

COMPANY LAW

(for Undergraduate Classes)

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PREFACE

This Text-Book of **Company Law** is specially prepared for undergraduate Students. It is prepared in accordance with the syllabus given in this book.

I do not claim any originality in the subject-matter of this book. I have drawn immense material from many standard books on this subject. Yet, this book is original in the exposition and presentation of the subject-matter. The subject-matter has been dealt with exhaustively and in very simple language.

I express my profound gratitude to my well-wishers for their encouragement in the preparation of this book. I am also thankful to **United Publishers, Mangalore**, for bringing out this book.

I shall consider my efforts amply rewarded if this book is found useful by the teachers and the students.

Suggestions for improvement of this book will be gratefully accepted.

Mangalore,

B.S. Raman

SYLLABUS

COMPANY LAW

Unit- I : An Introduction to Company: 12 Hrs.

Meaning, Features, Lifting the corporate veil - under Judicial discretion and statutory provisions, Kinds or types of companies - Special privileges or advantages of a Private Company. When does a private Company become a Public Company?

Unit- II : Formation of a Company: 12 Hrs.

Steps, Promoter, Legal Position of a promoter, Duties, Rights, and Liabilities of a Promoter, Effects of pre-incorporation contracts, Memorandum of Association, Clauses of Memorandum of Association, Doctrine of Ultra Vires, Articles of Association, Doctrine of constructive notice, Doctrine of Indoor Management, Prospectus - provisions of the Companies Act with regard to issue of prospectus, Contents. Types, Golden Rule for framing a prospectus. Consequences of Misstatement in prospectus, Liability of a Company for Untrue Statements.

Unit-III: Share Capital and Shares : 12 Hrs.

Types of share capital and shares, Sweat Equity shares, Provisions regarding allotment of shares, Irregular allotment, Rights shares, Bonus shares, Meaning of Calls on shares, Forfeiture of shares, surrender of shares, lien on shares. Underwriting of securities and listing of securities, Blank transfer and Forged transfer, Meaning of depository, Meaning of DEMAT Account and its features. Membership: Meaning, Modes of acquiring membership, who can be members? Termination of membership, Register of Members.

Unit- IV: Company Management : 12 Hrs.

Company Secretary – Qualification and Duties only. Directors – Qualification and Disqualification – Appointment and Removal – Duties and Liabilities.

Unit- V: Company Meetings: 12 Hrs.

Essentials - Types; Appointment of Chairman, methods of voting, Resolutions - Types; oppression and Mismanagement; Winding Up - Liquidation of company, Modes of winding up of a company.

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UNIT I INTRODUCTION TO COMPANY LAW

DEFINITION AND MEANING OF JOINT STOCK COMPANY

In common parlance, the term "company" means an association of persons for some purpose, say, for the purpose of conducting business or for the purpose of promoting art, science, religion, sports, education, etc. But, in the eyes of law, such an association is not recognised as a joint stock company unless it is incorporated under the Companies Act.

Section 3(1) of the Companies Act of 1956 defines the term 'Company' as "a company formed and registered under this Act or an existing company", and "an existing company means a company formed and registered under any of the previous Companies Acts."

This definition of 'Company' given by the Companies Act 1956 is not satisfactory, as it has failed to elaborate the true nature of a company.

In the absence of a satisfactory statutory definition, naturally, it would be better to consider some of the juristic definitions to understand the real meaning and nature of a company.

Lord Justice Lindley of England has defined a joint stock company as "A voluntary association or organisation of many persons who contribute money or money's worth to a common stock and employ it in some trade or business and who share the profit or loss arising therefrom. The common stock so contributed is denoted in money and is the capital of the company. The persons who contribute it or to whom it belongs are the members of the company. The proportion of capital to which each member is entitled is his share. The shares are of fixed value and the whole capital of the company is divided into equal number of shares. The shares are, generally, transferable, although under certain special circumstances, the right to transfer may be restricted."

In the words of Haney, "A joint stock company is an incorporated association, which is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal."

Chief Justice Marshall of the U.S.A. has defined a joint stock company as "a person, artificial, invisible, intangible and existing only in contemplation of law."

From these definitions, it is clear that a joint stock company is a voluntary association of persons, formed for the purpose of some business for profit, registered under the law, having an independent legal entity, a distinctive name, common seal and perpetual succession, with a joint stock (i.e., common capital) contributed by the members, divisible into transferable shares of fixed denomination and carrying limited liability. In short, it is an artificial person created by law with a perpetual succession and a common seal.

CHARACTERISTIC FEATURES OF A JOINT STOCK COMPANY

An analysis of the definition and meaning of a joint stock company reveals many distinctive characteristic features of a joint stock company. The main characteristic features of a joint stock company are:

1. Voluntary Association:

A joint stock company is a voluntary association or organisation of persons. No person can be compelled to become a member of a joint stock company. Similarly, no member can be compelled to give up his membership of a company.

2. Incorporated Association:

A joint stock company is an incorporated association. Incorporation or registration under the Companies Act is absolutely necessary for an association of persons or company to become a joint stock company. On incorporation, a company becomes a body corporate or corporation and becomes a separate person distinct from the individuals constituting it. If an association of persons or a company is not registered under the Companies Act, it cannot be called a joint stock company, and consequently, the liability of the members of such an unincorporated association will be unlimited (i.e., the private assets of the members will become liable for the payment of the debts of the association).

The significance of incorporation is as follows:

- (a) Incorporation under the Indian Companies Act gives a joint stock company a separate legal existence quite distinct from the members.
 - (b) Incorporation gives the joint stock company perpetual succession or permanent or continuous existence.
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- (c) Incorporation provides for the limited liability of the members of the company.
 - (d) Incorporation provides for the transferability of shares, of course, subject to the restrictions specified in the articles of association.
 - (e) Incorporation facilitates dealings between the company and the members of the company.
 - (f) It helps a person to have control of a company through the acquisition of the majority of shares carrying voting power.
 - (g) It facilitates separation of ownership and management of a company, entrustment of management to a board of directors elected from amongst the members, and thereby, facilitates representative management.

3. Specific Objects:

A joint stock company is formed for specific objects only, and the specific objects for which it is formed are expressly stated in the constitution (i.e., the memorandum of association) of the company. As such, a company can undertake only those activities which are intended to achieve the specified objects and those which are incidental thereto, but nothing else. In short, there are restrictions on the activities of a joint stock company.

The restrictions on the activities of a company provide protection to the shareholders as well as the creditors. They provide protection to the shareholders by ensuring that the funds contributed by them for the attainment of some specific objects are used only for those activities which are designed to achieve those specific objects and not in any other activities. They provide protection to the creditors by ensuring that the corporate funds (i.e., the funds of the company) to which they ultimately look for the repayment of their debts or loans are not wasted away in unauthorised activities.

4. Artificial Person Created by Law:

A joint stock company has no body and soul. In other words, it has no physical or natural existence. But it exists in the eyes of law (i.e., it is considered as an entity in the eyes of law). It is considered as an entity in the eyes of law, as it enjoys certain rights and privileges of a natural person. For instance, it can enter into contracts, sue and be sued in its own name, of course, through some human agency. So, a joint stock company is an artificial person created by law.

5. Not a Citizen:

No doubt, a joint stock company is a separate legal entity quite different from its members. But it cannot claim to be a citizen of the country (i.e., India) under the Constitution of India or the Citizenship Act of 1955. This point was upheld in the case of R.D. Singh Vs. Secretary, Bihar Small Industries Corporation (1975), State Trading Corporation of India Ltd. Vs. CTO and Others, Tata Engineering and Locomotives Ltd. Vs. State of Bihar.

It is true that a company cannot claim to be a citizen of the country. But it has nationality, domicile and residence. This is necessary for determining the jurisdiction of courts and for income-tax matters.

6. Separate Legal Entity or Corporate Personality:

A joint stock company has entity (i.e., existence) quite distinct (i.e., different) and independent of the existence of the members who constitute it. In other words, it has a separate legal entity quite different from that of its members. This point, i.e., the principle of separate legal entity (also known as veil of incorporation) has been very well emphasized in the leading case of Salomon Vs. Salomon & Co. Ltd.

In this context, it is better to know the facts of this case. One Salomon incorporated a public limited company, called Salomon & Co. Ltd. to take over his personal boots and shoes business. The seven subscribers to the memorandum of association of Salomon & Co. Ltd. were Salomon, his wife, daughter and four sons. In Salomon & Co. Ltd., Salomon's wife, daughter and four sons held one share each of £1 each. The board of directors of Salomon & Co. Ltd. consisted of Salomon, as the managing director, and his two sons as directors. Through a resolution of the board of directors, Salomon's personal business was transferred to Salomon & Co. Ltd. at an agreed price of £ 30,000. In payment of purchase consideration, Salomon was allotted 20,000 shares of £ 1 each, and debentures worth £ 10,000 with a charge on the assets of the company. Within a year of incorporation of the company, owing to the general trade depression, Salomon & Co. Ltd. had to be wound up. On the date of the winding up of the company, the company's position was as follows:

Total assets £ 6,000. Total liabilities; debenture creditors (i.e., amount due to Salomon) £ 10,000 and unsecured creditors (i.e., other creditors)

£ 7,000. In a suit filed before the House of Lords, it was argued, on behalf of the unsecured creditors, that Salomon and Salomon & Co. Ltd. were one and the same, and the company was a mere agent of Salomon. So, they (i.e., the unsecured creditors) should be paid in priority to Salomon. However, the House of Lords held that the company was, in the eyes of law, a separate person distinct from Salomon, and was not the agent of Salomon. So, as a secured creditor, Salomon was entitled to repayment in priority to unsecured creditors.

The separate entity of a company was also upheld in the Indian case of Inre Kondoli Tea Co. Ltd. In this case, a certain tea estate was transferred to a company by certain persons who became the shareholders of the company. These persons claimed exemption from ad valorem duty on the ground that the transfer was from them to themselves under another name. The court rejected their contention and held that the company was a separate body altogether from the shareholders, and the transfer was a transfer of the property, as if the shareholders had been totally different persons.

The significance of separate entity principle is:

- (i) As a joint stock company has a separate legal entity, it can enter into contracts, acquire and dispose of properties, sue and be sued in its own name like a natural person.
- (ii) Further, this feature has given perpetual existence to a joint stock company. That is, members may die, but the company continues to exist.
- (iii) Again, this feature has contributed to separation of ownership and management in the case of a joint stock company.

It is true that a joint stock company has a separate legal existence quite distinct from that of its members, and so, can act in its own name. But, as it has no physical existence, it cannot act by itself. It has to act only through some human agency, viz., the board of directors.

7. Separate Property:

A company is a legal entity (i.e., person) distinct from its members. **So, it has the right to own, enjoy and dispose of property in its own name.**

Though the capital of a company, with which the assets of the company have been acquired, was contributed by the shareholders,
