act. (Companies Act, 1956), any person is holding the office either of Managing director or Manager in more than two companies. He shall within one year choose not more than two of those companies as companies in which he wishes to continue to hold office. (sec.316 (3)).

(3) According to sec.269 the appointment of a Managing Director can be made only with the approval of the Central Government which will not be granted unless the Central Government is satisfied that (a) It is in the interest of the company to have a Managing director, (b) the person is a fit and proper person. (c) the appointment is not against public interest and (d) the terms and conditions of appointment are fair and reasonable.

The restrictions do not apply to private companies unless it is a subsidiary of a public company.

POSITION OF A MANAGING DIRECTOR IN THE COMPANY

The idea of appointing a Managing Director is to place one of the directors in charge of the day-to-day administration and to relieve the board of looking after the routine administration. The Managing director works in twofold capacities. Firstly, he is a director and has a seat in the board, and secondly as a manager he is the head of the administrative section and is in charge of the execution of the policies of the board.

POWERS OF MANAGING DIRECTOR

1. Managing directors exercise such powers as are delegated to him by the board. The powers are mentioned (1) in the agreement with the company or (2) in the resolution passed by the company General Meeting or by the Board or (3) in the memorandum or Article of Association.
2. A Managing director is entrusted with substantial powers of management. His powers do not include the administrative Acts of a routine nature when so authorized by the Board such as power to affix the common seal of the company to any document or to draw or endorse any cheque on the account of the company in the blank or draw and endorse negotiable instrument etc.

   Section 2 (26) says that the power as would be exercised by the Managing director would be subject to the superintendence, control and director of the Board of directors.

WHOLE TIME DIRECTOR

The term Whole time Director has not been defined in the act though it has been several times used side by side with the term of Managing director in some important sections of the act. Whole time director is an employee director with the company. He does not exercise substantial powers of management but performs important administrative functions.

MANAGER

According to section 2 (26) manager means an individual, who, subject to the superintendence, control and direction of the Board of directors, has the management of the whole or substantially the whole of the affairs of a company, and includes a director or any other person occupying the position of a manager by whatever names called and whether under a contract of service or not. He acts under the control and direction of the Board of directors. He manages the whole or substantial part of the affairs of the company. He may or may not be under a contract of service.

COMPANY MEETINGS

The company is an artificial person created by law having a separate entity distinct from its members. Being an artificial person, it cannot take decisions on its own. It has to take decisions on matters relating to its well being by way of resolutions passed at properly constituted and convened meetings of its shareholders or directors. The decisions about a company's management are taken by the directors in their meetings and they are to be ratified in the general meetings of the company by the shareholders. Generally, the purpose of a meeting is to consider issues of common interests to its attendants.

KINDS OF MEETINGS

The meetings of a company are of four kinds:

1. Meetings of the shareholders
    (i) General meetings
    (ii) Class meetings
2. Meetings of the Directors
3. Meetings of the Creditors
4. Meetings of the Debenture holders

STATUTORY MEETING

Every public company limited by shares and every company limited by guarantee and having a share capital, shall, within a period of not less than one month nor more than six months from the date on which the company is entitled to commence business hold a general meeting of the members of the company. This meeting is called 'the statutory meeting'. [Sec. 165 (1)] A meeting held prior to the statutory period of one month from the date of entitlement of a company to commence business cannot be called the statutory meeting. The notice for such a meeting should state it to be statutory. The statutory meeting is held only once in the life time of a company.

Private companies, public companies limited by guarantee and not having a share capital and unlimited companies are not required to hold the statutory meeting. However, a private company which becomes a public company by the application of Sec. 43 will have to comply with the provisions of the Act which are applicable to public limited companies from the date of its becoming a public limited company. A private company can commence business on the date of its incorporation. If the date of its becoming a public company is within 6 months of its incorporation, it must hold a statutory meeting in accordance with the provision of Section 165 (1). If it becomes a public company after 6 months of its incorporation, it is not required to hold the statutory meeting.

NOTICE

The company must give notice to its members 21 days before the holding of the statutory meeting. The notice convening the statutory meeting must specifically state that the meeting is the statutory meeting. The time, date and place of the meeting must be mentioned in the notice. However, a shorter notice may be sufficient if consent is accorded by the members of the company :

(a) If the company has a share capital, holding not less than 95% of such part of the paid up share capital of the company as gives a right to vote at the meeting.

(b) If the company has no share capital, holding not less than 95% of the total voting power exercisable at the meeting.

STATUTORY REPORT

The Board of Directors is required to prepare a report which is known as the 'statutory report" and must send this report to the members at least 21 days before the day on which the meeting is to be held [Section 165(2)]. If the report is sent later than is required, it will be deemed to have been duly forwarded if it is so agreed to by all the members entitled to attend and vote at the meeting. Thus the delay in sending the report can be condoned by unanimous consent of all the members present at the meeting. The statutory report is required to be certified as correct by at least two directors of the company, one of whom must be a Managing Director, if there is any. Thereafter the auditor must certify the report to be correct in so far as it relates to the shares allotted by the company, the cash received in respect of such shares and the receipts and payments of the company [Section 165(4)]. A copy of the report must be sent to the Registrar also [Section 165(5)].

CONTENTS OF STATUTORY REPORT

The statutory report shall set out:

(a) The total number of shares allotted, distinguishing those allotted as fully or partly paid-up otherwise than in cash, the extent to which they are partly paid up and the consideration for which they have been allotted.

(b) The total amount of cash received by the company in respect of all the shares allotted.

(c) An abstract of the receipts and payments made there out up to a date within 7 days of the date of the report.

(d) The name, address and occupations of the directors of the company and of its auditors and also if there be any, of its manager and secretary.

(e) The particulars of any contract which , or the modification or the proposed modification of which is to be submitted to the meeting for its approval.

(f) The extent to which each underwriting contract (if any) has not been carried out and the reason therefore.

(g) The arrears due on cash from every director and from the manager.

(h) Particulars of any commission or brokerage paid or to be paid in connection with the issue or sale of shares or debentures to any director.

PROCEDURE AT THE MEETING

A list showing the names, addresses and occupation of the members of the company and the number of shares held by them must be produced by the Board of Directors at the commencement of the statutory meeting. The list is to remain open and accessible to any member of the company during the continuance of the meeting [Section 165 (6)]. It is to be noted that the members of the company present at the meeting are at liberty to discuss any matter relating to the formation of the company or arising out of the statutory report, whether previous notice has been given or not but one resolution may be passed of which notice has not been given in accordance with the provisions of Companies Act. [Sec.165 (7)]

ADJOURNMENT OF STATUTORY MEETING

The meeting may adjourn from time to time and at any adjourned meeting any resolution of which notice has been given in accordance with the provisions of the Companies Act may be passed and the adjourned meeting will have the same power as an original meeting. [Sec. 165(8)]

PENALTY

If any default is made in complying with the above provisions, every director or other officer of the company who is in default shall be liable to a fine which may extend to Rs. 500. Besides, if default is made in delivering the statutory report to the Registrar or in holding the statutory meeting, the Court may order the compulsory winding up of the company.[Sec. 433 (b)]

OBJECTS

The obvious purpose of the statutory meeting with its preliminary report is to put the shareholders of the company as early as possible in possession of all the important facts relating to the new company what shares have been taken up, what moneys received, what contracts entered into, what sums spent on preliminary expenses, etc. Furnished with these particulars the shareholders are to have an opportunity of meeting and discussing the whole situation in the management methods and prospects of the company. If the shareholders fail to do so, they have only themselves to blame.

ANNUAL GENERAL MEETING

Every company must in each year hold in addition to any other meeting a general meeting, as its annual general meeting and must specify the meeting as such in the notices calling it [Section 166 (1)]. The annual general meeting is to be held in addition to any other general meeting that might have been held in a year. It appears that holding of an annual general meeting in every calendar year is a statutory necessity. Calendar year is to be calculated from 1st January to 31st December and not twelve months from the date of incorporation of the company.

FIRST ANNUAL GENERAL MEETING

A company must hold its first annual general meeting within a period of not more than 18 months from the date of its incorporation and if such general meeting is held within that period, it shall not be necessary for the company to hold any annual general meeting in the year of its incorporation or in the following year [Section 166(1)]. For example a company is incorporated in October 1994. Its first annual general meeting is required to be held within 18 months from the incorporation, i.e. up to March 1996 and if such a meeting is held within this period, no other meeting will be necessary either for 1995 or 1996.

SUBSEQUENT ANNUAL GENERAL MEETING

As already discussed a company is required to hold an annual general meeting in each year. Where a meeting called and held on a day in one year is adjourned to a date in the next year and held on that date, the meeting held on the latter date is not a different meeting and does not comply with the requirements of Section 166. However, the gap between one annual general meeting and the next should not be more than fifteen months.

POWER TO CONVENE AN ANNUAL GENERAL MEETING

The proper authority to convene an annual general meeting is the Board of Directors, and if the managing director, manager, secretary or other officer calls a meeting without such authority, it will not be effectual unless the Board ratifies the act before the meeting is held.

NOTICE

A public company must give at least 21 days notice for convening any general meeting including annual general meeting. Annual general meeting may be called after giving a shorter notice than 21 days if it is so agreed by all the members entitled to vote in the meeting (Section 171). In calculating 21 days, the date on which the notice is served and the day of the meeting are excluded.

DATE, TIME AND PLACE OF HOLDING THE ANNUAL GENERAL MEETING

Every annual general meeting shall be called at any time during the business hours, on a day that is not a public holiday. It shall be held either at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated [Section 166(2)]. The Central Government may exempt any class of companies from the provisions of Sec. 166 subject to such conditions as it may impose.

(a) A public company or a private company which is a subsidiary of a public company, may by its Articles fix the time for its annual general meetings and may also by a resolution passed in preceding annual general meeting fix the time for its subsequent annual general meetings and

(b) A private company which is not a subsidiary of a public company may in like manner and also by a resolution agreed to by all the members thereof, fix the time as well as the place for its annual general meetings [Sec. 166(2)]

ADJOURNMENT

Where an annual general meeting is held but adjourned, the adjourned meeting is nothing but continuance of the earlier meeting and therefore if in the adjourned meeting the Balance Sheet and the Profit and Loss Account of the company are laid and adopted and thereafter sent to the Registrar, Section 220(I) is not violated.

HOLDING OF ANNUAL GENERAL MEETING WHERE THE ANNUAL ACCOUNTS ARE NOT READY

According to Central Government instructions, in case the annual accounts are not ready for laying at the appropriate annual general meeting, the company must hold the annual general meeting within the time limit, transact all business other than the consideration of the accounts, announce when the accounts are expected to be ready for laying and pass a suitable resolution adjourning the said annual general meeting to a specific date or to a date to be specified later on. Thus the company cannot take the plea that the annual general meeting was not held because the accounts were not ready.

POWER OF CENTRAL GOVERNMENT TO CALL ANNUAL GENERAL MEETING

The Central Government may, on the application of any member of the company, call or direct the calling of a general meeting of the company. However, it is to be noted that the Court has no power to call such meeting. A general meeting held in pursuance of this order will be deemed to be an annual general meeting of the company. The Central Government may direct that only one member of the company present in person or by proxy shall be deemed to constitute a meeting. [Section 167]

PENALTY

If a default is made in holding an annual general meeting in accordance with the above provisions or in complying with the directions given by the Central Government, the company and every officer of the company who is in default shall be punishable with fine which may extend to Rs. 5000 and in the case of a continuing default, with a further fine which may extend to Rs. 250 for every day after the first during which the default continues. (Section 168)

IMPORTANCE

It is the annual general meeting at which the shareholders can exercise control over the affairs of the company. At this meeting some directors retire and come up for re-election and thereby the shareholders find an opportunity to refuse to re-elect a director of whose action and policy they disapprove. Appointment of auditors is also made at this meeting. Annual accounts are presented at this meeting for the consideration of the shareholders and the shareholders can ask any question relating to the account. It is at this meeting that dividends are declared. At this meeting the shareholders can discuss any other matters relating to the company's business.

EXTRA ORDINARY GENERAL MEETING

Regulation 47 of the Table A provides that all general meetings other than annual general meetings shall be called extraordinary general meetings. An extraordinary general meeting is called to consider those transactions or business which cannot be postponed till the next annual general meeting. Hence, it is a meeting of a company which is held between two consecutive annual general meetings for transacting some urgent or special business. An extraordinary general meeting may be convened:

1. By the Board of Directors on its own or on the resolution of members; or
2. By the requisitionists themselves on the failure of the Board to call the meeting ; or
3. By the Central Government.

1 EXTRAORDINARY MEETING CONVENED BY THE BOARD OF DIRECTORS

(A) On its own

Regulation 48(1) of Table A provides that the board may, whenever it thinks fit, call an extraordinary general meeting. An extraordinary general meeting may be convened by the Board of Directors if some business of special importance requires the approval of the members and which in the opinion of the Board of Directors cannot be postponed till the next annual general meeting. The directors can call an extraordinary general meeting by passing a resolution in a properly convened board meeting or by a circular resolution. Regulation 48(2) of Table A provides that "If at any time, they are not present within India, the number of directors capable of acting and forming a quorum, any director or any two members of the company may call an extraordinary general meeting in the same manner, as nearly as possible, as that in which such a meeting may be called by the Board”.

(B) On the requisition of members

The directors are bound to call an extraordinary general meeting of the company if the requisition is made :

(i) in the case of a company having a share capital, by the holders of at least one-tenth paid up capital having the right to vote on the matter of requisition ; or

(ii) in the case of a company not having a share capital, by members representing not less than one-tenth of the total voting power in regard to the matter of requisition.

The Board of Directors is under a legal obligation to proceed within 21 days of the deposit of the requisition to call a meeting. The meeting shall be held within 45 days of such deposit of the requisition with the company [Sec. 169(6)]. On receipt of the requisition, the Board shall send out notices for the meeting giving not less that 21 days' time.

3. Extraordinary meeting covered by the Central Government

If due to any reason it is impracticable to call or conduct an extraordinary general meeting, the Central Government may, either on its own or on the application of any director or any member who would be entitled to vote, order a meeting to be called, held and conducted in such manner as the Central Government thinks fit and may give such directions as it thinks expedient, including a direction that one member present in person or by proxy shall be deemed to constitute a meeting. Any meeting called, held and conducted in accordance with any such order of the Central Government will, for all purposes, be deemed to be a meeting of the company duly called, held and conducted. The word 'impracticable' may be taken to mean impossible to hold a peaceful or useful meeting. It has been held that the word 'impracticable' should be taken to mean impractical from a reasonable point of view.

CLASS MEETINGS

Class meetings are the meetings of the shareholders and the creditors. Class meetings are held to pass resolutions which will bind only the members of the particular class concerned. According to regulation 3(1), if the rights attached to any class of shares are to be varied, it can be done with the consent of the holders of 3/4 of the issued shares of that class in a separate meeting of that class of holders. Similarly, under Sec. 394, where a scheme of arrangement or compromise is proposed, the meetings of several classes of shareholders and creditors are required to be held. Class meetings can only be attended by the members of that class. Whenever it is necessary to alter or change the rights or privileges of a class as provided by the Articles, a class meeting must be called.

6.7 REQUISITES OF A VALID MEETING

A meeting to be in order must fulfill certain requirements.

1. Proper Authority

The Board of Directors is the proper authority to convene a general meeting of a company and for this purpose the board should pass a resolution at a duly convened meeting of the board. However, if the board fails to call a general meeting of the company, the members or the Central

Government or the Central Government may call such a meeting. Some defects in appointment or qualification of the directors present at the meeting of the board will not necessarily be fatal to the validity of the resolution passed at the meeting provided the board has acted bonafide.

2. Notice of Meetings (Sec. 171)

A proper notice of the meetings must be given to the members of the company. The notice must be given 21 days before the date of the meeting. The period of 21 days excludes the day of service of the notice and also the day on which the meeting is to be held. The length of the notice may be waived :

(a) in the case of an annual general meeting by the consent of all members;

(b) in the case of any other meeting by the consent of the holders of not less than 95% of the paid-up share capital or the total voting power where the company has no share capital.

Notice to whom (Sec. 172)

The notice is required to be given to

(a) all the members of the company who are entitled to vote on the matters which are proposed to be dealt with at the meeting ;

(b) all the persons who are entitled to a share in consequences of the death and insolvency of a member ;

(c) the auditor or auditors of the company. Deliberate omission to give notice of the meeting to members or to a single member will make the meeting invalid, but an accidental omission to give notice to or the non-receipt of notice by any member will not invalidate the proceedings at the meeting [Sec. 172 (3)].

CONTENTS OF NOTICE

Every notice of a meeting is required to specify the place and the day and hours of the meeting and must contain a statement of the business to be transacted at the meeting. If the time of holding meeting and other essential particulars are not specified in the notice, the meeting will be invalid and all resolutions passed at the meeting will be of no effect. The notice of general meeting must contain a statement of the business to be transacted at the general meeting of the company. The business to be transacted at a meeting may be general business or special business.

Section 173 provides (a) in the case of an annual general meeting, all business to be transacted at the meeting will be deemed special except the business relating to the consideration of accounts, Balance Sheet and reports of the Board of Directors and auditors, the declaration of dividends, the appointment of directors in the place of those retiring and the appointment of and the fixing of the remuneration of the auditors and (b) in the case of any other meeting, all business will be deemed special. If any special business is to be transacted at an annual general meeting a statement to that effect must be annexed to the notice of the meeting. The statement must set out all material facts concerning each item of business including in particular the nature of the concern or interest therein of every director or other managerial personnel. Thus every notice calling a meeting is required to specify the business to be transacted at the meeting. A notice of meeting must give a sufficiently full and frank disclosure to the members of the fact upon which they are asked to vote otherwise the resolution passed at the meeting will be invalid.

3. Quorum

Quorum means the minimum number of members that must be present at the meeting. The quorum is generally fixed by the company's article. Unless the articles provide for a large number, five members personally present in the case of a public company (other than a public company which has become such by virtue of Section 43-A) and two members personally present in the case of any other company will be the quorum for a meeting of the company. If within half an hour from the time appointed for holding a meeting of the company, a quorum is not present, the meeting will stand dissolved if it was called upon the requisition of members but in any other case it stands adjourned to the same day in the next week, at the same time and place or to such other day as the Board may determine. If at a adjourn meeting also the quorum is not present within half an hour from time appointed for holding the meeting the members present sufficient will be quorum [Section 174(5)]. Section 174 clearly indicate that the meeting must be attended by more than one member so as to constitute it as a meeting. But a few exceptions to this general rule may also be noted :

(a) Under Section 167, the Central Government may, on the application of any member of the company, call a general meeting of the company and may direct that even one member of the company present in person or by proxy shall be deemed to constitute a meeting.

(b) Under Section 186, the Central Government may call a meeting of the company other than an annual general meeting and may give direction that even one member of the company present in person or by proxy shall be deemed to constitute a meeting.

(c) In *East v. Bennet Bros. Ltd.,* one shareholder held all these preference shares in the company. A meeting of preference shareholders attended by him only was held to be a valid meeting.

4. Chairman of meeting

Before a meeting of a company can start its business, it is required to have a Chairman. It is the Chairman who is to preside at the meeting of the company. He is to conduct the meeting and to maintain the order. It is the Chairman who is to put up the resolution, count the votes and declare the result. Usually the articles provide for the appointment of a Chairman but if there is no provision in the articles to this effect, the members present in the meeting shall elect one of themselves to be the Chairman of such meeting on a show of hands [Section 175(1)]. If a poll is demanded on the election of the Chairman, it shall be taken forthwith [Section 175(2)] and in such a case the Chairman elected on the show of hands will exercise all the powers of the Chairman. If some other person is elected Chairman as a result of the poll, he will be the Chairman for the rest of the meeting [Section 175(3)]. He can adjourn the meeting in the event of disorder but he should do so only as a last resort, if his attempts to restore order have failed. A Chairman is not entitled to close the meeting prematurely and if he does so, a new Chairman may be elected and the meeting of the company may be continued. However, it is to be noted that where a meeting is called but it is not held due to pandemonium and confusion and a note to this effect is made in the minute book by the Chairman, the shareholders cannot elect a new Chairman because in such a case no meeting has actually been commenced and consequently no question of dissolving the meeting permanently by the Chairman arises.

Duties of the Chairman

(a) He must take care that the minority is not oppressed in any way.

(b) He must give the members who are present a reasonable opportunity to discuss any proposed resolution and it must be ensured that all the views are adequately aired. But at the expiry of a reasonable time, if he thinks fit, he should stop the discussion on any resolution.

(c) He must see that the meeting is properly convened and constituted i.e. proper notice was given to every person entitled to attend the meeting and his own appointment is in order. It is the Chairman who is to see whether a quorum is present before proceeding with the business.

(d) The Chairman must conduct the proceedings in accordance with the provisions of the Act, the companies Articles of Association or Table A or in the absence thereof, the common law relating to the meetings.

(e) He should adjourn the meeting when it is impossible, by reason of disorder or other like cause, to conduct the meeting and complete its business. He must not use this power in a malafide manner.

(f) He must take care that the opinion of the meeting is properly ascertained with regard to the questions before it. He must do so by putting the resolution in a proper form before the members and then declaring the result.

(g) He must keep order in the meeting. He must decide all questions which arise at the meeting and which require decision at the time.

(h) He should exercise his casting vote, if any, provided by the articles for the benefit of the company.

(i) The minutes of the meeting should be properly recorded and signed by the chairman.

MINUTES OF THE MEETING:

Every company must keep a record of all proceedings of every general meeting and of all proceedings of every meeting of its Board of Directors and of every committee of the board. These records are known as minutes and the books in which these records are written are called 'minute books'.

RULES OF KEEPING MINUTES (SEC. 193-196)

(a) Within 30 days of every such meeting, entries of the proceedings must be made in the books kept for that purpose. [Sec. 193 (1-A)]

(b) Each page of minutes book which records proceedings of a board meeting must be initialled or signed by the Chairman of the same meeting or the next succeeding meeting. In the case of minutes of proceedings of a general meeting, each page of the minute book must be initialled or signed by the Chairman of the same meeting.

(c) The minutes of each meeting must contain a fair and correct summary of the proceedings at the meeting.

(d) All the appointments of officers made at any of the meetings aforesaid must be included in the minutes. In the case of a meeting of the Board of Directors or of a committee of the board, the minutes must contain the names of the directors present at the meeting and the names of the directors dissenting from or not concurring in the resolution passed at the meeting [Sec. 193 (4)].

(e) The Chairman may exclude from the minutes, matters which are defamatory of any person, irrelevant or immaterial to the proceedings or which are detrimental to the interests of the company. Minutes of meetings kept in accordance with the above provisions are evidence of the proceedings recorded therein.

(f) The minutes books must be kept (i) at the registered office of the company; and (ii) be open during business hours to the inspection of any member without charge subject to reasonable restrictions but at least two hours each day must be allowed for inspection.

PENALTY

If default is made in complying with the provision of Section 193 in respect of any meeting, the company and every officer of the company who is in default shall be punishable with fine which may extend to Rs. 50.

VOTING AND ROLL

A vote is the formal expression of the will of the members of the house either for or against a proposal. The matters proposed and duly recommended in a general meeting of the company are decided by the voting of the members of the company. The procedure of voting is regulated by the Articles subject to the provisions of the Act. Members holding any share capital of the company have the right to vote on every motion placed before the company. However, the members holding preference shares can vote only on those motions which affect the rights attached to their capital. Share warrant holders, executors of a deceased member, receiver of an insolvent member cannot exercise any voting right unless registered as members. The voting rights of an equity shareholder at a poll are in proportion to his share of the paid up equity capital.

Voting may take place in either of the following two ways :

1. Voting by a show of hands At any general meeting, unless the Articles otherwise provide, a resolution put to the vote is in the first instance decided by a show of hands except when a poll is demanded [Sec. 177]. While voting by a show of hands, one member has one vote irrespective of the shares held by him. Proxies cannot be counted unless the Articles otherwise provide. The Chairman will count the hands raised and will declare the result accordingly. Chairman's declaration of the result of voting by the show of hands to be conclusive evidence [Sec. 178].

2. Voting by poll [Sec. 179] If there is dissatisfaction among the members about the result of voting by the show of hands, they can demand a poll. 'Poll' means counting the number of votes cast for and against a motion. The voting rights of a member on a poll shall be in proportion to his share of the paid-up equity capital of the company. Before or on the declaration of the result of voting on any resolution by a show of hands, a poll may be ordered to be taken by the Chairman of the meeting of his own motion, and shall be ordered to be taken by him on a demand made in that behalf by the person or persons specified below :

(a) In the case of a public company having a share capital, by any member or members present in person or by proxy and holding shares in the company:

  (i) which confer a power to vote on the resolution not being less than one tenth of the total voting power in respect of the resolution, or

  (ii) on which an aggregate sum of not less than fifty thousand rupees has been paid-up,

(b) In the case of a private company having a share capital, by one member having the right to vote on the resolution and present in person or by proxy if not more than seven such members are personally present, and by two such members present in person or by proxy, if more than seven such members are personally present,

(c) In the case of any other company, by any member or members present in person or by proxy and having not less than one tenth of the total voting power in respect of the resolution [Sec. 179(1)].

The demand for a poll may be withdrawn at any time by the person or persons who made the demand. [Sec. 179(2)]. The provisions of Section 179 apply to a private company, which is not a subsidiary of a public company unless the articles provide otherwise. A poll demanded on the question of adjournment or the election of the Chairman shall be taken forth with. A poll demanded on any other question shall be taken at such time not being later than forty eight hours from the time when the demand was made, as the Chairman may direct. Where a poll is taken, the meeting will be deemed to continue until the ascertainment of the result of the poll. Even a voter who was not present at the meeting when the poll was demanded to be taken, may vote personally in a poll held on the next day.

The Chairman of the meeting shall have the power to regulate the manner in which a poll shall be taken [Sec. 185(1)]. Where a poll is to be taken, the Chairman of the meeting shall appoint two scrutiniser to scrutinise the votes given on the poll and to report thereon to him [Sec. 184 (1)]. Of the two scrutiniser, one shall always be a member present at the meeting, provided such a member is available and willing to the appointed [Sec.184 (3)]. The Articles of a company may provide that no member shall exercise any voting right in respect of any shares registered in his name on which calls or other sums presently payable by him have not been paid (Sec. 181).

PROXIES

A meeting has right to vote either in person or by proxy. Any member of a company who is entitled to attend and vote at a meeting of the company can appoint another person (whether a member or not) as his proxy to attend and vote instead of himself but a proxy so appointed will have no right to speak at the meeting. Unless the articles otherwise provide, a proxy will not be allowed to vote except on a poll. A member of a private company, unless the articles provide otherwise is not entitled to appoint more than one proxy to attend on the same occasion. Besides unless the articles provide otherwise a member of a company not having a share capital is not entitled to appoint a proxy. The instrument appointing a proxy is required to be in writing and signed by the appointor or his attorney duly authorized in writing. A proxy is revocable but it should be revoked before the proxy has voted. If the member who has appointed a proxy personally attends and votes at the meeting, the proxy is revoked by such conduct of the member [Section 189]. Death of the member who has appointed a proxy revokes the authority of his proxy but if the company has no notice of such death, then the vote given by the proxy will be valid.

RESOLUTIONS

The decisions of a meeting take the form of resolutions carried by a majority of votes. A question on which a vote is proposed to be taken is called a 'motion'. Once a 'motion' has been put to the members and they have opted in favour of it, it becomes a resolution. A resolution may, thus, be defined as the formal decision of a meeting on a particular proposal before it.

TYPES OF RESOLUTIONS

Resolutions are of the following types :

1. Ordinary Resolutions ;
2. Special Resolutions ; and
3. Resolutions requiring special notice.

ORDINARY RESOLUTION

At a general meeting of which notice has been given, if votes cast in favour of the resolution by members exceed the votes, if any, cast against the resolution by members, the resolution so passed is an ordinary resolution [Sec. 189(1)] Unless the Companies Act or the memorandum or the articles expressly require a special resolution or resolution requiring special notice, an ordinary resolution is sufficient to carry out any matter.

TRANSACTIONS WHERE ORDINARY RESOLUTION IS REQUIRED

Important matters for which an ordinary resolution is enough are as follows :

(i) Issue of shares at a discount (Sec. 79)

(ii) Alteration of the share capital (Sec. 94)

(iii) Approval of the statutory report (Sec.165)

(iv) The consideration of accounts, the Balance Sheet and the report of the Board of Directors and of the auditors (Sec. 210)

(v) Appointment of auditors and fixation of their remuneration [Sec. 224(1)].

(vi) Appointment of the first directors who are to retire by rotation [Sec. 255(1)].

(vii) Increase or decrease in the number of directors within the limits prescribed by the Articles [Sec. 258].

(viii) Adoption of the appointment of sole selling agents [Sec. 294].

(ix) Removal of a director and appointment of another director in his place [Sec. 284(1)].

(x) Declaration of dividend [Sec. 205].

(xi) Appointment of liquidator in case of voluntary winding up and fixing his remuneration [Sec. 490(1)].

(xii) To rectify the name of company [Sec. 22].

(xiii) To cancel or redeem debentures [Sec. 21].

(xiv) To cancel directors by rotation [Sec. 256].

(xv) To approve the remuneration of directors [Sec. 309].

(xvi) To fill the vacancy in the office of Liquidator [Sec. 492].

SPECIAL RESOLUTION

The resolution is a special resolution, if

(i) the intention to propose the resolution as a special resolution has been duly specified in the notice calling the general meeting ;

(ii) the notice required has been duly given of the general meeting; and

(iii) the votes cast in favour of the resolution by members are three times the number of the votes, if any, cast against the resolution by the members [Sec. 189 (2)].

A copy of the special resolution must be filed with the Registrar within 30 days of its passing.

SPECIAL RESOLUTION MATTERS

In addition to the matters given in the articles of the company, the Companies Act specifies certain matters for which a special resolution must be passed ; for example,

(i) to alter the memorandum of the company [Sec. 17];

(ii) to alter the articles of the company [Sec. 31];

(iii) to issue further shares without pre-emptive rights [Sec. 81];

(iv) for creation of a reserve capital [Sec. 99];

(v) to reduce the share capital [Sec. 100];

(vi) to pay interest out of the capital to members [Sec. 208],

(vii) for authorising a director to hold an office or place of profit [Sec.314];

(viii) for voluntary winding-up of a company [Sec. 484].

RESOLUTIONS REQUIRING SPECIAL NOTICE

A resolution requiring special notice is not an independent class of resolutions. It is a kind of ordinary resolution, with the only difference that here the mover of the proposed resolution is required to give a special notice of 14 days to the company before moving the resolution, and the company shall then immediately give its members notice of the resolution in the same manner as it gives notice of the meeting. If that is not practicable, the company shall give not less than seven days notice before the meeting either by advertisement in a newspaper or in any other mode allowed by the articles (Sec. 190). In addition to the purposes enumerated in the articles requiring special notice, under the Act, special notice has to be given for the following matters :

(a) for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor and for a resolution providing expressly that a retiring auditor shall not be re-appointed (Sec. 225).

(b) for certain persons who shall not be eligible for appointment as directors whose period of office is liable to determination by retirement of directors by rotation (Sec. 261).

(c) for removing a director before the expiry of his period of office; and

(d) of any resolution to appoint a director in place of a director so removed (Sec. 284).

WINDING UP OF A COMPANY

Winding up of a company is defined as a process by which the life of a company is brought to an end and its property administered for the benefit of its members and creditors. An administrator, called the liquidator, is appointed and he takes control of the company, collects its assets, pays debts and finally distributes any surplus among the members in accordance with their rights. At the end of winding up, the company will have no assets or liabilities. When the affairs of a company are completely wound up, the dissolution of the company takes place. On dissolution, the company's name is struck off the register of the companies and its legal personality as a corporation comes to an end.

The procedure for winding up differs depending upon whether the company is registered or unregistered. A company formed by registration under the Companies Act, 1956 is known as a registered company. It also includes an existing company, which had been formed and registered under any of the earlier Companies Acts.

WINDING UP A REGISTERED COMPANY

The Companies Act provides for two modes of winding up a registered company.

Grounds for Compulsory Winding Up or Winding up by the Tribunal

- If the company has, by a Special Resolution, resolved that the company be wound up by the Tribunal.
- If default is made in delivering the statutory report to the Registrar or in holding the statutory meeting. A petition on this ground may be filed by the Registrar or a contributory before the expiry of 14 days after the last day on which the meeting ought to have been held. The Tribunal may instead of winding up, order the holding of statutory meeting or the delivery of statutory report.
- If the company fails to commence its business within one year of its incorporation, or suspends its business for a whole year. The winding up on this ground is ordered only if there is no intention to carry on the business and the Tribunal's power in this situation is discretionary.
- If the number of members is reduced below the statutory minimum i.e. below seven in case of a public company and two in the case of a private company.
- If the company is unable to pay its debts.
- If the tribunal is of the opinion that it is just and equitable that the company should be wound up.
- Tribunal may inquire into the revival and rehabilitation of sick units. It its revival is unlikely, the tribunal can order its winding up.
- If the company has made a default in filing with the Registrar its balance sheet and profit and loss account or annual return for any five consecutive financial years
- If the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality.

The petition for winding up to the Tribunal may be made by :-

- The company, in case of passing a special resolution for winding up.
- A creditor, in case of a company's inability to pay debts.
- A contributory or contributories, in case of a failure to hold a statutory meeting or to file a statutory report or in case of reduction of members below the statutory minimum.
- The Registrar, on any ground provided prior approval of the Central Government has been obtained.
- A person authorised by the Central Government, in case of investigation into the business of the company where it appears from the report of the inspector that the affairs of the company have been conducted with intent to defraud its creditors, members or any other person.
- The Central or State Government, if the company has acted against the sovereignty, integrity or security of India or against public order, decency, morality, etc.

Voluntary Winding Up of a Registered Company

When a company is wound up by the members or the creditors without the intervention of Tribunal, it is called as voluntary winding up. It may take place by:-

- By passing an ordinary resolution in the general meeting if :- (i) the period fixed for the duration of the company by the articles has expired; or (ii) some event on the happening of which company is to be dissolved, has happened.
- By passing a special resolution to wind up voluntarily for any reason whatsoever.

Within 14 days of passing the resolution, whether ordinary or special, it must be advertised in the Official Gazette and also in some important newspaper circulating in the district of the registered office of the company.

The Companies Act (Section 484) provides for two methods for voluntary winding up:-

Members' voluntary winding up

It is possible in the case of solvent companies which are capable of paying their liabilities in full. There are two conditions for such winding up:-

- A declaration of solvency must be made by a majority of directors, or all of them if they are two in number. It will state that the company will be able to pay its debts in full in a specified period not exceeding three years from commencement of winding up. It shall be made five weeks preceding the date of resolution for winding up and filed with the Registrar. It shall be accompanied by a copy of the report of auditors on Profit & Loss Account and Balance Sheet, and also a statement of assets and liabilities upto the latest practicable date; and
- Shareholders must pass an ordinary or special resolution for winding up of the company.

The provisions applicable to members' voluntary winding up are as follows:-

- Appointment of liquidator and fixation of his remuneration by the General Meeting.
- Cessation of Board's power on appointment of liquidator except so far as may have been sanctioned by the General Meeting, or the liquidator.
- Filling up of vacancy caused by death, resignation or otherwise in the office of liquidator by the general meeting subject to an arrangement with the creditors.
- Sending the notice of appointment of liquidator to the Registrar.
- Power of liquidator to accept shares or like interest as a consideration for the sale of business of the company provided special resolution has been passed to this effect.
- Duty of liquidator to call creditors' meeting in case of insolvency of the company and place a statement of assets and liabilities before them.
- Liquidator's duty to convene a General Meeting at the end of each year.
- Liquidator's duty to make an account of winding up and lay the same before the final meeting.

Creditor's voluntary winding up

It is possible in the case of insolvent companies. It requires the holding of meetings of creditors besides those of the members right from the beginning of the process of voluntary winding up. It is the creditors who get the right to appoint liquidator and hence, the winding up proceedings are dominated by the creditors.

The provisions applicable to creditors' voluntary winding up are as follows:-

- The Board of Directors shall convene a meeting of creditors on the same day or the next day after the meeting at which winding up resolution is to be proposed. Notice of meeting shall be sent by post to the creditors simultaneously while sending notice to members. It shall also be advertised in the Official Gazette and also in two newspapers circulating in the place of registered office.
- A statement of position of the company and a list of creditors along with list of their claims shall be placed before the meeting of creditors.
- A copy of resolution passed at creditors' meeting shall be filed with Registrar within 30 days of its passing.
- It shall be done at respective meetings of members and creditors. In case of difference, the nominee of creditors shall be the liquidator.
- A five-member Committee of Inspection is appointed by creditors to supervise the work of liquidator.
- Fixation of remuneration of liquidator by creditors or committee of inspection.
- Cessation of board's powers on appointment of liquidator.

As soon as the affairs of the company are wound up, the liquidator shall call a final meeting of the company as well as that of the creditors through an advertisement in local newspapers as well as in the Official Gazette at least one month before the meeting and place the accounts before it. Within one week of meeting, liquidator shall send to Registrar a copy of accounts and a return of resolutions.

Winding up an Unregistered Company

According to the Companies Act, an unregistered company includes any partnership, association, or company consisting of more than seven persons at the time when petition for winding up is presented. But it will not cover the following:-

- A railway company incorporated by an Act of Parliament or other Indian law or any Act of the British Parliament;
- A company registered under the Companies Act, 1956;
- A company registered under any previous company laws.
- An illegal association formed against the provisions of the Act.

However, a foreign company carrying on business in India can be wound up as an unregistered company even if it has been dissolved or has ceased to exist under the laws of the country of its incorporation.

The provisions relating to winding up of a unregistered company:-

- Such a company can be wound up by the Tribunal but never voluntarily.
- Circumstances in which unregistered company may be wound up are as follows:-
    - If the company has been dissolved or has ceased to carry on business or is carrying on business only for the purpose of winding up its affairs.
    - If the company is unable to pay its debts.
    - If the Tribunal regards it as just and equitable to wind up the company.
- Contributory means a person who is liable to contribute to the assets of a company in the event of its being wound up. Every person shall be considered a contributory if he is liable to pay any of the following amounts:-
    - Any debt or liability of the company;
    - Any sum for adjustment of rights of members among themselves;
    - Any cost, charges and expenses of winding up;
- On the making of winding up order, any legal proceeding can be filed only with the leave of the Tribunal.

OFFICIAL LIQUIDATORS

Under the present Act, the only person who is competent to act as the liquidator in a winding up is the official liquidator. For the purpose of winding up, there shall be attached to each high Court an official liquidator appointed by the Central Government, who may be either a whole time or part time officer depending upon the volume of work. In district courts the official receiver will be the official liquidator. The Central Government may appoint one or more deputy or assistant official liquidators to assist the official liquidator in the discharge of his functions. There is no provision in the Act, for the removal of the official liquidator [Sec. 448(1) & (1-A)].

LIQUIDATOR

On a winding up order being made, the official liquidator, by virtue of his office, becomes the liquidator of the company (Sec. 449). Where the official liquidator becomes or acts as liquidator, there shall be paid to the Central Government out of the assets of the company such fees as may be prescribed. A liquidator shall be described by the style of "The official liquidator" of the particular company in respect of which he acts and not by individual name [Sec. 452].

PROVISIONAL LIQUIDATOR

The Court may appoint the official liquidator to be the liquidator provisionally at any time after the presentation of the petition for winding up and before making winding up order [Sec. 450 (1)]. Before making such an appointment notice must be given to the company and a reasonable opportunity must be given to it to make representation. The Court may dispense with such notice where there are special reasons. Such reasons must be recorded in writing. A provisional liquidator is as much liquidator as a liquidator in the winding up of a company. But where a provisional liquidator is appointed by the Court, the Court may limit and restrict his powers. On a winding up order being made, the official liquidator shall cease to be provisional liquidator and shall become liquidator of the company.

GENERAL PROVISIONS FOR LIQUIDATORS

The liquidator shall conduct the proceedings in winding up the company and perform such duties as the Court may impose. The official liquidator gets his remuneration from the Central Government and as such he is not entitled to any further remuneration. For the services rendered by the official liquidator to the company, the Central Government shall pay such fees out of the assets of the company as may be prescribed. The acts of a liquidator shall be valid, notwithstanding any defect that may afterwards be discovered in his appointment or qualification. But his acts shall not be valid if they are done after it has been shown that his appointment was invalid [Sec. 451].

STATEMENT OF AFFAIRS [SEC. 454]

The company must make out and submit to the official liquidator a statement as to the affairs of the company in the prescribed form verified by an affidavit and containing the following particulars :

(a) The assets of the company, stating separately the cash balance in hand and at the bank and the negotiable securities held by the company;

(b) Its debts and liabilities;

(c) Names, residences and occupation of its creditors, stating separately the amount of secured and unsecured debts;

(d) In the case of secured debts, particulars of securities given, their value and the dates on which they were given ;

(e) The debts due to the company and the names, residences and occupations of the persons from whom they are due and the amount likely to be realised on account thereof; and

(f) Such further or other information as may be prescribed or as the official liquidator may require.

Note that the statement must be submitted and verified by one or more of the directors and by the manager, secretary or other chief officer of the company and it must be submitted within 21 days from the relevant date or within such extended time not exceeding three months [Sec. 454 (3)].

DUTIES OF THE LIQUIDATOR

They may be summarized as under :

(i) He must conduct equitably and impartially all proceedings in the winding up according to the provisions of the law.

(ii) He must submit a preliminary report to the Court as to :

(a) the amount of capital issued, subscribed and paid up and the estimated amount of assets and liabilities, giving separately, under the heading of assets such as

- (i) cash and negotiable securities;
- (ii) debts due from contributories;
- (iii) debts due to the company and securities, if any available in respect thereof ;
- (iv) immovable and movable properties belonging to the company; and
- (v) unpaid calls.

(b) if the company has failed, as to the causes of the failure; and

(c) whether in his opinion further inquiry is desirable as to any matter relating to the promotion, formation or failure of the company or the conduct of the business thereof.

Note that the Court may extend the period of six months for the submission of the above report by the official liquidator. The Court may also order that no such statement need be submitted.

(iii) The official liquidator may, if he thinks fit, make further reports, stating the manner in which the company was promoted or formed. He may state in the reports whether in his opinion any fraud has been committed by any person in its promotion or formation, or since the formation thereof. He may also state any other matters which, in his opinion, it is desirable to bring to the notice of the Court [Sec. 455(2)].

(iv) He must take into his custody and control the property of the company. Notice that so long as there is no liquidator, all the property and effects of the company are deemed to be in the custody of the Court [Sec. 456(2)].

(v) Control of powers : The liquidator must in the administration of the assets of the company and the distribution thereof among its creditors have regard to any directions which may be given by a resolution of the creditors or contributories at any general meeting or by the committee of inspection [Sec. 460(1)]. Any directions given by the creditors or contributories at any general meeting override any directions given by the committee of inspection.

(vi) To Summon Meetings of Creditors and Contributories : He may summon general meetings of the creditors or contributories for the purpose of ascertaining their wishes. But he shall be bound to summon such meetings, at such times, as the creditors or contributories may, by resolution, direct, or whenever requested in writing to do so by not less than one tenth in value of the creditors or contributories, as the case may be [Sec. 460 (3)].

(vii) Proper Books : The liquidator must keep proper books for making entries or recording minutes of proceedings at meetings and of such other matters as may be prescribed. Any creditor or contributory may, subject to the control of the Court, inspect any such books, personally or through his agent [Sec. 461].

(viii) He must, at least twice in each year, present to the Court an account of his receipts and payments as liquidator. The account must be in the prescribed form and must be made in duplicate. The Court gets the account audited, keeps one copy thereof in its records and delivers the other copy to the Registrar for filling. Each copy shall, however, be open to the inspection of any creditor, contributory or person interested. The liquidator must also send a printed copy of the accounts so audited by post to every creditor and to every contributory.

(ix) Within two months from the date of the direction of the Court, the liquidator must call a meeting of the creditors for determining the persons who are to be members of the committee of inspection, if such committee is to be appointed. Within 14 days of the meeting of the creditors, the liquidator must call a meeting of the contributories to consider the decision of the creditors.

(x) Within two months of the expiry of each year from the commencement of winding up, the liquidator must file a statement duly audited, by a qualified auditor with respect to the proceedings in, and position of, the liquidation.

The statement must be filed :

(a) in the case of a winding up by or subject to the supervision of the Court, in the Court ; and

(b) in the case of voluntary winding up, with the Registrar.

Note that when the statement is filed in the Court, a copy must simultaneously be filed with the Registrar and must be kept by him along with the other records of the company [Sec. 551].

POWERS OF THE LIQUIDATOR

A liquidator has two types of powers under the Act :

(a) Powers exercisable with the sanction of the Court ; and

(b) Powers exercisable without the sanction of the Court.

POWERS WITH THE SANCTION OF THE COURT

(a) to institute or defend any suit, prosecution or other legal proceedings, civil or criminal, on behalf of the company ;

(b) to carry on the business of the company for the beneficial winding up of the company;

(c) to sell the immovable and movable property and actionable claims of the company by public auction or private contract ;

(d) to raise any money required on the security of the assets of the company ;

(e) to appoint an advocate, attorney or pleader to assist him in the performance of his duties ;

(f) to do all such other things as may be necessary for winding up the affairs of the company and distributing its assets.

Note that the Court may by order provide that the liquidator may exercise any of the above powers without the sanction of the Court [Sec. 458).

POWERS WITHOUT THE SANCTION OF THE COURT

The liquidator may exercise the following powers without the sanction of the Court, namely, powers:

(a) to execute documents and deeds on behalf of the company and use, when necessary, the company's seal ;

(b) to inspect the records and returns of the company or the files of the Registrar without payment of any fee ;

(c) to draw, accept, make and endorse any bills of exchange, hundis or promissory notes with the same effect as if drawn, accepted, made, or endorsed by the company in the course of its business ;

(d) to prove, rank and claim in the insolvency of any contributory for any balance against his estate and to receive dividends in respect thereof;

(e) to take out, in his official name, letters of administration to any deceased contributory ;

(f) to appoint an agent to do any business which he is unable to do himself [Sec. 457(2)]. For example, he can appoint any advocate, attorney or pleader entitled to appear before the Court to assist him in the performance of his duties [Sec. 459], but with the sanction of the Court.

SUPERVISION AND CONTROL OVER LIQUIDATORS

1 Control by contributories and creditors

The contributories and creditors exercise control over the liquidator in the performance of his duties through the medium of the meetings which it is his duty to call from time to time. Any creditor or contributory may, subject to the control of the Court inspect the books which are maintained by the liquidator. The liquidator is also required to print and send a copy of the audited accounts to each creditor and contributory.

2. Control by Court

The liquidator shall apply to the Court for directions in relation to any matter arising in the winding up. The Court has the power to confirm, reserve or modify any act or decision of the liquidator if complained by any aggrieved person. The Court has the power to cause the accounts of the liquidator to be audited in such manner as it thinks fit.

3. Supervision by committee of inspection

The committee of inspection can inspect the accounts of the liquidator at all reasonable times. The liquidator is under an obligation to have directions from the committee of inspection.

4. Control by Central Government

Section 463 seeks to bring the conduct of the liquidators of companies under the control and scrutiny of the Central Government. Where a liquidator does not faithfully perform his duties and duly observe all the requirements imposed upon him by the Act or the rules there under with respect to the performance of his duties, or if any complaint is made to the Central Government by any creditor or contributory in regard thereto, the Central Government shall enquire into the matter, and take such action thereon as it may think fit The power includes the power to remove the liquidator from office. The Central Government may at any time require any liquidator of a company which is being wound up by the Court to answer any inquiry in relation to any winding up in which he is engaged. It may also, if it thinks fit, apply to the Court to examine him or any other person on oath concerning the winding up. The Central Government may also direct a local investigation to be made of the books and vouchers of the liquidator. The provisions of this section do not apply where the winding up has been completed after dissolution.

COMMITTEE OF INSPECTION (Sections 464, 465)

The Court may, at the time of making an order for the winding up or at any time thereafter, direct that there shall be appointed a committee of inspection to act with the liquidator. Where such a direction is given by the Court, the liquidator is required to convene, within 2 months from the date of the direction, a meeting of the creditors to determine who are to be the members of the committee, within 14 days from the date of the creditors' meeting, the liquidator must call a meeting of the contributories to consider the creditors' decision with respect to the membership of the committee. Contributories may accept the decision of the creditors with or without modification or reject it. If the contributories at their meeting do not accept the creditors' decision in its entirely, the liquidator shall apply to the Court for directions as to what the composition of the committee should be and who shall be its members. The committee shall consist of not more than 12 members, being creditors or contributories of the company in such proportion as may be agreed on by the meetings of the creditors and contributories and in case of difference of opinion, as may be determined by the Court. The Committee may inspect the accounts of the liquidator at all reasonable time.

The committee will meet at such times as it may from time to time appoint and the liquidator or any member of the committee may also call a meeting of the committee as and when he thinks necessary. The quorum for a meeting of the committee will be one-third of the total number of the members or two, whichever is higher. The committee may act by a majority of its members present at a meeting but shall not act unless a quorum is present. A member may resign by notice in writing signed by him and deliver to the liquidator. If a member of the committee is adjudged as insolvent or compounds or arranges with his creditor or is absent from five consecutive meetings of the committee without leave of those members, who together with himself, represent the creditors or contributories, his office shall become vacant. A member of the committee may be removed at a meeting of the creditors, if he represents creditors, or at a meeting of contributories if he, represents contributories, by an ordinary resolution of which seven days' notice has been given stating the objects of the meeting. When any vacancy has occurred in the committee, the liquidator will call a meeting of the creditors or contributories, as the case may be, and the meeting may reappoint the same person or appoint some other person in the vacancy. However, the liquidator may apply to the Court that the vacancy need not be filled in and if the Court is satisfied that in the circumstances of the case the vacancy need not be filled, it may make an order accordingly.

CONSEQUENCES OF WINDING UP

(i) Where the Court makes an order for winding up of company, the Court must forthwith cause intimation thereof to be sent to the Official Liquidators and the Registrar (Section 444).

(ii) On the making of a winding up order it is the duty of the petitioner in the winding up proceedings and of the company to file with the Registrar a copy of the order of the Court within 30 days from the date of the making of the order [Section 445(1)].

(iii) The winding up order is deemed to be notice of discharge to the officers and employees of the company, except when the business of the company is continued [Section 445(3)].

(iv) When a winding up order has been made, no suit or other legal proceedings can be commenced against the company except with the leave of the Court. Suits pending at the date of the winding up order cannot be further proceeded without the leave of the Court. According to sub-section (2) of Section 446 the Court which is winding up the company has jurisdiction to entertain or dispose of

(a) any suit or proceeding by or against the company;

(b) any claim made by or against the company;

(c) any application made under Section 391 by or in respect of the company ;

(d) any question of priorities or any other question whatsoever which may relate to or arise in course of the winding up of the company.

(v) An order for winding up operates in favour of all the creditors and of all the contributories of the company as if it had been made on the joint petition of a creditor and of a contributory (Section 447).

(vi) According to Section 536 any disposition of the property (including actionable claims) of the company, any transfer of shares in the company or alteration in the status of its members, made after the commencement of the winding up shall be void, unless the Court otherwise orders.

Thus the Court can direct that any such disposition of property or actionable claims or transfer of shares or alteration of status of the members will be valid. But unless the Court so directs, such disposition, transfer or alteration will be void.

(vii) Section 537 declares that any attachment and sale of the estate or effects of the company, after the commencement of the winding up, will be void. In the case of winding up by the Court any attachment, distress or execution put in force, without leave of the Court, against the estate or effects of the company after the commencement of the winding up will be void. Similarly any sale held, without leave of the Court, of any of the properties or effects of the company after the commencement of the winding up will be void. With leave of the Court, attachment and sale of the properties of the company will be valid even if such attachment and sale are made after the commencement of the winding up of the company. Besides this section does not apply to any proceedings for the recovery of any tax imposed or any dues payable to the Government. Thus I.T.O. can commence assessment proceedings without leave of the Court.

(viii) It is to be noted that winding up order does not bring the business of the company to an end. The corporate existence of the company continues through winding up till the company is dissolved. Thus the company continues to have corporate personality during winding up. Its corporate existence come to an end only when it is dissolved.

(ix) An order for winding up operates in favour of all the creditors and of all the contributories of the company as if it had been made on the joint petition of a creditor and of contributory.

(x) On a winding up order being made in respect of a company, the Official Liquidator, by virtue of the office, becomes the liquidator of the company (Section 449).

DISSOLUTION OF COMPANY IN WINDING UP BY THE COURT

The Court may make an order for the dissolution of a company in the following conditions:

(a) When the affairs of the company have been completely wound up ; or

(b) When the Court is of opinion that the liquidator cannot proceed with the winding up of a company for want of funds and assets or for any other reason and it is just and equitable in the circumstances of the case that an order of dissolution of the company should be made. Where such an order is made by the Court, the company will be dissolved from the date of the order of the Court. Within 30 days from the date of the order, the liquidator must send a copy of the order to the Registrar. On the dissolution, the corporate existence of the company comes to an end.

Company in liquidation exists as juristic personality until order of dissolution is based by the Court. After the order of dissolution, the legal personality of the company come to an end. The Court may declare the dissolution void within 2 years from the date of the dissolution.

MODULE V
EMERGING ISSUES IN COMPANY LAW

Company law, an ever evolving subject has undergone major transformation in the last decade. The impetus for such transformation germinated partially from the world wide move for market oriented policies and partially by disquieting features of globalization, resulting into focused attention on need for good corporate governance.

The advancements in information technology and influence of faster means of communications over corporate operations have also provided growth in corporate enterprises. In other words, the paradigm shift witnessed in the global economy and corporate sector world over, have cumulatively presented various issues that have triggered debate and become important factors for initiating change in company law in our country.

PRODUCER COMPANIES

Till recently, the Companies Act, 1956 (the Act), recognised only three types of companies, namely, companies limited by shares (sub-divided into public limited and private limited companies), companies limited by guarantees and unlimited companies. With the coming into force on February 6 of the Companies (Amendment) Act 2002, (1 of 2003), a fourth category, `producer companies,' finds a place in the Act. For this, a new Part IXA, divided into 12 chapters, has been included in the Act, comprising 46 sections, interestingly numbered as 581A to 581Z and 581ZA to 581ZT. However, the section that defines the various types of companies that can be incorporated under the Act remains unaltered.

The new concept of producer companies is based on the recommendations of an expert committee led by noted economist, Y. K. Alagh. The committee was asked (a) to frame a legislation that would enable incorporation of cooperatives as companies and conversion of existing cooperatives into companies and (b) to ensure that the proposed legislation accommodated the unique elements of cooperative business with a regulatory framework similar to that of companies.

The new type is termed as `producer company', to indicate that only certain categories of persons can participate in the ownership of such companies. The members have necessarily to be `primary producers,' that is, persons engaged in an activity connected with, or related to, primary produce.

A 'producer company' in accordance with section 581C (1) of the Companies Act 1956, is a company where there are ten or more individuals, and each of them is a producer in any two or more producer institutions. It can also be combination of ten or more individuals or producer institutions. These individuals and institutions should be desirous of performing the function of a producer company. The objects of the producer company should be specified under Sec. 581B of the Companies Act of 1956. It should also comply with the other provisions of the Companies Act of 1956

What is primary produce? In terms of the Act it is a produce of farmers arising from agriculture including animal husbandry, horticulture, floriculture, pisciculture, viticulture, forestry, forest products, re-vegetation, bee raising and farming plantation products: produce of persons engaged in handloom, handicraft and other cottage industries: by -products of such products; and products arising out of ancillary industries.

FORMATION

Any ten or more individuals, each of them being a producer, that is, any person engaged in any activity connected with primary produce, any two or more producer institutions, that is, producer companies or any other institution having only producers or producer companies as its members or a combination of ten or more individuals and producer institutions, can get a producer company incorporated under the Act.

The companies shall be termed as limited and the liability of the members will be limited to the amount, if any, unpaid on the shares. On registration, the producer company shall become as if it is a private limited company with the significant difference that a minimum of two persons cannot get them registered, the provision relating to a minimum paid-up capital of Rs. 1 lakh will not apply and the maximum number of members can also exceed 50.

Members' equity cannot be publicly traded but be only transferred. As such, "producer companies would not be vulnerable to takeover by other companies or by MNCs."

OBJECTS

The objects of producer companies shall include one or more of the eleven items specified in the Act, the more important being:

(i) Production, harvesting, procurement, grading, pooling, handling, marketing, selling, export of primary produce of members or import of goods or services for their benefit;

(ii) Processing including preserving, drying, distilling, brewing, venting, canning and packaging of produce of its members; and

(iii) Manufacture, sale or supply of machinery, equipment or consumables mainly to its members.

The other objects include rendering technical or consultancy services, insurance, generation, transmission and distribution of power and revitalisation of land and water resources; promoting techniques of mutuality and mutual assistance; welfare measures and providing education on mutual assistance principles.

It is to be noted that private limited or public limited companies are not hamstrung by such restrictions as to their objectives, provided they are legal.

MANAGEMENT

(a) Every producer company is to have at least five and not more than 15 directors. Minimum prescribed for private limited is two and for public limited three, while the maximum will depend on the number mentioned in the respective Articles. Usually the maximum is pegged at twelve.

(b) A full time chief executive, by whatever name called, is to be appointed by the board. He shall be an ex-officio director and will not be liable to retire by rotation. He shall be entrusted with substantial powers of management as the board may determine. This provision differs from that applicable to limited companies — a private limited need not have any chief executive while public limited companies, only with paid-up capital exceeding Rs. 5 crores, have to have a managing director.

(c) A stipulation that could dismay company secretaries is that only producer companies having an average annual turnover exceeding Rs. 5 crores in each of three consecutive years need have a whole-time secretary. It is not mentioned what would happen to the incumbent, if the turnover falls below this minimum. This is in contrast to the mandate that private and public limited companies having a paid-up capital of Rs. 2 crores or more should have a whole-time secretary.

MEMBERS' BENEFITS

Members will initially receive only such value for the produce or products pooled and supplied as the directors may determine. The withheld amount may be disbursed later either in cash or in kind or by allotment of equity shares.

Members will be eligible to receive bonus shares. An interesting provision is for the distribution of patronage bonus (akin to dividend) after the annual accounts are approved — patronage bonus means payment out of surplus income to members in proportion to their respective patronage (not shareholding). Patronage, in turn, is defined as the use of services offered by producer companies to their members by participation in their business activities. Incidentally, there is an error in drafting — the powers of the board include "determination of the dividend payable" — it should have been "patronage bonus payable."

RESERVES

Every producer company has to maintain a general reserve in every financial year and in case there is not sufficient funds in any year for such transfer, the shortfall has to be made up by members' contribution in proportion to their patronage in the business This is a well-thought out provision.

AUDIT

An unnecessary stipulation is that "without prejudice to the concerned sections in the Act," the auditors of producer companies have to specially report on some additional items such as debts due and bad debts, verification of cash balances and securities, details of assets and liabilities, loans extended to directors and details of donations and subscriptions. These are all integral parts of any audit, both statutory and internal and one fails to understand the logic behind this stipulation.

INTERNAL AUDIT

It is mandated that every producer company should carry out internal audit of its accounts by chartered accountants. The Act has not so far made it compulsory for limited companies to carry out internal audit, although listed companies, by virtue of the clause in the listing agreement relating to corporate governance, are to have a full-scale internal audit system.

RESOLUTION OF DISPUTES

Any dispute relating to the formation, management or business of producers companies is to be settled by conciliation or by arbitration under the Arbitration and Conciliation Act, 1996 as if the parties to the dispute have consented in writing to such procedure. The arbitrator's decision shall be final. This seems to be inequitable since usually an arbitration award can be appealed against in high courts.

LIMITED LIABILITY PARTNERSHIP

A limited liability partnership, or LLP, is a relatively new creation. It operates much like a limited partnership, but gives each member of the LLP protection from personal liability, except to the extent of their investment in the LLP. Generally, partners in a limited liability partnership aren't responsible for another partner's debts, obligations, or liabilities resulting from negligence, malpractice or misconduct.

It is viewed as an alternative corporate business vehicle that provides the benefits of limited liability but allows its members the flexibility of organising their internal structure as a partnership based on a mutually arrived agreement. Owing to flexibility in its structure and operation, the LLP would also be a suitable vehicle for small enterprises and for investment by venture capital.

Keeping in mind the need of the day the parliament enacted the Limited Liability Partnership Act, 2008 which received the assent of the president on 7th January, 2009.

The salient features of the LLP Act 2008 inter alia are as follows.

1) The LLP shall be a body corporate and a legal entity separate from its partners. Any two or more persons, associated for carrying on a lawful business with a view to profit, may be subscribing their names to an incorporation document and filing the same with the registrar, from a Limited Liability Partnership. The LLP will have perpetual succession.
2) The mutual rights and duties of partners of an LLP inter se and those of the LLP and its partners shall be governed by an agreement between partners or between the LLP and the partners subject to the provisions of the LLP Act 2008.
3) The LLP will be a separate legal entity, liable to the full extent of its assets, with the liability of the partners being limited to their agreed contribution in the LLP which may be of tangible or intangible nature or both tangible and intangible in nature.

4) Every LLP shall have at least two partners and shall also have at least two individuals as Designated Partners, of whom at least one shall be resident in India. The duties and obligations of Designated Partners shall be as provided in the law.
5) Every limited liability partnership shall have either the words “limited liability partnership” or the acronym “LLP” as the last words of its name.
6) The winding up of the LLP may be either voluntary or by the tribunal to be established under the Companies Act, 1956. Till the tribunal is established, the power in this regard has been given to the High Court.
7) The LLP Act 2008 confers powers on the central Government to apply provisions of the companies Act, 1956 as appropriate, by notification with such changes or modifications as deemed necessary. However such notifications shall be laid in draft before each house of parliament for a total period of 30 days and shall be subject to any modifications as may be approved by both houses.
8) The Indian Partnership Act, 1932 shall not be applicable to LLPs.

FORMATION OF LIMITED LIABILITY PARTNERSHIP (SECTION 11)

1) For a limited liability partnership to be incorporated.
   (a) Two or more persons associated for carrying on a lawful business with a view to profit shall subscribe their names to an incorporation document.
   (b) The incorporation document shall be filed in such manner and which such fees, as may be prescribed with the Registrar of the state in which the registered office of the Limited Liability Partnership is to be situated, and
   (c) There shall be filed along with the incorporation document, a statement in the prescribed form, made by either an advocate, or a Company Secretary or a Chartered Accountant or a Cost Accountant, who is a engaged in the formation of the Limited Liability Partnership and by anyone who subscribed his name to the incorporation document, that all the requirements of this Act and the rules made hereunder have been complied with in respect of incorporation and matters precedent and incidental thereto.
2) The incorporation document shall
   (a) Be in a form as may be prescribed.
   (b) State the name of the Limited Liability Partnership.
   (c) State the proposed business of the Limited Liability Partnership.
   (d) State the address of the registered office of the Limited Liability Partnership.
   (e) State the name and address of each of the persons who are to be partners of the Limited Liability Partnership on incorporation.
   (f) State the name and address of the persons who are to be designated partners of the Limited Liability partnership on incorporation.

(g) Contains such other information concerning the proposed Limited Liability Partnership as may be prescribed.

3) If a person makes a statement under clause (c) of sub- section (1) which he (a) knows to be false, or (b) does not believe to be true.

Shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees.

INCORPORATION BY REGISTRATION (SECTION 12)

(1) When the requirements imposed by clauses (b) and (c) of sub-section (1) of section 11 have been complied with, the Registrar shall retain the incorporation document and, unless the requirement imposed by clause (a) of that sub-section has not been complied with, he shall, within a period of fourteen days.

(a) Register the incorporation document, and

(b) Give a certificate that the limited liability partnership is incorporated by the name specified therein.

(2) The registrar may accept the statement delivered under clause (c) of sub-section (1) of section 11 as sufficient evidence that the requirement imposed by clause (a) of that sub-section has been complied with.

(3) The certificate issued under clause (b) of sub-section (1) shall be signed by the Registrar and authenticated by his official seal.

(4) The certificate shall be conclusive evidence that the Limited Liability Partnership is incorporated by the name specified therein.

EFFECT OF REGISTRATION (SECTION 14)

On registration, a limited liability partnership shall, by its name be capable of

(a) Suing and being sued.

(b) Acquiring, owing, holding and developing or disposing of property, whether movable or immovable, tangible or intangible.

(c) Having a common seal, if it decides to have one, and

(d) Doing and suffering such other acts and things as bodies corporate may lawfully do and suffer.

CORPORATE GOVERNANCE

Corporate governance refers to the structures and processes for the direction and control of companies. Corporate governance concerns the relationships among the management, Board of Directors, controlling shareholders, minority shareholders and other stakeholders. Good corporate governance contributes to sustainable economic development by enhancing the performance of companies and increasing their access to outside capital.

The term Corporate governance was born when the study of the concept of governance was linked by the business or corporate world. The issue of corporate governance has acquired centre-stage as a consequence of foreign direct investments flowing into India.

Corporate governance may be defined as "A set of systems, processes and principles which ensure that a company is governed in the best interest of all stakeholders". In simple sense, It is the process of managing the corporate by establishing better relation with the top management and other interested parties to the affairs of the company with a view to maximize the shareholders' value in the long run through better business practices, better quality of work life and culture.

Accordingly good corporate governance implies the following

1. Optimal utilization of resources for enhancing the value of the company and effectively monitoring of executives performance and supporting the entrepreneurship spirit.
2. Ethical behavior of the company in honoring and protecting the rights of all the stakeholders.

The core principles of corporate governance are fairness, transparency, accountability and responsibility. That is

a) Fairness to ensure the right of shareholders including minority shareholders.
b) Transparency through disclosure of information on financial performance governance and ownership.
c) Accountability for handling resources of the company on the part of board of governors.
d) Responsibility in discharging its functions including compliance with regulations and code of conduct.

RELEVANCE AND PROVISIONS UNDER LISTING AGREEMENT

In recognition of the importance of corporate governance as an integral part of corporate financial practices, the SEBI has mandated corporate governance in the listing requirement in clause 49 of the listing agreement.

Clause 49 of the listing agreement to the Indian Stock Exchange comes into effect from 31 December 2005.All existing listed companies were required to comply with the provisions of the new clause by 31st December 2005.

The major provisions included in the new clause 49 are:-

1. The board will lay down a code of conduct for all board members and senior management of the company to compulsorily follow.
2. The CEO and CFO will certify the financial statements and cash flow statements of the company.

3. If while preparing financial statements, the company follows a treatment thatis different from that prescribed in the accounting standards it must disclose that in the financial statements.
4. The company will have to lay down procedures for informing the board members about the risk management and minimization procedures.
5. Where money is raised through public issues etc, the company will have to disclose the uses/ applications of funds according to major categories as part of quarterly disclosure of financial statements.

Further on as annual basis, the company will prepare a statement of funds utilized for purposes other than those specified in the offer document/ prospectus and place it before the audit committee. Clause 49 contains both mandatory and non-mandatory requirements.

MANDATORY REQUIREMENTS REFER PRIMARILY TO

1. Board of Directors with respect to their composition, independence, procedures, code of conduct and disclosures.

A. **COMPOSITION OF BOARD OF DIRECTORS**

The Board of directors of the company should have an optimum combination of executive and non- executive directors with not less than 50 percent comprising of non-executive directors. Where the chairman of the board is a non executive director at least one- third of the board should comprise of independent directors and in case he is an executive director, at least half of the board should comprise of independent directors. An independent directors means a non- executive directors of the company.

B. NON-EXECUTIVE DIRECTORS COMPENSATION AND DISCLOSURES

All fees/compensation if any, paid to non- executive directors, including independent directors, would be fixed by the board of directors and require previous approval of shareholders in general meeting.

C. OTHER PROVISIONS RELATING TO BOARD

The board should meet at least four times a year, with a maximum time gap of three months between any two meetings.

D. CODE OF CONDUCT

A code of conduct for board members and senior management has to be laid down by the board which should be posted on the website of the company. All board members and senior management should affirm compliance with the code an annual basis and the annual report shall contain a declaration to this effect signed by the CEO.

2. Audit committee and its composition, powers, role and responsibilities.

A. QUALIFIED AND INDEPENDENT AUDIT COMMITTEE

A qualified and independent audit committee should be set up, giving the terms of reference subject to the following.

1) The audit committee should have minimum three directors as members. Two- third of the member of audit committee shall be independent directors.
2) All members of audit committee shall be financially literate and at least one member should have accounting or related financial management expertise.
3) The chairman of the audit committee should be an independent director.
4) He should be present at annual general meeting to answer shareholders queries.

B. MEETING OF AUDIT COMMITTEE.

Minimum number of audit committee meeting in a year is four and not more than four months should elapse between two meetings. The quorum would be either two members or one third of the members of the audit committee whichever is greater.

C. POWER OF AUDIT COMMITTEE.

The audit committee should have powers to investigate any activity within its term of reference, to see information from any employee and obtain outside legal or other professional advices.

D. ROLE OF AUDIT COMMITTEE.

Some of the roles of the committee are

1) To ensure that the financial statement is correct, sufficient and credible.
2) Recommending to the board, the appointment, re-appointment and if required the replacement or removal of the statutory auditor and the fixation of audit fees.
3) Reviewing with the management, the annual financial statement before submission to the board for approval.
4) Reviewing the matters pertaining the internal audit system.
5) Discussions with the statutory auditors.
6) Subsidiary companies to ensure their better control and supervision.

4. Disclosures in the context of related party transactions, risk management and minimization procedures, utilization of proceeds from initial public offerings, investor education and protection.

5.CEO/CFO certification regarding the correction of the financial statement and compliance with prescribed accounting standards.

6.Separate report on corporate Governance in the annual reports with respects to compliance of mandatory requirements, and

7.Compliance certificate obtained either from the auditors or practicing company secretaries.

Non mandatory requirements refer to those requirements which are not compulsory and can be adopted at the discretion of the company.

These include requirements.

1. Regarding the maximum tenure of the independent directors.
2. Formation of a remuneration committee for determining the remuneration packages for executive directors.
3. Moving towards a regime of unqualified financial statements.
4. Training of board members.
5. Evaluation of non- executive board members, and
6. Establishing a mechanism for employees to report unethical behavior to the management under a whistle Blower Policy.

SECURITIES EXCHANGE BOARD OF INDIA (SEBI)

It was officially established by The Government of India in the year of 1992 with SEBI Act 1992 being passed by the Indian Parliament. SEBI is having its Headquarter at the business district of Bandra Kurla Complex in Mumbai, and has Northern, Eastern, Southern and Western Regional Offices in New Delhi, Kolkata, Chennai and Ahmedabad respectively.

Controller of Capital Issues was the regulatory authority before SEBI came into existence; it derived authority from the Capital Issues (Control) Act, 1947.

Initially SEBI was a non statutory body without any statutory power. However in the year of 1995, the SEBI was given additional statutory power by the Government of India through an amendment to the Securities and Exchange Board of India Act 1992. In April, 1998 the SEBI was constituted as the regulator of capital markets in India under a resolution of the Government of India.

ESTABLISHMENT OF SEBI

The Board named Securities Exchange Board Of India (SEBI) shall be having perpetual succession and a common seal, with power subject to the provisions of this Act, to acquire, hold and dispose of property, both movable and immovable, and to contract, and shall, by the said name, sue or be sued. The head office of the Board shall be at Bombay and the Board may establish offices at other places in India.

MANAGEMENT OF THE BOARD

1. The Board shall consist of the following members, namely:-

(a) A Chairman;

(b) Two members from amongst the officials of the Ministry of the Central Government dealing with Finance and administration of the Companies Act, 1956(1 of 1956)];

(c) One member from amongst the officials of the Reserve Bank;

(d) Five other members of whom at least three shall be the whole-time members to be appointed by the central Government.

2. The general superintendence, direction and management of the affairs of the Board shall vest in a Board of members, which may exercise all powers and do all acts and things which may be exercised or done by the Board.

3. The Chairman shall also have powers of general superintendence and direction of the affairs of the Board and may also exercise all powers and do all acts and things which may be exercised or done by that Board.

4. The Chairman and members referred to in clauses (a) and (d) of sub-section (1) shall be appointed by the Central Government and the members referred to in clauses (b) and (c) of that sub-section shall be nominated by the Central Government and the Reserve Bank respectively.

5. The Chairman and the other members referred to in clauses (a) and (d) of sub-section (1) shall be persons of ability, integrity and standing who have shown capacity in dealing with problems relating to securities market or have special knowledge or experience of law, finance, economics, accountancy, administration or in any other discipline which, in the opinion of the Central Government, shall be useful to the Board.

FUNCTIONS OF BOARD

(1) Subject to the provisions of this Act, it shall be the duty of the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit.

(2) Without prejudice to the generality of the foregoing provisions, the measures referred to therein may provide for -

- ✓ regulating the business in stock exchanges and any other securities markets;
- ✓ registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities markets in any manner;
- ✓ registering and regulating the working of the depositories, participants, custodians of securities, foreign institutional investors, credit rating agencies and such other intermediaries as the Board may, by notification, specify in this behalf;
- ✓ registering and regulating the working of venture capital funds and collective investment schemes],including mutual funds;
- ✓ promoting and regulating self-regulatory organisations;
- ✓ prohibiting fraudulent and unfair trade practices relating to securities markets;
- ✓ promoting investors' education and training of intermediaries of securities markets;
- ✓ prohibiting insider trading in securities;
- ✓ regulating substantial acquisition of shares and take-over of companies;

- ✓ calling for information from, undertaking inspection, conducting inquiries and audits of the stock exchanges, mutual funds, other persons associated with the securities market]intermediaries and self- regulatory organizations in the securities market;
- ✓ calling for information and record from any bank or any other authority or board or corporation established or constituted by or under any Central, State or Provincial Act in respect of any transaction in securities which is under investigation or inquiry by the Board;”
- ✓ performing such functions and exercising such powers under the provisions of the Securities Contracts (Regulation) Act, 1956(42 of 1956), as may be delegated to it by the Central Government;
- ✓ levying fees or other charges for carrying out the purposes of this section;
- ✓ conducting research for the above purposes;
- ✓ calling from or furnishing to any such agencies, as may be specified by the Board, such information as may be considered necessary by it for the efficient discharge of its functions;”
- ✓ performing such other functions as may be prescribed.

(3)The Board shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit, in respect of the following matters, namely :

(i) the discovery and production of books of account and other documents, at such place and such time as may be specified by the Board;

(ii) summoning and enforcing the attendance of persons and examining them on oath;

(iii) inspection of any books, registers and other documents of any person referred to in section 12, at any place;]

(iv) inspection of any book, or register, or other document or record of the company referred to in sub-section (2A);

(v) issuing commissions for the examination of witnesses or documents.

POWERS

For the discharge of its functions efficiently, SEBI has been invested with the necessary powers which are:

1. To approve by−laws of stock exchanges.
2. To require the stock exchange to amend their by−laws.
3. Inspect the books of accounts and call for periodical returns from recognized stock exchanges.
4. Inspect the books of accounts of financial intermediaries.

5. Compel certain companies to list their shares in one or more stock exchanges.
6. Levy fees and other charges on the intermediaries for performing its functions.
7. Grant license to any person for the purpose of dealing in certain areas.
8. Delegate powers exercisable by it.
9. Prosecute and judge directly the violation of certain provisions of the companies Act.
10. Power to impose monetary penalties.

SECURITIES APPELLATE TRIBUNALS

Securities Appellate Tribunals means a Securities Appellate Tribunal established under subsection (1) of section 15 K of the Securities and Exchange of India Act 1992

ESTABLISHMENT OF SECURITIES APPELLATE TRIBUNALS

(1) The Central Government shall, by notification, establish one or more Appellate Tribunals to be known as the Securities Appellate Tribunal to exercise the jurisdiction, powers and authority conferred on such Tribunal by or under this Act [or any other law for the time being in force]

(2) The Central Government shall also specify in the notification referred to in sub-section (1) the matters and places in relation to which the Securities Appellate Tribunal may exercise jurisdiction.

COMPOSITION OF SECURITIES APPELLATE TRIBUNAL

A Securities Appellate Tribunal shall consist of a Presiding Officer and two other Members, to be appointed, by notification, by the Central Government:

Provided that the Securities Appellate Tribunal, consisting of one person only, established before the commencement of the Securities and Exchange Board of India (Amendment) Act, 2002, shall continue to exercise the jurisdiction, powers and authority conferred on it by or under this Act or any other law for the time being in force till two other Members are appointed under this section.

TENURE OF OFFICE OF PRESIDING OFFICER AND OTHER MEMBERS OF SECURITIES APPELLATE TRIBUNAL

The Presiding Officer and every other Member of a Securities Appellate Tribunal shall hold office for a terms of five years from the date on which he enters upon his office and shall be eligible for re-appointment:

Provided that no person shall hold office as the Presiding Officer of the Securities Appellate Tribunal after he has attained the age of sixty-eight years:

Provided further that no person shall hold office as Member of the Securities Appellate Tribunal after he has attained the age of sixty-two years.

PROCEDURE AND POWERS OF THE SECURITIES APPELLATE TRIBUNAL

(1) The Securities Appellate Tribunal shall not be bound by the procedure laid down by the Code of Civil Procedure, 1908(5 of 1908), but shall be guided by the principles of natural justice and, subject to the other provisions of this Act and of any rules, the Securities Appellate Tribunal shall have powers to regulate their own procedure including the places at which they shall have their sittings.

(2) The Securities Appellate Tribunal shall have, for the purposes of discharging their functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908(5 of 1908), while trying a suit, in respect of the following matters, namely:

(a) Summoning and enforcing the attendance of any person and examining him on oath;

(b) Requiring the discovery and production of documents;

(c) Receiving evidence on affidavits;

(d) Issuing commissions for the examination of witnesses or documents;

(e) Reviewing its decisions;

(f) Dismissing an application for default or deciding it *ex parte*;

(g) Setting aside any order of dismissal of any application for default or any order passed by it *ex parte*;

(h) Any other matter which may be prescribed.

(3) Every proceeding before the Securities Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code (45 of 1860), and the Securities Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973(2 of 1974).

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