PART II

INCORPORATION OF COMPANY AND MATTERS INCIDENTAL THERETO

Certain Companies, Associations and Partnerships to be Registered as Companies under Act.

S. 11. Prohibition of associations and partnerships exceeding certain number.—(1) No company, association or partnership consisting of more than ten persons shall be formed for the purpose of carrying on the business of banking, unless it is registered as a company under this Act, or is formed in pursuance of some other Indian law.

(2) No company, association or partnership consisting of more than twenty persons shall be formed for the purpose of carrying on any other business that has for its object the acquisition of gain by the company, association or partnership, or by the individual members thereof, unless it is registered as a company under this Act, or is formed in pursuance of some other Indian law.

(3) This section shall not apply to a joint family as such carrying on a business; and where a business is carried on by two or more joint families, in computing the number of persons for the purposes of sub-sections (1) and (2), minor members of such families shall be excluded.

(4) Every member of a company, association or partnership carrying on business in contravention of this section shall be personally liable for all liabilities incurred in such business.

(5) Every person who is a member of a company, association or partnership formed in contravention of this section shall be punishable with fine which may extend to [1][*ten thousand rupees*].

NOTES

Eng. Act, 1948 : Secs. 429-434
Eng. Act, 1985 : Secs. 716, 720

Previous Act : Sec. 4

Companies Act, 1956

Excepting drafting improvements, there is no change in this section. The words "as such" in sub-section (3) have been newly added in order to take away the exemption from those cases where the members of a joint family, otherwise than as members of such family carry on the business.

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1. The words "one thousand rupees" substituted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 5 (w.e.f. 13-12-2000).

Companies (Amendment) Act, 2000

Sub-section (5) has been amended by the Companies Amendment Act, 2000 to enhance the penalty by way of fine from one thousand Rupees to ten thousand Rupees.

Object and Scope of Section

The section is intended to prevent the mischief arising from large trading undertakings being carried on by large fluctuating bodies, so that persons dealing with them did not know with whom they were contracting and so might be put to great difficulty and expense. This was a public mischief to be redressed. *Smith v. Anderson,* (1880) 15 Ch D 247 at 273.

In sub-section (1) the words "or is formed in pursuance of some other Indian law" probably mean 'formed and having its existence recognised by some other law in force in India'. *Cf. Re, Ilfracombe Permanent Mutual Benefit Building Society,* (1901) 1 Ch 102.

Where the members of a chit fund together with the organiser were less than 20, the association was held to be out of the scope of this section. *Sketna Dev Padmiah v. Firm of Srigiri Venkiah,* AIR 1953 Hyd 142 at 143.

Meaning of—'Person'

The word 'person' is not defined in this Act but in the General Clauses Act, 1899 [s. 3 (39)] as including a company or other association or body of individuals. Notwithstanding this, it has been held that the expression 'persons' in this section means only individuals and not bodies of individuals, *Senaji Kapurchand v. Pannaji Devichand,* AIR 1930 PC 300 **affirming** ILR 50 Mad 175. See also *Akola Gin Combination v. North Cote Ginning Factory,* AIR 1914 Nag 26. This confusion has been cleared by the decision of Madras High Court in *Sri Murugan Oil Industries (P.) Ltd. v. A.V. Suryanarayan Chettiar,* (1963) 33 Com Cases 833 : AIR 1963 Mad 128 where it was held that in case a company enters into a partnership, the company shall be taken as one person. There is no reason why incorporated bodies which are legal persons and each of which consists of more than twenty members cannot form themselves into partnerships for carrying on joint business, provided that they are authorised by their memorandum of association. Nor can there be any legal objection for companies and individuals forming partnership firms for purposes of trade. For the purposes of the next section (s. 12), the word 'person' has been held as including companies and corporations (*Cf.* HALSBURY'S LAWS OF ENGLAND, 51 (Vol. 7, para 75, 4th Edn.).

Illegal association

An association contravening this section is an illegal association and while it cannot sue on a contract made by it, its members will be individually liable on such contract. There can be no cause of action on the basis of an illegal association. *Kumaraswami Chettiar S.N.T. v. M.S.M. Chinnathambi Chettiar,* (1950) 20 Com Cases 286 : AIR 1951 Mad 291. The consequence of the illegality of a partnership is that its members have no remedy against each other for contribution or apportionment in respect of partnership dealings and transactions.

An illegal association under the section is not an association for illegal purpose. Section 11 only makes the association illegal, that is, the law does not recognise the right of more than 10 or 20, as the case may be, persons to carry on business as an association. But that does not imply that the business of the association is unlawful. Failure to register a firm under the Companies Act can have no effect upon the legality of its business. *Ravje Khimji v. Devchand Ghelabhai,* AIR 1951 Kutch 55.

The mere fact that an association is formed on the orders of the Government does not take it out of the scope of this section if the other requirements are satisfied. Thus a syndicate called "Punjab Yarn Dealer Syndicate" was formed on the orders of the Government and it was held that the order could not be taken to authorise the formation in viola-

tion of the Companies Act. *Pala Shah Hazari Shah v. Daya Lal P. Shah,* (1956) 58 Punj LR 338 (Punj).

An illegal association cannot sue to recover any debt or other property. *Jennings v. Hammond,* (1882) 9 QBD 225. Nor can it be sued to recover money lent to it to carry out its objects. *Phillips v. Davies,* (1888) 5 TLR 98 and persons making other contracts with an illegal company may not be able to enforce them against it. *Re, Padstow Total Loss and Collision Assurance Association,* (1882) 20 Ch D 137. But any person who is in possession of money or property received on behalf of an illegal association may be sued to render an account. See *Greenberg v. Cooperstein,* (1926) 1 Ch 657.

It would seem, however, that the rights and liabilities of persons in relation to illegal associations have not been clearly settled, and each case will have to be decided on principles of equity.

Although the members of an association do not at its inception exceed twenty, the association will nevertheless become illegal, if the membership subsequently exceeds twenty. This is clear from the language of sub-section (4). It has been held that it did not matter that an association in its inception was comprised of less than twenty persons and subsequently grew beyond that figure. CAVE. J observed that otherwise "we would be making a laughing stock of the Act". *Thomas, Re,* (1884) 14 QBD 379.

But such an association may get itself registered, and after becoming legal may enforce its claims (*ibid*).

Carrying on business for 'acquisition of gain' [Sub-section (2)]

Note that the section will apply only where a company, association or partnership carries on a business and has for its objects the acquisition of gain either by itself or by any of its members.

Both the expressions 'business' and 'acquisition of gain' are, however, to be given the widest possible meaning; charitable, religious, scientific and other associations not having for their object the acquisition of gain being alone excluded. *IRC v. Korean Syndicate Ltd.,* (1920) 1 KB 598 and on appeal (1921) 3 KB 258. The expressions indicate undertakings of a commercial nature as distinguished from literary, social and other associations and clubs. The test is whether what is done will be considered by ordinary persons as carrying on business. In all cases, the ordinary businessman's point of view has to be adopted. *Armour v. Corporation of Liverpool,* (1939) 1 All ER 363 (Ch D). See *D.D. Dawson v. King,* (1939) 9 Com Cases 254 (Rang), where the liability to punishment under the section arose as soon as money was collected and business operations commenced for a proposed company and it was immaterial that share certificates had not been issued to the members.

The term 'carrying on business for acquisition of gain' must be construed widely so as to include any form of commercial undertaking, even though the gain may not be capable of being distributed, as in the case of companies licensed under section 25 of the Act. Neither the word 'business' nor the word 'gain' is susceptible of precise definition. The test is what ordinary persons describe as the carrying on of a business for gain. See *Armour v. Liverpool Corporation,* (1939) 1 All ER 363. The term 'gain' was interpreted by the Rangoon High Court in *Tan Waing v. Bo Hein,* (1933) 3 Com Cases 112 : AIR 1932 Rang 167 wherein CHIEF JUSTICE PAGE, who delivered the judgment, observed: "The word 'gain' means acquisition. It has no other meaning. Gain is something obtained or acquired. It is not limited to pecuniary gain. The word 'pecuniary' will have to be added to limit it so. And still less is it limited to commercial profit. Commercial profits, no doubt, are gains but there is nothing limiting gain simply to a commercial profit. The words may be taken as referring to a company which is formed to acquire something, as distinguished from a company for spending something, and in which the individual members are simply to give something away or to spend something and not to gain any-

thing". **Approved** in *Dayal Singh v. Desraj,* (1963) 1 Comp LJ 100 (Punj). Also see *Pattada Uthayya v. Pattada Somayya,* (1956) 26 Com Cases 121 (Mys).

An association of more than twenty members who had blended together for the purpose of purchasing cloth and selling it at a profit and for distribution the same among the members was held to be hit by the provisions of the section. The mere fact that a number of such associations of cloth dealers were formed under the advice of the Textile Control Department for convenience of organising purchases and sales could make no difference, and would not absolve such a body from the necessity of getting itself registered if the business which it carried on was for the profits of the members. There was no need to incorporate in the Act a statutory provision barring a suit by such an illegal body. It is a fundamental principle that an illegal body cannot maintain a suit. *Union of India v. The Commercial Association, Amritsar,* AIR 1959 Punj 104.

Four firms consisting of more than twenty individuals formed a syndicate which was not registered as a company and entered into a pooling contract with three of the firms for the sale or purchase of yarn. A suit was brought against the three firms by the fourth firm to recover damages for failure to take delivery of 1,500 bales. It was held that the transaction was in the nature of business within the meaning of this section and as the syndicate was composed of more than 20 individuals, and not registered, it was an illegal association and the suit was not maintainable. *Pannaji Devichand v. Senaji Kapurchand,* (1934) 4 Com Cases 444 : AIR 1934 Bom 361.

Where the evidence available from the plaintiff's own witnesses was clear to show that an element of acquisition of gain did enter into the formation of Naj Vitran Committee and was also one of the objects with which it was formed, it was held that the association was in violation of this section and therefore the plaintiff was not entitled to sue for recovery of his loan. *Bapulal v. Laxmi Bharat Trading Co.,* AIR 1966 Raj 14 at 16, 17.

Where an association of more than twenty persons, like the Bombay Stock Exchange, which is not registered, does not carry on business for acquisition of any gain for itself, the same has been held not to come within the prohibition of sub-section (2). *Ruia V.V. v. Dalmia S.,* (1968) 38 Com Cases 572 : AIR 1968 Bom 347. The prohibition under this section will come into play only on four conditions being satisfied—(1) There must be a company or partnership, etc. of more than 20 persons, (2) it must not have been registered under the Companies Act or any other Indian law, (3) it must have been formed for the purpose of carrying on business other than banking, (4) Finally the business must have for its object acquisition of gain by the company, partnership, etc. at pp. 577, 578 (*ibid*).

Similarly, the association of cloth dealers which had for its objects only a fair distribution of the quota of cloth allotted by the Central Government amongst its members was held to be not an association for gain to its members. *Bhawanilal Lachchi Ram v. Badri,* AIR 1964 MP 153. A trade association is not unlawful merely because it has not been registered. *Bhola Nath Shankar Das v. Lachmi Narain,* (1931) 1 Com Cases 328 (All).

It was pointed out by RANGNEKAR J. in *New Mofussil Co. Ltd. v. Rustomji,* (1936) 38 Bom LR 408 (a case under the Act of 1913): "if an association is not formed for carrying on any business, but as the result of the combination or agreement between the members, there is gain, either to the association or to its members, the case does not fall within the purview of sec. 4 (now sec. 11) of the Act. He therefore held that a "pool" agreement between various partnership firms (consisting of more than 20 members in all), for the purpose of eliminating unnecessary competition and for regulating prices, was not within the section so as to make the partnership compulsorily registrable under sec. 4 of Act, 1913. Associations formed for mutual indemnity and trusts of hazardous securities, like shares, for the purpose of investment and for the saving of loss, are not compulsorily registrable, as there is no "business" which they seek to carry on". *Smith v. Anderson,* 15 Ch D 247.

Following have been held to be associations not for gain:

(1) Superannuation fund, *Armour v. Corporation of Liverpool,* 1939 Ch 422.

(2) Land development and housing associations confined to their members only because they are not supposed to do any business of selling land or houses. *Wigfield v. Potter,* (1881) 45 LT 612; *Siddal, Re,* (1885) 29 Ch D 1; *Crowther v. Thorley,* (1884) 50 LT 43.

(3) A sickness benefit club (state club) *One and All Sickness and Accident Assurance Association,* (1909) 25 TLR 674.

(4) Investment trust in which though members were more than twenty, the management trustees were less than twenty. *Smith v. Anderson,* (1880) 15 Ch D 247.

(5) Bombay Stock Exchange. *Ruia (V.V.) v. Dalmia S.,* (1968) 38 Com Cases 572 : AIR 1968 Bom 347.

(6) An association of cloth dealers which had for its objects only a fair distribution of the quota of cloth. *Bhawanilal Lachchi Ram v. Badri,* AIR 1964 MP 153.

Following have been held to be association for acquisition of gain:

(1) A mutual insurance club. *Arthur Average etc. Association,* (1875) 10 Ch App 542; *Padstow Total Loss Assn.,* (1882) 20 Ch D 137.

(2) A building and loan society, *Shaw v. Benson,* (1883) 11 QBD 563; *Greenberg v. Cooperstein,* (1926) 1 Ch 657.

Position of joint families [Sub-section (3)]

The section does not apply to the case of a single joint family carrying on any business whatever may be the number of its members. But it must be noted that while the joint Hindu family as such, that is in its capacity of joint family, does not come under the section, if members of the family carry on business as partners instead of as a joint family, they will come under the prohibition.

An association of more than twenty persons carrying on business for gain is only permissible if it is a Hindu joint family business. Such an association would be illegal even if it is a partnership of two or more joint families as s. 11(3) in terms indicates. It is not correct to say that when two or more joint families represented by their *kartas* enter into a partnership the number of members for the purpose of this section would be the *kartas* and not the other members of the joint family represented by their *kartas*. Such a partnership of *kartas* would be illegal if the number of adult members of the joint family exceeds 20. *Shyamlal Roy v. Madhusudan Roy,* AIR 1959 Cal 380 at 385.

As the expression used in the section is 'member of joint family' and not 'coparceners of joint family', it is clear that it includes all the members—males and females, other than minors who are expressly excluded.

As regards two or more joint families carrying on business, the Supreme Court in *Agarwal & Co. v. CIT,* (1970) 77 ITR 10 : AIR 1970 SC 1343, has observed that "the assumption in section 4(3) of the Companies Act, 1913 (corresponding to section 11(3) of the Companies Act, 1956) that a Hindu joint-family can be a partner in a partnership appears to be based on an erroneous view of the law". But the observation does not take into account the fact that the section covers also cases of associations other than partnership, and there is no reason why two or more joint-families cannot carry on business in such associations, without coming within the scope of the Partnership Act. In such cases, if, by reason of a minor member of any one of the joint families attaining majority, the number of persons exceeds the limit prescribed by sub-section (1) or (2) as the case may be, the association, if it carries on business, will *ipso facto* become illegal. But as regards the application of the penal provisions of sub-section (5), it may well be contended that the provision will apply only where a company, association or partnership, is formed in contravention of the section and not where the illegality supervenes at a subsequent stage. See however *Nibaran v. Lalit,* AIR 1939 Cal 187.

Male and female members to be included

Department's views.—"Both male and female adult members have to be taken into account in computing the number specified in sub-sections (1) and (2) for the purpose of sub-section (3) of section 11 of the Companies Act." (*Department's letter No.* 8/10(11)/65-CL-V, dated 11-2-1965).

Joint rights and ownership

The word 'association' in this section implies the existence of a legal relationship involving joint or mutual rights and/or relations. Where in a chit fund there are a large number of subscribers, there is no legal relationship between them and they do not come within the prohibition of this section. *'G.K. Naidu v. G.K. Mouleshwar'*, AIR 1962 AP 406; *T.P. Naidu v. A.S. Mudaliar*, AIR 1919 Low Burma 102.

The concept of an association under the section is that of carrying on business collectively. Joint-ownership, or one-time ventures are not covered by this section. For example, the section does not prevent the ownership of an asset by more than 20 persons, provided that owning assets is not the business of the persons.

The defendant had obtained a license for catching elephants in a Hill District. He organised a *kheda* but not having sufficient money of his own, subsequently joined in the enterprise the plaintiff and several other persons numbering over twenty persons under a deed of partnership which provided that the entire charge of catching and selling elephants would rest with the defendant and that the other partners would not be allowed to interfere with that. It also appeared that although the defendant's *patta* authorised him to take partners, there was no promise on the part of the Government to recognise, nor did it recognise, them as partners in the business so as to create direct relationship between them and the Government. The deed of partnership was not one executed by all the partners in favour of all but one between the defendant on the one side and the other partners on the other. It was held **applying** the principles of *Smith v. Anderson*, LR 15 Ch Div 247 (1880) and *Crowther v. Thorle*, 32 WR 330 (1884), that the case did not come within the scope of section 4 of the Companies Act, 1882 [S. 11 of 1956 Act]. All the members of a company or association must be directly interested in the management of the concern either personally or through their duly constituted agent. *Bipul Chandra Gupta v. Hazi Nasir Ali*, (1908-9) 13 CWN 638 (Cal).

Distinction between company and partnership firm

Partnership is merely an association of persons for carrying on the business of partners and 'firm', is a compendious method of describing the partners. But a company incorporated under the Companies Act is a separate juristic person distinct from the shareholders. A firm, however, is not a person. *Bacha F. Guzdar (Mrs.) v. CIT*, (1955) 25 Com Cases 1 : AIR 1955 SC 74. A pooling contract is not a partnership or an association, *Madan Gopal v. Shewal Das*, (1934) 4 Com Cases 339 (Lah), nor a chit fund, *T.P. Naidu v. A.S. Mudaliar*, AIR 1919 Low Burma 102.

Sub-partners not to be counted.—A sub-partner is not a member of the firm and does not affect the number of members for the purposes of this section *Chandulal Damodardas v. Keshavlal Kuberdas Amin*, (1936) 6 Com Cases 295, 298 (Bom); see also *B.C. Ginning Factory v. Govinda Vishnusa*, (1934) 4 Com Cases 214, 218 (Nag), where 16 joint families totalling to 48 members formed partnership and it was held that the section was not violated because agreement was between the families only and their members were mere sub-partners.

Professional firms exempted in U.K.

Part IV of the English Companies Act, 1985, has expressly exempted professional partnerships from the applicability of the section which corresponds to the present section of the Indian Act.

The exemption of professional partnerships has been extended under s. 717 of the English Act of 1985 to limited partnerships also.

Consequences of illegality [Sub-sections (4) and (5)]

One of the consequences of the illegality of an association as emphasised by Sub-section (4) is that every member shall be personally liable for all the business obligations of the association. In addition, the members are also liable to a fine up to Rs. 10,000. Though the members of such an association cannot be punished for having formed themselves into a company, they can be punished for continuing to be members of it. *Muthuveeran Chettiar v. Mottayan Chettiar,* (1942) 12 Com Cases 86 : AIR 1942 Mad 283.

The offence is compoundable under section 621A.

Neither the association nor its members can initiate any proceeding for enforcing any contract made with a third person. For example, the price of goods sold cannot be recovered. An association of this kind cannot be wound up under the Act, not even under the provisions relating to unregistered companies. There can also be no suit between members for dissolution and accounts. Where an association, formed for the purpose of gain is not registered, although under the law it ought to have been registered, none of its members can sue in a court of law for partition of its existing assets. *Mewaram v. Ramgopal,* AIR 1926 All 591; *Madan Lal v. Janki Prasad,* AIR 1927 All 487. See also *Kumaraswami Chettiar (S.N.T.) v. Chinnathambi (M.S.M.),* (1950) 20 Com Cases 286 : AIR 1951 Mad 291; *Pattada Uthayya v. Pattada Somayya,* (1956) 26 Com Cases 121, 125 (Mys). In *Seth Badri Prasad v. Nagarmal,* AIR 1959 SC 559 at 563 : (1959) 29 Com Cases 229 the Supreme Court **approved** the opinions expressed in the Privy Council decision in *Senaji Kapur Chand v. Pannaji Devichand,* AIR 1930 PC 300, and held that when the association is itself illegal, the court cannot assist the plaintiffs in getting accounts made so that they may recover their share of the profits made by the illegal association. But the subscribers will be entitled to sue for recovery of their subscriptions and for this purpose, have the assets realised, as according to the Supreme Court, no illegal contract is sought to be enforced thereby, but rather the continuance of illegality is sought to be prevented. *Seth Badri Prasad v. Seth Nagar Mall, (Supra).* It was also held that where there is a contravention of legal provisions, it being a matter of law, a plea about it can be raised at any stage of the proceeding.

The Ajmer High Court in its decision in *Jagannath v. Peerulal,* AIR 1953 Ajmer 14, **not following** the decision of the Allahabad High Court in *Mewaram v. Ram Gopal,* AIR 1926 All 591, held that a suit by members of an association, which is illegal by reason of non-registration, for refund of the amount contributed and for rendition of accounts is maintainable. The Court **followed** the decision in *U. Sein Po v. U. Phyu,* AIR 1930 Rangoon 21.

Where the business of a partnership had been carried on for some time, and the contribution by the plaintiff to the business of the association, illegal under s. 4 of the Companies Act, 1913, [CA 1956, s. 11] had been applied to the business, the plaintiff cannot claim the refund of his contribution. But where the agreement has been made and the contribution has been paid by one associate to another, but the business has not been started, there is an equitable principle that the associate should get back the money. The principle of *pari delicto* does not come into play because the *delict* though contemplated and agreed to had not yet been committed. *Ram Dass v. Mukut Dhari,* AIR 1952 VP 1 at 3.

An illegal association has no *locus standi* in court and cannot sue in respect of any cause of action, *Waller v. Gipps,* (1885) 6 N S W Eq 40 (Australia). A contract with an illegal association being unenforceable, a guarantee given under it would not make the surety liable. *Eaton Robins and Co. v. Nel,* (1909) 26 SC 365 (S. Africa). An illegal association formed for the business of money lending cannot sue on a pronote in its favour, since the consideration for the note is illegal. *Jennings v. Hammond,* (1882) 9 QBD 225; *Shaw v. Benson,* (1883) 11 QBD 563 (CA).

The effect of non-registration is that the company, association or partnership will have no legal existence as such but it does not prevent the individual members from transacting business with third parties. A contract entered into by a member of an unregistered

association in individual capacity with third parties cannot be held illegal or void from the mere fact that one of the contracting parties was a member of the association which had no legal existence. *Hasanali Khurjibhai v. Ratilal Nyalchand Chitalia,* AIR 1953 Sau 141 at 142.

Members of illegal company may be indicted for theft.—The members of an illegal company may be beneficial owners of property. If an officer of the company embezzles funds entrusted to him, he may be indicted for theft—*R. v. Tankard,* (1894) 1 QB 548 : (1894) All ER Rep Ext 1483.

Directors' liability.—Directors of an illegal association are personally liable for the goods sold to the company. *Masterton v. Blair,* (1871) 2 VR 19 (Australia). A person who sold stationery to an association not knowing of its illegality was allowed to recover from those with whom he contracted. *One and All Sickness and Accident Assurance Association, Re,* (1909) 25 TLR 674.

Winding up of illegal company.—On its own petition or that of a member of an illegal company cannot be wound up by the Court under the Companies Act, *Re, Mexican and South American Mining Co., Barclay's* Case, (1858) 26 Beav 177 at 179, 180, or on the petition of a creditor, particularly where the petitioner had notice of the illegality. *Re, Padstow Total Loss and Collision Assurance Association,* (1882) 20 Ch D 137, (1881-5) All ER Rep 422 CA. Where, however, a winding up order happens to be made, it is effective unless and until discharged on appeal and, while it exists, the illegality of the company is not a bar to proceedings in the winding up. *Re, Arthur Average Association,* (1876) 3 Ch D 522; *Re, Queen's Average Association, ex parte Lynes,* (1878) 38 LT 90.

Sale of shares of illegal company.—The sale of shares or scrip in an illegal company is illegal. *Josephs v. Pebrer,* (1825) 3 B&C 639. A broker who is employed to sell or purchase them cannot recover from his principal any commission or any sums expended on his behalf. *Re, Edmond, ex parte Neilson,* (1853) 3 De GM & G 556. The buyer cannot recover any purchase money paid to the broker if he was aware of the illegality. *Buck v. Buck,* (1808) 1 Camp 547.

Company's right to set up defence of illegality

The defence of illegality is not open to the company in an action against it by an innocent stranger. The reason is that the company would be taking advantage of its own wrong. In *Appa v. Ramkrishna,* (1929) 31 Bom LR 1187 : AIR 1930 Bom 5, the plaintiff sued to recover moneys due at the foot of an account from the defendants who were carrying on business in the native State of Sangli, and the defendants contended that their firm was an illegal firm under sec. 4 of the Companies Act of 1913 and that the plaintiff should therefore be non-suited. It was held that, assuming that the Act applied to the defendants, it was not open to them to rely on the illegality of their association as an answer to the plaintiff's claim. It would be otherwise of course, if the person dealing with the association, had knowledge of its illegality. The Court **followed** *South Wales Atlantic Steamship Co.,* (1876) 2 Ch D 763.

An illegal company may set up its own illegality in answer to proceedings against it. *Doolan v. Midland Rly. Co.,* (1877) 2 App Cas 792 at 806, HL. Where this defence is allowed the company may not be allowed costs. *Phillips v. Davies,* (1888) 5 TLR 98; *Re, Ilfracombe Permanent Mutual Benefit Building Society,* (1901) 1 Ch 102.

Penalty for default (sub-section (5))

Every person who is a member of a company or association or partnership formed in contravention of this section is punishable with fine upto Rs. 10,000.

Offence compoundable.—The offence is compoundable under section 621A.

Section not applicable to foreign companies and other bodies corporate

The application of the section is confined to 'companies' and does not extend to 'bodies corporate' [See definition in section 2(7) and (10)]. The prohibition in the section has,

therefore, no application to corporations incorporated under any special laws or to foreign companies or other bodies corporate.

MEMORANDUM OF ASSOCIATION

General Notes

THE MEMORANDUM of association is the document which lays the foundation of the company. Its five clauses are of primary importance as they provide the basic features of the company's constitution. After registration the memorandum becomes a public document. While the memorandum must comply with the provisions of the Companies Act, all other documents of the company cannot go beyond the memorandum. The document controls the business field of the company and the conduct of its management through its objects clause. The company has to keep itself within the limits set by the memorandum. Those who deal with the company are deemed to have notice of the contents of the memorandum. The result is that the outsiders who come into contact with the company have also to observe the conditions stated in the memorandum. The courts cannot impose any liability upon the company, whether in reference to insiders or outsiders, which would have the effect of taking out any portion of the corporate money or resources for any purpose not warranted by the terms of incorporation as specified in the memorandum. Thus the document affects the life of the company in its internal as well as external relations. That is why its contents are not permitted to be altered except with the sanction of one or the other public authorities. The name of the company cannot be changed without the approval of the Central Government. The objects may be altered by passing special resolution. The registered office may be shifted from one State to another only with the sanction of the Company Law Board. Authorised share capital may be increased by passing ordinary resolution but paid-up capital may be reduced only with the sanction of the High Court and liability of members may be increased only with their consent in writing. Every alteration must be registered with the Registrar, otherwise it lapses and becomes a waisted effort. The memorandum must be printed. Computer printing is recognised for this purpose. An advance approval of the proposed name should be obtained before going to the length of printing the document. [See *Selvarajan & Co. v. ROC*, (1987) 62 Com Cases 220 (Mad)].

By and large, similar provisions apply to the memorandum of association of a producer company under Chapter II of Part IXA to this Act.

Its provisions may be supplemented by the articles of association which contain the working rules for the management of the company's affairs.

Memorandum of Association

S. 12. Mode of forming incorporated company.—(1) Any seven or more persons, or where the company to be formed will be a private company, any two or more persons, associated for any lawful purpose may, by subscribing their names to a memorandum of association and otherwise complying with the requirements of this Act in respect of registration, form an incorporated company, with or without limited liability.

(2) Such a company may be either—

(a) a company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them (in this Act termed "a company limited by shares"); or

(b) a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake

by the memorandum to contribute to the assets of the company in the event of its being wound-up (in this Act termed "a company limited by guarantee"); or

(c) a company not having any limit on the liability of its members (in this Act termed "an unlimited company").

NOTES

Previous Act : Sec. 5

Eng. Act, 1948 : Sec. 1
Eng. Act, 1985 : Sec. 1

'Seven or more persons' : 'Two or more persons'

Though for forming a public company, seven or more persons, and for forming a private company, two or more persons are required to subscribe their names to a memorandum of association, it is not necessary that the subscribers should have any personal beneficial interest in the shares subscribed for by them. All of them may be nominees of a single person and their subscribing their names may be merely a formality. This position became established by the decision in *Salomon v. Salomon & Co.*, (1897) AC 22. A related case to the *Salomon* case is that of *Broderip v. Salomon*, (1895) 2 Ch 323 (CA). Broderip was the person to whom Salomon had sold his debenture. The *Salomon* case was an appeal from this decision to the House of Lords. The practice of nominee shareholdings is also statutorily recognised in various sections of the present Act [*Cf.* Section 49(3).]

'Person' includes a company and on behalf of company as well as of any other person, an agent duly authorised may sign. But a 'firm' as such cannot sign, as a firm is not 'person'. If the partners of a 'firm' subscribe, they become joint holders of the share or shares subscribed for. The Registrar will not accept the signature of the firm as a subscriber but only if the partners individually sign as joint subscribers. See *Re, Land Credit Co. of Ireland, Weikersheim's* case, (1873) 8 Ch Appeal 831; *Re, Glory Paper Mills Co., Dunster's* case, (1894) 3 Ch 473. Nor is a firm entitled to be registered as member in the name of the firm but only in the names of the individual partners. *Re, Vagliano & Anthracite Collieries Ltd.*, (1910) 79 LJ Ch 769.

The promoters must subscribe for atleast as many shares as would make up company's paid up capital to the minimum prescribed limit under Sec. 3(1)(iii)/(iv)(b).

Subscriber

Any person who is competent to contract can be a subscriber. A company being a legal person can subscribe. A partnership not being a legal person cannot do so; an individual partner must subscribe.

A subscriber to the memorandum of association need not be beneficially interested in the shares for which he has subscribed as may be the case in the case of the trustee of a trust, where the beneficiary or beneficiaries are other persons. *Salomon v. Salomon & Co.*, 1897 AC 22. According to the *Department's Circular No.* 8/15/8, dated 1-9-1958 "an agent may sign a memorandum, on behalf of a subscriber if he is authorised by a power of attorney to do so." See *Whitley Partner's, Re,* (1886) 32 Ch D 337. The same course may also be followed in respect of any amendment to the memorandum and articles of association, suggested by the Registrar (*Department's Circular No.* 128/HCC/64, dated 27-7-1964). The full text of the Circular is reproduced hereunder:

Text of Department's Circular.—"It has been brought to the notice of the Company Law Board that some Registrars of Companies have been insisting that the Memorandum of Association of a company and any amendment thereto should be signed by the subscribers themselves and not through their constituted attorneys and that this is causing some practical difficulties, especially where some of the subscribers to the memorandum are foreign parties who may be collaborating with Indian promoters. The matter has been carefully examined by the Company Law Board and it has been decided that when it is not possible for a company, it may be signed on its behalf by an agent if the latter is authorised by a power of

attorney to do so. The same course may also be followed in respect of any amendment to the memorandum or articles which it may be found necessary to make as a result of any suggestions in this behalf made by the Registrar concerned after the scrutiny of the memorandum and articles presented to him for registration of articles. In this connection, attention is also invited to the last sentence of para 2 of the former Department of Company Law Administration's *circular letter No.* 8/15/8 dated the 1st September, 1958 wherein it was stated that "An agent may sign the memorandum on behalf of a subscriber if he is authorised by a power of attorney to do so".

A suggestion has been made to the Company Law Board that it would be helpful to promoters if the Registrar could scrutinise and approve the draft Memorandum and Articles of a proposed company before they are presented to him for registration. Though it may not be possible for Registrars to accept a definite commitment in this regard, the Board is of the view that the Registrars should to the extent possible offer their help and advise to those who may approach them in drawing up the Memoradum and Articles. This would be specially desirable in cases where promoters have no prior experience of company promotion. All Registrars are advised to take necessary action accordingly." [*Department's Circular No.* 128/HCC/64, dated 27-7-1964].

A person becomes a subscriber by signing the memorandum as a subscriber and at the place intended for that purpose. If a person's name does not appear in the list of subscribers he is not a subscriber even if his signature appears on all the other pages of the memorandum. *Arthanari Transports (P.) Ltd. v. K.P. Swami Goundar,* (1965) 35 Com Cases 930.

A minor cannot be a signatory to the memorandum and articles of association of a company to be incorporated since he is not competent to contract. The guardian of a minor who subscribes to a memorandum on behalf of the minor will be deemed to have subscribed in his personal capacity. See *Palaniappa v. Official Liquidator,* AIR 1942 Mad 470 and notes under Sec. 41.

"Persons" include corporations and infants. An infant member can repudiate the contract which arises from his signature but such repudiation does not invalidate the incorporation. *Herfordshire Brewery Co., Re,* (1874) 43 LJ Ch 358.

In the case of a joint Hindu family, as it is not a person it cannot be a subscriber, though the *kartha* or manager may be one. If the *kartha* or manager uses family funds, it is a matter of accountability or adjustment as between the family members *inter se* and the company whose shares are subscribed for is not concerned with it.

In the case of an illiterate subscriber to the memorandum and articles of association, the thumb impression or mark duly attested by the person writing for him should be given. The person attesting the thumb mark should make an endorsement on the document to the effect that it has been read and explained to the subscriber. (*Department's Letter No.* 8/31/15/80 CL-V, dated 31-3-1981).

As regards the Central Government and State Governments none of them can be a subscriber but the President of India or the Governor of a State may be one through the Secretary to the Government of India or the State Government, as the case may be. Section 187-A shows that the Act contemplates only the President of India and Governors of the State as capable of becoming the members of a company. See also Article 299 of the Constitution.

Incorporated company as subscriber.—An incorporated company can subscribe to the memorandum of a company by authorising a person to sign on its behalf. Since subscription to memorandum inevitably means investment in the shares of a company, it is necessary that a resolution as required by s. 292(1)(d) should be passed at a meeting of the Board authorising the investment. The provisions of section 372A which restrict one company's right to invest its funds in the securities of another company should also be kept in mind.

Partnership cannot be member

Department's Clarification.—"A firm, not being a person cannot be registered as a member of a company except where the company is licenced under section 25 of the Companies Act, 1956. Companies which have firms registered as shareholders should be advised to take steps to rectify the position

within a specified time. In case the irregularity persists, despite a warning, necessary action can be taken under section 150(2) of the Act". [*Circular No.* 4/72, dated 9-3-1972].

Subscription by NRIs, resident foreigners and foreign companies

All the subscribers may be foreigners and the company will still be an Indian company if registered in India. *General Company for Promotion of Land Credit, Re,* (1870) 5 Ch App 363 and **affirmed** in *Princess of Reuss v. Bos,* (1871) LR 5 HL 176; *Attorney General v. Jewish Colonization Association,* (1901) 1 KB 123. Similarly, a company will be a foreign company, if registered outside India, even though all the shareholders be Indian citizens. *Janson v. Driefontein Consolidated Mines Ltd.,* (1902) AC 484; *Gramophone and Typewriter Ltd. v. Stanley,* (1908) 2 KB 89. After the coming into force of the Foreign Exchange Regulation Act, 1973, (Jan. 1, 1974) the above decisions have to be applied subject to the provisions of section 19(1)(b) and (d) of that Act.

The position under FERA, 1973, before its repeal and replacement by FEMA, 1999 was that non-residents could not be subscribers to the memorandum or articles of association without the general or special permission of the Reserve Bank of India [section 19(1)(b) and (d) of the 1973 Act]. The words 'create an interest in a security' (as used in the provisions) included both subscribing for shares and being allotted shares on application. For a person not resident in India to become a member, Reserve Bank's permission was necessary even though he might be a citizen of India. Further, having regard to sections 29(1) and 26(5) of the said Act, it would appear that without Reserve Bank's permission, even resident foreigners could not be subscribers, as their subscribing their names amounted to creating an interest in a business in India and subscribing for shares in a company a mode of purchasing such shares.

Since FEMA, 1999 has dropped major provisions of FERA, and there being no trace of provisions parallel to the above sections, the position of law depends upon clarifications and notification issued under FEMA.

Subscription by persons residing abroad

DCA Circular dt. 16-2-1995—It is clarified that there cannot be any restriction for incorporation of a company where all the subscribers to the Memorandum & Articles of Association/proposed directors are residing abroad, being either foreign nationals or NRIs subject to the approval of RBI, where necessary (Part VI). [*Circular No.* 1/95, *F. No.* 14/6/96-CL-V, dated 16-2-1995].

General permission to NRIs to subscribe to the Memorandum and Articles of Association under FERA, 1973.—*[In order to facilitate NRIs to set up new companies in India, Reserve Bank, *vide* its Notification No. FERA 143/93-RB, dated 26th April, 1993, has granted general permission under section 29(1)(b) read with section 19(1)(d) of the Foreign Exchange Regulation Act, 1973 to NRIs to subscribe to the Memorandum and Articles of Association and to take up the shares of Indian companies for their incorporation. The general permission also empowers such Indian companies to issue shares to NRIs provided the total face value of the shares to be issued does not exceed Rs. 10,000 and the company is not engaged in any activity relating to agriculture and plantation. The Indian company is required to file a declaration of the issue to Reserve Bank in form DSS within a period of 90 days from the date of its incorporation. The repatriability or otherwise of this investment will be decided by Reserve Bank while granting permission under section 19(1)(d) of the Act for issue of further shares to NRIs. [*RBI Exchange Control Manual,* 1993, para 10C.4]

Permission further liberalised w.e.f. 31-10-1995.—The above facility has now been extended to companies "engaged in other activities except agriculture or plantation" *vide Notification No.* FERA 169/95-RB, dated 31-10-1995.

Direct investment in Firms/Companies in India by NRIs.—NRIs are permitted to make direct investment in partnership/proprietorship concerns in India as also by way of subscription to shares/debentures of Indian Companies. They are also permitted to place

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* Subs. by AD (MA Series) Circular No. 1/96, dated 31-1-1996.

funds in company deposits. Similar facilities are also available to OCBs with certain exceptions. Wherever the investments are allowed with repatriation benefits, the funds for the purpose should be received by inward remittances from abroad or from the investor's NRE/FCNR Accounts. However, in respect of investment on non-repatriation basis, funds in NRO Accounts could also be used. [*RBI Exchange Control Manual,* 1993, para 10C.5].

§ For Text of FEMA, 1999 see *Appendix* 101.

The RBI has issued the following Regulations under FEMA, 1999 in respect of these matters:—

— FEM (Deposit) Regulations, 2000 [For text see *Appendix* 110]

— FEM (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 [For text see *Appendix* 118]

For details and further study see B J CHACKO, NRI GUIDE ON TAXATION, INVESTMENTS AND INCENTIVES, Latest Edition.

Lawful purpose

Every purpose is lawful, unless it is forbidden by law or is contrary to public policy. Subject to the purpose being lawful, there is no limit put upon the purposes for which a company may be formed. A company proposed to be registered for an illegal purpose—illegal under any law of this country, cannot properly be registered. *R. v. Registrar of Joint Stock Companies, Ex parte More,* (1931) 2 KB 197, 201 : (1932) 2 Com Cases 99; *R. v. ROC ex p. Bowen,* (1914) 3 KB 1161 (Sale of lottery tickets).

Where the purpose is not lawful, or where any of the objects is illegal, the Registrar may refuse to register; and if he registers, the certificate of registration is not conclusive for the purpose of legitimating the unlawful part of the business. *Performing Rights Society Ltd. v. London Theatre of Varieties,* (1922) 1 KB 539 and the registration itself may be cancelled by the Central Government taking appropriate proceedings. See *Bowman v. Secular Society Ltd.,* 1917 AC 406 (at 438-9). Where a company is registered with objects which involve it entering into contracts which are sexually immoral and hence illegal, the court would grant judicial review of the Registrar's decision to register the company and would strike it off the register. *R. v. Registrar of Cos., ex parte Attorney-General,* 1991 BCLC 476 (QBD). As regards the effect of a company being illegal, see Notes under section 35, *post.*

An unlawful or illegal object in the Memorandum of Association is void and unenforceable.

There is no distinction between the word 'purpose' occurring in section 12 ("lawful purpose") and the word 'objects' occurring in section 13. *Indian Iron & Steel Co. Ltd., Re,* (1957) 27 Com Cases 361 (Cal).

A company will be regarded as having enemy character, if the persons having *de facto* control of its affairs are resident in an enemy country or, wherever they may be, are acting under instructions from or on behalf of the enemy. *Daimler Co. Ltd. v. Continental Tyre and Rubber Co. (Great Britain) Ltd.,* (1916) 2 AC 307; See also *Kuenigl v. Donnersmarck,* (1955) 1 All ER 46 : (1956) 26 Com Cases 1 (QBD).

Investment company trading over prices.—The plaintiff company was authorised to carry on investment business under the [English] Financial Services Act, 1986. The company was carrying on the business of taking bets in the movement of a number of stock market and commodity prices which involved the company's clients placing bets as to the price movement. The plaintiff company won a bet and the other party, the defendant, became indebted but refused to pay saying that the business was unlawful. It was held by the Court of Appeal that the transaction between the plaintiff and the defendant constituted a contract the purpose of which was to make a profit or avoid a loss by reference to

the fluctuations in an index and also constituted a dealing in investments and the plaintiff company was entering into such transactions in the ordinary course of business and being within the permissible range under the Financial Services Act, they were free from the operation of the Gaming Acts. *City Index Ltd. v. Leslie,* (1991) BCLC 643 (CA).

Precaution to be taken in registering Prize Chit Business Companies

Department's Instructions.—The object clauses of the Memorandum of Association of Companies may be scrutinized carefully before their incorporation to see that there is no clause therein which is repugnant to the provisions of Prize Chits and Money Circulation Scheme (Banning) Act, 1978. [*Circular No.* 3/79 (14/20/79-CL-V), dated 16-11-1979].

In a letter addressed to the Registrars of Companies the Department of Company Affairs has further observed: "In continuation of this Department's circular No. 3/79, dated the 16th November, 1979 on the above subject, I am directed to enclose a copy of the letter No. 464/Leg. 13A/82-83, dated 9-8-1982 of the Reserve Bank of India and to say that the suggestion made therein may be kept in view while registering companies with the main objects of conducting Prize Chit Business." [No. 14/20/79-CL-V, dated 20-9-1982].

"We invite a reference to D.O. letter No. DNBC 322/Leg. 13A/79-80, dated 6-8-1979. It is observed that despite the Govt. Circular No. 3/79/14/20/79-CL-V to all Registrars of Companies, incorporation of companies with the main objects of conducting prize chit business continues unabated especially in Delhi. We enclose a statement showing the names of fifty four such companies and the relevant clause in their Memorandum of Association which is repugnant to the provisions of the Prize Chits & Money Circulation Schemes (Banning) Act, 1978. A few such companies have filed writ petitions in the High Courts at Calcutta and Agartala (Bench) contending, *inter alia,* that the Registrar of Companies has not objected at the time of registration to the type of business they proposed to carry on and hence they were carrying on lawful business. In the circumstances we once again request you to instruct all the Registrars of Companies (except in the State of Jammu & Kashmir) to exercise caution while registering such companies." [*RBI Letter No.* DNBC 464/Leg. 13A/82-83, dated 9-8-1982].

Limited liability of members

The use of the word 'limited' indicates that the liability of the members for the debts and other liabilities of the company, is limited to the amount contributed or undertaken by them towards the share capital of the company.

Where the liability of the member is limited, the fact that the company is authorised to carry on business in a country according to whose laws a member of the company is liable for its corporate debts, does not make him liable. *Risdon Iron and Locomotive Works v. Furness,* (1905) 1 KB 304 and on appeal (1906) 1 KB 49.

Liability of members of different kinds of company

Company limited by shares.—The liability of a member in the case of a company limited by shares is limited to the amount for the time being remaining unpaid on the nominal amount of his shares. But, except where the articles otherwise provide, there is no liability to pay any balance amount due on the shares, except in pursuance of calls duly made in accordance with law and the articles while the company is a going concern, or of calls made in the event of winding up of the company. The liability of a member under the English Insolvency Act, 1986, s. 74(2)(d), to pay whatever is unpaid of the nominal value of shares is a statutory liability (*Hansraj Gupta v. Asthana,* (1932) LR 60 Ind App 1, PC) but it does not extend to share premium, which is a matter for contract between the member and the company (*Niemann v. Smedley* [1973] VR 769; *Re Vedelago* (1992) 8 ACSR 135 (Aust.).

Guarantee company.—The liability of a member in the case of a company limited by guarantee, where the company has no share capital, is limited to the amount which he has undertaken by the memorandum of association to contribute to the assets of the company in the event of its being wound up; and where the company has a share capital, he is liable in addition to the amount so undertaken, also to contribute to the extent of any sums remaining unpaid on the shares held by him. [Section 426(2).]

Unlimited company.—In the case of an unlimited company the liability of each member extends to the whole amount of the company's debts and liabilities, but he will be

entitled to claim contribution from other members. In case the company has a share capital the articles of association must state the amount of share capital and the amount of each share (*vide* Schedule I, Table E) and the liability on the shares, so long as the company is a going concern, is the only liability which can be enforced by the company, though the liability of each member is unlimited so far as creditors are concerned. See *Re, Mayfair Property Co., Bartlett v. Mayfair Property Co.,* (1898) 2 Ch 28.

Obviously in the case of an unlimited company, the liability is similar to that of partners although the creditors cannot directly institute legal proceedings against the individual members. Creditors have to institute proceedings for winding up but the official liquidator can call upon the members to discharge the debts and liabilities without limit. Under section 32, an unlimited company can get itself re-registered as a limited liability company but such conversion will not affect prior debts, liabilities and obligations.

An 'unlimited company' is not the same as an unincorporated company, though in both cases, the liability of the members is unlimited. The difference between the two is that while an unlimited company registered under the Companies Act is a legal person with perpetual succession and a common seal, capable of borrowing, suing, and being sued and holding property in its own name, in the case of an unincorporated association the individual members alone have rights and duties, and the association as such has no existence as a legal entity.

Company as a partner

Whether a company can enter into a partnership or not is no longer open to doubt. The Deptt. of Company Affairs has in its *Circular No.* 1-81 (20-1-81-CL-V), dated 14-9-1981 expressed the following view: "A question has been raised whether an incorporated company can enter into a partnership with some other person or some other company. The matter has been examined by this department in consultation with the Department of Legal Affairs and I am directed to say that *prima facie* a company entering into a partnership with some other person or some other company would be *ultra vires* and will be against the principle that a particular company or an incorporated body cannot lawfully employ funds for purposes not authorised by its constitution which would normally be the memorandum and the articles of association. However, a company or an incorporated body, if so authorised by its constitution, can enter into partnership with an individual person or with another company irrespective of nationality and residence. This would, however, require the company to adopt very special articles since many of the provisions of the Partnership Act would be difficult to apply to such a partnership. In view of this, while considering applications for registration of firms with bodies corporate as partners under the Indian Partnership Act, 1932, the State Governments should examine the applications before them and find out whether the memorandum and articles of association of the applicant incorporated companies contain any special articles which authorise the incorporated companies to enter into partnerships and the articles also take care of the possible anomalies which have been pointed out in the Calcutta High Court's ruling in the case of *Ganga Metal Refining Company P. Ltd. v. Income-tax Commissioner West Bengal,* (1968) 38 Com Cases 117 : AIR 1967 Cal 429."

The correctness of the Department's view is open to doubt. The Act itself recognises the legality of a company being partner in a partnership firm. Section 370(1A) contemplates a loan made to a partnership firm having a body corporate as a partner. Schedule VI Part I on assets side under the heading 'Investment', requires the disclosure of capital invested in a partnership firm. Clause (v) of sec. 2(g) of the MRTP Act also contemplates a partnership firm having bodies corporate as its partners. A company being a juristic person can do all that a natural person can, and there is nothing in the principles of partnership which excludes a company from being a partner. A company which is authorised to carry on a business is by implication authorised to carry the same business in partnership or as joint venture.

In PALMER'S COMPANY LAW, p. 207 (24th edition, para 18-12) the position of company as a partner is thus stated: "A company may be a partner in a partnership, indeed all the partners in a partnership may be companies. These companies, like all partners (except limited partners of a limited partnership), are liable for all the debts of the partnership without limitation, that the liability of the incorporators, *i.e.*, the members of those partnerships, is limited is irrelevant."

§ Also refer to Notes in section 3, *ante.*

Secretarial Action Points for incorporation of a private limited company

1. Select, in order of preference, a few suitable names, not less than four, indicative of the main objects of the company. In this connection, refer to guidelines for availability of names and Departmental Instructions regarding procedure in processing of applications. (Ref. *Appendices 1* and 2 of M C BHANDARI'S GUIDE TO COMPANY LAW PROCEDURES).

2. Ensure that the name does not resemble the name of any other company already registered; or any existing trade mark and also does not violate the provisions of Emblems and Names (Prevention of Improper Use) Act, 1950.

3. Apply to the concerned Registrar of Companies to ascertain the availability of name in Form 1A of General Rules and Forms, along with a fee of Rs. 500. The Registrar of Companies informs the status of the application within 14 days. If the name proposed is not available, apply for a fresh name.

4. Arrange for the drafting of the Memorandum and Articles of Association (M&A) by the solicitors, vetting of the same by Registrar of Companies and printing of the same.

5. Arrange for stamping of the M & A with the appropriate stamp duty.

6. Get the M & A signed by at least 2 subscribers in case of a private company and 7 subscribers in case of a public company, each of whom shall also write in his own hand, his father's name, occupation, address and the number of shares subscribed for, up to the required minimum and have it witnessed by at least one person, who shall also write in his own hand, his father's name, occupation and address. The M & A should be signed all the subscribers or their agents duly authorised by a power of attorney.

7. Ensure that the M & A should be dated on a date after the date of stamping.

8. Get the following forms duly filled up and signed:—

(a) Declaration of compliance—Form No. 1 duly stamped

(b) Notice of situation of the registered office of the company—Form No. 18

(c) Particulars of directors, manager or secretary—Form No. 32.

9. File the following with the ROC with necessary registration and filing fee—

(i) The stamped and signed copy of M & A with two extra copies.

(ii) Form Nos. 1, 18 and 32 (in duplicate).

(iii) Any other agreement referred to in the M & A.

(iv) Any agreement proposed to be entered into with any individual for appointment as managing or whole time director.

(v) Certified true copy of the Registrar of Companies' letter intimating availability of name.

(vi) Power of attorney from the subscribers in favour of any person for making corrections on their behalf in the documents and papers filed for registration.

10. Pay the registration and filing fee by cash or demand draft or treasury challan.

11. Obtain the certificate of incorporation from the Registrar of Companies. The private limited company can commence business immediately on receipt of the certificate of incorporation.

Additional steps for formation of a public limited company

1. Arrange for payment of application and allotment money in cash by the subscribers on the shares taken or agreed to be taken by them.

2. File the statement in lieu of prospectus with the Registrar in accordance with Schedule III of the Companies Act.

3. File a declaration in Form 20 [duly stamped] duly signed by one of the directors or secretary with the concerned Registrar to the effect that the application and allotment monies have been paid/will be paid in respect of the shares taken up/agreed to be taken up by the directors.

4. Obtain the certificate of commencement of business from the Registrar.

S. 13. Requirements with respect to memorandum.—(1) The memo-randum of every company shall state—

(a) the name of the company with "Limited" as the last word of the name in the case of a public limited company, and with "Private Limited" as the last words of the name in the case of a private limited company;

(b) the State in which the registered office of the company is to be situate; [1][* * * *]

[2][(c) in the case of a company in existence immediately before the commencement of the Companies (Amendment) Act, 1965, the objects of the company;

(d) in the case of a company formed after such commencement,—

(i) the main objects of the company to be pursued by the company on its incorporation and objects incidental or ancillary to the attainment of the main objects;

(ii) other objects of the company not included in sub-clause (i); and

(e) in the case of companies (other than trading corporations), with objects not confined to one State, the States to whose territories the objects extend.]

(2) The memorandum of a company limited by shares or by guarantee shall also state that the liability of its members is limited.

(3) The memorandum of a company limited by guarantee shall also state that each member undertakes to contribute to the assets of the company in the event of its being wound-up while he is a member or within one year after he ceases to be a member, for payment of the debts and liabilities of the company, or of such debts and liabilities of the company as may have been contracted before he ceases to be a member, as the case may be, and of the costs, charges and expenses of winding-up, and for adjustment of the rights of the contributories among themselves, such amount as may be required, not exceeding a specified amount.

(4) In the case of a company having a share capital—

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1. The word "and" omitted by Act 31 of 1965, s. 5 (w.e.f. 15-10-1965).
2. Clauses (c), (d) and (e) were substituted for previous clause (c) by section 5 of the Companies (Amendment) Act (XXXI of 1965) (w.e.f. 15-10-1965).

(a) unless the company is an unlimited company, the memorandum shall also state the amount of share capital with which the company is to be registered and the division thereof into shares of a fixed amount;

(b) no subscriber of the memorandum shall take less than one share; and

(c) each subscriber of the memorandum shall write opposite to his name the number of shares he takes.

NOTES

Eng. Act, 1948 : Sec. 2
Eng. Act, 1985 : Secs. 2 and 25

Previous Act : Secs. 6, 7, 8

Name Clause [Sub-section (1)(a)]

The name of every private company shall contain as its last words, the words "Private Limited" and every public company shall contain as its last word "Limited". The object is that the name of a company should indicate whether it is a private or a public company barring the cases covered by section 25. See also Notes under sections 20, 21, 22, 23 and 147.

This provision is extended to existing companies by section 24.

It is an offence under section 631 to carry on any business or trade using the word "Limited" as a part of the name where the person using it is not so entitled. This kind of illegality does not invalidate contracts made in the ordinary course of business or trade. *Cotronic (UK) Ltd. v. Dezonie,* 1991 BCLC 721. Approval of ROC is required for the proposed name or change of name of a company. The Registrar can refuse to register a company's memorandum if the proposed name carries scandulous or obscene words *R. v. R.O.C, ex parte Bowen,* (1914) 3 KB 1161 at 1167 (DC). There are certain other words also which cannot be used without the permission of the Registrar, *e.g.*, the word "University" (*ibid*).

Registered Office [Sub-section (1)(b)]

Under clause (b) of sub-section (1), it is only necessary that the *State* in which the registered office is situated must be mentioned. Under section 146, notice of the exact place of the registered office must be given to Registrar within 30 days after the date of incorporation. The notice must be given in Form 18 (See *Appendix I*). Besides the address, the name and address of the police station under whose jurisdiction the registered office is situated must also be mentioned in the prescribed form. Once the State has been declared, the company can fix its office anywhere it likes within that State and change it from time to time within the city on giving notice to the Registrar or carry it to another city of the same State by a special resolution of shareholders. *Arya Insurance Company Limited, In re,* (1937) 7 Com Cases 130 : AIR 1937 Cal 81.

§ See also Notes under section 146, *post.*

Main and subsidiary objects : Amendment by Act of 1965

In the place of clause (c) of sub-section (1), clauses (c), (d) and (e) have been substituted by section 5 of the Companies (Amendment) Act, 1965. The Notes on clauses stated: "This clause seeks to implement the recommendation of the Daphtary—Sastri Committee based on the observations contained in paragraphs 2 to 5 of the Commission's Report. The purpose of the amendment is to provide for clear definitions of the main and the subsidiary objects of a company in its Memorandum of Association". (*Clause* 5).

As an act, which is beyond the powers of a company as specified in the memorandum, is *ultra vires*, the practice has become common of making the objects in a company's memorandum as wide as possible, in order to obviate the necessity of seeking consent of general meeting by special resolution when any new venture is contemplated.

The purpose of the amendment is to enable shareholders and others interested to have a clear idea of the main objects and other objects. This combined with the amendment of section 149 inserting a new provision therein requiring that both at the initial stage and at later stages, whenever a company embarks on any kind of business activity, sanction of the company by special resolution should be obtained, will afford an opportunity to shareholders to inform themselves of the actual business or business in which the company is engaged or proposes to engage.

The amendment gives effect to the following recommendation in para 6 of Part II of the *Report of Vivian Bose Commission of Inquiry* :

"(i) The Act should be suitably amended to provide that every company shall clearly state its purposes and objects under two separate categories, *viz.*,

(a) the principal and ancillary objects, which the company intends at the time of its incorporation to pursue; and

(b) all other objects which are separate from the principal and ancillary ones mentioned in item (a) above.

(ii) A provision should be made in the Act to the effect that a company shall not engage itself in any activities coming within the scope of Clause (b) unless such activities are sanctioned by a special resolution of the company in general meeting." (*Report* : Para 6.)

Fully endorsing the above recommendation, the *Daphtary-Sastri Committee* advised that: "Statutory provision should be made, therefore, whereby even at the initial stage, the shareholders have an opportunity to inform themselves of the principal industrial or business activity the company would embark upon. The promoters, the signatories to the memorandum and the first directors of a company should be required to obtain the approval of the company in general meeting by a special resolution, of the decision of the directors regarding the activities the company shall engage in, in the first instance. Thereafter, sanction of the company in general meeting by special resolution should also be obtained, if the directors later on propose to engage in new activities. Every such resolution shall be incorporated in all copies of the memorandum of the company. Provision should be made in the Capital Issues (Control) Act for informing the controller of the starting of a fresh business enterprise in accordance with the special resolutions. A copy of the special resolution enlarging the business of the company should be furnished to the Registrar of Companies of the State".

Existing companies not affected.—In giving effect to the recommendations, however, the *Joint Select Committee* excluded existing companies from the operation of the new provisions for the following reasons.—"It was represented to the Committee that if the existing companies were also to be required to re-draft their object clauses, then that would require the passing of special resolution under the Act, which would involve tremendous time and effort not commensurate with the results intended. The Committee, therefore, feel that this clause should be amended to provide that the provisions of existing clause (c) of section 13 of the Act should continue to apply to companies in existence immediately before the commencement of the Companies (Amendment) Act, 1965 and the provisions of the proposed new clause requiring the division of objects into (i) main objects and objects ancillary thereto and (ii) other objects should apply only to new companies (*Report* : Para 13).

Objects clause to be stated in three heads.—The effect of the amended clause (d) of sub-section (1) is that in the case of companies formed after the amendment came into force, the objects clause is divided into 'main objects' and 'objects incidental thereto' and 'other objects', the doing of any business pertaining to the 'other objects' being required to comply with the provisions of section 149(2-A). Note, however, that the main objects themselves may comprise several businesses obviating the need to resort to the provisions of section 149(2-A).

See Tables B, C, D and E of Schedule I which contain the forms of the memorandum of association that should be adopted by the different kinds of companies as per section 14. The objects are now required to be stated under three heads: (1) main objects, (2) incidental and auxiliary objects and (3) other objects. The view of Department on this point is reproduced hereunder:

Department's view.—The Department of Company Affairs is of the view that having regard to the provisions of sub-section (1)(*d*) of section 13 of the Companies Act, the objects clause of the Memorandum of Association of a company should be spilt up as follows:

(a) Main objects to be pursued on its incorporation;

(b) Objects incidential, or ancillary to the attainment of the objects specified in (a) above; and

(c) Other objects not indicated in (a) and (b) above.

Such an arrangement, it is felt, would be in line with section 13(1)(d) of the Companies Act and at the same time make clear that clause (d)(i) of the said sub-section included (i) objects other than main objects and also (ii) objects incidental or ancillary thereto. [*Company News & Notes January 1, 1968*].

Few and precisely defined objects to be included

Department's Instructions.—Department has in a letter addressed to the Registrars of Companies, given following instructions:

"As you are aware Section 13 of the Companies Act, 1956 was amended by Companies (Amendment) Act, 1965 so as to require the companies to specify clearly the main objects of the company to be pursued by the company on its incorporation and objects incidental or ancillary to the attainment of the main objects and other objects of the company not included as main objects or objects incidental or ancillary to the main objects. It has been, however, observed that while companies comply with these broad outlines in their memorandum of association, cases are not rare where a very large number of items and activities are being included in the objects clause. It was noticed that in one case as many as 106 sub-clauses were found included.

It was also noticed in the same case that though the main object of the company was to buy, acquire, hold and deal etc. in shares, stocks, debentures and other securities, it was found that the company had not carried on any such business activity and was in fact dealing with plastics and chemicals. The later item of activity was perhaps covered by items under 'other objects'.

The matter has been examined in the *department* and it is felt that it is necessary for the companies incorporated under the Companies Act, 1956 to have clearly defined the spheres of business activities and promoters of companies should be pursuaded at the time of incorporation of companies to have a few reasonably well defined and clear objects under the main objects clause and a limited number of 'other objects' which should be consistent with the intended or proposed activities of the company and within the financial capability of the company as determined by its capital structure.

I am directed to bring the above views of the department to all the Registrars of Companies with a request to ensure that the above broad outlines are kept in mind while registering companies under the Companies Act, 1956. They should also ensure that the companies carry on only the business that they are allowed to carry on under their Memorandum of Association and transgression in this behalf should be taken up with the companies for corrective action as soon as it comes to notice." [*Department's File No.* 8/15(13)/82-CL-V, dated 22-12-1982].

Effect of amendment on statement of objects [Clauses (c) and (d) of sub-sec. (1)]

The effect of these clauses as amended by the Act XXXI of 1965 is this: In the case of an 'existing company,' that is, existing prior to the Amendment Act, if any new business not germane to the business which it is already carrying on, is to be started, the provisions of section 149(2-A) clause (a) read with sub-section (2-B) should be complied with, and in the case of a company formed after the Amendment Act, if any business coming under the 'other objects' clause (d) is to be started, the provisions of the said section 149(2-A) clause (b) read with sub-section (2-B) of that section should be complied with.

Main objects and ancillary objects

The words "to be pursued by the company on incorporation" in s. 13(1)(d) are pertinent. This implies that the objects stated in the main objects are to be pursued by the company immediately after incorporation or within a reasonable time thereafter. While registering a company, the concerned Registrar of Companies is entitled to satisfy him-

self that the objects included in the main objects clause are really the objects intended to be pursued by the company either immediately or within a reasonable time after its incorporation. The Registrar must satisfy himself by reference to certain documents information or explanations furnished by the company.

The terms 'incidental' or 'ancillary' in the same clause mean activity arising out of or directly connected to the main activity. For example, the production of by-products is incidental to the manufacture of the main products and also the powers of the company to carry on its objects, like investment of surplus funds, to borrow etc. Whether an activity is incidental or ancillary to the main activity will have to be determined by reference to the facts and circumstances of each case.

Where the main objects of the company have failed to materialise, the court may order winding-up under 'just and equitable' clause of s. 433. *Bristol Joint Stock Bank, Re,* (1890) 44 Ch D 703, 712; *Suburlun Hotel Co., Re,* (1867) LR 2 Ch App 737, 750. *Baku Consolidated Oilfields Ltd., Re,* (1944) 1 All ER 24, the company took-over a business of which it was deprived by acquisition and later received compensation, *sub-nom, Baku Consolidated Oilfields Ltd.,* (1994) 1 BCLC 173.

A company may be restrained by an injunction from exceeding its objects. *Stephens v. Mysore Reefs (Kangundy) Mining Co. Ltd.,* (1902) 1 Ch 745, Injunction issued; *Pedlar v. Road Block Gold Mines of India Ltd.,* (1905) 2 Ch 427, injunction was refused.

Indication of 'Main objects'

Department's Instruction.—There are divergent practices in the offices of ROCs as to the number of clauses/objects that can be allowed under "Main Objects" to be pursued by the company on its incorporation *vide* section 13(1)(d)(i) of the Companies Act. ROCs are advised to follow the general principle that in case of object oriented names like Hindustan Sugar Limited, the main object should constitute only of that object (like sugar in case of Hindustan Sugar Ltd.), while in case of non-object oriented names (like Tata Sons Limited) there should be no restriction as to the number of main objects. Similar should be the approach in case of companies having names with general expressions like "Industries/Enterprises", etc. without prefixing the nature of industry or enterprise. In either case, it may be ensured that objects specified in the Memorandum of Association are those specified against Column No. 5 of Form 1A (Part V). [*Circular No.* 1/95, *F.No.* 14/6/96-CL-V, dated 16-2-1995].

Registration as Commercial Company under English Act.—The English Companies Act, 1985, s. 3A permits a company's memorandum to state that its object is to carry on business as a general commercial company. Before this statutory permission the position taken by the courts was that a statement in the memorandum that the company was formed to carry on any business whatever which the company might think would be profitable to the shareholders was not a proper statement of objects, *Crown Bank, Re,* (1890) 44 Ch D 634, though the courts had relaxed their approach in this respect in *Bell Houses Ltd. v. City Wall Properties Ltd.,* (1966) 2 QB 656 (CA).

Objects of non-trading corporations [Sub-section (1)(e)]

In the case of a non-trading corporation whose objects extend to more than one State, the States to which the objects will extend have to be mentioned s. 13(1)(e).

A company incorporated for Kuries business (in this case in Kerala) has been held to be a trading corporation. *John v. Oriental Kuries Ltd.,* (1994) 2 Ker LT 353 (Ker). See also notes under section 2(49).

Trustee company.—A company can act as a trustee. It is not necessary that the objects should always be commercial objects. *S. Ramachandra Adityan v. Educational Trustee Co. P. Ltd.,* (2003) 113 Com Cases 334 (Mad).

Objects, powers and interpretation

The memorandum of association of a company is its charter defining the object of its existence and operations. As pointed out in *Cotman v. Brougham,* 1918 AC 514, its purpose is 'to enable the shareholders, creditors and those dealing with the company to know what is its permitted range of enterprise'. The objects clause or clauses in the memoran-

dum are to be so construed as to confer on the company all powers reasonably required to the attainment of the objects.' "A memorandum of association like any other document must be read fairly and its import derived from a reasonable interpretation of the language which it employs". *Egyptian Salt and Soda Co. Ltd. v. Port Said Salt Association Ltd.*, (1931) 1 Com Cases 285 : AIR 1931 PC 182; *Deuchar v. Gas, Light and Coke Co.*, 1925 AC 691. The natural and ordinary meaning of the language used in the several clauses should be taken into consideration for determining whether a particular transaction does or does not fall within the objects stated in the memorandum. *Bell Houses Ltd. v. City Wall Properties Ltd.*, (1966) 36 Com Cases 779 : (1966) 2 All ER 674 (CA).

In the case of *Bell Houses Ltd.* (*supra*) the Court of Appeal apparently approved of a clause providing that the company may 'carry on any other trade or business whatsoever which can in the opinion of the Board of Directors be advantageously carried on as ancillary to any of the above businesses. From this it would appear that the modern practice is to water down the *ultra vires* doctrine as regards dealings of companies with third parties, provided the dealings are honest.

Where the objects clause provided that the company may enter into any partnership for any purpose which may benefit the company, it was held that this enabled the company to enter into partnership for manufacturing garments. *Sivashanmugam (S) v. Butterfly Marketing (P.) Ltd.*, (2001) 105 Com Cases 763 : (2001) 43 CLA 28 (Mad—DB).

Where the object clause concluded with the words that each clause was independent of other clauses and one of the clauses authorised the company to carry on the work of merchants generally, it was held that this empowered the company to operate a chain of garages and the company was liable to the supplier of petrol to the garages. *Re, New Finance and Mortgage Co. Ltd. (In liquidation)*, (1975) 1 All ER 684 (Ch D). See also *Newstead (Inspector of Taxes) v. Frost*, (1980) 1 All ER 363 (HL).

If the objects clause has a specific main object followed by general words, the general words should not be construed as enabling the company to throw its main object altogether and embark on some new venture. *Eastern Telegraph Co. Ltd., Re* (1947) 2 All ER 104: (1948) 18 Com Cases 46 (Ch D). The objects clauses should be construed as independent of each other so as to give full effect to each of them. *In re, Bilasrai Joharmal*, AIR 1962 Bom 133. In "HALSBURY'S LAWS OF ENGLAND, para 943, p. 693 [4th edn., vol. 7(1)] the proper approach to construction of objects clauses, is stated thus: "The ordinary rules of construing documents apply to the construction of the objects clauses of a memorandum of association. The first question is, what is the fair construction of the memorandum as a whole? General words following a particular specification may be considered *ejusdem generis*, but there is no special rule of interpretation by reference to what are the main or principal objects of a company where the question is whether something done or proposed to be done is *ultra vires*....." *In re, Akola Electric Supply Co. (Pvt.) Ltd.*, (1962) 32 Com Cases 215 : AIR 1962 Bom 133 the proper mode of construing the objects clauses of memorandum of association is discussed and the case-law on the subject reviewed.

The memorandum has to be construed like any other document. Articles may be looked into for explaining ambiguities but they cannot be used for extending the scope of the memorandum. *Dr. Lakshmanaswami Mudaliar v. LIC*, (1963) 33 Com Cases 420 : AIR 1963 SC 1185.

Further the memorandum of association is not to be considered as limiting the powers conferred by the provisions of the Companies Act itself or by any other law.

A company may set out in its memorandum of association as many objects and powers as it thinks proper. The registering authority cannot object to the prevailing practice of drafting objects clause which permits the carrying out of diverse activities. The purpose of the Act is not to limit the powers of the company and compel them undergo the tedious and costly process of having to amend the objects whenever a new business venture is planned.

Main objects rule of construction.—In setting out the objects of a company, its memorandum usually states the several powers which the company will be entitled to exercise in carrying out its objects. Though the practice of inserting powers in the objects clause was criticised in *Cotman v. Brougham,* 1918 AC 514, the practice has become so common and widespread that the Registrar usually does not refuse to register a memorandum containing, besides its objects, the several powers which a company may exercise in effectuating its objects. The result is "to bury beneath a mass of words the real objects or objects of the company with the intent that every conceivable form of activity shall be found included somewhere within its terms. In view of the ruling in *Trevor v. Whitworth,* (1887) 12 AC 409 that 'a company cannot employ its funds for the purposes of any transactions which do not come within the object specified in the memorandum' the adoption of a wide range of objects clauses in the memorandum protects in a way the activities of the company from being questioned as *ultra vires* its powers. See also *Anglo-Overseas Agencies Ltd. v. Green,* (1960) 3 All ER 244: (1961) 31 Com Cases 38 (QBD) wherein it was held that the 'main objects' rule stood excluded by the concluding clause in the memorandum which declared that the objects in any paragraph thereof were in no way limited or restricted by reference to any other paragraph or the name of the company.

The intention to treat a particular object as the main object can also be known from the conduct of the company towards that object *North of England Zoological Society v. Chester R.D.,* (1959) 3 All ER 116 (CA). When something is stated amongst the objects, it would have to be treated as an object and alterable in the same manner though it was a bare function like distribution of the company's assets in winding-up and could have been stated in the articles also. *Hampstead Garden Suburb Trust Ltd., Re,* (1963) 33 Com Cases 166, 183 : 1962 Ch 806 (Ch D). See also notes under sections 26 and 36 and also under heading 'Interpretation of memorandum of association' under S. 1.

Where the power to make investments, as permitted by the objects clause was found to be exercisable only in connection with the company's principal business or when it had surplus funds, it was held that without such linkage the company's money could not be used for investing in shares of other companies or for acquiring control over them. *Rajan Nagindas Doshi v. British Burmah Petroleum,* (1972) 42 Com Cases 197 (Bom).

Doctrine of *ultra vires*.—It is *ultra vires* for a company to act beyond the scope of its memorandum. Any attempted departure will be invalid and cannot be validated even if assented to by all the members of the company. By *ultra vires* is meant an act or transaction of a company, which, though it may not be illegal, is beyond the company's powers by reason of not being within the objects of the memorandum of association. The memorandum is, so to speak, the area beyond which a company cannot travel. *Ashbury Ry. Carriage Company v. Riche,* (1875) LR 7 HL 653. An act beyond the objects mentioned in the memorandum is *ultra vires* and void and cannot be ratified. *Dr. Lakshmanaswami Mudaliar v. LIC,* (1963) 33 Com Cases 420 : AIR 1963 SC 1185. Where no connection or nexus exists between the exercise of a power and the attainment of an object, exercise of power will be *ultra vires. Radha Cinema & Co. v. Chitralipi Films,* 1974 Tax LR 2180 at 2185 (Cal). See also *Attorney General v. Mersey Rly. Co.,* (1907) 1 Ch D at 81 **overruled** by House of Lords in (1907) AC 415 (HL). *Cf.* GORE BROWNE ON COMPANIES, 33 (42nd Edn.).

The question, whether a stated 'object' is truly an independent object or purpose, is always a question of construction. Normally, where a sub-clause in a memorandum states that one of the objects is 'to lend or advance' money, this clause is construed only as a power ancillary to the main objects. A transaction which is within the powers, express or implied, of the company, but is entered into for a purpose not authorised by the objects clause is itself *ultra vires. Re, Introductions Ltd.,* (1969) 1 All ER 887 **followed.** The answer to the question whether a disposition of the property of a company was made for the benefit and to promote the prosperity of a company, although directly relevant is not conclusive nor always even relevant to the question whether the disposition was *ultra vires* the company or not. *Rolled Steel Products Ltd. v. British Steel Corporation,* (1982)

3 All ER 1057 (Ch D) **following** *Re, Horsley and Weight Ltd.*, (1982) 3 All ER 1045 : (1984) 1 Comp LJ 105 (CA).

It is a question dependant on the true construction of the memorandum of association and all the circumstances of the case whether the proceeding in question will facilitate or is otherwise incidental to the business which the company was formed to carry on. Thus a newspaper company may pay the cost of defending the editor in a libel action. *Breay v. Royal British Nurses Association,* (1897) 2 Ch 272 (CA). A chemical company may distribute money to scientific institutions for the furtherance of scientific education and research. *Evans v. Brunner, Mond & Co. Ltd.*, (1921) 1 Ch 359. No act of the company can be *ultra vires* if on the true construction of its memorandum it is *intra vires*. *Bell Houses Ltd. v. City Wall Properties Ltd.*, (1966) 2 All ER 674 : (1966) 36 Com Cases 779 (CA). An act of a company is not *ultra vires* merely because it is in breach of a statutory provision which renders the act voidable. *Finance and Issue Ltd. v. Canadian Produce Corpn. Ltd.*, (1905) 1 Ch 37.

But where profits are made or property is acquired by *ultra vires* or incurring *ultra vires* expenditure, the Company may retain the same. *Ayers v. South Australian Banking Co.*, (1871) LR 3 PC 548; *National Telephone Co., v. Constables of St. Peter Port,* 1900 AC 317.

It must, however, be noted that the *ultra vires* doctrine is nowadays very largely frustrated by the ingenuity of company draftsmen who, by enumerating all objects possible under the sun, have in actual practice fouled the doctrine and made it ineffective, except in very rare cases.

Thus in the case of *Bell Houses Ltd. v. City Wall Properties Ltd.*, quoted *supra,* where the objects clause included a power 'to carry on any other trade or business whatsoever which can, in the opinion of the Board of Directors, be advantageously carried on by the company,' the said clause was held to be quite in order by Court of Appeal.

The objects clause of a memorandum usually contains at the end some such words as "and to do all such other things as are incidental or conducive or as the company may think conducive to the attainment of the above objects." These words cannot be construed as widening the scope of the objects clause but will only be taken to include such incidental powers as are necessarily implied in carrying out the main object. See *Attorney-General v. Great Eastern Railway,* (1880) 5 App Cas 473 at 478.

Doctrine of *ultra vires* under English Law

The doctrine of *ultra vires* has become considerably reduced in its scope in England. It is provided by English Act, 1985, s. 35, as follows:

S. 35 Company's capacity: power of directors to bind it.—(1) In favour of a person dealing with a company in good faith, any transaction decided on by the directors is deemed to be one which it is within the capacity of the company to enter into, and the power of the directors to bind the company is deemed to be free of any limitation under the memorandum or articles.

(2) A party to a transaction so decided on is not bound to enquire as to the capacity of the company to enter into it or as to any such limitation on the powers of the directors, and is presumed to have acted in good faith unless the contrary is proved.

Thus a company was held bound by a debenture issued on its behalf under a transaction which appeared to be 'decided on by directors', though in fact no formalities like the holding of a Board meeting authorising the transaction in accordance with company's articles had been observed. The court said that a minute of a Board meeting which was produced before the court and which authorised the transaction was a *prima facie* proof and the directors were not permitted to say that no such meeting was ever held. *TCB Ltd. v. Gray,* (1986) 1 All ER 587 : 1986 BCLC 113 (Ch D).

Memorandum, Articles and the rule of Constructive Notice

§ For Notes on this subject, see s. 36, *post.*

Corporate charitable spending and *ultra vires* rule

Under S. 293(1)(e), the Board of Directors can with the consent of the company in general meeting contribute for any charitable or other purpose any amount not exceeding Rs. 50,000 (fifty thousand) in one financial year or five per cent of the average net profits during the preceding three financial years whichever is greater. This is the statutory authority. No question as to vires of such payments are likely to arise but apart from this, directors have no right to practice charity out of the company's money unless their charitable benevolence is also related to the promotion of the company's objects. The position was thus explained by LORD JUSTICE BOWEN in *Hutton v. West Cork Rly. Co.*, (1883) 23 Ch D 654 : "Charity has no business to sit at Board of Directors qua-charity. There is however a kind of charitable dealing which is for the interest of those who practice it, and to that extent and in that garb, charity may sit at the board, but for no other purpose."

A company known as the 'League against Cruel Sports Ltd.' contributed £ 80,000 to a political party which committed itself if elected to introduce legislation banning certain sports. The payment was made in two parts: £ 50,000 without restriction on its use and £ 30,000 to be used specifically for advertising the party's commitment to animal welfare. The payment of £ 30,000 was held to be proper but the payment of £ 50,000 was held to be *ultra vires* as it could be used for purposes unconnected with the donor's objects and was therefore recoverable by the company. *Simmonds v. Heffer,* 1983 BCLC 298 (Ch D).

The effect of these decisions is that apart from the statutory authorisation under sections 293(1)(e) and 293A, charity can be practised out of the company's assets only for the purpose of promoting the company's objects. In *Dr. Lakshmanaswami Mudaliar v. LIC,* (1963) 33 Com Cases 420 : AIR 1963 SC 1185, a sum of Rs. 2 lakhs was donated by an insurance company from the shareholder's dividend account to a trust formed with the object of promoting technical or business knowledge, including knowledge in insurance. There was no obligation on the trustees to utilise the funds for promoting education in insurance and even if they did, it was not certain if these persons would take up employment with the company. The donation was held to be *ultra vires*, and the trustees were personally liable to repay the amount received by them and to which they were not lawfully entitled.

Power to make gifts

As held in the *Lakshmana Mudaliar's* case *supra,* payments made for charitable purposes would be *ultra vires* unless there is a specific enabling clause in the memorandum. Similarly, a company can make gifts of property or other cash gifts only if there is specific clause in the memorandum of association. At the same time, it is submitted that the power to make gifts must be for the purpose of promoting a company's object. It would not be permissible for the company to make gifts to third parties where there is no nexus to the activities of the company.

Manner of exercising powers and *ultra vires* rule

In *Re, Lee Behrens & Co. Ltd.,* (1932) 2 Ch 46 : (1932) 2 Com Cases 588. Eve J. laid down the following test for legitimating the exercise of corporate powers and to escape the rigour of the *ultra vires* rule:

"(1) Is the transaction reasonably incidental to the carrying on the company's business?

(2) Is it a *bona fide* transaction?

(3) Is it done for the benefit and to promote the prosperity of the company?"

These tests were **approved** and **followed** in *Parke v. Daily News Ltd.,* (1962) 2 All ER 929 : (1962) 32 Com Cases 1060 (Ch D) and *Re, Wand M. Roith Ltd.,* (1967) 1 All ER 427 (Ch D). But this view has been held to be **no longer good law** in *Re, Horsley and Weight Ltd.,* (1982) 3 All ER 1045 : (1984) 1 Comp LJ 105; *Re, Halt Garage (1964) Ltd.,* (1982) 3 All ER 1016 : (1984) 1 Comp LJ 326 and *Rolled Steel Products (Holdings) Ltd. v. British Steel Corpn.,* 1984 BCLC 466. And in this last mentioned case BROWNE WILKINSON J summarises the position as follows (at pp. 517-518):

(1) To be *ultra vires*, a transaction has to be outside the capacity of the company, not merely in excess or abuse of the powers of the company.

(2) The question whether a transaction is outside the capacity of the company depends solely upon whether, on the true construction of its memorandum of as-

sociation, the transaction is capable of falling within the objects of the company as opposed to being a proper exercise of the powers of the company.

(3) Notwithstanding the fact that the provision authorising the company to enter into the particular transaction is found in the objects clause and there is a provision requiring each paragraph to be construed as a separate object, such provision may be merely a power (and not an object) if either it is incapable of existing as a separate object or it can only be construed as a power ancillary to the other objects in the strict sense.

(4) If a transaction falls within the objects (and therefore the capacity) of the company, it is not *ultra vires* the company and accordingly it is not absolutely void.

(5) If a company enters into a transaction which is *intra vires* (as being within its capacity) but in excess or abuse of its powers, such transaction will be set aside at the instance of the shareholders.

(6) A third party, who has notice (actual or constructive) that a transaction, although *intra vires* the company, was entered into in excess or abuse of the powers of the company, cannot enforce such transaction against the company and will be accountable as constructive trustee for any money or property of the company received by the third party.

(7) The fact that a power is expressly or impliedly limited so as to be exercisable only 'for the purposes of the company's business' (or other words to that effect), does not put a third party on inquiry as to whether the power is being so exercised, *i.e.* such provision does not give him constructive notice of excess or abuse of such power.

In the same case of *Rolled Steel,* SLADE LJ extensively surveyed the relevant authorities and formulated his conclusions in terms of the following proposition [at pp. 507-508]:

(1) The basic rule is that a company incorporated under the Companies Acts only has the capacity to do those acts which fall within its objects as set out in its memorandum of association or are reasonably incidental to the attainment or pursuit of those objects. Ultimately, therefore, the question whether a particular transaction is within or outside its capacity must depend on the true construction of the memorandum.

(2) Nevertheless, if a particular act (such as each of the transactions of 22 January, 1969 in the present case) is of a category which, on the true construction of the company's memorandum, is *capable* of being performed as reasonably incidental to the attainment or pursuit of its objects, it will not be rendered *ultra vires* the company merely because in a particular instance its directors, in performing the act in its name, are in truth doing so for purposes other than those set out in its memorandum. Subject to any express restrictions on the relevant power which may be contained in the memorandum, the state of mind or knowledge of the persons managing the company's affairs or of the persons dealing with it is irrelevant in considering questions of corporate capacity.

(3) While due regard must be paid to any express conditions attached to or limitations on powers contained in a company's memorandum (*e.g.*, a power to borrow only up to a specified amount), the court will not ordinarily construe a statement in a memorandum that a particular power is exercisable 'for the purposes of the company' as a condition limiting the company's corporate capacity to exercise the power; it will regard it as simply imposing a limit on the authority of the directors: see the *David Payne* case.

(4) At least in default of the unanimous consent of all the shareholders (as to which see below), the directors of a company will not have *actual* authority from the

company to exercise any express or implied power other than for the purposes of the company as set out in its memorandum of association.

(5) A company holds out its directors as having *ostensible* authority to bind the company to any transaction which falls within the powers expressly or impliedly conferred on it by its memorandum of association. Unless he is put on notice to the contrary, a person dealing in good faith with a company which is carrying on an *intra vires* business is entitled to assume that its directors are properly exercising such powers for the purposes of the company as set out in its memorandum. Correspondingly, such a person in such circumstances can hold the company to any transaction of this nature.

(6) If, however, a person dealing with a company is on notice that the directors are exercising the relevant power for purposes other than the purposes of the company, he cannot rely on the ostensible authority of the directors and, on ordinary principles of agency, cannot hold the company to the transaction.

An *ultra vires* act, being void, cannot be set right by subsequent ratification. Directors who throw away the company's money on an unauthorised object are personally liable to make good the company's loss. In *Aviling Barford Ltd. v. Perion Ltd.*, 1989 BCLC 626 (Ch D), it was held that it would be a breach of a director's fiduciary duty to sell a property for £ 3,50,000, when he knows that it is worth £ 6,50,000. Since the recipient of the property was aware of the facts constituting the breach, he was also accountable as a constructive trustee. The sale to the defendant was not a genuine exercise of the power of plaintiff company to sell its property. It was a sale at an undervalue for the purpose of enabling L, the sole beneficial owner of the plaintiff company, to obtain an unauthorised return of capital and hence was *ultra vires* and unratifiable. The court referred to *Ridge Securities Ltd. v. IRC*, (1964) 1 All ER 275, where PENNYCUICK J was concerned with a tax avoidance scheme by the solvent company which involved the grant of a debenture to its parent under which very large and uncommercial sums were payable purportedly as interest. He said that the 'interest' payments were *ultra vires* because they were dressed-up gifts of capital to the parent company. He said: [at p. 288]. "A company can only lawfully deal with its assets in furtherance of its objects. The corporators may take assets out of the company by way of dividend, or, with the leave of the court, by way of reduction of capital, or in a winding up. They may of course acquire them for full consideration. They cannot take assets out of the company by way of voluntary disposition, however described, and if they attempt to do so, the disposition is *ultra vires* the company."

The decision in *Ridge Securities* (*supra*) was **followed** by OLIVER J in *Halt Garage (1964) Ltd., Re*, (1982) 3 All ER 1016 : (1984) 1 Comp LJ 326. In that case the liquidator of the company challenged payments of £ 30 a week purporting to be director's remuneration to a director-shareholder who had rendered no services to the company. It was held that in so far as the payments exceeded £ 10 a week, which was considered to be a maximum remuneration reasonably payable to some-one who merely held the office of a director, they were dressed-up returns of capital to a shareholder and therefore *ultra vires*. It is also *ultra vires* a company under the Companies Act to make a present of bonus shares. *Eddystone Marine Insurance Company, Re*, (1893) 3 Ch 9.

The payment of salary to a director's son and his use of the company's motor car while he was still a school boy was held to be misapplication of the company's money. It was designed to give the director an unauthorised increase of salary without approval of the Board of directors and also to lessen his tax liability. The payment was invalid on both counts. *Gencor ACP Ltd. v. Dalby*, (2000) 2 BCLC 734 (Ch. D).

Acts contrary to law.—In *Australian Agricultural Co. v. Oatmont Pty Ltd.*, (1992) 106 FLR 314 (Aust) the Northern Territory Court of Appeal distinguished acts contrary to the law under which a company is constituted (such as an illegal payment of dividend out of capital)—such acts could be called *ultra vires*—from acts contrary to other laws

(such as, in this case holding land contrary to statutory ceiling which applies to any person natural or legal), which acts should not be called *ultra vires* because they are not beyond the capacity or authority of the company.

Loans, borrowings, guarantees and *ultra vires* rule

A bank or other person lending to company for purposes *ultra vires* the memorandum cannot recover. *Introductions Ltd. v. National Provincial Bank Ltd.*, (1969) 1 All ER 887 : (1969) 2 Comp LJ 28 **affirming** (1968) 2 All ER 1221. But nothing prevents the company from repaying the money, though it cannot recover the money re-paid. If the lender had lent the money for discharging any debts or liabilities of the company lawfully incurred, the lender may recover the amount lent for discharging such debts and liabilities. *Cunliffe Brooks & Co. v. Blackburn Bldg. Society*, (1884) 9 App Cases 857 (HL). The lender is also entitled to a tracing order, and if the money lent can be traced into any investments or property held by the company or has increased the company's assets, the lender will be recouped *Cf. Sinclair v. Brougham*, 1914 AC 398 (HL). *Re, Diplock, Diplock v. Wintle*, (1948) 2 All ER 318. A person handed over money to a company and the latter paid that sum into its overdrawn account at its bank. The company then went into receivership. Tracing was not possible. It was held that there might in certain circumstances be a claim for unjust enrichment if the bank was aware of the fiduciary relationship between the plaintiff and the company and the fact that the money had been paid into the account for the plaintiff—*Style Financial Services Ltd. v. Bank of Scotland*, The Times Scots Law Report, May 23, 1995 [CS (III)]. Where money is borrowed *intra vires* but is afterwards misapplied by a director, the lender's right to recover from the company is not affected. *David Payne & Co. Ltd., In re*, (1904) 2 Ch 608 : (1904-7) All ER Rep Ext-1501 (CA).

If there is a power to borrow and raise money, the method of raising finances is not to be gone into. Accordingly, borrowing by participating in competitive bidding for a chit fund was held to be not a wrongful method. *Nellai Metal Rolling Mills P. Ltd. v. Southern India Central Benefit Fund P. Ltd.*, (1986) 1 Mad LJ 370 at 376 (Mad).

Where the objects enumerated in a company's memorandum contained a clause for giving guarantee in respect of another company's liabilities and incurring expenses for purposes other than those relating to the company's own business, and the company incurred those obligations, they could not be challenged as *ultra vires* transactions, as they were within the objects stated in the memorandum. *Charterbridge Corporation Ltd. v. Lloyds Bank Ltd.*, (1969) 39 Com Cases 824 (Ch D). Distinction must always be drawn between a company's borrowing powers and the authority of the directors to borrow. Where the directors exceed their authority, the excess part may not be *ultra vires* and may be only irregular depending upon the facts and circumstances. The company will be bound if the excess is within the director's ostensible authority and the lender acted in good faith or if the transaction was ratified by the company. Thus, where the directors mortgaged the company's property exceeding the limits of their authority, it was held that the lending bank was entitled to retain possession and to claim restitution before it could be compelled to surrender possession. *Deonarayan Prasad Bhadani v. Bank of Baroda Ltd.*, (1957) 27 Com Cases 223, 239 (Bom). See also *Shiv Ram Batta v. Punjab Textile Mills Ltd.*, (1948) 18 Com Cases 294, 302 (Lah) (ratification of borrowing by directors beyond their powers at p. 301), and *Madras Native Permanent Fund Ltd., Re*, (1931) 1 Com Cases 256, 260 (Mad), where it was held that an *ultra vires* loan transaction does not create the relationship of debtor and creditor.

Sums paid to a local authority by a bank under a swaps agreement that was *ultra vires* the authority, could be recovered in full as the agreement was a total nullity. *Guinness Mahon and Co. Ltd. v. Kensington and Chelsea LBC, The Times*, March 2, 1998 (CA).

Implied powers

The powers exercisable by a company are to be confined to the objects specified in the memorandum. While the objects are to be specified, the powers exercisable in respect of them may be express or implied and need not be specified.

Every company may necessarily possess certain powers by virtue of its being an incorporated body, such as, for instance, a power to appoint and act by agents, and where it is a trading company, a power to borrow and give security for the purposes of its business, and also a power to sell. Such powers as these are incidental or properly to be inferred from the powers expressed in the memorandum. *Oakbank Oil Co. v. Crum*, (1882) 8 App Cas 65. The principle underlying the exercise of such powers is that a company in carrying on the trade for which it is constituted must be in a position to do all such things as may fairly be regarded as incidental to or consequential upon that trade. See *Egyptian Salt and Soda Co. v. Port Said Salt Association*, (1931) 1 Com Cases 285 : AIR 1931 PC 182 and all cases referred to therein. To the same effect, *Columbia Bitulithic Ltd. v. Vancouver Lumber Co.*, (1915) 20 DLR 954; *Shamnugger Jute Factory Co. v. Ram Narain Chaterjee*, (1886) ILR 14 Cal 189; *Gujarat Ginning & Mfg. Co. v. Motilal Hirabhai Spg. Co.*, AIR 1930 Bom 84 where it was observed that an express power to purchase land implies a power to lease or sell land.

In actual practice the implied power of a trading company to borrow is too indefinite to be relied upon for it is not always easy to decide whether a company is a trading company or not. Further the question will frequently arise whether a borrowing is or is not for the purpose of the company's business. It is, therefore, invariably the practice to give an express power to borrow in the memorandum of association.

In the case of a non-trading corporation unless there is something in the memorandum or articles to show expressly or by way of necessary inference that the company is empowered to borrow, a power to borrow money cannot be implied. Such a company will have only such powers as are necessary to enable it to discharge duties and fulfil the purposes for which it is constituted. *Baroness Wenlock v. River Dee*, (1885) 10 App Cases 354 (HL).

As regards implied powers, the rule nowadays is to assume that "quite apart from any general words in a company's memorandum, it has power to do all that is reasonably necessary for attaining its objects. The Court has become increasingly ready to imply powers of this nature" PALMER'S COMPANY PRECEDENTS, 17th Edn., Part 1, page 278. See *American Home Assurance Co. v. Tjmond Properties Ltd.*, 1986 BCLC 181 : (1987) 2 Comp LJ 114.

Virtually speaking, all companies have implied powers to compromise *bona fide* disputes. *Bath's* case, (1878), 8 Ch D 334. There is an implied power to pay gratuities to employees while the company is a going concern. *Hampson v. Price's Patent Candle Co.*, (1876) 45 LJ Ch 437; *Cyclists' Touring Club v. Hopkinson*, (1910) 1 Ch 179. A colliery company, an omnibus company, a shipping company and a trading company have been held to have an implied power to borrow. *Jackson v. Rainford Coal Co.*, (1896) 2 Ch 340; *Bryon v. Metropolitan Saloon Omnibus Co.*, (1858) 27 LJ Ch 685; *Australian Auxiliary Steam Clipper Co. v. Mounsey*, (1858) 27 LJ Ch 729, *General Auction Estate Co. v. Smith*, (1891) 3 Ch 432. On the other hand, a building society, a school board, a literary and scientific institution were held not to be entitled to borrow in the absence of specific powers to do so. *Blackburn Building Society v. Cunliffe, Brooks & Co.*, (1882) 22 Ch D 61.

In case of trading company, the power to borrow naturally implies the power to mortgage its property, *In re, Patent File Company*, (1870) LR 6 Ch 83.

In the absence of any regulation in the articles or provision in any statute, the following powers also will normally be implied in the case of trading company:

(1) power to acquire and hold shares in any other company,

(2) power to invest surplus funds not required for immediate use *Burland v. Earle*, (1902) AC 83,

(3) power to acquire, hold and dispose of property of any kind,

(4) power to trade in partnership or joint venture with any other person or body corporate,

(5) power to appoint employees and agents and such other acts and things which are usually required in the carrying of any business for profit.

The doctrine of implied powers, it should be noted, has been developed by judges all over the world in a manner to meet in the principles of justice and equity harmoniously with the diversified and specialised development of economic activity under modern conditions.

Powers which are not implied.—The following powers have been held not to be implied and it is, therefore, prudent in case where deemed necessary, to include them expressly in the objects clauses:—

(1) acquire any business similar to company's own. *Ernest v. Nicholls,* (1857) 6 HLC 401;

(2) entering into agreement with other persons or companies for carrying on business in partnership or for sharing profits, joint venture or other arrangements. Very clear powers are necessary to justify such transaction. *Re, European Society Arbitration Act,* (1878) 8 Ch 679;

(3) taking shares in other companies having similar objects. *Re, Barned's Banking Co., ex parte. The Contract Corporation,* (1867) 3 Ch App. 105. *Re, William Thomas & Co. Ltd.,* (1915) 1 Ch 325;

(4) taking shares of other companies where such investment authorises the doing indirectly that which will not be *intra vires* if done directly;

(5) promoting other companies or helping them financially. *Joint Stock Discount Co. v Brown,* (1869) LR 8 Eq 381;

(6) a power to sell and dispose of the whole of a company's undertaking;

(7) a power to use funds for political purposes;

(8) a power to give gifts and make donations or contribution for charities not relating to the objects stated in the memorandum;

(9) entering into contracts of suretyship or guarantee.

Statutory powers.—But where in respect of any of the above and similar matters, power is given by any statute, such power may be exercised, even though the memorandum does not provide for them.

It is, however, important to note, that in the case of any objects clause enabling the exercise of any powers express or implied, the powers can only be exercised for the purpose of the company. "Acts incidental" are those which have a reasonably proximate connection with the objects specified. *Dr. Lakshmanaswami Mudaliar v. LIC,* (1963) 33 Com Cases 420 : AIR 1963 SC 1185.

Powers which can be 'implied' or considered 'incidental'.—A company carrying on business for profit cannot be said to have 'implied' power to enter into contracts of suretyship or guarantee, to invest in shares of other companies or undertakings carried on by individuals, firms etc. or to enter into partnerships or joint-ventures with other bodies corporate or individuals or make gifts or charitable contributions. Nor are such powers 'incidental' to the carrying on of its business. There must be express provision in the objects clause of the memorandum of association authorising the exercise of such powers.

Inherent powers

The Companies (Amendment) Bill, 1993, which was subsequently withdrawn, carried in its Second Schedule [Schedule II] a list of inherent powers. They are of continuing validity inspite of the fact that the Bill was withdrawn. The list had the Departmental

approval. The points enumerated are a part of the third schedule [Schedule III] of the Malaysian Companies Act, 1965. They have also been incorporated in the Companies Act of Singapore (Revised 1988). The text of the Schedule II of Companies Bill, 1993 is reproduced below as a matter of guidance for practices which companies may adopt :

SCHEDULE II

[*See* clauses 2(26), 26 and 27]

[Companies Bill, 1993]

Inherent Powers to be adopted with or without modifications in, or to be excluded from, the memorandum of association by a company

Every company shall have the following inherent powers and unless excluded or modified shall be deemed to be part of the memorandum of association of a company:—

1. to acquire and undertake the whole or any part of the business, property and liabilities of any person carrying on any business which the company is authorised to carry on or possession of property suitable for the purposes of the objects of the company;

2. to apply for, purchase or otherwise, acquire any patent, patent right, copyright, trade marks, formulate, licence, lease, concessions, conferring any exclusive or limited right to use, or any secret or other information as to any invention which may seem capable of being used for any of the purposes of the company or the acquisition of which may directly or indirectly to benefit the company; and to use, exercise, develop or gant licences in respect of or otherwise turn to account the property, rights, or information so acquired;

3. to amalgamate or enter into any arrangement for sharing of profits (except entering into partnership), union of interest, co-operation, reciprocal concession, lease, licence or otherwise with any person carrying on or transaction which the company is authorised to carry on or engage in;

4. to enter into any arrangement with any Government or authority whether municipal, local or otherwise or any person, that may seem conducive to the company's objects or any of them; and to obtain from any such Government or authority any rights, privileges and concessions which the company may think it desirable to obtain; and to carry out, exercise and comply with any such arrangement, rights, privileges and concessions;

5. to establish or support or aid in the establishment and support of associations, institutions, funds, trusts, and conveniences for the benefit of past or present employees or directors of the company or the dependents of such persons; and to grant pensions and allowances, to make payments towards insurance; to subscribe or guarantee money for charitable or benevolent objects or useful objects for general public;

6. to promote any other company or companies for the purpose of acquiring or taking over all or any of the property, rights, and liabilities of the company or for any other purpose which may directly or indirectly benefit the company;

7. to purchase or import, take on lease or in exchange, hire or otherwise acquire any movable or immovable property and any rights or privileges which the company may think necessary or convenient for the purposes of its business and in particular any land, buildings, casements, machinery, plant and stock-in-trade;

8. to invest and deal with money of the company, not immediately required in such manner as may, from time to time, be thought fit subject to provisions of the Act;

9. to lend and advance money or give credit to any person or company; to give guarantee or indemnify for the payment of money or the performance of contracts or obligations by any person; to secure or undertake in any way the repayment of moneys lent or advanced to, or the liabilities incurred by any person subject to the provisions of the Act;

10. to borrow or secure money in such manner as the company may think fit or to make repayment of any debt, liability, perform any contract entered into or the issue of debentures, perpetual or otherwise, charged upon all or any of the company's property (both present and future), including its uncalled capital; and to purchase, redeem, or pay off any such securities;

11. to remunerate any person for services rendered, or to be rendered, in placing or assisting to place or guaranteeing the placing of any of the shares in the company's capital or any debentures or other securities issued by the company.

12. to draw, make, accept, endorse, discount, execute, and issue promissory notes, bills of exchange, bills of lading, and other negotiable or transferable instruments;

13. to sell or dispose of, to improve, manage, develop or exchange the undertaking, property or rights of the company or any part thereof for such consideration as the company may think fit;

14. to adopt such means of making known and advertising the business and products of the company as may be expedient;

15. to apply for, promote, and obtain any order, regulation, or other authorisation or enactment which may directly or indirectly benefit the company;

16. to procure recognition of the company in any country or place outside India;

17. to issue or allot fully or partly paid shares in the capital of the company in payment or part payment of any movable or immovable property purchased or otherwise acquired by the company or any services rendered to the company;

18. to take or hold mortgages, liens, and charges or secure payment of the purchase price, or any unpaid balance of the purchase price, of and part of the company's property of any kind sold by the company, or any money due to the company from buyer;

19. to produce gas and generate electricity necessary for the purposes of the business of the company and to process or deal with all products resulting from or ancillary to such production.

20. to pay out of the funds of the company all or any expenses which the company may lawfully pay for services rendered for formation and registration of the company and for promotion of any other company by it subject to the provisions of the Act.

21. to insure any of the properties, undertakings, contracts, risk or obligations of the company in any manner whatsoever.

22. to make donations either in cash or in kind for such objects or causes as may be directly or indirectly conductive to any of the company's objects or otherwise expedient;

23. to aid and support, any person, association, body or movement, whose object is solution, settlement or surmounting of industrial or labour problems or the promotion of industry, trade or business of the Company or for the promotion of Science and Technology, Cultural activities, Sports, environment, rural development and other social and welfare activities;

24. to establish or support associations, institutions, schools, hospitals, guest houses, clubs, funds, and trusts which may be considered beneficial to any employees or ex-employees and to officers and ex-officers of the company or the dependents of any such person;

25. to refer all questions, disputes or differences arising between the Company and any other person (other than a Director of the Company) in connection with or in respect of any matter relating to the business or affairs of the Company to arbitration in such manner and upon such terms as the Company and such other person may mutually agree upon in each case and such reference to arbitration may be in accordance with the provisions of the Arbitration Act, 1940 (10 of 1940) and the Rules of the International Chamber of Commerce relating to arbitration, and to institute legal proceedings or defend any proceedings and to appoint advocates, Consultants or Advisors in this behalf;

26. to enter into negotiation or collaboration, technical, financial or otherwise with any person or Government for obtaining any grant, licence or on other terms, formulae and other rights and benefits, and to obtain technical information, know-how and expert advice for the production, manufacture and export or sale of all types of goods which the Company is authorised to produce or to deal in;

27. to arrange for the marketing in India and abroad and sale of the products and by-products of the Company and purchase of raw materials, goods and articles as are necessary for carrying on the business of the Company and, for that purpose, either to establish its own own shops, agencies, or marketing organisations or to appoint selling or buying agents or distributors or both (whether individuals, firms or bodies corporate) in any place in or outside India and to allot, specify, alter or modify their areas of operation or the terms and conditions of their appointment and to pay remuneration to such selling or buying agents or distributors or both by way of such commission or in such other manner as the Company may deem fit;

28. to create any depreciation fund, reserve, reserve fund, sinking fund, insurance fund, or any special or other fund whether for repayment of redeemable preference shares, redemption of debentures or debenture-stock, for dividends, for equalising dividends, for repairing, improving, extending and maintaining any part of the property of the Company;

29. to open and operate any type of bank accounts with the Bank and obtain credit facilities with or without securities for its business;

30. to train or pay for training in India or abroad of any of company's employees or officers or any candidate in the interest of or furtherance of the company's objects;

31. to establish research and development centres for the business of the comany.

Who can plead rule of *ultra vires*

It is quite obvious that the rule of *ultra vires* was devised for the protection of the company's interest and it is not capable of being used against the company's interest. Hence others cannot defeat on the ground of *ultra vires* the claim of a company which has already matured. This question was raised in *Anglo Overseas Agencies Ltd. v. Green,* (1960) 3 All ER 244 : (1961) 31 Com Cases 38 (QB) but the court held, without dealing with the question that the transaction in question was *intra vires*. The question was again raised in *Bell Houses Ltd. v. City Wall Properties Ltd.,* (1966) 2 All ER 674 : (1966) 36 Com Cases 779, where the attempt to defeat the company's claim for consultancy charges earned by the managing director was allowed not to be frustrated by holding that the services were rendered not outside but within the company's general powers. Where the contract or transaction is only in an executory stage, such a plea will be accepted, see *Bell Houses Ltd. v. City Wall Properties Ltd., supra.*

In *Sivashanmugham (S) v. Butterfly Marketing (P.) Ltd.,* (2001) 105 Com Cases 763 : (2001) 43 CLA 28 (Mad—DB), the court observed ***obiter*** as follows: 'A third party may not take advantage of the doctrine of *ultra vires* acts in order to avoid the performance of obligations voluntarily undertaken with full opportunity to know the extent of the company's power before entering into the transaction'.

Shareholders' right to restrain *ultra vires* dealings

An *ultra vires* contract is as null and void as that of a minor. *Steel Equipment & construction Co. (P.) Ltd., Re,* (1968) 38 Com Cases 82, 92 (Cal). No court will pass a decree, not even on consent basis to enforce an *ultra vires* contract. *Beauforte (Jon) (London) Ltd.,* (1953) 1 All ER 634. An *ultra vires* contract is however not illegal. *Universal Mutual Aid & Poor Houses Association Ltd., Re,* (1934) 4 Com Cases 256, 262 (Mad). Consequently, a shareholder can get back the money paid by him to the company under an *ultra vires* allotment of shares. A transferee of shares from him would not have been so allowed. *Margaret Linz v. Electric Wire Co. of Palestine Ltd.,* (1948) 18 Com Cases 201, 205 : AIR 1949 PC 51.

In an Australian case it was recognised that the minority shareholders of a company may, under exceptions to the rule in *Foss v. Harbottle,* be able to bring an action on behalf of the company to restrain the controllers from inducing the company to breach general criminal prohibitions where such a breach might place the company's assets at risk. *Oatmont Pty. Ltd. v. Australian Agricultural Co. Ltd.,* (1991) 5 ACSR (Aust).

Interpretation of the clauses in the memorandum of association (in this case, relating to the deployment of assets of the company) is not a matter of mere internal management. A single member of the company can maintain a suit for a declaration as to the true construction of the clauses in question. *Bharat Insurance Co. Ltd. v. Kanhaya Lal Gauba,* (1934) 4 Com Cases 411 (Lah).

Shareholders' right in respect of *ultra vires* matters

It has generally been considered as an accepted exception to the principle of *Foss v. Horbottle,* (1843) 2 Hare 461: 67 ER 189, that a shareholder can bring a direct action to restrain the company and its directors from pursuing an *ultra vires* transaction and to get an order against directors involved in an *ultra vires* expenditure to make good the company's loss. But there may be circumstances which will prevent such action on the part of a minority shareholder. One such case was before the Chancery Division in *Smith v. Croft (No. 2),* (1987) 3 All ER 909 : (1987) BCLC 206 (Ch D). Where a 14.5% minority shareholder alleged that the executive directors who all belonged to the majority group had paid themselves excessive remunerations and dressed up gifts by way of reimbursement, that the company's associated companies were provided with the company's money to enable them to purchase the company's shares, it was held that the first two payments were not shown to be either excessive or unreasonable but that payments to associated companies for purchasing the company's shares were illegal and not ratifiable, but be-

cause a great majority of the shareholders which included a public financial institution who were independent of the wrongdoers, had decided to abandon or compromise the company's rights and the company being not entitled to sue, the minority shareholder also became disentitled from proceeding with the matter. For critical examination of the decision see L. S. SEALY, CASES AND MATERIALS IN COMPANY LAW, 541, (6th edn., 1996).

Financial Corporation and its borrower company's extra-territorial powers

The insistence by a State Financial Corporation upon a company to confine its activities to one State only, militates against the express provisions of section 13(1)(e). *Kalitara Wood Industries Ltd., In re,* (1989) 3 Comp LJ 24, 27 (CLB).

Statutory Corporations and *ultra vires*

A statutory fund was created in the hands of a corporation to encourage economic development of remote and isolated communities. It lent money to a company which was not anywhere near such communities. The company could not pay back. The guarantor of the loan was sued. Holding him not liable, here is what the court laid down: [*Communities Economic Development Fund v. Canadian Pickles Corpn.,* (1992) LRC (Comm) 589 (Canada SC).

As a statutory corporation the fund had only those powers granted to it by statute and any acts or contracts exceeding those powers were *ultra vires* and null and void. The fund had acted contrary to its objects in s. 3 of the Communities Economic Development Fund Act, RSM 1987, c C155 by making a loan to a company that was not located in a remote and isolated community and, therefore, pursuant to s. 9(7) of the Act (which prohibited loans in contravention of the Act) had acted *ultra vires.* Although s. 26(2) of the Act granted the fund the capacity and powers of a common law corporation, which were the same as those of a natural person and had the effect of abolishing the *ultra vires* doctrine, s. 9(7) of the Act could only be interpreted as limiting the wide powers of s. 26(2) because otherwise s. 9(7) would be superfluous and every word of a statute must be given meaning. Section 7(c) of the Act, which enabled the fund to exercise the powers in Pt III of the Corporations Act, which in turn abolished the doctrine of *ultra vires,* was intended only to give the fund incidental and ancillary powers necessary to further its statutory objects since there was clearly a legislative intention in s 9(7) of the Act to retain the doctrine of *ultra vires* for the fund. Further, although s. 16(3) of the Corporations Act stated that no act of a corporation was invalid only because it was contrary to its articles or the Corporations Act, that section was part of a legislative scheme to abolish the doctrine of *ultra vires* whereas it was intended to retain the doctrine for the fund. Finally, s. 9(7) of the Act prevailed over s. 16(3) of the Corporations Act by virtue of s. 26(5) of the Act. Accordingly, the fund had acted *ultra vires.* The Court referred to *Canadian Bank of Commerce v. Cudworth Rural Telephone Co.,* [1923] SCR 618 (Canada).

The guarantor was also held not liable for being the guarantor of an invalid debt. He was also not liable under the quasi-contractual liability for money had and received for the benefit of the provider of the money. The court said that it was of the essence of an action for money had and received that the defendant had actually received the money sued for. As the guarantor had received no money, it followed that he was not liable on the basis of money had and received.

Limited liability of members [Sub-section (2)]

The provisions of the legislation relating to liability of members of limited liability companies are of the utmost importance. They concern a fundamental right of the member who normally is only willing to become a member on the understanding that the position of his liability would not be altered without his consent. Accordingly, no alteration in the memorandum or the articles can compel a member to take up more shares than the number which he held at the date when the alteration was made, or increase his liability to contribute money. Any provision to the contrary in the memorandum or articles would be null and void. *McKewan's* case, (1877) 6 Ch D 447 and *Biddulph and District Society v. Agricultural Wholesale Society,* (1927) AC 76; *Hole v. Garnsey,* (1930) AC 472. A limited company cannot reregister as unlimited without the written assent of every mem-

ber. This right has been described by JENKINS LJ as "individual rights of membership." It is, indeed, an individual membership right of the highest order because..... it cannot be overruled by a majority of even all the members other than the opposing one. *Edwards v. Halliwell,* (1950) 2 All ER 1064, 1067 (CA).

A member can, by contract with another member or a third party undertake to subscribe to more shares in the company. Such obligation is of contractual nature and not an obligation flowing from his status as a member of the company.

Subscribers' liability [Sub-section (3)]

Section 13 provides that no subscriber to the memorandum shall take less than one share and each subscriber shall write opposite his name the number of shares he takes. Where this was not done a person whose name was mentioned as subscriber was held not to be a subscriber. *Arthanari Transport (P.) Ltd. v. K.P. Swami Goundar,* (1965) 35 Com Cases 930 (Mad—DB). All the subscribers put together must make up the minimum prescribed capital limit as per amended provisions in S. 3(1)(iii) and (iv).

The liability of each subscriber is equal to the total amount due on the shares subscribed for by him. The liability will not be discharged by his taking a transfer of the shares allotted to any other person nor by the allotment to him of any shares credited as fully paid up to which some other person is entitled. *Migotti's* case, *Re, South Blackpool Hotel Co.,* (1867) LR 4 Eq 238; *Forbes and Judd's* case, *Heyford Iron Works Co.,* (1870) 5 Ch App 270.

If a subscriber subscribes in his own name, but in fact as an agent, the obligation will be discharged by the principal taking the shares subscribed for. *Dunster's* case, (1894) 3 Ch App 473. If a subscriber subscribes for a certain number of preference shares or equity shares or both, he may be permitted to vary his choice, provided he takes up on the whole shares of a total value not less than the value subscribed for. *Cf. New Buxton Lime Co., Duke's* case, (1876) 1 Ch D 620.

Share capital—authorised, issued and subscribed [Sub-section (4)]

In the case of a company limited by shares or a company limited by guarantee and having a share capital the amount of the share capital with which the company is to be registered is usually called the *authorised or nominal capital,* and it must be stated in the memorandum. Such capital may be increased according to the circumstances and requirements of the company in the course of its career after incorporation (section 94).

The authorised or nominal capital sets the limit of capital available for issue and the issued capital can never exceed that limit.

Out of the issued capital, the total amount actually subscribed or agreed to be subscribed is known as subscribed capital, and this subscribed capital again may be wholly paid or partly paid in which latter case the balance would be payable on future calls when made. The amount actually paid by the shareholders is called the paid-up capital.

In the case of an 'unlimited company' which has a share capital divided into shares of definite amount, although liability of each member is unlimited as against the creditors of the company, the liability on the shares is the only liability to the company, so long as it is a going concern. [*Cf. Re, Mayfair Property Co.,* (1898) 2 Ch 28].

Where the memorandum dealt with the matter to the extent of giving the company power to issue *inter alia* preference shares as part of the original capital and there was no such provision in the articles but in the articles there was an express provision as regards any future issue of new shares, the company was entitled to exercise the powers expressly conferred on it by the memorandum. *A.E. Compbell v. T.E. Rofe,* (1933) 3 Com Cases 81, 88 (PC).

§ See also section 3(1)(iii) and (iv) regarding the minimum paid up capital of the Company.

Division into Shares of Fixed amount [Sub-section (4)(a)]

The words "shares of a fixed amount" require that the amount of shares must be stated in the memorandum in a monetary form. "Fixed amount" does not mean an amount

which can be paid in a legal tender nor does it require the share capital to be stated in terms of a single total amount.

Flexibility to fix denomination for issue of Equity Shares

SEBI Guidelines 2000.—See Notes under Sec. 56.

Fixed amount in different currencies.—The fixed amount cannot be stated in two currencies *i.e.* share of $ 1 (US) or £ 1, but it may be stated in different currencies for different shares. The company was permitted to have a share capital of different shares of £ 30 million, $ 30 (US) million, 30 million Swiss Francs and 30 million Deutsch marks. *Scandinavian Bank Group Plc., Re,* (1987) 2 All ER 70, 73, 74, 79 (Ch D); *Re Australian Pacific Technology Ltd.* [1995] 1 VR 457 (Aust) in which the court approved the issue of shares with a nominal value of 0.01 cent each. But in India it appears that the nominal share capital of a company must be in India and cannot be in any foreign currency.

Mode of execution by illiterate subscriber

Department's Clarification.—When the executant of a memorandum of association is illiterate, he shall give his thumb impression or mark which should be described as such by the subscriber or person writing for him. [*Department's Letter No.* 8/15/58-PR, dated 13-9-1958].

Scrutiny by Registrar of draft memorandum and articles

Department's Instructions.—"A suggestion has been made to the Company Law Board that it would be helpful to promoters if the Registrar could scrutinise and approve the draft Memorandum and Articles of a proposed company before they are presented to him for registration. Though it may not be possible for Registrars to accept a definite commitment in this regard, the Board is of the view that the Registrars should to the extent possible offer their help and advise to those who may approach them in drawing up the Memorandum and Articles. This would be specially desirable in cases where promoters have no prior experience of company promotion. All registrars are advised to take necessary action accordingly." [*Circular No.* 128/HCC/64, dated 27-7-1964].

Note : In practice, vetting of draft memorandum and articles of association has been discontinued by ROCs.

Modification in reference to Government companies

In applying section 13 to Government companies in clause (a) of sub-section (1) of S. 13 the words "in the case of a public limited company, and with 'private limited' as the last words of the name in the case of a private limited company" shall be omitted. *Notification No.* GSR 1234, dated 30-12-1958. Thus, a Government company, incorporated as a private company in terms of section 3(1)(iii) is not required to use the word 'Private' as part of its name.

Secretarial Practice Notes

Check whether:—

(a) the memorandum of association has been prepared in one of the formats given in tables B, C, D and E of Schedule I as the case may be?

(b) the memorandum and articles have been 'printed' (see Notes below section 15)?

(c) the memorandum and articles have been stamped before signatures in accordance with the applicable stamp duty rates in the State?

(d) the object clause in the memorandum of association is classified into three parts, *viz.* main objects to be pursued immediately after incorporation; objects incidental or ancilliary to the attainment of main objects; and other objects, and whether such objects are brief and particularly the "other objects" give the company enough liberty to diversify into different kinds of business, in future?

(e) all the subscribers to the memorandum and articles have signed it in their own hand and added their names, description (son of, occupation and address)?

(f) file with the Registrar of Companies following documents:

(i) Signed memorandum and articles, each duly stamped

(ii) Declaration of compliance in Form No. 1

(iii) Situation of registered office (Form No. 18)

(iv) List of persons who are proposed first directors (Form No. 32, in duplicate)

(v) When any director is appointed by the articles, his consent to act as such and, if required, his undertaking to take and pay for his qualification/shares (Form No. 29) in case of a public company

(vi) A copy of ROC's letter approving name

(vii) Registration fee

(g) collect certificate of incorporation from ROC

(h) obtain seal, registers and forms of share certificates

(i) take steps for appointment of full time directors, if not appointed by articles

(j) prepare agenda for full Board meeting

(k) appoint first auditor in Board meeting within one month from the date of incorporation of the company, *vide* section 224(5).

(l) take steps for obtaining certificate for commencement of business, in case of public companies

(m) take steps for preparing statement in lieu of prospectus

(n) file with ROC particulars of secretary, and return as to allotment.

Documents involved: 1. Memorandum and articles of association duly stamped and executed by subscribers and witnessed; 2. Form Nos. 1, 18, 29 and 32; 3. Letter of the Registrar indicating availability of name and to check that the name in the memorandum and articles is correctly specified.

S. 14. Form of memorandum.—The memorandum of association of a company shall be in such one of the Forms in Tables B, C, D and E in Schedule I as may be applicable to the case of the company, or in a Form as near thereto as circumstances admit.

NOTES

Eng. Act, 1948 : Sec. 11. Previous Act : Sec. 151(1).

It has to be noted that the memorandum of association of a company should be in one of the Forms specified in Tables B, C, D and E of Schedule I or as near thereto as the circumstances other than a company limited by shares should also be in the Forms given in Tables C, D and E of Schedule I. (*Vide* section 29).

It is adherence to the form rather than the content which is enjoined by the section. *Gaiman v. National Association for Mental Health,* (1971) Ch 317.

S. 15. Printing and signature of memorandum.—The memorandum shall—

(a) be printed,

(b) be divided into paragraphs numbered consecutively, and

(c) be signed by each subscriber (who shall add his address, description and occupation, if any), in the presence of at least one witness who

shall attest the signature and shall likewise add his address, description and occupation, if any.

NOTES

Eng. Act, 1948 : Sec. 3
Eng. Act, 1985 : Sec. 2

Previous Act : Sec. 9

A subscriber to the memorandum and articles must add to his address, particulars of his occupation also.

A company being a legal person may be a subscriber to the memorandum though it cannot be deemed to be a director. (See section 254).

How to subscribe

A subscriber may subscribe the memorandum in his own hand or he can subscribe by the hand of an agent duly authorised by him. Where a company or other body corporate is a subscriber the memorandum must be signed by a duly authorised agent. *Whitley Partners Ltd., Re,* (1886) 32 Ch D 337.

In subscribing the memorandum of association care must be taken to write clearly, the number of shares subscribed for in words or figures, but if more than one share is subscribed the words or figures must be written by each subscriber. The subscribers should subscribe for such number of shares as may constitute the minimum paid up capital as required by section 3(1)(iii)/(iv). The signature should set out the full name of the subscriber, and should be followed by the subscriber's address clearly written and sufficiently explicit.

If a person does not sign in the way as required by the prescribed form or does not fill the particulars prescribed, he does not become a subscriber to the memorandum. *Arthanari Transports P. Ltd. v. K.P. Swami Gounder,* (1965) 35 Com Cases 930 (Mad).

How to witness

As regards the witnesses to the signatures of the subscribers, one witness for all the signatures will suffice, and, in that case, the words "Witness to the above signatures" will be used; but sometimes the same witness cannot attest all the signatures, and in that case the form of attestation must be altered. It may run thus:

Witness to the above signatures other than that of A.

or,

Witness to the signatures of the above B.

The witness or witnesses must in each case give his address or their addresses. This also should be clearly written and sufficiently explicit for identification. One subscriber cannot witness and attest the signature of the other subscriber or subscribers.

There is no objection to one witness attesting all the signatures provided he is not himself a subscriber to the memorandum. *Seal v. Claridges,* (1881) 7 QBD 516. If the attestation of a memorandum of association which has been registered turns out to be irregular it does not render the same void. *Chotalal v. Dal Sukram,* (1892) ILR 17 Bom 472.

Power of Attorney for correction in documents

Department's Circular.—Power of Attorney is required for corrections in the documents at the time of incorporation of companies, filing of prospectus and other documents. While in case of correction of documents, Power of Attorney is required from the signatory concerned, in case of corrections to be made in the Memorandum & Articles of Association and Prospectus, Power of Attorney is insisted upon from all the subscribers of the Memorandum and Articles of Association/directors who have signed the prospectus. At times, some ROCs insist upon either separate Power of Attorney from each person or

jointly executed with the stamp paper of the adequate value as if executed by the person individually. It is hereby clarified that only one Power of Attorney from all subscribers or directors is enough on usual value stamp in such cases. ROCs should accept the Power of Attorney in the manner as classified here and no objection be raised in this behalf. ROCs should also not insist upon any authorisation from the Board of Directors for appointing a Power of Attorney or where the professionals or company's representative come over to ROC to make oral enquiry or submission on any matter (Para xvii(a)). [*Circular No.* 1/95, *F.No.* 14/6/94-CL-V, dated 16-2-1995 issued].

Subscription induced by misrepresentation

A subscriber to the memorandum cannot, after the issue of the certificate of incorporation, repudiate his subscription on the ground that he was induced to sign by misrepresentation. *Re, Metal Constituents Ltd., Lord Lurgan's* case, (1902) 1 Ch 707.

Subscribers as members and their liability

The subscribers of the memorandum are deemed to have agreed to become members of the company, and on its registration shall be entered as members in its register of members (s. 41).

It is not necessary that there should be a formal allotment of shares to the subscribers and therefore no return as to allotment is required in this respect.

The obligation to pay for the shares subscribed applies even if the subscriber is the nominee of another person.

Offset and Computer Printing

Department's Clarifications.—(1) Offset and Computer Printing.—The department is of the view that offset printing is one of the methods of printing developed recently. This system is as good as normal printing and hence there does not appear any objection in accepting the same by the Registrar for the purpose of Registration (*Circular No.* 3/81 (*Department's F. No.* 8/31/15/80-CL-V), dated 15-12-1981). Computer printing is also recognised for this purpose. *Selvarajan & Co. v. ROC,* (1987) 62 Com Cases 220 (Mad).

(2) Xerox copies.—The Department of Company Affairs *vide* its *Letter No.* 8/31/15/80 CL-V, dated 30-4-1981 has stated that it is not permissible to accept Xerox copies of the Memorandum and Articles of Association for the purposes of registration of companies. This restriction, however, does not apply to copies supplied to members as required by S. 39. If a Xerox copy is a faithful reproduction of the original, there is no reason why it cannot be given to members.

(3) Computer laser printed documents for registration.—The provision in section 15 of the Companies Act, 1956 requires that the memorandum shall be printed. A similar provision exists in section 30 with regard to articles. At present Registrars accept the above documents if they are printed on letter press offset print. The question has been raised whether computer printed documents should be accepted for registration of companies. The opinion expressed by the Court and legal experts has been reviewed and the same is in favour of accepting computer printed documents.

2. The Department of Company Affairs has received representations that in view of development of computerised laser printing, the same should be recognised as a method of printing memorandum and articles under sections 15 and 30 of the Companies Act, 1956.

3. It has now been decided by the Government that with immediate effect the Registrar of Companies shall accept computer laser printed documents for purposes of registration provided the documents are neatly and legibly printed and comply with the other requirements of the Act. This will be an additional option available to public to use laser print besides offset printing for submiting the memorandum and articles for registration of companies. [*Press Note No.* 2/93, CL-V, dated 22-6-1993]. To the same effect *Department's Circular No.* 7/93, dated 22-6-1993.

Stamp duty

The stamp duty on the memorandum of association, being a State subject is different in different States. Please refer *Appendix* 134 for Table of Fees and Stamps'. Refer also K. KRISHNAMURTHY'S INDIAN STAMP ACT, 8th Edn., 2002.

Foreigners and non-residents subscribers, Reserve Bank permission required

Earlier without the permission of the Reserve Bank of India, no foreigner (whether resident or non-resident) and no non-resident citizen and also no company with more than 40% non-resident interest can be a subscriber as per section 29(1-A) of the Foreign Ex-

change Regulation Act, 1973 in any company (other than a banking company) engaged in any activity relating to agriculture or plantation. Subscribing for shares is a form of acquisition by purchase.

For current position see Notes under sections 72 and 108 *post*.

[1][**S. 15-A. Special provision as to alteration of memorandum consequent on alteration of name of State of Madras.**—Where, in the memorandum of association of a company in existence immediately before the commencement of the Madras State (Alteration of Name) Act, 1968 (LIII of 1968), it is stated that Madras is the State in which the registered office of that company is situate, then, notwithstanding anything contained in this Act, the said memorandum shall, as from such commencement, be deemed to have been altered by substitution of a reference to the State of Tamil Nadu for the reference to the State of Madras and the Registrar of the State of Tamil Nadu shall make necessary alterations in the memorandum of association and the certificate of incorporation of the said company.]

[2][**S. 15-B. Special provision as to alteration of memorandum consequent on alteration of name of State of Mysore.**—Where, in the memorandum of association of a company in existence immediately before the commencement of the Mysore State (Alteration of Name) Act, 1973 (31 of 1973), it is stated that Mysore is the State in which the registered office of that company is situate, then, notwithstanding anything contained in this Act, the said memorandum shall, as from such commencement, be deemed to have been altered by substitution of a reference to the State of Karnataka for the reference to the State of Mysore and the Registrar of the State of Karnataka shall make necessary alterations in the memorandum of association and the certificate of incorporation of the said company.]

S. 16. Alteration of memorandum.—(1) A company shall not alter the conditions contained in its memorandum except in the cases, in the mode, and to the extent, for which express provision is made in this Act.

(2) Only those provisions which are required by section 13 or by any other specific provision contained in this Act, to be stated in the memorandum of the company concerned shall be deemed to be conditions contained in its memorandum.

(3) Other provisions contained in the memorandum, including those relating to the appointment of a managing director [3][* * * *] or manager, may be altered in the same manner as the articles of the company, but if there is any express provision in this Act permitting of the alteration of such provisions in any other manner, they may also be altered in such other manner.

(4) All references to the articles of a company in this Act shall be construed as including references to the other provisions aforesaid contained in its memorandum.

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1. Ins. by the Madras State (Alteration of Name) (Adaptation of Laws on Union Subjects) Order, 1970, (w.e.f. 14-1-1969).
2. Ins. by the Mysore State (Alteration of Name) (Adaptation of Laws on Union Subjects) Order, 1974, (w.e.f. 1-11-1973).
3. The words "managing agent, secretaries and treasures" omitted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 6 (w.e.f. 13-12-2000).

NOTES

Eng. Act, 1948 : Secs. 4 and 23
Eng. Act, 1985 : Secs. 2 and 17.

Previous Act : Sec. 10

Companies Act, 1956

"Sub-clause (1) corresponds to section 10 of the existing Act and section 4 of the English Act. Sub-section (2) brings out the intention quite clearly. Sub-section (3) compare the proviso to section 10 of the existing Act. It has been generalised so as to refer to everything which need not be included in the memorandum". (*Clause 13* of the Bill).

As sub-sections (2) and (3) have effected important changes in the law, decisions given with reference to the provisions of the previous Act or the English Act have to be applied with caution.

Companies (Amendment) Act, 2000

The terms "managing agents, secretaries and treasurers" in sub-section (3) have been omitted by the Amendment Act, 2000. The amendment is of consequential nature.

Scope of section

Only those provisions required by section 13 or by any other provision of the Act to be stated in the memorandum and not any other matters which may be additionally stated therein are to be deemed to be the conditions. Where, for instance, the right to dividend in respect of any class of shareholders is inserted in the memorandum of association of a company, limiting the dividend to a certain percentage, it cannot be regarded as a condition but may be altered by a special resolution. *In re, Rampuria Cotton Mills Ltd.*, (1959) 29 Com Cases 85 : AIR 1959 Cal 253. A statement in the memorandum as to the terms, conditions and remuneration of any managerial personnel does not become a part of the memorandum. It can be altered without going to the court for its sanction and without recourse to special resolution as contemplated by section 17. *Chandulal and Co. Ltd. v. Natwarlal C. Bhalakia,* (1957) 27 Com Cases 377 : AIR 1956 Bom 257 (DB). Neither the transfer of the undertaking of a company to another company nor the dissipation of assets for any cause is either an alteration of memorandum or a reduction of capital. *Shyamapada Chakrabertty v. Controller of Insurance,* AIR 1962 SC 1355 : (1962) 32 Com Cases 258.

As regards alteration of conditions in the memorandum, see sections 17 to 19, 21 to 23 and 94, 100 and 323. Not all alterations of conditions are required to be confirmed by the Company Law Board [*Cf.* section 94].

Alteration of matters other than conditions in the memorandum may be effected in the same manner as alteration of articles, or in any other manner provided by the Act.

The rule of S. 16 will, apply only to those conditions of the memorandum which fall within sub-sections (1) and (2). Other provisions though contained in the memorandum which may be altered in the same manner as the articles will not obviously fall within the rule.

§ For alteration of any condition in the memorandum which may be made by an order under section 397/398, see section 404.

Alteration of the memorandum in the case of a banking company also requires a 'no objection' certificate from the Reserve Bank of India (*vide* section 49-C of the Banking Regulation Act, 1949).

Converting limited liability of directors into unlimited liability

Though such an alteration is an alteration of a condition contained in the memorandum, section 323 provides for such alteration by special resolution and no confirmation by the Company Law Board is necessary therefor.

Alteration of additional clauses

The procedure stated in this section has to be followed only for the alteration of the conditions contained in the memorandum. And only such provisions are regarded as conditions as are required by section 13 to be stated in the memorandum, that is, its five clauses. Anything else contained in the memorandum can be altered simply by passing a special resolution. See *Ramkumar Potdar v. Sholapur Spinning & Weaving Co. Ltd.*, (1934) 4 Com Cases 481 (Bom). *Ahmedabad Jubilee Mills v. Chotta Lal,* (1908) 10 Bom LR 141; *Venkataramana v. The Coimbatore Mercantile Bank,* AIR 1924 Mad 126. The English law is thus stated in PALMER: "Occasionally additional provisions are inserted into the memorandum clauses, for example, defining rights attached to different classes of shares, rights as regards dividend, voting and participation in assets on a winding up, and various other matters. There is nothing illegal in the insertion in the memorandum of such additional provisions, which likewise could have been contained in the articles, but it must be borne in mind that, if inserted without qualification, they become conditions contained in the company's memorandum within the meaning of section 2(7) of English Act of 1985. [Indian Act, 1956, s. 16(2), (3)]

Where the additional provision is contained in the objects clause, the procedure relating to objects has to be followed. But where the additional provisions are in the nature of class rights, the procedure relating to alteration of class rights would also have to be followed. *Re, Hampstead Garden Suburb Trust Ltd.,* (1962) 2 All ER 879.

Spelling and grammatical mistakes

The spelling and grammatical mistakes in the memorandum of association may be rectified by passing a special resolution without seeking the approval of the Company Law Board under section 17. This is so because under section 16 alteration of the conditions contained in the memorandum only requires the approval of CLB [Now Central Government].

Note : As and when the Companies (Second Amendment) Act, 2002 comes into force, the power under sections 17, 18 and 19 shall become transferred to the Central Government to be exercised by it in place of the Company Law Board. The Guidance Note should be read keeping this changeover in mind.

ICSI Guidance Note on Compliance Certificate (August 2003)

The ICSI has issued a Check List for issue of Compliance Certificate under proviso to Sec. 383A(1) in respect of the matters specified under Rule 3 of the Companies (Compliance Certificate) Rules, 2001.

Paragraphs 26 to 29 under Rule 3 relate to alteration of memorandum and read as follows:

Paragraph-26.—The company has altered the provisions of the Memorandum with respect to situation of the company's registered office from one state to another during the year under scrutiny after complying with the provisions of the Act. [See Notes under sec. 17]

Paragraph-27.—The company has altered the provisions of the Memorandum with respect to the objects of the company during the year under scrutiny and complied with provisions of the Act. [See Notes under sec. 17]

Paragraph 28.—The company has altered the provisions of the Memorandum with respect to name of the company during the year under scrutiny and complied with the provisions of the Act.

Prescribed Check List

ALTERATION OF THE MEMORANDUM WITH RESPECT TO NAME CLAUSE

Check whether:

(i) the company had obtained the availability of new name from the Registrar of Companies;

(ii) the Board of Directors had called and held the general meeting within six months of the date of Registrar's letter intimating the availability of name;

(iii) the company has passed the special resolution for the change of name and obtained approval of the Central Government (Registrar of Companies) in this respect;

(iv) the company has filed with the Registrar of Companies certified true copy of the special resolution along with the relevant explanatory statement and the letter issued by the Registrar of Companies making the new name available with the company;

(v) the ROC has issued a fresh Certificate of Incorporation incorporating the alterations consequent to change of name;

(vi) every copy of memorandum issued after the date of alteration is in accordance with the alteration;

(vii) the name has been painted/affixed/printed on the name board, business letters, bill heads, Memorandum and Articles; and

(viii) new common seal has been adopted by the Board.

Paragraph 29.—The company has altered the provisions of the Memorandum with respect to share capital of the company during the year under scrutiny and complied with the provisions of the Act.

Prescribed Check List

ALTERATION OF MEMORANDUM WITH RESPECT TO SHARE CAPITAL

Check whether:

(i) the Articles of Association authorise the alteration of share capital;

(ii) the Board of directors have passed a resolution approving the alteration of capital as above;

(iii) the company had called and held the general meeting and obtained approval of the company in general meeting by an ordinary resolution for the alteration;

(iv) the company has filed Form No. 5 and Form No. 23 (if the articles are amended), with the ROC; and

(v) every copy of Memorandum and Articles issued after the date of alteration is in accordance with the alteration.

ALTERATION OF OBJECTS

Prescribed Check List [as per ICSI's Guidance Note, March, 2003]

Check whether the provisions of the Memorandum with respect to the objects of the company was altered during the year. If so, check whether :

(a) the company has filed with the ROC in Form No. 23 the special resolution passed by the company within one month from the date of such resolution;

(b) the ROC issued certificate registering alterations; and

(c) the alterations had been incorporated in all the copies of the Memorandum.

§ For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

§ For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

Secretarial Practice Notes:

§ See Secretarial Practice Notes under sections 17, 20, 94, 100 and 106.

[1][*S. 17. Special resolution and confirmation by Central Government required for alteration of memorandum.—(1) A company may, by special resolution, al-*

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1. **Subs. by the Companies (Second Amendment) Act, 2002 (11 of 2003), s. 7. Prior to its substitution it stood as under:**

"S. 17. Special resolution and confirmation by [1][Company Law Board] required for alteration of memorandum.

(1) A company may, by special resolution, alter the provisions of its memorandum so as to change the place of its registered office from one State to another, or with respect to the objects of the company so far as may be required to enable it—

(a) to carry on its business more economically or more efficiently;

(b) to attain its main purpose by new or improved means ;

(c) to enlarge or change the local area of its operations ;

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

(e) to restrict or abandon any of the objects specified in the memorandum;

[Footnote 1 contd.]

ter the provisions of its memorandum so as to change the place of its registered office from one State to another, or with respect to the objects of the company so far as may be required to enable it—

(a) to carry on its business more economically or more efficiently; or

(b) to attain its main purpose by new or improved means; or

(c) to enlarge or change the local area of its operations; or

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

(e) to restrict or abandon any of the objects specified in the memorandum; or

(f) to sell or dispose of the whole or any part of the undertaking, or of any of the undertakings, of the company; or

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[Footnote 1 contd.]

(f) to sell or dispose of the whole, or any part, of the undertaking, or of any of the undertakings, of the company; or

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

[2][(2) The alteration of the provisions of memorandum relating to the change of the place of its registered office from one State to another shall not take effect unless it is confirmed by the Company Law Board on petition.]

(3) Before confirming the alteration, the [3][Company Law Board] must be satisfied—

(a) that sufficient notice has been given to every holder of the debentures of the company, and to every other person or class of persons whose interests will, in the opinion of the [4][Company Law Board], be affected by the alteration ; and

(b) that, with respect to every creditor who, in the opinion of the [3][Company Law Board], is entitled to object to the alteration and who signifies his objection in the manner directed by the [3][Company Law Board], either his consent to the alteration has been obtained or his debt or claim has been discharged or has determined, or has been secured to the satisfaction of the [3][Company Law Board]:

Provided that the [3][Company Law Board] may, in the case of any person or class of persons, for special reasons, dispense with the notice required by clause (a).

[4][(4) The [1][Company Law Board] shall cause notice of the petition for confirmation of the alteration to be served on the Registrar who shall also be given a reasonable opportunity to appear before the [1][Company Law Board] and state his objections and suggestions, if any, with respect to the confirmation of the alteration.]

(5) The [3][Company Law Board] may make an order confirming the alteration [5][* * * * *] on such terms and conditions, if any, as it thinks fit, and may make such order as to costs as it thinks proper.

(6) The [1][Company Law Board] shall, in exercising its powers under this section, have regard to the rights and interests of the members of the company and of every class of them, as well as to the rights and interests of the creditors of the company and of every class of them.

(7) The [6][Company Law Board] may, if it thinks fit, adjourn the proceedings in order that an arrangement may be made to the satisfaction of the [6][Company Law Board] for the purchase of the interests of dissentient members; and may give such directions and make such orders as it thinks fit for facilitating, or carrying into effect, any such arrangement :

Provided that no part of the capital of the company may be expended in any such purchase."

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1. Company Law Board was subs. For 'the Court' by section 5 of the Companies (Amendment) Act, 1974.
2. Subs. by the Companies (Amendment) Act, 1996 from the following:
   "(2) The alteration shall not take effect until, and except in so far as, it is confirmed by the Company Law Board on petition."
3. Subs. by Act 41 of 1974, s. 5 for "Court" (w.e.f. 1-2-19975).
4. Subs. by Act 65 of 1960, s. 6.
5. The words 'either wholly or in part, and' omitted by the Companies (Amendment) Act, 1996.
6. Subs. by Act 41 of 1974, s. 5 for "Court" (w.e.f. 1-2-1975).

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

(2) The alteration of the provisions of memorandum relating to the change of the place of its registered office from one State to another shall not take effect unless it is confirmed by the Central Government on petition.

(3) Before confirming the alteration, the Central Government must be satisfied—

(a) that sufficient notice has been given to every holder of the debentures of the company, and to every other person or class of persons whose interests will, in the opinion of the Central Government, be affected by the alteration; and

(b) that, with respect to every creditor who, in the opinion of the Central Government, is entitled to object to the alteration, and who signifies his objection in the manner directed by the Central Government, either his consent to the alteration has been obtained or his debt or claim has been discharged or has been determined, or has been secured:

Provided that the Central Government may, in the case of any person or class of persons, for special reasons, dispense with the notice required by clause (a).

(4) The Central Government shall cause notice of the petition for confirmation of the alteration to be served on the Registrar who shall also be given a reasonable opportunity of appearing before the Central Government and state his objections and suggestions, if any, with respect to the confirmation of the alteration.

(5) The Central Government may make an order confirming the alteration on such terms and conditions, if any, as it thinks fit, and may make such order as to costs as it thinks proper.

(6) The Central Government shall, in exercising its powers under this section, have regard to the rights and interests of the members of the company and of every class of them, as well as to the rights and interests of the creditors of the company and of every class of them.

(7) The Central Government may, if it thinks fit, adjourn the proceedings in order that an arrangement may be made to the satisfaction of the Central Government for the purchase of the interests of dissentient members; and may give such directions and make such orders as it thinks fit for facilitating or carrying into effect, any such arrangement:

Provided that no part of the capital of the company may be expended for any such purchase.].

NOTES

Eng. Act, 1948 : Sec. 5.
Eng. Act, 1985 : Secs. 4, 5 and 6.

Previous Act : Secs. 12, 13 and 14

Note : As and when the Companies (Second Amendment) Act, 2002 [11 of 2003] comes into force, the power under this section shall become transferred to Central Government and would be exercised by the Central Government in place of Company Law Board. The commentary should be read keeping this changeover in mind.

Companies Amendment Acts of 1974 and 1988

The jurisdiction hitherto exercised by the Court under sections 17, 18, 19, 79, 141 and 186 was taken away and conferred on the Company Law Board. The reason for the change is thus stated in the Notes on Clauses: "The Administrative Reforms Commission has recommended that the functions which are now discharged by the Courts under the Companies Act, 1956, may be reviewed and those which are essentially of an administrative nature may be transferred to the Executive. This recommendation of the Administrative Reforms Commission has been examined and it is proposed to transfer some of the functions of the Court of administrative nature to the Central Government." (*Clauses* 4, 8, 11, 12).

The Joint Committee of Parliament which considered the Bill recommended the substitution of 'Company Law Board' for 'Central Government' as the Committee was of the view that the powers to be exercised being of a *quasi*-judicial nature should not be exercised by the Central Government but must be conferred by the statute itself on the Company Law Board which, in its view, was fitted to exercise such powers. (*Report*: para 20).

In order to enable the Company Law Board to discharge its functions efficiently, section 10-E was amended by the Amendment Act of 1974 and has been further amended by the Amendment Act of 1988. Though the Company Law Board has now taken the place of the 'Court', yet, as the Company Law Board also will be guided in the disposal of cases by the ruling of the Courts, the references to judicial decisions given in the Notes in the previous editions of the book are given in this edition also.

Though 'Company Law Board' was substituted for 'the Court' by the Companies Amendment Act, 1974, proceedings pending in the Court at the time of coming into force of the amendment, were saved by section 5 (2) of the Amendment Act, which provide as follows:—"Nothing contained in sub-section (1) shall apply to any proceedings under section 17 or under sub-section (4) of section 18 which is pending at the commencement of the Companies (Amendment) Act, 1972, before, any Court or to any alteration of the memorandum of a company which has been confirmed, before such commencement by any Court."

The object of sub-section (4) inserted by Act LXV is "to empower the Registrar to appear before court in case he desires to point out any irregularity in an alteration to its memorandum proposed by a company." (*Joint Committee Report,* para. 15)

Companies (Amendment) Act 1996

The Amendment Act of 1996 made this change in the structure of s. 17 that for any alteration of the objects clause all that is necessary is a special resolution. Sanction of the Company Law Board has been dispensed with. The emerging situation, therefore, is that while companies are free to alter their objects without CLB [*Now Central Government*] sanction, the alteration has to be confined within the limits set by sub-section (1). Any alteration in excess of the permitted range will amount to a violation of the Act.

Sanction of the CLB remains necessary for inter-state shifting of registered office. Now as a result of the Second Amendment Act of 2002, this sanction would be accorded by the Central Government instead of the CLB after enforcement.

The commentary relating to alteration of the objects clause, now not requiring confirmation by CLB, has been, however, retained because the restrictions envisaged by sub-s. (1) are still applicable as a contract between the company and its members. Thus objects are not freely alterable. They are alterable only within the limits of sub-s. (1).

Companies (Second Amendment) Act, 2002 [11 of 2003]

This section has been substituted by the Companies (Second Amendment) Act, 2002. The existing provisions of section 17 empower the Company Law Board to confirm an alteration of the memorandum of association of a company relating to shifting of registered office of a company from one State to another. Now this power has been conferred upon the Central Government. (The conferment will take place from the effective date of

the enforcement of the amendment) The amendments are of a consequential nature. Notes on clauses of a Bill stated thus:

"This clause seeks to substitute a new section for section 17 of the Companies Act, 1956. The existing provisions contained in section 17 of the Act empower Company Law Board to confirm alteration of memorandum of association of a company. It is now proposed to confer this power upon the *National Company Law Tribunal. This amendment is of consequential nature (*Clause* 7 of the Companies (Amendment) Bill, 2001)."

It may be recalled that originally this power vested with the High Courts and was conferred on the Company Law Board by the Companies (Amendment) Act, 1974. This is for the first time that the power is being conferred on the Central Government.

Difference between English and Indian Acts

Under the English Act it is left to specified number of shareholders or debenture-holders objecting to any alteration of the memorandum, to take the initiative of making an application to the Court. Under the Indian Act, an application for confirmation of the alteration must be made by the company and be subjected to scrutiny by the Company Law Board. The alteration is not to take effect until confirmed by the Company Law Board. This procedure has been confined by the Amendment Act of 1996 only to inter-State shifting of the registered office of the company. So far as any alteration of the objects is concerned, the requirement of CLB approval has been dispensed with. Now companies are free, within the limits of sub-section (1), to alter their objects simply by passing a special resolution.

The restriction on the company's powers to alter its objects only for one or more of seven purposes as stated in s. 17 was removed in England by the Companies Act, 1989, so that a company can reconstruct its object clause in any way it thinks fit, provided that the reconstructed clause does express objects or purposes which the company is to pursue in the future. [s. 110, 1989 Act]. The amended section 17 of the Companies Act, 1956 (India) still retains the requirement of keeping the alteration within the limits of sub-section (1).

Special resolution for alteration of memorandum

In *Parikh Engineering & Body Building Co. Ltd., Re* (1975) 45 Com Cases 157 (Pat) a learned Judge of the Patna High Court held that where a special resolution was found ineffective for want of 21 days notice in calling and holding the meeting for passing the resolution, the unanimous consent of 95% or more of the shareholders would be sufficient for making the resolution effective as a special resolution. Section 171(2) only provides that a general meeting may be called by giving shorter notice than 21 days if consent is accorded thereto, as provided therein by all the members in the case of an annual general meeting and by 95% of the holders of voting rights or voting power as provided therein in the case of any other meeting. That section does not dispense with the necessity of calling and holding the meeting necessary for passing the required special resolution. And section 192 (4) covers only cases of resolutions agreed to by all the members.

Where two shareholders of a company contested the validity of the special resolution on the ground that they had not received any notice, their objection was ignored because they were holding shares jointly with another and that other had attended the meeting. *K.G. Khosla Compressors Ltd., Re,* (1998) 91 Com Cases 546 : (1997) 4 Comp LJ 461 : (1997) 14 SCL 97 : (1997) 27 Corpt LA 139 (CLB—Northern).

The case of *Bratton Seymore Service Co. Ltd. v. Oxborough,* 1992 BCLC 693 (CA) confirmed that a company's constitution cannot be rectified to reflect the true intention of the subscribers. Its wording can only be altered in the prescribed manner, that is, by a special resolution.

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* Originally this power was proposed to be transferred to NCLT but at the time of passing of the Bill the power was given to Central Government.

Resolution by Postal Ballot by listed Company

The special resolution for alteration in the object clause of the Memorandum needs to be passed through postal ballot in terms of section 192A by a listed public company.

See Rule 4(a) of the Companies (Passing of the Resolution by Postal Ballot) Rules, 2001.

§ For futher discussion see Notes under section 192-A and *Appendix* 41 for Relevent Rules.

Power of Company Law Board

It is clear from the provisions of section 17 that if the alteration proposed is one of the several things enumerated in the clauses (a) to (g) of section 17(1), the Company Law Board had jurisdiction to confirm the alteration. This power is fenced round by safeguards which are calculated to protect the interest of creditors, shareholders, and that of general public. As a result of the Amendment Act of 1996, the requirement of CLB approval has been confined only to inter-state shifting of the registered office of the company.

The creditors are protected by express provisions in the section itself. Their consent has to be procured and their claims have to be satisfied in certain events mentioned in the section itself. The public and the shareholders, individually and collectively, are protected by the necessary publicity of the proceedings and the discretion which is vested in CLB.

Appeal against orders of CLB

It may be noted that there was no provision for appeal against the orders of the Company Law Board in respect of a petition under section 17 and the matter was taken care of under the writ jurisdiction. Subsequently section 10F was brought in. It provided for appeals to the High Court. Section 17 has been again amended. The power which was being exercised by the CLB has been vested in the Central Government by the Companies (Second Amendment) Act, 2002 (w.e.f. enforcement date). Once again without making any provision as to appeal. There is no provisions in sections 17, 18 and 19 as to where an appeal would lie against Central Government's decisions. It would seem, therefore, that the remedy would be by way of a writ to the High Court under Articles 226 & 227 and Supreme Court under Article 32.

Whether two resolutions can be confirmed in one petition

In *Northern Enterprises Corporation (P.) Ltd., Re,* (1974) 44 Com Cases 334 (P & H) a single judge of the Punjab and Haryana High Court held that consolidated petition for confirmation of two different special resolutions passed at different meetings was not competent, because s. 17 and Rule 38 and the prescribed form No. 11 of CLB (Bench) Rules, 1975 (*since repealed*) quite clearly showed that each special resolution had to be the subject-matter of distinct petitions. In our view this is too technical an approach to adopt. The requirements of the Act and the Rules could be equally satisfied by filing a single petition in respect of more than one special resolution by seeking recourse to the inherent powers of the Bench under Regulation 44/48 of CLB Regulations, 1991.

Scope of permitted alteration

While the extent of permitted alteration remains the same, the only effect of the amendment of 1996 is that in so far as the alteration is confined to change of objects, the CLB sanction was not necessary. But because sub-section (1) is still applicable to all kinds of alteration and the CLB sanction is still necessary for alteration of the registered office clause for bringing about inter-State shifting of the office, all the cases cited below continue to be relevant to the interpretation of s. 17.

Alteration of objects.—The clauses (a) to (g) are generally liberally construed. In a petition for confirmation of alteration in the memorandum to carry on certain trades since a doubt was entertained by the company whether it would be *ultra vires* of the powers of the company, it was found that those trades were already being carried on with profit, and the object of the petition was only to regularise the position. So the company was allowed

to include in the memorandum carrying on of those items of trade only. *Bolsom Bros. (1928) Ltd., Re,* (1935) Ch 413 : (1935) 5 Com Cases 401. At a time when alteration of objects required sanction of the court, the court said in a case that the question as to whether a company should enlarge its scope of operation or embark on some new kind of business different from that which is already being carried on is a matter which primarily concerns its directors, shareholders and creditors including holders of debentures. If the members and creditors do not object and if it be not shown to the court that the new business which the company proposes to indulge in is of a speculative type or is otherwise objectionable, the court would not stand in the way of the alteration of the objects clause. *Fort Gloster Jute Mfg. Co. Ltd. Re,* (1963-64) 68 CWN 481 (Cal).

In the case of *Nagaisuree Tea Co. Ltd. v. Ram Chandra Karnani,* (1966) 2 Comp LJ 208 (Cal), the addition of the usual clause enabling a company to amalgamate, enter into partnership or arrangement etc. with any other person or company was confirmed.

While the provisions of the section should no doubt be given liberal interpretation, such interpretation should not travel beyond the section. The decision *Re, Motilal Padampat Sugar Mills Co.,* (1964) 34 Com Cases 86 (All) appeared to be rather not in keeping with the section. In this case a sugar manufacturing company was allowed to undertake steel manufacturing subject to the requirement that vague words like "etc." should be dropped and that for a five year period a separate profit and loss account for the new business should be prepared.

The additional business must not be destructive of or inconsistent with its existing business. See *Re, Cyclist's Touring Club,* (1907) 1 Ch 269; *Re, Parent Tyre Co.,* (1923) 2 Ch 222; *Re Bolsom Bros. (1928) Ltd.,* 1935 Ch 413 : (1935) 5 Com Cases 401. The scope of the section is fully discussed by S. P. MITRA, J., in a decision of the Calcutta High Court: *In re, Goneshberi Tea Co. (Private) Ltd.,* (1964) 34 Com Cases 556 (Cal).

An alteration must be only in relation to objects, or of some provision pertaining to the manner in which the company may carry out its objects. *Re, Scientific Poultry Breeders' Association Ltd.,* 1933 Ch 227 : (1933) 3 Com Cases 89 (CA).

In deciding as to whether a company should be allowed to start additional business, an application made in this behalf was not disallowed merely because the new business was wholly different from and bore no relation to the existing business of the company. All that is essential is that it should be capable of being conveniently and advantageously continued with the existing business and is not destructive of or inconsistent with the existing business. *In re, New Asiatic Insurance Co. Ltd.,* (1965) 2 Comp LJ 24, 28 (Punj). See also *Ambala Electric Supply Co. Ltd.,* (1963) 33 Com Cases 585 (Punj); *In re, Modi Spinning & Weaving Mills Co. Ltd.,* (1963) 33 Com Cases 901 (All); *Standard General Assurance Co. Ltd., Re,* AIR 1965 Cal 16. "A company carrying on business in jute was permitted to alter its memorandum for the manufacture of rubber goods. It was also held that it is not necessary that the alteration be confirmed only after the company obtains an industrial licence for opening the new factory." *Juggilal Kamlapat Jute Mills Co. Ltd. v. Registrar of Companies,* (1967) 37 Com Cases 20 : AIR 1966 All 417; *In re, Rajendra Industries (P.) Ltd.,* (1967) 37 Com Cases 563 (Mad). A company carrying on investment business was permitted after its insurance business was taken over by the Government, to alter its memorandum to carry on the business of engineers, metallurgists, textiles and importers and exporters. *In re, New Asiatic Insurance Co. Ltd.,* (1967) 37 Com Cases 331 (Punj); *Industrial Cables (India) Ltd. v. Registrar of Companies,* (1973) 43 Com Cases 353 (P&H); *New Asarwa Mfg. Co. Ltd., Re,* (1975) 45 Com Cases 151, 156 (Guj).

The CLB could sanction very extensive alterations of the objects of a company including a power to purchase other undertakings, a power to amalgamate with other undertakings and a power of sale of the whole undertaking of the company. *New Westminster Brewery Co. Ltd., Re,* (1911) 105 LT 946. The CLB would not fetter commercial enterprises by a narrow construction of the Companies Act. The jurisdiction was of the widest scope and an alteration could be refused only where it appeared that creditors,

shareholders or others having a special interest were being prejudiced. *Crown Lumber Co., Re,* (1943) 4 DLR 415 (Canada).

But the Company Law Board would not sanction an alteration for carrying on a new and totally independent business, if it could not be conveniently or advantageously combined with any of the existing businesses. "Where the court dismissed the application, observing that with the name of the company as the Bharat Mining Corporation Ltd., it will be not only illogical but misleading to the world dealing with this company to introduce independent and separate businesses like construction of buildings, to buy and sell buildings to enter into contracts with the Government for construction of dams, bridges etc. *In re, Bharat Mining Corporation Ltd.,* (1967) 37 Com Cases 430 (Cal). In *Samantaraj Films (P.) Ltd., Re,* (1974) 44 Com Cases 477 (Orissa) B.K. PATRA. J. of the Orissa High Court confirmed the alteration of a memorandum so as to include a clause like the following:—"To give any donation or grant for any religious, educational or any other social purpose or for the benefit of humanity or any section thereof". It looks doubtful whether such an alteration, however laudable the object, can be held to come within any of the seven clauses of sub-section (1).

Contribution to charitable or other funds is 'lawful purpose', and memorandum can be altered to enable the company to make such contribution. *Goneshberi Tea Co. (Pvt.) Ltd., Re,* (1964) 34 Com Cases 556 (Cal).

In the case of a banking company, an application for the confirmation of an alteration was not be maintainable unless a certificate was given by the Reserve Bank that it had no objection *vide* section 49-C of the Banking Regulation Act, 1949.

Powers of CLB was discretionary

The power of the Company Law Board under this section was discretionary. Wide power was given to the Board to confirm the alteration either wholly or in part and on such terms and conditions as it might think fit. *Jayantilal Ranchhoddas Koticha v. Tata Iron and Steel Co. Ltd.,* (1957) 27 Com Cases 604 : AIR 1958 Bom 155; *Gagalbhai Jute Mills P. Ltd., Re,* (1965) 67 Bom LR 723 (Bom). A resolution for alteration could be confirmed only if there was satisfaction that it was in the interests of the company. An alteration unconnected with the existing objects or where the change would alter the basis of the company was not confirmed. *Re, Bolsom Bros. (1928) Ltd.,* 1935 Ch 413 : (1935) 5 Com Cases 401; *Re, Scientific Poultry Breeder's Association Ltd.,* 1933 Ch 227 : (1933) 3 Com Cases 89 (CA). Before confirming the alteration satisfaction had to be recorded as regards not only the interests of creditors and members but of every other person or class of persons whose interests might be affected by the alteration. Where the interests of the State of Orissa and its revenue were likely to be affected, an alteration so as to change the registered office of a company from the State of Orissa to West Bengal was refused to be confirmed. A change sought on the ground of less tax burden in the other State is not a good ground. *Orient Paper Mills Ltd. v The State,* (1958) 28 Com Cases 523 : AIR 1957 Orissa 232. The objection that the State is deprived of its revenue, since a new company could have been floated instead of altering the objects, is misconceived. *New Asarwa Mfg. Co. Ltd., Re,* (1975) 45 Com Cases 151, 156 (Guj).

Interest of creditors.—A company owed Rs. 7.5 crores to depositors. It applied for CLB permission for alteration of objects. The CLB found that the company did not propose a new issue for raising money for the new business and, therefore, there was every likelihood that the new business would be carried on with depositors' money and thereby exposing it to new risks. The proposed alteration was not allowed. The CLB observed that while such permissions had to be liberally granted, it was equally the duty of the CLB to ensure that the cost and expenditure of the new project was met out of the company's own legitimate funds or from sources legally permitted. *Sipani Automobiles Ltd. Re,* (1993) 78 Com Cases 557 (CLB).

Alteration to convert into Nidhi Company.—In *Lord Mahaveer Goutham Benefit Fund Ltd., Re,* (1994) 79 Com Cases 535 (CLB Mad), the Company Law Board refused to confirm an alteration to the effect that the company shall not be entitled to carry on hire purchase and finance business, which was not covered by any of the clauses of s. 17. The company wanted to alter its objects so as to bring them in line with the requirements of the Central Government for recognising a company as a *Nidhi* company under s. 620A. This matter was neither covered by any of the clauses of s. 17 nor the Central Government had issued any guidelines under s. 620A spelling out the requirements of recognising *Nidhi* companies. The CLB did not confirm the alteration but advised the Central Government to issue the necessary guidelines because more and more companies especially in the southern region were seeking recognition as *Nidhi* companies.

Contributions to political parties.—Though the discretionary power of the Company Law Board under the section was wide, there was no power to confirm an alteration which did not fall within the seven sub-clauses of sub-section (1). Where an amendment of the memorandum of association of a company was sought to be confirmed by the Court in order to empower the company to contribute to the political funds of the party in power and in order to enable that party to succeed in the election as in the company's view the stability, security and efficiency of its own business depended on the success and continuance in power of that party, it was held that the alteration fell within sub-clause (b) of sub-section (1). See *Jayantilal Ranchhoddas Koticha v. Tata Iron and Steel Co. Ltd.,* (1957) 27 Com Cases 604 : AIR 1958 Bom 155; *In re, Dehri Rohtas Light Ry. Co. Ltd.,* (1960) 30 Com Cases 387 : AIR 1959 Pat 514; *Morgan v. Tate and Lyle Ltd.,* (1954) 2 All ER 413 (HL). In exercising the discretion the considerations of business morality, national interest etc. were duly considered. *Cf. Indo-Pharma Pharmaceutical Works Private Ltd.,* (1968) 38 Com Cases 313 (Bom). "Alteration for contribution to political parties was allowed without any condition that it should be disclosed in the balance sheet." *In Re, Maharaja Shree Umaid Mills Ltd.,* (1961) 31 Com Cases 273 (Raj); *Indian Steel and Wire Products Ltd. v. CIT, West Bengal,* (1968) 38 Com Cases 660 (Cal); "General welfare or public interest is for the legislature and not for the court. Provided the alteration is within the ambit of the company's power under section 17(1) and does not prejudice any of the interests which the CLB is required to safeguard by section 17(3), the CLB has no power under section 17(2) to refuse to confirm the alteration. *Re, Sri Natesar Spinning and Weaving Mills (P.) Ltd.,* (1960) 30 Com Cases 54 : AIR 1960 Mad 257.

If the shareholders of the company after considering all relevant factors are of opinion that by making contributions to Labour Welfare Funds they would satisfy various aspirations of the workers and ensure smooth running of the company, it would not be proper for the CLB to impose its own view on them. *Goneshberi Tea Co. P. Ltd., In re,* (1964) 34 Com Cases 556, 565 (Cal).

§ See also Notes under s. 293-A.

Recalling erroneous Orders by CLB.—The CLB would have jurisdiction to recall an erroneous order confirming alterations. See *Ugar Sen Parsotam Das v. Chamber of Commerce, Hapur,* (1936) 6 Com Cases 402, 407 : AIR 1937 All 432.

Department's views as regards alteration and diversification of objects

These circulars belong to a period when the whole of the jurisdiction under s. 17 was exercisable by the Court. Subsequently the jurisdiction was transferred to the CLB. Now the requirement of CLB sanction for change of objects has also been ended but the requirement of confining the alteration to the seven points formula of sub-section (1) remains applicable. It appears that for any violation of sub-section (1), shareholders or creditors can raise objections and these will naturally go before the Civil Court. Hence these clarifications have once again regained their vitality as to how changes in objects are to be viewed in the contexts of the seven points of sub-section (1).

Clarification I. "It is often seen that companies having inadequate resources propose to take up objects which may be entirely new, having regard to the existing objects. There have been cases in which companies having very unsatisfactory financial condition have attempted to insert entirely new objects in

the Memorandum on the plea that they expected to do very well if they could take up the newly proposed business. It has been decided that all such cases of undesirable diversification of activities should be opposed at the Court. Whether a proposal for diversification is undesirable or not is to be decided on due consideration of the facts of the particular case and having regard to the policy of the Government on the subject. Government do not favour existing companies taking up new lines of activity which are not reasonably connected with the activities in which they are already engaged.

The reasons for this policy are as follows—

(1) The need to broad-base investment in industries instead of giving the existing shareholders a preferential right to increase their investment in the existing companies;

(2) through the spreading of investment in the manner indicated above, to prevent rise in the shares of existing well-established concerns;

(3) to encourage the growth of managerial talent by enlarging the field for the exercise of top managerial powers;

(4) to enable the shareholders to obtain information about the performance of an undertaking readily from the accounts which are statutorily required to be submitted to the shareholders; and

(5) to enable the State to ascertain the relative efficiency of investment and management in different lines of activity more readily through a scrutiny of the financial accounts which may not be readily available for the constituent units if they are grouped into one company.

In no case, alteration in the objects clause should be opposed where the industrial licence has been given to the company enabling it to branch off into other activities". [*Company News and Notes*, October 1, 1963 issue]

Clarification II. "A reference is invited to sub-section (4) of section 17 of the new Companies Act, 1956 which enjoins the Court [Now CLB], to which a petition has been made by a company for confirmation of an alteration in its memorandum of association, to give the Registrar a reasonable opportunity to appear before the Court [Now CLB] and state his objections and suggestions with respect to the confirmation. This provision is new and was inserted in the Act because it was considered necessary that the Registrar should have the right to appear before the Court [Now CLB] in case he desires to point out any irregularity in the proposed alteration. The Government of India are, however, anxious that this right is judiciously exercised by the Registrars so as not to create an impression in the mind of the public that the new provision is being made use of to harass or unnecessarily interfere with the management of companies. This should be borne in mind whenever any occasion arises for having recourse to the provisions referred to above. In all cases of doubt, Registrars are advised to consult their Regional Directors in the matter before exercising the right conferred on them by the said sub-section." [*Circular letter No.* F. 2(7)-PR/56, dated 20-3-1956].

Clarification III. Change of name during pendency of petition under s. 17.—I am directed to state that it has come to the notice of the Department that in Northern and Eastern Regions, sometimes the Registrars of Companies are permitting change of name of a company based on the company pursuing certain provisions listed in "other objects" as contained in its Memorandum of Association. This change of name is being done while a petition is already lying before the Company Law Board for shifting "object/s", given in "other objects" to main objects in Memorandum of Association.

The aforesaid action of the Registrar of Companies amounts to pre-judging the issue particularly when the matter is pending before Company Law Board under section 17 of the Companies Act, 1956, for approval of CLB for shifting a provision from other objects to the main objects clause in MOA.

In view of the above circumstances, you are advised not to permit change of name during the pendency of a petition under section 17 of the Act before Company Law Board. [*Circular No.* 4/96, *F.No.* 3/7/96-CL-V, dated 13-5-1996].

Note.—This circular should now be read in the light of the Companies (Amendment) Act, 1996 which has permitted the companies to change their objects without sanction of CLB and therefore there are going to be no pending proceedings for CLB sanction for alteration of objects.

Change of place of registered office [Sub-section (1)]

Before the Companies (Second Amendment) Act, 2002 the power of confirming inter state shifting of registered office was vested in the CLB. With effect from the enforcement of the Amendment Act confirmation of resolution for inter-state change of registered office would have to be taken by the Central Government. The commentary should be read keeping this change in mind.

The change of place contemplated is a change within the States of India. Where a company wanted to change from a State in India to Pondicherry which had not merged *de*

jure into India, the Court held that it had no jurisdiction to entertain an application regarding such change. *Krimens Oil Mills Private Ltd. v. Registrar of Companies,* AIR 1958 Mad 450; *Safe Bank Ltd., Nagpur v. Provincial Government,* (1949) 19 Com Cases 241, 245 (Nag). Where the registered office is changed from one State to another, the State has no right to object on the ground of loss of possible future revenue, though it may do so as a creditor in respect of arrears of revenue due to it. The shifting of the registered office is purely a domestic matter for the shareholders of the company. The company is the best judge of how to run its business more economically or conveniently or where to situate its registered office for efficient running of business. See *In re Mackinnon Mackenzie & Co. Private Ltd.,* (1967) 37 Com Cases 516 (Cal); *Parikh Engg. & Body Building Co. Ltd., Re,* (1973) 43 Com Cases 275 (Cal). But see **contra** *Orissa Chemicals and Distilleries (P.) Ltd., In Re,* (1962) 32 Com Cases 497 : AIR 1961 Orissa 162. *Rank Films Distributors v. Registrar of Companies,* (1968) 38 Com Cases 487 (Cal). See also *Bharat Commerce and Industries Ltd. v. ROC,* (1973) 43 Com Cases 275 (Cal). See also *Zuari Agro Chemical Ltd. v. F.S. Wadia,* (1974) 44 Com Cases 465; *Orient Paper Mills Ltd. v. State,* (1958) 28 Com Cases 523, 535 : AIR 1957 Orissa 232. A person who has no stake in the company either as a shareholder or as a creditor cannot object to the shareholders' resolution. The personal creditors of the managing director of the company were held to have no *locus standi* in the matter. Their criminal proceedings against the managing director could not stand in the way of shifting of registered office. *Seaways Maritime P. Ltd. Re,* (2000) 39 CLA 49 : (2000) 27 SCL 201 : (2001) 1 CLJ 141 (CLB). As regards matter to be considered when confirming the special resolution for shifting the registered office of a Company from one State to another, see *Minerva Mills Ltd. v. Government of Maharashtra,* (1975) 45 Com Cases 1 (Bom).

In *Neelachal Auto Ltd. Re,* (2000) 38 CLA 217 : (2000) 27 SCL 71 : (2000) CLC 1693 : (2001) 2 Comp LJ 476 : (2001) 105 Com Cases 288 (CLB) shifting of the registered office from Bihar to Maharashtra was allowed. The company had two manufacturing units—one at Jamshedpur (Bihar) and the other at Pune (Maharashtra). It had undertaken massive expansion programme at Pune Unit and that necessitated the shifting, while its existing factory at Jamshedpur was to be continued.

Where a company duly resolved by a special resolution to shift its registered office from Bombay to Goa, the Company Law Board, in confirming the alteration, observed that the resident shareholders of Bombay could not object as a special class of shareholders. *Zuari Agro Chemicals Ltd. v. F.S. Wadia,* (1974) 44 Com Cases 465 (Bom). The company has a legitimate right to carry its registered office to a State where a majority of shareholders are residing. The CLB held that a permission of this kind cannot be denied to a company. The special resolution of the company was accordingly confirmed *Pal-Peugeot Ltd., Re,* (1997) 89 Com Cases 808 : (1997) 26 Corpt LA 35 : (1997) 3 Comp LJ 334 (CLB). A company which had been taken over by another company was permitted to shift its registered office to the place of the registered office of the other company. *K.G. Khosla Compressors Ltd., Re,* (1998) 91 Com Cases 546 : (1997) 14 SCL 97 at 106 : (1997) 4 Comp LJ 461 (CLB—Del). A company had all its manufacturing units in Uttar Pradesh and had no production unit in West Bengal, its special resolution to carry its registered office from West Bengal to Uttar Pradesh was confirmed. *Upper Ganges Sugar & Industries Ltd. Re,* (2000) 27 SCL 369 : (2001) 105 Com Cases 377 (CLB—EB). A company was allowed to shift its registered office from Bihar to West Bengal inspite of the fact that the Bihar Government had granted lease of land for the company's factory on the condition that it would not shift its registered office. The CLB also said that interest free loans, sales tax, electricity and other subsidies would have no bearing on the proposed shifting. *Usha Beltron Ltd. Re,* (2000) 27 SCL 124 : (2001) 40 CLA 186 : (2001) 104 Com Cases 411 (CLB—FB). The State Government was held to have no *locus standi* to object to inter-state shifting on the ground of loss of revenue. *Metal Box India Ltd. Re,* (2000) 37 CLA 15 : 2000 CLC 988 : (2000) 2 Comp LJ 390 (CLB—Eastern). In another similar case the State Government was not allowed to object on the grounds that the shifting was for no good cause and that it would involve revenue loss to the State and also loss of employment opportunities in the State. *SPML India Ltd., Guwa-*

also loss of employment opportunities in the State. *SPML India Ltd., Guwa-hati Re,* (2000) 4 Comp LJ 177 : (2000) 27 SCL 115 : (2001) 104 Com Cases 486 : (2001) CLC 794 (CLB).

Employees' union, which was a registered body and which represented quite a number of the employees at the registered office of the company, would have the *locus standi* to appear and oppose the application on the ground that their interests would be likely to be prejudicially affected if the resolution is confirmed by the court (CLB) and to bring to the notice of the court that the company, in passing the resolution, did not act *bona fide*, so as to enable the court to consider whether it would be just and equitable to confirm the resolution. It was also held that it was not open to the employees' union or to the ROC to urge that by transfer of the registered office there would be loss of revenue to the State of Bengal or that there would be unemployment in the State or that the meeting at which the special resolution was passed was not itself valid. *Bharat Commerce & Industries Ltd., Re,* (1973) 43 Com Cases 162 (Cal.) **following** *Rank Film Distributors of India Ltd. v. ROC,* (1968) 38 Com Cases 487 : AIR 1969 Cal 32. Where the shifting of the registered office was in accordance with a scheme approved by the BIFR, it was held that the workers had no right of objection because their continuance in the company's employment was ensured unless, of course, a worker preferred voluntary retirement. *Metal Box India Ltd. Re,* (2000) 37 CLA 15 : (2000) CLC 988 : (2000) 2 Com LJ 390 : (2000) 24 SCL 144 : (2001) 105 Com Cases 939 (CLB—EB).

In any case where the registered office is sought to be transferred from one State to another, the Company Law Board before making an order confirming or refusing to confirm the change will consider primarily the interests of the company and its shareholders and also whether the change is *bona fide* and not against the public interest, that is to say, the interests of the country's economy as a whole. Such consideration will be especially necessary in the case of foreign-controlled companies changing their registered office from extraneous motives without caring for the social and/or economic effects of the transfer on the several segments of the country's population.

A company cannot, however, alter its memorandum of association so as to carry its registered office from one country to another, nor has the Company Law Board any jurisdiction to sanction such alteration. See *Kriemens Oil Mills Pvt. Ltd. v. Registrar of Companies,* AIR 1958 Mad 450.

From the provision of section 17 it is plain enough that what has to be decided upon by a special resolution is the alteration of the memorandum and not merely the change of place of the registered office. Again what is required to be confirmed is the alteration of the memorandum and not the change of place of the registered office. The change of place of the registered office cannot be confirmed without there being any corresponding alteration in the memorandum decided upon by a special resolution. Where the special resolution was: "It is hereby resolved that the registered office of the company be shifted from Chhindwara to Bombay in Maharashtra State after taking proper and legal steps". It was held that the resolution could not be confirmed under section 17. *Jamai Majri Co. P. Ltd., Re,* (1963) 12 Jab LJ 80 Short Notes (MP).

It is not necessary that the meeting for passing a special resolution for inter-state shifting of registered office should be held at the registered office of the company. It may be held at any place allowed by s. 166(2). *Metal Box India Ltd. Re,* (2000) 37 CLA 15 : 2000 CLC 988 : (2000) 2 Comp LJ 390 (CLB—EB).

Where a company wanted to shift its registered office from New Delhi to Gurgaon, the Company Law Board, confirmed the company's resolution subject to this condition, that Delhi based shareholders, who were willing to attend annual general meetings, must be provided free transport facility. *A.K.G. Acoustics (India) Ltd., Re,* (1996) 3 Comp LJ 355 (CLB). A similar order was passed in *Welcure Drugs and Pharmaceuticals Ltd. (Co. Petition No.* 197/17/96-CLB decided during May, 1996), where the shifting was from New Delhi to Bhiwandi.

Change in registered office clause to avail loans.—In *Kalitara Wood Industries Ltd., Re,* (1989) 3 Comp LJ 24, 27 (CLB), the Company Law Board deprecated the tendency of the State Financial Corporation and State Industrial Development Corporation of certain States to insist on the registered office of the company to be shifted to that State in order to avail of the financial assistance. The permission to shift can be allowed even if the existing loans of financial corporations require that the company must remain where it was. The refusal by the Court to permit the company to carry its registered office to Andhra Pradesh in 1970 would not prevent the CLB from granting such permission in 1979 because by that time the factory and the main business of the company were already in Andhra Pradesh. *Promode Kumar Mittal v. Southern Steel Ltd.,* (1980) 50 Com Cases 555 (Cal) where the court also pointed out that an application once rejected can be subsequently allowed in the context of changed circumstances.

Obstructions caused by host State.—If the hopes and aspirations of a company to set up an industry in a particular State are frustrated by some action on the part of the State Government itself, the CLB will not deny the right of the company to shift its registered office to any other State which is willing to provide the necessary facilities. *Paradise Plastic Enterprises Ltd., Re,* (1989) 3 Comp LJ 248, 250 (CLB).

Arrangement with dissenting shareholders [sub-section (7)]

The Company Law Board may adjourn confirmation proceedings when there are dissenting members. Sub-section (7) gives this power to enable the CLB to make an arrangement for purchasing the interest of dissentient members. If an arrangement has been arrived at, the CLB may give directions and make orders which are necessary for facilitating or implementing the arrangement. It has been specially provided that no part of the capital of the company is to be expanded for the purpose of making such a purchase of shares.

Note : The Companies (Second Amendment) Act, 2002 has transferred this power to the Central Government. As and when amendment becomes effective the power of confirmation under S. 17 would be exercised by the Central Government.

Efficient and economical conduct of business [Sub-section (1)(a)]

When a company is not in fact carrying on any business it cannot alter its objects under this clause. *Re, Drages Ltd.,* (1942) 1 All ER 194. An alteration to the memorandum providing for payment of remuneration to the members of the governing body will enable the company to carry on its business more economically or more efficiently. *Re, Scientific Poultry Breeders Association Ltd.,* (1933) Ch 227 : (1933) 3 Com Cases 89 (CA).

The words 'efficiently and economically' are capable of giving a very wide power to the company to alter its objects clause for more economic and efficient functioning. *Indian Iron and Steel Co. Ltd., Re,* (1957) 27 Com Cases 361 (Cal).

"To attain its main purpose" [Sub-section (1)(b)]

In clause (b), note the expression "to attain its main purpose" not to attain its main objects. To ascertain which of the numerous matters set out in the memorandum comprises its main objects one has first to look at the memorandum and then get assistance from the evidence as to what in fact have been the main objects and if there is doubt, also have reference to what has actually been done. *North of England Zoological Society v. Chester RDC,* (1959) 3 All ER 116 (CA). Under this head an alteration can only be made to enable the company to attain its main purpose, not any purpose. *Government's Stock Investment Co. (No. 2),* (1892) 1 Ch 597; *Kirkaldy Cafe Co.,* 1921 SC 681; *Incorporated Glasgow Dental Hospital v. Lord Advocate,* (1927) SC 400.

Enlarge or change the local area of operations [Sub-section (1)(c)]

When the effect of the alteration was to enlarge the area of the company's operation, the order of confirmation normally imposed a condition that the company's name indicating that its business was carried on in a particular area should be changed. *Indian Mechanical Gold Extracting Co., Re,* (1891) 3 Ch 538; *Re, Egyptian Delta Land & Investment Co. Ltd.,* (1907) 51 Sol Jo 211.

Conveniently or advantageously combined with existing business [Sub-section (1)(d)]

This gives wide scope for carrying on any business which may conveniently or advantageously be combined with the existing business—which means that the field for alteration of the memorandum is extensive, the only condition being that it should not be prejudicial to or destructive of the existing business. When a company does not carry on any "existing" business, or has stopped such business this clause does not apply. *In re, Eastern Woollen Mills Ltd.*, SHELAT J., (1958) 60 Bom LR 1121, 1124 (Bom).

The question whether any given additional business may be conveniently or advantageously combined with the existing business is within the discretion of those engaged in the business, the views of the shareholders also being given foremost regard. The question must be considered as a business proposition keeping in mind that the new business is not destructive of or inconsistent with the existing business. *In re, Bhutoria Brothers (Private) Ltd.*, (1958) 28 Com Cases 122 : AIR 1957 Cal 593. *Re, Dalmia Cement (Bharat) Ltd.*, (1964) 34 Com Cases 729 (Mad). The case of *Pondicherry Textiles Corpn. v. K.K. Ramanujam*, (1998) 91 Com Cases 441 : (1997) 4 Comp LJ 260 : (1997) 26 C.L.A. 357 (CLB—Mad) highlights the necessity of adopting a business-like approach in examining whether the newly adopted objects are capable of presenting a convenient and advantageous combination with the existing objects. This aspect will remain important despite the fact that approval of the Company Law Board is no longer necessary and the matter is wholly a part of the domestic jurisdiction. Any shareholder can challenge on the ground that there is violation of s. 17 because uncombinable objects are being herded together. Such challenge cannot be presented by a person who is not a member of the company.

A company which carried on distillery business and was empowered to carry on other objects allied to that business could not alter its objects so as to include a cinema business as it was not a business which could be said to be conveniently or advantageously carried on with the distillery business. *Punjab Distilling Industries Ltd. v. Registrar of Companies*, (1963) 33 Com Cases 811 (Punj). But a company which was formed for generating power was allowed to carry on 'cold storage and other allied business'. *In re, Ambala Electric Supply Co. Ltd.*, (1963) 33 Com Cases 585 (Punj).

The general considerations on which an alteration of memorandum to carry an additional business was permitted were thus stated by LAWRENCE, J., in *Patent Tyre Company Ltd., In re*, (1923) 2 Ch 222 at 228: "It is essentially a business proposition, whether an additional business can or cannot be conveniently carried on under existing circumstances with the business of the company. The additional business, of course, must not be destructive of or inconsistent with the existing business; it must leave the existing business substantially what it was before; but the additional business may be one which is different from the original business and yet may well be conveniently and advantageously combined with the business which is being carried on." See also *New Asiatic Assurance Co. Ltd., In re*, (1965) 2 Comp LJ 24 (Punj); *Straw Products Ltd. v. ROC*, (1969) 39 Com Cases 974 (Orissa). A charitable or other associations registered under section 25 may also alter its memorandum. See *Re, Chartered Surveyors' Benevolent Fund Incorporated*, (1936) 2 All ER 1631; *Dominion Students Hall Trust, Re*, 1947 Ch 183.

Where the existing memorandum provided that each clause should be construed independently as a separate object, the court confirmation of an alteration adding new subclauses was refused except on condition of deleting the provision in question or limiting its application. *Cole (EK) Ltd., Re*, (1945) 1 All ER 521 (Ch D).

The validity of a resolution to undertake new business had to be examined in connection with the company's legitimate business and not in connection with an unauthorised business though the company was actually carrying on that business. Thus where a company was manufacturing hinges without any authority in the memorandum and it wanted to combine with it the production of sewing machines also, it was held that s. 17(1)(d) would not cover such a case. *Link Electro-Mechancial Works (P.) Ltd. v. Registrar of*

Companies, U.P., (1963) 2 Comp LJ 111 (All). Where the business sought to be acquired was unlawful (Chit fund in the nature of lottery) confirmation of the necessary alteration was refused. *Udumalpet Nidhi Ltd., Re,* (1934) 4 Com Cases 152, 155 (Mad).

Where a banking company whose business was nationalised wanted to shift over to other business, the resolution for alteration of the objects clause was confirmed. *Mahaluxmi Bank Ltd. v. ROC, W.B.*, (1961) 31 Com Cases 287 : AIR 1961 Cal 666. Where a company was no longer carrying on any business due to financial difficulty and had also leased out its premises, it could be permitted to alter its object clause to enable it to undertake new business. *In Re, Motilal Hirabhai Spg. Wvg. & Mfg. Co. Ltd.*, (1970) 40 Com Cases 1216 (Guj). Where a company's forward business in foodgrains and jaggery was banned, the company was allowed it to alter objects so as to undertake the same business in cotton. *Re, Delhi Bharat Grain Merchants Assn. Ltd.*, (1974) 44 Com Cases 214 (Del).

Where the business of a company was nationalised and it proposed to undertake new objects, the same was allowed, keeping in mind only two things, *viz.*, whether the company was financially sound and whether there were any objections. *Re, United Collieries Ltd.*, (1975) 45 Com Cases 226 (Cal). The CLB accepted this view and it laid down that it was not necessary that the company should have been actually carrying on some business to which a new object might be added. A company could undertake any new convenient or advantageous objects even if at the moment it was not carrying on any of the businesses specified in its objects. *Geo Rubber Exports Ltd., Re,* (1991) 72 Com Cases 713 CLB. **Following** *Canara Bank Ltd., Re,* (1973) 43 Com Cases 157 (Kar); *New Asiatic Insurance Co. Ltd., Re,* (1965) 2 Comp LJ 24 (Punj); *Central Bank of India Ltd.* (Company Petition No. 167 of 1970 (Bom); *Tinnevelly Tuticorin Electric Supply Co. Ltd.* (Company Petition No. 224(17) CLB of 1975). Thus a company which was not able to implement its original objects at all and it was granted a licence by the Government for a new industrial object its application for sanction of the resolution for adopting the new objects, was allowed. *Super Byteron Systems Ltd. Re* (1991) 5 CLA 169 (CLB—NB). Where the directors and members were willing to undertake new business, there were no objecting creditors and the company was financially sound, the alteration was permitted. *Orissa Cement Ltd. v. ROC, Orissa,* 1975 Tax LR 1330 (Orissa). In circumstances similar to this case, a company carrying on business in production of batteries and flash lights was allowed to enter into diverse other fields of consumer goods, real estate, consultancy services etc., etc., *Union Carbide Ltd., Re,* (1991) 6 Corpt LA 6 (CLB).

The Company Law Board refused to allow the applicant company to diversify its activities and venture into new fields when it found that instead of meeting the cost and expenditure of the new project out of the company's own legitimate funds, there was every apprehension that the company might embark upon the new project with the monies refundable to the various depositors. This approach would be prejudicial to public interest. *Sipani Automobiles Ltd., Bangalore,* (1993) 78 Com Cases 557 (CLB).

Negative objects.—Any new positive object could be added with the sanction of the Company Law Board to the existing objects of the company. But an object negatively expressed, *e.g.*, that "the company shall not undertake the following objects", could not, in the opinion of the Company Law Board, be allowed. *SMP Mutual Benefit Ltd., Re,* (1994) 4 Comp LJ 385 (CLB—Delhi); *Balaji Mutual Benefit Ltd., Re,* (1994) 4 Comp LJ 551 (CLB—New Delhi).

Shifting of object from one part of objects clause to other.—A company was carrying on the services of registrar and share transfer agent. This object was mentioned in the "other objects" part of its objects clause. Securities and Exchange Board Regulations, subsequently introduced, required such companies to have the service of such agency to be included in the main objects of the company. The company accordingly applied to the Company Law Board for confirmation of the alteration. The CLB did not grant its confirmation because it was not a typical alteration within the meaning of section 17. *Mafatlal Consultancy Services (India) Ltd., Re,* (1995) 17 Corpt LA 385 (CLB—Bom).

In an allied case on the subject, *Sarvin Securities P. Ltd., Re,* (1995) 17 Corpt LA 387 (CLB—Bom) the CLB laid down that any new business started long after the company's incorporation could not be shown as the main object of the company by alteration of the company's memorandum.

Wholly new object for a wholly different business—A company engaged in the business of running nursing homes became insolvent and was put under administration under the [English] Insolvency Act, 1986. The memorandum contained an inserted clause enabling the company, *inter alia*, to carry on business as nursing home proprietors. There was no special resolution in the company's records nor any with the office of the Registrar but because all the shareholders had acquiesced it was held, that that was a good consent and had the effect of a special resolution. But another important aspect of the matter remained open to doubt and this was whether section 4 of the 1985 Act would permit the adoption of a wholly new object for a wholly different business. *Home Treat Ltd., Re,* (1991) BCLC 705 (Ch D).

"Restrict or abandon any of the objects" [Sub-section (1)(e)]

Even for deleting any portion of the object clause, the procedure laid down in this section had to be followed. The CLB [*now Central Government*] had jurisdiction to confirm alteration which involved the abandonment of objects which were in their character fundamental. See *Jewish Colonial Trust, Re,* (1908) 2 Ch 287.

The words 'restrict or abandon' have been held not to include in the case of a charitable company, substitution of one kind of beneficiary of charity with another. *Hampstead Garden Suburb Trust Ltd., Re,* (1963) 33 Com Cases 166 : 1962 Ch 806 (Ch D).

Amalgamation [Sub-section (1)(f)]

Where a company asked for bare power to amalgamate by altering its memorandum of association, there was no scope for interlocutory relief of injunction. *Hari Krishna Lohia v. Hoolungooree Tea Co. Ltd.,* (1970) 40 Com Cases 458 : AIR 1969 Cal 312 (DB); *Nagaisuree Tea Co. Ltd. v. Ram Chandra Karnani,* (1966) 2 Comp LJ 208 (Cal). Section 398 gives jurisdiction to the Court to sanction an arrangement, even though there may be no power in the objects clause of the Memorandum of Association of the company. *In re, Marybong & Kyel Tea Estate Ltd.,* (1977) 47 Com Cases 802 (Cal).

Requirement of Notice—Position of creditors [sub-section (3)]

Note.—Since by virtue of the Amendment Act of 1996, sanction of CLB is not necessary for changing objects, decisions under this heading will remain directly relevant to inter-State change of registered office because that still requires CLB [*now Central Government*] sanction.

The position of creditors was explained by the Andhra Pradesh High Court in *Re, Commercial and Industrial Bank Ltd.,* (1959) 29 Com Cases 157 at 161 (AP). The court said that it is a matter which the shareholders of the company have to decide and when the shareholders of the company after considering the *pros and cons* of the matter have agreed that the proposed amendments should be made in the memorandum, it is difficult to see how the creditor can object to it. The creditor is only concerned with his money and when the company is ready to give him security for his claim there is no reason why the court should not confirm the resolution.

A scheme for the rehabilitation of a sick industrial company prepared and approved by the BIFR involved inter-state shifting of the company's registered office. The scheme made provisions for settlement of the dues of creditors. It was held that in a petition for confirmation of the resolution for shifting the office, the CLB could not ask for payment of any dues to any creditor since the BIFR scheme was binding upon eyeryone concerned. *Metal Box India Ltd. Re,* (2000) 37 CLA 15 : 2000 CLC 988 : (2000) 2 Comp LJ 390 : (2000) 24 SCL 144 : (2001) 105 Com Cases 939 (CLB—EB).

Where a company had a large number of creditors, the Company Law Board said that it would not be desirable to exempt the company from publishing a general notice in newspa-

pers on the plea that the company would have to bear heavy publication charges. *Classic Welding Products P. Ltd. Re,* (2003) 44 SCL 184 : (2003) 54 CLA 141 (CLB—Chennai).

Objects of Banking Companies

The objects of a banking company can be altered with an additional requirement to be satisfied, *viz.*, approval of RBI, *vide* S. 49C of the Banking Regulations Act, 1949.

Interest of creditors and members [Sub-section (6)]

Though the provision enables the CLB [*now Central Government*] to take care of the interests of creditors and members, the power of the CLB [*now Central Government*] does not thereby become confined to those interests only. The Board can take into account all the affected interests. See sub-section (3)(a) which requires notice to be given to every person whose interest is affected by the alteration. *Orient Paper Mills Ltd., Re,* (1958) 28 Com Cases 523, 529 : AIR 1957 Ori 232.

Creditor's objection

Before the Amendment Act of 1996, a company could alter its objects only with the approval of the Company Law Board. The Company Law Board had to take care of the creditors' objections also, if any. In a matter of this kind before the Company Law Board in *Symphony Comfort Systems Ltd., Re,* (1998) 91 Com Cases 404 (1997) 13 SCL 99 : (1997) 3 Comp LJ 331 (CLB—Mumbai) the Board had to consider a creditor's objection. The company had disputed his claim and had a counter-claim against him for which a civil suit was pending. The Board observed that it had no jurisdiction to adjudicate upon the creditor's claim. The objection was brushed aside.

Objection by creditor of group company.—A special resolution for inter-State shifting of registered office was confirmed by the Company Law Board [*now Central Government*] as passed by the shareholders with a direction that the interests of all the creditors should be safeguarded including that of the sole objector, who, though not a direct creditor of the company, was a creditor of one of the companies in the same group. *Deutsche Babcock Power Systems Ltd., Re,* (1999) 2 Comp LJ 516 : (1999) 21 SCL 133 : (1999) 33 CLA 305 : (1999) 97 Com Cases 341 (CLB–SB).

Objection by employees.—A company resolved to carry its registered office from one State to another. Some employees objected on the ground that shifting of the office would prejudice their cases pending before labour courts. The Company Law Board [*now Central Government*] confirmed the company's resolution with this direction that the company should safeguard the workers' interest. The Board said that the resolution was to be confirmed subject to the conditions that the interests of none of the employees of the company shall be prejudiced either by way of transfer or retrenchment or otherwise and further that pending cases before several courts at Karnataka between employees and the company should not be adversely affected *J.L. Morison (India) Ltd., Re,* (1999) 95 Com Cases 907 : (1999) 1 Comp LJ 158 : (1999) 32 CLA 154 (CLB–SB).

A resolution of the company to shift its registered office from Karnataka to Tamil Nadu was adopted without any objections from any quarters whatsoever. It was sanctioned subject to the condition that the interest of employees working at the registered office of the company should not be adversely affected. *EEC (India) Software Centre Ltd. Re,* (2001) 32 SCL 298 (CLB—Chennai). The decision to shift rests with the shareholders. The company is the best judge as to the location of its registered office. The State Government cannot interfere. The grounds for shifting could not be rebutted by the State Government. The alteration was confirmed subject to the condition that creditors' and employees' interest should not be affected. *Usha Deltron Ltd. Re,* (2000) CLC 2216 (CLB—Cal).

Provisions which could be altered

(i) Provisions of the memorandum, specified in S. 13(3); (ii) increase of capital (s. 94); (iii) cancellation of shares not taken by any person [s. 94 (1)]; (iv) conversion of shares

into stock and *vice versa* [s. 94(1) (c)]; (v) consolidation of shares [S. 94(1) (b)]; (vi) sub-division of shares [s. 94(1) (d)]; (vii) making the liability of directors unlimited (s. 323) can be altered without any special resolution and any provision in the company's articles taking away this power would be inoperative. *Miheer Hemant Mafatlal v. Mafatlal Industries Ltd.*, (1987) 89 Bom LR 86 (Bom).

As a result of the Amendment Act of 1996, objects clause of the memorandum can be altered simply by passing a special resolution and without any sanction.

Petition before CLB for confirmation of change in Registered Office clause

Such petition is not necessary for change of objects. CLB sanction is necessary only for inter-State shifting of registered office.

The petition under sub-section (2) for confirming alteration in Memorandum of Association as to change of place of the registered office from one State to another has to be made in Form No. 1 of Annexure-II and as per Regulation 36 of CLB Regulations, 1991 before the Regional Bench of the Company Law Board, accompanied by the following documents and application fee of Rs. 1000/- :

(1) Copy of the memorandum and articles of association.

(2) Copy of the notice calling the meeting with Explanatory Statement.

(3) Copy of the Special Resolution sanctioning the alteration by the members of the company.

(4) Copy of the minutes of the meeting at which the Special Resoultion was passed.

(5) Copy of the latest audited balance-sheet with the profit and loss account of the company with auditor's report and directors' report.

(6) List of creditors and debenture holders and evidence of service of notice on them under U.P.C.

(7) Affidavit veryfying list of creditors as per Regulation 36(7).

(8) Affidavit proving despatch and service of notice together with newspaper cuttings.

(9) Affidavit verifying the petition.

(10) Acknowledgment receipts from the Registrar of Companies/Regional Director and/or from the Chief Secretary of the State Government/Administrator, where applicable [See Regulation 14(3) (and 36(2))].

(11) Bank draft evidencing payment of application fee.

(12) Memorandum of appearance in Form No. 5 of Annexure II with copy of the Board Resolution or the executed Vakalatnama, as the case may be.

Publish a general notice, at least once, in the district in a daily newspaper published in English and in the principal language of the district in which the registered office of the company is situated, and circulating in that district clearly indicating the substance of the petition and stating that any person whose interest is likely to be affected by the proposed alteration of the memorandum may intimate to the Bench Officer within twenty-one days of the date of publication of that notice stating the nature of interest and grounds of opposition. Where no objection has been received from any of the parties who have been duly served, the Bench Officer may put up the petition for orders without hearing.

The company shall, not less than one month before filing the petition, publish a general notice in the daily newspapers (in regional language and in English language) circulating in the District in which registered office is situated for inviting objections, if any, and also serve under certificate of posting individual notices on each debenture-holder and creditor [Regulation 36(1)(i)]. Petition is required to be filed within two months from the date upto which the list of creditors is prepared and notice to creditors/debenture-holders be issued Under Postal Certificate (UPC) within one month before the date of filing the petition before CLB [*Regulation* 36(6)]. The company may seek dispensation from the

requirement of service of notice on the debenture-holders/creditors by making an interlocutory application, in terms of Regulation 48.

In case of change of registered office from one State to another, notice of the petition may be served by registered post on the Chief Secretary of the State Government or the Administrator or the Lt. Governor, as the case may be. A copy of the petition shall also be served on the Registrar of Companies (also on the Regional Director in case of a section 25 company). An affidavit to prove despatch, publication and service of notice should be enclosed with the petition.

It may also be ensured that the services of employees and workers are not terminated and they are also not retrenched consequent upon shifting of the registered office.

§ For text of CLB Regulations 1991 refer *Appendix* 3.

ICSI Guidance Note on Compliance Certificate [August, 2003]

The ICSI has issued a check list for issue of Compliance Certificate under the proviso to sec. 383A(1) in respect of matters specified under Rule 3 of the Companies (Compliance Certificate) Rules, 2001. Paragraph 26 under Rule 3 relates to alteration of memorandum with respect to change of registered office from one state to another. Paragraph 27 relates to alteration of memorandum with respect to the objects of the company. Paragraphs 26 and 27 read as follows:

Paragraph-26.—The company has altered the provisions of the Memorandum with respect to situation of the company's registered office from one state to another during the year under scrutiny after complying with the provisions of the Act.

Paragraph-27.—The company has altered the provisions of the Memorandum with respect to the objects of the company during the year under scrutiny and complied with provisions of the Act.

Prescribed Check List

ALTERATION IN THE MEMORANDUM OF ASSOCIATION WITH RESPECT TO CHANGE IN REGISTERED OFFICE FROM ONE STATE TO ANOTHER AND OBJECT CLAUSE

Check Whether :

(i) the Board of directors had passed a resolution for change in registered office of the company/alteration of object clause;

(ii) the Board had called a general meeting and necessary special resolution has been passed at the said meeting;

(iii) a certified true copy of the special resolution along with the certified true copy of the explanatory statement was filed with the Registrar in Form No. 23, within thirty days from the date of passing of the resolution;

(iv) a petition has been filed before the Company Law Board*, for confirmation of the alteration of Memorandum relating to change of place of the company's registered office from one State to another;

(v) a certified true copy of the order of the CLB* confirming the Alteration of Memorandum in respect of registered office of the company together with the printed copy of the Memorandum as altered was filed with the ROC of each State;

(vi) the Registrar of each State registered the same and issued the Certificate of registration under his hand; and

(vii) every copy of the memorandum issued after the date of alteration is in accordance with the alteration.

Secretarial Practice Notes:

Check whether:

(i) the alteration falls under any of the purposes specified in section 17(1)(a) to (g)?

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* **Power transferred to the Central Government from the commencement of the Companies (Second Amendment) Act, 2002 (11 of 2003).**

(ii) a special resolution passed, minutes recorded and Form 23, under the Companies (Central Government's) General Rules and Forms, 1956, duly filed along with the explanatory statement with the Registrar of Companies?

(iii) provisions of the Company Law Board Regulations, 1991 regarding petition to the Company Law Board has been complied with?

(iv) the Company Law Board confirmed the alteration?

(v) the order of the Company Law Board has been filed with the Registrar(s) in Form 21 within three months along with a printed copy of the memorandum duly altered?

(vi) the Registrar(s) issued certificates registering the alterations?

(vii) any extension of time for filing the Company Law Board order with the Registrar was sought? [Section 18(4)]. If so, whether the documents filed within the extended period?

(viii) Form 18 duly filed with Registrars of the concerned States and Certificates obtained within 30 days of the change? (when situation of registered office changed)

(ix) provisions of Clause 33 of the listing agreement complied with? (applicable only to listed companies)

(x) the change had been incorporated in the memorandum, as altered and other documents?

(xi) members' requests for memorandum and articles, as altered met within seven days (section 39)?

Documents Involved: 1. Memorandum of Association, (2) Minutes of Board/General Meeting, (3) Forms 18, 21 and 23, (4) Order of the Company Law Board, (5) Registrar's Certificates, (6) Intimation to Stock Exchange, (7) Forms under the Company Law Board Regulations, 1991, (8) Petition under section 17 to Company Law Board along with prescribed documents.

[1][*S. 17A. Change of registered office within a State.—No company shall change the place of its registered office from one place to another within a State unless it is confirmed by the Regional Director.*

(2) The company shall make an application in the prescribed form[2] *to the Regional Director for confirmation under sub-section (1).*

(3) The confirmation referred to in sub-section (1), shall be communicated to the company within four weeks from the date of receipt of application for such change.

Explanation.—For the purposes of this section, it is hereby declared that the provisions of this section shall apply only to the companies which change the registered office from the jurisdiction of one Registrar of Companies to the jurisdiction of another Registrar of Companies within the same State.

(4) The company shall file, with the Registrar a certified copy of the confirmation by the Regional Director for change of its registered office under this section, within two months from the date of confirmation, together with a printed copy of the memorandum as altered and the Registrar shall register the same and

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1. Section 17A inserted by the Companies (Amendment) Act, 2000 (53 of 2000), with effect from 1-3-2001, *vide* Notification No. SO 176(E), dated 27-2-2001.
2. Form 1AD is the prescribed form *vide* Rule 4BBA of the Companies (Central Government's) General Rules and Forms, 1956, issued *vide* GSR 51(E), dated 31-1-2001.

certify the registration under his hand within one month from the date of filing of such document.

(5) The certificate shall be conclusive evidence that all the requirements of this Act which respect to the alteration and confirmation have been complied with and henceforth the memorandum as altered shall be the memorandum of the company.].

NOTES

Companies (Amendment) Act, 2000

This section has been inserted by the Companies (Amendment) Act, 2000 (with effect from the date to be notified by the Central Government in official gazette) to provide that confirmation of the Regional Director shall be required for shifting the registered office of a company from the jurisdiction of one Registrar to the jurisdiction of another within the same State (Cf. *Clause* 7 of the Notes on Clauses of the Bill).

This section has came into enforce with effect from 1-3-2001. [*vide Notification S.O. 176(E), dt. 27-2-2001*].

Statement of Objects and Reasons.—Para 12 of the Statement of Objects and Reasons annexed to the Companies (Second Amendment) Bill, 1999 stated that—

"this new provision is to authorise Regional Directors to allow change of registered office of companies from the jurisdiction of one Registrar of Companies to another Registrar of Companies within the same State".

The Parliamentary Standing Committee on Home Affairs in its 64th Report on the Companies (Second Amendment) Bill, 1999 recommended as follows:

Committee's recommendation.—The Committee recommends that it may be clarified in the rules that the provision of new section 17A shall apply only in case of change of registered office of a company from the jurisdiction of one Registrar of Companies (ROC) to another ROC in the same State [*Para 16.10*].

In order to ensure that a company does not unnecessarily suffer and the Regional Directors remain altert, it may be prescribed in the rules that after an application has been filed in the office of Regional Director, it has to confirm the same within a stipulated period of 30 days, and upon lapse of the specified period it will be deemed that Regional Director has consented to such change [*Para 16.11*].

Scope of section

As per Section 146, the registered office of a company may be shifted—

(i) outside the local limits of the city, town or village within the State on the authority of a special resolution;

(ii) to any other place within the same city, town or village on the authority of a resolution passed by the Board of directors of a company.

The section lays down the procedure to be followed for changing the location the registered office within the State. The provisions have to be complied with apart from making an application to the Regional Director for confirmation of the change of place of registered office within the same State.

Although not so stated under sub-section (4), the company is required to file a certified copy of the order of the Regional Director with both the Registrars of Companies within the same State.

The plain language of section 17A shows that the Regional Director's confirmation is necessary in case of shifting of registered office of a company within the same state from the jurisdiction of one ROC to be jurisdiction of other ROC.

The intention is to cover such cases in which there are more than one ROC offices in one State, for example, Tamil Nadu (one in Chennai and one in Coimbatore) and Maharashtra (one in Mumbai and one in Pune) and the shifting involves the change of jurisdiction of such Registrars.

Procedure for filing Application to Regional Director.—Rule 4BBA of Companies (Central Governments) General Rules and Forms, 1956 prescribes the procedure. It is reproduced below:

"**4BBA. Change of registered office within a State.**—(1) The company seeking confirmation from the Regional Director for shifting its registered office from the jurisdiction of one Registrar of Companies to the jurisdiction of another Registrar of Companies within the same State shall make an application in Form 1AD to the Regional Director alongwith a fee of Rs. 500/-.

(2) The Regional Director shall pass an order in writing confirming the change after giving necessary opportunity of being heard to the parties within four weeks from the date of receipt of application.

(3) The company shall file a copy of the confirmation order passed by the Regional Director with the concerned Registrar of Companies within two months from the date of the confirmation order and the Registrar shall make necessary changes in the register and transfer the records to the Registrar of Companies under whose jurisdiction the company has shifted its registered office."

Relevant Rules and Forms.—The application form [Form 1AD] should be filed with the Registrar of Companies from where the company proposes to shift its registered office and copy for information to the Registrar of Companies under whose jurisdiction registered office is proposed to be shifted. [*Press Release dt. 20-2-2001*].

§ For text of the Rules and Forms refer *Appendix* 1.

Printed Copies of Memorandum, as altered [Sub-section (4)]

Since no alteration in the Memorandum of association is involved as there is no alteration in shifting the registered office from one State to another, the requirement of filing printed copy of memorandum, as altered, under sub-section (4) does not arise.

Penalty for default :

The default is punishable under Section 629A in the absence of any specific penalty provided under this section.

The offence is compoundable under section 621A.

ICSI Guidance Note on Compliance Certificate [August, 2003]

Prescribed Check List

SHIFTING OF REGISTERED OFFICE FROM A PLACE UNDER THE JURISDICTION OF ONE ROC TO A PLACE UNDER THE JURISDICTION OF ANOTHER ROC WITHIN THE SAME STATE

Check whether:

(i) the company has passed a special resolution in the general meeting for shifting its registered office from a place under the jurisdiction of one ROC to a place under the jurisdiction of another ROC, within the same State;

(ii) it has made application in Form 1 AD to the Regional Director for confirmatior of special resolution;

(iii) the RD had passed the confirmation order of the resolution within four weeks from the date of receipt of the company's application;

(iv) the company has filed with the ROC, from whose jurisdiction it proposes to shift the registered office, a copy of the confirmation order of the Regional Director along with the printed copy of the memorandum as altered within 2 months from the date of confirmation by the Regional Director; and

(v) the ROC from whose jurisdiction Registered Office has been shifted, has registered the documents and certified the registration under his hand within one month from the date of filing of such documents.

S. 18. Alteration to be registered within three months.—[1][(1) A company shall file with the Registrar—

(a) a special resolution passed by a company in relation to clauses (a) to (g) of sub-section (1) of section 17, within one month from the date of such resolution; or

(b) a certified copy of the order of the [2][*Central Government*]made under sub-section (5) of that section confirming the alteration, within three months from the date of order,

as the case may be, together with a printed copy of the memorandum as altered and the Registrar shall register the same and certify the registration under his hand within one month from the date of filing of such documents.]

(2) The certificate shall be conclusive evidence that all the requirements of this Act with respect to the alteration and the confirmation thereof have been complied with, and thenceforth the memorandum as so altered shall be the memorandum of the company.

(3) Where the alteration involves a transfer of the registered office from one State to another, a certified copy of the order confirming the alteration shall be filed by the company with the Registrar of each of the States, and the Registrar of each such State shall register the same, and shall certify under his hand the registration thereof; and the Registrar of the State from which such office is transferred shall send to the Registrar of the other State all documents relating to the company registered, recorded or filed in his office.

(4) The [2][*Central Government*] may, at any time, by order, extend the time for the filing of documents [3][or for the registration of the alteration] under this section by such period as it thinks proper.

NOTES

Eng. Act, 1948 : Sec. 5(7). Previous Act : Sec. 15.

Note : As and when the Companies (Second Amendment) Act, 2002 comes into force, the powers and functions of CLB under this section shall become transferred to the Central Government to be exercised by it in place of the Company Law Board. The commentary should be read keeping this changeover in mind.

Companies (Amendment) Act, 1960

Sub-sections (1) and (4) were amended by the Companies (Amendment) Act, 1960 based on recommendations of the Companies Act Amendment Committee, 1957 so that the Registrar should be required to certify the registration of the order made under section 17(5) within one month from the date of filing the relevant documents by the company and the Court (Now CLB) be empowered to extend this period. The recommendations of the Committee are reproduced below:

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1. Subs. by the Companies (Amendment) Act, 1996 (w.e.f. 1-3-1997) for the following:
"(1) A certified copy of the order of the Company Law Board made under sub-section (5) of section 17 confirming the alteration together with a printed copy of the memorandum as altered, shall, within three months from the date of the order, be filed by the company with the Registrar who shall register the same and certify the registration under his hand within one month from the date of the filing of such documents."
2. **Subs. for "Company Law Board", by the Companies (Second Amendment) Act, 2002 (11 of 2003), s. 8. Earlier Subs. by Act 41 of 1974, s. 5 for "Court" (w.e.f. 1-2-1975).**
3. Ins. by Act 65 of 1960, s. 7.

"Under section 17(2), an alteration of the memorandum under sub-section (1) shall not take effect until and except insofar as it is confirmed by the Court on petition. Sections 18 and 19 provide for registration of the altered memorandum with the Registrar and for the consequences of a failure to register. Under section 18(1), read with sub-section (4), a copy of the altered memorandum and a copy of the Court's order confirming the alteration have to be *filed* with the Registrar within three months of the date of the order of such further time as might be granted by the Court. If the company has done this, it has done all that it is or can be required to do. Section 19(2) provides that if the registration is not effected within three months next after the date of the order of the Court confirming the alteration or within such further time as may be allowed by the Court for filing the documents under sub-section (4) of section 18, such alteration and the order of the Court confirming it shall become void. There is no period prescribed within which after the order of the Court has been filed, the Registrar should register and certify the alteration. Under section 18(4) the Court has no power to extend the time for registration." (*Report* Para 30 Pages 25, 26).

Companies (Amendment) Act, 1974

§ "Company Law Board" was substituted for "Court" by the Amendment Act XLV of 1974. As regards the reasons for this, see Notes under section 17.

Companies (Amendment) Act, 1996

Registration of Alteration.—As a result of the Companies (Amendment) Act, 1996 an alteration of objects requires under s. 17 only a special resolution and no further sanction of any authority is necessary. The sanction of CLB [*Now Central Government*] is still necessary for inter-State shifting of the registered office. The consequential change in the requirements of s. 18 is that for registering the alteration with the ROC, in the case of alteration of objects, the company would have to file a copy of its special resolution alongwith a printed copy of the altered memorandum within one month and for registering inter-State shifting of registered office, a copy of the Special Resolution together with a copy of the order of CLB [*Now Central Government*] within three months from the date of the order.

Companies (Second Amendment) Act, 2002 [11 of 2003]

The power of CLB has been conferred on the Central Government by the Companies (Second Amendment) Act, 2002 (11 of 2003). The notes on clauses of the Bill stated, thus:

Notes on clauses.—This clause seeks to amend sections 18, 19, 43, 49, 55A and 58A of the Companies Act, 1956 relating to alteration of memorandum of association to be registered within three months, effect of failure of such registration, consequences of default in complying with conditions constituting a company as private company, investments of company to be held in its own name, powers of Securities and Exchange Board of India so far as they relate to issue and transfer of securities and acceptance of deposits without issuing advertisement. It is proposed to confer the powers of the Company Law Board in the aforesaid sections upon the Tribunal. These amendments are of consequential nature. (*Clause* 8 of the Companies (Amendment) Bill, 2001)."

However as per official amendments moved at the time of passing the Bill before the Lok Sabha, the functions and powers under this section have been conferred on the Central Government.

Exclusion of time taken for obtaining copies [Sub-section (1)]

Under the provisions of section 640-A, the time taken for obtaining a copy of the order will be excluded in computing the period of time for filing it with the Registrar. See *Saroja Mills Ltd. v ROC,* (1964) 34 Com Cases 336 (Mad); *Beauty Art Dyers & Cleaners (P.) Ltd. v ROC,* (1974) 44 Com Cases 460 (Bom).

CLB Regulations, 1991 Reg. 29(4).—As per regulation 29(4) of CLB Regulations, 1991, a copy of the order shall be communicated to the petitioner-company, free of cost.

The period of 3 months under section 18 has to be calculated from the date of receipt of the certified copy of the order by the company.

Department's Clarification.—The Department of Company Affairs *vide Letter No.* 12/31/75-CL-V, dated 26-2-1977 has clarified that the date of order for the purpose of section 18 shall be the date on which the CLB [*Now Central Government*] approves and signs the formal order, and not the date of last hearing.

Effect of filing the order without accompanying documents.—The Company Law Board in *Shivalik Steels & Alloys P. Ltd., Re, (No. 2),* (1992) 73 Com Cases 194 (CLB) observed: "Form 21 is merely in the nature of a covering letter and does not provide for any additional information. Supplying a copy of the altered memorandum is again in the nature of a formality for record purposes. Thus, in effect the object contemplated under section 18(1) is served with filing of the certified copy of the order. Mere failure to file the accompanying document does not nullify the filing of the basic document. Hence, the question of seeking extension of time by the company for filing the document does not arise. But, since obligation has been cast on the Registrar under section 18(1) to register the alteration within one month and as the complete formalities have not been fulfilled he could not effect the registration within the specified time. Therefore, there is need for granting extension of time under section 18(4) to facilitate the Registrar to register the alteration."

Registration of alteration for inter-State change of registered office [Sub-s. (3)]

Department's Clarification.—The main spirit behind section 18(3) of the Companies Act, 1956 in regard to the filing of the Court's (*Now Central Government*) order confirming the transfer of the company's Registered Office from one State to another State with the Registrar of Companies of each State is that the Registrar of Companies from whose State the Registered Office is transferred should keep the Court (*Now Central Government*) order duly registered in his office as an evidence to such shifting and should transfer all other records of the company to the Registrar of Companies to whose State the Registered Office has been so shifted. The other Registrar of Companies will register the other copy of the Court (*Now Central Government*) order and keep that order with the records transferred to him by his counterpart. (*Circular No.* 2/75 *F. No.* 26/1/75 CL-III).

No time limit prescribed under sub-section (3)—Department's Clarification.—A question has been raised about the applicability of sections 18 and 637B of the Companies Act, 1956 to a case where there has been delay on the part of a company in filing copy of the CLB (*Now Central Government*) order under s. 17 in respect of shifting of the registered office of the company from one State to another. The above matter has since been examined very carefully. The department is of the view that an order by the CLB (*Now Central Government*) under s. 17(1) relating to the shifting of the registered office from one State to another comes under s. 18(3) and will, therefore, be governed by the procedure prescribed thereunder. In other words, sub-section (3) of section 18 is an independent sub-section and will cover only cases which relate to the transfer of the registered office from one State to another State. Such cases will, therefore, not be covered by the provisions of sections 18(1) and 18(4). Since no time limit has been prescribed under s. 18(3), the provision of s. 637B(*b*) will also not apply to such cases. In terms of the above view, a company will continue to remain on the register of the ROC of the State from which it is proposed to shift and also in respect of which it has got an order of CLB under s. 17(1) till it files the aforesaid order with him and the ROC certifies under his hands about such transfer. [*Department's Letter No.* 6616/31/4/78-CL-V, dated 17-4-1978].

Extension of time for registration [Sub-section (4)]

The Company Law Board has been given the power under sub-section (4) to extend the time for filing and registration of the documents by such period as it thinks proper. The Punjab High Court has explained in *Shiv Prakash Janakraj & Co. Pvt. Ltd. v. ROC,* (1963) 2 Comp LJ 228 (Punj) the kind of prayer which has to be made under this sub-section. The court said that an application under this sub-section should pray: (1) that the delay in filing the certified copy of the order may please be condoned and the documents already filed may please be ordered to be taken on record (2) that the alteration of the memorandum as sanctioned may please be ordered to be registered by the registrar (3) that the court may pass any other order that it considers necessary.

A company shifted office from Karnataka to Delhi. The order of the Company Law Board was filed before the Registrar of Companies, Karnataka within the prescribed time.

There was delay of one month and 18 days in filing the order in the office of the Registrar of Companies at Delhi. The court held that there was sufficient compliance and, therefore, time for complying with the remaining formality was to be extended. *Ishita Properties Ltd. Re,* (2002) 112 Com Cases 547 : (2002) 4 Comp LJ 476 (CLB—Southern).

§ For interpretation of the scope of sub-section (4) of this section and sub-section (2) proviso of section 19, see Notes under section 19.

Application before CLB for extension of time.—The application under sub-section (4) for extension of time for filing documents for registration of alteration is to be made in Form No. 1 of Annexure-II to the CLB Regulations, 1991 before the Regional Bench of the Company Law Board, accompanied by the following documents and a fee of Rs.100/- :

(1) Application supported by affidavit

(2) Bank draft evidencing payment of application fee.

§ For the text of the CLB Regulations, 1991 refer *Appendix* 3.

Appeal against orders of CLB

Section 10F provides for appeal against the orders of the Company Law Board. The power of the CLB has been vested in the Central Government by the Companies (Second Amendment) Act, 2002 (11 of 2003) (w.e.f. enforcement date). There is no provision for an appeal against Central Government's decisions. It would seem, therefore, that the remedy would be by way of a writ to the High Court under Articles 226 & 227 and Supreme Court under Articles 32.

Prescribed Form

The order of the Company Law Board shall be filed with the Registrar along with Form No. 21 given in *Appendix* 1.

Secretarial Practice Notes : Alteration to be registered within three months

§ See Secretarial Practice Notes and Action Points under Section 17.

S. 19. Effect of failure to register.—(1) No such alteration as is referred to in section 17 shall have any effect until it has been duly registered in accordance with the provisions of section 18.

[1][(2) If the documents required to be filed with the Registrar under section 18 are not filed within the time allowed under that section, such alteration and the order of the [2][*Central Government*] made under sub-section (5) of section 17 and all proceedings connected therewith, shall, at the expiry of such period, become void and inoperative :

Provided that the [2][*Central Government*] may, on sufficient cause shown, revive the order on application[3] made within a further period of one month.]

[4]Note— Nothing contained in sub-section (1) shall apply to any proceedings under section 17, or under sub-section (4) of section 18, which is pending at the commencement of the Companies (Amendment) Act, 1974, before any Court or to any alteration of the memorandum of a company which has been confirmed, before such commencement, by any court.

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1. Subs. by Act 65 of 1960, s. 8.
2. **Subs. for "Company Law Board", by the Companies (Second Amendment) Act, 2002 (11 of 2003), s. 8. Earlier Subs. by Act 41 of 1974, s. 5 for "Court" (w.e.f. 1-2-1975).**
3. Application fee Rs. 100/- under the Company Law Board (Fees on Application & Petitions) Rules, 1991. For the text, see *Appendix* 6.
4. Added by s. 5(2) of the Amendment Act (XLI of 1974).

NOTES

Note : As and when the Companies (Second Amendment) Act, 2002 comes into force, the power under this section shall become transferred to the Central Government to be exercised by it in place of the Company Law Board. The commentary should be read keeping this change in mind.

Previous Act : Section 16.

Companies (Amendment) Act, 1960

Sub-section (2) was amended by the Companies (Amendment) Act, 1960 and the changes are only clarificatory.

Companies (Amendment) Act, 1974

The powers of the court were conferred on the CLB by the Companies (Amendment) Act, 1974 w.e.f. 1-2-1975.

§ See Notes under section 17 also.

Companies (Second Amendment) Act, 2002 [11 of 2003]

Powers transferred to Central Government.—Consequential changes have been made in this section as the power of the CLB will be exercised by the Central Government after the effective date of the amendment. Notes on clauses of the Bill is reproduced hereunder:

Notes on Clauses.—This clause seeks to amend sections 18, 19, 43, 49, 55A and 58A of the Companies Act, 1956 relating to alteration of memorandum of association to be registered within three months, effect of failure of such registration, consequences of default in complying with conditions constituting a company as private company, investments of company to be held in its own name, powers of Securities and Exchange Board of India so far as they relate to issue and transfer of securities and acceptance of deposits without issuing advertisement. It is proposed to confer the powers of the Company Law Board in the aforesaid sections upon the Tribunal. These amendments are of consequential nature. (*Clause* 8 of the Companies (Amendment) Bill, 2001).

Time for filing order and extension thereof

As per section 18, the company shall file with ROC :

(1) a copy of the special resolution in relation to alteration of object clause within one month; or

(2) a certified copy of the order of CLB for shifting the registered office from one State to another, within three months from the date of the order.

If extension of time for filing of the documents is to be sought, then the Company Law Board must be moved within one month or three months, as the case may be, before the special resolution or the order becomes void and inoperative. Once it is so moved within the period of limitation, it may "at any time", by order, extend the time for the filing of documents. If this has not been done, then on sufficient cause being shown, the Company Law Board may revive the order, if the application has been made within a month. The period of one month in this case commenced from the date of the order becoming void and inoperative. This is 'a further period' which is added to the three months allowed under section 18 sub-section (1). *National Industrial Corporation Ltd. v. ROC, Punjab,* (1963) 33 Com Cases 265 (Punj).

Section 18(4) only means that if at any time before the order becomes void and inoperative, application is made for extension of time, the Company Law Board may, by order, extend the time. The Company Law Board can extend the time only so long as the order is alive *i.e.*, before it becomes void and inoperative. See also *Janardhana Mills Ltd. v. ROC,* (1964) 34 Com Cases 333 (Mad). Where extension of time for filing of documents was sought after sixty days after the expiry of 30 days from the date of the special resolution, it was held that the resolution had become void and there was no question of

granting extension of time. *Ganga Textiles Ltd. v. ROC,* (1998) 94 Com Cases 36 : (1998) 3 Comp LJ 103 : (1998) 16 SCL 677 : (1998) 29 CLA 467 (CLB—SB). But in the case of *Project Engineering (P.) Ltd. v. ROC,* (1967) 37 Com Cases 566 (Mad), it has been held that the application under the proviso to sub-section (2) can be made even after the expiry of the period of three months, *i.e.*, after the order becomes void. To the same effect *Webfil Ltd., Re,* (1990) 4 Corpt LA 264 (CLB).

The scope of the provisions of sections 18 and 19(2) read together is this: Under section 18, extension or extensions of time may be granted for filing and registration. If the filing is not done within the time originally allowed or where application for extension is made and granted, within the extended time so granted, then the proceedings become void. If even after the order becomes void, application is made within one month from the date of its becoming void, showing sufficient cause, the order may be revived. In *Shivalik Steels and Alloys Ltd., Re,* (1992) 73 Com Cases 194 (CLB) an application for extension of time was made five months after the date of the order and the same was rejected. Where, however, the order of the CLB was filed within the time but it was not accompanied with the altered memorandum and the requisite fee, it was held that the section was substantially complied with and the company could be allowed even out of time to fulfil the rest of the formalities. The Registrar was directed to intiate proceedings against the company against unauthorised shifting because the company had shifted its office even before the alteration was registered. *Shivalik Steels and Alloys Ltd., Re, (No. 2),* (1992) 73 Com Cases 174 (CLB).

Revival of CLB's order

It has been held by the Punjab High Court in *Shiv Parkash Janakraj & Co. (P.) Ltd. v. ROC,* (1963) 2 Comp LJ 228 (Punj) that once the three month period prescribed by s. 18 has run out, the whole proceedings of alteration and order of confirmation become void and inoperative. The only course now open to the company is to apply to the CLB under s. 19(2) for revival of the order. The CLB accordingly refused to entertain the petition of the company under s. 18 and advised them to proceed under s. 19(2).

In case, the application for revival of order made under section 17 is not filed within the period prescribed under this section, the order passed by the CLB becomes *non est*, and the only remedy available to the company is to initiate *de-novo* proceedings under section 17.

Department's Clarification.—"Cases have come to the notice of Government where, even when the companies failed to apply to the Court within a period of three months for extension of time to file the order or within a further period of one month for revival of the order, Courts have passed orders granting applicant companies extension of time to file copies of the orders with the Registrars. Such orders of extension are not in conformity with the law and whenever the Registrars get an opportunity they should bring the above position of law to the notice of the Court". [*Circular No.* 20(26)-CL-IV/61, dated 31-7-1961].

Extension of time for obtaining copy of order

In calculating the time, the time taken for obtaining a copy of the order will have to be excluded (section 640-A). See *Saroja Mills Ltd. v. ROC,* (1964) 34 Com Cases 336 (Mad); *Shri Amba Motor Agencies (P.) Ltd. v. ROC,* (1978) 48 Com Cases 89 (Delhi). (Advocate misplacing certified copy of the order, held to be sufficient cause for condonation of delay).

Application before CLB

The application for revival of order under section 19 can be made in Form No. 1 of Annexure-II to the CLB Regulations, 1991 before the Regional Bench of CLB [*Now Central Government*] along with an application fee of Rs. 100/-and the following documents:

(1) Application duly supported by affidavit,

(2) Bank draft evidencing payment of application fee.

§ For the text of CLB Regulations, 1991 refer *Appendix* 3.

Appeal against orders of CLB

See Notes under Sec. 18 under the same heading.

Central Government's power under Section 637-B to condone delay in filing

The Central Government is empowered under S. 637B(*b*) to condone delay in filing any document with the Registrar. In view of the express provisions made in sections 18(4) and 19, the delay in filing the order of Company Law Board beyond the permissible time limit cannot be condoned by the Central Government.

Secretarial Practice Notes : Effect of failure to register

§ See Secretarial Practice Notes and Action Points under section 17.

Provisions with Respect to Names of Companies

S. 20. Companies not to be registered with undesirable names[1].—(1) No company shall be registered by a name which, in the opinion of the Central Government, is undesirable.

[2][*(2) without prejudice to the generality of the foregoing power, a name which is identical with, or too nearly resembles,—*

(i) the name by which a company in existence has been previously registered, or

(ii) a registered trade mark, or a trade mark which is subject of an application for registration, of any other person under the Trade Marks Act, 1999;

may be deemed to be undesirable by the Central Government within the meaning of sub-section (1).

(3) The Central Government may, before deeming a name as undesirable under clause (ii) of sub-section (2), consult the Registrar of Trade Marks.]

NOTES

Eng. Act, 1948 : Sec. 17. Previous Act : Sec. 11(1)(3).

Changes made by the Trade Marks Act, 1999

Section 20(2) has been amended by Section 158 of the Trade Marks Act, 1999 to provide that a name which is identical with, or too nearly resembles, the registered trade mark or trade mark which is the subject matter of an application pending for registration, may be deemed to be undesirable. The newly inserted sub-section (3) by the same Act also provides that before deeming a name undesirable, the Central Government (power delegated to Registrars) may consult the Registrar of Trade Marks, in this behalf.

It may be noted that the *Circular No.* 10(1)-RS/65 dated 27-11-1965 issued by the Department of Company Affairs in regard to guidelines for deciding cases for availability of names by ROCs (reproduced in the Notes under the Section), item No. 17 provides *inter-alia* that if the proposed name of a company includes the name of registered trade mark,

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1. Necessary applications may be made in Form 1A of the Co's. (Central Govt's.) General Rules & Forms, 1956 accompanied by a Fee of Rs. 500/- *vide* R. 4A(1) of the Rules.
2. Sub-section (2) substituted and sub-section (3) inserted by Trade Marks Act, 1999, prior to the substitution of sub-section (2), it read :

"(2) Without prejudice to the generality of the foregoing power, a name which is identical with, or too nearly resembles, the name by which a company in existence has been previously registered, may be deemed to be undesirable by the Central Government within the meaning of sub-section (1)".

such a name should not be made available, unless the consent of the owner of the trade mark has been produced by promoters.

In view of the changes made in this section, statutory protection has now been given to the trade marks, whether already registered or pending registration under the Trade Marks Act, 1999 in the matter of availability of names.

The Registrar of Companies will now be required to keep record of registered trade marks and trade marks in respect of which applications for registration are under consideration of the Registrar of Trade Marks, to ensure that the name of a proposed company or the proposed change of the name of an existing company is not identical with or too nearly resembling any trade mark.

Sub-section (3), as worded, provides that the Central Government (power delegated to Registrar of Companies) may consult the Registrar of Trade Marks before deeming a name as undesirable.

Objects and name of company

The name of a company may be relevant in construing its memorandum and to see what its main object is and whether its substratum is gone. *Cotman v. Brougham,* (1918) AC 514 (HL). In this context, it may be pointed out that one of the guidelines relating to availability of name lays down that if the proposed name of a company is not in consonance with its principal objects as set out in the memorandum, the name may not be made available, particularly when there is some indication of business in the name itself. If consequent upon alteration of its objects, the name of the company becomes misleading, a condition may be imposed that the name should also be changed so as to convey the enlarged field of operation by virtue of the alteration. *In re, Indian Iron & Steel Co. Ltd.,* (1957) 27 Com Cases 361 (Cal). This principle is reflected in the guidelines relating to the availability of name. The Central Government may not make a name available if it includes the word "Industries" or "business" unless the name is indicative of the business of the proposed company; for otherwise it serves as a lever for the company to enlarge its activities.

The section is aimed at only the company's name and not at any other manner in which the public could be misled. In applying the provisions what has to be determined is whether the company's name is so misleading that it is likely to cause harm to the public. It is not sufficient to show that the name is misleading, a likelihood of harm must also be shown. The statutory question does not require that instances of anyone actually having been misled by the name must be shown. The presence or absence of such instances is a matter to be taken into account in deciding whether a name is misleading. It is also not necessary to consider any particular section of the public who might be misled. Applying these principles, the name "The Association of Certified Public Accountants of Great Britain"was held to be not allowable. JACOB J in *Association of Certified Public Accountants of Britain v. Secretary of State for Trade and Industry*, (1997) 2 BCLC 307 : (1998) 1 WLR 164 (Ch. D.) explained the reasons as follows : [at p. 315]. "Does the name of the Association, 'The Association of Certified Public Accountants of Great Britain', give a misleading indication of the nature of its activities? I have come to the conclusion that it does. I think the word 'certified' indicates, or is likely to indicate, to a substantial number of persons, that there is something objectively significant about the members' qualification, training and experience. I do not see why 'certified' should have the same meaning for all organisations. But there must be enough of substance—the word implies something of substance. Only professional indemnity insurance, and three years' experience is less than one would reasonably expect from an association with its present name. Next I must consider whether the name is likely to cause harm to the public. I think it is. People go to accountants expecting not only probity but a level of expertise. I think if you went to someone calling themselves a 'Certified Public Accountant' you would expect more by way of formal professional qualification than just professional indemnity insurance and some experience. And you would be willing to pay more ac-

cordingly. So the misleading name is likely to cost the public money. That is harm, irrespective of other forms of potential harm which might also occur."

Injunction against use of similar name and passing off action

Intention to deceive not necessary.—The section does not affect the jurisdiction of the Court under the general law to restrain the registration of a company under a name so similar to that of the plaintiff as to be calculated to deceive, though the defendant may not have the intention to deceive. The jurisdiction of the court in such cases rests on the position that the use of a name closely resembling a name under which another is carrying on his business is calculated to deceive or cause confusion between the two businesses and results in causing injury to the other person by diverting his customers and affecting his credit or goodwill. See *Ewing v. Buttercup Margarine Co. Ltd.,* (1917) 2 Ch 1 where the plaintiff, who carried on business under the trade name of the Buttercup Dairy Company, was held entitled to restrain a newly registered company from carrying on business under the name of the Buttercup Margarine Company Ltd. on the ground that the public might reasonably think that the registered company was connected with his business. See also *Montreal Lithographing Co. v. Sabiston,* (1899) AC 610; *Maxim's Ltd. v. Dye,* (1978) 2 All ER 55; *Warnink v. Townsend & Sons (Hull),* (1979) 3 WLR 68; *Cadbury-Schweppes Pty. Ltd. v. Pub Squash Co. Pty. Ltd.,* (1981) 1 All ER 213; *Porzelack K.G. v. Porzelack (U.K.) Ltd.,* (1987) 1 WLR 420; *Ad-Lib Club Ltd. v. Granville,* (1971) 2 All ER 300.

Where a company attempts to get registered, or is registered by a name so similar to that of any other company, firm or individual, as to be likely to deceive or cause confusion, the aggrieved party may file a suit for injunction or other appropriate relief. The remedy by application to the Central Government does not exclude such civil remedy. See *British Bata Shoe Co. Ltd. v. Czechoslovakia Bata Co. Ltd.,* (1946) 64 RPC 72; *Sturtevant Engineering Co. Ltd. v. Sturtevant Mill Co. of U.S.A. Ltd.,* (1936) 3 All ER 137. In *Hendriks v. Montagu,* (1881) 17 Ch D 638, the Universal Life Assurance Society (which was not incorporated) obtained an injunction to prevent Montagu and his associates registering a company with the name Universe Life Assurance Association Ltd. It is not necessary to prove that the deception was intended (*British Diabetic Association v. Diabetic Society Ltd.,* (1995) 4 All ER 812). In such cases the Courts act either on the ground that a fraud is likely to be practised or that some other party has acquired a property in the name and that the use of a name similar to the one in which another party carries on business is calculated to deceive or cause confusion between the two businesses and is likely to affect the other man's property by diverting the customers, and the credit and goodwill of the other man's business.

It is not necessary to prove either that there is fraud, or a deliberate intention to confuse, or that the public has been misled. It will be sufficient to show that the name with which a company proposes to be registered is "calculated" to mislead, the word "calculated" has not been used to import intention but to show a certain effect with something more than moral certainty of deception. *Per* JAMES LJ in *Hendriks v. Montagu,* (*Supra* at 465, 646) (CA); *North Cheshire and Manchester Brewery Co. v. Manchester Brewery Co.* (*Supra*).

Proprietory right and Monopoly.—But mere similarity of name is not in itself enough to give a right to an injunction or other remedy as there is no right of property in a name. As pointed out in *D. W. Boulay v. D. W. Boulay,* (1868) LR 2 (PC) the law does not recognise the absolute right of a person to a particular name to the extent of entitling him to prevent the use of the name by another person. In the case of companies, however, registration will be refused if there is likelihood of deception or confusion. This principle extends also to the use of names of partnership firms and individuals, where the name forms part of the goodwill of an existing business. This right is independent of the provisions of this section which relates only to companies. A person cannot be permitted to name a company even after his personal name if that name resembles the name of an existing company. *K.G. Khosla Compressors Ltd. v. Khosla Extraktions Ltd.,* AIR 1986 Del

151. See also *Fine Cotton Spinners and Doublers Assn. Ltd. v. Harwood Cash & Co. Ltd.*, (1907) 2 Ch 184 : 24 RPC 533; *Prakash Roadlines Ltd. v. Prakash Parcel Service (P.) Ltd.*, (1A Nos. 14319/91 and 14690 of 1991 in Suit No. 3007 of 1991), (Delhi) **(Unreported)** as to use of the word 'Prakash' by two transport companies.

Under Company Law, a company by registering its name gains a monopoly of the use of that name. Even if the company is not registered, the court will restrain the registration under the Act of a projected new company which was intended to carry on the same business as the unregistered company and to bear a name so similar to its name as to be calculated to deceive the public. *K.M. Multani v. Paramount Talkies of India Ltd.*, (1943) 13 Com Cases 90, 94 (Bom). The court should be satisfied that the name in which the company seeks to register itself is "likely to mislead" or is "calculated to deceive" irrespective of the intention of the promoters. *National Bank of India Ltd. v. National Bank of Indore*, AIR 1923 Bom 110. The 'Indian National Congress' which was a registered society under this name for certain purposes was allowed to restrain the registration of a company under the same name and for similar purposes. *U. Srinivas Malliah v. Krishna Kumar Chaterjee*, AIR 1952 Cal 804.

A company, on discovering, that another company has been or is about to be registered under the same name as itself may have a common law right to restrain the newcomer from the use of that name. It will certainly have the right if the name has been used with the intention of misleading third parties, or for some fraudulent purpose. *Turton v. Turton*, (1889) 42 Ch D 128; *Reddaway v. Banham*, (1896) AC 199. The original company can show that confusion has existed, or that persons have dealt with the second company believing it to be the old one; in that respect, the sound as well as the spelling of the name is material. *Ouvah Ceylon Estates v. Uva Ceylon Rubber Estates*, (1910) 27 TLR 24.

Passing Off.—To counter passing off by a company that has already been registered, an injunction may be obtained requiring the company's controllers not to allow the company to continue to be registered with a deceptive name, so that they must either change the company's name or dissolve it (*La Societe Anonyme des Anciens Etablissements Panhard et Levassor v. Panhard Levassor Motor Co. Ltd.*, (1901) 2 Ch 513. The court will even prevent the use of the name of a world-wide organisation. *Sheraton Corpn. of America v. Sheraton Motels Ltd., The Times*, July 13, 1963. The basis of the action for passing off is a proprietary right not so much in the name itself but in the goodwill established through the use of the name in connection with the plaintiff's business.

The reason for the rule was explained in *Society of Motor Manufacturers and Traders Ltd. v. Motor Manufacturers and Traders Mutual Insurance Co. Ltd.*, (1925) 1 Ch 675 by LAWRENCE J. "Under the Companies Act, a company by registering its name gains a monopoly of the use of that name since no other company can be registered under a name identical with it or so nearly resembling it as to be calculated to deceive" at page 686. The name of a company is a part of its business reputation and that would definitely be injured if a new company could adopt an allied name. In this case, the plaintiff society was incorporated in 1902 under the name: The Society of Motor Manufacturers and Traders Ltd. In the year 1924 the defendant society was incorporated under the name: Motor Manufacturers and Traders Mutual Insurance Ltd. The plaintiff company brought an action to restrain the use of this name. It was held that the defendant company's name could not be regarded as one "calculated to deceive". "Anyone who took the trouble to think about the matter would see that the defendant company was an insurance company and that the plaintiff society was a trade protection society and I [LAWRENCE J.] do not think that the defendant company is liable to have its business stopped unless it changes its name simply because a thoughtless person might unwarrantedly jump to the conclusion that it is connected with the plaintiff society."

The common law remedies of restraining the use of a company's name for passing off and deceptive purposes, and recovering compensation for loss and seeking an account of the benefits obtained, are available to a company whose name has been misused. Such remedies do not become suspended because of the special provisions in sections 20 and

22 of the Companies Act. The remedies available in the law of tort for unauthorised use of business name and under intellectual property laws for unauthorised use of trade marks etc. and the safeguards provided in the Companies Act, they all operate in different fields. *Montari Overseas Ltd. v. Montari Industries Ltd.*, (1996) 20 Corpt LA 313 (Delhi). The action of passing off does not become excluded when a new company is formed and incorporated with a name which is deceptively similar to the name of the existing company. *Montari Industries Ltd. v. Montari Overseas Ltd.*, (1995) 18 Corpt LA 58 (Del).

The fact that the word in a company's name which causes the confusion with another business is the name of one of the company's shareholders is no defence to a passing-off action: a company does not have a right to trade under the name of one of its shareholders if to do so would damage another's business (*M.P. Guimaraens and Son v. Fonseca and Vasconcellos Ltd.*, (1921) 38 RPC 388). However, if the company's business is or will be different from that of the complaining party, confusion is not likely to arise, and an injunction will not be granted. *Dunlop Pneumatic Tyre Co. Ltd. v. Dunlop Motor Co. Ltd.*, 1907 SC (HL) 15, where the respondents carried on a motor-repairing company; similarly an interdict was refused in *The Scottish Union and National Insurance Co. v. The Scottish National Insurance Co. Ltd.*, 1909 SC 318 (Scot.).

'Trade' is interpreted widely, so as to include professional and artistic work and activities of pressure group such as the 'Countryside Alliance'. *Burge v. Haycock*, (2001) LTL Dt. 31-5-2001. It is only business reputation and goodwill that can be protected by an action for passing off, and not the reputation like that of a political party. *Kean v. McGivan* [1982] FSR 119. Also the business must be carried on within the jurisdiction of the court in which proceedings are taken. *Harrods Ltd. v. Harrods (Buenos Aires) Ltd.* [1997] FSR 420. If traders have similar business names but no common field of activity then there is no passing off. *Wombles Ltd. v. Wombles Skips Ltd* [1977] RPC 99.

Use of the name of a company to mark goods so that people may believe they are the goods of another trader is a form of passing off which is regarded particularly serious by the courts. An honest mistake is no defence. *Baume and Co. Ltd. v. A.H. Moore Ltd* [1958] RPC 226, in which the defendant company was prohibited from continuing to import watches made by a Swiss company. Baume & Mercier SA, marked 'Baume & Mercier'. The public might confuse them with the 'Baume' watches which the plaintiff company had sold for about 80 years; *Parker-Knoll Ltd. v. Knoll International Ltd* [1962] RPC 243.

A recent development is the use of the law of passing off to counter people who register companies with names which existing traders or famous people might want to use as trading names in the future and who are then asked to buy the companies for a large sum. This has been described as an abuse of the registration process and a mandatory injunction will be issued in such a case to require the company to change its name. *Glaxo plc v. Glaxowellcome Ltd.*, (1996) FSR 388; *Direct Line Group Ltd. v. Direct Line Estate Agency Ltd.* (1997) FSR 374.

Company Names.—The position and practice as to injunctions is thus stated in KERLY'S – TRADE MARKS AND TRADE NAMES, p. 503 (13th Edn., 2001) : "Most recent authorities on trading names concern the names of limited companies rather than of individuals or of partnerships. The relief claimed in such cases may well include an injunction that will require the defendant to take steps to change its name. Citing *Manchester Brewery v.North Cheshire*, (1899) AC 83. *Hendriks v. Montagu*, (1881) 17 Ch.D. 638 for one form of injunction. Non-profit making companies stand in the same position as trading companies in this respect : *Lagos Chamber of Commerce v. Registrar of Companies*, (1955) 72 RPC 263, PC.

Where an injunction is granted against a limited company carrying on business under its registered name, the injunction is usually suspended for a short time to allow the company to change its name. *Lloyd's v. Lloyd's (Southamption)*, (1912) 29 RPC 433; *Midland Countries Dairy v. Midland Dairies*, (1948) 65 RPC 429; *Letters v. Letters (Craigton)*, (1967) RPC 209 (Scots)."

Use of Corporate name for Joint Venture Company.—Where a corporate partner to a joint venture allowed the company's name to be used by the joint venture company, it was held that permission stood impliedly withdrawn when the joint venture company left the corporate group and, therefore, the continued use of that name might constitute passing off—*Dawnay Day and Co. Ltd. v. Cantor Fitzgerald International, The Times* July 14, 1999 (CA). [PALMER IN COMPANY, September, 1999].

A joint venture agreement had a clause to the effect that if at any time the equity participation of the foreign collaborator fell below 40%, the company would stop using the foreign company's trade name. This clause was not incorprated in the company's articles, even so it was held that the foreign company on disposing off its whole equity, was entitled to call upon the Indian participator, to change its name. A temporary mandatory injunction was granted to prevent passing off . *Banker Hughes Ltd. v. Hiroo Khushalani,* (2000) 102 Com Cases 203 (Del).

In *Teju Singh v. Shanta Devi,* AIR 1974 AP 274, the court declined to grant injunction against the defendant carrying on business in the name of "Only 1 day Electric Dry-cleaners" on the application of plaintiff who was also carrying on the business of dry-cleaners in the name of "One Day Electric Dry-cleaners", on the ground that the sign boards were totally different in their design and the names were only of a descriptive nature and not distinctive so as to sustain the passing off action.

Use of family or surname.—The Kriloskar group of companies wanted to prevent a company from using the word "Kriloskar" as a part of its name because it would amount to passing off to the market the products of the Kriloskar group of companies and also to enjoy the benefit of goodwill created by that group. The court did not issue a temporary stay order. There is a right to use in a *bona fide* manner one's own name or the name of a place or ancestral name. *Kriloskar Proprietary Ltd. v. Kriloskar Dimensions P. Ltd.,* (1999) 96 Com Cases 726. A group of companies belonging to the same family was known as "Manipal Group of Companies". Owing to a family dispute the company became divided into two groups and the business also became divided into two branches. The name "Manipal" was associated with the family and not with any particular company or goods. All the companies were not carrying the word "Manipal" as part of name. Hence, neither group could be injuncted from using the word "Manipal" as part of company name. *Manipal Housing Finance Syndicate Ltd. v. Manipal Stock and Share Brokers Ltd.,* (1999) 98 Com Cases 432 (Mad). In *Tussaud v. Tussaud,* (1890) 44 Ch. D 678, the company that owned Madame Tussaud's Waxworks was granted an injunction to prevent a member of the Tussaud family from registering a company called 'Louis Tussaud Ltd. for carrying on a similar waxworks show.

Word in ordinary use.—A company having a word in ordinary use as part of its name cannot prevent another company from using the same word. So, Aerators Ltd. were unable to prevent the registration of Automatic Aerators Patents Ltd. because the word "aerator" was a word in common use in the English language and Aerators Ltd. had no monopoly of it: *Aerators Ltd. v. Tollitt,* (1902) 2 Ch 319. In some cases the court may make the restraint purely local, and if the locality of operation or intended operation, or if the type of business is such that there is no real danger of confusion, the court will not grant an injunction. *Lee v. Haley,* LR 5 Ch 155.

Invented Name.—A company has no copyright in any of the words forming part of its name, even if one of those words was invented as a result of research and labour being expended in the invention. However, the use of such a word by a company in its name would be restrained by an injunction if the effect of using the word is to give a misleading impression that the company using it subsequently is connected with the company which first used it. *Re, Exxon Corporation v. Exxon Insurance Consultants International Ltd.,* (1981) 2 All ER 495 (Ch D) **affirmed** in (1981) 3 All ER 241 (CA). See also *La Societe Anonyme Des Anciens Establishments Panhard et Levassor v. Panhard Levassor Motor Co. Ltd.,* (1901) 2 Ch 513; *Ewing v. Buttercup Margarine Co. Ltd.,* (1917) 2 Ch 1 (CA); *Waring & Gillow Ltd. v. Gillow and Gillow Ltd.,* (1916) 32 TLR 389 (injunction refused); *Asiatic Govt. Security Life*

Assurance Co. Ltd., case, (1939) 9 Com Cases 208 (Mad) (Injunction refused). But where a company has carried on business under a particular name for a considerable time, it cannot be objected to. *Jay's Ltd. v. Jacobi,* (1933) 1 Ch 411.

In BUCKLEY ON THE COMPANIES ACTS, 13th Edn. it is stated at p. 48: "The jurisdiction in these cases rests either upon fraud or upon property; not that there is property in the name, but that the use of a name closely resembling that in which another carries on business is calculated to deceive or cause confusion between the two businesses and to affect property by diverting customers to the person taking the name or by affecting the credit or goodwill of the person whose name is taken. Where this is not the case there is no jurisdiction." This passage was cited with **approval** in *Bhandari Homeopathic Laboratories v. L.R. Bhandari (Homeopaths) (P.) Ltd.,* 1976 Tax LR 1382 (Del). See also *Executive Board of Methodist Church in India v. Union of India,* (1985) 57 Com Cases 443 (Bom) and *K.G. Khosla Compressors Ltd. v. Khosla Extraktions Ltd.,* AIR 1986 Del 181.

HALSBURY'S LAWS OF ENGLAND (4th Edition) deals with the above topic in Vol. 7 at paras 128 to 134 : Vol. 7(1), 4th Edn., 1996 Reissue, paras 154 to 165, and it is also dealt with in ENGLISH & EMPIRE DIGEST, Vol. XI, pages 48 to 61 paras 180 to 253. To illustrate, a few cases on this topic are:

(a) *'Daimler Motor Co. (1904) Ltd. v. London Daimler Co. Ltd.,* (1907) 24 RPC 379 (CA).

(b) Sheraton Hotels and Sheraton Motels resemble each other. *Sheraton Corporation of America v. Sheraton Motels Ltd.,* (1964) RPC 202.

(c) "Suhner & Co." and "Suhner Ltd." resemble each other. *Suhner & Co. A.G. v. Suhners Ltd.,* (1967) RPC 336.

(d) In *Dunlop Pneumatic Tyre Co. Ltd. v. Dunlop Motor Co.,* (1907) AC 430, it was held that there was no proof that anyone would be misled into thinking that the two companies were the same, and that the pursuers had no right to exclusive use of the name of *'Dunlop'*. .

Field of business activity.—Two important factors to be taken in view in naming a company are: the nature of the name, and the type of the business. If the type of the business is the same and the name similar to an existing company, an objection will naturally arise since it is likely to mislead the public. *Aerators Co. v. Tollik,* (1902) 2 Ch 319; *Lloyds Bank v. Lloyds Investment Co.,* (1912) 28 TLR 379.

Names which can or cannot co-exist

The following names have been allowed to co-exist: *London and Provincial Law Assurance Society* with *London and Provincial Joint Stock Life Assurance Company,* (1848) 17 LJ Ch 37; *London Assurance Corporation* with *London and Westminster Assurance Corporation,* (1863) 32 LJ Ch 664; *Colonial Life Assurance Co.* with *Home and Colonila Assurance Co.,* (1864) 33 Beav 548; *Merchant Banking Company of London* with *Merchants' Joint Stock Bank,* (1878) 9 Ch D 567. But the Manchester Brewery Co. obtained an injunction against the North Cheshire and Manchester Brewery Co. on the ground that the latter might be considered to have absorbed the former, (1899) AC 83. The question is in each case one of fact, *i.e.* whether confusion has arisen or will arise. But a company cannot appropriate a descriptive word or title so as to obtain a monopoly of it, *Aerators Ltd. v. Tollit,* (1902) 2 Ch 319, where it was held that the plaintiff company could not prevent the registration of Automatic Aerators Patent Co. The Electromobile Co. also failed to restrain the British Electromobile Co. from trading in that name: (1908) 98 LT 258; and the Trade Extension Co. failed against the Expansion of Trade : (1909) 54 SJ 101; even when the word is a word whose use was first adopted by the complaining company, *British Vacuum Cleaner Co. v. New Vacuum Cleaner Co.,* (1907) 2 Ch 312. In this case the plaintiff company was forming subsidiary companies using the words 'Vacuum Cleaner', which was another ground for refusing relief. See also *Electromobile Co. v. British Electromobile Co.,* (1908) 98 LT 258." GORE BROWN ON COMPANIES, 227 (44th

Edn. by BOYLE & SYKES Vol. I, 1987). The Registrar may himself refuse to register a company in such a case. *R. v. Registrar of Companies,* (1912) 3 KB 23.

§ For a detailed study on the subject of Trade Marks and Passing-Off refer.

(1) DR. VENKATESWARAN-LAW OF TRADE MARKS AND PASSING-OFF, 4th Edition.

(2) KERLY-LAW OF TRADE MARKS AND TRADE NAMES, 13th Edn., 2001.

(3) KAILASAN AND VEDARAMAN – LAW OF TRADE MARKS & GEOGRAPHICAL INDICATIONS, Edn., 2003.

Conversion of Private into Public Company, *vice versa* and unlimited into Limited Co.

If a private company converts itself into a public company or public company into a private company there will be a change of its name as the word " private" has to be omitted from or added to its name, as the case may require. So also the conversion of an unlimited company, into a limited company, as the word " limited" has to be added at the end. But this change will not require Central Government's approval under section 21.

Fraudulent intention is not necessary

It is not necessary to prove any fraudulent intention on the part of the defendants; it is sufficient if the name adopted by them will be likely to mislead. *British Vacuum Cleaner Co. v. New Vacuum Cleaner Co.,* (1907) 2 Ch 312; *North Cheshire & Manchester Brewery Co. v. Manchester Brewery Co.,* (1899) AC 83.

Dissolved or amalgamated company

The prohibition against similarity of names does not apply where an existing company is in the course of being dissolved and testifies its consent to the satisfaction of the Registrar. This power is frequently exercised in the U.K. especially in cases of reconstruction or amalgamation. PALMER'S COMPANY PRECEDENTS, 261 (17th Edn., Vol. I).

Availability of names

As the section provides that no company shall be registered by a name which, in the opinion of the Central Government, is undesirable and that a name identical with or closely resembling the name of an existing company is not to be permitted, the Department of Company Affairs has provided for ascertaining by making of an application beforehand whether a proposed name is acceptable for registration.

Department's guidelines for deciding cases for availability of names*

Superseding all previous Circulars and Instructions (*Circular Letter No.* 10(1)—RS/60, dated 1-4-1960 and *Circular Letter No.* 10/(19)—RS/61, dated 15-3-1962) the Department of Company Affairs has laid down the following principles for deciding cases for availability of names:

Guiding instructions for availability of names.—The procedure for scrutinising the availability of names for new companies has recently been re-examined carefully in this Department, having taken into account the difficulties experienced by some Registrars in following the instructions given to them *vide* Department's Letter No. 10(19)-RS/61, dated 15th March, 1962. This letter, together with the enclosed set of instructions as revised, consolidates, and is in *supersession* of all the previous instructions issued from time to time by this *Department*. An illustrative list of names considered to be un-desirable within the meaning of Section 20 of the Companies Act, has also been given herewith. The guiding instructions for deciding cases of making a name available for registration are given in *Appendix* 'A' to this letter. In addition to these, the Registrars of Companies are requested to note the following general instructions also:

1. As the Registrars have hitherto been doing, they should refer only doubtful and hard cases where they might find it difficult to take a decision, to the Research and Statistics Division at the Headquarters.

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* These administrative guidelines have no statutory backing and are only guiding instructions on the matters.

2. Where consultation with the Regional Director on the spot is possible, Registrars of Companies would take advice before referring doubtful and hard cases to the Headquarters.
3. In order to find out the availability of names, the Registrars are advised to consult the All India Index Cards of companies in their offices, if any kept uptodate or the alphabetical list of companies contained in the following publications issued by the Department:
   (i) Annual Blue Book on Joint Stock Companies, Part II, 1958-59 and its supplementaries giving newly registered companies upto March, 1964.
   (ii) All India lists of new company registrations maintained in the field offices from 1st April, 1964 to date.
   (iii) Fortnightly list of names made available to promoters by the Registrars, circulated from the Research and Statistics Division.
   (iv) List of foreign companies having a place of business in India.
4. The Registrars will prepare separate slips and not one consolidated list as per specimen given at *Appendix* 'B' in respect of each of the name allowed by them and send them in a bunch to the Research and Statistics Division on the 1st and 16th of every month. A consolidated list of such new names allowed by the Registrars will be drawn up here and it would then be circulated among the field offices for their ready information, and use. The advantage of this arrangement is too obvious to need emphasis.
5. The Registrars of Companies may ask the promoters to suggest a panel of three to five names quite distinct from each other for consideration.
6. The Registrars should adopt a polite attitude and persuade the Company promoters to suggest names consistent with the guiding principles. They should explain the difficulties of the Administration in approving names likely to create confusion in the minds of the public and harm the interests of the promoters.
7. In case any of the names proposed by the promoters is not agreed to by the Registrars as available, it should be open to them to follow up the matter by subsequent letters or application for the same fee within a reasonable period which may normally be construed to mean three months from the date of rejection of the name/names proposed.
8. The Registrars may permit the promoters to use the name of the firm in brackets after the duly approved name as incorporating or successor to (name of the firm) in order to fulfil the desire of the promoters to retain the goodwill of their business in cases where the names of firms seeking registration under the Companies Act is considered as undesirable within the meaning of section 20 of the Act.
9. Registrars should ascertain from the promoters if the proposed name/names were applied for to any other Registrar of Companies and if so, with what result. In case there is some difference of opinion between the two Registrars in making the name available, then the case may be referred to the Board for advice.
10. The name of a proposed company allowed by the Registrars to the promoters for registration under the Companies Act should not be kept reserved for more than three months (w.e.f. 21-3-1995 it is now six months *vide* amended R. 4A of the Companies (Central Govt.'s) General Rules & Forms 1956).
11. It is necessary that the 'keywords' of a proposed name/names are checked separately with the names of the existing companies beginning with those 'keywords' so as to avoid any possibility of allowing a name with a little re-arrangement of the same words of the existing company which may be said to be closely resembling each other.

I may further add that although it is not possible to lay down hard and fast rules for determining whether a particular name or any two names too nearly resemble each other, each case, however, will be decided on its merits. As already emphasised in the earlier circular letter of this Department on the subject dated 15th March, 1962, that the various criteria set out in the guiding principles at *Appendix* 'A' are not exhaustive but only illustrative of what is considered to be undesirable names under section 20 of the Companies Act and that, by the very nature of the subject all possible cases could not be covered. It is, therefore, suggested that where the Registrars find that certain proposed names could not be judged in the light of the instructions given above and give rise to doubt, the same may be referred to the Research and Statistics Division at the Headquarters after availing of the help of the Regional Director if available on the spot.

Guiding instructions for deciding cases of making a name available for registration

Departments' guiding principles.—The Department has evolved the following guiding principles for deciding availability of names:

A name which falls within the categories mentioned below will not generally be made available:

(1) If it is not in consonance with the principal objects of the company as set out in its memorandum of association. This does not necessarily mean that every name should be indicative of its objects, but when there is some indication of business in the name then it should be in conformity with its objects.

(2) If the Company/Companies' main business is finance unless the name is indicative of that particular financial activities, *viz.*, Chit Funds/Investments/Loans, etc.

(3) If it includes any word or words which are offensive to any section of the people.

(4) If the proposed name is the exact Hindi translation of the name of an existing company in English especially an existing company with a reputation.

(5) If the proposed name has a close phonetic resemblance to the name of a company in existence for example, J.K. Industries, Ltd., Jay Kay Industries Limited.

(6) If the name is only a general one like Cotton Textile Mills Ltd., or Silk Manufacturing Ltd. and not specific like Calcutta Cotton Textiles Mills Limited or Lakshmi Silk Manufacturing Company Limited.

(7) If it includes, the word "Co-operative". Sahakari or the equivalent of word "Co-operative" in the regional languages of the country.

(8) If it attracts the provisions of the Emblems and Names (Prevention of Improper Use) Act, 1950 as amended from time to time, *i.e.*, use of improper names prohibited under this Act.

Department of Company Affairs Circulars, General Circular No. 24 of 2001, dt. 21-11-2001.—Instruction No. 8 of the Guiding instructions circulated, vide this Department's letter No. 10(1)-RS/65, dated 27th November, 1965, provides that a name in the category mentioned below will not generally be made available:—

> "If it attracts the provisions of the Emblems and Names (Prevention of Improper Use) Act, 1950, as amended from time to time, i.e., use of improper names, prohibited under this Act."

2. It is observed from a communication received from the Department of Consumer Affairs that the above-said instructions are not being followed scrupulously.

3. The ROCs are advised to take into account the provisions of the above-said Emblems and Names Act while making names available to companies under the Companies Act, 1956. All the ROCs are requested to adhere to the above instructions for strict compliance.

(9) If it connotes Government's participation or patronage unless circumstances justify it, *e.g.*, a name may be deemed undesirable in certain context if it includes any of the words such as National, Union, Central, Federal, Republic, President, Rashtrapathi, Small-Scale Industries, Cottage Industries and Financial Corporation, etc.

(10) If the proposed name contains the words 'British India.'

(11) If the proposed name implies association or connection with Embassy or Consulate which suggests connection with local authorities such as Municipal, Panchayat, Delhi Development Authority or any other body connected with the Union or the State Government.

(12) If the proposed name is vague like D.J.M.O. Limited or T.N.V.R. Private Limited or S.S.R.P. Limited.

(13) If a proposed name implies association or connection with or patronage of a national hero or any person held in high esteem or important personages who are occupying important positions in Government so long as they continue to hold such positions.

(14) If it resembles closely the popular or abbreviated descriptions of important companies like Tisco (Tata Iron & Steel Company Limited), H.M.T. (Hindustan Machine Tools), I.C.I. (Imperial Chemical Industries), Texmaco (Textile Machinery Corporation), Wimco (Western India Match Company), etc. In some cases, the first word or the first few words may be the key words and care should be taken that they are not exploited. Such words should not be allowed even though they have not been registered as trade marks.

(14A) Where the existing companies are stated and found to be well-known in their respective fields by their abbreviated names, these companies may be allowed to change their names, by way of abbreviation with the prior approval of the Regional Director concerned.

Department's Circular, dated 31-3-1993.—The abbreviated name will be considered only in case of change of name under section 21 of the Companies Act, 1956, with the prior approval of the Regional Director concerned and should not be allowed for adoption by new companies. [*Circular No.* 4/93; *F. No.* 3/14/93—CL-V, dated 31-3-1993]

Press Note, dated 5-5-1993.—As per existing guidelines, the companies well-known in their respective field by abbreviated names, are allowed to change their names by way of abbreviation (*e.g.* ABC Ltd.) with the approval of the Department of Company Affairs after following the requirement of Section 21 of the Companies Act, 1956. It has now been decided that any such change of name will require only the prior approval of Regional Director concerned. The companies will, however, continue to make applications in Form No. 1A for availability of the proposed changed names to the concerned Registrar of Companies. It may be noted that the abbreviated name will not be allowed for adoption by a new company proposed to be incorporated under the Act. [*No.* 3/14/93-CL-V: *Press Note No.* 1/93, dated 5-5-1993]. The power of Central Government is now vested with the Registrar.

Department's Circular, dated 16-2-1995.—Presently, there is a restriction on use of abbreviated names (like ITC Limited) in case of existing companies requiring approval of the Regional Director concerned. No such approval of Regional Director will now be necessary and ROCs may take a final decision on such applications in the light of existing guidelines. (*Para iii*). [*Circular No.* 1/95 *F. No.* 14/6/94-CL-V, dated 16-2-1995]

(15) If it is different from the name/names of the existing company/companies only to the extent of having the name of a place within brackets before the word limited; for example, Indian Press (Delhi), Limited, should not be allowed in view of the existence of the company named Indian Press Limited. To this rule, however, frequent exceptions are made in the case of subsidiary and in the case of a company carrying on local business and in other cases on their merits. As for an example, 'Corner Garage (Delhi) Private Limited' may be allowed notwithstanding that there is an existing company 'Corner Garage Private Limited' at Calcutta. So would be 'Regent Cinema Limited' at Madras, if there is a company by the name Regent Cinema (Delhi) Limited. These names may also be allowed if they are in the same group or management.

(16) If the proposed name includes common words like 'Popular' 'General' 'Janta', if they are in the same State doing the same business. But in case of companies in different business in the same State and in all cases when the registered office of the company is in different States, the name might be allowed. For instance, if there is 'Popular Drug House Private Limited' existing another company by the name of 'Popular Plastic Private Limited' should not be objected to.

(17) If it includes a name of registered trade-mark unless the consent of the owner of the trade-mark has been produced by the promoters. It may not be possible in all cases to check up the proposed name with the trade mark, however, if the Registrars are in the knowledge or some interested party/parties bring to their notice a trade mark which is included in the proposed name then it should not be allowed unless a no-objection certificate is obtained from the party who has registered the trade mark in its own name.

[**Note** : Section 20(2)/(3) has been amended by the Trade Marks Act, 1999. The amended section now provides statutory protection of trade marks in the matter of availability of name]

(18) If a name is identical with or too nearly resembles, the name of which a company in existence has been previously registered. A few illustrations of closely resembling names are given below for guidance. The names as proposed in column 1 should not (normally) be made available in view of the companies in existence as shown in column 2. However, if a proposed company is to be under the same management or in the same group and like to have a closely resembling name to the existing companies under the same management or group with a view to have advantage of the goodwill attached to the management or group name such a name may be allowed.

Even in the case of unregistered companies or firms which have built up a reputation over a considerable period, the principle (that if a name is identical with or too closely resembles the name by which a company has been previously registered and is in existence, it should not be allowed) should be observed as far as practicable. In view of the difficulty in checking up whether a proposed name is identical with or too nearly resembles the name of an unregistered company or a firm of repute, it should at least be ensured that a proposed name is not allowed if it is identical with or too nearly resembles the name of a firm within the knowledge of the Registrar. The cases of foreign companies of repute should also be similarly treated even if there are no branches of such companies in India.

	Proposed name	*Existing company too nearly resembling name*
1.	Hindustan Motor and General Finance Company.	Hindustan Motor Limited.
2.	The National Steel Mfg. Co. Private Limited.	National Steel Works.
3.	Trade Corporation of India Limited.	State Trading Corporation of India Limited.
4.	Viswakaram Engineering Works Private Limited.	Viswakaram Engineer (India) Private Limited.
5.	General Industrial Financing & Trading Co. Ltd.	General Financial & Trading Corporation.
6.	India Land & Finance Limited.	Northern India Land & Finance Limited.
7.	United News of India Limited.	United Newspapers Limited.
8.	Hindustan Chemicals and Fertilizer Limited	Hindustan Fertilizers Limited.

(19) If it is identical with or too nearly resembles the name of a company in liquidation, since the name of a company in liquidation is borne on the register till it is finally dissolved. A name which is identical with or too closely resembles the name of a company dissolved as a result of liquidation proceeding should also not be allowed for a period of 2 years from the date of such dissolution since the dissolution of the company could be declared void within the period aforesaid by an order of the Court under section 559 of the Act.

Further, as a company which is dissolved in pursuance of action under section 560 of the Act can be revived by an order of the Court before the expiry of 20 years from the publication in the Official Gazette of the company being so struck off, it is considered desirable to stop or conditionally allow the registration of a proposed name which is identical with or too nearly resembles the name of such dissolved company for a period indicated below. Since the period of 20 years as prescribed under the law is considered an unduly long period, the registration of a proposed name which is identical with or too nearly resembles the name of company dissolved in pursuance of section 560 should not be allowed for a period of first five years only. During the next five years such a proposed name may be allowed subject to the condition that in the event of the dissolved company being restored to life by an order of the Court the new company would have to change its name. After a lapse of ten years, names identical with or too nearly resembling those of the dissolved companies may be allowed without any such condition.

(20) If it is different from the name of an existing company merely by the addition of words like New, Modern, 'Nav' etc. Names such as New Bata Shoe Company, New Bharat Electronic, etc. should not be allowed. Different combination of the same words also requires careful consideration. If there is a company in existence by the name of "Builders and Contractors Limited" the name "Contractors and Builders Limited" should not ordinarily be allowed.

(21) If it includes words like, "Bank", 'Banking', 'Investment', 'Insurance' and 'Trust'. These words may, however, be allowed in cases where the circumstance justify it. In cases of banking companies the Reserve Bank of India should be consulted and its advice should be taken before a name is allowed for registration. The purpose of such consultation is to prevent small banking companies from misleading the general public by adopting the names of some well-established and leading banks functioning elsewhere than in India. In case of differences of opinion with the Reserve Bank of India the matter should be referred to the Board for advice.

(22) If the name includes the word 'Industries' or 'Business' unless the name is indicative of the business of the proposed company for otherwise it serves as a lever for the company to diversify its activities.

(23) If it includes proper name which is not a name or surname of a director— such names should not be allowed except, for valid reasons. For example, for sentimental reasons, sometimes the names of relatives such as wife, son and daughter of the director may have to be allowed, provided one other word suggested makes the name quite distinguishable.

(24) If it is intended or likely to produce a misleading impression regarding the scope or scale of its activities which would be beyond the resources at its disposal. For example, names like Water Development Corporation of India (Private) Ltd., Telefilm of India (Private) Ltd., All India Sales Organisation Ltd., Inter-Continental Import and Export Company Ltd., etc. should not be allowed, when the authorised capital is to be only a few lakhs, and the area of operation limited to a State. Words like "International", "Hindustan", 'India', 'Bharat' 'Continental', 'Asiatic' may be allowed only if the scope and scale of business of the proposed company justify the use of such words. However, the words 'Jai Hind', 'Jai Bharat', 'Nav Bharat', 'New India' etc., included in the proposed name need not stand the same test as

Hindustan, India etc. (as they do not give the same sense). Similarly the words, Bharat, India, etc., if stated in the brackets before the words limited or private limited need not stand the same test as the words India, etc., put at the beginning of the name. Also the word 'India' or 'Bharat' in brackets before the words limited or private limited does not necessarily mean that the company is an Indian Branch of some foreign company, such as Marsdon Electricals (India) Private Limited.

(25) If the proposed name includes the word "State" along with the name of the State such as Kerala State Company Limited should not be allowed as it would give an impression of the Kerala State Government participating in the share capital of the proposed company. However, if the name of a State only is included without the addition of the word 'State' in the proposed name then it may be allowed as it is not likely to give the impression that the company has the State Government's interest in it.

(26) If the proposed name includes the word 'Corporation' unless the company could be recorded as a big sized company. However, the word 'Corporation' and 'Company' may be regarded as closely resembling for purposes of allowing a new name. For example, a company by the name of Rajasthan Finance Company should be regarded as undesirable within the meaning of section 20 of the Act as another company by name "Rajasthan Finance Corporation" already exists.

(27) If the proposed name includes words like French, British, German, etc., unless the promoters satisfy that there is some form of collaboration and connection with the foreigners of that particular company or place the name of which is incorporated in the name. Thus, the name 'German Tool Manufacturing Company Ltd.', should not be allowed unless the company has some connection with Germany.

(28) Even where except for the first word all the other words of the proposed name are similar to those of an existing company, the first word should be considered to be sufficient to distinguish it from the name of the existing company. For example 'Oriental... Limited." [*Circular letter No.* 10(1)-RS/65, dated 27-11-1965. See also *Circular No.* 10(19)—RS/61, dated 5-5-1962].

The word "Hindustan" should be kept reserved only for public sector companies. It may, however, be allowed to be used in the names of the private sector companies in a large way of business. Similarly the word "corporation" may be allowed in the name of the company in case the authorised capital is more than Rs. 5 crores. (*Circular. No.* 16/74—F.No. 27/9/74-CL-III, dated 27-8-1974).

Judicial review of the Department's Circular.—Instruction number 18 of *Circular No.* 10(a)-RS-61, dated 5-5-1962, cited above came up for consideration before the Bombay High Court in *Executive Board of the Methodist Church in India v. Union of India,* (1985) 57 Com Cases 443 (Bom). MRS. MANOHAR, J. held that where the company, already in existence with a certain name, had become defunct and the name with which it was registered was also of misleading character in the sense that it was not a true representative of the world organisation known as the Methodist Church, the consent of such a company was not necessary for approving the name of a new company which is the true representative of the Methodist Church movement in India and which had necessarily to register itself under that name. The refusal of the Registrar was wrong. The court accordingly ordered the Registrar to register the company under the words "Methodist Church" and to strike out the name of the earlier defunct company. The learned Judge discusses the effect of authorities as to misleading names at pp. 449, 450 including HALSBURY'S LAWS OF ENGLAND, Para 130 (4th Edn., Vol. 7) : [4th Edn., 1988 Reissue Vol. 7(1), Paras 157-158] : 4th Edn., 1996 Reissue, paras 159 to 162.

Further Guidelines for availability of names

Departmental Circular, dt. 13-5- 1999.—As ROCs are aware, this Department had issued exhaustive guidelines on avoiding undesirable names for companies as mentioned in section 20 of the Companies Act, 1956 through *Circular No.* 10(19)-RS/61 dated 5-5-1962. Further guidelines were also issued through *Circular No.* 2/90 (No. 1/1/90-CL-V-27/1/89-CL-III) dated 5-1-1990.

2. In recent times, this Department had received a few references which needed further clarification. The following guidelines/clarifications are accordingly issued.

3. Names starting with small letters/having small letters/alphabets

3.1. In the past the name-search for allowing names for companies used to be a manual search based on list of names already in existence on a particular date, names made available by different ROCs (which used to be circulated periodically) etc. The name search is no longer manual. It has become a computerised operation in all ROC offices. In view of this, some of the old constraints (like alphabetical listing) which could be a restrictive factor in the manual system do not exist under the present computerised system.

3.2. ROCs may therefore now allow names starting with small alphabets (like i2 Technologies.. Ltd.' etc.) as such names are being increasingly used by many companies in other countries. It should, however, be ensured that the name starting with small alphabets does not have phonetic or visual resemblance to the name of a company in existence.

4. Change of name by companies on Computer Software Business

4.1 In recent times it appears that quite a few companies whose principal object was not computer software and who had actually been involved in financing activities have changed their names to indicate as if they were in the business of computer software. For this purpose they have included words like—"Infosys; Software; Systems; Infosystem; Computers; Cyber; Cyberspace etc." in their names.

4.2. In order that investors are not misled by the strategy adopted by a few companies. ROCs are hereby advised that in future they should allow change of name to companies to reflect the business of software only if a substantial portion of their income (as reflected from their audited accounts or accounts certified by a Chartered Accountant) is derived from software business. If this is not proved then such change of name should not be allowed.

5. Companies in Insurance Sector

5.1 It may be recalled that in Guideline No. 21 (printed above) you have been advised not to allow the word 'bank', 'banking', 'investment', 'insurance', and 'trust' unless circumstances justify it. As you may be aware, the insurance sector is likely to be opened for entry by Private Sector. The activities of the Insurance Sector would be regulated by the Insurance Regulatory Authority which has already been set up.

5.2 In view of this, in partial modification of the abovementioned Guideline, it is hereby clarified that ROCs may allow companies to be registered by them with the word 'insurance' or 'risk corporation' as part of the name only after consulting the Reserve Bank of India and Insurance Regulatory Authority (Jeevan Bharti Building, Tower 1, Connaught Circus, New Delhi-110 001) as the case may be.

Department's Clarification, dated 30-6-2000.—Attention is invited to this Department's Circular No. 6 of 1999 (5/35/98-CL.V), dated 13th May, 1999, in regard to allowability of names for entrepreneurs seeking to promote companies for providing insurance services. In terms of the above circular, such names were being given only after consulting the Insurance Regulatory Authority until now. Consequent, on the coming into force of the Insurance Regulatory Development Authority Act, 1999, with effect from 19th April 2000, the Department has received a reference from the Insurance Regulatory Authority advising that the embargo on registration of names by new companies could be lifted. In view of this all ROCs are advised that they may allow names with the word insurance/assurance or risk corporation as part of the name without any need to consult the Insurance Regulatory Authority. It is hereby clarified that such names can be allowed only to new companies and not for change of name as existing companies are not allowed to carry on any insurance activity. [*Circular No. 5, Dated 30-6-2000*].

Department's circular dated 25-4-2003.—In partial modification of General Circular No. 5/2000 dated 30th June, 2000, it is hereby further clarified that since the Insurance Regulatory and Development has notified the Insurance Regulatory and Development Authority (Insurance Regulations, 2002 permitting private sector companies to carry on the insurance business, the Registrar of Companies may permit change of name of existing companies on their changing the objects to undertake the business of insurance brokers also. (*Circular No. 19/2003, dated 25-4-2003, F. No. 5/6/2003-CL V.*)

6. Use of Generic Names

6.1. Guideline No. 5 relates to inadvisability of allowing companies to have only generic names without any other proper noun preceding/succeeding it. Under this category would come the word 'Y2K' (i.e. Year 2000).

6.2. It may kindly be noted that this is a generic one and cannot be allowed for any company as a 'stand alone' name. [*Issued by DCA, vide No. 5/35/98-CL.V*; General Circular No. 6/99, dated 13-5-1999].

Use of Name of "Chamber of Commerce" in UK.—In England the Company and Business Names (Chamber of Commerce, etc.) Act 1999 restricts the use of the name chamber of commerce by companies.

Guidelines as to use of key words

"With a view to maintain uniformity, the following guidelines may be followed in the use of key words, as part of name, while making available the proposed names under sections 20 and 21 of the Companies Act, 1956.

	Key words	*Required authorised capital*
		Rs.
(1)	Corporation.	5 crores.
(2)	International, Globe, Universal, Continental, Inter-Continental, Asiatic, Asia, being the first word of the name.	1 crore.
(3)	If any of the words at (2) above is used within the name (with or without brackets).	50 lakhs.
(4)	Hindustan, India, Bharat, being the first word of the name.	50 lakhs.
(5)	If any of the words at (4) above is used within the name (with or without brackets).	5 lakhs.
(6)	Industries/Udyog.	1 crore.
(7)	Enterprises, Products, Business, Manufacturing..	10 lakhs.

2. These names with key words at Serial Nos. (6) and (7) may be considered when the company proposes to deal in various business activities or the company is already carrying on various business activities (in the case of change of name)." *F. No.* 27/1/87- CL-III, dated 13-3-1989 : (1989) 65 Com Cases 536 (St.).

No objection from applicants who do not sign memorandum & articles

I. Department's Circular.—"As per Application Form for availability of names (Form No. 1A), prescribed under rule 4A of the Companies (Central Governments) General Rules and Forms, 1956, the promoters are, *inter alia*, required to give the names and addresses of the prospective directors or promoters, as also the name and address of the person(s) applying for availability of name. You are requested to advise your constituents to ensure that the application form is filled up in all respects and application is made by one or more amongst the promoters. The Registrars of Companies have been advised to ensure at the time of registration of a new company that the subscribers to the memorandum and the articles of association tally with the list of promoters/first director stated in the application for availability of name and in case, one or more of the promoters are not interested to participate in the promotion of a new company at a later stage. 'No objection letter' from such promoter(s) is made available to the Registrar, while submitting the documents for registration. The Registrars of Companies are also being advised to dispose of applications for availability of name ordinarily within 14 days of the receipt of application and to correspond with the applicant promoter(s), in this behalf." *No.* 27/1/89-CL-III, dated 17-2-1989 : (1989) 65 Com Cases 575 (St.)

II. Department's Circular.—"I am directed to refer to this Department's *Circular No.* 27/1/89-CL-III, dated 17th February, 1989 [*Printed above*] on the above subject, wherein you were requested to advise your constituents to ensure that the application form is signed by one or more amongst the promoters and in case one or more of the promoters are thereafter no more interested in participating in the promotion of the new company, a no objection letter from such promotor is made available to the Registrar of Companies at the time of registration of the new company. Instances came to the notice of the Department that some promoters are pre-empting the names, which is not a healthy practice. It has, accordingly, been decided that, in future, Registrars of Companies should register the company only in cases where the promoters, as per availability of name and application, are also the subscribers to the memorandum and articles of association of the proposed company at the time of its registration. In case of any change in the name(s) amongst the subscribers, the changed subscribers are advised to make fresh application for availability of name. The Registrar may, as per existing procedure, allow the same name, if otherwise available, after three months from the date when the name was allowed to the original promoter(s)." *Circular No.* 1 of 1990, dated 5th January, 1990 : (1990) 67 Com Cases 230 (St.).

III. Department's Circular dated 16-2-1995.—The Department *vide Circular No.* 27/1/89/CL-III, dated 17-2-1989 [*Printed above*] advised the ROCs to ensure that at the time of registration of a new company, the subscribers to the Memorandum of Association should tally with the list of promoters/first directors stated in the application for availability of name, and in case one or more of the promoters are not interested in participation in the promotion of a new company at a later stage, a "no objection" letter from such promoter(s) is made available to ROC. This circular was amended on 5-1-1990 (No. 1/90) [*Printed above*] to the effect that ROCs should register the company only in case where the promoters, as per the availability of name application, are also subscribers to the Memorandum. On reconsideration, it has now been decided, in partial modification of the above circular, that so long as there is at least one promoter common, both in the name availability application and the subscription clause of Memorandum

& Articles of Association, and others have no objection, the company may be registered. (*Para ii*). [*Circular No.* 1/95, *F.No.* 14/6/94-CL-V, dated 16-2-1995].

Incorporation of Stock Exchanges, advance approval of name by SEBI

I am directed to draw your attention to this Department's *Circulars No.* 27/22/85- CL-III, dated 13-1-1986 and 18-9-1991 and *Circular No.* 27-05-92-CL-III, dated 23-3-1993 on the above subject and to enclose a copy of letter, dated 18-3-1996 [*Printed below*] received from the Chairman, SEBI in this regard. You are, requested to ensure that under no circumstance a company is registered with the words 'Stock Exchange' as part of its name without obtaining in principle approval/no objection of Securities and Exchange Board of India. It may kindly be noted that non-compliance with these instructions will be viewed very seriously.

Copy of SEBI's letter, dated 18-3-1996.—It has come to our notice that certain companies calling themselves Stock Exchanges are enrolling members and collecting substantial deposits from them. The companies who have not obtained permission to operate as a stock exchange under section 19 of Securities Contracts (Regulation) Act, 1956 or have not been granted recognition by Central Government/SEBI under section 4 of the above Act are collecting such deposits in violation of the provisions of the said Act. Section 19(1) of Securities Contracts (Regulation) Act, 1956 prohibits organising or assisting in organising any stock exchange without the permission of the Central Government/SEBI.

In this regard, we request you not to allow such names to new companies which have the words 'Stock Exchange' in them unless they have been given in-principle approval or 'No objection' from SEBI. This would ensure that the investors are not misled by such names into dealing with members of unrecognised stock exchanges. [*Circular No.* 3/96, *vide No.* 3/4/96-CL-V, dated 12-4-1996].

Incorporation of Venture Capital Companies

Department's Circular.—As per guidelines issued by the Ministry of Finance, Department of Economic Affairs *vide* press release No. S. 11(86)-CCI/11/87, dated 25-11-1988, only such venture capital companies which abide by these guidelines shall take advantage of tax benefits. As per guidelines, approval would be given for establishment of venture capital companies/funds by the Department of Economic Affairs or such authority as may be nominated by the Government. It is possible that some promoters may float a company and call it a Venture Capital Company but may not avail of the tax benefits available to such companies and in such a situation, a common investor would not be able to distinguish between approved venture companies which are within the discipline of the guidelines and eligible for tax benefits from those who call themselves Venture Capital Companies, but prefer to remain outside the guidelines and forego any tax benefit. To avoid such eventuality, it has been decided that the words "Venture Capital/Venture Capital Company/Venture Capital Fund/Venture Capital Finance Company" or such similar name, as part of the proposed name of a company be only allowed when the company or the promoters have obtained approval from the Department of Economic Affairs or such authority as may be nominated by the Government, in this behalf". *Circular No.* 13/90, dated 27-8-1990.

§ For Guidelines for Venture Capital Companies see *Appendix* 273, also see SEBI (Venture Capital Funds) Regulations, 1996, *Appendix* 195.

Incorporation of Asset Management Companies (AMCs) other intermediaries

Guidelines for registration of AMCs

Department's Circular I.—The following guidelines are issued in respect of registration of Asset Management Companies (AMCs), in consultation with the Securities and Exchange Board of India :

(a) Approval of AMC by SEBI:

As per guidelines, AMC shall be authorised for business by SEBI on the basis of certain criteria and the memorandum and articles of association of the AMC would have to be approved by SEBI. Accordingly, you are advised not to register any company under the Companies Act, 1956, without the memorandum and articles of association being approved by SEBI.

(b) Authorised capital of AMC:

The primary objective of setting up of an AMC is to manage the assets of the mutual funds and other activities which it can carry out, such as, financial services consultancy which do not conflict with the fund management activity and are only secondary and incidental. That being so, it may not be practical to expect a company to be set up with a paid-up capital of Rs. 5 crores to carry on only incidental activities, without any assurance of its receiving an approval from SEBI to act also as an Asset Management Company for a mutual fund. You should, therefore, not have any objection in registering an AMC if the authorised capital of such a company is approved by SEBI.

2. A copy of these guidelines may also be placed on the notice board of your office for general information. (*Department's Circular No.* 4/92; *F. No.* 3/14/92-CL-V, dated 2-9-1992, addressed to Registrar of Companies)

Department's Circular II.—"Some Registrars are insisting upon the promoters proposing to carry on activities as merchant bankers, registrars to an issue, investment advisers, portfolio manager etc. to obtain prior approval of SEBI before making available the proposed name or incorporation of a company. In this connection, it may be pointed out that under section 12 of the SEBI Act, 1992 the intermediaries associated with securities market are required to seek registration by making an application to SEBI, as per regulations made thereunder, which *inter alia* require the applicant to state the date and place of registration, details of directors, as also to furnish Memorandum and Articles of Association, if the applicant is a company. However, in terms of Regulation 18(2) of the SEBI (Mutual Fund) Regulations, 1993, Asset Management Companies (AMC's) are required to submit to SEBI their respective Memoranda and Articles of Association for approval. Therefore, unlike the Memoranda and Articles of Association of other intermediaries, it would be in the interest of concerned AMC's to get their Memoranda and Articles of Association cleared by SEBI before the same are presented to the concerned Registrar of Companies for registration. In view of the above, you are requested not to insist upon seeking prior approval of SEBI for registration of intermediaries like merchant bankers, Registrar to an issue, investment adviser, portfolio manager etc. However, this *Department's Circular No.* 4/92 (No. 3/14/92-CL-V) dated 2-9-1992 will continue to be in force and you may register an AMC only after its draft Memorandum and Articles of Association is cleared by SEBI." (*Department's Circular No.* 5/94; *F. No.* 3/14/92-CL-V, dated 15-4-1994, addressed to Registrars of Companies).

Use of the words 'Nidhis' or 'Mutual Funds' as part of name.—The Registrars of Companies (ROCs) have been directed by the Department of Company Affairs (DCA) not to allow registration of names with words "mutual funds" forming part of some Non-Banking Financial Companies (NBFCs/Nidhis under section 20 of the Companies Act, 1956), unless such companies are going to be incorporated actually as mutual funds. ROCs have been informed that companies declared as nidhis and mutual benefits societies under section 620A of the Companies Act are not mutual funds. Therefore, names with words "mutual funds" forming part thereof shall also not be allowed to companies proposed to be incorporated as "nidhi" or "mutual benefit societies". It has come to the notice to the DCA that some NBFCs or nidhis have been registered with words "mutual funds" forming part of their names, although they are not actually mutual funds. This is likely to create confusion in the minds of investors. In the cases where NBFCs or nidhis have already been incorporated with words "mutual funds" in their names, the ROCs [*sic*, NBFCs] have been asked to get their names changed under section 21 of the Companies Act, 1956, within a reasonable time of six months failing which, report would be sent to the DCA for initiating action for withdrawal of notification issued in their favour under section 620A of the Companies Act. [*PIB Press Release, New Delhi, dated 14th February, 2000.*]

Corporate Identity Number

Department's General Circular No. 12/2000, dated 25th October, 2000.—It has been decided that all Registrar of Companies will allocate a corporate identity number (CIN) to each company registered on or after 1st November, 2000. The CIN has been designed to help easily identify companies belonging to a State, industry, ownership or age. It will be 21-digit number. The first letter denotes the listed or unlisted company. The first five digits represent the economic activity of the company, the second two places, represent the State in which the company's registered office is located, the next four places, indicate the year in which the company was incorporated, the next three places, indicate ownership code and the last six places in the CIN are the unique number assigned to every company in any particular economic activity, in a particular State, of a particular year of incorporation and of a particular ownership category. For example, the few CIN for a new well known companies are presented below:

Steel Authority of India Ltd. L 27104DL1973UGCXXXXXX

Tata Engineering & Locomotive L 3410MH1943PLCXXXXXX

The complete listing of State code and the ownership code is reproduced in text of Circular. Training schedule for the officers and staff of Registrars of Companies in this regard is being chalked out by the NIC and will be sent to you shortly. All Registrars of Companies are directed to act accordingly.

Allotment of CIN to companies registered prior to 1-11-2000.

Department's General Circular No. 8/2001, dt. 30-3-2001. See *Appendix* 37.

Release of Search Facilities on filing status of Balance Sheets and Annual Returns on DCA Website

Press Note Dt. 14-3-2002.—Shri Arun Jaitley, Hon'ble Minister of Law, Justice & Company Affairs had, on 4th April, 2001, released following Search Facilities on Department of Company Affairs website (http://dca.nic.in) for the benefit of the public:

(a) **Company Directory:** This facilitates search on companies (over 5.8 lacs) registered at the offices of the Registrar of Companies (ROCs). Search provides filtering on category of the company and State where company is registered. Result of the search is displayed as registration number, state of registration and name of the company.

(b) **Names Approved for Registration:** This facilitates search on the names approved by ROCs and are in pipeline for registration of the company.

(c) **ROC Fee Computation:** This facilitates computation of fee charged for various services such as name approval, incorporation of new company, filing of statutory documents, etc., rendered by ROCs.

Allocation of specific economic activity based upon main object clause instead of code "00000"

General Circular No. 9/2001, dt. 15-5-2001.—In continuation of this Department's General Circular No. 12/2000 (issued vide letter No. 1/6/2000-CL.V) dated 25th October, 2000, I am directed to say that the step 2 for implementation of Corporate Identity Number (CIN) provides that in a case if a company is operating in diverse fields, the economic activity as "0000" has to be assigned.

2. Some difficulties may be faced while implementing of Corporate Identity Number (CIN) while doing industry-wise analysis in case of company operating in diverse fields is shown as having economic activity "00000". You are, therefore, requested that instead of entering the code "00000" as economic activity of a company, a specific economic activity of the company based upon the main object in the company's Memorandum of Association [item I of the Object Clause (IIIA)] be entered in the second five digits representing the economic activity of the company. [*No. 1/6/2000-CLV, issued by DCA.*]

§ For the text of the Circular see *Appendix* 37.

Delegation of powers to Registrar.—Powers of the Central Government under this section have been delegated to Registrars of Companies, *vide* GSR No. 507(E), dated 24-6-1985.

Prescribed Rules and Form

Every application for name availability shall be in Form No. 1-A, accompanied by a fee of Rs. 500/-and the Registrar shall furnish the required information ordinarily within 7 days (w.e.f. 21-3-1995 *vide* amended R. 4A of the Companies (Central Govt.'s) General Rules & Forms, 1956). The name is valid for a period of 6 months from the date of intimation by the Registrar. See Form No. 1-A and Rule 4-A in *Appendix* 1.

Department's Circular to ROCs, dated 16-2-1995.—In view of computerisation in this area in most of the offices, you are advised to make arrangements for a computer terminal being available in your office for few hours on all working days to the promoters or their representatives with a view to ascertain the availability of proposed names. ROC, Bangalore, has already implemented this procedure *w.e.f.* 1-11-1994. This will ensure that the names applied for would be made available promptly when an application for this purpose is made subsequently by the promoters. (*Para i*).

Rules are being separately amended to extend the validity period of availability of names from three to six months and to make availability of names within seven days instead of fourteen days as per existing rules, however, the ROCs where computer facility is available may endeavour that name availability applications are disposed of within three working days after their receipt. (*Para iv*). [*Circular No.* 1/95, *F.No.* 14/6/94-CL-V, dated 16-2-1995].

Secretarial Practice Notes

Check whether:—

(a) the name (or names selected in order of priority) comply with the guidelines and is not too general?

(b) in case the proposed name consists of key word, the significance thereof be explained?

(c) application in Form 1A made to the Registrar for seeking availability of name with application fee of Rs. 500?

(d) main objects stated in the application correspond to the object clause of memorandum of association?

(e) the names of proposed promoters (subscribers) and directors stated in the application tally with the names given in the Memorandum and Articles of Association?

S. 21. Change of name by company[1].—A company may, by special resolution and with the approval of the Central Government signified in writing, change its name:

[2][*Provided* that no such approval shall be required where the only change in the name of a company is the addition thereto or, as the case may be, the deletion therefrom, of the word "Private", consequent on the conversion in accordance with the provisions of this Act of a public company into a private company or of a private company into a public company.]

NOTES

Eng. Act, 1948 : Sec. 18(1) Previous Act : Sec. 11 (4)

Companies (Amendment) Act, 1965

The proviso to the section was added by section 6 of the Companies (Amendment) Act, 1965. The Notes on clauses stated : "This amendment does away with the technical necessity of obtaining Government's approval under section 21, for the mere addition or deletion of the word "Private" from a company's name, consequent on its conversion from a public into a private company or *vice versa*" (*Clause* 6).

Scope of section

The section prescribes a special resolution and approval of the Central Government for changing the company's name. The proviso to the section dispenses with the approval of the Central Government when the only change occurring in the name is the deletion or addition of the word 'private' consequent upon the conversion of the company from private to public and *vice versa*. It should be noted that a public company can be converted into a private company with the approval of the Central Government under s. 31(1).

§ See section 31(1) proviso and Notes thereunder.

The approval of the Central Government need not be previous approval and it can be obtained even after the change of name. *Bihari Mills Ltd., In re,* (1985) 58 Com Cases 6, 28 (Guj). If it is discovered after the certificate is issued embodying the altered name, that a special resolution required by the Act was not properly passed, an application may be made to the Registrar to vacate the registration. *Australasian Mining Co., Re,* (1893) WN 74.

Where a company's business was nationalised it was not allowed to change its name to enable it to carry on the same business. *Surendra Nath Shukla v. Indian Airlines Corporation,* AIR 1966 Cal 272.

Change of name of Banking Company

In the case of a banking company a certificate of 'no objection' for the change of name is also required from the Reserve Bank before approval of the Central Government is granted. See section 49-B of the Banking Companies Act, 1949 (as amended by the Banking Companies (Amendment) Act, 1959 and *Departmental Circular No.* 28(12)—CL-IV, dated 24-12-1960.

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1. Necessary applications may be made in Form 1A of the Co's. (Central Govt.'s) General Rules & Forms, 1956 accompanied by a Fee of Rs. 500/- *vide* R. 4A(1) of the Rules.
2. Ins. by Act 31 of 1965, s. 6 (w.e.f. 15-10-1965).

Prior RBI approval for change in names of NBFC

RBI Circular dated 13-01-2000.—Instances have been brought to our notice of some NBFCs changing their name, more particularly to add infotec tag with a view to taking advantage of the capital market sentiments, which may not only jeopardise the interest of the depositors, but also of the investors. Such a change in the name and the business plan of the company may also result in the principal business of the NBFC becoming non-financial, thereby affecting its eligibility for grant and holding of certificate of registration under section 45-IA(4) of the RBI Act. It has, therefore, been decided in the public interest that an NBFC intending to change its present name would need to obtain prior permission of RBI before approaching the Registrar of Companies for change of name. Any violation of these directions would attract serious action against the company as provided for under the RBI Act including cancellation of the certificate of registration if already granted, or rejection of its application for registration, as the case may be. [*Circular No. DNBS (PD) CC No. 12/02.01/99-2000 dt. 13-1-2000 issued to NBFCs and RNBCs by RBI*].

Department's Guidelines regarding change of name

In considering applications for change of name not from conversion of private into public or public into private company, the Central Government considers the following points:—

(1) whether the reasons are sufficient,

(2) whether the proposed name is in consonance with the principal objects of the company and with the kind or kinds of business actually carried on, and

(3) whether the proposed name is not undesirable.

A company seeking to change its name or the promoters of a company under a proposed name may make application to the Registrar of Companies of the State in which the registered office of the company or of the proposed company is or is to be situate, for information as to whether the changed name or the name with which the proposed company is to be registered, as the case may be, is undesirable within the meaning of section 20. Every such application shall be in Form No. 1-A and be accompanied by a fee of Rs. 500 and the Registrar of Companies shall furnish the required information ordinarily within fourteen (now seven days w.e.f. 21-3-1995 *vide* amended R. 4A of the Companies (Central Govt.'s) General Rules & Forms, 1956) days of the receipt of the application.

Where the Registrar of Companies informs the company or the promoters of the company that the changed name or the name with which the proposed company is to be registered, as the case may be, is not undesirable, such name shall be available for adoption:

(*a*) by the said company for a period of six months or,

(*b*) by the said promoters of the company for a period of six months *vide Notification No.* GSR 283(E), dated 21-3-1995, w.e.f. 21-3-1995 *vide* amended R. 4A (*earlier 3 months*), from the date of intimation by the Registrar. *Cf.* The Companies (Central Government's) General Rules and Forms, 1956, Rule 4-A (See *Appendix* 1).

Approval policy about change of name on adoption of new business—Department's instructions.—In case the change in the name of the company is being proposed with a view to undertaking a new line of business not presently authorised by the memorandum, the change of name should be allowed only after necessary amendments have been made in the memorandum of association and duly approved by the Company Law Board. (*Extract from the Seventh Annual Report* year ended 31st March, 1963.)

Department's Guidelines as to change of name.—Generally it is advisable to consult the Registrar of Companies before taking the contemplated step to change the name and seeking Central Government's approval therefor. Text of the Department's Guidelines issued in this regard are reproduced hereunder:

Guidelines regarding change of names.—Section 21 of the Companies Act lays down that a company may, by special resolution and with the approval of the Central Government signified in writing, change its name. A reference is also invited to this Department *letter No.* 8/21/56-PR, dated the 6th February, 1957, informing that for any change of name of a company involving the deletion or addition, as the case may be, of the word 'Private' as a result of its conversion from a private limited company into a public limited company or *vice versa*, the approval of the Central Government should be obtained under section 21. As it has been observed that applications under this section received in the Department do not always contain full particulars necessary to enable Government to take decision without further reference to the parties concerned, the nature of the information/documents required to be furnished by the applicants is indicated in the succeeding paragraphs for the information and guidance of all concerned.

In considering an application for change of name not resulting from conversion, the Central Government generally examines it from the following angles:

(i) Whether the reasons adduced by the company for the change of name are sufficient;

(ii) Whether the proposed name is in consonance with the principal objects of the company as set out in its memorandum of association and with the business actually carried on by it, where such consideration is relevant; and

(iii) Whether the proposed name is not undesirable.

As regards (i) and (ii), the question is decided on the merits of each case. As regards (iii) the proposal is considered in the light of the principles set out in Annexure 'A' [Annexure 'A' not reproduced as irrelevant] to this letter. These principles are however, not exhaustive but only illustrative, their main object being to ensure that a company does not adopt a name likely to mislead the public, that the proposed name is inoffensive and is consistent with the resources and objects of the company. The companies will therefore be well-advised to consult the Registrar of Companies concerned in the first instance with a view to ascertaining whether the name proposed to be adopted by them would be available for registration. While making much consultation they should furnish the particulars specified in Annexure 'B' to this letter in duplicate. [(Annexure 'B' not reproduced as irrelevant)].

In the case of a Banking company, if it desires to change its name as a result of its decision to give up the business of Banking, it is required first to alter its memorandum of association so as to eschew the business of banking as defined in section 5(1)(b) of the Banking Companies Act, 1949 and apply to the Central Government under section 21 of the Companies Act only after effecting the said alteration in accordance with the requirements of law. In such cases, the applicant company should also attach a copy of a certificate from the Reserve Bank of India that the Bank has no objection to the proposed change.

All applications for change of name, not resulting from conversion should be made after passing the necessary special resolution and accompanied by the following particulars:

(a) Detailed reasons for the change of name;

(b) An uptodate copy of the memorandum and Articles of association;

(c) A copy each of the balance-sheet and profit and loss account for the last two financial years;

(d) A certified copy of the communication received from the Registrar in token of his having recorded the special resolution in terms of section 192 of the Act; and

(e) Where the change is as a result of alterations in the objects of the company as set out in its memorandum of association, whether or not a certified copy of the Court's order under section 17 has been filed with the Registrar and the requisite certificate of registration obtained from him under section 18 of the Act.

As regards the change of name due to conversion, it has been decided that in future the company concerned should furnish all the particulars set forth in Annexure 'C' to this letter. It is also required to pass a separate special resolution in terms of section 21 of the Act. [Annexure 'C' Not reproduced as irrelevant].

Departments' Guidelines for deciding cases for availability of names

§ See Notes under Section 20 *ante*.

Abbreviated names of companies and approval by ROC

Department's Circular, dated 16-2-1995.—Presently, there is a restriction on use of abbreviated names (like ITC Limited) in case of existing companies requiring approval of the Regional Director concerned. No such approval of Regional Director will now be necessary and ROCs may take a final decision on such applications in the light of existing guidelines. (*Para* iii). [*Circular No.* 1/95, *F.No.* 14/6/94-CL-V, dated 16-2-1995].

Note.—Earlier to the above position, the Departments' Circular was as follows:

Department's Circular, dated 31-3-1993 and Press Note, dated 5-5-1993.—As per existing guidelines, the companies well-known in their respective field by abbreviated names, are allowed to change their names by way of abbreviation (*e.g.* ABC Ltd.) with the approval of the Department of Company Affairs after following the requirement of Section 21 of the Companies Act, 1956. It has now been decided that any such change of name will require only the approval of Regional Director concerned. The companies will, however, continue to make applications in Form No. 1A for availability of the proposed changed names to the concerned Registrar of Companies. It may be noted that the abbreviated name will not be allowed for adoption by a new company proposed to be incorporated under the Act [*Press Note No.* 1/93, dated 5-5-1993]. To the same effect *Circular No.* 4/93; *F.No.* 3/14/93—CL-V, dated 31-3-1993.

Change of name during pendency of petition under section 17

Department's Circular.—I am directed to state that it has come to the notice of the Department that in Northern and Eastern Regions, sometimes the Registrars of Companies are permitting change of name of a company based on the company pursuing certain provisions listed in "other objects" as contained in its Memorandum of Association. This change of name is being done while a petition is already lying before the Company Law Board for shifting "object/s" given in "other objects" to main objects in Memorandum of Association. The aforesaid action of the Registrar of Companies amounts to pre-judging the issue particularly when the matter is pending before Company Law Board under section 17 of the Companies Act, 1956, for approval of CLB for shifting a provision from other objects to the main objects clause in MOA. In view of the above circumstances, you are advised not to permit change of name during the pendency of a petition under section 17 of the Act before Company Law Board. [*Circular No.* 4/96; *F.No.* 3/7/96-CL-V, dated 13-5-1996].

Note.—This Circular should now be taken in the light of the Companies (Amendment) Act, 1996 which has permitted the companies to change their objects without sanction of CLB and therefore there are going to be no pending proceedings for CLB sanction for alteration of objects.

Effect of change of name

The change of name does not affect the entity of the company or its continuity as the same entity. It remains for all practical purposes the same entity with the same rights, privileges and liabilities as before. *Pioneer Protective Glass Fibre (P.) Ltd. v. Fibre Glass Pilkington Ltd.*, (1986) 60 Com Cases 707 (Cal—DB). This becomes further clear from the fact that the courts have been holding that proceedings commenced by the company in its former name can be continued under its new name. *Solvex Oils and Fertilizers v. Bhandari Cross-Fields (P.) Ltd.*, (1978) 48 Com Cases 260 (P & H); *Gur Narain Jagat Narain & Co. v. Motor & General Sales Ltd.*, 1980 All LJ 508 (All). (Dealing with deemed public company, changing name by dropping word, 'Private').

§ Also refer Notes under section 23(3), *ante.*

Listing companies to notify stock exchange

Where the company's shares are listed on any stock exchange, the change of name must be notified to the exchange.

Delegation of powers to Registrar.—The powers of the Central Government under this section have been delegated to the Registrar of Companies. (*Notification* GSR No. 507(E), dated 24-6-1985).

§ See Notes under section 637.

Modification in reference to Government Companies.—To section 21 the following proviso shall be added:

"*Provided* that nothing in this section shall apply to a Government Company where the change in its name consists only in the deletion of the word 'Private' therefrom". *Notification* GSR No. 1649, dated 13-11-1965.

Prescribed Form

Every application for seeking change of name shall be made in Form No. 1-A accompanied by a fee of Rs. 500/- and the Registrar shall furnish the required information within a period of 7 days [cf Rule 4A].

The proposed change name shall be available for adoption by the company within a period of 6 months from the date of intimation by the Registrar. See Form 1A and Rule 4A in *Appendix* 1.

Secretarial Action Points for change of name by company

1. Call a Board meeting, decide on the change of name and apply to the concerned ROC for availability of name in Form No. 1A. For speedy clearance, three or four names

may be suggested. In this regard, follow the guidelines issued by the Central Government and ensure that the name does not violate the provisions of the Emblems and Names (Prevention of Improper Use) Act, 1950. [Refer *Appendix* 290].

2. After the proposed change of name is made available by ROC, hold a Board meeting for approving the day, date, venue and notice of general meeting for passing a special resolution for change of name and for changes being made in the Memorandum and Articles of Association of the Company.

3. Send notice of the general meeting to the shareholders, auditors and 3 copies each to the stock exchanges where the company is listed.

4. Hold a general meeting and pass a special resolution.

5. File Form 23 with ROC within 30 days of passing of the resolution.

6. File 6 copies of the amendments to the memorandum with the stock exchanges where listed.

7. Apply to the ROC for approval of change of name. No format has been prescribed but the application should be accompanied by the following documents:—

(a) detailed reasons for the change of name,
(b) a certified true copy of the amended memorandum and articles,
(c) a certified true copy of the annual report of the company for the last two financial years,
(d) a certified copy of the confirmation from the ROC regarding availability of the new name,
(e) a certified copy of the special resolution,
(f) a certified copy of the receipt issued by the Registrar acknowledging the filing of the special resolution,
(g) payment of application fees in cash or demand draft in favour of the Registrar of Companies.

8. On approval being accorded for change of name, ROC shall issue a fresh certificate of incorporation and obtain the same.

9. Make necessary changes in every copy of the memorandum and articles, books, records, documents, registers, letter-heads and sign boards of the company.

10. Arrange for a new common seal, adopt the same in a Board meeting and keep the old common seal under lock and key.

11. Affix a rubber stamp of the new name on all the share certificates/debenture certificates/letters of allotment issued by the company as and when they are received for transfer, etc.

Secretarial Practice Notes:

(a) *Check whether*:
  (i) a board resolution has been passed?
  (ii) an application made to the Registrar in Form No. 1A along with a fee of Rs. 500 for ascertaining the availability of proposed name and the Registrar has approved the name?
  (iii) a special resolution is passed and Form 23 duly filed with the Registrar?
  (iv) approval of the Registrar obtained?
  (v) fresh certificate of incorporation obtained from the Registrar?
  (vi) intimation sent to the stock exchange in the case of listed companies?
(b) Ensure that the name was changed on the name board, seal, business letters, bill heads, memorandum and articles etc. (section 147).

Documents Involved: (1) Minutes of Board/General Meeting, (2) Approval letter of Registrar of Companies, (3) Forms 1A and 23, (4) Fresh Certificate of Incorporation, (5) Intimation to Stock Exchange, (6) Memorandum and Articles as altered.

S. 22. Rectification of name of company.—*(1)* [1][*If, through inadvertence or otherwise, a company, on its first registration or on its registration by a new name, is registered by a name which,—*

(i) in the opinion of the Central Government, is identical with, or too nearly resembles, the name by which a company in existence has been previously registered, whether under this Act or any previous companies law, the first-mentioned company, or

(ii) on an application by a registered proprietor of a trade mark, is in the opinion of the Central Government identical with, or too nearly resembles, a registered trade mark of such proprietor under the Trade Marks Act, 1999, such company,—]

(a) may, by ordinary resolution and with the previous approval of the Central Government signified in writing, change its name or new name; and

(b) shall, if the Central Government so directs within twelve months of its first registration or registration by its new name, as the case may be, or within twelve months of the commencement of this Act, whichever is later, by ordinary resolution and with the previous approval of the Central Government signified in writing, change its name or new name within a period of three months from the date of the direction or such longer period as the Central Government may think fit to allow.

[2][*Provided that no application under clause (ii) made by a registered proprietor of a trade mark after five years of coming to notice of registration of the company shall be considered by the Central Government.*]

(2) If a company makes default in complying with any direction given under clause (b) of sub-section (1), the company, and every officer who is in default, shall be punishable with fine which may extend to [3][*one thousand rupees*] for every day during which the default continues.

NOTES

Eng. Act, 1948 : Sec. 18(2)
Eng. Act, 1985 : Sec. 28(2)

Previous Act : Sec. 11(2)

Changes made by Trade Marks Act, 1999

This section has been amended by the Trade Marks Act, 1999. The amendment has increased the power of the Central Government to order rectification of name where it con-

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1. Subs. by the Trade Marks Act, 1999, s. 158 and Sch for the following :
'If, through inadvertence, or otherwise, a company on its first registration or on its registration by a new name, is registered by a name which, in the opinion of the Central Government, is identical with, or too nearly resembles, the name by which a company in existence has been previously registered, whether under this Act or any previous companies law, the first-mentioned company—'
2. Ins. by the Trade Marks Act, 1999, s. 158 and Sch.
3. Subs. for the word "one hundred rupees" by the Companies (Amendment) Act, 2000 (53 of 2000), s. 8 (w.e.f. 13-12-2000).

stitutes an infringement of a registered trade mark. The new provision is that the proprietor of the registered trade mark may make an application to the Central Government for an order for rectification of name because it is identical with or too nearly resembles the applicant's registered trade marks. Such application must be made within five years from the date on which the registration of the company with offensive name comes to the notice of the registered trade mark owner.

As to what constitutes infringement of registered trade marks, see sec. 29 of the Trade Marks Act, 1999.

Companies (Amendment) Act, 2000

The Amendment Act of 2000 enhanced the penalty amount from one hundred rupees to one thousand rupees. Sub-section (2) was accordingly amended.

Compulsory change of name on Central Government's direction

This section makes a thorough change in the procedure as regards rectification of name of a company and also confers power on the Central Government to compel a change of name, penalising default in compliance with its direction.

Where the company challenges the directions of the Central Government, the court would have to be convinced not merely that the name was misleading but also that harm might result if it were not changed. In *Association of Certified Public Accountants of Britain v. Secretary of State for Trade and Industry,* 1997 2 BCLC 307 : (1998) 1 WLR 164 the court confirmed a direction to the Association to change its name. The form of harm to the public which was identified in the case was that people would be likely to pay more for the services of members of the Association because of the word 'Certified' in its name, which was said to give a misleading impression of the level of qualification required of members.

From the wording of the section, it appears that the Central Government can compel a company to change its name only if the name is identical with or too nearly resembles that of an existing company but not on ground on which registration could have been refused in the first instance under S. 20.

In an English case, the Diabetic Society was required to change its corporate name to something that did not impinge upon the goodwill of The British Diabetic Association. There was sufficient similarity between these two names to necessitate a change, even though there was no intention to mislead the public. *British Diabetic Association v. The Diabetic Society,* (1995) 4 All ER 812. Further the power must be exercised within twelve months of registration of a new company or changed name of an existing company. Reason for this provision is supported in BUCKLEY ON THE COMPANIES ACT, 14th Edn. 1981, p. 62. After twelve months the Central Government cannot exercise the powers and ordinary procedure for alteration of name would have to be followed. The aggrieved company may resort to civil proceedings to compel change of the name.

There is no provision anywhere for an extension of this period of 12 months and the court cannot be called upon to extend it by resorting to the writ of mandamous *Sidhvi Constructions (India) P. Ltd. v. ROC, Hyderabad,* (1997) 90 Com Cases 299 : (1997) 1 Comp LJ 339 (AP). The court cannot be called upon to pass orders either under writ jurisdiction or otherwise which are against the law. *Hope Textiles P. Ltd. v. Union of India,* (1994) 205 ITR 508 : 1995 Supp (3) SCC 199. The only remedy which survives after the expiry of the period is a court action to restrain the use of the name and passing off. *Concord Intrenational (Mauritius) Ltd. v. Concorde Tourist Guide Agency Ltd.*, (1985) LRC (Comm) 751 (Mauritius CA).

A company was registered at Madras with the word "Kilburn" as a part of its name for which permission was granted by a Calcutta based company. The Madras company floated two other companies in Madras and got them registered with the word "Kilburn" as part of name. It was found as a fact that the permission given by the Calcutta company did not ex-

tend to the two new companies. An order issued to such companies to change their names was held to be justified. *Kilburn Electricals Ltd. v. Regional Director, CLB* (2000) 99 Com Cases 243 : (2000) 6 Comp LJ 351 (Mad). A similar rectification order passed in *Kalpana Polytech India Ltd v. Union of India,* (1998) 16 SCL 207 (Cal) was held to be justified. The word "Kalpana" was already part of the petitioner company's name and the respondent company was prevented from using it as a part of its name. It was further held that the court could not in a writ petition go into the question of evidence and interfere with the order. The decision in *Kalpana case* was **reversed** on appeal by the Division Bench in *Kalpana Polytec India Ltd. v. UOI,* (2001) 106 Com Cases 558 : (2001) 45 CLA 40 : (2001) 34 SCL 710 (Cal—DB), the Bench being of the view that the decision of the Regional Director as upheld by the single judge was in the nature of prevention of passing off. The Regional Director is not competent to consider the intricacies and technicalities of a passing off action. The word "or otherwise" should be construed *ejusdem generis* with the preceding word "inadvertence". Hence, if a name has been registered with a state of mind akin to inadvertence only then the power under s. 22 will be available to the Regional Director. In other cases, the matter would have to go in for a civil court adjudication.

Where the name of the respondent company included the registered trade mark of the petitioner company without its consent, the court ordered cancellation of the registration of the respondent company. The court further directed that before cancelling the registration, the Registrar of Companies should permit the change of name of the respondent company, if it applies for the same in accordance with law before him within 16 days from the date of the order, provided the new name as suggested was not violative of the provisions of section 20 or any other law, for the time being in force.

The power of the Central Government under the section can be exercised within the twelve-month period only. In counting this, the period of any court stay order in the matter would be excluded. *Sen & Pandit Electronics Ltd. v. Union of India* AIR 1999 Cal 289 : (2000) 36 CLA 68 : (2003) 115 CC 299 : (2002) 6 CLJ 96 : (2004) 49 SCL 618 (Cal).

In *New Zealand Conference of Seventy-Day Adventists v. ROC,* (1997) 1 NZLR 751 (HC), the Seventh-Day-Adventists Church operated as unincorporated society. Some members of the church decided to form a company to promote vegetarianism and organic farming under the name "Seventh-Day-Adventist Resource Centre Ltd." The church asked them to remove the words "Seventh-Day Adventist" so as to remove any suggestion of association with the Church. They aksed the Registrar to direct the company for compulsory change of name. The Registrar replied declining to direct a change. The church appealed to the High Court. The appeal was dismissed. The court held as follows:

1. In cases such as this the relevant test against which names were to be measured was the test specified in the statute, that is to say, whether the name should not have been reserved at the time of incorporation. The starting point was the state of the legislation in 1991.
2. The proper approach to an application of the modified test for "undesirability" properly involved the question whether a name was undersirable:
   (a) because its use would contravene an enactment; or
   (b) because it was identical to, or almost identical to, the name of another company or name reserved for another company; or
   (c) because in the opinion of the Registrar, it was offensive; or
   (d) because there was some other exceptional circumstance which would make use of the name undesirable.

The Court in the *Seventh-Day Methodist* case was also not convinced that the name involved any statutory violations. The court said: Before it could safely be predicated that the use of a name would contravene the Fair Trading Act it must be possible to postulate with confidence that there would be no way in which the name could be used without contravening the Fair Trading Act. It was not possible at the time of reservation to state

that this was a name "the use of which would contravene" the Fair Trading Act. The court **applied** the ruling in *George v. Registrar of Companies*, (1981) 2 NZLR 237 and *Black v. Fulcher*, (1988) 1 NZLR 417 (CA).

Reasoned order necessary.—Explaining the nature of the power under the section and the manner in which it ought to be exercised, the Gujarat High Court stated as follows: "In the matter of exercise of powers under Section 22 of the Act, since a final order passed under Section 22 of the Act results into civil consequences, the order must be passed by observing the principles of natural justice, but in the present case the order is only a non-speaking order. Furthermore, when the Registrar had granted registration and when the question is of change or giving direction to the company to change the name it can also be said that the direction to the company under Section 22 of the Act is in the nature of quasi-judicial power and, therefore, the authority taking decision must record the reasons so that all concerned can come to know that on what ground the order is passed. In the instant case, since no reasons, whatsoever, have been recorded, it can be assailed by the petitioner on the ground that the order is without proper application of mind. In the result the order dated 26-9-2000 is quashed and set aside only on the ground that the same does not record reasons for passing final order with further clarification that it will be open to the respondent No. 1 to move the respondent No. 2 (Central Government) for reconsidering the matter afresh after giving opportunity of hearing to the petitioner and it will also be open for respondent No. 2 to record reasons for passing the order and then pass final order under Section 22 of the Act." *Pino Bisazza Glass P. Ltd. v. Bisazza India Ltd.*, 2002 CLC 1560 (Guj).

Restraint of misleading names through injunctions and passing off actions

The registration of a name under company law does not provide efficient protection against an action at common law for an injunction at the suit of anyone prejudiced by the adoption of the name. Such action is normally founded on: (1) contract; or (2) the tort of passing off.

A company, or individual controlling a company, may contract not to use a particular name. If this undertaking is broken and the company is registered under that name, an injunction restraining the company from using that name may be claimed.

Where the objection to the corporate name of the defendants on the ground that it infringe their name was taken by the plaintiff seven years after the incorporation of the company by the defendants, no interim injunction was issued against the use of the corporate name by the defendants. The balance of convenience lay in their favour. The doctrine of acquiescence as also the doctrine of honest and concurrent user was attracted to the matter. *Atlas Cycles (Haryana) Ltd. v. Atlas Products (P.) Ltd.*, (2003) 53 CLA 22 (Del). The Court said that it has to see whether there is deceptive resemblance between the plaintiff's and the defendant's marks and the resemblance is such as is likely to cause confusion in the market or in the mind of the purchaser. It can be a fit case for restraining the defendant from using the offending trade mark. On facts, the court restrained the use of the word 'Atlas' after prefacing with 'House of', that is House of Atlas'. *Ibid.*

§ See commentary under S. 20 under the heading "Court's power to restrain use of similar names".

Delegation of power to Regional Directors.—The powers of the Central Government under this section have been delegated to the Regional Directors. (*Notification* GSR No. 288(E), dated 31-5-1991.) (See Notes under section 637).

Section 22(1)(i) does not contemplate any application being made. In the absence of any prescribed format, the aggrieved (old) company may make the complaint by way of a letter, to the Regional Director, who may pass order after giving a hearing to the newly incorporated company. Section 22(1)(ii) requires an application to be made by the owner of a registered trade mark. In terms of the proviso to sub-section (1), the limitation period is 5 years from the date on which the applicant comes to know of the infringement.

Penalty for default [sub-section (2)]

Default in complying with the direction given by the Regional Director to rectify the name of the company is punishable with fine which may extend to Rs. 1000/- for every day during which the default continues. This is a continuing offence and is not subject to any bar of limitation in filing prosecution.

Compoundable Offence.—The offence is compoundable under section 621-A.

Secretarial Practice Notes:

(a) Check whether any rectification of name by the company *suo motu* or at the instance of the Regional Director was effected ? If so, check whether:
   (i) the previous approval of the Regional Director was obtained or the Regional Director directed the company to effect the change in name of the company?
   (ii) an ordinary resolution was passed?
   (iii) a fresh certificate of incorporation obtained from the Registrar?

(b) Ensure that the name has been changed on the name board, seal, memorandum, articles, letters, bill heads etc. (Section 147).

Documents Involved: (1), Minutes of Board/General Meeting, (2) Approval of Regional Director, (3) Fresh Certificate of Incorporation, (4) Intimation to stock exchange, (5) Altered Memorandum and Articles, (6) Common Seal of the Company.

Secretarial Action Points for rectification of name on Central Government's directions

Ensure that the direction of the Central Government for change of name is issued within twelve months of registration and the name of the company is identical with or resembles the name of an existing company.

S. 23. Registration of change of name and effect thereof.—(1) Where a company changes its name in pursuance of section 21 or 22, the Registrar shall enter the new name on the register in the place of the former name, and shall issue a fresh certificate of incorporation with the necessary alterations embodied therein; and the change of name shall be complete and effective only on the issue of such a certificate.

(2) The Registrar shall also make the necessary alteration in the memorandum of association of the company.

(3) The change of name shall not affect any rights or obligations of the company, or render defective any legal proceedings by or against it; and any legal proceedings which might have been continued or commenced by or against the company by its former name may be continued by or against the company by its new name.

NOTES

English Act, 1948 : Sec. 18(3) & (4) Previous Act : Sec. 11 (5) & (6)

Inaccurate description of name

Mistake in or inaccurate description of the name of a company will not make a contract of the company unenforceable if the company is otherwise identifiable from other facts

and circumstances. In this respect a company is in the same position as a natural person. A company, even like any natural person, has also other characteristics than its mere name, by reference to which it can be identified, such as the kinds or classes of business it carries on, place of its registered office, place or places where it carries on its business, particular shareholders and particular directors associated with it, etc. See *Goldsmith (F.) (Sicklesmere) Ltd. v. Baxter,* (1970) 40 Com Cases 809 : (1969) 3 All ER 733. See also, *John Wilkes (Footwear) Ltd. v. Lee International (Footwear) Ltd.,* 1985 BCLC 444 (CA) which decides that liability is not absolute and that a person would only be liable if he authorises the signing of a document in such a way that the name of the company does not properly appear or, in other words, only culpable corporate officers may be liable.

Effect of change of name upon legal proceedings [Sub-section (3)]

Sub-section (3) protects only the continuance of pending legal proceedings which had been commenced by the company in its former name. It will not protect legal proceedings commenced in such former name, after the change of name has been effected and registered in the register of joint stock companies by the Registrar, even though the mistake was *bona fide.* See *Malhati Tea Syndicate Ltd. v. Revenue Officer, Jalpaiguri,* (1973) 43 Com Cases 337 : AIR 1972 Cal 78.

The change of name does not affect the entity of the company or its continuity as the same entity. It remains for all practical purposes the same entity with the same rights, privileges and liabilities as before. Even where a proceeding has been instituted in the old name, it will not be regarded as a proceeding instituted in the name of a company which is not in existence. It would be a mere case of misdescription of name. The Calcutta High Court has expressed this opinion in *Pioneer Protective Glass Fibre (P.) Ltd. v. Fibre Glass Pilkington Ltd.,* (1986) 60 Com Cases 707 (Cal) (DB). See also *Kalipada Sinha v. Mahalaxmi Bank Ltd.,* AIR 1966 Cal 585 : (1962) 32 Com Cases 511, (name allowed to be substituted at the execution stage); *Jai Jai Ram Manohar Lal v. National Building Material Supply,* AIR 1969 SC 1267, (amendment of name allowed before the decree); *Purshottam Umedbhai and Co. v. Manilal & Sons,* AIR 1961 SC 325, (rectification of name allowed); *Patel Roadways (P.) Ltd. v. Bata Shoe Co. (P.) Ltd.,* (1979) 2 Cal HCN 279; (a partnership firm becoming a company, substitution of name allowed in pending proceedings; also to the same effect) *Shree Choudhary Cold Storage, (1972) v. Ruby General Insurance Co. Ltd.,* AIR 1982 Cal 124 : (1983) 54 Com Cases 639. All these authorities clearly demonstrate that a change of name does not bring into existence a new company. The company remains the same entity as it was before. Only the name changes. A new certificate of incorporation has no doubt to be issued but that does not incorporate a new company.

The same principles apply where a private company converts itself into a public limited company. It may continue its existing proceedings in its new name. *Solvex Oils and Fertilizers v. Bhandari Cross Fields (P.) Ltd.,* (1978) 48 Com Cases 260 (P & H). A private company, deemed to be a public company under S. 43A and therefore changing its name by dropping the word 'Private' can continue the existing proceedings under its altered name. *Gur Narain Jagat Narain & Co. v. Motor & General Sales Ltd.,* 1980 All LJ 508 (All). That rights and liabilities are not at all affected by change of name is further demonstrated by Division Bench of Calcutta High Court in *Economic Investment Corpn. Ltd. v. CIT, (WB),* AIR 1970 Cal 389 : (1970) 40 Com Cases 1. Income Tax authorities were allowed in this case to attach the assets of a company in the hands of a bank though they were deposited with the bank in the company's old name. Decree can be executed in the new name or in the old name of the company: *Abdul Qayum (F.S.) v. Manindra Land and Building Corporation Ltd.,* (1955) 25 Com Cases 143 : AIR 1955 All 192. See also *Srinivasaiah D. v. Vellore Varalakshmi Bank Ltd.,* (1954) 24 Com Cases 55 : AIR 1954 Mad 802. Where the change of address of the company was not communicated to the Registrar, the absence of service of notice at the old address could not be excused. *Janbazar Manna Estate Ltd., Re,* (1931) 1 Com Cases 243, 248 (Cal).

Mutation of name in other company's register of members.—The company which has changed its name would be entitled to ask those companies in which it is holding share to substitute a company's new name in their register of members in place of the old name. *Sulphur Dyes v. Hickson & Dadajee Ltd.*, (1995) 83 Com Cases 533 (Bom).

English Law.—The position is thus stated in PENNINGTON'S COMPANY LAW, 72 (Fifth edn. 1985) : p. 75, 7th Edn, 1995 : "In civil proceedings the name of the defendant company must be amended when the plaintiff learns of the change of name, but it appears that he may make the amendment as of right, and in cases where leave of the court is necessary, leave will be given as of course. See *Mitchell v. Harris Engineering Co. Ltd.*, (1967) 2 All ER 682 (CA).

Other formalities on change of name.—Besides requiring the substitution of the new name in the place of the former name in name board and all registers and other books and documents pertaining to the company's business and affairs, the change of name will also necessitate the issuing of new share certificates in the place of the ones issued under the old name, and will also require the renewal of debenture bonds and other credit securities where necessary. There will also have to be effected necessary changes in the charges registered with the Registrar under Part V of the Act. (Sections 125 to 145).

Of course, the first part of sub-section (3) says that the change of name shall not affect rights or obligations of the company and, therefore, creditors and others having had transactions with the company will not be prejudiced by the change of name.

Modification with reference to Government Companies.—In section 23, after sub-section (1), the following sub-section shall be inserted, namely:—

"(1-A) Where the change in the name of a Government company consists only in the deletion of the word 'Private' therefrom, that Government Company shall, not later than three months, from the date thereof, inform the registrar of the aforesaid change and thereupon, the registrar shall delete the word 'Private' before the word 'Limited' in the name of the company upon the register and shall also make the necessary alterations in the certificate of incorporation issued to the Company". *Notification GSR No.* 1649, dated 13-11-1965.

Secretarial Practice Notes.—See Secretarial Practice and Procedure Notes under section 22.

S. 24. Change of name of existing private limited companies.—(1) In the case of a company which was a private limited company immediately before the commencement of this Act, the Registrar shall enter the word "Private" before the word "Limited" in the name of the company upon the register and shall also make the necessary alteration in the certificate of incorporation issued to the company and in its memorandum of association.

(2) Sub-section (3) of section 23 shall apply to a change of name under sub-section (1), as it applies to a change of name under section 21.

NOTES

This section is consequential to clause (a) of sub-section (1) of section 13, so far as existing private companies are concerned.

S. 25. Power to dispense with "Limited" in name of charitable or other company.—(1) Where it is proved to the satisfaction of the Central Government that an association—

(a) is about to be formed as a limited company for promoting commerce, art, science, religion, charity or any other useful object; and

(b) intends to apply its profits, if any, or other income in promoting its objects, and to prohibit the payment of any dividend to its members,

the Central Government may, by licence, direct that the association may be registered as a company with limited liability, without the addition to its name of the word "Limited" or the words "Private Limited".

(2) The association may thereupon be registered accordingly; and on registration shall enjoy all the privileges and (subject to the provisions of this section) be subject to all the obligations, of limited companies.

(3) Where it is proved to the satisfaction of the Central Government—

(a) that the objects of a company registered under this Act as a limited company are restricted to those specified in clause (a) of sub-section (1), and

(b) that by its constitution the company is required to apply its profits, if any, or other income in promoting its objects and is prohibited from paying any dividend to its members,

the Central Government may, by licence, authorise the company by a special resolution to change its name, including or consisting of the omission of the word "Limited" or the words "Private Limited", and section 23 shall apply to a change of name under this sub-section as it applies to a change of name under section 21.

(4) A firm may be a member of any association or company licensed under this section, but on the dissolution of the firm, its membership of the association or company shall cease.

(5) A licence may be granted by the Central Government under this section on such conditions and subject to such regulations[1] as it thinks fit, and those conditions and regulations shall be binding on the body to which the licence is granted, and where the grant is under sub-section (1), shall, if the Central Government so directs, be inserted in the memorandum, or in the articles, or partly in the one and partly in the other.

[2][(6) It shall not be necessary for a body to which a licence is so granted to use the word "Limited" or the words "Private Limited" as any part of its name and, unless its articles otherwise provide, such body shall, if the Central Government by general or special order so directs and to the extent specified in the direction, be exempt from such of the provisions of this Act as may be specified therein.]

(7) The licence may at any time be revoked by the Central Government, and upon revocation, the Registrar shall enter the word "Limited" or the words "Private Limited" at the end of the name upon the register of the body, to which it was granted; and the body shall cease to enjoy the exemption granted by this section:

Provided that, before a licence is so revoked, the Central Government shall give notice in writing of its intention to the body, and shall afford it an opportunity of being heard in opposition to the revocation.

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1. Part B and Part C of the Companies Regulations, 1956 are relevant to this section.
2. Subs. by Act 65 of 1960, s. 9.

[3][(8)(a) A body in respect of which a licence under this section is in force shall not alter the provisions of its memorandum with respect to its objects except with the previous approval of the Central Government signified in writing.

(b) The Central Government may revoke the licence of such a body if it contravenes the provisions of clause (a).

(c) In according the approval referred to in clause (a), the Central Government may vary the licence by making it subject to such conditions and regulations as that Government thinks fit, in lieu of, or in addition to, the conditions and regulations, if any, to which the licence was formerly subject.

(d) Where the alteration proposed in the provisions of the memorandum of a body under this sub-section is with respect to the objects of the body so far as may be required to enable it to do any of the things specified in clauses (a) to (g) of sub-section (1) of section 17, the provisions of this sub-section shall be in addition to, and not in derogation of, the provisions of that section.]

(9) Upon the revocation of a licence granted under this section to a body the name of which contains the words "Chamber of Commerce", that body shall, within a period of three months from the date of revocation or such longer period as the Central Government may think fit to allow, change its name to a name which does not contain those words; and—

(a) the notice to be given under the proviso to sub-section (7) to that body shall include a statement of the effect of the foregoing provisions of this sub-section; and

(b) section 23 shall apply to a change of name under this sub-section as it applies to a change of name under section 21.

(10) If the body makes default in complying with the requirements of sub-section (9), it shall be punishable with fine which may extend to [4][*five thousand rupees*] for every day during which the default continues.

NOTES

Eng. Act, 1948 : Sec. 19
Eng. Act, 1985 : Sec. 30

Previous Act : Sec. 26

Companies Act, 1956

Two important changes to be noted in this section are:

(1) the provision in sub-section (4) enabling a firm as such, though it is not a legal entity, to become a member and enjoy the privileges or membership and

(2) the exemption, as regards any association coming under this section if and to the extent to which the Central Government so directs, from the obligation of sending lists of its members to the Registrar and of maintaining register of directors and intimating

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3. Subs. by s. 9, *ibid*, for sub-section (8).
4. Subs. for the word "five hundred rupees" by the Companies (Amendment) Act, 2000 (53 of 2000), s . 9 (w.e.f. 13-12-2000).

changes therein to the Registrar and otherwise complying with the provisions of section 303.

Recommendations of Company Law Committee.—As regards the first change, it is based on the following recommendation of the Company Law Committee:

Partnership firm may become member.—"Recent judicial decisions have thrown doubt on the point whether a firm, as distinct from a company, can be a member of an association not for profit. We are not unaware of the complications that might result from admission of firms into the membership of associations incorporated under section 26, but we consider that the balance of advantage is distinctly in favour of such admission. For, the usefulness of many associations not for profit is likely to be seriously undermined if important business houses are debarred from participating in the activities of such associations in their own right merely because they are firms and not companies. We, therefore, recommend that this section should be suitably amended to enable firms to be members of associations not for profit. We consider it necessary, however, that those associations should be required to provide in their articles that, on the dissolution of the partnerships the membership of those firms in these associations would also automatically lapse". (*Report*: Para 38).

As regards the second change, it was effected by the Joint Committee with the following explanation:

Power to exempt filing of list of members.—"It was pointed out that if the companies referred to in this clause were exempted from the requirement of submitting lists of their members to the Registrar, no one could find out who were, in fact, members of that company and that this might lead to undesirable and harmful results. The power to grant this exemption has, therefore, been vested in the Government so that they might use their discretion in restricting the exemption to deserving cases." (*Report*: Para 17).

Companies (Amendment) Act, 1960

The reason for amending sub-sections (6) and (8) is, thus, given—There are several sections in the Act, provisions of which either cannot be fully complied with by non-profit making companies *e.g.* Chambers of Commerce, trade associations, clubs, etc., because of their peculiar constitution and manner of working, or seldom serve any useful purpose in the case of such bodies. Government, therefore, propose to take power to modify the requirements of such sections in their application to such companies. Most of these sections deal with procedural matters. *e.g.*, holding of meetings, election of directors, proxies, voting by show of hands, etc. [*Notes on clauses*: Clause 9 of the Companies (Amendment) Bill, 1959].

The Joint Committee further, recommended as follows: "The committee feel that the Central Government should have a general power to grant exemption to companies licensed under section 25 of the Act from any provisions of the Act according to the circumstances and exigencies of each case and that the power need not be confined only to the sections mentioned in this clause. The clause has been amended, accordingly." (*Report*: Para 19).

Companies (Amendment) Act, 2000

The Amendment Act of 2000 enhanced the penalty amount from five hundred rupees to five thousand rupees. Sub-section (10) was accordingly amended.

Statement of specified capital not required

A company registered under section 25 before or after the commencement of Companies (Amendment) Act, 2000 shall not be required to have minimum paid up capital specified in Section 3.

Meaning of charitable company and other allied institutions

For the meaning of the words 'charitable and other allied institutions', see section 11 of the Income-tax Act, 1961 as annotated by CHATURVEDI & PITHISARIA, INCOME-TAX LAW, 992-1007 (5th Edition, Vol. I, 1998). It is a question of fact in each case *T. Jacob v. Assessing Authority and Tahsildar, Taluk Office, Trivandrum,* (1989) 1 Comp LJ 97 (Ker).

It is necessary for a company (Stock Exchange in this case) to qualify for exemption under Income-tax Act that there should be in its memorandum or articles a prohibition of distribution of profits among its members *Delhi Stock Exchange Assn. Ltd. v. CIT,* (1997) 12 SCL 133 (SC) **affirming** *Delhi Stock Exchange Assn. Ltd. v. CIT,* (1980) 126 ITR 532 (Del).

Advantages of section 25 companies

Licence to drop the word "Limited" as the last word of the name of the company and yet enjoy the protection of limited liability is an advantage to the company in itself. That is why this privilege is confined to companies which would not distribute their profits among members. This privilege is frequently used by bodies which pursue charitable objects as identified in the section. Other associations, like chambers, clubs, etc. also make use of this privilege. All the advantages of incorporation are enjoyed by such bodies and yet they are free from indicating through their name that they are incorporated with limited liability. Their officers and members enjoy immunity from personal liability. Admission to membership is generally controlled through the decision of the governing body and though the membership of the governing body is through election, the right to contest may be given only to a member who makes a donation. Section 25 companies are allowed to admit to membership even a partnership firm. They also enjoy many other exemptions from the operative provisions of the Companies Act. The Central Government has been vested with the power to grant exemptions.

Clubs registered as Section 25 Companies

Many clubs are registered as Section 25 companies. They do not have a Board of directors but have a management committee which is elected annually. It is submitted that the members of the committee are in the same position as directors of a company. They have the same rights, duties and obligations as prescribed under the Companies Act, 1956 and as laid down in various decisions of courts. Consequently, a member of the committee who fails to disclose his interest under Section 299 will be liable to vacate office in terms of Section 283(1)(i). The committee members also owe a fiduciary duty to the club. They cannot utilise their position to make profit for themselves. If they do so, they will be liable in proceedings for breach of trust.

Section 25 company as holding company

There is nothing in the section to debar a section 25 company from promoting companies and becoming holding companies. Ideally such companies can promote companies with projects with a research orientation having a long gestation; once the projects take off, the section 25 company can divest its holdings and promote another project of similar nature. This can be done without a profit motive.

Obligations and privileges of limited liability companies [Sub-section (2)]

An association registered under the Companies Act, which has been granted a licence under sub-section (1), is subject to all the obligations under the Act, except as exempted under sub-section (6) and is entitled to all the benefits of incorporation and privileges of limited liability.

By virtue of the provisions of S. 68(1) of the Charities Act, 1993 [English], if a Charitable Company's name does not show that it is a charitable organisation then the fact that it is a charity must appear on all business letters, notices, and other publications, bills of exchange, promissory notes, cheques, endorsements and orders for money or goods pur-

porting to be signed for and on behalf of the company and also on conveyances executed by the company and all bills, invoices, receipts and letters of credit. Persons dealing with such companies have to take notice of the fact that the company's contractual capacity is limited. In *Rosemary Simmons Memorial Housing Association Ltd. v. United Dominions Trust Ltd.*, (1986) 1 WLR 1440 : (1987) 1 All ER 281. MERVYN DAVIES J. held that it was beyond the capacity of an incorporated charity to give away its assets to a non-charitable body (presumably this does not refer to gifts to the objects of the charity). All this became necessary because the application of the doctrine of *ultra vires* has been abolished in reference to such companies.

Department's Clarifications

Clarification I.—Applicability of section 293.—In the view of the *Department* there is nothing in section 25 to indicate that the provisions of section 293 would not apply to a company coming within the scope of that section. On the other hand, it is expressly stated in section 25(2) that the companies will be subject to all the obligations of limited companies imposed by the various provisions of the Act. [*Department's File No.* 38/2/68-CL-III.]

Clarification II.—Applicability of section 370 [see now Section 372A]*.—So far as grant of loan is concerned, the same has to be computed with reference to the lending company's subscribed capital and its free reserves. A section 25 company may or may not have share capital. If it has share capital, the provisions of section 370 of the Companies Act, [see now Section 372A]* 1956, become applicable in the same manner as they are applicable to any other company. In case it does not have share capital and is a guarantee company simpliciter, even then it can have free reserves, and percentages under section 370 [see now Section 372A]* can be computed in relation to such free reserves alone. Hence, in either case, the provisions of section 370 [see now Section 372A]* become applicable to the grant of loan by a section 25 company.

2. As regards giving guarantee or providing security by a company, the existence of share capital or free reserves is not relevant and as such in these cases, the provisions of section 370 [see now Section 372A]* are also attracted.

3. In view of the above, it appears that provisions of section 370 of the Act [see Now Section 372A]*, are applicable to a section 25 company, unless it qualifies for an exemption under sub-section (2) of section 370 of the Companies Act, 1956. [see Now Section 372A]* [*Department's File No.* 1/6/88-CL-V, dated 28-4-1989.]

Note : *Section 370 ceased to be operative w.e.f. 31-10-1998. The legal position stated in the Clarification continues to be valid by virtue of the provisions of section 372A which came into operation w.e.f. 31-10-1998.

Grant of licence to an existing company [Sub-section (3)]

An existing company can avail itself of the privileges under this section by restricting its objects for non-profit making purposes as specified in sub-section (1). The company will have to pass a special resolution and to seek the approval of the Central Government for change of its name, including for deletion of the words "Limited" or "Private Limited", as the case may be. For alteration of its object clause, a special resolution and the approval of the Company Law Board will be necessary.

Membership, transfer of Interest etc.

§ For detailed Notes on the point see under section 37.

Partnership firm as member [Sub-section (4)]

Though a firm is not a legal person like a body corporate, sub-section (4) of this section enables firms to become members of any association registered under this section such as a chamber of commerce or social club or charitable institution and enjoy all such privileges as are enjoyed by bodies corporate which become members of such associations. But by reason of their firms being members, the individual partners of such firms cannot claim the status and privileges of membership for each of them. For instance, if the articles of association or other regulations prescribe that only members are eligible for appointment as directors, no partner of a firm which is a member, will be qualified for the appointment, unless he is himself a member in his own right. Thus, the firm is recognised only for the limited purposes of membership of section 25 companies.

Department's Clarification.—"A firm, not being a person, cannot be registered as a member of a company except where the company is licenced under section 25 of the Companies Act, 1956. Companies which have firms registered as shareholders should be advised to take steps to rectify the position within a specified time. In case the irregularity persists, despite a warning, necessary action can be taken under section 150(2) of the Companies Act, 1956." [*Circular No.* 4/72, dated 9-3-1972].

Validation of existing registration of firms as members

Section 640 is enacted in order to validate the registration of firms already registered as members of any association licensed under s. 26 of Act of 1913, so as to date back from the date of registration of the association.

Grant of licence [Sub-section 5]

This section provides for conferment of a special privilege on any association, which is proposed to be formed as a limited company under the Companies Act, for serving public interest, without a profit motive. Firstly, on a licence being granted by the Central Government, such a company becomes exempted from the use of the words 'Limited' or 'Private Limited' as a part of its name: and secondly it enjoys exemption from such of the provisions of the Act as are specified by the Government in this behalf.

Procedure for making application for grant of licence

The Companies Regulations, 1956 prescribe the procedure for making an application to the Regional Director for grant of licence under section 25 to new associations (Regulations 3 to 6) and to companies already registered under the Act as a Limited Company (Regulations 7 to 9) and for publication of general notice in newspaper (in the form set out in Annexure II).

§ For text of the Companies Regulations, 1956 refer *Appendix* 2.

Department's Circular.—For Department's instructions as regards procedure for dealing with application for grant of licence under this section refer *Appendix* 9.

Power of exemption [Sub-section (6)]

The Central Government has been conferred with a general power to grant exemption from any provision of the Act according to circumstances and exigencies, and the said power is not confined only to particular sections.

Certain special exemptions are also provided by section 263-A. The provisions of the Act relating to voting by show of hands (section 177), retirement of directors by rotation (sections 255 and 256), and appointment of directors by individual voting (section 263) are not to apply to companies coming under this section.

In exercise of the powers conferred by sub-section (6) of section 25 of the Companies Act, 1956 (1 of 1956), the Central Government has directed that a body to which a licence is granted under section 25 aforesaid shall be exempt from the provisions of the said Act specified in column (1) of the Table below to the extent specified in the corresponding entries in column (2) of the said Table.[1]

TABLE

Provisions of Act		*Extent of exemption*
Section 2(45)	...	[2]In so far as it required the appointment of an individual to perform the duties which may be performed by a secretary under the said Act and any other ministerial or administrative duties only if he possesses the prescribed qualifications.
Section 147	...	The whole.

1. *Vide* SO 1578, Published in the Gazette of India, Part II, sec. 3 (ii) on 8th July, 1961; SO 2767, dated 5-8-1964; GSR 73, dated 30-12-1965, S.O. 35(E), dated January 9, 1976.
2. *Vide Notification No.* SO 35(E), dated January 9, 1976.

Provisions of Act		*Extent of exemption*
Section 160 (1)(aa)	...	The whole.
Section 166(2)	...	The whole, provided that the time, date and place of each annual general meeting are decided upon before-hand by the Board of Directors having regard to the directions, if any, given in this regard by the company in general meeting.
Section 171(1)	...	A general meeting may be called by giving a notice in writing of not less than 14 days.
[3]Section 193	...	Minutes may be recorded within 30 days of the conclusion of every meeting in case of companies where the articles of association provide for confirmation of minutes by circulation.
Section 209(4A)	...	Books of account relating to a period of not less than four years immediately preceding the current year shall be preserved.
[4]Section 219	...	Documents referred to in sub-clause (1) may be sent to members not less than fourteen days before the date of the general meeting instead of 21 days.
Section 257	...	Shall not apply to companies whose articles provide for election of directors by ballot.
[5]Section 259	...	The whole.
Section 264(1)	...	The whole.
[6]Section 280	...	The whole.
Section 282	...	The whole.
Section 285	...	Shall apply only to the extent that the Board of Directors, Executive Committee or Governing Committee of such companies shall hold at least one meeting within every six calendar months.
Section 287	...	Shall apply only to the extent that the quorum for the Board Meeting shall be either eight members or ¼th of its total strength whichever is less provided the quorum shall not be less than two members in any case.
[7]Section 292	...	Matters refered to in clauses (c), (d) and (e) of sub-section (1) may be decided by Board by circulation instead of at a meeting.
Section 299	...	Shall apply only to cases to which sub-sections (1) and (3) of section 297 apply.
Section 301	...	A register shall be maintained only of contracts to which sub-sections (1) and (3) of section 297 apply.
Section 303(2)	...	The whole.

3. *Vide* Notification No. SO 2767, dated 5-8-1964.
4. *Vide* Notification No. GSR 73, dated 30-12-1965.
5. *Vide* Notification No. SO 2767, dated 5-8-1964.
6. Since omitted by the Amendment Act, 1965.
7. Added *vide* Notification No. SO 2767, dated 5-8-1964.

Note that any exemption granted by the Central Government cannot be taken advantage of, where the body concerned has, by its articles, made its own provision in respect of the subject-matter of such exemption.

Election of directors and nomination by member-company

Exemption from provisions of Ss. 255, 256.—These provisions relate to retirement of directors by annual rotation and filing of vacancies. Section 25 companies can be exempted from the application of these provisions. It has been held that the grant of such exemption should normally be express and that only in rare cases it would be inferred by necessary implication. The articles of the company in this cases provided for election of committee once in five years. The articles were approved by the Central Government and the approval was incorporated in the licence itself. The court said that such approval amounted to exemption from s. 256 by necessary implication. *C.P. Singhania v. Garware Club House,* 2003 CLC 1179 (Bom) : (2003) 46 SCL 659.

Department's Clarification.—There can be no objection to the nomination and election by a member-company, which has not paid the subscription for the relevant year (*Department's Circular No.* 23(29)-CL-IV/64, dated 7-5-1964):

Text of Circular.—"Section 25 Companies make provisions in their articles of association that the companies in their membership will not be entitled to vote in the election of directors (committee members) unless they have paid their subscription for the relevant year. The member companies are entitled to nominate their representatives for election to the committee. In case, one of the nominees happen to be nominated by a member company, which has not paid the subscription for the relevant year, the point for clarification is whether such nomination and his subsequent election as committee member will be invalid under the law. The Articles of Association of the company concerned do not as such disqualify a person being nominated for election by a member company which has not paid the subscription."

Cancellation of licence [Sub-section (7)]

The Central Government is empowered to revoke the licence granted under sub-section (1), *albeit* after affording an opportunity of hearing. This power has, however, to be invoked on *bona fide* considerations, and though not explicitly stated, such an order has to be a speaking one to be in consonance with principles of natural justice. In the event of a *mala fide* or arbitrary action to cancel the licence, the aggrieved association may challenge the order of the Central Government under Article 226 of the Constitution.

Merger of business undertaking into section 25 Companies.—Where the other requirements of a valid merger etc., were satisfied the objection of the Registrar to a scheme of arrangement and reconstruction of four different companies into a s. 25 company in the nature of a charitable trust was brushed aside because if any violation of the conditions of licence under s. 25 was involved that could be taken care of by the Government under its powers under s. 25 and was not a ground for refusing the proposed merger of business undertakings into a charitable undertaking. *Walvis Flour Mills Co. P. Ltd., Re,* (1993) 76 Com Cases 376 (Bom).

Alteration of objects with approval [Sub-section (8)]

A body licensed under this section cannot alter any provision of its memorandum in respect of its objects, except with the previous approval of the Central Government. If the alteration comes within any of the clauses of sub-section (1) of section 17, the provisions of that section must also be complied with, *inter alia*, by obtaining the approval of the Company Law Board.

In England an alteration of a Charitable Company's objects clause requires prior written consent of the Commissioner of Charity under the Charities Act, 1993, s. 64.

Discontinuation of name on revocation of licence [Sub-section (9)]

Where the licence is granted to a body the name of which (contains the words) "Chamber of Commerce", within a period of 3 months (or such period as may be extended) from the date of revocation of licence by the Central Government, that name must be changed

so as not to contain the said words. As regard the change of name thereupon, the company is required to comply with the provisions of section 23.

Penalty for default [Sub-section (10)]

The offence under sub-section (9) for failure to remove from the name of the company, the words "Chamber of Commerce", is punishable with fine up to Rs. 5000/-per day during which the default continues.

Compoundable Offence.—The offence is, however, compoundable under section 621-A.

No specific penalty has been provided for the contravention of sub-section (8), in regard to alteration of the objects clause in the memorandum of association without the approval of the Central Government. Accordingly, for such contravention, the company and its officers in default shall be punishable as laid down under section 629-A. The offence is, however, compoundable under section 621A.

Civil Court's jurisdiction in respect of internal management

Where a charitable trust is registered as a company under this section, a suit for administration of the trust or framing of a scheme of management is not barred by Company Court Jurisdiction under section 10. *Gomathinayagam Pillai (M.) v. Sri Manthiramurthi High School Committee,* (1963) 33 Com Cases 346 (Mad) (DB).

A civil court directed that all the decisions of the board of directors of sec. 25 company in question should be taken at meetings attended by all its three original directors. It was held that a resolution passed at a board meeting which was not so attended was null and void. *Vohra (Dr. V.J.S.) v. Ms. Balji Kaur Vohra,* (2000) 38 CLA 265 (CLB).

Writ against Chamber of Commerce

A Chamber of Commerce is not a State within the meaning of Article 12 of the Constitution and no writ can lie against it, *M.L. Shaw, Re,* (1984) 1 Comp LJ 146 (Cal). In this case, the Chamber was registered as a section 25 company.

Bombay Chamber of Commerce and Industry—exempted from sections 370 and 372.—In exercise of the powers conferred by sub-section (6) of section 25 of the Companies Act, 1956 (1 of 1956), the Central Government hereby directs that the Bombay Chamber of Commerce and Industry, a body to which a licence is granted under section 25 of the said Act, shall be exempt from the operation of the provisions of sections 370 and 372 thereof in so far as they relate to the requirement of prior approval of the Central Government. (*Department's F. No.* 1/6/88-CL-V, dated 14-2-1990).

Associated Chamber of Commerce and Industry—exempted from section 370.—In exercise of the powers conferred by sub-section (6) of section 25 of the Companies Act, 1956 (1 of 1956), the Central Government hereby directs that Associated Chambers of Commerce and Industry of India, a body to which a licence is granted under section 25 of the said Act, shall be exempt from the operation of the provisions of section 370 thereof in so far as they relate to the requirement of prior approval of the Central Government. (*Department's F. No.* 1/6/88-CL-V, dated 14-2-1990).

Western U.P. Chamber of Commerce & Industry exempted from section 372 : S.O. 270(E), dated 26-4-1993.—In exercise of the powers conferred by sub-section (6) of section 25 of the Companies Act, 1956 (1 of 1956), the Central Government hereby directs that the Western U.P. Chamber of Commerce & Industry, body to which a licence is granted under section 25 of the said Act, shall be exempt from the operation of the provisions of section 372 thereof in so far as they relate to the requirement of previous approval of the Central Government. [*Department's F. No.* 1/6/88-CL-V, dated 26-4-1993.]

Application of Stamp Act, and Sales-tax Law

Registration under this section as a members' club is *prima facie* proof that the club is not an association for profit and consequently there is no element of sale by the club to its members when refreshments are served so as to warrant levy of sales tax. *Cosmopolitan Club v. Deputy Commercial Tax Officer,* AIR 1952 Mad 814 : (1952) 3 STC 77 **affirmed** in (1955) 6 STC 1 (Mad).

Companies registered under this section need not have their Memorandum and Articles stamped under Article 39 of the Indian Stamp Act, 1899.

Charitable companies licensed under this section and other laws (Income Tax Act)

The grant of a licence under this section is not conclusive of the fact that a company is registered for a charitable purpose within the meaning of S. 2(15) of the Income-tax Act. It is only a relevant consideration. *Hyderabad Race Club, Hyderabad v. CIT, A.P.I., Hyderabad,* (1985) 153 ITR 521 (AP—FB). See also *CIT v. The Ootacamund Gymkhana Club,* 1978 Tax LR 74 (Mad—FB).

Income and rent received from members not taxable.—Receipts from various facilities provided by a club (s. 25 company) to its members as a part of the privileges, benefits and conveniences attached to membership, was held to be not a trading activity. The surplus generated by excess of receipts over and above the expenditure could not be said to be income for the purposes of IT Act. The receipts were in respect of drinks and refreshments provided to members. *CIT, Bihar v. Bankipur Club Ltd.,* (1997) 2 SCC 394.

Application of Companies (Auditor's Report) Order, 2003

The Department of Company Affairs notified the Companies (Auditor's Report) Order, 2003 [CARO 2003] *vide* GSR 480(E), dated 12-6-2003, CARO 2003 supersedes the existing Manufacturing and Other companies (Auditors Report) Order, 1988. The concept has made greater inroads in the new reporting order. For example CARO 2003 requires reporting even about the end-uses raised in a public issue. CARO 2003 is applicable for every financial year ending on or after 1-7-2003. The clauses of the Old Order were classified on the basis of the activity of the Company. Nevertheless, CARO 2003 puts no activity limitations, the clauses being applicable to all companies, excepting.

Bombay Insurance and Section 25 Companies

General Circular No.32/2003 dated 10-11-2003.—The Government have received representations stating the difficulty in complying with the new Order at short notice, in view of the absence of a Guidance Note from the Institute of Chartered Accountants of India, and in view of the need for maintaining records of a company in a manner that will ensure the compliance of the Order, Government have given consideration to the difficulty expressed. It has been decided that it is not possible, at this point of time, to review the Order, or postpone the effective date as issued, for accounts prepared in respect of financial year ending on the 1st July, 2003 or thereafter. However, keeping in view the difficulties of the companies as well as the professionals involved, it has also been decided that while companies to whom the Order is applicable, should make serious efforts to comply with the new Order from the effective date, cases of non compliance for accounts pertaining to financial year which closed on 31st December, 2003 or earlier, Government would take a lenient view provided the accounts at least carry MAOCARO Report, if required.

However, accounts in respect of financial years ending on 1st January, 2004 or thereafter, will have to strictly follow CARO, 2003. Companies and professionals who do not comply with the Order will be liable for action as per law.

§ For text of the CARO, 2003 refer *Appendix* 24.

Articles empowering Central Government to give directions

Where the article of a company licenced under this section for export promotion empowered the Central Government to give directions in national or public interest, it was held that in the exercise of this power an attempt by the Government to divest the executive committee of the company of the power to deal with the company's staff was arbitrary and without jurisdiction. *Apparel Export Promotion Council, New Delhi v. Union of India,* (1997) 90 Com Cases 309 : AIR 1994 Mad 57.

Suspension from membership

Members of a club suspended.—Some members of a club licensed under section 25 were suspended for a few weeks by the Committee of management by reason of their

adverse remark on the functioning of the Committee. The suspended members moved the High Court by means of a writ petition for an order that the provision in the Company's article should be struck down in view of the circular issued by the department of company affairs that a member of a public company cannot be expelled from his membership. The court rejected the petition being of the view that neither temporary suspension of the exercise of membership rights was an expulsion from membership nor a departmental instruction can be enforced against the field officers under the Companies Act directly by means by a writ petition. *Leela Kumar (L.) v. Government of India,* (1997) 27 Corpt. LA 145 (Mad).

Transfer of shares of section 25 companies listed with OTCEI

An instrument of transfer shall be in Form 7BB in case of section 25 Companies listed with OTC Exchange of India, *vide* Rule 5A sub-rule (2A) of the Companies (Central Government's) General Rules & Forms, 1956.

§ For the text of the Form 7BB and Rule 5A, see *Appendix* 1.

Delegation of powers to Regional Directors

The powers of the Central Government under this section have been delegated to the Regional Directors *vide Notification GSR No.* 288(E), dated 31-5-1991. (See Notes under section 637).

Application Fee payable by Section 25 Companies

The Companies (Fees on Applications) Rules, 1999.—According to new Rules, Section 25 companies would now have to pay Rs. 500/- for any application made by them. For issue of licence under section 25, the fees are being increased from Rs. 60/- to Rs. 500/-. Earlier, the rate was Rs. 60/-. [*Departments Press Note* 4/99 dated 16-7-1999].

The Companies (Fees on Applications) Rules, 1999 have been promulgated *vide* Notfn. No. 501(E), dated 6-7-1999 (w.e.f. 10-8-1999) superceding the earlier Companies (Fees on Applications) Rules, 1968.

§ For text of the Rules see *Appendix* 5.

Secretarial Practice Notes:

If the company had licence issued under section 25, check that :

(i) the company had not applied its profits or income by way of dividend to its members;

(ii) the company had not altered objects clause of memorandum; without prior approval of the Regional Director (This is in addition to the provisions of section 17);

(iii) conditions of licence complied with;

(Also see Regulations 3 to 14 of the Companies Regulations, 1956) Extent of exemptions from the provisions of the Companies Act for such companies.)

Documents Involved: (1) Annual Report, (2) Memorandum and Articles, (3) Minutes of Board/Committee/General Meeting, (3) Licence issued by Regional Director.

ARTICLES OF ASSOCIATION

General Notes

THE Articles of Association constitute the second important document which must be registered in the case of certain types of company together with the memorandum. Companies have grown in status to be rightly recognised as socio-economic institutions with wide-ranging social and business responsibility. They are no longer a wholly private affair. They have become a public phenomenon. A company is the centre of a complex web

of human relations. The conflicting interests of group of persons, like shareholders, who are providers of capital and interested only in an ever rising dividend curve; management, who are interested in higher remuneration; the workforce, which is interested in more wages and possibly less work and the consumers of the company's products who are interested in better quality at minimum possible prices, have to be held in a state of harmony. The articles constitute a set of rules regulating the affairs of the company. Each article is a rule for the regulation of the relations between the company and its shareholders and relations between the shareholders and the management. Each article is a rule of conduct for regulating the internal affairs and management of the company. Articles provide the rule book of the association of members and may have to deal with a variety of situations and relations. Those incorporating a new company may not be able to visualise many such situations. That is why for their guidance and help, model forms of articles set out in different Tables suited to the requirements of different types of company are given in the Schedule I of the Act. It is safe to adopt the model articles because they have the hallmark of Parliamentary approval, but they are rarely adopted in practice. By far the bulk of the articles deal with relations between the management and the shareholders, matters like shares and share capital, company meetings and directors and secretary. In addition, the listed companies have also to include in their articles certain compulsory provisions which are designed to facilitate free transferability of shares. Private companies have also to include in their articles certain prescribed restrictions. Articles are to be in a printed form and signed by the signatories to the memorandum. Articles may be altered by the company in general meeting by special resolution.

An important implication of the articles is that their provisions amount to a public notice, known as constructive notice, to all those who deal with the company. They are deemed to have notice of the manner in which the articles require the company to deal with a particular situation. That is why when articles are altered by the company, the alteration has to be recorded with the Registrar of Companies.

The memorandum and articles together are the constitutional framework of the company. Everybody having any concern with the company, whether as a director, member, debentureholder, creditor or dealer having trade relations with the company, has to bear in mind the constitution of the company, and no person may seek to deviate the company from its constitution. The memorandum and articles affect the company's internal as well as external relations.

The memorandum and articles bind the company to the members and the members to the company by constituting a contract between them. Those who become members of the company are bound by its constitution. The memorandum and articles give rise to two doctrines of company law, namely, the principles of constructive notice and that of indoor management. Constructive notice compels those dealing with the company to consult for their own protection the provisions of the memorandum and articles and to deal with the company only in the manner prescribed. The rule of "indoor management" compels those handling the company's affairs to assure proper internal proceedings because they cannot prejudice outsiders by raising internal irregularities of their own making as a defence. The doctrine of constructive notice has been abolished in England by the Companies Act of 1985 in reference to memorandum and articles and now the basic requirement is that dealings with a company should be in good faith and without actual notice that the memorandum and articles were being violated. Indoor management is an application of the principles of the law of agency coupled with the equitable doctrine of estoppel. (See Notes under S. 290).

Articles of Association

S. 26. Articles prescribing regulations.—There may in the case of a public company limited by shares, and there shall in the case of an unlimited company or a company limited by guarantee or a private company limited by shares, be

registered with the memorandum, articles of association signed by the subscribers of the memorandum, prescribing regulations for the company.

NOTES

Eng. Act, 1948 : Sec. 6.
Eng. Act, 1985 : Sec. 7.

Previous Act : Sec. 17(1).

Scope of section

In case of a public company limited by shares, there is no obligation to register articles of association, and if it is registered without articles, the regulations in Table 'A' are deemed to be the articles of the company. Other companies, must have their own set of articles.

Articles are compulsory in cases of unlimited companies, companies limited by guarantee and a private company limited by shares. They are compulsory in these cases because section 27 prescribes certain compulsory provisions to be included in the articles of such companies.

Nature, function and scope of articles of association

The articles of association of a company is its Magna Carta. Each shareholder is irrefutably attributed with notice of their purport and content. Even if disputed, the shareholder is presumed to have constructive knowledge of the same. *Rajakumar (S.S.) v. Perfect Castings Pvt. Ltd.*, (1968) 38 Com Cases 187 (Mad).

The articles regulate the internal management of the company. They define the powers of its officers. They also establish a contract between the company and the members and between the members *inter se*. This contract governs the ordinary rights and obligations incidental to membership in the company. *Naresh Chandra Sanyal v. Calcutta Stock Exchange Association Ltd.*, AIR 1971 SC 422, 426: (1971) 41 Com Cases 51. It is by virtue of this section that the binding character of the articles is established, and not because the members have signed them. *In re, Link Industries Ltd.*, (1957) 27 Com Cases 468 (Mad).

Articles of Association of a company are not 'law' and do not have the force of law. *Co-operative Central Bank Ltd. v. Additional Industrial Tribunal*, AIR 1970 SC 245, 252 **followed** in *Kinetic Engineering Ltd. v. Sadhana Gadia*, (1992) 74 Com Cases 82 (CLB). In this case the CLB held that if any provision of the articles or the memorandum is contrary to any provisions of any law, it will be invalid in toto. A provision in the articles enabling the Board of Directors to reject transfers of less than in lots of 50 shares was held invalid being contrary to s. 22A of the Securities Contracts Regulation Act, 1956 (*ibid* at p. 88). To the same effect is the Supreme Court decision in *V.B. Rangaraj v. V.B. Gopalkrishnan*, (1992) 73 Com Cases 201 : AIR 1992 SC 453.

Articles subordinate to memorandum.—The articles of a company are subordinate to and controlled by the memorandum of association which is the dominant instrument and contains the general constitution of the company. The memorandum is fundamental and can be altered only under certain circumstances provided by the Act. But the articles are only internal regulations, over which the members of the company have full control and may alter them according to what they think fit. "The memorandum is, as it were, the area beyond which company cannot go; inside that area, the shareholders may make such regulations for their own Government as they think fit". *Ashbury Railway Carriage and Iron Co. v. Riche*, (1875) LR 7 HL 653, 671; *Birds Investments Ltd. v. CIT*, (1965) 35 Com Cases 143 (Cal). Care has to be taken to see that regulations provided for in the articles do not exceed the powers of the company as laid down by its memorandum, *Ashbury v. Watson*, (1885) 30 Ch D 376 (CA). Articles going beyond the memorandum are *ultra vires*. *Shyamchand Nandi v. Calcutta Stock Exchange*, AIR 1949 Cal 337. Hence, any articles that go beyond the company's sphere of action are inoperative, and anything done under the authority of such articles is void and incapable of ratification.

But neither the articles nor the memorandum can authorise the company to do anything so as to contravene any of the provisions of the Act. See *Re, Peveril Gold Mines,* (1898) 1 Ch 122 (CA).

Articles in relation to memorandum

Though the articles are subordinate to the memorandum yet if there be any ambiguity in the memorandum, the articles may be used to explain it but not so as to extend the objects. *London Financial Association, v. Kelk;* (1884) 26 Ch D 107; The memorandum and the articles must be read together at all events so far as may be necessary to explain any ambiguity appearing in the terms of the memorandum, or to supplement it upon any matter as to which it is silent. *Angostura Bitters (Dr. J.G.B. Siegert & Sons) Ltd. v. Albert Kerr,* 1933 AC 550 : (1934) 4 Com Cases 1. Thus, JESSEL M.R., in *Anderson's* case, *Re, Wedgwood Coal and Iron Co.,* (1877) 7 Ch D 75, 99, held: "Where there are two contemporaneous documents executed and assented to by the same persons at the same time....it appears to me that the ordinary rule applies, according to which contemporaneous documents are to be read together, so that if there is an ambiguity in one it may be explained by the other."

The distinction between the two documents was further emphasised by BOWEN L.J. in *Guinness v. Land Corporation of Ireland,* (1882) 22 Ch D 349, 381, where he observed: "The memorandum contains the fundamental conditions upon which alone the company is allowed to be incorporated. They are conditions introduced for the benefit of the creditors, and the outside public, as well as of the shareholders. The articles of association are the internal regulations of the company. How can it be said that in all cases the fundamental conditions of the charter of incorporation, and the internal regulations of the company are to be construed together..... In any case it is, as it seems to me, certain that for anything which the Act of Parliament says shall be in the memorandum you must look to the memorandum alone. If the legislature has said one instrument is to be dominant you cannot turn to another instrument and read it in order to modify the provisions of the dominant instrument." Where the memorandum clearly establishes the rights of shareholders, a reference in the memorandum to the articles and an ambiguity said to arise from the construction of the articles should not be used to depart from the clear meaning of the memorandum so as to diminish those rights, *Scottish National Trust Co. Ltd.,* 1928 SC 499 (Scot); *Kinetic Engineering Ltd. v. Sadhana Gadia,* (1992) 74 Com Cases 82 (CLB).

The memorandum and articles being contemporaneous documents, the ordinary rule of construction applies, according to which an ambiguity in one document may be explained by the other or an inconsistency may be explained by taking the two together. *Anderson's* case, (1877) 7 Ch D 75 at 99, CA; *Re, Duncan Gilmour & Co. Ltd.; v. Inman,* (1952) 2 All ER 871. Even in respect of matters which are, but need not have been stated in the memorandum, such as the rights of different classes of shareholders, the memorandum cannot be overridden by the articles, *Andrews v. Gas Meter Co.,* (1897) 1 Ch 361 at 369 CA; *Re, Southern Brazilian Rio Grande do sul Rly. Co. Ltd.,* (1905) 2 Ch 78. The articles may be referred to for the purpose of explaining or supplementing its provisions as to such matters. *Re, Southern Brazilian Rio Grande do sul Rly. Co. Ltd.,* (1905) 2 Ch 78 at 84.

Any act of the company beyond the memorandum is *ultra vires* and generally beyond the power of ratification. But any act outside the articles is only irregular and can be ratified by the members.

Invalidity of articles by reason of conflict with Act, memorandum and other laws

Any provision in a company's articles will be ineffective if it is in conflict with the memorandum, the Companies Act or any other law for the time being in force *Noble v. Laygate Investments Ltd.,* (1978) 2 All ER 1067. For example, statutory rights of members under the Companies Act cannot be nullified through articles. Ordinary examples are, right to apply for winding up, *Peveril Gold Mines Ltd., Re,* (1898) 1 Ch 122 (CA); articles prohibiting members from proceeding against the company for enforcement of

their individual membership rights. *St. Johnson Football Club Ltd. v. Scottish Football Assn. Ltd.*, (1965) Scottish Lt. 171 (OH); exclusion of the right to alter articles *Ayre v. Skelsey's Adamant Cement Co. Ltd.*, (1905) 21 TLR 464 (CA); deprivation of dissenting shareholders' rights, *Baring Gould v. Sharpington Combined Pick and Shovel Syndicate*, (1899) 2 Ch 80 (CA) **approved** in *Bisgood v. Henderson's Transvaal Estates Ltd.*, (1908) 1 Ch 743; right to information about the affairs of the company *e.g.*, as to reserve fund and accounts *Newton v. Birmingham Small Arms Co. Ltd.*, (1906) 2 Ch 378; deprivation of the right to retain shares properly acquired *Walker and Hacking Ltd., Re*, (1887) 57 LT 763.

A power to borrow in the memorandum cannot be enlarged by the articles into a power to issue irredeemable debenture stock. *Re, Southern Brazilian Rio Grande do sul Rly. Co. Ltd.*, (1905) 2 Ch 78. Where the memorandum defines the rights of the respective classes of shareholders such rights cannot be altered by the articles. *Ashbury v. Watson*, (1885) 30 Ch D 376 (CA). The articles are void to the extent of inconsistency even if the provision in the memorandum with which it is inconsistent is not required by law to be there—*Ashbury v. Watson, (Supra)*.

"Articles violating other laws are also void, *e.g.*, articles providing that transfer of shares in lots less than fifty would not be accepted being violative of Securities Contracts Regulations Act, 1956 in reference to listed companies. *V.B. Rangaraj v. V.B. Gopalakrishnan*, (1992) 73 Com Cases 201 : AIR 1992 SC 453.

Articles of Stock Exchange Company.—A provision in the articles of association of a stock exchange incorporated as a company to the effect that defaulting members would lose membership cannot be said to be inconsistent with any of the provisions of the Companies Act, 1956. *Rajendra Prasad Bagaria v. Bhubuneshwar Stock Exchange Assn. Ltd.*, (1999) 21 SCL 313 (Ori).

Articles of club registered as company.—A club was registered as a company. In accordance with its articles it was providing facilities exclusively to its members and their guests on "no profit – no loss basis. Even so, some surplus was generated and the same was being used for maintenance and development of the club and was not used for paying dividend to members. It was held that the business of the club was governed by the doctrine of mutuality. Hence, not only the surplus arising from the activities of the club, but also the annual value of its building (as contemplated by s. 22, IT Act) was beyond the purview of levy of income tax. *Chelmsford Club v. CIT, Delhi*, (2000) 3 SCC 214.

Construction of articles

In construing any article, all relevant articles may be taken into account and if the words used are ambiguous, attempt should be made to reconcile them and adopt such construction of the words as would avoid conflict between them. This principle of construction does not apply where the words are clear and unambiguous. *Shiv Omkar Maheswari v. Bansidhar Jagannath*, (1957) 27 Com Cases 255 : AIR 1956 Bom 459. In this case it was held that the article providing for settlement of disputes arising out of or in the course of dealings and transactions between members (of a chamber of commerce, in this instance) by arbitration did not include a dispute as to the existence of the dealings or transactions themselves.

Articles of association constitute a document of commercial nature. They should not be interpretated meticulously, *e.g.*, in the nature of conveyances. The court should follow the words of VAISEY J to the effect that they should be validated to the extent possible, *Rayfield v. Hands*, (1958) 2 All ER 194 : (1958) 28 Com Cases 460. Where the conduct of the parties reveals that there has been some practice in vogue for several years which was accepted by every one concerned without any challenge or question, then that practice in itself becomes an indication that the articles of association were understood in that sense. *Sunil Dev v. Delhi & District Cricket Assn.*, (1990) 2 Comp LJ 245, 255 : (1994) 80 Com Cases 174 (Del).

According to the Madras High Court, however, articles of association of a company being a business document has to be interpreted strictly, unless there are compelling circumstances to import into it a meaning other than normal. *Rajakumar (S.S.) v. Perfect Castings Pvt. Ltd.*, (1968) 38 Com Cases 187 (Mad). "The articles of association of the company should be regarded as a business document and should be construed so as to give them reasonable business efficacy where a construction tending to that result is admissible on the language of the articles preference to a result which would or might prove unworkable". Per JENKINS LJ in *Holmes v. Keyes (Lord)*, (1958) 2 All ER 129 : (1958) 28 Com Cases 419 (CA). Though the general presumption is that every material term in the articles regulating a company have been expressed, yet in some cases certain terms are necessarily implied in order to give effect to the intention of the parties. *Someshchandra Manilal v. Jivan Lal Chinai*, AIR 1956 Bom 190 : (1956) 26 Com Cases 148.

§ See also Notes under s. 36 under the heading "Construction of articles".

Directors bound to work according to articles

President's power to nominate directors and give directions.—In *Fertilizers Corporation of India v. Their Workmen*, AIR 1970 SC 867 at 873, the Supreme Court held that where the articles of association gave powers to the President of India to give directions regarding the working of the company, the exercise of the powers of the Board of Directors was, apart from other restrictions, subject to the directions issued by the President from time to time. Unless the exercise of pleasure by the Government is shown to be *mala fide* or against public interest, the court cannot interfere with the order nominating a person as a director in the place of another. *G. Karunakaran v. State of Kerala*, (1987) 61 Com Cases 334 (Ker).

Terms in articles by implication

The question before the Court of Appeal in *Bratton Seymour Service Co. Ltd. v. Oxborough*, (1992) BCLC 693 (CA) was whether a term could be imported into a company's articles by implication. The company was set up to manage development of flats. The issue was whether it was possible to imply a term that the shareholders, who were the owners of the flats, should make contributions for the upkeep of the amenity areas of the development. The court said that the articles of a company constitute a statutory contract with its own distinctive features. For example, the articles cannot be defeated on the grounds of misrepresentation, nor rectified on the grounds of mistake, whereas an ordinary contract is subject to these processes. It may be possible for the court to infer a term purely by way of constructional implication, but it is not possible to go further and imply a term from extrinsic circumstances. It is not possible to imply a term that the shareholders of the company should be under an obligation to make an additional financial contribution. This also seemed to the court to be going beyond the language of the articles.

A joint venture agreement provided restrictions on the rights of the members of the company created by the joint venturers on transferability of their shares. But the restriction as to transferability was not carried into the articles of the company. The court said that restriction had not acquired its binding force on the members of the company though it was binding on the partners to the joint venture. The transfer was, therefore, valid and it was validly registered. *Crompton Greaves Ltd. v. Sky Cell Communication Ltd.*, (2002) 39 SCL 704 (Mad—DB).

Doctrine of constructive notice

§ For Notes under this topic, see under s. 36.

S. 27. Regulations required in case of unlimited company, company limited by guarantee or private company limited by shares.—(1) In the case of an unlimited company, the articles shall state the number of members with which

the company is to be registered and, if the company has a share capital, the amount of share capital with which the company is to be registered.

(2) In the case of a company limited by guarantee, the articles shall state the number of members with which the company is to be registered.

(3) In the case of a private company having a share capital, the articles shall contain provisions relating to the matters specified in sub-clauses (a), (b) and (c) of clause (iii) of sub-section (1) of section 3; and in the case of any other private company, the articles shall contain provisions relating to the matters specified in the said sub-clauses (b) and (c).

NOTES

Eng. Act, 1948 : Sec. 7(1)(2). Previous Act : Sec. 17(2) & (4).
Eng. Act, 1985 : Sec. 7.

Number of members fixed by articles [Sub-section (2)]

Where the articles of a guarantee company specified maximum number of members and the executive committee enrolled greater number of members, the court did not allow a member to complain of this without showing some suffering as a member. *Dharani Pal Bhasin v. B.N. Khanna,* (1988) 64 Com Cases 651 (Del).

For detailed notes on guarantee companies, see Notes under S. 37, for unlimited companies, see Notes under S. 13 and for private companies, see Notes under S. 3.

Private company [Sub-section (3)]

A private company having a share capital must provide in the articles, the three restrictions specified in sub-clauses (a), (b) and (c) of clause (iii) of sub-section (1) of section 3, *viz* (a) as to the right to transfer shares (b) limit as to number of its members (c) invitation to public to subscribe for any shares in or debentures of the company. Any other private company must provide in its Articles, restrictions as given under sub-clauses (b) and (c) as mentioned above. An additional requirement has been prescribed by the Amendment Act of 2000. Clause (d) has been added to section 3(1)(iii) so as to prescribe that the articles of a private company shall include a restriction prohibiting any invitation or acceptance of deposits from persons other than its members, directors, or their relatives.* In the absence of these provisions, it cannot retain its character of a private company and will be treated as a public company.

Note *A consequential change of this kind, though not expressely brought in by the legislature in section 27, will arise by implication.

Transfer of interest in guarantee company

Certain Stock Exchanges are guarantee companies and do not have any share capital. Members are issued membership cards and their interest can be transferred through a nomination procedure prescribed in their articles of association. Under section 82, shares as well as interest of a member in a company is treated as movable property and can be transferred in a manner mentioned in the articles. A member of the Stock Exchange, which is a guarantee company, without share capital will have an interest in that company (Stock Exchange) and can transfer his interest in the manner mentioned in the articles and the prescribed nomination procedure will have to be followed. There is no need for executing any share transfer form or payment of any share transfer fee. In the absence of any share certificate, the provisions of section 108 of the Act will not apply. There is no provision for levy of stamp duty under the Indian Stamp Act, 1899.

Guarantee company's right to refuse transfer of member's interest

The Supreme Court has emphasised that the right of a guarantee company to refuse to accept the transfer by a member of his interest in the company is on a different footing than that of a company limited by shares. The guarantee company here was running a stock exchange. The right of an existing member to transfer his interest to another person would involve the question of that person's admission to the membership of the organisation. Such membership may carry privileges much different from those of ordinary shareholders. Accordingly, the Supreme Court characterised the decision of the High Court that the same principles were applicable as much to transfer of membership as to shares, as wrong. The matter was remitted for reconsideration. *Narendra Kumar Agarwal v. Saroj Malso,* (1996) 85 Com Cases 172 (SC). The Court noted the difference in the set of articles in Sch. I which are applicable to guarantee companies and companies limited by share.

S. 28. Adoption and application of Table A in the case of companies limited by shares.—(1) The articles of association of a company limited by shares may adopt all or any of the regulations contained in Table A in Schedule I.

(2) In the case of any such company which is registered after the commencement of this Act, if articles are not registered, or if articles are registered, in so far as the articles do not exclude or modify the regulations contained in Table A aforesaid, those regulations shall, so far as applicable, be the regulations of the company in the same manner and to the same extent as if they were contained in duly registered articles.

NOTES

Eng. Act, 1948 : Sec. 8.
Eng. Act, 1985 : Sec. 8(1)(2).

Previous Act : Secs. 17(2) and 18.

Scope of application of 'Table A'

Sub-section (2) applies only in the case of companies limited by shares which are registered after the commencement of this Act.

The provision does not apply to existing companies which have not adopted any separate articles and have adopted only a few special articles, having adopted Table A of Schedule I of the previous Act, either wholly or in part. There are a good number of existing companies, especially private companies, which have adopted either wholly or in part, the regulations in Table A of Schedule I of Act VII of 1913. In such cases the saving clause in section 657 will enable those companies to continue to be regulated by the said Table A of the said Act of 1913 to the extent that it is applicable.

In the case of any company the regulations in Table A will, so far as they are applicable, apply to that company, unless the company's own articles expressly exclude or modify those regulations in their application to itself.

If Table A is to be excluded it must be done in clear language. Where articles are not registered, sub-section (2) of this section will apply. See *Prayan Prasad v. Gaya Bank & Traders Association Ltd.,* (1931) 1 Com Cases 85 : AIR 1931 Pat 44. Even if articles are registered, to the extent to which they do not exclude or modify the regulations in Table A, those regulations will also be applicable. See also *Seth Mohanlal v. Grain Chambers Ltd.,* (1968) 38 Com Cases 543 : AIR 1968 SC 772.

Articles adopted on the lines of any of the regulations in Table A cannot be *ultra vires,* as the Parliament has enacted the same along with the Act and as being consistent with the provisions of the Act. *New Balkis Ersteling v. Randt Gold Mining Co.,* 1904 AC 165;

Lock v. Queensland Investment and Land Mortgage Co., (1896) 1 Ch 397 and on appeal, 1896 AC 461 (HL).

§ **Construction of articles.**—See Notes under Ss. 27 and 36.

Matters requiring provision in articles

Where in respect of any matter or for the doing of anything or exercising any power such as the issuing of redeemable preference shares, or the appointment of additional directors or the appointment of an alternate director, authority is required to be given under the articles of association of a company, and the company's existing articles do not contain any provision in that behalf, the proper course is to have the articles amended so as to contain the necessary provision, before proceeding to exercise the power.

Option regarding articles of association of public company

Section 26 read with section 28 gives a public limited company three options regarding the articles of association:

(a) To register no articles at all in which event Table A will apply in its entirety.

(b) To register a short form of articles of association comprising the special articles of the company and incorporating regulations of Table A to complete the regulations of the company.

(c) To register a full set of articles of association and exclude all regulations of Table A.

Both courses (b) and (c) are of common occurrence. The partial adoption of Table A has particular advantages for small companies, *firstly* because of economy of printing, and *secondly* because any provision of Table A is legal beyond any doubt. *Per* KAY LJ in *Lock v. Queensland Investment and Land Mortgage Co.*, (1896) 1 Ch 397, 406-407.

Articles of a private company

Under section 3(1)(iii), the certain characteristics of a private company are to be specified in its articles of association. It is, accordingly, necessary for a private company to register its articles containing the said characteristics. The Company may adopt all or any of the provisions of Table A.

Removal of *lacunae* in articles

Where the articles adopted by the company do not provide a comprehensive regulation of the internal affairs of the company, the question then arises how these *lacunae* have to be filled. Here two cases have to be distinguished:

(1) The company has expressly excluded the application of Table A. The *lacuna* can only be removed by reference to the general law.

(2) The company has not expressly excluded the application of Table A, *i.e.* it has partially adopted that regulation. The *lacuna* is removed by reference to Table A.

The principles of statutory interpretation will apply to Table A and to articles which adopt Table A in part. *Fell v. Derby Leather Co. Ltd.*, (1931) 2 Ch 252 : (1931) All ER Rep 636.

Secretarial Practice Notes : Adoption of Table A

Check the extent of applicability of Table A of Schedule I to the Act.

S. 29. Form of articles in the case of other companies.—The articles of association of any company, not being a company limited by shares, shall be in such one of the Forms in Tables C, D and E in Schedule I as may be applicable, or in a Form as near thereto as circumstances admit:

[1][*Provided* that nothing in this section shall be deemed to prevent a company from including any additional matters in its articles in so far as they are not inconsistent with the provisions contained in the Form in any of the Tables C, D and E adopted by the company.]

NOTES

Previous Act : Sec. 151(1)

Purport and effect of section

The following view of the purport and effect of S. 29 has been presented by the High Court of Delhi in *Pramod Chopra v. Apparels Export Promotion Council,* ILR (1984) 1 Delhi 717, 729, 734 (Del): The legislature in section 29 of the Act says that the articles of association of a company not being limited by shares shall be in such one of the forms in Tables C, D and E in Schedule I as may be applicable or in a form as near thereto as circumstances admit. The Schedule is as much a part of the Statute, and is as much an enactment as any other part. Schedules are tables of details appended at the end of an Act. The intention of the legislature is clear that the articles of association should be in the form prescribed by the Act. At the same time some flexibility in the frame of the articles of association is given but they have to be as near thereto as the circumstances of the case may admit. The statutory provision is not worded in such a way that an undeviating conformity to the form is required. There could be variations in the articles consistent with the model form. The articles could also be supplemented where there was need but in a way compatible with the prescribed form. The divergence could not be in disharmony with the form prescribed in the Act. It would surely be in accordance with the prescribed form if the articles are substantially in accordance with it and they do not depart from the prescribed form in any material respect. But if the deviation is destructive of the provision contained in the prescribed form, then that deviation is void being *ultra vires* of the statutory provision. The aim and object of the Act and form in Table C giving every member a right of one vote would be defeated, if the direction of the legislature is not strictly observed. It is thus imperative to adopt the form. An absolute enactment must be obeyed or fulfilled exactly, but it is sufficient if a directory enactment is obeyed or fulfilled substantially.

Form of articles of unlimited and guarantee companies

In the case of an unlimited company or a company limited by guarantee, any articles adopted by it in addition to those applicable to it as per Table C, D or E of Schedule I, should not be inconsistent with the provisions of such Table.

It has been held that in the case of a company limited by guarantee and having no share capital, such as a club or a library, society, an article giving power to the Board of Directors or managing committee to expel a member is not invalid as inconsistent with Table C articles, (English Companies Act, 1948, Section 11, considered). *Gaiman v. National Assn. for Mental Health,* (1971) 41 Com Cases 929 : (1970) 2 All ER 362 (Ch D). However, in *P.C. Arvindhan v. M.A. Kesavan,* 1973 Tax LR 1844 (Ker), it was held that a provision in the articles of a guarantee company that prevented its members from participating in the annual general meeting was illegal and void, and also inconsistent with or contrary to "Table C".

The rule in this section is only directory and not mandatory and a company coming under it may adopt such articles as will suit its individual needs *Gaiman's* case, (*supra*). A guarantee company running a stock exchange could adopt in the articles a provision for expulsion of members in the interest of maintaining discipline among them. It was permissible being not contrary to the Companies Act. The member in question had joined a company as its managing director, inspite of the prohibition in the articles on holding

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1. Ins. by Act 65 of 1960, s. 10.

office in any other company. He refused to give up that office even after notice by the company. His expulsion was held to be justified. *Madras Stock Exchange Ltd. v. SSR Rajkumar,* (2003) 116 Com Cases 214 : (2003) 4 Comp LJ 50 : (2004) 49 SCL 319 (Mad).

Power of attorney for rectification of errors in documents

Department's Circular.—Department has issued a *Circular No.* 1/95, *F. No.* 14/6/94-CL-V, dated 16-2-1995, on this point. Text of the circular has been reproduced under S. 15 under the above heading.

S. 30. Form and signature of articles.—Articles shall—

(a) be printed;

(b) be divided into paragraphs numbered consecutively; and

(c) be signed by each subscriber of the memorandum of association (who shall add his address, description and occupation, if any,) in the presence of at least one witness who shall attest the signature and shall likewise add his address, description and occupation, if any.

NOTES

Eng. Act, 1948 : Sec. 9. Previous Act : Sec. 19.
Eng. Act, 1985 : Sec. 7(3).

Scope of section

The provisions of this section are similar to section 15, relating to Memorandum of Association. The occupation if any of each subscriber besides his name, address and description must be added in his own hand, and further the attestor also must give his name, address, description and occupation, if any.

§ For *Departmental circulars* regarding offset and computer printed articles of association, refer Notes under section 15.

§ Also refer to Notes on section 15.

Meaning of term 'Description'

In BLACK'S LAW DICTIONARY, (Sixth Edition) p. 445, the word 'description has been defined as: "A method of pointing out a particular person by referring to his relationship to some other person or his character as an officer, trustee, executor etc. Since occupation is required in addition to description, the import of the word 'description' would be to mean relationship to some other person like 'son of..... or wife of....." Also refer P RAMANATHA AIYER-LAW LEXICON, 2nd Edn., Reprint 2003.

Stamp duty on articles

The stamp duty on articles of association being a State subject, varies from State to State. Refer *Appendix* 134 'C' for 'Table of Fees and Stamps'. See also K. KRISHNAMURTHY—INDIAN STAMP ACT, 8th Edition, 2002.

Improperly stamped articles.—If the articles, though improperly stamped were registered and acted upon for years, they must be held to be effectual. *Ho Tung v. Man On Insurance Co. Ltd.,* (1902) AC 232 (PC); *Kunj Kishore v. Buldeo Mills,* (1914) 36 All 416.

Secretarial Practice Notes

Check whether:—

(a) the articles include all matters that may normally be required, or table A has been adopted to the extent not specifically covered by the articles?

(b) in case of a private company, the articles shall include the conditions specified in section 3(1)(iii)?

(c) in case of a company proposed to be listed, the articles do not include matters found objectionable under Listing Guidelines/Agreement?

(d) articles are duly 'printed' and stamped according to the stamp duty rates of the concerned State?

(e) the subscribers have added their name, father's name and address by their own hands and their signatures are duly attested?

S. 31. Alteration of articles by special resolution.—(1) Subject to the provisions of this Act and to the conditions contained in its memorandum, a company may, by special resolution, alter its articles:

[1][*Provided* that no alteration made in the articles under this sub-section which has the effect of converting a public company into a private company, shall have effect unless such alteration has been approved by the Central Government.[2]]

(2) Any alteration so made shall, subject to the provisions of this Act, be as valid as if originally contained in the articles and be subject in like manner to alteration by special resolution.

[1][(2-A) Where any alteration such as is referred to in the proviso to sub-section (1) has been approved by the Central Government, a printed copy of the articles as altered shall be filed by the company with the Registrar within one month of the date of receipt of the order of approval.]

(3) The power of altering articles under this section shall, in the case of any company formed and registered under Act No. 19 of 1857 and Act No. 7 of 1860 or either of them, extend to altering any provisions in Table B annexed to Act No. 19 of 1857, and shall also, in the case of an unlimited company formed and registered under the said Acts or either of them, extend to altering any regulations relating to the amount of capital or its distribution into shares, notwithstanding that those regulations are contained in the memorandum.

NOTES

Eng. Act, 1948 : Sec. 10.
Eng. Act, 1985 : Sec. 9.

Previous Act : Sec. 20.

Companies (Amendment) Act, 1960

Conversion of public company into private company : *Recommendation of Company Law Committee.*—The amendments give effect to the following recommendation of the Companies Act Amendment Committee: "The Act does not prevent the conversion of a public company into a private company by amending its articles by a special resolution and otherwise complying with the requirements of the Act. On account of the restrictions placed by the Act on the management of public companies, there has been in recent months a tendency to convert public companies into private companies. While such conversions are no doubt primarily matters for the shareholders, and, in fact the consent of the Court is not required, it seems to us that, having regard to the fact that they can be effected merely by the adoption of a special resolution which may have commanded the positive support of only a minority of the members of a company, some form of control of these conversions is necessary if certain of the objects of the Act are to be achieved. At

1. Ins. by Act 65 of 1960, s. 11.
2. Power now vested with the Registrar of Companies *vide* Notification No. GSR 281(E), dated 21-3-1995. Relevant Rules is R. 4-B and 20A of the Companies (Central Govt's.) General Rules & Forms, 1956 and relevant form is form No. 1B.

present, the Department is exercising some control over such conversions by resorting to section 21 and regarding the addition of the word "Private" consequent upon such conversion as change in the name of the company which, under the section requires the approval of the Central Government. But this is a change required to be made by the Act and section 21 cannot bear the strain the Department seeks to put upon it." (*Report*: Para 34).

Scope and limits of power of alteration

Statutory power.—The power to alter articles is a statutory power and a company cannot contract itself out of the power, and provide that any of its articles are to remain unaltered. Any restriction on the exercise of the power except to the extent provided in the Act or any other law will be invalid. An article in terms providing that no alteration shall be made without the consent *e.g.*, of *X* is contrary to the Act and ineffective. *Cf. Bushell v. Faith,* (1969) 1 All ER 1002 (CA), **affirmed** in (1970) 1 All ER 53 : (1970) 40 Com Cases 944 (HL). See also *Andrews v. Gas Meter Co.,* (1897) 1 Ch 361; *Malleson v. National Insurance and Guarantee Corporation,* (1894) 1 Ch 200; *Chithambaram Chettiar (N.P.N.M.) v. Krishna Aiyangar,* ILR 33 Mad 36; 'The Insurance Act (IV of 1938) abolished the dividend scheme which was the basis of the rules of the association. So by means of a resolution, an amendment was made to the rules substituting a guarantee scheme. Since the alteration was made for the benefit of the association as a whole it was valid'. *All India Rly. Men's Benefit Fund v. Jamadar Baheshwarnath Bali,* (1945) 15 Com Cases 142, 146 : AIR 1945 Nag 187. The reason for the rule is thus stated in MAYSON: "The articles of association concern themselves with the internal administration of a company. Such matters cannot remain static for all time and so alterations must be possible" COMPANY LAW, 118 (19th Edn., 2002-2003). It is for this very reason that the power of alteration has not been subjected to any limitation except that the power is subject to the Act and the memorandum.

An illustration of the unfettered character of the power is the decision in *Andrews v. Gas Meter Co.,* (1897) 1 Ch 361 (CA) where a company was permitted to issue preference shares by changing articles though there was no such authority in the company's memorandum. The power was allowed to be used for imposing the company's lien upon the shares of its members and for varying class rights subject, of course, to the limits otherwise applicable. *Allen v. Gold Reef of West Africa Ltd.,* (1900) 1 Ch 656; *Australian Estates and Mortgage Co. Ltd.,* (1910) 1 Ch 414 at 424. The power conferred on the company under this section to alter the articles by a special resolution cannot be abused by the majority of the shareholders so as to oppress the minority. *Mathrubhumi Printing and Publishing Co. Ltd. v. Vardhman Publishers Ltd.,* (1992) 73 Com Cases 80, 96 (Ker) (DB).

The House of Lords had to consider in *Russell v. Northern Bank Development Corpn. Ltd.,* (1992) BCLC 1016 : (1993) 3 Comp LJ 45 (HL) the effectiveness of a shareholders' agreement which provided that the share capital of the company could only be increased if all the shareholders consented in writing. The agreement had been signed by all the current shareholders, comprising four working shareholders and an investor, and by the company itself, and thus reflected the intention of all the participants. Under normal contractual principles, that should have been enough to ensure that each shareholder had a power of veto over future increases in share capital. The House of Lords had to decide whether this clear intention could nonetheless be overridden on the basis that the provision was in fact an invalid attempt to fetter the company's statutory power to increase its capital by ordinary resolution. Their Lordships held that the agreement bound the shareholders themselves not to vote on any exercise of the relevant statutory power that would be contrary to the provision, but that it could not bind the company. Company law thus gives shareholders a right to vote on the exercise of a statutory power as they think fit which cannot be taken away by the company's constitution or by any contractual undertaking given by the company itself, although they can bind themselves contractually as to how they exercise this right.

A shareholder has no right to assume that his company's articles would always remain in a particular form and he cannot object to an alteration as fraudulent provided it was passed *bona fide* and did not unfairly discriminate. *Greenhalgh v. Arderne Cinemas,* (1950) 2 All ER 1120 (CA).

Articles cannot be altered, if the alteration is repugnant to, or inconsistent with, any statute or general law or if it is such as to defeat the provisions of any law. The articles cannot be altered to enable the company to carry on an illegal scheme (lottery business). *Pioneer Mutual Benefit Society v. Asst. Registrar,* (1933) 3 Com Cases 37, 40 : AIR 1933 Mad 129. The power to alter cannot be used to violate any statutory provision or principle of law *e.g.* to take away a shareholder's right to present a winding up petition. *Peveril Gold Mines,* (1898) 1 Ch 122; *Payne v. Cork Co.,* (1900) 1 Ch 308; *Greene, Re,* (1949) 1 All ER 167; *Ramakrishna Industries (P.) Ltd. v. P.R. Ramakrishnan,* (1988) 64 Com Cases 425 (Mad). When the court under section 397 or 398 makes any alteration in the memorandum or articles of association, the company cannot make any alteration inconsistent with the court's order except as provided in section 404. PALMER'S COMPANY PRECEDENTS, 399 (17th Edn., Vol I). A company cannot by a clause in its articles exempt any article from liability to alteration under this section. *Walker v. London Tramways Co.,* (1879) 12 Ch D 705; *Malleson v. National Insurance Corpn.,* (1894) 1 Ch 200. A company cannot contract not to alter its articles. *Allen v. Gold Reefs of West Africa Ltd.,* (1900) 1 Ch 656: (1900-3) All ER 746.

A provision of the articles which has the effect of limiting the company's share capital to a fixed amount would have no effect being contrary to the Act. *Miheer Hemant Mafatlal v. Mafatlal Industries Ltd.,* (1987) 89 Bom LR 86 (Bom).

All members become bound by a valid alteration whether they voted for or against it. *Hari Chandana Yoga Deva v. Hindustan Co-op. Insurance Society Ltd.,* AIR 1925 Cal 690.

Stringent provisions can be made in the articles so long as they are not contrary to the provisions of the Act. Where the Act provides for an ordinary resolution for transacting a particular business, the articles may prescribe for special resolution. Similarly, a public company which is required to give notice of 21 days' for a general meeting, may provide in its articles to give 30 days' notice. Such a public company cannot, however, provide for giving less than 21 days' notice. The articles cannot make a provision for appointment of a particular firm as auditors, as the shareholders have the right to appoint them under the Act.

Bona fide **for benefit of company as a whole**

The power of alteration of the articles [and of those parts of the memorandum which may be altered in the same manner as the articles as per section 16(3)] must be exercised *bona fide* for the benefit of the company as a whole. *Shuttleworth v. Cox Bros. & Co., (Maidenhead) Ltd.,* (1927) 2 KB 9. If a majority of shareholders alter the articles solely for their own benefit and not in the interest of the company, the alteration is bad. *Geary v. Metrose Co-op. Dairy Co. Ltd.,* (1930) NZLR 768.

"The power" said LINDLEY, M.R. [at p. 671], "thus conferred on corporations to alter the regulations is limited only by the provisions contained in the company's memorandum of association. It must be exercised for the benefit of the company as a whole and it must not be exceeded. These conditions are always implied and are seldom, if ever, expressed. But if they are complied with I can discover no ground for judicially putting any other restrictions on the power conferred by the section than those contained in it." *Allen v. Gold Reefs of West Africa,* (1900) 1 Ch 656 **followed** in *All India Rly. Men's Benifit Fund v. Jamadar Baheshwarnath Bali,* (1945) 15 Com Cases 142 : AIR 1945 Nag 187.

The power of alteration cannot be exercised in a manner that would constitute a fraud on the minority. An alteration in the articles whereby the majority may require any member to sell his shares to any other member is liable to be struck down if the compulsion is not for the benefit of the company as a whole. *Clemens v. Clemens Bros. Ltd.,* (1976) 2 All ER 268; *Brown v. British Abrasive Wheel Co.,* (1919) 1 Ch 290; *Dafen Tinplate Co. Ltd. v. Llanelly Steel Co. (1907) Ltd.,* (1920) 2 Ch 124; *Sidebottam v. Kershaw, Leese & Co. Ltd.,* (1920) 1 Ch 154.

Wide as the power of alteration is, the articles cannot be so altered as to deprive a minority of their rights ; and the power must be exercised *bona fide* in the interest of the company and for the benefit of the company as a whole. The expression "for the benefit of the company as a whole means for the benefit of the shareholders as a general body. Its effect should not be such as to discriminate between the majority shareholders and the minority shareholders so as to give the former an advantage of which the latter are deprived." There must also be honesty in what is being-done. See *Greenhalgh v. Arderne Cinemas,* (1950) 2 All ER 1120 (CA). See also *Mathrubhumi Printing & Publishing Co. Ltd. v. Vardhman Publishers Ltd.,* (1992) 73 Com Cases 80, 98 (Ker) (DB) where the entire case law is reviewed.

An alteration of articles for the purpose of providing that the shares of an expelled member would be compulsorily transferred against the wishes of some of the existing members, or even against his wishes and without his signature, was held to be valid exercise of the power of alteration. *Gothami Solvent Oils Ltd. v. Mallina Bharathi,* (2001) 105 Com Cases 710 : (2001) 31 SCL 178 : (2001) 42 CLA 267 : (2001) 3 Comp LJ 127 : (2001) CLC 1377 (AP). **Reversing** decision of CLB on this point in *Mallina Bharati Rao v. Gowthami Solvent Oils Ltd.,* (2001) 105 Com Cases 700 (CLB). For facts of the case see notes on s. 41 under the heading "Expulsion from membership".

On a review of the authorities the position is thus summarised in HALSBURY'S LAWS OF ENGLAND, 381 para 554 (Vol. 7(1) 4th Edn., Reissue, 1988): "Any alteration must be made in good faith for the benefit of the company as a whole, that is, of the corporators as a general body. Subject to this, articles may be freely altered. It is for the shareholders and not the court to determine whether or not the alteration is for the benefit of the company and the court will not readily interfere with an alteration made in good faith unless it is of such a character that no reasonable person could have regarded it as made for the benefit of the company. The alteration may affect the rights of the member as between himself and the company by retrospective operation, since the shares are held subject to the statutory power of altering the articles."

The points which emerge from the above cases can be usefully listed in terms of the following propositions:

(1) It is not necessary to show to validate an alteration that a particular member will get some benefit out of it, but it would be necessary to show that the alteration is needed for the equal good of the members as a whole and that the burdens and benefits of the alteration will fall upon all the members alike.

(2) The alteration should not discriminate between members by conferring privileges on some and depriving others of their rights *e.g.* depriving members of their pre-emptive rights or increasing their liability. A member may, however, be subjected to a sacrifice if it is for the good of the organisation *e.g.* expelling a member and acquiring his shares at a fair value if his personal competing business is causing harm to the company.

(3) All majority powers have to be exercised in absolute good faith for the benefit of the organisation as a whole, but good faith is not lost merely because the alteration operates to the disadvantage of some members.

Injunction to restrain alteration of articles .—An application was made for an injunction to restrain the holding of an extraordinary general meeting which was called to

pass a special resolution for effecting changes in the articles of the company. The changes were intended to bring about smooth, proper and harmonious functioning of the management of the company. The plaintiff shareholder, who was opposing the alteration, was not facing any dilution of his legitimate expectations in joining the company. Hence, the court came to the conclusion that the matter should be left to the wisdom of the shareholders to pass or to drop the motion. *K.G. Khosla v. Rahul C. Kirloskar,* (1996) 2 Comp LJ 281 : (1997) 24 CLA 30 : (2001) 103 Com Cases 984 (Del).

Expulsion of member by Board of Directors

Department's Circulars.—Department of Company Affairs by its *Circular No.* 32/75, dated 1-11-1975 has opined that an amendment of the articles of association which confers on the Board of Directors the power to expel a member is opposed to the fundamental principles of company jurisprudence and is *ultra vires* the company. For the complete text of circular see Notes under S. 41 under heading "Expulsion from membership".

This opinion of the Department has not found favour with the judiciary. The courts have upheld not only the power of expulsion but also the compulsory transfer of expelled member's shares against his wishes under signature of directors provided there is a provision to that effect in the company's articles. The Andhra Pradesh High Court upheld alteration of articles for this purpose, though the expulsion was not upheld on the facts of the case. *Gothami Solvent Oils Ltd. v. Mallina Bharathi,* (2001) 105 Com Cases 710 at 721 : (2001) 31 SCL 178 : (2001) 42 CLA 267 : (2001) 3 Comp LJ 127 : (2001) CLC 1377 (AP).

Adoption of new set of regulations

Department's Circular.—The Department has clarified: "A company can never replace its articles; it is only the regulations contained therein which may be changed. Accordingly the concerned company can adopt an entirely new set of regulations in place of those now contained in its existing articles by passing a special resolution to that effect in accordance with the provisions of section 31 of the Companies Act, 1956. The new set of regulations proposed to be adopted should form a part of the special resolution and the explanatory statement to be annexed to the notice of the general meeting under section 173(2) of the Act should set out all material facts concerning the proposed alterations in the existing articles. [*Circular letter No.* 8/32(31)/63-PR, dated 23-10-1963].

Alteration of articles in breach of contract and liability in damages

A company is not precluded from altering its articles even if by such alteration a breach of contract will be involved. No injunction can issue to prevent the adoption of a new article. But if thereby the company commits a breach of contract, it may be liable in damages to the other party to the contract. By effecting alterations in its articles a company cannot defeat or escape from its contractual obligations. *Southern Foundries, (1926) Ltd. v. Shirlaw,* (1940) 2 All ER 445 : (1940) 10 Com Cases 255 (HL).

In *Hari Chandana Yoga Deva v. Hindustan Co-op. Insurance Society Ltd.,* AIR 1925 Cal 690, the plaintiff had taken out a policy of life insurance in the defendant company entitling him to draw from the company a certain sum on a certain date. The company altered its articles by which such sums were made payable out of a special fund, which at the time the amount became payable to the assured was insolvent. It was held that "the effect of the alteration of articles was that it involved a fundamental breach of contract which the company had previously entered into with the plaintiff and in respect of that contract the (new) article was inapplicable.

In *Southern Foundries* (*Supra*) case it was held by the HOUSE OF LORDS that a company was not prevented from altering its articles by the fact that such an alteration would be a breach of contract, but that an action for damages may lie for the breach. In that case a director was by contract appointed to be a managing director for 10 years, and the articles provided that, "subject to the provisions of any contract," the managing director should cease to be managing director if he ceased to be a director. The articles were altered in such a way as to authorise another company to remove any director. The HOUSE OF LORDS held that there was an implied undertaking by the company not to remove the managing director and not to alter its articles so as to create a right to do so. Conse-

quently, the managing director was held entitled to damages for breach of contract. LORD PORTER said, (1940) AC 701 at pp. 740-1: "A company cannot be precluded from altering its articles thereby giving itself power to act upon the provisions of the altered articles—but so to act may nevertheless be a breach of contract if it is contrary to a stipulation in a contract validly made before the alteration. Nor can an injunction be granted to prevent the adoption of the new articles and in that sense they are binding on all and sundry, but for the company to act upon them will none the less render it liable in damages if such action is contrary to the previous engagements of the company." In *Cumbrian Newspapers Group Ltd. v. Cumberland & Westmorland Herald Newspaper & Printing Co. Ltd.*, (1986) 2 All ER 816 : (1986) BCLC 286 Ch D, SCOTT J said, at p. 306, that this dictum represented the law.

For a statement of the same principle, see *Mathrubhumi Printing & Publishing Co. Ltd. v. Vardhman Publishing Ltd.*, (1992) 73 Com Cases 80, 99 (Ker—DB), where it was held that a company may be held liable to pay compensation if an alteration of articles amounts to a breach of contract, but it does not mean that the alteration itself is invalid [at p. 98]. The court surveyed cases on the power of alteration at pp. 97-102.

Where compensation would not be an adequate remedy the court may restrain by injunction the company from changing its articles. This was the position in *British Murac Syndicate Ltd. v. Alperton Rubber Co. Ltd.*, (1915) 2 Ch 186. In this case the articles of a company provided that as long as 'M' was holding 5,000 shares in the company he would have the right to nominate two directors on the company's Board. He did so but the company refused to accept them. He insisted upon having them on the Board. The company tried to prevent this by changing articles and depriving him of the power of nomination. The court restrained the company from doing so. But see *State of Karnataka v. Mysore Coffee Curing Works Ltd.*, (1984) 55 Com Cases 70 (Kar), where the court refused to restrain the company from amending its Articles so as to cancel the power conferred therein on the State Government to nominate three directors including the chairman of the company. The court based its conclusion on the fact that the power conferred by sub-section (1) is unfettered except to the extent of the proviso to the sub-section. In our view, this decision is of doubtful validity. The Articles of Association constitute a contract between the company and its members. In this case, the company was modifying the contract unilaterally, which it was not entitled to do, even if the statutory procedure for alteration had been followed.

Thus it appears that the company will be precluded from altering its articles in that rare case only in which the situation is not otherwise remediable. *Baily v. British Equitable Assurance Co.*, (1904) 1 Ch 374, on appeal held the House of Lords that the principle is of general application and even a shareholder is presumed to know that the rights conferred by the articles are subject to the power of alteration provided by the law and he cannot complain unless he can show that the alteration sought to be effected is either (1) a breach of a separate contract made with him or with his class or (2) that it is not made *bona fide* or for the benefit of the company as a whole. *British Equitable Assurance Co. Ltd. v. Baily*, (1906) AC 35 (per LORD MAC NAGHTEN) (HL). See also *Chithambaram Chettiar (NPNM) v. Krishna Aiyangar*, ILR 33 Mad 36, where the pay of the secretary as specified in the articles was reduced by changing the articles and the company was not precluded from doing so. The right to alter articles by special resolution is not vested in the company but in the members and cannot be taken away by a contract made by the company. Such a contract cannot be implied. Even if such a contract is entered into, the right of the members to requisition a meeting and amend the articles by special resolution cannot be taken away. *Punt v. Symons & Co. Ltd.*, (1903) 2 Ch 506; *Allen v. Gold Reefs of West Africa Ltd.*, (1900) Ch 656; *Cumbrian Newspapers Groups Ltd. v. Cumberland and Westmorland Herald Newspaper and Printing Co. Ltd.*, (*Supra*). If the articles are validly altered, the company cannot be prevented from acting on the altered articles although it may involve a breach of contract. *Southern Foundries (1926) Ltd. v. Shirlaw*, (*Supra*).

Alteration against memorandum

One of the limitations envisaged by S. 31 upon the power of alteration is that there should be nothing in the altered articles which is inconsistent with the memorandum. See *British and American Trustee and Finance Corporation v. Couper,* (1894) AC 399 at 417, and *Andrews v. Gas Meter Co.,* (1897) 1 Ch 361 (CA); *Shyam Chand Nandi v. Calcutta Stock Exchange,* AIR 1949 Cal 337.

Contrary to the earlier beliefs which were generated by the decisions in *Hutton v. Scarborough Cliff Hotel Co.,* (1865) 62 ER 717, it has become an established fact since the case of *Andrews* (*supra*) that anything can be done by changing articles which is not forbidden by the memorandum expressly or impliedly.

Increase of members' liability

The liability of members cannot be increased either by asking them to contribute more capital or otherwise simply by changing articles. It requires consent of the members in writing as prescribed by S. 38.

§ For detailed notes see Notes under S. 38.

Increase in number of directors

Where the articles used the following words "Unless otherwise determined by a General Meeting the number of directors shall not be less than 5 nor more than 9", increasing the number of directors in a General Meeting does not amount to alteration of the articles and it does not require special resolution. *Gurprasad Kapoor v. Rameshwar Prasad,* (1933) 3 Com Cases 153, 158 and 164 : AIR 1933 All 344; *Topandas Mohanlal Advani v. Yeotmal Electric Supply Co.,* (1940) 10 Com Cases 133 : AIR 1940 Sind 87.

Alteration of articles by consent or by unanimous agreement

When all the shareholders interested in a company entered into an agreement which modified the articles of association, but was not drafted as a resolution nor passed at a general meeting, the articles could nevertheless be deemed to be effectively modified. This is on the basic principle of company law that all the shareholders of a company acting together can do anything *intra vires* the company. Section 31(1) does not undermine that principle but merely lays down the procedure whereby some only of the shareholders can validly alter the articles. *Cane v. Jones,* (1981) 1 All ER 533 (Ch D).

There can be a provision in the articles that a particular article or a set of articles will not be alterable without the consent of a named person. Such a provision is binding on the company though it remains subject to the company's superior statutory right of alteration. Such provisions are generally necessary to protect the special rights of the person concerned in the company. The protection can be afforded in one of the two ways. He can be allotted certain shares with special rights which are not alterable except with his consent. This method was adopted in *Cumbrian Newspaper Groups Ltd. v. Cumberland and Westmore Land Herald Newspaper & Printing Co. Ltd.,* (1986) 2 All ER 816: (1987) 2 Comp LJ 39. Second method is available to a private company in whose articles it can be provided that the shareholder whose special rights are to be protected will have multiple number of votes per share over the subject-matter of his interest. The validity of such a provision has been recognised by the House of Lords in *Bushell v. Faith,* (1970) 1 All ER 53 (HL).

§ For further details about variation of class rights, see Notes under S. 106, *post.*

Rectification of mistake in articles

A mistake, whether clerical or any other, in the articles of a company can only be rectified by altering the articles by special resolution in accordance with this section. It cannot be set right by application to Court. *Evans v. Chapman,* (1902) 86 LT 381; *Scott v. Frank*

F. Scott (London) Ltd., (1940) 3 All ER 508 : (1941) 11 Com Cases 127 (CA). See also SARKAR SPECIFIC RELIEF ACT, Edn. 1997 section 26(1).

The mere passing of a special resolution inconsistent with an existing article, is not enough unless it expressly alters the articles concerned. See HALSBURY'S, LAWS OF ENGLAND pp. 380-381 para 553 (Vol. 7(1) Fourth Edn. Reissue, 1988).

But in the case of a *quasi*-partnership company the court may prevent the articles to be acted upon if it is proved that they failed to reflect the members' true intention. *Caratti Holding Co. Pty. Ltd. v. Zampatti,* (1978) 52 ALJR 732 (PC); *Kounis v. Kounis,* (1987) 11 ACLR 854 (Aust); *Medefield Pty. Ltd.,* (1977) 2 ACLR 404 (Aust).

Retrospective alterations

Articles may be so altered as to have retrospective operation, *e.g.*, the insertion of a lien clause so as to give the company a lien on shares of members for debts incurred both before and after the insertion of the clause. *Allen v. Gold Reefs of West Africa,* (1900) 1 Ch 656. *Sidebottom v. Kershaw, Leese & Co. Ltd.,* (1920) 1 Ch 154. But alterations should not be such as to throw an increased liability on members, more than they contracted for when they became members. See section 38 and *Bailey v. New South Wales Medical Defence Union Ltd.,* (1995) 184 CLR 399 (Aust.) discussed in MAYSON, FRENCH & RYAN ON COMPANY LAW, 19th Edn., 2002-2003.

Section 31(2) cannot be understood to mean that any alteration made in the articles would have retrospective effect as if it were there from the inception of the articles of association. It is only for the limited purpose of making the alteration equally valid with other articles that it is to be treated as if it were originally there in the Articles. If the position were otherwise, then several transactions of the company could be unsettled by an alteration of the articles. The words of S. 31(2) "originally contained" do not mean "retrospectively contained". They are used only to indicate that newly added articles also become a valid part of the articles "originally contained", for otherwise, many a settled transactions would become unsettled. *Swaminathan M. v. The Chairman & Managing Director,* 1988 Writ LR 41, 51 (Mad) **followed** in *Mathrubhumi Printing and Publishing Co. Ltd. v. Vardhaman Publishers Ltd.,* (1992) 73 Com Cases 80, 97 (Ker—DB).

In *James v. Buena Ventura Nitrate Grounds Syndicate Ltd.,* (1896) 1 Ch 456, 466 : (1895-9) All ER Rep Ext 1968 it was held that validity of what has already been done by the company cannot be affected by a subsequent alteration of articles. A company cannot alter its articles so as to alter the director's remuneration with effect from a date prior to the date of the special resolution. *Swabey v. Port Darwin Gold Mining Co.,* (1889) 1 Meg 385 (CA); In *Pepe v. City and Suburban Permanent Building Society,* (1893) 2 Ch 311 the rules of the society were altered after a member had given notice to withdraw from the society, thus affecting this right to withdraw according to the earlier rules. A great caution, it seems, would now be necessary in taking away existing rights by altering articles because it may in circumstances amount to an oppression or unfair prejudice to a member *qua member*.

In a company limited by shares, when after a transfer is presented for registration, the company alters its articles by restricting the right to transfer the shares, with a view to preventing the registration of the particular transfer, the alteration does not deprive the applicant of his right to have the transfer registered in accordance with the articles before alteration. *Vardhman Publishers Ltd. v. Mathrubhumi Ltd.,* (1991) 71 Com Cases 1, 37 (Ker) **following** *McArthur Francis Whiney v. Gulf Line Ltd.,* (1909) SC 732. Upholding this principle but **reversing** the Single Bench decision on facts, the Division Bench held that in this case when transfer documents were first lodged there was no valid lodgement because the stamps were not cancelled as required by the Stamp Act and before there could be a valid lodgement the company had altered its articles which enabled it to refuse registration. This alteration was a valid exercise of the power under this section. It was neither confiscatory nor deprivatory of rights with retrospective effect. It was only prospective alteration and was as much applicable upon future share transfer applications as

upon an application which was presented again after having been rejected earlier on a technical ground. It could have been challanged either on the ground that it constituted a fraud on the minority or an oppression within the meaning of s. 397. *Mathrubhumi Printing and Publishing Co. Ltd. v. Vardhaman Publishers Ltd.*, (1992) 73 Com Cases 80 (Ker) (DB). The power to alter the articles is undisputably very wide. But the articles shall not be so altered as to deprive the minority of their rights. That means no majority of shareholders can, by altering the articles retrospectively, affect to the prejudice of the non-consenting owners of shares the right already existing under a contract nor take away the right already accrued. (*Mathrubhumi* case) (Ker—DB).

Notice of meeting for alteration of articles

Notice of meeting for alteration of articles should disclose full facts and be accompanied by a copy of the proposed amendments. *Bimal Singh Kothari v. Muir Mills Co. Ltd.*, (1952) 22 Com Cases 248 : AIR 1952 Cal 645; *Normandy v. Ind Coope & Co. Ltd.*, (1908) Ch 84. An amendment to the articles made without due notice is invalid. *Sardar Gulabchand v. Punjab Zamindari Bank Ltd.*, (1940) 10 Com Cases 188, 199 (Lah); because there cannot be an alteration behind the back of a member, *Madhavramachandra Kamath v. Canara Banking Corpn. Ltd.*, (1941) 11 Com Cases 78 : AIR 1941 Mad 354.

§ See also Notes under sections 173 and 189.

Omnibus resolution to amend several articles

Where an omnibus resolution is proposed to be passed for amendment of several articles, and certain amendments are proposed in the general meeting or it is proposed to drop certain clauses, the question arises whether such a resolution can be passed. Amendment of the special resolution is valid provided the notice convening the meeting contains words such as 'to consider and, if thought fit to pass with or without modification, the following resolution as a special resolution'. The amendment must be within the scope of the notice and should not commit the meeting to anything beyond the business proposed in the resolution of which notice had been sent to the members.

Irregular alterations

An alteration which has been irregularly pushed through is liable to be set aside by court action. But court may have regard to a long course of practice and recognise as valid an alteration which has been acted upon for many years. *Ho Tung v. Man on Insurance Co.*, (1900) 2 AC 232; *Duff v. Galvin*, 1934 NZLR 158. A very minor defect arising out of strict non-conformity with the provisions contained in section 173(2) might not render an amendment of the articles null and void. *Joseph Michal v. Travancore Rubber & Tea Co. Ltd.*, (1986) 59 Com Cases 898 (Ker). It has been held that an article which has been improperly altered may bind the company when it is incorporated in a contract with a third party. *Muirhead v. Forth and North Sea Steamboat Mutual Insurance Assn.*, (1894) AC 72 (HL).

Ratification of directors' irregular acts

Where an act is within the competence of the company but has been done by the directors in an irregular manner the same can be ratified by the shareholders by an ordinary resolution and that would not amount to an alteration of the articles. *Grant v. United Kingdom Switchback Rly.*, (1888) 40 Ch 135.

Power of CLB to order alterations

The CLB is empowered under S. 404 either to order the alteration of a company's memorandum or articles or prevent an alteration as may be necessary for putting an end to complaints of oppression or mismanagement.

§ For a study of this subject, see Notes under S. 404, *post.*

Conversion of public company into private company [Sub-section (1) (proviso)]

The proviso to sub-section (1) applies only to cases of converting a public company into a private company by means of altering the articles so as to comply with the provisions of section 3(1)(iii).

It does not apply to cases of reducing the membership of a public company below seven as such reduction does not convert a public company into a private company. Nor does it offend any provision of the Act. But its effect is to attach personal liability to the members as provided in section 45, and to expose it to the danger of being wound up under section 433(d).

§ See also Notes under the heading "Companies (Amendment) Act, 1960" where the significance of the proviso to sub-section (1) to this section is explained in the Committee Report on the amendment in the 1956 Act by the 1960 Amendment Act.

Special Resolution by postal ballot in case of Listed Public Company.—When a listed public company wants to convert itself into a private company, necessary changes in its articles of association would have to be made by a special resolution passed by means of a postal ballot. [cf. Section 192A] See Rule 4(b) of Companies (Passing of the Resolution by Postal Ballot), Rules, 2001 in *Appendix* 41.

Approval of Central Government.—For getting the approval of the Central Government for alteration of the Articles converting a public company into a private company, application has to be made in accordance with Form No. 1-B and as provided in Rule 4-B of the Companies (Central Government's) General Rules and Forms, 1956 in *Appendix* 1 as per the following Departmental instructions:—

Departmental instructions.—"The application is to be made within three months from the passing of the special resolution for conversion. The applicant company has to give *inter alia* information relating to its existing capital structure, reasons for conversion, number of members of the company at the time when the decision for conversion was taken and also has to attach current Memorandum and Articles of Association, latest balance-sheet and profit and loss account. A copy of the minutes of the meeting at which the decision for converting a company was taken is also to be attached. The application is also to be accompanied by treasury challan duly receipted or fee payable as per table of fees prescribed by Government." [For table of fees see Notes under section 637-A].

In case the Central Government approves of the conversion, the company has to file a printed copy of its articles, as altered by it, within one month of the date of receipt of the order of approval under sub-section (2-A) of section 31 of the Companies Act, 1956.

Guiding principles : Government approval for converting public into private company.—In considering applications for conversion, the guiding criterion is whether a proposal would be in the best interests of the company itself and that there is a large measure of agreement among the shareholders to the proposed conversion. In particular, an attempt is made to ascertain if the proposal is prompted merely by a desire to overcome the restrictions imposed by some of the provisions of the Companies Act, which apply only to public companies *e.g.*, sections 295, 372, etc., or if the conversion is generally needed for carrying on the business of the company more efficiently. A company having more than 25 shareholders is advised to obtain the written consent of all the shareholders who had not voted for the conversion before Government's approval is considered. To protect the interests of unsecured creditors, the Department has also been insisting on companies obtaining the consent to conversion of every creditor to whom the company owes substantial amounts." (Para 68, *Sixth Annual Report for the year ended March 31, 1962*).

In almost all cases where a public company is converted into a private company, one of the motives which prompts such conversion is to avoid the restrictions imposed on public companies and enjoy the special privileges and exemptions available to private companies under the Act. If the Central Government should refuse to accord its approval to conversion on this ground, it will be improper and legally challengeable. (See further Notes under section 44).

After a public company is converted into a private company, it is important that a copy of the special resolution authorising the conversion and altering the Articles so as to comply with section 40(1) should be included in every copy of the Articles issued thereafter. The company must be in a position to give the certificate required by section 161(2)(b).

Secretarial Action Points for conversion of public company into private company

1. Hold a Board meeting to decide on the conversion

2. Make application to the Registrar of Companies, accompanied by the following documents:—

(a) a copy of the Annual Report of the company for the last three years

(b) a certified copy of the Board resolution

3. Upon receipt of approval from the Registrar of Companies, fix up the day, date, time, place and agenda for the general meeting and approve the notice of general meeting to pass a special resolution

4. Send notice of the general meeting to the shareholders, auditors, debenture trustees (if any) and three copies each to all the stock exchanges where the shares of the company are listed

5. Hold general meeting and pass special resolution; in case of listed public company, pass special resolution by postal ballot [*See S. 192-A*].

6. File special resolution along with explanatory statement with the ROC

7. Apply for and obtain fresh certificate of incorporation from Registrar

8. Make necessary changes in the memorandum and articles, letter heads, records, documents and registers of the company

9. Adopt a new common seal in the next Board meeting.

Reconversion of deemed public company into private company

Department's Clarification I.—The Department has clarified that reconversion of a deemed Public Company into a private company, even if such reconversion needs an alteration in the articles of association, will not have to go through the procedure laid down in proviso to section 31(1), [*Circular No.* 11/72(32/1/72-CL-III), dated 19-5-1972].

§ Also see Notes below section 43A, *post.*

Clarification II.—"Clause 5 of the Companies (Amendment) Bill, 1972 seeks to amend section 43A of the Companies Act, 1956, with a view to enlarging the scope of the section. In view of this application under the proviso to sub-section (1) of section 31 of the Act for conversion of a public company into a private company should be critically examined and conversion allowed only if the applicant company is closely held one having no public interest involved in it." [*Circular No.* 34/72, dated 3-10-1972].

Note : These circulars have become, redundant on Section 43A, except sub-sec. (2), becoming inoperative w.e.f. 13-12-2000.

Delegation of powers to ROCs.—The powers of the Central Government under this section have been delegated to the Registrar of Companies. (*Notification GSR No.* 281(E), dated 21-3-1995.) (See Notes under section 637). Earlier this power was exercised by Regional Director.

Filing of resolution and approval of Registrar.—In the case of conversion of public company into private company, two filings of the resolution with the Registrar are required, first, a copy of the special resolution altering the Articles for converting the public company into a private company will have to be filed as required by, and within the time provided in section 192. Then after obtaining approval of the Central Government, another filing of the articles as altered as required by sub-section (2-A) of this section has to be made within one month of the date of receipt of the order of approval.

§ See further Rule 20-A of Companies (Central Government's) General Rules and Forms, 1956 (*Appendix* 1) regarding filing a copy of the application to Registrar.

ICSI Guidance Note on Compliance Certificate (August 2003)

The ICSI has issued a Check List for issue of Compliance Certificate under proviso to Sec. 383A(1) in respect of the matters specified under Rule 3 of the Companies (Compliance Certificate) Rules, 2001.

Paragraph 30 under Rule 3 relates to alteration of articles of association and read as follows:

***Paragraph-30.*—The company has altered its Articles of Association after obtaining approval of members in the general meeting held on.....and the amendments to the Articles of Association have been duly registered with the Registrar of Companies.**

Prescribed Check List

ARTICLES OF ASSOCIATION [Item (b)]

Check whether the Articles were altered during the year. If so, check whether :

(i) the Board of Directors have passed a resolution approving the alteration of articles;

(ii) the company had called and held the general meeting and obtained approval of the company in general meeting by a special resolution for the alteration;

(iii) copy of the special resolution containing the amendments to the Articles of Association along with Form No. 23 have been duly filed with the ROC within 30 days; and

(iv) the alteration had been incorporated in all copies of Articles.

Conversion of a Public Company (other than Section 43A Company) into a Private Company*

Check whether:

(i) Board resolution was passed for convening a general meeting to obtain consent of the members and submission of application to ROC;

(ii) notice of general meeting was sent to all the members and Auditors of the company;

(iii) in case of listed company, 3 copies of notice was sent to Stock Exchange where the shares of the company are listed;

(iv) special resolution for conversion of Public Company into Private Company for alteration of Articles of Association and for incorporation of essential characteristics were passed;

(v) minutes were duly recorded in the minutes book;

(vi) copy of the proceedings were sent to the concerned Stock Exchange.

(vii) within 30 days, the Company had filed Form 23 with the Registrar of Companies;

(viii) within 3 months from the date of passing the special resolution, an application in form 1B with requisite document were filed with the ROC;

(ix) The ROC had issued a fresh/modified Certificate of Incorporation;

(x) The Articles of Association were re-printed and one copy was filed with the ROC within one month from date of receipt of approval from ROC;

(xi) Alteration of the name had been effected on the Memorandum, Articles of Association, common seal, letter head of the company etc.

* This matter is not directly referred to in the 33 paragraphs appended to the Form prescribed under the Companies (Compliance Certificate) Rules. The Check List given by the ICSI under 'Check List for Other Compliances' [4. Sundry Items (d)] is for the guidance of CSP who may, in the course of his scrutiny, come across non-compliance with regard to this matter. CSP need not qualify such non-compliance.

§ For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

§ For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

Change of Registration of Companies

S. 32. Registration of unlimited company as limited, etc.—(1) Subject to the provisions of this section,—

(a) a company registered as unlimited may register under this Act as a limited company; and

(b) a company already registered as a limited company may re-register under this Act.

(2) On registration in pursuance of this section, the Registrar shall close the former registration of the company, and may dispense with the delivery to him of copies of any documents with copies of which he was furnished on the occasion of the original registration of the company; but, save as aforesaid, the registration shall take place in the same manner and shall have effect, as if it were the first registration of the company under this Act.

(3) 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, to, with or on behalf of the company before the registration, and those debts, liabilities, obligations and contracts may be enforced in the manner provided by Part IX of this Act in the case of a company registered in pursuance of that Part.

NOTES

Eng. Act, 1948 : Sec. 16.
Eng. Act, 1985 : Sec. 677.

Previous Act : Sec. 67.

Scope of section

Conversion of unlimited company into limited company.—Clause (a) of sub-section (1) gives liberty to a company which has been registered with unlimited liability to get itself registered with limited liability. The whole procedure of registering a new company would have to be followed, for it is not a mere question of change of liability.

Re-registration of company already registered as limited company.—It is difficult to understand clause (b) of sub-section (1). Possibly it means that a company already limited by shares may be re-registered, as a company limited by guarantee or *vice versa*. It might, perhaps also cover cases of companies which are declared entitled to be registered under this Act by Part IX of the Act, namely, companies registered under the earlier Acts, under a different pattern of registration.

Note further that as per sub-section (2), registration or re-registration of a company under this section will proceed in the same manner as the first registration, and all the formalities as to procedure, filing etc. will have to be gone through.

As regards making the liability of the directors of a limited company unlimited, see the provisions of section 323.

It may be noted that there is no provision in the Act to convert a limited company into unlimited. For such conversion consent of all the members of the company will be necessary. In the case of such company there need be no obligation of disclosure of several matters in the same way as in the case of individuals and partnership firms.

In case a company limited by shares is sought to be re-registered as a company limited by guarantee without share capital, it would seem to be hit by s. 100 and the procedure for reduction of capital would have to be gone through.

The English Companies Act of 1967 provides for conversion of a limited company into an unlimited company and *vice versa* under sections 43 and 44.

General Provisions with Respect to Memorandum and Articles

S. 33. Registration of memorandum and articles.—(1) There shall be presented for registration, to the Registrar of the State in which the registered office of the company is stated by the memorandum to be situate—

(a) the memorandum of the company;

(b) its articles, if any; and

[1][(c) the agreement, if any, which the company proposes to enter into with any individual for appointment as its managing or whole-time director or manager.]

(2) A declaration[2] by an advocate of the Supreme Court or of a High Court, an attorney or a pleader entitled to appear before a High Court, or [3][a secretary, or a chartered accountant, in whole-time practice in India] who is engaged in the formation of a company, or by a person named in the articles as a director, [4][* * *], manager or secretary of the company, that all the requirements of this Act and the rules thereunder have been complied with in respect of registration and matters precedent and incidental thereto, shall be filed with the Registrar; and the Registrar may accept such a declaration as sufficient evidence of such compliance.

[5][*Explanation.*—For the purposes of this sub-section, "chartered accountant in whole-time practice in India" means a chartered accountant within the meaning of clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 (38 of 1949) who is practising in India and who is not in full time employment.]

(3) If the Registrar is satisfied that all the requirements aforesaid have been complied with by the company and that it is authorised to be registered under this Act, he shall retain and register the memorandum, the articles, if any, and the agreement referred to in clause (c) of sub-section (1), if any.

NOTES

Eng. Act, 1948 : Sec. 12.
Eng. Act, 1985 : Secs. 10 and 12.

Previous Act : Sec. 22.

Agreement with managerial personnel [Sub-section (1)(c)]

Sachar Committee recommendations.—"Clause (c) of sub-section (1) of this section refers to the agreement proposed to be entered into for appointing managing agents or secretaries and treasurers. We feel that this clause should rather be substituted as follows:—

(c) The agreement, if any, which the company proposes to enter into with any individual, as Director, Managing Director or whole-time director.

Sub-section (2) of this section provides for a declaration to be filed by an advocate, a pleader, an attorney or a chartered accountant. We feel that a practising company secretary is equally competent to file this declaration and should be included in this sub-

1. Subs. by the Companies (Amendment) Act, 1988 (w.e.f. 15-6-1988), for clause (c)[* * * *], the words already omitted by Act, XVII of 1969 by reason of the abolition of the system of managing agents and secretaries and treasurers.
2. Prescribed Form of Declaration is Form No. 1 of the Co's. (Central Govt's) General Rules & Forms, 1956.
3. The words "a chartered accountant practising in India" subs. by the Companies (Amendment) Act, 1988, s. 6(b)(i), (w.e.f. 15-6-1988).
4. Omitted the words 'managing agent' and 'secretaries and the treasurers' by the Companies (Amendment) Act, 1988, s. 6(b)(ii), (w.e.f. 15-6-1988).
5. Ins. by the Companies (Amendment) Act, 1988, s. 6(6)(iii) w.e.f. 15-6-1988, *vide* GSR No. 559(E), dt. 10-6-1988.

section. Necessary addition may, therefore, be made in this section providing for a declaration to be filed alternatively also by a practising member of the Institute of Company Secretaries of India." (Para 17.8 of the *Sachar Committee Report*).

Companies (Amendment) Act, 1988.—As recommended by Sachar Committee, this section was amended w.e.f. 15-6-1988 by Companies (Amendment) Act, 1988. Clause 6 of Notes on clauses stated as under:

"Sub-clause (a)—With the abolition of the office of managing agents and secretaries and treasurers, reference to such office in section 33 is being substituted by reference to managing and whole-time directors.

Sub-clause (b)—Statutory declaration of compliance of the formalities of incorporation which is presently authorised to be given by a practising advocate, or a Chartered Accountant may as well be given by a practising Company Secretary. The amendment proposed in this clause seeks to achieve this."

As per section 33(1)(c) an agreement which the company proposes to enter into for appointment of managing or whole-time director or manager is required to be filed along with the memorandum and Articles of Association at the time of registration of a company. Further, it may be noted that after incorporation, copies of the agreement or resolution relating to the appointment of managing director is to be filed with the Registrar within thirty days of executing the agreement or passing the resolution under section 192(4)(c).

Declaration of compliance [Sub-section (2)]

The statutory declaration of compliance can be signed by a secretary in whole-time practice, as defined in section 2 (45A), besides an advocate of the Supreme Court or High Court, an attorney or pleader entitled to appear before High Court or Chartered Accountant in whole-time practice, as defined in the Explanation. The words 'in whole-time practice in India' are used now to apply in respect of all the concerned professionals. The Act does not define the said expression in relation to an advocate, attorney or pleader. The said expression has also not been defined in the Advocate's Act, in the absence of which, the statutory declaration can only be signed by an advocate or attorney, who is engaged in the practice of the profession on whole-time basis and is not employed elsewhere. It may be noted that a director, manager or secretary named in the articles can also sign the declaration.

Prescribed Form.—For Form of Declaration, see Form No. 1 in *Appendix* 1.

Requirement of Stamp Act

Article 39 of the First Schedule to the Indian Stamp Act, 1899 prescribe the stamp payable for the memorandum of association of a company. The rate of stamp duty may vary from State to State. For the Schedule of stamp duty refer K. KRISHNAMURTHY'S INDIAN STAMP ACT, Eighth Edn., 2002. The printed copy of the memorandum and articles should be stamped before they are signed and dated. The memorandum of any association not formed for profit and registered under section 25 of the Companies Act, 1956 is exempted from stamp duty.

Registration fee

Table of fees.—The registration fee is payable at the time of filing the documents for incorporation of a company, on the scale of fees prescribed in Schedule X (as amended by SO 419(E), dated 27-4-2000 (w.e.f. 1-5-2000) and *vide* Notfn. SO 658(E), dated 12-7-2000).

For convenience, a ready reckoner for registration fee payable w.e.f. 1-5-2000 on different amounts of nominal share capital is given hereunder:

Ready Reckoner for the Registration Fee w.e.f. 1-5-2000

Authorised Share Capital (Rs.)	Registration Fee Payable (Rs.)	Authorised Share Capital (Rs.)	Registration Fee Payable (Rs.)
1,00,000	**4000-00**	**20,00,000**	**46,000-00**
1,50,000	5500-00	20,50,000	47,000-00
2,00,000	7000-00	21,00,000	48,000-00
2,50,000	8500-00	21,50,000	49,000-00
3,00,000	10000-00	22,00,000	50,000-00
3,50,000	11500-00	22,50,000	51,000-00
4,00,000	13000-00	23,00,000	52,000-00
4,50,000	14500-00	23,50,000	53,000-00
5,00,000	**16000-00**	24,00,000	54,000-00
5,50,000	17000-00	24,50,000	55,000-00
6,00,000	18000-00	**25,00,000**	**56,000-00**
6,50,000	19000-00	25,50,000	57,000-00
7,00,000	20000-00	26,00,000	58,000-00
7,50,000	21000-00	26,50,000	59,000-00
8,00,000	22000-00	27,00,000	60,000-00
8,50,000	23000-00	27,50,000	61,000-00
9,00,000	24000-00	28,00,000	62,000-00
9,50,000	25000-00	28,50,000	63,000-00
10,00,000	**26000-00**	29,00,000	64,000-00
10,50,000	27000-00	29,50,000	65,000-00
11,00,000	28000-00	**30,00,000**	**66,000-00**
11,50,000	29000-00	30,50,000	67,000-00
12,00,000	30000-00	31,00,000	68,000-00
12,50,000	31000-00	31,50,000	69,000-00
13,00,000	32000-00	32,00,000	70,000-00
13,50,000	33,000-00	32,50,000	71,000-00
14,00,000	34,000-00	33,00,000	72,000-00
14,50,000	35,000-00	33,50,000	73,000-00
15,00,000	36,000-00	34,00,000	74,000-00
15,50,000	37,000-00	34,50,000	75,000-00
16,00,000	38,000-00	35,00,000	76,000-00
16,50,000	39,000-00	35,50,000	77,000-00
17,00,000	40,000-00	36,00,000	78,000-00
17,50,000	41,000-00	36,50,000	79,000-00
18,00,000	42,000-00	37,00,000	80,000-00
18,50,000	43,000-00	38,00,000	82,000-00
		39,00,000	84,000-00
		40,00,000	**86,000-00**

Authorised Share Capital (Rs.)	Registration Fee Payable (Rs.)	Authorised Share Capital (Rs.)	Registration Fee Payable (Rs.)
41,00,000	88,000-00	**15,00,00,000**	**8,56,000-00**
42,00,000	90,000-00	16,00,00,000	9,06,000-00
43,00,000	92,000-00	17,00,00,000	9,56,000-00
44,00,000	94,000-00	18,00,00,000	10,06,000-00
45,00,000	96,000-00	19,00,00,000	10,56,000-00
46,00,000	98,000-00	**20,00,00,000**	**11,06,000-00**
47,00,000	1,00,000-00	21,00,00,000	11,56,000-00
48,00,000	1,02,000-00	22,00,00,000	12,06,000-00
49,00,000	1,04,000-00	23,00,00,000	12,56,000-00
50,00,000	**1,06,000-00**	24,00,00,000	13,06,000-00
51,00,000	1,07,000-00	**25,00,00,000**	**13,56,000-00**
52,00,000	1,08,000-00	26,00,00,000	14,06,000-00
53,00,000	1,09,000-00	27,00,00,000	14,56,000-00
54,00,000	1,10,000-00	28,00,00,000	15,06,000-00
55,00,000	1,11,000-00	29,00,00,000	15,56,000-00
56,00,000	1,12,000-00	**30,00,00,000**	**16,06,000-00**
57,00,000	1,13,000-00	31,00,00,000	16,56,000-00
58,00,000	1,14,000-00	32,00,00,000	17,06,000-00
59,00,000	1,15,000-00	33,00,00,000	17,56,000-00
60,00,000	**1,16,000-00**	34,00,00,000	18,06,000-00
65,00,000	1,21,000-00	**35,00,00,000**	**18,56,000-00**
70,00,000	**1,26,000-00**	36,00,00,000	19,06,000-00
75,00,000	1,31,000-00	37,00,00,000	19,56,000-00
80,00,000	**1,36,000-00**	38,00,00,000	20,06,000-00
85,00,000	1,41,000-00	39,00,00,000	20,56,000-00
90,00,000	**1,46,000-00**	**40,00,00,000**	**21,06,000-00**
95,00,000	1,51,000-00	41,00,00,000	21,56,000-00
1,00,00,000	**1,56,000-00**	42,00,00,000	22,06,000-00
2,00,00,000	2,06,000-00	43,00,00,000	22,56,000-00
3,00,00,000	2,56,000-00	44,00,00,000	23,06,000-00
4,00,00,000	3,06,000-00	**45,00,00,000**	**23,56,000-00**
5,00,00,000	3,56,000-00	46,00,00,000	24,06,000-00
6,00,00,000	4,06,000-00	47,00,00,000	24,56,000-00
7,00,00,000	4,56,000-00	48,00,00,000	25,06,000-00
8,00,00,000	5,06,000-00	49,00,00,000	25,56,000-00
9,00,00,000	5,56,000-00	**50,00,00,000**	**26,06,000-00**
10,00,00,000	**6,06,000-00**	1,00,00,00,000	51,06,000-00
11,00,00,000	6,56,000-00	2,00,00,00,000	1,01,06,000-00
12,00,00,000	7,06,000-00	3,00,00,00,000	1,51,06,000-00
13,00,00,000	7,56,000-00	4,00,00,00,000 and above	2,00,00,000
14,00,00,000	8,06,000-00		

(Maximum fee not to exceed Rs. Two crores in any case)

I. Amendment to Schedule X to the Companies Act and of Companies (Central Government's) General Rules and Forms, 1956.

Press Note No. 7 (Series 2000), dated 28-4-2000.—The rate of fees payable by the companies to the Registrar of Companies for filling, etc., of various forms and returns under various provisions of Companies Act, 1956, have been revised with effect from May 1, 2000. This revision has been done by notifying a new Schedule X in the Gazette of India Extraordinary, dated April 27, 2000. This Schedule supercedes the earlier Schedule X.

2. Further the Companies (Central Government's) General Rules and Forms, 1956, have also been amended for revision of fees in respect of certain matters as shown below:

(*i*) For filing of Form 13 under rule 6(c) the fee has been revised from existing Rs. 10 to Rs. 50;

(*ii*) For registering any document under rule 20 in pursuance of section 601 of the Companies Act, 1956, relating to a foreign company, the fee has been revised from existing Rs. 200 to Rs. 1,000;

(*iii*) Fees payable under rule 21A(7) to Registrar of Companies for inspecting any document in pursuance of section 610(1)(a) has been revised from existing Rs. 10 to Rs. 50;

(*iv*) Fees payable under rule 21A(8)(i) to the Registrar of Companies for requiring a certificate of incorporation in pursuance of section 610(1)(b) has been revised from existing Rs. 10 to Rs. 50.

2.2 Relevant Notification (GSR No. 363(E)) relating to amendment in Companies (Central Government's) General Rules and Forms, 1956, has been issued on April 27, 2000.

3. All companies and individuals are request kindly to note these revised rates which will come into effect from May 1, 2000.

4. Copies of these two notifications and this press note has been placed at the web page of the Department of Company Affairs at the Internet address http://www.nic.in/dca.

II. Schedule X amended w.e.f. 4-8-2000.

PIB Press Release, dated 4-8-2000.—The Government (Department of Company Affairs) has issued a Notification amending further Schedule X of the Companies Act. Accordingly, the existing paragraph 1.3 shall read : "for filing a notice of any increase in the nominal share capital of a company, the difference between the fees payable on the increased share capital on the date of filing the notice for registration of company and the fees payable on existing authorised capital, at the rates prevailing on the date of filing the notice."

The amended Schedule has come into force with immediate effect.

The amendment has been effected under sub-section (1) of section 641 of the Companies Act, 1956.

Earlier, the Schedule X was amended by a notification with effect from May 1, 2000.

Guidelines for Additional Fees for belated filing of documents

Press Note No. 3/94, dated 16-6-1994.—Government has prescribed Guidelines for payment of additional fees in case of documents filed belatedly with the Registrar of Companies *vide* its Press Note No. 3/94, dated 16-6-1994 issued by the Department of Company Affairs, Ministry of Law, Justice and Company Affairs. These Guidelines have been issued in order to bring uniformity in the approach of different Registrars of Companies and to bring down the pendency of a large number of documents required to be registered with ROCs, so that the document filed with ROCs are registered without any delay and are made available to public for inspection.

Text of Guidelines.—For the text of the Guidelines see under Schedule X.

Refund of excess Registration Fees deposited by companies for Form No. 5

General Circular No: 7/2003, Dt. 27-1-2003.—The Department had issued a notification No.S.O.419 (E) dated 27th April, 2000 revising Schedule X to the Companies Act, 1956 for filing a notice for increase in the nominal share capital of a Company. In the said notification an anomaly had crept in, on arriving at the difference between the fees payable on the nominal share capital on the date of filing of the notice and the fees paid on the nominal share capital before the increase. Therefore, by a further notification of No. S.O. 658(E) dated 12th July, 2000 effective from 12th July, 2000, the said anomaly was removed. The notification had come to notice of the public after a few days and during the intervening period, a few Companies had paid fees calculated on the basis of the notification dated 27th April, 2000 and thereby they had paid excess fees for registration of Form No. 5.

2. Companies have approached the department and courts for refund of the excess registration fees paid by them on account of the said anomaly.

3. The department has decided in consultation with Integrated Finance Division to refund the excess registration fees paid by Companies on or after 12.7.2000. It is, hereby, clarified that Companies may seek refund by making a fresh request to the concerned Registrar of Companies (ROC) with proof of excess payment. It is further clarified that only the actual excess registration fees and interest, if any, charged by the ROC on late filing of Form No.5 would be refundable. The Companies will not claim any cost and interest.

4. ROC concerned will forward the claim of the Company duly certified by the concerned Pay & Accounts Officer to the department for issue of "Refund Sanction Order".

5. It is further clarified that no other notification other than notification No. S.O. 419(E) dated 27th April, 2000 and notification No. S.O. 658(E) dated 12th July, 2000 only are dealt with herein above.

6. This issues with the concurrence of Integrated Finance Division *vide* their Diary No. 51/CA/03 dated 20.01.2003.

[*Issued by Government of India Ministry of Finance and Company Affairs, Department of Company Affairs (No.2/5/2002-CL.V)*].

Satisfaction of Registrar [Sub-section (3)]

On the presentation of the documents and declaration mentioned in sub-sections (1) and (2) the Registrar has to be satisfied not only that the requirements of sub-sections (1) and (2) have been complied with but also whether the provisions of the other sections of the Act such as the requirement as to the number of subscribers, the lawful nature of the object for which the company is formed, the name being not undesirable within the meaning of section 20, are duly complied with; and not only that, whether the documents bear the proper stamp duty and the conditions imposed by any other law for the time being in force are all fulfilled.

It is not as though the Registrar is bound to register the company immediately on the presentation of the documents mentioned in sub-sections (1) and (2). The requirement of the sub-section that the Registrar is further to be satisfied that the company "is authorised to be registered under this Act" is wide enough to empower him to see that all legal requirements are satisfied, if there is any defect he may return the documents for rectification. *Re, Barned's Banking Co. Peel's* case, (1867) 2 Ch App 674. He can rightly refuse to register a company where the object for which it is formed is unlawful. *R. v. ROC, ex p. More,* (1931) 2 KB 197 : (1932) 2 Com Cases 99. (Sale of lottery tickets in England was the object of Company in the case.) The duty of the Registrar as to registration is not purely ministerial. He will consider whether the requirements of the Act have been complied with and refuse registration if they are not, and he will also refuse registration where, in his opinion, the name of the company is undesirable (See s. 20). But if he improperly refuses to register, he may be compelled to register by a writ of *mandamus. R. v. ROC, ex parte, Bowen,* (1914) 3 KB 1161.

To the extent to which the Registrar is required to satisfy himself as to whether the requirements for registration have been complied with, his decision is within his powers and cannot be interfered with by the Court unless it is perverse or clearly wrong. See *Bowman v. Secular Society,* 1917 AC 406 : *R. v. ROC,* (1912) 3 KB 23; *R. v. ROC, ex parte, Bowen, (Supra)*; *R. v. ROC, (supra); Cf. Cotman v. Brougham,* 1918 AC 514 at 519 and 523.

Duty of Registrar of Companies

In *T.V. Krishna v. Andhra Prabha (P.) Ltd.,* (1960) 30 Com Cases 437 at 446-447 : AIR 1960 AP 123, the Andhra Pradesh High Court said : "It is manifest that once the conditions envisaged in paragraphs (1) and (2) are satisfied the Registrar has no option but to register the company. It is not competent for him to refuse registration on any extraneous considerations or for any reason other than non compliance with the provisions of sub-sections (1) and (2). The only duty cast on the registrar is to see that the requirements prescribed by sub-sections (1) and (2) are complied with. It is not within his prov-

ince to make enquiries into matters which are unconnected with the conditions enumerated in sub-sections (1) and (2) or into collateral matters to probe into the motives of the promoters". The allegation in this case was that the company was formed to affect the future interest of the company's workers. The court expressly pointed out that the Registrar would be exceeding his jurisdiction by going into questions of that kind. See also *Executive Board of the Methodist Church in India v. Union of India,* (1985) 57 Com Cases 443 (Bom).

Judicial review and writ remedies

A writ cannot be issued to cancel the registration of a company under the Companies Act. *Malik Mohamed v. Capital Stock Exchange Kerala Ltd.,* (1991) 72 Com Cases 333 (Ker).

Under the doctrine of judicial review a registration can be declared to be a nullity where the company ought not to have been registered. But this power cannot be used in reference to a company whose existence is not confirmed by the public register because the formalities for incorporation required by national law had not been complied with. *Ubbink-Isolatie BV v. Dak-en Wandtechniek BV,* (1990) BCLC 182 CJEC (Court of Justice of European Community).

Registration of branch in Member State of European Community

An English company applied for registration of a branch in Denmark. Registration was refused on the ground that the registration requirements of Danish law, e.g., the requirement of minimum share capital, were not complied with. The question was whether the refusal was contrary to the community law. The court held that it was contrary to Articles 52 and 58 of the Treaty for a member state to refuse to register a branch of a company in the circumstances of the instant case. The court said that the fact that the national of a member state who wished to set up a company chose to do so in a member state whose rules of company law seemed the least restrictive and to set up branches in some other member states did not, in itself, constitute an absue of the right of establishment. The right to form a company in accordance with the law of a member state and to set up branches in some other member states was inherent in the exercise, in a single market, of the freedom of establishment guaranteed by the Treaty. The fact that a company did not conduct any business in the member state in which it had its registered office and pursued its activities only in the member state in which its branch office was established was not sufficient to prove the existence of abuse or fraudulent conduct which would have entitled the state to deny that company the benefit of the community provisions relating to the right of establishment. *Centros Ltd. v. Erhvervs-og Selskabsstyrelsen,* (2000) 2 BCLC 68 (ECJ).

Power of Attorney for correction of documents

The Department has issued Circular No. 1/95, dated 16-2-1995 on this subject.

§ For text see Notes under s. 15 *ante.*

Registration of Memorandum

§ Refer to check list of activities for formation of company under s. 12.

Registration of Asset Management Companies [AMCs]/other intermediaries

Government has formulated a set of Guidelines for registration of Asset Management Companies in consultations with SEBI. No company can be registered under this Act without the memorandum and articles of association being approved by SEBI. [*Circular No.* 4/92, dated 2-9-1992].

§ See *Department's Circular No.* 4/92, dated 2-9-1992 and *No.* 5/94, dated 15-4-1994 reproduced under S. 20.

§ For the text of the Guidelines for "Asset Management Companies" (AMCs), See SEBI Mutual Funds Regulations, 1996, "Chapter IV Constitution and Management of Assets Management Company and Custodian" in *Appendix* 184.

Secretarial Practice Notes:

Check that:

(i) memorandum and articles of the company filed with the Registrar duly stamped and signed by signatories thereto and witnessed.

(ii) a declaration in Form 1 by an advocate of Supreme Court, or of a High Court, an attorney or a pleader entitled to appear before a High Court or a Secretary or a chartered accountant in whole-time practice in India, or by a person named in the articles as a director, manager or secretary of the company, filed with the Registrar.

(iii) Fees based on nominal capital (Schedule X) paid by Bank Draft in favour of Registrar of Companies.

(iv) Power of attorney on a non-judicial stamp paper of requisite value (refer Stamp Act of the concerned State or Union territory) by the subscribers to the memorandum and articles of association in favour of one of them or any professional for making necessary corrections on their behalf in the documents for registration and to collect the certificate of incorporation filed with ROC alongwith documents for registration.

(v) Form Nos. 18, 29 and 32 are also usually filed along with the memorandum and articles. There is no requirement to file form No. 29 in case of a private limited company.

(vi) Copy of letter making available the proposed name is filed with ROC alongwith documents for registration.

Documents involved.—(1) Memorandum and Articles, (2) Letter of authority on a non-judicial stamp paper, (3) Form Nos. 1, 1A, 18, 29 and 32. Form 29 is required only for a public limited company, (4) Registrar's letter indicating availability of the name.

S. 34. Effect of registration.—(1) On the registration of the memorandum of a company, the Registrar shall certify under his hand that the company is incorporated and, in the case of a limited company, that the company is limited.

(2) From the date of incorporation mentioned in the certificate of incorporation, such of the subscribers of the memorandum and other persons, as may from time to time be members of the company, shall be a body corporate by the name contained in the memorandum, capable forthwith of exercising all the functions of an incorporated company, and having perpetual succession and a common seal, but with such liability on the part of the members to contribute to the assets of the company in the event of its being wound up as is mentioned in this Act.

NOTES

Eng. Act, 1948 : Sec. 13.
Eng. Act, 1985 : Sec. 13.

Previous Act : Sec. 23.

Effect of incorporation : Company as separate legal person

One of the characteristics of a company is that it is an incorporated body of persons. It is constituted into a distinct and independent person in law and is endowed with special rights and privileges. It is not like a partnership firm or a family—the mere aggregate of

its members. It is in point of law a person distinct from its members. If the members of an incorporated company are collected in a room together, we do not see the company, but the members; for it must be remembered that the company is intangible; it exists only in contemplation of law; it has no physical body. As LORD CHANCELLOR SELBORNE said in one case; "It is a mere abstraction of law."

A company is a separate legal entity notwithstanding the fact that there was only one governing director who also held a majority of the shares of the company. The separate legal entity enabled a director, representing the company, to enter into a contract of employment with himself in his individual capacity. *Lee v. Lee's Air Farming Ltd.,* (1961) 31 Com Cases 233, 246, 248, 249 : (1960) 3 All ER 420 (PC). See another example of controlled company in *Rainham Chemical Works Ltd. v. Balvedere Fish Guano Co.,* (1921) 2 AC 465.

Two companies which are incorporated with the same set of shareholders are nevertheless distinct and separate entities. *Pattinson v. Bindhya Debi,* AIR 1933 Pat 196.

This characteristic has far-reaching consequences, and offers to a company and its shareholders many special advantages and privileges; in particular it enables the company to contract with its shareholders and others to use a common seal, and to acquire and hold property in its corporate name.

The possession of a common seal with its name engraved on it in legible characters [section 147(1)] is a statutory requirement of an incorporated body, having a legal personality of its own.

A company may own property and even carry on business in names other than its own. *Lachminarain Kanoria & Co. v. Victory Jute Mills,* (1966) 36 Com Cases 53 (Cal). A property can be acquired under the Land Acquisition Act, 1894 for the purposes of a company. A company's purpose is capable of being equated with a public purpose. *Shyam Nandan Prasad v. State Bank of Bihar,* (1993) 4 SCC 255. It is, however, necessary that the purposes of the company should be capable of serving general public and not merely the interest of private persons. *Srinivasa Cooperative House Building Society v. Madam Gurumurthy Shashtri,* (1994) 4 SCC 675. A company may also act, as several banking companies are actually doing, as trustee, executor or administrator, provided its constitution, *i.e.*, its memorandum of association permits or authorises the doing of such business. In *Akhil Deshastha etc. Mandal v. Joint Charity Commissioner* (1973) 43 Com Cases 361 : AIR 1972 Bom 313, the mandal had for its objects religious and charitable purposes and was incorporated as a company limited by guarantee and therefore, it was a juristic person and capable, as such, of owning property and functioning as a trustee.

A company does not loose its separate entity as a legal person whatever be the manner in which it is financed. The workers of a company in the private sector were not permitted to go in for writ petition against the company by trying to identify it with the instrumentality of the State by reason only of the fact that a large number of company's directors were nominees of public financial institutions and its financial structure was composed heavily of loans from such institutions. *Madras Labour Union v. Binny Ltd.,* (1996) 87 Com Cases 438 (Mad) **following** *Guest Keen Williams Ltd. v. Guest Keen Williams Junior Management Staff Assn.,* (1990) II LLJ 522 (Cal).

Further study.—For a study in economic terms, see DR. IGE OMOTAYO BOLODEOKU, ECONOMIC THEORIES OF THE CORPORATION AND CORPORATE GOVERNANCE : A CRITIQUE, 2002 JBL 411; OLIVER HART, AN ECONOMIC PROSPECTIVE OF THE THEORY OF THE FIRM, (1989) 89 Colum L Rev. 1757.

Perpetual Succession

Section 34 lays stress upon the fact that the body corporate which emerges from registration shall have perpetual succession. The element of perpetual succession prevents the dislocation of the company by the death, bankruptcy, or lunacy of any of its members. If a partner of a partnership firm dies or becomes bankrupt, the firm is dissolved, and if the

surviving or continuing partners go on with the business they in law, constitute a new firm. But in the case of a company, the death or bankruptcy of a member has no such effect, for the company is a distinct person, and it continues to exist as the same person until it is not only wound up, but also dissolved in the manner specified in the Act. Hence, if a company has today ten members and tomorrow they all transfer their shares to ten other members, the company remains the same person. Changes among the shareholders no more affect the company than changes of the company's servants.

The advantage of incorporation is that the company never dies. It has perpetual succession and remains in existence however often its members change, until it is dissolved by liquidation. (PALMER'S COMPANY GUIDE, 36th Edn., pages 2-3). The company has an identity and existence independent of the estate and undertakings owned by it, so that even if the estate is taken over by the Government, that does not constitute a taking over of the management of the company. *Gopalpur Tea Co. Ltd. v. Peshok Tea Co. Ltd.*, (1982) 52 Com Cases 239, 241 (Cal).

In GOWERS' COMPANY LAW [6th Edn., 1997 p. 86] there is the following forceful illustration of the concept of perpetual succession: "During the 1939-1945 War all the members of one private company, while in general meeting, were killed by a bomb. But the company survived; not even a hydrogen bomb could have destroyed it." This observation has found a real illustration in the Australian case of *Re Noel Tedman Holdings Pty Ltd.* [1967] QdR 561—A man and his wife were the sole shareholders and directors of two companies. They were both lost in a road traffic accident. Their deaths did not cause the termination of their companies' legal existence. The companies continued as owners of property and parties to uncompleted contracts. The personal representatives of the deceased shareholders were allowed by the court to appoint new directors of the companies so as to realise their property for the benefit of the deceaseds' estates.

Legal personality

Company a 'person' for purposes of Consumer Protection Act.—The definition of "person" in S. 2(1)(m) of the Consumer Protection Act (CPA) would include a company by reading it with S. 3(42) of the General Clauses Act. The legislative intent on the point is evident from S. 25 and S. 27 of the CPA. The penalty provision in S. 27 of the CPA as applicable to a company has to be taken applicable to those who are officially responsible for the conduct of the company's affairs. *Ravi Kant v. NCDR Commission,* (1997) 25 Corpt LA 347 (Del).

Company a 'person' under Money Lenders Act.—Companies registered under the Companies Act, 1956, would come within the definition of "money lender" under section 2(7) of the Kerala Money-lenders Act and would, therefore, be bound by all the other provisions of the Act applicable to a money lender including the liability to take a licence. The court found that certain institutions which were covered by the definition of "person" within the meaning of that word under the General Clauses Act, 1897 were excluded under the Act, but companies were not excluded. *Link Hire Purchase and Leasing Co. Ltd. v. State of Kerala,* (2001) 103 Com Cases 941 at 945 (Ker).

Complaint by company for dishonour of cheque.—Where a company was the recipient of a cheque which was dishonoured, it was held that the company was competent to make a complaint under S. 138 of the Negotiable Instruments Act. The money represented by the cheque was the company's money and not that of its functionaries and therefore the company alone could file a complaint, *Nandgopal v. NEPC Agro Foods Ltd.*, (1995) 83 Com Cases 213 (Mad). In another similar case the complaint was filed by the manager of the company who was duly authorised for the purpose and therefore the complaint was competent. *Solar Solvent Extractions Ltd. v. South India Viscose Ltd.*, (1995) 83 Com Cases 540 (Mad). The principle was also **applied** in *Sagayadurai v. J.D. Electronics,* (1999) 95 Com Cases 337 (Mad). The court noted that the definition of 'company' in *Explanation* (a) to s. 141 of the Negotiable Instruments Act, 1881 shows that any body corporate including a firm has to be represented by some human agency in

prefering a complaint before the court. The dictates of common sense, practical wisdom, prudence and experience impel the court in such a situation to allow the company to present a complaint before the court represented by some person connected with the affairs of the company. The person connected with the affairs of the company or the firm, in the normal run of things, may be either its manager, partner, managing partner or director or any other person authorised by the company. In this case there was no dispute that the complainant was a manager of the firm. [see at p. 338] The court noted that the same view has been expressed in *Gopalakrishna Trading Co. v. D. Bhaskaran,* (1994) 80 Com Cases 53. A complaint by zonal manager was held to be maintainable. *K.K.C. Textile Mills v. Maize Products,* (1998) 93 Com Cases 919 (Mad).

A complaint filed by the Deputy General Manager who was so authorised by the Chief General Manager was held to be *prima facie* competent. The Court said that whether the authorisation was valid or not would be determined at the trial. *Pappillon Exports Ltd. v. MMTC Ltd.,* (2001) 105 Com Cases 882 (Mad). A complaint filed by a company under s. 138 of the Negotiable Instruments Act, 1881 through a senior manager who was authorised for the purpose was held to be maintainable. It is not a case of a joint petition by the manager and the company. *Medchell Chemicals and Pharmaceuticals P. Ltd. v. Dr. DC Malik,* (1998) 94 Com Cases 259 (Mad). A complaint by the administrative manager of the company was held to be competent. *Geekay Exim. (India) v. State of Gujarat,* (1998) 94 Com Cases 516 (Guj) [sections 141 and 142 of the NI Act, 1881]. The court **followed** *Sagaydurai v. JD Electronics, (Supra).* See also *Bank of India v. Rajesh Sareen,* (1998) 2 Comp LJ 64 (Delhi), proceedings on behalf of a bank by the holder of power of attorney. See also *Raj Cylinders & Containers v. Hindustan General Insurance Ltd.,* AIR 1998 Del 418 : (1999) 33 CLA 327 : (2001) 103 Com Cases 161 : (2001) 29 SCL 344 (Delhi), [authorisation of managing director]. *Shoes East Ltd. v. Modella Knitwear Ltd.,* (2001) 103 Com Cases 816 (P&H). (Director authorised to file complaint).

§ See also Notes under section 5, *ante.*

Company's right to sue for defamation and other wrongs.—Incorporation brings into existence a legal person which develops into its own separate existence as a business or enterprise entities. The publication of any statement which disparages its business, defames the company at the same time. Hence the company is entitled to sue in damages for libel or slander as the case may be. *Metropolitan Saloon Omnibus Co. Ltd. v. Hawkins,* (1859) 28 LJ Ch 830; *South Hetton Coal Co. Ltd. v. North-Eastern News Assn. Ltd.,* (1894) 1 QB 133 (CA). A company, as a person separate from its members, may even sue one of its own members for libel (*Metropolitan Saloon*). In the case of a company or a trading corporation, words calculated to reflect upon it in the way of its property or trade or business, and to injure it therein, are actionable without proof of special damage; but if they refer only to the personal character or reputation of its officers, then proof of special damage is necessary. *Union Benefit Guarantee Company v. Thakorlal Thakor,* (1935) 37 Bom LR 1033; *D&L Caterers Ltd. v. D'Ajou,* (1945) KB 364. [cf. RATANLAL & DHIRAJLAL-LAW OF TORTS, 264 (24th Edn., 2002).

A company has a right to seek damages where a defamatory material published about it affects its business. Preparation of video cassettes by the workmen of a company showing their struggle against the company's management was held to be not actionable unless it was shown that the cassette would be defamatory. The court did not restrain the exhibition of the cassette. *TVS Employees Federation v. TVS And Sons Ltd.,* (1996) 87 Com Cases 37 : (1997) 27 Corpt LA 1 (Mad—DB).

A corporation cannot obviously bring a suit for torts which are only wrongs against living persons, *e.g.* assault and false imprisonment. It cannot also sue for a tort committed essentially against its shareholders or employees unless the tort has also some impact on the governance or business or property of the corporation. *Bognor Regis. UDC v. Campion,* (1972) 2 QB 169. This is for the reason that a corporation's personality is different and distinct from the individuals constituting it and the employees acting for it. Subject to these general reservations, a corporation can sue for torts committed against it. A corporation can thus sue for malicious presentation of a winding-up petition *Quartz Hill Gold Mining Co. v. Eyre,* (1883) II QBD 674 or a libel charging it with insolvency or with dis-

honest or incompetent management. *Metropolitan Saloon Onmibus Co. v. Hawkins,* (1889) 4 Hd No. 87. It was once held that a corporation cannot maintain an action for libel charging it with corruption for it is only individuals and not the corporation who can be guilty of such an offence. *Mayor etc. of Manchester v. Williams,* (1891) 1 QB 94. Recent authorities show that this view is erroneous and that a trading corporation is entitled to sue in respect of defamatory matters which can be seen as having a tendency to damage it in the way of its business. *Derbyshire County Council v. Times News Paper Ltd.,* (1993) 1 All ER 1011 (HL) p. 1017. See further *National Union of General and Municipal Workers v. Gillan,* (1946) KB 81; *Willis v. Brooks,* (1947) 1 All ER 191.

A limited liability company, no less than an individual, can maintain an action for slander without proof of special damage, where the words are calculated to injure its reputation in relation to its trade or business. *D. & L. Caterers Ld. v. D'Ajou,* (1945) 1 KB 364. It can be defamatory to allege that directors allowed the company to continue trading at a time when it ought to have been facing insolvency. *Aspro Travel Ltd. v. Owners Abroad plc.,* (1996) 1 WLR 132 (CA).

The Supreme Court has accepted the possibility of the defamation of a company having its radiating effect upon directors of the company. The directors' right to complain would arise under a combination of IPC and CrPC provisions. The court said that in view of *Explanation* 2 to section 499 of the Indian Penal Code, 1860, a publication containing defamatory imputations against a company would not escape from the purview of the offence of defamation. If a company is described as engaging itself in nefarious activities, its impact would certainly fall on every director of the company and hence he can legitimately feel the pinch of it. Where derogatory remarks about a hospital run by a private limited company were published in a daily newspaper and a director of the company filed a complaint against the editor of the paper, alleging defamation, it was held that the director of the hospital would fall within the purview of "person aggrieved" as envisaged in section 199(1) of the Code and the prosecution was maintainable. *John Thomas v. Dr. K. Jagdeesan,* (2001) 106 Com Cases 619 : (2001) 4 Comp LJ 28 (SC), **upholding** the decision of the Madras High Court. [Crl. R.P. No. 241 of 1995 dated 3-4-2001 **unreported**].

Right to Privacy.—A company, or any body corporate, does not enjoy a right or privacy either under the [English] Broadcasting Act 1996 or the European Convention on Human Rights. *R. v. British Standards Commission ex p. British Broadcasting Corporation,* The Times September 14, 1999. (UK). This decision was **reversed** by the Court of Appeal in *R. v. Broadcasting Standards Commission, ex p British Broadcasting Corpn.,* (2001) 1 BCLC 244 (CA). The Court of Appeal held that a company can complain about unwarranted infringement of its privacy under the Broadcasting Act, 1996. The company does have activities of a private nature which need protection from unwarranted intrusion. If the company were not protected under the Act from such activities, it would leave a company at a disadvantage under a legislation which is designed to encourage and achieve proper standards of conduct. It was most unlikely that that was what Parliament intended. The complaint was about the secret filming of transactions in Dixons' shops by the BBC and that this was an infringement of the company's privacy.

In industrial tribunal proceedings the tribunal enjoys discretion, wherever considered appropriate, to protect the identity of a company which was a defendant to a compalint. Orders restricting publicity are not confined to protection of natural persons. It may be appropriate to make such an order in the case the company's name if revealed would serve to identify the individual respondent—*M v. Vincent* [1998] ICR 73. [PALMER IN COMPANY 1998 June]

Capacity for suits.—Companies incorporated under the Act are capable of suing and been sued in their corporate names. This feature considerably facilitates legal proceedings by and against company. *Satyavart Sidhantalankar v. Arya Samaj,* (1947) 17 Com Cases 21 (Bom). The company's corporate identity is not affected by any change in shareholding or membership. A suit filed by a company is not to be dismissed only because the

ownership of the company has changed and it has resulted in change of name. The court also said that a change in the membership of a company is no ground for dismissal of a suit pending against it. The change in this case was due to takeover of the company by a French group. *Memtec Ltd. v. Lunarmech,* (2001) 103 Com Cases 1078 at 1079 : (2001) 30 SCL 55 : (2002) 46 CLA 20 (Del).

A company's right to sue arises when some loss is caused to its own personality. A company was held not entitled to sue its advisers who advised a pension scheme suitable for directors and the scheme turned out to be less beneficial than other available schemes. The company could not establish any loss on its part. Any loss would be felt by the beneficiaries of the scheme and not by the employing company. The company was under no obligation to make up any shortfall. *P. Boyes Contracts Ltd. v. Mardun Investment Co.,* 1994 SLT 1298 (Scot).

A company was not allowed to claim compensation for stress and inconvenience caused to its business where that stress and inconvenience had been suffered by the directors and employees personally. *Firsteel Cold Rolled Products v. Anaco Precision Pressings,* The Times, November 21, 1994 (UK).

Company cannot be guardian.—Company orders made against guardians of children under section 55(1) of the (English) Children and Young Persons Act 1933 in the case of criminal damage caused by such children are not available against limited companies having responsibility for children because a company cannot be a "guardian". *Marlowe Child and Family Services Ltd. v. D.P.P.,* (1998, Court of Appeal **unreported** but noted in [1998] 8 CL 212).

***Forma pauperis* suit by company.**—In *Union Bank of India v. Khaders International Construction Ltd.,* (1995) 83 Com Cases 530 (Ker) it was held that the word "person" occurring in Order 33, rule 1 of the Civil Procedure Code is not limited to a natural person and includes a juristic person as well. The court, therefore, recognised that it was open to a company to sue in *forma pauperis* **affirmed** by the Supreme Court in *Union of India v. Khader International Construction,* (2001) 105 Com Cases 856 : (2001) 3 Comp LJ 137 (SC). The official liquidators of an insolvent company which is being wound up have the right to institute a suit in *forma pauperis* on behalf of the company. *Gendalal Cotton Mills v. Basant Kumaribai,* AIR 1961 Bom 1 : (1960) 30 Com Cases 555; *Perumal Goundan v. Thirumalarayapuram Jananukoola Dhanasekhara Sangha Nidhi,* AIR 1918 Mad 362. Section 35 of the Court Fees Act, 1870 exempts a person from payment of court fee if his income is below the specified amount. It has been held that this exemption would be available to companies also. *Mamata Papers P. Ltd. v. State of Orissa,* (2000) 99 Com Cases 294 (Ori).

Legal Aid when corporate body concerned in action in representative capacity.—Under the Legal Aid Act, 1988 (English) a corporate body was entitled to apply for aid if it acted in representative fiduciary or official capacity on behalf of an individual. The court found on facts that the company was not prosecuting the claims for damages on behalf of a client but on its own behalf and in its own capacity and was, therefore, not entitled to any aid under the Act. *R.V. Chester and North Wales Legal Aid Area Office,* (1998) 2 BCLC 436 (CA). The Indian version of the English Act, 1988 is the Legal Services Authorities Act, 1987.

Criminal complaint by company.—A criminal complaint can be filed by a company but it must be represented by a natural person. It is not necessary that the same person should act as a representative throughout. The complaint by a company is liable to be dismissed because of the absence of the representative in the same way in which an individual complaint is liable to be dismissed for absence of the complainant. *Associated Cement Co. Ltd. v. Keshvanand,* (1998) 91 Com Cases 361 : (2000) 6 Comp LJ 190 (SC).

It has been held that the authority to file a criminal complaint on behalf of a payee company should be conferred on some person by the Board of directors or under Articles of Association or Rules governing the management of the company. The complaint was filed in this case by the manager. There was no material to show that the manager was authorised

for the purpose. The complaint was held to be not maintainable. *Nayagam Lourd Prakash v. Standard Chartered Bank,* (2003) 115 Com Cases 161 (AP).

A complaint was filed by the power of attorney holder authorised by a director. The holder of power of attorney was examined and evidence was closed. Subsequent to this, the company's application to examine the director who authorised the power of attorney was not allowed. The director was not listed as a witness. He could not be examined. The defect could not be cured at the belated stage. [S. 138, NI Act, S. 311, CrPC] *Danday Knit Garments v. Subiksha Spinners P. Ltd.,* (2003) 115 Com Cases 307 (Mad).

A complaint can be filed by a person whose actions would bind the company. Where a cooperative bank was the payee of the cheque and a complaint was filed by the manager on authorisation of the managing director, the court refused to quash the complaint. *N.K. Ramaswamy Iyengar v. Bangalore District and Bangalore Rural District Cooperative Central Bank Ltd.,* (2003) 115 Com Cases 667 (Kant). Where a complaint was filed in respect of a dishonoured cheque by the assistant manager (credit control) who was authorised by the chief executive of the company, the complaint was held to be valid. The authorisation had the effect of implied ratification. *The Waterbase Ltd. v. K. Ravindra,* (2003) 115 Com Cases 752 (AP).

A complaint filed by the manager of the company was not allowed to be quashed for absence of authorisation because manager or managing director are ordinarily incharge of the company's affairs. The court said that instead of quashing the complaint the company should be allowed to show that the complaint was filed by a competent person. *Credential Finance Ltd. v. State of Maharashtra,* (2001) 105 Com Cases 864 (Bom). A complaint was filed by a company for dishonour of a cheque. The filing was done by a principal officer who was not authorised by a resolution of the Board of directors. Even so the complaint was held to be maintainable. *Standard Chartered Bank v. Ravi Bhandari,* (2002) 111 Com Cases 544 (Delhi).

Dismissal of company's complaint on default in appearance.—A Government company's complaint was dismissed and the person sought to be accused was acquitted for non-appearance of the complainant. Acquittal could not be disturbed under s. 482 of the Criminal Procedure Code, 1974. The complaint was under s. 138 of the Negotiable Instruments Act, 1881. *H.P. Agro Industries Corpn. Ltd. v. MPS Chawla,* (1998) 92 Com Cases 686.

Substitution of representative in complaint by company.—A complaint was filed by the company under s. 138 of the Negotiable Instruments Act, 1881. The officer who was representing the company resigned from his position in the company. The company sought substitution of another officer and filed the power of attorney in favour of the new officer. The court ordered that the substitution be permitted. *Rasi Cements Ltd. v. Prithviraj,* (1998) 92 Com Cases 560 (Mad). The court **followed** the decision of the Supreme Court in *K.M. Mathew v. State of Kerala,* AIR 1992 SC 2206 : (1992) LW (Cri) 14; *Benhur T. and I Pvt. Ltd. v. State of Kerala,* (1998) 1 RCR (Cr) 611 (Ker).

In *Associated Cement Company Ltd. v. Keshvanand,* AIR 1998 SC 596 THOMAS J observed [at P. 600]. "No Magistrate shall insist that the particular person, whose statement was taken on oath at the first instance, alone can continue to represent the company till the end of the proceedings. There may be occasions when a different person can represent the company e.g. the particular person who represents the company at the first instance may either retire from the company's services or may otherwise cease to associate therewith or he would be transferred to a distant place. In such cases it would be practically difficult for the company to continue to make the same person represent the company in the court. In any such eventuality it is open to the *de jure* complainant company to seek permission of the court for sending any other person to represent the company in the court."

Company and its undertaking.—A company and its undertaking are two different things so that when a company's undertaking is taken over and not the company itself, the company remains alive as a separate legal entity capable for all its functions as well as liable to be sued for claims against it, excepting those which are taken over. *Mookerjee (B.) v. State Bank of India,* (1993) 76 Com Cases 292 : AIR 1992 Cal 250 (Cal). The

Court **followed** *Radha Ram Badri Nath v. Amritsar Sugar Mills Ltd.*, (1977) 47 Com Cases 625 (P&H—FB).

Company as a citizen and right to claim fundamental rights

A company is a legal person, but it is not a 'citizen' so as to claim the fundamental rights granted to citizens by the Constitution. See *State Trading Corporation of India Ltd. v. CTO*, (1963) 33 Com Cases 1057 : AIR 1963 SC 1811, **followed** in *Tata Engineering & Locomotive Co. Ltd. v. State of Bihar*, AIR 1965 SC 40 : (1964) 34 Com Cases 458; *Narasaraopeta Electric Corpn. Ltd. v. State of Madras*, (1951) 21 Com Cases 297 (Mad). This is the effect of S. 2(f) of the Citizenship Act of 1955 which expressly excludes a company or association or body of individuals from citizenship. The effect in reference to the Constitution of India is that while companies can claim the benefit of all the fundamental rights which are guaranteed to citizens only. In order, however, to relieve any apprehension on the part of companies HIDAYATULLAH J (afterwards CJ) observed in the *State Trading Corporation* case: "There is no cause for anxiety about corporations in general and companies in which States hold all or the majority of the shares in particular. They are amply protected under our Constitution. There can be no discrimination, no taxation without authority of law, no curbs involving freedom of trade, commerce or intercourse, and no compulsory acquisition of property. There is sufficient guarantee there and if more is needed then any member (if citizen) is free to invoke Article 19(1)(*f*) and (*g*) and there is no doubt that the corporation in most cases will share the benefit. We need not be apprehensive that corporations are at the mercy of State Governments. Taking lead from this statement the Supreme Court in subsequent decisions reduced the hardship which is likely to be caused by the denial of citizenship by holding that a citizen shareholder may on his own behalf and also on behalf of the company claim the benefit of Article 19 if as a result of some action of the State his rights which he was enjoying through the company were also affected. Accordingly in *Bennet Coleman & Co. v. Union of India*, AIR 1973 SC 106 it was observed: 'It is now clear that the fundamental rights of citizens are not lost when they associate to form a company. When their fundamental rights as shareholders are impaired by State action their rights as shareholders are protected. The reason is that the shareholder's rights are equally and necessarily affected if the rights of the company are affected.

In *T.D. Kumar & Bros. (P.) Ltd. v. Iron & Steel Controller*, (1961) 31 Com Cases 714 (Cal) it was held that a company which had been ordinarily resident in India for 5 years preceding the commencement of the Constitution of India, *viz.*, January 26, 1950, was to be regarded as a citizen and continued to be a citizen and was therefore entitled to the fundamental right to carry on business guaranteed under article 19(I)(g) of the Constitution. The Court **applied** the decision in *Chiranjilal Chaudhari v. Union of India*, (1951) 21 Com Cases 33 : AIR 1951 SC 41.

No writ in the nature of mandamus can be issued against a company inasmuch as it is not an authority and is beyond the scope of Article 226. *Praga Tools Corporation v. C.V. Imanual*, AIR 1969 SC 1306 : (1969) 39 Com Cases 889.

The effect of these decisions and also that of the decision in *Godhra Electricity Co. Ltd. v. State of Gujarat*, AIR 1975 SC 32 is that the company acquires a standing by impleading a shareholder with itself in the petition. It was by virtue of these decisions that in all the matters arising out of nationalisation of banks, the individual shareholders of banks were allowed to claim the protection of Article 19 of the Constitution. See, *e.g.*, *R.C. Cooper v. Union of India*, AIR 1970 SC 564; *Delhi Cloth and General Mills Ltd. v. Union of India*, AIR 1983 SC 937 : (1983) 54 Com Cases 674. It is submitted that on a consideration of these cases, the following principles emerge:

(i) A company is not a 'citizen' and, therefore, cannot maintain a writ petition for enforcement of fundamental freedoms under Article 19 which are conferred on 'citizens' alone;

(ii) if fundamental or other constitutional right is conferred on a 'person', a writ can be filed by a company because it is a 'person'.

(iii) a writ petition filed by a shareholder will be maintainable for enforcement of the fundamental freedoms only if he can establish that by the action of the Government, his company's rights as well as his personal rights have been impaired.

(iv) the rights of a company and the rights of its shareholders are not co-extensive.

(v) generally writ is filed by a company along with a shareholder, who is an Indian citizen, so that the petition is maintainable.

Statutory existence and residence of company

A company incorporated under the Companies Act is not created by the Companies Act, but comes into existence in accordance with the provisions of the Act. It is not a statutory body because it is not created by statute. It is a body created in accordance with the provisions of the statute. *Sukhdev Singh v. Bhagat Ram,* (1975) 45 Com Cases 285, 297 : AIR 1975 SC 1331.

As regards exercise of powers, a company being the creature of a statute, can have no powers other than those which are expressly conferred upon it by the Act and/or its memorandum of association and those incidental to the objects defined or enumerated in the memorandum. See the leading cases of *Ashbury Ry. Carriage & Iron Co. v. Riche,* (1875) LR 7 HL 653; *Cotman v. Brougham,* 1918 AC 514. The conceptual nature of the company carries natural limitations, for example, it cannot marry or drive a lorry. *Richmond London Borough Council v. Pinn & Wheeler Ltd.,* 1989 RTR 354.

As regards residence, domicile and nationality of a company the place of registration will normally be considered to determine them. But where the persons in *de facto* control of the company are all foreigners, there is no reason why it should not be regarded as a foreign company though registered in India. *Cf. Daimler Co., Ltd. v. Continental Tyre and Rubber Co., (Great Britain) Ltd.,* (1916) 2 AC 307 (HL). The position under the tax laws may be different as explained by LORD LOREBURN LC in *De Beers Consolidated Mines Ltd. v. Howe,* (1906) AC 455 (HL) : "In applying the conception of residence to a company, we ought, I think, to proceed as nearly as we can upon the analogy of an individual. A company cannot eat or sleep, 'Neither can it be a television entertainer or author'; *per* VISCOUNT DILHORNE in *Newstead v. Frost,* (1980) 1 All ER 363 at 368 HL; but it can keep house and do business. We ought, therefore, to see where it really keeps house and does business. An individual may be of foreign nationality, and yet reside in the United Kingdom. So may a company. Otherwise it might have its chief seat of management and its centre of trading in England under the protection of English law, and yet escape the appropriate taxation by the simple expedient of being registered abroad and distributing its dividends abroad.

The decision of KELLY CB AND HUDDLESTON B in the *Calcutta Jute Mills v. Nicholson,* (1876) 1 Ex D 428; and the *Cesena Sulphur Co. v. Nicholson,* (1874-80) All ER Rep 1102 *ibid*; involved the principle that a company reside for puposes of income-tax where its real business is carried on. These decisions have been acted upon ever since. I regard that as the true rule, and the real business is carried on where the central management and control actually abides. "In relation to an artificial construct such as a corporation, the notion of 'residence' is applicable only by way of analogy, not even a close analogy in some respects. Thus, for example, whilst there is little difficulty in seeing an individual as having two or more residences (if only, say, as between town and country), the position as to companies may be different." Citing *Unit Construction Co. Ltd. v. Bullock (Inspector of Taxes),* (1959) 3 All ER 831 at 837-838 : (1960) AC 351 at 368; *Kwok Chi Leung Karl v. Comr. of Estate Duty,* (1988) 1 WLR 1035. "A corporation resides in a country if it carries on business there at a fixed place of business, and, in the case of an agency, the principal test to be applied in determining whether the corporation is carrying on at the agency is to ascertain whether the agent has authority to enter into contracts on behalf of the corporation without submitting them to the corporation for approval." *Jabbour v. Custodian of Absentee's Property of State of Israel,* (1954) 1 All ER 145 at 152 : (1954) 1 WLR 139 at 146.

For other examples of residence for taxation purposes, see *Dickie & Co. v. Municipal Board,* AIR 1956 Cal 216; *Davies v. British Geon Ltd.,* (1957) 27 Com Cases 448, 450, 462; *Calcutta Stock Exchange Association Ltd., Re,* (1935) 3 ITR 105, 110 (Cal). LINDSAY J listed a number of factors for this purpose in *Little Olympian Each Ways Ltd. (No. 2), Re,* (1995) 1 BCLC 48 (Ch D). In determining whether a company is ordinarily resident out of the jurisdiction for the purpose of making an order for security for costs against the company, the test is the same as is applied in tax cases for assessing a company's place of residence, namely, where the central control and management of the company actually abides. Where a company's central management and control are not operated in accordance with the company's constitution, the court can examine the activity as it is. There will be a range of factors, that the court will take into consideration in assessing where a company's central control and management are located. Such factors are:

(i) the congruence between the facts of management and the requirement of the company's articles of association as to the location of its management. *Unit Construction Co. Ltd. v. Bullock,* (1959) 3 All ER 831 at 834-835 : (1960) AC 351 at 363;

(ii) the company's objects;

(iii) the place of incorporation of the company;

(iv) where the real trade and business of the company is carried on;

(v) where the company's administrative work is carried out;

(vi) where the directors, who could control the steps which were taken at local level, *Cesena Sulphur Co. Ltd. v. Nicholson,* (1876) 1 Ex D 428 : [1874-80] All ER Rep 1102 or in whom management has been confided, met, *Goerz & Co. v. Bell,* (1904) 2 KB 136; *De Beers Consolidated Mines Ltd. v. Howe,* (1906) AC 455 at 459; *Swedish Central Ry. Co. Ltd. v. Thompson,* (1925) AC 495 at 503; and

(vii) where the chief office of the company is physically located, *Jones v. Scottish Accident Ins. Co. Ltd.,* (1886) 17 QBD 421 at 422-423, physical presence of the company as 'where it keeps house', where the chief office is situate or the company secretary is to be found.

In *Unit Construction Co. Ltd. v. Bullock (Inspector of Taxes),* (1959) 3 All ER 831 an English parent company had four subsidiaries, one undeniably in U.K. and three incorporated and registered in Kenya. The English subsidiary made payments to the African subsidiaries and claimed to be entitled to deduct those payments for the purposes of United Kingdom income tax. It could do so only if the African subsidiaries were resident in the United Kingdom and carrying on a trade wholly or partly in the United Kingdom. The House of Lords held, applying the *De Beers* 'central management and control' test, that the African subsidiaries were resident here. The parent company's board had formally resolved that the local management in Africa had been so bad that the management of the African subsidiaries must be taken over by the directors of the parent company in London. The peculiar feature in the present case was that the boards of the African subsidiaries did not function at all at the material times even as a rubber stamp. LORD RADCLIFFE said that they never purported to function as a board of management. When a board fails to act at all, not even as a rubber stamp, one can see that it may be right to look through its by then wholly theoretical power of veto.

It remains to be considered whether the present case falls within that rule. This is a pure question of fact to be determined, not according to the construction of this or that regulation or by-law, but upon a scrutiny of the course of business and trading." Other cases show that the 'central management and control' of a company may in fact be divided, so that its residence is in more than one country: see, *e.g. Union Corpn. Ltd. v. IRC,* (1952) 1 All ER 646 (CA); **affirmed** on other grounds (1953) 1 All ER 729 (HL).

See further, P.ST.J. SMART, 'Corporate domicile and multiple incorporation in English private international law' [1990] JBL 126.

Service of court summons.—The residence of the company for communications purposes is the place of its registered office. Accordingly, where the premises of the registered office had remained closed during the time summons were supposed to have been served, there was no presumption that there had been a valid service. *Harendra Nath Ghosal v. Superfoam P. Ltd.,* (1992) 74 Com Cases 740 (Cal).

Enemy character.—A company though registered in this country will nevertheless be regarded as having enemy character if the persons in control of its affairs are residents in the enemy country or wherever they may be resident, are acting in accordance with the directions or wishes of the enemy. *Kuenigl v. Donnersmarck,* (1955) 1 All ER 46 : (1956) 26 Com Cases 1 (QB); *Daimler Co. Ltd. v. Continental Tyre and Rubber Co. Ltd., (Supra).*

Company cannot be a witness.—A company cannot take any oath or make affirmation and therefore cannot become a witness. Art. 20(3) of the Constitution mandating that 'no person accused of any offence shall be compelled to be a witness against himself' does not apply to companies. *Godrej Soap Ltd. v. State,* (1991) 70 Com Cases 248, 251 (Cal).

Company's privilege against self incrimination.—A company is entitled as much as an individual to the protection against self incrimination enshrined in Art. 20(3) of the Constitution. Accordingly, a company was not ordered to produce certain documents which would have incriminated it to a charge of tax evasion (Octroi Duty) and just as the company could not be compelled to produce them, its employee who was having the custody of those documents, could not be compelled without the consent of the company. However, such documents can be searched and seized in the exercise of power under the Code of Criminal Procedure. *State of Maharashtra v. Nagpur Electric Light and Power Co. Ltd.,* (1961) 31 Com Cases 324 (Bom—DB).

A limited company could be a commercial agent and, therefore, enjoy the benefit of the rights conferred by the Commercial Agents Regulations 1993—*AMB Imballagii Plastici SRL v. Pacflex Ltd.,* (1998) 17 Trading Law Reports 557. The Court of Session (Outer House) gave guidance on the proper principles of interpretation to be used when construing legislation (such as the Commercial Agents Regulations 1993) implementing E.C. Directives—*Roy v. MR Pearlman Ltd., The Times* May 13, 1999.

Liability in Tort and Crime

"A company can be guilty of acting with intent to deceive and making a statement which it knows to be false or be indicted for conspiracy to defraud. It can also be guilty of and be fixed for contempt of Court. Notwithstanding its impersonal nature it may sue for an injury done to its reputation in the way of its business by a libel, or a slander or by an imputation of insolvency, and may be sued for malicious prosecution, maintenance, infringement of copyright, molesting a person in the exercise of his calling or negligence, and may be guilty of malicious libel." BUCKLEY'S COMPANIES ACTS (14th Edn., pages 55, 56). As regards the personal liability of a company in tort, see *Bolton (HL) Engineering Company Ltd. v. T.J. Graham & Sons Ltd.,* (1956) 3 All ER 624 (HL).

A company cannot personally commit any tort or crime. It cannot even authorise any tort or crime because its authority always remains circumscribed by the objects clause of its memorandum and that clause cannot contain anything unlawful. Questions have, therefore, often arisen as to the extent to which a company can be held liable for any tort or crime committed by those who are working for it.

In criminal law though there has been a necessary pre-occupation with a fundamental dividing line which recognises that certain acts, which only a natural person can perform, lie beyond a company's vicarious liability. Where, for example, a statutory order stated that "... no person shall drive or cause or permit to be driven" a prescribed vehicle, the

Divisional Court quashed a company's conviction on the basis that the act of driving the goods vehicle in question is a physical act which can be performed only by natural persons and not a company. *Richmond London Borough Council v. Pinn and Wheeler Ltd.*, (1989) RTR 354 : 1989 Crim. LR 510 : (1989) 133 Sol Jo 399. The statutory offence of "permitting" cannot be committed vicariously by a company although direct liability may well accrue on the basis that the act and *mens rea* of a directing mind and will of the company can be identified as that of the company. *Manga Plant Ltd. v. Mitchell,* (1966) Crim LR 394. Accordingly, caution is required in choosing an appropriate offence with which a company may be charged where vicarious liability appears to be the foundation of the case. *London Borough of Southwark v. Allied Domecq Leisure Ltd.*, [1999] E.H.LR. 231.

A club registered as a company was not convicted for serving liquour without licence to members because the members had organised that service by forming a members' club and, therefore, they were consuming their own property. *Trebanog Working Men's Club Ltd. v. MacDonald,* (1940) 1 KB 576 : (1940) 1 All ER 454 (KB).

Liability in Torts.—In the field of tort the governing principle is that a master will be liable for the torts of his servants if they occur in the course of the servant's employment and in the case of agents, if they are within the scope of the agent's authority. In this respect the courts cannot permit the defence of *ultra vires*. If that defence were to prevail "no company could ever be sued if the directors of the company after resolution did an act which the company by its memorandum of association had no power to do. That would be absurd. *Campbell v. Paddington Corpn.*, (1911) 1 KB 869. The court accordingly held the corporation liable for blocking the view across a premises of an important event. The defence of the corporation that it had no authority to cause the obstruction was brushed aside by the court saying that: "The only way in which this corporation can act is by its council, and the resolution of the council is the authentic act of the corporation." For further case-law on vicarious liability, see *Pearks, Gunston & Tee Ltd. v. Ward,* (1902) 2 KB 1; *Moussell Bros. Ltd. v. L. & N.W. Rly.*, (1917) 2 KB 836; *Chuter v. Freeth & Pocock Ltd.*, (1911) 2 KB 832.

Where an act of this kind is done without any authority whatsoever, the company would not be liable. Thus a railway company was held not liable for false imprisonment when a station master arrested a person for not paying fare, his authority being limited only to detaining goods for non-payment. BLACKBURN J said: "In the present case an act was done by the station-master completely outside the scope of his authority, which there can be no possible ground for supposing the railway company authorised him to do." The court also emphasised the fact that the company itself had no power to detain any person on that ground. *Poulton v. London and S.W. Ry. Co.,* (1867) LR 2 QB 534. The lack of authority on the part of the company is, however, of not much consequence now. Noting this development, Gower observes: "Although at first sight it may appear absurd that the commission of a tort or crime can ever be within the authorised objects or powers of companies, they are constantly made liable for both the overwhelming weight of academic opinion favours the view that they may be liable whethr or not the offence was committed in the course of *ultra vires* activities." PRINCIPLES OF MODERN COMPANY LAW, (171, 4th edn., 1979). Similarly, it is observed in PALMER'S COMPANY LAW (207, 24th edn. 1987): "It is believed that in these circumstances the company is liable for the torts of its agents or servants, even though these torts are *ultra vires* its objects. *Obiter dicta* in American decisions and eminent writers can be quoted in support of this view. It is thought that this view is in harmony with the scanty modern indications of English judicial opinion on this issue." See also PENNINGTON'S COMPANY LAW (126, 5th edn., 1985) and *Standard Investments Ltd. v. Canadian Imperial Bank of Commerce,* 1986 LRC (Comm) 571 where the company was held liable for the conduct of its President and Chairman in committing breach of fiduciary obligations.

It has been held that despite wilful wrongdoing, malice or fraud, a company may be vicariously liable for tortious acts of employees. *Barwick v. English Joint Stock Bank,*

(1967) L.R. 2 Exch. 259. *Cf. Citizens' Life Assurance Co. v. Brown,* 1904 AC 423. Acting contrary to corporate instructions will not necessarily negate the company's vicarious liability. *Canadian Pacific Railway Co. v. Lockhart,* [1942] A.C. 591. Equally, dishonest conduct will not necessarily negate vicarious liability. *Lloyd v. Grace, Smith & Co.,* [1912] A.C. 716.

The law has to divide very carefully sets of circumstances which indicate whether vicarious liability attaches. In *Morris v. C.W. Martin & Sons Ltd.,* [1966] 1 Q.B. 716 : [1965] 3 W.L.R. 276 : [1965] 2 All ER 725, the Court of Appeal was confronted by facts which indicated dishonest appropriation of a fur coat by an employee of the company who was deputed to clean it. SALMON L.J. said : "A bailee for reward is not answerable for a theft by any of his servants but only for a theft by such of them as are deputed by him to discharge some part of his duty of taking reasonable care. A theft by any servant who is not employed to do anything in relation to the goods bailed is entirely outside the scope of his employment and cannot make the master liable. [(1966) 1 QB 716 at pp. 740-741]. This shows that the company's vicarious liability depends usually on a significant interplay between the identification of the "course and scope of employment" and on the other hand, the authority of the individual whose conduct is under scrutiny. LORD LOREBURN said, in *Glasgow Corporation v. Lorimer,* [1911] A.C. 209 (HL). "...it is [not] good law to say that the corporation is bound by anything said by one of its servants which is connected with the business of that servant. The question is whether or not there is any authority to communicate on behalf of the corporation any comment or statement of opinion at all". (1991) AC 209 at 215 (HL).

In *Moore v. Bresler Ltd.* [1944] 2 All ER 515, saw the conviction of the company in respect of fraud which arose from the activities of two employees at a branch office : one the branch general manager, the other the branch sales manager. Despite an exercise of powers which defrauded the company the court was willing to uphold the conviction on the basis of the branch managers having acted within the limits of their authority to sell goods.

The Court of Session in Scotland held that an employee accused of sexual harassment of a fellow employee was not acting within the course of his employment. He must have been motivated purely by personal non-sense : *Ward v. Scotrail Railways Ltd.,* 1999 SC 255 (Scot-Outer House).

In *Green v. London General Omnibus Co. Ltd.,* (1859) 7C BNS 290 : 141 ER 828 the court held that a company could be liable in an action concerning the intentional acts of misfeasance of its servants, provided that they were sufficiently connected with the scope and object of its incorporation. It was against this background that ERLE C.J. stressed that : "The doctrine ..... that a corporation having no soul cannot be actuated by a malicious intention, is more quaint than substantial." *Ibid* at p. 295. ERLE C.J. considered it as established by the parties : ".. an action for a wrong will lie against a corporation, where the thing complained of is a thing done within the scope of their incorporation, and is one which would constitute an actionable wrong if committed by an individual".

In *M.C. Mehta v. Union of India,* AIR 1987 SC 1086, the Supreme Court held as follows regarding the liability to pay compensation for tortious liability:

> "We would therefore hold that where an enterprise is engaged in a hazardous or inherently dangerous activity and harm results to anyone on account of an accident in the operation of such hazardous or inherently dangerous activity resulting, for example, in escape of toxic gas the enterprise is strictly and absolutely liable to compensate all those who are affected by the accident and such liability is not subject to any of the exceptions which operate *vis-a-vis* the tortious principle of strict liability under the rule in *Rylands v. Fletcher.*
>
> "We would also like to point out that the measure of compensation in the kind of cases referred to in the preceding paragraph must be correlated to the magnitude and capacity of the enterprise because such compensation must have a deterrent ef-

fect. The larger and more prosperous the enterprise, the greater must be the amount of compensation payable by it for the harm caused on account of an accident in the carrying on of the hazardous or inherently dangerous activity by the enterprise." The Court left open a question as to whether a company which is "a private corporation" engaged in an activity which has potential to affect the life and health of the people" was amenable to the writ jurisdiction." For a review petition on the same cause of action see *Union Carbide Corporation v. Union of India,* (1991) 3 Comp LJ 213 (SC). See also *Charanlal Sahu v. Union of India,* AIR 1990 SC 1480; *Union Carbide Corporation v. Union of India,* AIR 1990 SC 273.

Government undertakings like 'U.P. Financial Corporation' in this case are entitled to the benefit of Art 226 of the Constitution for protection of their interest and if a writ is presented through a director, it will be competent whether there was any resolution of the Board or not. *Uptron Anand Ltd. v. U.P. Financial Corporation,* (1987) 2 Comp LJ 215 (All) (DB).

Slander or libel.—A company is responsible for a slander or libel published by one of its officers, where the act is done in the course of employment which is authorised by the company. *Citizens' Life Assurance Co. v. Brown,* (1904) AC 423 : (1904-7) All ER Rep 925 (PC). A company can sue for damages for defamation just as private individual can provided it is defamed in the way of its business. *D & L Caterers Ltd. v. D'Ajou,* (1946) 16 Com Cases 1, 4, 7 (CA); *Bognor Regis UDC v. Campion,* (1972) 2 All ER 61. "It has been argued that while a company can sue for defamation it should not be treated in the same way as a person and in particular that a company should not be able to sue for general damage to its reputation but only for injury to its assets, including proved financial loss arising from damage to goodwill. See RICHARD KINDER, *Defaming a Company by Disparaging its Products,* 1992 JBL 570." But it cannot sue for an injury done to its members before its incorporation. *Gidney v. Anglo Indian Federation,* (1931) 1 Com Cases 186, 187 (Rang). A company can sue for libel or slander which damages its business. *Metropolitan Saloon Omnibus Co. Ltd. v. Hawkins* (1859) 4 H & N 87; *South Hetton Coal Co. Ltd. v. North-Eastern News Association Ltd.* [1894] 1 QB 133, (CA). A company as a person separate from its members, may even sue one of its own members for libel. *Metropolitan Saloon Omnibus Co. Ltd. v. Hawkins* (*Supra*). Where a company is a political party, it cannot sue for defamation, because there is no business which could be damaged and also there is an overriding public interest in freedom to criticise political institutions though individual party members, even candidates for election, who believe themselves to be defamed can sue. *Goldsmith v. Bhoyrul* [1998] QB 459. For further details, see RATANLAL DHIRAJLAL, LAW OF TORTS, 36, 37, 254, 255, 273 (24th Edn., 2002).

Liability for Fraud.—Where a company made a false statement on a bill of lading with the expectation that the document would be used to induce a bank to make payment under a letter of credit then that company could be held liable in the tort of deceit. *Standard Chartered Bank v. Pakistan National Shipping Corporation,* (2000) 1 Lloyds Reports 218 : (2000) 1 All ER (Comm) 1 (CA). On appeal to the House of Lords, their Lordships held that the managing director who made the fraudulant representation was also liable personally. *Standard Chartered Bank v. Pakistan National Shipping Corpn.,* (2003) 1 All ER 173 (HL) : (2003) 1 BCLC 244. For details see Notes under s. 291 under the heading "Liability for Fraud".

§ See also Notes in section 291 under the heading "Liability for fraud".

Liability in Crime.—The corporate person of the company being beyond the reach of physical punishment, its liability can be only in terms of financial indictment and for that the governing principles would have to be more or less the same as in civil matters, that is, the company would be responsible where the criminal conduct of those working for it is either within the range of their authority or in the course of their employment. *Javali (M.V.) v. Mahajan Borewell & Co.,* (1998) 91 Com Cases 708 (1997) 4 Comp LJ 129: (1997) 27 Corpt LA 52 (SC). Thus a company has been fined under Defence Regulations for making a false statement, *DPP v. Kent & Sussex Contractors Ltd.,* (1944) 1 All ER 119; for common law conspiracy to defraud, *R. v. ICR Haulage Ltd.,* (1944) 1 All ER 691

: (1945) 15 Com Cases 47 (CCA), "for intent to deceive despite the fact that the acts were not those of its directors but merely of its secretary and a branch manager", *Moore v. Bresler Ltd.*, (1944) 2 All ER 515 (KBD); the quotation is from GOWER, PRINCIPLES OF MODERN COMPANY LAW, (208, 4th edn. 1979), for giving false warranty as to an item of food, *Chuter v. Freeth & Pocock Ltd.*, (1911) 2 KB 832 : (1911-13) All ER Rep 138. Once the facts relating to the precise position of the person alleged to form the directing mind of the company have been ascertained, it is a question of law whether that person, in doing a particular act, is or is not to be regarded as the company. *Tesco Supermarkets Ltd. v. Natrass*, (1971) 2 All ER 127 at 131 HL *per* LORD REID. The main considerations are the relative position in the company which he holds and the extent to which, as a matter of fact, he is in actual control of its operations or a section of them without effective superior control. In *R. v. Andrews Weatherfoil Ltd.*, (1972) 1 All ER 65 it was held that not every 'high executive' binds the company. Where a company was prosecuted for conspiracy and the only other person was its sole director, the company was not convicted, the court said that "where the sole responsible person in the company is the defendant himself, it would not be right to say that there were two persons or two minds". *R. v. McDonnell*, (1966) 1 All ER 193 per NIELD J. It is necessary for the application of this principle that the act in question must be that of a "responsible officer", in the sense that his act can be regarded as the act of the company.

In *DPP v. Kent Sussex Contractors Ltd.*, (1944) KB 146 : (1944) 1 All ER 119, it was said : "Once the ingredients of the offences are stated in that way it is unnecessary ... to require whether it is proved that the company's officers acted on its behalf. The officers are the company for this purpose... The offences created ... are those of doing something with intent to deceive or of making a statement known to be false in a material particular. There was ample evidence ... that the company, by the only people who could act or speak or think for it had done both these things ..."

In *R. v. ICR Haulage Ltd.*, (1944) KB 551 (at 559), a company's conviction for conspiracy to defraud was upheld by the Court of Criminal Appeal. STABLE J. giving judgment stressed that the Court was not deciding ; "... that in every case where an agent of the company acting in its business commits a crime the company is automatically to be held criminally responsible .... Whether in any particular case there is evidence to go to the jury that the criminal act of an agent, including his state of mind, intention, knowledge or belief is the act of the company ... must depend on the nature of the charge, the relative position of the officer or agent, and the other relevant facts and circumstances of the case".

The House of Lords has ruled that a company cannot be physically present on premises so as to steal; corporate persons can be present on the premises only through a representative. *Deutsch Genossenschaft Bank v. Burnhope*, (1995) 4 All ER 717 : (1996) 1 Lloyd's Rep 113 (HL).

It is possible now to charge a company and to find it guilty of the crime of manslaughter provided that the incident occured in the course of the company's business and the person responsible for the incident was occupying such a position in the company that he could be described as the embodiment of the company itself. *R. v. H.M. Coroner for East Kent, ex p., Spooner*, (1987) 3 BCC 636 (DC); *R. v. P.&O. Ferries (Dover) Ltd.*, (1990) 93 Cr App Rep 72. **Following** these principles in *R. v. O.L.L. Ltd.*, (1994) Times, 9 December, a company was held criminally responsible for the death of four young persons who were sent out by the company in the ordinary course of its business on a canoeing trip without proper instructions or supervision. The *mens rea* of the managing director was attributed to the company and both were convicted. It has been suggested that conviction of a small company will be easier on the application of this principle because the relationship between the actual culprit and the company can be identified with greater certainty but that in the case of a large company, with too many managers, the responsibility for the incident becomes so diffused among the officers that it is difficult to know who was individually guilty. Hence when the question is of attributing the act or state of

mind of an individual to a company, different rules would have to be invoked in different circumstances depending upon a number of factors. *Meridian Global Funds Management Asia Ltd. v. Securities Commission,* (1995) 2 BCLC 116 (PC). It has been opined in *Attorney General's Reference (No. 2 of 1999)* (2000) 2 BCLC 257 (CA) that on a charge of manslaughter by gross negligence, a non-human defendant, such as a corporation, could not be convicted in the absence of evidence establishing the guilt of an identified human individual for the same crime. This opinion was expressed by the Court on a reference by the Attorney General on the following two questions:

"1. Can a defendant be properly convicted of manslaughter by gross negligence in the absence of evidence as to that defendant's state of mind?

"2. Can a non-human defednant be convicted of the crime of manslaughter by gross negligence in the absence of evidence establishing the guilt of an identified human individual for the same crime?"

The case arose out of a railway accident caused by driver's error who alone was prosecuted along with the company there being a finding of a serious fault of senior management in the company. The Court said that it would have been open to the jury to convict if they were satisfied that the deaths occurred by reason of a gross breach by the defendant of its personal duty to have a safe system of train operation. The identification theory, attributing to the company the mind and will of senior directors and managers, was developed in order to avoid injustice: it would bring the law into disrepute if every act and state of mind of an individual employee was attributed to a company which was entirely blameless. As a matter of general observation, the court said:

"Large companies should be as susceptible to prosecution for manslaughter as one-man companies. Where the ingredients of a common law offence were identical to those of a statutory offence, there was no justification for drawing a distinction as to liability between the two and the public interest required the more emphatic denunciation of a company involved in a conviction for manslaughter."

A company was not convicted under the Trade Descriptions Act, 1968 (English) for false advertisement caused by a shop manager, the HOUSE OF LORDS observing that a shop manager, one of the several hundred, could not be identified with the company. "The reference in s. 20 of the Trade Description Act, 1968 [English] to "any director, manager, secretary or other similar officer of the body corporate" affords a useful indication of the grades of officers who may for some purposes be identifiable with the company, although in any particular case the constitution of the company concerned should be taken into account." *Tesco Supermarkets Ltd. v. Nattrass,* (1971) 2 All ER 127 (HL). In this case LORD REID said : "... normally the board of directors, the managing director and perhaps other superior officers ... carry out the functions of management and speak and act as the company. Their subordinates do not". In *Baxters (Butchers) Ltd. v. Manley,* (1985) 4 Tr. L. 219 the issue was the adequacy of a company's operational system in the retail sector. For a variety of reasons the Divisional Court held that the company's system was inadequate. Among other reasons for its decision that there was evidence for the magistrates' court to proceed, the Divisional Court pointed to inadequate supervision by a district manager, and failure by the company to prescribe the implementation of company rules and attendant legislation that had been given to that manager. See further *John Henshall (Quarries) Ltd. v. Robert Miller (Contractors) Ltd.,* (1970) 2 QB 54, "counselling and procuring" under the Road Traffic Act, 1960 (English). A company has been fined under the Contempt of Courts Act, 1981 (English). See *Phonographic Performance Ltd. v. Amusement Caterers (Peckham) Ltd.,* (1963) 3 All ER 493 and *Re, Garage Equipment Assn.'s Agreement,* (1964) LR 4 RP 491 as cited in PALMER'S COMPANY LAW (197, 23rd edn., 1982) where it is also observed that "a company is not vicariously liable for contempt if its agent does not know that the act constitutes contempt", on the authority of *Z. Ltd. v. A.Z. and AA-LL,* (1982) 2 WLR 288 at 303.

Dean v. John Menzies (Holdings) Ltd., 1981 Scot L.T. 50 (Scot) was a case involving the question whether a company could be convicted of the Scots common law crime of "shamelessly indecent conduct", an offence involving *mens rea*. By a majority it was held that the complaint was incompetent by virtue of the fact that a company could not form the *mens rea* for such an offence :

"Many as are the attributes which have been imputed to a company, a sense of shame has never been regarded as one of them..." [at p. 59].

Elsewhere in the case LORD MAXWELL could not be satisfied that the common law of Scotland recognised any "clear single fiction" which would for the purposes of criminal responsibility attribute human characteristics and conduct of the sort alleged in this case : His Lordship said : "It appears to me unrealistic to suggest that the accused company will be guilty if, but only if, some individuals or individual, whose status is not precisely defined but who must be vaguely at or near director level, had knowledge of the contents of the magazines ... and acted in a shameless and indecent manner in deciding to sell them. That, however, seems to me to be the result of applying the controlling mind fiction." [at p. 64].

A company can be charged with responsibility for acts of pollution occurring in a site which is under the control of its employees who may not be in the position of being regarded as the controlling mind of the company. *National Rivers Authority v. Alfred McAlpine Homes East*, The Times, February 3, 1994 (UK). A corporate shipowner may not be held liable for the failings of subordinates if he can show that he had taken all reasonable care to assure that the ship was operated in safe manner. *Seaboard Offshore Ltd. v. Secy. of State for Transport*, (1994) 2 All ER 99 : (1994) 1 WLR 541 (HL).

Where nobody is incharge of the company's affairs at the material time, a complaint would be maintainable against the company. Section 33 of the Insecticides Act, 1968 indicates this by using the words "as well as the company". *Hindustan Chemical Industries v. State of Punjab*, (1997) 88 Com Cases 794 (P&H).

A company may be criminally liable for breach of any of the provisions of an Act or other statutory duty and may be convicted in all cases where *mens rea* is not an essential element, *R. v. Tyler & International Commercial Co.*, (1891) 2 QB 588; *Director of Public Prosecutions v. Kent and Sussex Contractors Ltd.*, (1944) 1 All ER 119 : (1944) 14 Com Cases 133 (KB).

Where an Act provides a strict duty for employee welfare and the employer is under a duty to take all reasonably practical steps to ensure the safety of workers, it has been held that it is not enough for him to show that reasonable steps were taken to delegate the responsibility to another person. The aim of the protective legislation would be defeated if directors were permitted to get out of their responsibilities by simple delegation. *R. v. British Steel Plc.*, (1995) 1 WLR 1356 (CA).

The Calcutta High Court in *A.K. Khosla v. T.S. Venkatesan*, (1994) 80 Com Cases 81 (Cal) listed some of the offences under the Indian Penal Code, 1860 which involve *mens rea* and said that a company being a juristic person cannot be prosecuted for such offences. But an indictment may properly be laid against a company when a crime is committed in the course of its business, though it cannot be guilty of conspiracy with its own director as being without a mind, it cannot act in concert with any body. See *Regina v. Mcdonnell*, (1966) 36 Com Cases 125 : (1966) 1 All ER 193.

As regards criminal liability involving proof of *mens rea*, the present position, as recognised by the courts is that the mental state of those in control and/or management of the company is attributed to the company itself as its "directing mind and will" and accordingly the company may be indictable for their criminal acts or omissions done in the course of its business and within the limits of their authority. For a review of the authorities on this subject, see *Esso v. Udharam Bhagwandas Japanwalla*, (1975) 45 Com Cases 16 (Bom—DB).

If there is anything in the definition or contents of a particular section in a statute which will prevent the application of the section to a company, certainly a company cannot be proceeded against, *e.g.*, rape cannot be committed by a company. Then again it is quite clear that a company cannot generally be tried where *mens rea* is essential and also where the only punishment for the offence is imprisonment because it is not possible to send a company to a prison. *Anath Bandhu Samanta v. Corporation of Calcutta,* (1952) 22 Com Cases 175, 177 (Cal); see also, *Hawke v. E. Hulton,* (1909) 2 KB 93; *State of Maharashtra v. Syndicate Transport Co. P. Ltd.,* AIR 1964 Bom 195, 200. However, criminal proceedings can be instituted against the principal officers of the company in such cases. *Vijaya Commercial Credit Ltd. v. Sixth ITO,* (1988) 63 Com Cases 581, 584 (Kant); *Adding Machines (India) (P.) Limited v. The State,* (1988) 63 Com Cases 588, 589 (Cal); *Modi Industries Ltd. v. B.C. Goel,* (1983) 54 Com Cases 835, 841 (All); see also, *Rangoon Electric Tramway & Supply Co. Ltd. v. Emperor,* (1933) 3 Com Cases 432, 437 (Rang).

A company to be convicted of the offence of running an entertainment business without a licence by virtue of the doctrine of delegation, the company would have to be charged with the same offence as the manager of the premises. *Southwark L.B.C. v. Allied Domecq Leisure Ltd.,* The Independent November 30, 1998 (CS—QBD).

In a reverse situation, it was held that directors couldnot be made liable under section 53 of the MRTP Act, 1969, unless the company was itself prosecuted. *M.L. Lakotia v. State,* (1988) 66 Com Cases 118 (Del). When a company is prosecuted, the summons must issue against the company itself and not against the individual who is its managing director. *Sudhir Ranjan Roy Chowdhury v. N.K. Mazumdar,* (1944) 14 Com Cases 174 : AIR 1944 Pat 210.

Attribution of *mens rea*.—There appears to be a limitation of vicarious liability to offences of strict or absolute liability. In reality the courts have not always observed such a limitation. The ground for such a limitation is that a person should not be responsible for the acts or omissions of another, in respect of which there is ignorance and no authorisation despite the fact that those acts or omissions occurred in the course of employment. Of particular significance are offences involving matters of delegation by companies because they are typically vulnerable to vicarious liability. Where criminal liability is dependent on proscribed conduct relating to land or premises, a company may be vicariously liable by virtue of its ownership of that land or those premises and the person to whom responsibility is delegated has contravened the law in question. *Mousell Bros. Ltd. v. London and North Western Railway Co.,* [1917] 2 K.B. 836. The fact of that delegation may be sufficient to justify any requisite *mens rea* being attributed to the company.

When director's/employees knowledge is company's knowledge.—In *Meridian Global Funds Management Asia Ltd. v. Securities Commission,* (1995) 2 BCLC 116 at 122: LORD HOFFMANN, delivering the opinion of the Board, considered more broadly the problem of attributing knowledge to a company. He said 'But there will be many cases..... in which the court considers that the law was intended to apply to companies and that, although it excludes ordinary vicarious liability, insistence on the primary rules of attribution would in practice defeat that intention. In such a case, the court must fashion a special rule of attribution for the particular substantive rule. This is always a matter of interpretation: given that it was intended to apply to a company, how was it intended to apply? Whose act (or knowledge, or state of mind) was *for this purpose* intended to count as the act etc. of the company? One finds the answer to this question by applying the usual canons of interpretation, taking into account the language of the rule (if it is a statute) and its content and policy.' The same issue appears to emerge from the facts of the House of Lord decision in *J.C. Houghton & Co. v. Nothard, Lowe and Wills Ltd.,* (1927) All ER 97 at 103. Here VISCOUNT DUNEDIN observed that : "The knowledge of the company can only be the knowledge of persons who are entitled to represent the company. It may be assumed that the knowledge of directors is in ordinary circumstances the knowledge of the company."

In *Supply of Ready Mixed Concrete, Re,* (1995) 1 BCLC 613 : (1995) 1 All ER 135, the issue was whether a company should be held to be in breach of an injunction in circumstances where some of its employees had disregarded the injunction contrary to the instructions of senior management, it was held that the company were liable. LORD TEMPLEMAN said [(1995) 1 BCLC 613 at 620]: 'An employee who acts for the company within the scope of his employment is the company. Directors may give instructions, top management may exhort, middle management may question and workers may listen attentively. But if a worker makes a defective product or a lower manager accepts or rejects an order, he is the company.'

§ See Notes under s. 291 *post* under the heading "Theft of company's property by director".

Whether or not a company is fixed with the knowledge acquired by an employee or officer will depend on the circumstances. It is necessary first to identify whether the individual in question has the requisite status and authority in relation to the particular act or omission in point (see *El Ajou v. Dollar Land Holdings plc.,* (1994) 1 BCLC 464 at 473 : (1994) 2 All ER 685 at 696). It follows from this that information given to a particular employee, however senior, may not be attributed to the company if that employee is not empowered to act in relation to that particular transaction. An employee who acts for the company within the scope of his employment will usually bind the company since he is the company for the purpose of the transaction in question (per LORD TEMPLEMAN in *Re, Supply of Ready Mixed Concrete,* (1995) 1 BCLC 613 at 620 : (1995) 1 All ER 135.

The company may be liable to third parties or be guilty of criminal offences even though that employee was acting dishonestly or against the interests of the company or contrary to orders. But different considerations apply where the company is the victim, and the employee's activities have caused or assisted the company to suffer loss. The company will not be fixed with knowledge where the employee or officer has been defrauding it. This has long been the law. Accordingly, employees' knowledge would not be attributed to the companies if they were acting dishonestly and were parties to the fraud. See also *El Ajou v. Dollar Land Holdings plc.,* (1994) 1 BCLC 464 : (1994) 2 All ER 685 (CA) on the subject "Directors knowledge as knowledge of company" fully discussed under s. 291.

A suggestion for the potential relevance of agency is to be found in the following words of PEARSON J. in *Regina Fur Ltd. v. Bossom,* (1957) 2 Lloyds Reports 466 at 468. "... in deciding whether ... the knowledge of the agent is to be imputed to the company or other principal, one should consider, mainly at any rate, (1) the position of the agent in relation to the principal and whether the agent had a wide or narrow sphere of operations, and (2) the position of the agent in relation to the relevant transaction and whether he represented the principal in respect of that transaction".

In *Canadian Dredge & Dock Co. Ltd. v. R.,* (1985) 19 CCC (3d.) 1 (Canada) the court was concerned with identification in relation to *mens rea* offences. The "directing mind and will" could be comprised in the board, the managing director, the manager and any other person exercising executive power delegated by the board. Where a director is formally excluded from participation in company business, but nevertheless trespasses on that territory, it seems unlikely that those acts can be identified with the company. On the other hand, it is probably not possible to subtract someone from the directing mind and will of the company just because, when doing the act which may attract liability, the director was performing a function which would ordinarily lie outside the sphere of board functions. Per MUSTILL L.J. (*obiter*) in *The Ert Stephanie,* [1989] 1 Ll. Rep. 349, at 351, 352 (CA).

When knowledge not attributable to Company

There are two exceptions to the general rule relating to agency principles for the identification of agents' knowledge with the company. A director's knowledge cannot be identified with the company : "... if the knowledge ... is the knowledge of a director who is

himself *particeps criminis* [as] artificer of such infringement...." [1927] All ER 97 at 103 (*per* LORD DUNEDIN).

In the case of *Houghton,* where these words were spoken in the judgment, the agent was the wrongdoer referred to. Subsequently, the courts reinforced this principle notably in *Belmont Finance Corporation Ltd. v. Williams Furniture Ltd.,* [1979] Ch. 250 : [1979] 1 All ER 118 and in *Attorney-General's Reference (No. 2 of 1982),* [1984] Q.B. 624 : [1984] B.C.L.C. 60 : [1984] B.C.C. 98. In Bellmont the Court of Appeal refused to agree that knowledge concerning deprivation of the company of substantial assets could be attributed. In the AG's Reference, the Criminal Division of the Court of Appeal held (following *Belmont*) that the position in criminal law is the same so that a person charged with theft from a company cannot claim that his knowledge, *inter alia,* is that of the "victim" company.

A second exception occurs on those occasions where subject information is received beyond any duty to account for it to the company. Where, for example, the information in question is communicated privately, as in *Re David Payne & Co. Ltd.,* (1904) 2 Ch. 608; *Halifax Mortgage Service Ltd. v. Stepsky,* (1996) Ch 1. In *The Hellespont Arden,* (1997) 2 Lloyds Rep. 547, the court held that a managing director had no responsibility for communicating particular information to the company. In *R. v. Roziek,* (1996) 3 All ER 281 : (1996) 1 Cr. App R 260. LEGGATT L.J. concluded that : "... information given to a particular employee, however senior, may not be attributed to the company if that employee is not empowered to act in relation to that transaction. An employee who acts for the company within the scope of his employment will usually bind the company for the purpose of the transaction in question ... The company may be liable to third parties or be guilty of criminal offences even though that employee was acting dishonestly or against the interests of the company, or contrary to orders'.

Directors liability for issuing post dated cheque.—Where a director signed and issued a post dated-cheque for paying for the goods purchased by the company, and the company was sought to be prosecuted under the Indian Penal Code for the offences of cheating under s. 420, the cheque being dishonoured and for conspiracy under s. 120-B for deceiving the supplier, the court held that such a conduct of a single director without the backing of a decision of the Board of Directors, cannot be regarded as the act of the company for criminal indictment. *Rachana Flour Mills P. Ltd. v. Lal Chand Bhanagadiya,* (1987) 62 Com Cases 15 (AP).

Liability for perjury.—A company can commit perjury through evidence given by a director who was witness on its behalf—*Odyssey (London) Ltd. v. OIC Run-off Ltd.,* (2000) TLR 201 (CA) See Notes on the case by PETER WATTS in (2000) 116 Law Quarterly Review at p. 527.

Liability for contempt

It has been held that it is wrong to impose a fine for contempt jointly and severally upon a company and one of its directors. The liability of each defendant should be determined individually. *McMillan Graham Printers Ltd. v. R.R. (U.K.) Ltd.,* The Times, March 19, 1993 (UK).

The company's punishment for contempt is naturally on the basis of attribution of an employee's conduct to the company. The circumstances in which the doctrine of attribution will come into play were examined by the House of Lords in *Supply of Ready Mixed Concrete, Re,* (1995) 1 BCLC 613 : (1995) 1 All ER 135 (HL); *Director General of Fair Trading v. Pioneer Concrete (UK) Ltd.,* (1995) 1 BCLC 613 : (1995) 1 All ER 135 (HL). The company was charged with committing breach of an injunction. The injunction had restrained the company from giving effect to or enforcing agreements restricting competition. The company accordingly forbade the employees from entering into such restrictive arrangements and also took reasonable steps to prevent them from doing so. Nevertheless an employee entered into agreements with other companies for price-fixing and job allocation which constituted a breach of the injunction order. The employee was act-

ing within the course of his employment but not within the scope of his authority because he had been instructed against such agreements. Nevertheless the company was held to be punishable for contempt. Their Lordships said that when the local manager of the company and the managers of two other companies concluded the allocation agreement they did so not as individuals but as representatives of their respective companies. The fact that the company had forbidden the employee from entering into such agreements and was also taking reasonable steps to prevent them would go to mitigation of punishment but not to wiping out the liability for the offence. A fine of £ 20,000 was imposed by way of punishment. Their Lordships pointed out that liability can only be escaped by completely effective preventive measures. How great a burden the devising of such measures will cast upon individual employees will depend upon the size and nature of the particular organisation. There are, of course, many areas of business life, not only in the consumer protection field, where it has become necessary for employers to devise strict compliance procedures.

The wilful disobedience of a court order on the part of a company by which it was directed to pay salary to its workers would make it liable to civil contempt under the Contempt of Courts Act, 1971 as well as Article 215 of the Constitution of India, though the High Court Rules provide that such order is executable as decree. *Rashtriya Mill Mazdoor Sangh v. Khatau Makanji Spinning & Weaving Co. Ltd.*, (2000) 100 Com Cases 33 : (1998) 29 CLA 389 (Bom).

Punishment for contempt does not absolve the contemner from his liability, in this case, to answer for fraud in booking on behalf of the company, plots and flats for applicants. *Delhi Development Authority v. Skipper Construction Co. (P.) Ltd.*, (1997) 89 Com Cases 362 (SC).

Section 12 Sub-sections (4) and (5) of the Contempt of Courts Act, 1971 deal with punishment of companies. There is the following comment on these provisions by S. PAL in his book THE LAW OF CONTEMPT, pp. 287, 288 (3rd Edn., 2001) : "It should be noted that sub-section (4) applies only when a company is found guilty of contempt *in respect of any undertaking* given to a court and since sub-section (5) deals with contempt of court referred to in sub-section (4), the net effect of the two sub-sections is that their application is limited to cases of *undertakings* given to court. It is submitted that this does not mean that punishment should not be imposed on a company or persons in control of the company for other types of contempt because, as already pointed out, the Supreme Court has clearly laid down that the jurisdiction of High Court to punish for contempt of itself is a special one flowing from Article 215 of the Constitution of India. *R.L. Kapur v. State of Madras*, AIR 1972 SC 858 : 1972 (1) SCC 651. Since the section is not exhaustive of the kinds of punishment that can be imposed, sequestration of assets (particularly of a company) continues to be available. *Sebastian M. Hongray v. Union of India*, AIR 1984 SC 1026 : 1984 (3) SCC 82."

Prosecution of company for evasion of Income-tax laws

A company was not allowed to be prosecuted for evasion of income-tax under section 277 of the Income-tax Act, 1961 because the section provided imprisonment and the company being a juristic person could not have been imprisoned. *P.V. Pai v. R.L. Rinawma*, (1993) 77 Com Cases 179 (Kar). The court did not agree with the opinion of the High Court of Delhi in *Delhi Municipality v. J.B. Bottling Co.*, 1975 Cr LJ 1148 to the effect that the company could be prosecuted under the Prevention of Food Adulteration Act under which there is compulsory imprisonment and fine. The only difference is that imprisonment is not possible. In the conviction of a company under the Prevention of Food Adulteration Act, 1954, which provides for compulsory imprisonment, it was held that as against the company the award of fine only was valid. The company being a juristic person could not suffer imprisonment. *Oswal Vanaspati and Allied Industries v. State of U.P.*, (1992) 75 Com Cases 770 (All) (FB). The same view was taken of a prosecution under the Income-tax Act. Only the fine portion of the conviction was valid against the

company and there was no immunity against prosecution. *Manian Transports v. S. Krishna Moorthy*, (1993) 1 Comp LJ 153 (Mad).

Punishment by way of imprisonment of officer

The court should not award any punishment less than the minimum prescribed by law. A company failed to deduct tax at source. The trial court inflicted the punishment of fine alone. It was held in revision that the principal officer should undergo imprisonment also for three months. *ITO v. D. Manoharlal Kothari*, (1999) 96 Com Cases 275 (Mad); *Electrical Fittings and Equipment, D. Manoharlal Kothari v. ITO*, (1999) 96 Com Cases 275 (Mad).

Company distinct from its shareholders

A shareholder has got no interest in the property of the company though he has undoubtedly a right to participate in the profits if and when the company decides to divide them... The company is a juristic person and is distinct from the shareholders. The dividend is a share in the profits declared by the company as liable to be distributed among the shareholders. There is nothing in the Indian law to warrant the assumption that a shareholder who buys shares, buys any interest in the property of the company which is juristic person entirely distinct from the shareholders. The true position of a shareholder is that on buying shares he becomes entitled to participate in the profits of the company in which he holds the shares, if and when the company declares, subject to the Article of Association, that the profits or any portion thereof should be distributed by way of dividends among the shareholders. He has undoubtedly a further right to participate in the assets of the company which would be left over after winding up. *Bacha F. Guzdar v. CIT*, AIR 1955 SC 74 : (1955) 25 Com Cases 1. GOVARDHAN J of the Madras High Court cited this passage with **approval** in *Naga Brahma Trust v. Translanka Air Travels (P.) Ltd.*, (1997) 88 Com Cases 136 at 140 (Mad). The court observed that lease-hold rights of a company cannot be said to be the rights of its shareholders. Accordingly, if the company admits new members, it cannot be described as a device for subletting the lease to new members against the provisions of the lease-deed. The premises of a company were with a tenant. The principal share-holder sought eviction on the ground that she needed the premises for personal business. The court did not identify her personal need with that of the company. *Tunstall v. Steigman*, (1962) 2QB 593 : (1962) 2 All ER 417 (CA).

The protection under tenancy legislation against eviction which was available to a tenant who was carrying on business on the premises was not allowed to be claimed by a husband-wife company which was carrying on the business, the tenancy being in favour of the couple. *Cristina v. Seear* [1985] 2 EGLR 128.

In the case of a wholly-owned Government company, it was held that it did not become the agent of the President or Governor, or the Central or State Government. Notice to the President or Governor (or to officers who held shares as nominees) would not be a notice to the company. *Heavy Engg. Mazdoor Union v. State of Bihar*, AIR 1970 SC 82 : (1969) 39 Com Cases 905.

Similarly a person holding by himself and through nominees, practically all the shares of a company was not regarded as having became the owner of the company's business or assets and the profits of the company would not be treated as his profits. *Gramophone and Typewriter Ltd. v. Stanley*, (1908-10) All ER 833 (CA). Sale of shares of a company owning lands does not constitute sale of the lands so as to attract Delhi Land (Restriction on Transfer) Act, 1972. *Scindia Potteries & Services Ltd. v. Deputy Land and Development Officer*, (1990) 41 DLT 261 (Del).

Where a company was registered dealer under a sales tax legislation, it was held that only the company could be proceeded against as dealer for any violation of the statutory provision and not any shareholder though he might be playing a leading role in the management of affairs. *Rameswar Agarwala v. State of W.B.*, (1955) 25 Com Cases 341, 342 (Cal—DB).

A member of a company has no *locus standi* to challenge any decree passed against the company or the execution thereof unless his rights as such shareholder are affected nor can such challenge be raised by the guarantor of a loan taken by the company. *Vivek Kumar v. Pearl Cycle Industries Ltd.*, (1983) 54 Com Cases 77 (Del). The fact of a loan to a person by the principal shareholder for which an action was filed and was dismissed was not allowed to support the plea of *res judicata* to a proceeding by the company against the same person on the company's own loan. *Barakot Ltd. v. Epiette Ltd.*, (1998) 1 BCLC 283 (CA). A distinction should be maintained between a company's legal entity and its actions, assets, rights and liabilities on the one hand and the individual shareholders and their actions, assets, rights and liabilities on the other. *EBM Co. Ltd. v. Dominion Bank*, (1937) 7 Com Cases 448, 459 : AIR 1937 PC 279.

A suit to recover the property of a company, to enforce its rights, or to redress any wrong done to it, can be filed only by the company itself. See *Burland v. Earle*, (1902) AC 83 (PC); *Clarkson v. Davies*, (1923) AC 100 : (1922) All ER Rep Ext 809 (PC). A shareholder cannot apply under Order XXI, Rule 90 CPC to set aside the execution sale of the company's assets. *Shyamlal Purohit v. Jagannath Ray*, (1970) 40 Com Cases 138, 147, 149 (Cal).

A shareholder does not have an interest in any particular asset of the company. He is not a necessary or a proper party in a suit concerning the particular assets. *Purna Investment Ltd. v. Bank of India*, (1984) 55 Com Cases 737, 738, 741 (Cal).

A company is distinct from its Board of Directors. They also cannot enforce a right in their individual capacity which belongs to the company. *Tata Engineering and Locomotives Co. Ltd. v. State of Bihar*, AIR 1965 SC 40 : (1964) 34 Com Cases 458; *Prithvi Cotton Mills v. Broach Borough Municipality*, AIR 1968 Guj 124 at 148. A suit filed by the directors of a company to challenge a term in a lease agreement of the company on the ground that it was fraudulently interpolated was held to be incompetent because only the company had the *locus standi* to sue and not the directors. *Rajendra Nath Dutta v. Shibendra Nath Mukherjee*, (1982) 52 Com Cases 293 at 298 (Cal).

A shareholder cannot insure the company's property in his own name even if he is the owner of all or most of the company's shares. The property belongs to the company and the shareholder has no insurable interest in it. *Macaura v. Northern Assurance Co.*, (1925) AC 619 (HL); *Caparo Industries Plc. v. Dickman*, (1990) BCLC 273 : (1990) 1 All ER 568 (HL); *Verderame v. Commercial Union Assurance Company Plc.*, (1992) BCLC 793 (CA). For details see under the heading "Insurance Broker's duty to principal shareholder" *infra*. The possessions of the company are not the property of its members. *Bank Voor Handle en Scheepvaart NV v. Slatford*, (1953) 1 QB 248. However, it has been held that where an Act permits the incorporation of a company with one shareholder and one director, such shareholder-director would have a insurable interest in the property of the company. *Constitution Insurance Co. of Canada v. Kosmopoulos*, (1980-1984) LRC (Comm) 784.

Where the majority of the partners of a firm formed a limited company and sold their own buses, which were being used by the partnership, to the company, the company carrying on the business which was hitherto being done by the firm, and the dissenting partners having sued for an account of the profits of the company claiming that it was the business of the partnership which was being conducted under the name of the artificially created company, it was held that the company was a *persona* totally different from partners in majority who were shareholders in the company and the business of the company being not the business of the partnership, section 37 of the Partnership Act 1932 did not apply. The court also said that section 67 of the Trusts Act did not also apply since there was no fiduciary relationship between the company and the dissenting partners; and that therefore the dissenting partners had no right to, and could not sue for, an account of the profits of the company. *Dhulia-Amalner Motor Transport Ltd. v. Raychand Rupsi Dharamsi*, (1952) 22 Com Cases 306 (Bom).

Guarantors not discharged by change of management.—The change in the management of a company does not affect the liability structure of the company. So the guarantors of the company's debts are not discharged by reason merely of a change in management. *Punjab National Bank v. Lakshmi Industrial and Trading Co. P. Ltd.*, AIR 2001 All 28 : (2000) 6 Comp LJ 450 : (2002) 111 Com Cases 109 (All).

Company not agent of shareholders.—No shareholder can lay any claim to the rights vested in the company or be bound by any obligations, duties or liabilities unless it can be shown that he was using the company as his agent. *J.H. Rayner (Mincing Lane) Ltd. v. Department of Trade & Industry*, (1990) 2 AC 418 HL. The fact that the members exercise some manner of control over the affairs of the company or that they are the ultimate beneficiaries of the company's business, etc., is not sufficient in itself to constitute the company as an agent of its members. (*ibid* at p. 515). LORD PARKER OF WADDINGTON summarised the law as follows in *Daimler Co. Ltd. v. Continental Tyre & Rubber Co. (Great Britain) Ltd.*, (1916) 2 AC 307 at p. 338: "No one can question that a corporation is a legal person distinct from its corporators; that the relation of a shareholder to a company..... is not in itself the relation of principal and agent or the reverse; that the assets of the company belong to it and the acts of its servants and agents are its acts, while its shareholders, as such, have no property in the assets and no personal liability for those acts." Accordingly, the members do not owe any duty in respect of, and cannot be made liable in tort for, the company's acts. *Kuwait Asia Bank Ltd. v. National Mutual Life Nominees Ltd.*, (1991) 1 AC 187 : (1990) BCLC 868 : (1990) 3 All ER 404 (PC). ALDERSON B said in *Bligh v. Brent*, (1837) 2Y & C Ex 268 : 'The individual members of a corporation are quite as distinct from the metaphysical body called "the corporation", as any others of his Majesty's subjects are'. This principle confers on the members of a corporation the benefit of immunity from liability for the corporation's debts except to the extent where such liability is imposed by statute or by the company's constitution.

In *Wurzel v. Houghton Main Home Delivery Service Ltd.*, (1937) 1 KB 380 (DC), the lorry of the defendant company was used to deliver coal to its members. The members paid delivery charges to the company. It was held that the vehicle was used for carriage for hire or reward, which made it a public carrier whereas it was licenced for private carriage. The company was convicted for breach of license.

In *Farrar v. Farrars Ltd.*, (1888) 40 Ch D 395 (CA) three individuals were joint mortgagees of a stone quarry. When the interest on the mortgage debt was not paid they decided to exercise their power of sale. They sold the quarry to Farrars Ltd., a company in which two of them held shares. The mortgagors asked for the sale to be rescinded on the ground that it was a sale by the mortgagee to themselves. The court refused to agree. LINDLEY LJ explained, at pp. 409-10. "It is perfectly well settled that a mortgagee with a power of sale cannot sell to himself either alone or with others, nor to a trustee for himself.....A sale by a person to himself is no sale at all....." "A sale by a person to a corporation of which he is a member is not, either in form or in substance, a sale by a person to himself. To hold that it is, would be to ignore the principle which lies at the root of the legal idea of a corporate body, and that idea is that the corporate body is distinct from the persons composing it." This will not relieve the mortgagees of their duty to realise fair market value of the mortgaged property. *Tse Kwong Lam v. Wong Chit Sen*, (1983) 1 WLR 1349 (PC).

Shareholders' experience is company's experience.—Where a company's tender for publication of telephone directory was not accepted because the company had nothing on its records to show that it had the technical experience which was one of the requisites of the tender, it was held that the company was not qualified for the tender and that the experience of the company's shareholders could not be regarded as that of the company. *New Horizons Ltd. v. Union of India*, AIR 1994 Del 126 : (1997) 89 Com Cases 785. This decision of the High Court of Delhi was **reversed** by the Supreme Court in *New Horizons Ltd. v. Union of India*, (1997) 89 Com Cases 849 : (1997) 27 Corpt LA 56 (SC). The court said that it is permissible to see through the corporate veil to find out from the

shareholders or from the people controlling the company's affairs something about the nature of the company. The company was composed of a few joint venturers all of whom contributed machinery, equipment and personal expertise. The court continued to say that in such circumstances the experience of the company can only mean the experience of its constituents. Such experience having been ignored by the tender evaluation committee on a wrong hypothesis thereby disqualifying the tenderer, resulted in a legal wrong to the tenderer. The committee was the victim of misguidance.

Shareholders cannot treat company's assets as their own.—Two men in total control of a limited company by reason of their shareholdings and directorships are (while acting in concert) capable of jointly stealing the property of the company. They cannot then contend that through their joint consent, the company had given its consent. The shareholders cannot by their unanimous consent permit or authorise the directors to do an act which is beyond the company's powers. The joint will of the shareholders cannot prevail in reference to an act which neither they nor the company is authorised to do. *A.G's Reference (No. 2 of 1982),* (1984) 2 All ER 216 : 1984 BCLC 60 (CA).

Directors of a private company are equally liable for a misapplication of the company's funds or for other misfeasance. In *Re, Geo Newman & Co.,* (1895) 1 Ch 674, 685, one Newman had converted his business into a "private" company, and had applied funds of the company, with the privity and consent of the other members, to *ultra vires* purposes. It was held that he was guilty of misfeasance, and that the fact that it was a private company did not in any way exempt or protect him. See also *HC Shastri v. Dolphin Cornpack Pvt. Ltd.,* (1998) 93 Com Cases 201 : (1998) 4 Comp LJ 75, (Del) the assets of the company were not allowed to be used for payment of the debts of a shareholder. Unless a company's incorporation could be viewed as a sham, company property would fall outside the scope of distribution of matrimonial assets on divorce. *Wilson v. Wilson,* 1999 S.L.T. 249 (Scot).

The last surviving member of a company or his legal representatives were not permitted to sue for dissolution and accounts. They too would have to seek the appointment of a liquidator and the later may appoint the legal representatives of a member as agents to run the business of the company for beneficial winding up. *Ashok Krishna Nagvenkar v. Hari Vishnoo Lotlekar,* (1989) 66 Com Cases 321 (Bom).

On the nationalisation of coal mines, it was found in the case of a company that it had sold an item of its immovable property to a director's wife. The court pierced behind the veil to see the genuinness of the transaction and found that it was a sham arrangement. The transaction was set aside. The property remained that of the company and became vested in the Government. *Subhra Mukherjee v. Bharat Coking Coal Ltd.,* 2000 CLC 677 : (2000) 101 Com Cases 257 : AIR 2000 SC 1203.

Shareholder's property is not company's property.—A company has no *locus standi* to protest against a statutory operation which has affected the interest of the company's shareholders only. In a case of this kind in *Kathiawar Industries Ltd. v. Custodian General of Evacuee Property,* AIR 1967 Punj 337 at p. 338 the Court observed: [at p. 338]: "That a limited company has its own entity apart from the shareholders is a proposition which has not been disputed at the Bar and indeed cannot be contested. Once that position is accepted, as indeed it must, there is no escape from the conclusion that the limited company cannot set itself as a spokesman for the shareholders whose interests have been found to have merged in the Custodian as evacuee property. As observed by the Bench, the other shareholders who have become evacuees may feel that there is no answer they have on the merits. It is said that the petitioner is represented by its directors who have chosen to contest the decision of the Custodian on the ground that the company has a lien over the shares which have been declared to be evacuee property. It is important to remember that the directors of the company represent the controlling interest and they cannot be equated with the company itself. The position remains that the company

being different from the shareholders it has no *locus standi* to bring a petition on their behalf."

The property of a company cannot be considered to be the property of members. The fact that the majority of shareholders of a company have migrated to India does not and cannot change the nationality and domicile of the company. Where a company never made any efforts to change its domicile by transferring its registered office from Hyderabad (Sind) to any territory in India before the partition of the country, the company could not be held to have migrated to India in the circumstances mentioned in the Displaced Persons (Claims) Act of 1950. *Hyderabad (Sind) Electric Supply Co. Ltd. v. Union of India,* AIR 1959 Punj 199, 204. The tenancy rights of the shareholder which were being used by the company, the company's right to use ended when the shareholders withdrew their permission. *Rajdhani Chit Fund P. Ltd. v. Mukesh Maheshwari,* (1999) 96 Com Cases 837 (Del).

Liability of company is not liability of shareholders/directors

The shareholders cannot be made liable under a decree against a company. *Nihal Chand v. Kharak Singh Sunder Singh,* (1936) 6 Com Cases 418, 421 (Lah); *Harihar Prasad v. Bansi Missir,* (1932) 2 Com Cases 32, 36, 41 (Pat) (FB). Similarly, the individuals constituting the company cannot be responsible for sales tax/Income tax dues of the company. It is only the assets of the company which can be proceeded against. *Desiraju Vankatakrishna Sarma, Re,* (1955) 25 Com Cases 32, 35 : AIR 1955 AP 26; *Parameshwari Das v. Collector of Bulandshahr,* (1955) 25 Com Cases 343 (All). *G.C. Mehrotra v. Deputy Collector (Collections) Sales tax,* (1998) 93 Com Cases 617 (All) [case on recovery of Income tax dues].

A director's personal telephone was not allowed to be disconnected for the company's arrears. *Kailash Prasad Modi v. Chief General Manager, Orissa Telecommunications,* AIR 1994 Ori 98. The liability of a company for its telephone bill is not automatically transferred to its directors by reason of the fact that there has been default in payment. The court distinguished in this respect the position of the partners of a firm. *V.V. Rama Rao v. Union of India,* (1998) 30 CLA 131 (AP). The liability of a Chit Fund Company was not allowed to be enforced against the Company's director. The attachment of his property for this purpose was held to be not permissible. *Kurakose v. PKV Group Industries,* (2002) 111 Com Cases 826 : (2002) 37 SCL 817 : 2002 CLC 1208 : (2002) 50 CLA 41 (Ker).

Director not employer of company's employees.—A director is not an employer of the company's workers for the purposes of the Employees' State Insurance Act, 1948. *Employees' State Insurance Corpn. v. S.K. Aggarwal,* (1998) 94 Com Cases 75 (SC) : (1998) II LLJ 794.

Director's/Shareholder's liability is not company's liability.—The Government was not permitted to deny a licence to a company under Inland Vessels Act, 1917 for the liabilities and defaults of personal nature on the part of a company's director. *Sar Desai Transhippers P. Ltd. v. State of Goa,* (1997) 25 Corpt LA 357 (Bom).

Where a director furnished a guarantee in his personal capacity, a suit on the guarantee was not allowed to be maintained against the company. *Himachal Pradesh State Electricity Board v. Shivalik Casting P. Ltd.,* (2003) 115 Com Cases 310 : (2004) 50 SCL 212 (HP).

Shareholders' action *res judicata* against company

The controlling shareholder of a company commenced an action against a company for recovery of a loan which was supposed to have been made by one company to the other. The claim was dismissed on the ground that it did not disclose a cause of action because the alleged loan agreement pre-dated the incorporation of the defendant company. A subsequent action by the company itself on the same claim, though this time on the basis of a written agreement, was held to be prevented by *res judicata.* The company was wholly

owned and controlled by one person and the action by the company could have been at his behest. *Barakot Ltd. v. Epietle Ltd.*, (1997) 1 BCLC 303 (QBD).

Common management.—The mere fact that two companies had the common managing directors was held to be not sufficient for treating the two companies as one unit. Both companies belonged to the category of textile mills. The matter under consideration had arisen under the Payment of Gratuity Act, 1972. *Sri Ganeshar Textile Mills Ltd. v. Appellate Authority under PG Act,* (2001) CLC 583 (Kant).

Decree against company in same group.—A decree against a company cannot be satisfied by attachment and sale of properties belonging to other companies even if they are being managed by the same group of persons. *Punjab National Bank v. Bareja Knipping Fasteners Ltd.*, (2001) 103 com Cases 958, 959 : (2001) 30 SCL 456 (P&H).

Lifting the corporate veil

As regards the true legal position of a company or corporate body and the circumstances under which its entity as a corporate body will be ignored and the corporate veil lifted, so that the individual shareholder may be treated liable for its acts, the Supreme Court has expressed itself as follows:—

"The true legal position in regard to the character of a corporation or a company which owes its incorporation to a statutory authority is not in doubt or dispute. The corporation in law is equal to a natural person and has a legal entity of its own. The entity of the corporation is entirely separate from that of its shareholders; it bears its own name and has a seal of its own; its assets are separate and distinct from those of its members; it can sue and be sued exclusively for its own purpose; its creditors cannot obtain satisfaction from the assets of its members; the liability of the members or shareholders is limited to the capital invested by them; similarly the creditors or the members have no right to the assets of the corporation. This position is well established ever since the decision in case of *Salomon v. Salomon & Co.*, 1897 AC 22 was pronounced in 1897 and indeed, it has always been the well recognised principle of common law. However, in course of time, the doctrine, that a corporation or company has legal and separate entity of its own has been subjected to certain exceptions by the application of the fiction that the veil of the corporation can be lifted and its face examined in substance. The doctrine of the lifting of the veil thus marks a change in the attitude that law had originally adopted towards the concept of the separate entity or personality of the corporation. As a result of the impact of the complexity of the economic factors, judicial decisions have sometimes recognised exceptions to the rule, about the juristic personality of the corporation. It may be that in course of time these exceptions may grow in number and to meet the requirements of different economic problems, the theory, about the personality of the corporation may be confined more and more."

"The doctrine of the lifting of the veil has been applied, in the words of PALMER, in five categories of cases: where companies are in relationship of holding and subsidiary (or sub-subsidiary) companies; where a shareholder has lost the privilege of limited liability and has become directly liable to certain creditors of the company on the ground that, with his knowledge, the company continued to carry on business six months after the number of its members was reduced below the legal minimum; in certain matters pertaining to the law of taxes, death duties and stamps, particularly where the question of the "controlling interest" is in issue; in the law relating to exchange control, and in the law relating to trading with the enemy where the test of control is adopted (PALMER'S COMPANY LAW, 20th Edn., page 136 Now page 215, 24th Edn., 1987). In some of these cases judicial decisions have no doubt lifted the veil and considered the substance of the matter."

"GOWER has similarly summarised this position with observation that in a number of important respects, the Legislature has rent the veil woven by the *Salomon* case. Particularly is this so, says Gower, in the sphere of taxation and in the steps which have been taken towards the recognition of enterprise—entity rather than corporate entity. It is sig-

nificant, however, that according to GOWER the courts have only construed statutes as "cracking open the corporate shell" when compelled to do so by the clear words of the statute; indeed they have gone out of their way to avoid this construction whenever possible. Thus, at present the judicial approach in cracking open the corporate shell is somewhat cautious and circumspect. It is only where the legislative provision justifies the adoption of such a course that the veil has been lifted. In exceptional cases where courts have felt "themselves able to ignore the corporate entity and to treat the individual shareholder as liable for its acts" the same course has been adopted. Summarising his conclusions, Gower has classified seven categories of cases where the veil of a corporate body has been lifted. But it would not be possible to evolve a rational consistent and inflexible principle which can be invoked in determining the question as to whether the veil of the corporation should be lifted or not. Broadly, where fraud is intended to be prevented, or trading with enemy is sought to be defeated, the veil of corporation is lifted by judicial decisions and the shareholders are held to be "persons who actually work for the corporation." *Tata Engineering and Locomotive Co. Ltd. v. State of Bihar,* (1964) 34 Com Cases 458 : AIR 1965 SC 40. See also *Andhra Pradesh State Road Transport Corporation v. Income-tax Officer,* AIR 1964 SC 1486 : (1964) 34 Com Cases 473; *Life Insurance Corporation v. Hari Das Mundhra,* (1966) 36 Com Cases 371, 392 (All). In *Shri Ambica Mills Ltd., Re,* (1986) 59 Com Cases 368, 392 (Guj), it was held that when the question of fraud by some officers is on the anvil, the court cannot be precluded from tearing of the veil to reach the substance of the matter. Likewise where unjust enrichment has resulted from a transaction the veil would be pierced by court to prevent that. *Nellie Wap-share v. Pierce Leslie & Co.,* AIR 1960 Mad 410.

In the case of *P.N.B. Finance Ltd. v. Shital Prasad Jain,* (1983) 54 Com Cases 66 (Del) a Division Bench of the Delhi High Court granted to the plaintiff company an order of interim injunction restraining defendant companies from alienating the properties of their ownership on the ground that the defendant companies were merely nominees of 1st defendant who had fraudulently used the money borrowed from the plaintiff company and bought properties in the name of defendant companies. Protection under the doctrine of corporate veil could not be invoked in the facts and circumstances of the case. See also *A Company, Re,* 1985 BCLC 333 (CA).

In *Re, FG (Films) Ltd.,* (1953) 1 All ER 615 (Ch D) the court refused to compel the board of film censors to register a film as an English film, which was in fact produced by a powerful American film company in the name of a company registered in England in order to avoid certain technical difficulties. The English company was created with a nominal capital of £ 100 only, consisting of 100 shares of which 90 were held by the American president of the company. Two out of three directors were British and all the funds were to be provided by the American company. The court held that the real producer was the American company and that it would be a travesty of facts to hold that the American company and American president were merely agents of the English company for producing the film.

Shareholders cannot be the principals for the company but if so, it should be proved that the company was their agent in one or more transactions. *Ebbow Vale U.D.C. v. South Wales Traffic Area Licensing Authority,* (1951) 2 KB 366 (CA); *Pegler v. Craven,* (1952) 1 All ER 685 (CA).

Where the Government subsidy granted to one company was adjusted against the dues of two other companies owned by the same group of promoters and having some of the common shareholders and directors, the court in the absence of fraud declined to pierce the corporate veil. *Orissa Industries Ltd. v. State of Orissa,* 1983 Tax LR 2501 (DB) (Ori).

The court would refuse to resort to the doctrine of lifting the corporate veil when it would defeat, instead of promoting, the aims of a statutory enactment. The Supreme Court adopted this approach in *Life Insurance Corporation of India v. Escorts Ltd.,*

(1986) 59 Com Cases 548 : AIR 1986 SC 1370.[1] A group of 13 companies incorporated abroad combined to purchase the shares of a company in India under schemes sponsored under the Foreign Exchange Regulation Act, 1973. The Act encouraged investment by non-resident Indians to a certain extent and to a slightly higher extent in the case of companies belonging to non-resident Indians. For ascertaining whether a company belongs to non-resident Indians the test prescribed in the Act is that of 60% shareholding in non-resident Indian hands. It was prayed before the Supreme Court that all the thirteen companies belonged to one family trust which was operated by a single person. The purchases ostensibly effected in name of 13 companies were in reality effected by one man and FERA was consequently violated. The Supreme Court refused to lift the veil for the purpose. The policy and purpose of FERA is to attract investment by non-resident Indians. The lifting prayed for here would go against that policy. Where the legislature desired 'lifting' they expressly provided that the character of shareholding may be examined to ascertain whether a company incorporated abroad belonged to non-resident Indians. That amounts to saying that there is no authorisation under the Act for lifting the veil in any other case.

The same approach dominated the decision in another case where the court refused to examine whether the purchase by one foreign company of the shares of another foreign company amounted to purchasing the shares of an Indian company. *Carrasco Investments. Ltd. v. Special Director, Enforcement Directorate,* (1994) 79 Com Cases 631 (Del).

In *Re, Shaw Wallace & Co. Ltd.,* (CLB Order dt. 31-10-1985) the Company Law Board noted that the powers conferred on the Central Government under section 250(3) are so clear and direct in themselves that they do not involve or make necessary the lifting of the corporate veil.

The following version of the subject as it appears in PALMER COMPANY LAW, have been cited by D.P. WADHWA J in *New Horizons Ltd. v. U.O.I.,* (1997) 89 Com Cases 785 [at 798-807] (Del): In PALMER COMPANY LAW, 25th Edn., the Para 2. 1508, it is mentioned that the veil of corporateness can be lifted in the following cases under the English Law:

(1) Where companies are in the relationship of holding and subsidiary (or sub-subsidiary) companies, the Companies Acts require, on principle, group accounts.

(2) Where a shareholder has lost the privilege of limited liability and has become directly liable to certain creditors of the company on the ground that, with his knowledge, the company continued to carry on business six months after the number of its members was reduced below the legal minimum.

(3) In certain matters pertaining to the law of taxation, particularly where the question of the "controlling interest" is in issue.

(4) In the law relating to trading with the enemy, where the test of control is adopted.

(5) In the law of merger control in the United Kingdom. The Fair Trading Act, 1973, adopts the test of "distinct enterprises". Cessation of being "distinct enterprises", irrespective of the legal form of those enterprises, constitutes, subject to certain conditions, a merger situation.

(6) In the competition law of the European Economic Community, as contained in articles 85 and 86 of the EEC Treaty and in secondary legislation on that subject, a holding company and a subsidiary, which does not determine its behaviour on the market in an autonomous manner, are treated as forming an economic unit. An arrangement between a holding company and its non-autonomous subsidiary does not fall under article 85 and a holding company incorporated in a country which is not a member of the EEC is regarded as being present in the EEC if it has a non-autonomous subsidiary in EEC territory.

(7) The court will not allow an abuse of section 429 by the formation of a new company by members holding nine tenths of the shares in an existing company, if the new company is formed solely for the purpose of expropriating the shares of the minority shareholders in the existing company.

(8) The courts have further shown themselves willing to "lift the veil" where the device of incorporation is used for some illegal or improper purpose. So, where a transport company sought to obtain licences for its vehicles, which it was unlikely to obtain if it made application on its own behalf, by causing the application to be made by a subsidiary company to which the vehicles were to be transferred, the court refused to treat parent and subsidiary as independent bodies, and decided the application on the basis that they were one commercial unit. Similarly, where a vendor of land sought to avoid an action for

specific performance by transferring the land in breach of contract to a company he had formed for the purpose, the court treated the company as a mere "sham" and made an order for specific performance against both the vendor and the company. However, a rearrangement of a group of companies so as to minimise the extent of any future tort liability that could be enforced in respect of the group's activities is a proper use of the possibilities provided by company law and will not entitle the court to lift the corporate veil. Where a bankrupt obtained credit for himself through the "charade" of a company, he committed an offence under what is now section 360(1)(a) of the Insolvency Act, 1986, although normally the offence is not committed if the credit is obtained for another person.

(9) Where a private company is founded on a personal relationship between the members, the court is prepared to order the winding up of the company under the "just and equitable" clause (section 122(1)(g) of the Insolvency Act, 1986), if a member commits a breach of good faith which the members owe each other as the result of the personal relationship and thereby acts inequitably. That these *quasi*-partnership companies may be wound-up by the court by virtue of section 122(1)(g) in appropriate circumstances constitutes a lifting of the veil of corporateness, because here the substance of the association prevails over its legal form. In *Ebrahimi v. Westbourne Galleries Ltd.*, (1973) AC 360 (HL), LORD WILBERFORCE, when commenting on the words "just and equitable" in what is now section 517(1)(g), said that "the words are a recognition of the fact that a limited company is more than a mere judicial entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations *inter se* which are not necessarily submerged in the company structure."

(10) Where the court considers it appropriate to issue a Mareva injunction (or another injunction founded on section 37 of the Supreme Court Act, 1981) "the court will use its power to pierce the corporate veil if it is necessary to achieve justice irrespective of the legal efficacy of the corporate situation under consideration.

(11) It has sometimes been argued that there is emerging in English and Scottish law a general principle that all companies in a group of companies will be treated as a single entity. Certainly, there are many cases in which the distinction between parent and subsidiary company has been ignored by the court, of which notable recent examples are *DHN Food Distributors Ltd. v. Tower Hamlets LBC*, (1976) 1 WLR 852 and *Revlon Inc. v. Cripps and Lee*, (1980) FSR 85. In the former, for the purpose of a statutory claim for compensation arising out of a compulsory purchase, the holding company, which ran the business, was held to be entitled to compensation for disturbance of that business, even though the land that had been compulsorily acquired belonged to a subsidiary company. In the latter, a trade mark, owned by a Swiss subsidiary of an international group, was regarded as an asset of the group as a whole.

On the other hand, *DHN Food Distributors Ltd.'s* case, (1976) 1 WLR 852 (CA) was distinguished in a similar compensation case by the House of Lords in *Woolfson v. Strathclyde Regional Council*, (1978) SLT 159 and the underlying principle of the separate corporate entity applied even in a group situation. In *Adams v. Cape Industries Plc.*, (1990) 2 WLR 657, the Court of Appeal regarded all the cases in which the parent/subsidiary distinction had been ignored as turning on the wording of particular statutes or contracts. It was denied that there was a general principle that all companies in a group should be regarded as one. Nevertheless, this did not preclude treating, say, a subsidiary as the agent or the alter ego of its parent, provided the facts of the case justified such a conclusion. However, it would seem that the facts would have to reveal a very high degree of control by the parent over the subsidiary before a court would conclude that an agency relationship had been established. In *Cape Industries Plc.'s* case, (1990) 2 WLR 657, although the group ran a single integrated mining division with little regard to corporate formalities as between members of the group, and although the parent exercised a degree of overall supervision over the subsidiary in question (NAAC), in particular by setting its maximum level of expenditure and its dividend and borrowing levels, and by subjecting the subsidiary to the broad business policies of the parent, an agency relationship was not found to have been established. This seems to have been because the subsidiary retained control of its day-to-day business and because the corporate forms applicable to NAAC as a separate legal entity were observed.

A somewhat similar approach was taken in *Lonrho Ltd. v. Shell Petroleum Co. Ltd.*, (1980) QB 358 (CA) **affirmed** in (1980) 1 WLR 627 (HL), where the question arose whether English holding companies could be compelled by an English court to give discovery of documents held by their Rhodesian and South African subsidiaries under the Rules of the Supreme Court, 1965, Ord. 24, rr. 2 and 3, which required the disclosure of all documents (except privileged ones) in the "possession, custody or power" of a party. It was clear that the Rhodesian and South African documents were not in the possession or custody of the English holding companies but the question was whether they were in their "power". The Court of Appeal held that much depended on the facts of the individual case and that in the present case the documents were not in the "power" of the holding companies, as the subsidiaries enjoyed a great deal of autonomy and compliance with a request for disclosure would have exposed the directors of the subsidiaries to criminal prosecution in the countries in which they carried on business. The House of Lords **affirmed** this decision of the Court of Appeal in *Lonrho Ltd. v. Shell Petroleum Co. Ltd.*, (1980) QB 358.

(12) In *Amalgamated Investment and Property Co. Ltd. (In Liquidation) v. Texas Commerce International Bank Ltd.*, (1982) QB 84 (CA), the plaintiffs undertook a guarantee for loans advanced by the defendant bank to one of the plaintiff's subsidiaries. Some of these loans were given, for exchange control reasons, through a wholly-owned subsidiary of the bank in the Bahamas named Portsoken, but the guarantee was never expressly extended to the Portsoken loans. The Court of Appeal held that the plaintiff's guarantee covered the Portsoken loans. LORD DENNING M.R. said that Portsoken had to be regarded as the alter ego of its parent, the bank, but the other judges (EVELEIGH AND BRANDON L. JJ.) preferred to found their judgments in favour of the bank on an estoppel created by the course of dealing between the parties."

Fraudulent investment schemes.—The court can lift the corporate veil so as to find out and expose persons who were floating fraudulent investment schemes at high returns in the name of the company. The fraud is criminal offence of cheating. The court ordered police investigation. The property acquired by fraud, cheating, *etc.* was ordered to be followed and seized from wherever it was lying. *Ali Jawad Ameerhasan Rizvi v. Indo French Biotech Enterprises Ltd.*, (1999) 95 Com Cases 373 : (1999) 1 Comp LJ 288 (Bom); *Securities and Exchange Board of India v. Libra Plantation Ltd.*, (1999) 1 Comp LJ 294 (1999) 95 Com Cases 373 (Bom); *Dindas Shankar Thange v. State of Maharashtra*, (1999) 1 Comp LJ 299 (1999) 95 Com Cases 373 (Bom).

Lifting corporate veil, principle or policy

In *Creasey v. Breachwood Motors Ltd.*, (1993) BCLC 480 (QBD) (noted 1993 JBL 41), the employer, Welwyn Ltd., dismissed its general manager. He issued a writ alleging wrongful dismissal. Shortly thereafter Welwyn ceased trading. The company paid off all its creditors and then transferred its remaining assets to another company. The plaintiff obtained a default judgment against the company but by that time it had no assets and stood dissolved. The transferee company to which the company's assets were transferred (Motors) was ordered to pay the decree. The court stated that the takeover of the company's assets had been carried out without regard to the separate entity of the company and the interests of its creditors, particularly the plaintiff. When the directors transferred the company's assets and business, they did so in total disregard of their duties as directors and shareholders. Accordingly, it was held that this constituted a case in which the courts would be justified in lifting the corporate veil and treating Motors liable for the company's liability to the plaintiff.

A learned commentator puts the following comment on the case: "This decision does not appear to fit neatly into any of the established categories where the courts have been prepared to pierce the veil—unless it is accepted that in reality, policy is generally the pivotal factor underlying these decisions. However, the cases do appear to support the proposition that adherence to the *Salomon* principle will not be doggedly followed where this would cause an unjust result. Such an approach was given explicit judicial recognition in the American case of *Re, Clark's Will*, 204 Minn 574 at 578 (1939) where STONE J. said: "Many cases present avowed disregard of corporate entity.... But they all come to just this—courts simply will not let interposition of corporate entity or action prevent a judgment otherwise required. Corporate presence and action no more than those of an individual will bar a remedy demanded by law in application to facts. Hence the process is not accurately termed one of disregarding corporate entity. It is rather and only a refusal to permit its presence and action to divert the judicial course of applying law to ascertained facts. The method neither pierces any veil nor goes behind any obstruction, save for its refusal to let one fact bar the judgment which the whole sum of facts requires..." "Against this background then, the decision can be more readily explained. The problem that can naturally arise from this approach is the uncertainty which it casts over the safety of incorporation. The use of policy to erode established legal principle is not necessarily to be welcomed." [JOHN P. LAVRY, *Lifting The Corporate Veil*, (1993) JBL 41 at 42].

The decision in *Creasey's* case (*supra*) was also **not approved** by the Court of Appeal in *Ord v. Belhaven Pubs Ltd.* (1998) 2 BCLC 447 (CA). In a sense, it may not matter

what langauge is used, 'lifting the corporate veil' or 'piercing the corporate vail', as long as the principle is clear. "For metaphor can be used to illustrate a principle; it may also be used as a substitute for analysis and may therefore obscure reasoning". *The Coral Rose (No. 1)* (1991) 4 All ER 769 at 779. "Some authorities have suggested that the court will use its powers to pierce the corporate veil whenever it thinks it necessary to achieve justice". *A Company Re* (1985) BCLC 333 at 337-338. But such broad statement was disapproved by the Court of Appeal in *Adams v. Cape Industries plc* (1990) BCLC 479 at 513 : (1990) Ch 433 at 536. In *Yukong Line Ltd. v. Rendsburg Investments* (1998) 2 BCLC 485 : (1998) 4 All ER 82 (QBD) the case of *The Tjaskemolen* (1997) 2 Lloyd's Rep 465 was cited [at p. 500] in support of the proposition that when it can be established that assets have been deliberately transferred out of a company by its *alter ego* to his own use in order to defeat potential claims against the company, the court may pierce the corporate veil and treat him as liable for the liabilities of the company. In *Tjaskemolen* case a ship was sought to be released from arrest for arrears on the ground that at the time of the arrest it had already been sold by the company in arrears to another company in the same group, but the court found the transaction to be a sham because it was never intended that the supposed buyer should pay a full price to the supposed seller. This case was found to be not an analogy to the facts of the *Yukong* case. The court said [at p 502 of (1998) 2 BCLC 485] : "It is one thing to hold that a purported transfer to be ineffective, and another to hold the would-be transferee liable to the plaintiff in damages for the antecedent wrongs of the would be transferee."

According to a decision of the Supreme Court, corporate veil can be lifted so as to expose any persons to liability who have committed a fraud upon the public from their sheltered position. In this case a large number of persons were decieved by a company in a scheme of booking plots-flats which was operated with utter dishonesty and fraud towards persons coming into the scheme. Persons playing such frauds, though in the name of a company, can be held personally liable. *Delhi Development Authority v. Skipper Construction Co. P. Ltd.*, (1997) 89 Com Cases 362 (SC). The fact that they have been punished for contempt of court does not absolve them from liability.

The principle is of general application. It is not confined to the Companies Act or any taxing measure. Lifting can be resorted to in all cases depending upon (a) the relevant statutory or other provisions; (b) the object sought to be achieved; (c) the impugned conduct; (d) the involvement of public interest and (e) the interest of the affected parties. *Bijay Kumar Agarwal v. Ratan Lal Bagaria,* AIR 1999 Cal 106.

Lifting corporate veil—statutory provisions

The Act itself provides for circumstances when corporate veil will be lifted and the individual members/directors will be made liable for certain transactions. The statutory provisions are as follows:

Reduction of membership below statutory minimum (Section 45).—This section provides that if the number of member of a company is reduced below 7 in the case of a public company or below 2 in the case of a private company and the company continues to carry on the business for more than 6 months, while the number is so reduced, every person who knows this fact and is a member of the company is severally liable for the debts of the company contracted during that time.

Improper use of name (Section 147).—Under sub-section (4) of this section, an officer of a company who signs any bill of exchange, hundi, promissory note, cheque wherein the name of the company is not mentioned in the prescribed manner, such officer can be held personally liable to the holder of the bill of exchange, hundi, etc. unless it is duly paid by the company.

Liability for fraudulent conduct of business (Section 542).—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 the creditors of the company or any other person or for any

fraudulent purpose, the persons who were knowingly parties to the carrying on of the 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.

American law

In *United States v. Milwaukee Refrigerator Transit Company,* (1905) 142 F, edn. 247, SANBORN J of the U.S. Supreme Court held as follows: "Where the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud or defend crime, the law will disregard the corporate entity and treat it as an association of persons."

Shareholders cannot ask for lifting veil for their purposes

The premises of a shop were allotted on a licence to the individual licencee. She set up a wholly-owned private company and transferred the premises to that company without Government consent. She could not save herself from the resulting consequences of the illegality by saying that she and her company were virtually one and the same person. The shareholders of a company cannot ask that the corporate veil be lifted to see the oneness between them and their company. *Premlata Bhatia v. Union of India,* (2004) 58 CL 217 (Delhi).

Piercing the veil in liquidation proceedings

The Official Liquidator of a company in winding up found the books of another concern, a trust, being kept and maintained in the company's office. It was found that they were separate entities formed under different enactments and were treated separately for tax and accounting. Though the company had not invested in the trust, large amounts of the trust funds were being used by the company in its business at no interest. The Liquidator claimed the assets of the trust as really those of the company. It was held that the doctrine of lifting the veil could not be invoked here to declare that the assets of one legal entity were those of the other as veils are torn mainly in cases of control rather than of ownership (Further in this case there was no diversion of business, no parent-subsidiary relationship, or agency business, no motive or fraud, no clubbing of profits). *Official Liquidator v. E.N. Vasudevan,* 1979 Tax LR NOC 178 (Ker).

Piercing the veil in tax matters

In *CIT v. Sri Meenakshi Mills Ltd.,* AIR 1967 SC 819, a branch each of the three assessee mills (respondents) and a branch of a bank (in which substantial number of shares were held by the assessee mills and a director who occupied special position both in the assessee companies and the bank) were established in a Native State (Pudukottai) outside the taxable territory of the British India with the intention of helping financial operations of the assessee-mills and the director, who was the moving figure both in the bank and the assessee-mills, and evading tax. The Court held that the Income-tax authorities were entitled to pierce the veil of corporate entity and to look at the reality of the transaction to examine whether the corporate entity was being used for tax evasion. In this case, a separate corporate entity was brought into existence outside the taxable territory with the ulterior motive of evading the tax obligation by the assessee mills. The Supreme Court observed at page 616:

"It is true that from the juristic point of view, the company is a legal personality entirely distinct from its members and the company is capable of enjoying rights and being subjected to duties which are not the same as those enjoyed or borne by its members. But in certain exceptional cases the court is entitled to lift the veil of corporate entity and to pay regard to the economic realities behind the legal facade. For example, the court has power to disregard the corporate entity if it is used for tax evasion or to circumvent tax obligation. For instance, in *Apthorpe v. Peter Schoenhofen Brewing Co.,* (1899) 4 TC 41 (CA), the Income-tax Commissioners had found as a fact that all the property of the New York company, except its land, had been transferred to an English company, and that the New York company had only been kept in being to hold the land, since aliens were not allowed to do so under New York law. All but three of the New York company's shares were held by the English company, and as the Commissioners also found, if the business was technically that of the New York company, the latter was merely the agent of the English company. In the light of these findings, the Court of Appeal, despite the argument based on *Salomon's* case, (1897) AC 22, held that the New York business was that of the English company which was liable for English Income-Tax accordingly. In another case, *Firestone Tyre and Rubber Co. v. Lewellin,* (1957) 1 WLR 464 : (1958) 33 ITR 741, an American company had an arrangement with its distributors in the continent of Europe whereby they obtained supplies from the English manufacturers, its wholly owned subsidiary. The English company credited the American with the price received after

deducting the costs *plus* 5 per cent. It was conceded that the subsidiary was a separate legal entity and not a mere emanation of the American parent and that it was selling its own goods as principal and not its parent's goods as agent. Nevertheless, these sales were a means whereby the American company carried on its European business and it was held that the substance of the arrangement was that the American company traded in England through the agency of its subsidiary."

In *Juggi Lal Kamalapat v. CIT,* AIR 1969 SC 932, a company promoted by the assessee firm prematurely terminated the managing agency contract with the firm and assigned the managing agency to another company in which the partners of the assessee firm held controlling shares. The same partners continued to conduct the managing agency business of the (managed) company but as directors of the newly formed managing agency company. The assessee firm sought to avoid tax on the amount of compensation received for loss of office by claiming that it was capital gain. It was found that the termination of the contract of managing agency with the firm was a colourable transaction, the payment of compensation was collusive and the partners of the firm continued to run and enjoy the benefit of managing agency as shareholders and directors of the newly formed company. It was a collusive device practised by the managed company and the assessee firm for the purpose of evading income-tax both in the hands of the payer and of the payee. Thus, in this case, the whole transaction was a sham one and was stage-managed merely with a view to evade income-tax. The court did not, therefore, accept the plea that managing agency company was a separate legal entity different from the assessee firm and observed that in a matter of this description the Income-tax authorities were entitled to pierce the veil of the corporate entity and look at the reality of the transaction.

Likewise a sale by one company to another having same shareholders and former company owning all shares in the latter could not escape the separate legal entity concept and the transaction was held taxable under the Income-tax Act. *CIT v. Associates Clothiers Ltd.,* AIR 1963 Cal 629. Similarly, a transfer of property of a firm to a company was held to be a sale although the partners of the firm and the shareholders of the company were identical. *John Foster & Sons v. IRC,* (1894) 1 QB 516.

Again it was pointed out in *McDowell & Co. Ltd. v. Commercial Tax Officer,* (1985) 154 ITR 148 at p. 161 : (1985) 2 Comp LJ 131 (SC): "It is up to the court to take stock to determine the nature of the new and sophisticated legal devices to avoid tax and consider whether the situation created by the devices could be related to the existing legislation with the aid of 'emerging' techniques of interpretation as was done in *Ramsey (WT) Ltd. v. IRC,* (1981) 1 All ER 865 (HL); *Burmah Oil,* (1982) Simon's Tax Cases 30 and *Dawson's* case, (1984) 1 All ER 530 (HL), to expose the devices for what they really are and to refuse to give judicial benefication." The decision in *McDowell's* case was explained and distinguished by the Madras High Court in *Valliappan (MV) v. ITO,* (1988) 170 ITR 238 (Mad), where it was held that a legitimate transaction which did not amount to a dubious device was not hit by the new approach of the English Courts as well as by the judgment of the Supreme Court in *McDowell's* case. See also *CWT v. Arvind Narottam,* (1988) 173 ITR 479 : AIR 1988 SC 1824; *Union of India v. Playworld Electronics Pvt. Ltd.,* (1990) 68 Com Cases 582 : AIR 1990 SC 202, where the court observed: "The court is entitled to lift the mask of corporate entity, if the concept is used for tax evasion, or to circumvent tax obligation, or to perpetuate of fraud. However, tax planning may be legitimate provided it is within the frame-work of the law. Colourable devices cannot be part of tax planning".

Lifting of corporate veil is permissible in tax matters even when there is no statutory authorisation for that purpose. A company transferred its business to another company which was not taxable, but the company was carrying on some other business also which was taxable. The company remained liable to pay the tax applicable to such business. *India Waste Energy Development Ltd. v. Govt. of NCT of Delhi,* (2003) 114 Com Cases 82 (Del).

When there was evasion of excise duty the corporate veil was directed to be lifted to find if the director could be proceeded against and whether he was liable for all duties and penalties. *Santanu Ray v. Union of India,* (1988) 3 Comp LJ 259 (Del). In the absence of specific proof that a company and a partnership firm were units of a Hindu Undivided Family, the benefit of a central excise exemption notification could not be denied

to the company by invoking the doctrine of lifting the corporate veil. *Weldcraft Orissa P. Ltd. v. ACCE,* 1977 Tax LR 1981 (Ori).

In *Western Coalfields Ltd. v. Special Area Development Authority,* AIR 1982 SC 697 the Supreme Court refused to lift the veil in the case of a company whose share capital was owned entirely by the Government of India and held that the company was a distinct legal entity and that the land and buildings owned by the company were the property of the company, not of the Government of India. The company, therefore, could not escape liability to pay property tax under a statute which exempted "buildings and lands owned by or vesting in the Union Government", from such tax.

An attempt of a taxing department to club the income of two companies in a single assessment was challenged in *Deputy Commissioner (CT) v. Cheran Transport Corpn. Ltd.,* (1992) 74 Com Cases 563 (Mad). An engineering company and a transport company about which it was observed that they were once by mistake assessed separately and that their income should have been brought under single assessment, the court could not dispose of the matter on merits and remitted it back to the assessing officer for reconsideration saying that in cases like this it is not enough to find that the two companies were separate legal entities and that it was necessary to examine whether they were truly separate and independent or one was dependent on the other or was a colourable device for avoiding legal obligations. Remitting the matter of two associate companies back to tax authorities, MISHRA J conducted a vast survey of English, American and Indian authorities, cited passages from PENNINGTON'S COMPANY LAW and the six point formula suggested in *Apthorpe v. Peter Schoenhoffen Brewing Co.,* (1899) 4 TC 41 (CA) and adapting them to the facts of the case noted [at p. 571] those six points for the guidance of the taxing authorities:

1. Were the turnovers treated separately for each corporation?
2. Were the persons conducting the business guided by the same head and brain?
3. Were the persons conducting the business of the engineering corporation the same as those conducting the business of the transport corporation?
4. Did the engineering corporation decide for itself what should be done and what capital should be embarked upon the venture?
5. Did the business turnover of the engineering corporation stand separately and independently?
6. Who effectually controlled the engineering corporation?

Where penalties were imposed on an individual who was convicted of cheating the public revenue, the court held that it was entitled to lift the veil of corporate personality if there was evidence that companies had been used to effect a tax fraud. *R. v. Allen, The Times* October 13, 1999. [PALMER IN COMPANY 1999 November].

Piercing the veil in holding-subsidiary relationships

The principle of lifting or piercing the veil is also applicable to cases of holding company—subsidiary relationships, where in spite of their being separate legal personalities, the facts and circumstances show that they are in reality parts of one concern owned by a parent company or a group as a whole. In spite of the rigid rule in *Salomon v. Salomon & Co.* (1897 AC 22) as regards the independent corporate existence of a company, the Courts *esp.* in U.S.A. have developed a body of law governing the instances in which the corporateness of companies as separate legal entities may be disregarded. In *Industrial Development Corpn., Orissa v. Regional Provident Fund Commr.,* (2002) 112 Com Cases 527 (Ori), the court said that a holding company could not be made liable for dues of its subsidiary in respect of the Employees Provident Fund. The holding company, being an independent incorporated entity, was not an employer of its subsidiary's workmen. The subsidiary was not a branch of the holding company. Sums due from the subsidiary could not be recovered from the holding company.

Two public companies holding shares in each other.—Two public companies were holding shares in each other and had common directors. Even so the Supreme Court was of the view that it could not be said that the shareholders of one company had interest in the business of the other company or that the companies had interest in the business of each other. They could not be regarded as "related persons" for the purposes of the Central Excise Act, 1944 [S. 4(4)(c)]. *Collector of Central Excise, Ahmedabad v. I TEC (P.) Ltd.*, (2002) 112 Com Cases 470 (SC).

Non observance of corporate formalities.—Where the corporate formalities are not substantially observed the broader business entity comprising the holding company and subsidiary as a whole may be held liable for the debts and other liabilities of either or both of them under following circumstances:—

(1) Where the business affairs of both the parent company and the subsidiary are intertwined and the business transactions, property, bank and other accounts, employees, management etc. are intermingled.

(2) Where the subsidiary is inadequately financed as a separate business as regards meeting its normal obligations.

(3) Where the parent company and the subsidiary are operating portions of a single business and the financing as well as managerial activities come from the holding or parent company.

(4) Where the enterprises of both the companies are not held out to the public as separate.

(5) Where the subsidiary is being operated in an "unfair" manner *i.e.* not in its interests primarily but in the interest of the parent company so as to funnel its profits to that company.

Failure to delineate between the operation of both may mislead the creditors and the public into believing that they are dealing with the broader corporate entity and not with the subsidiary as a separate business. Where the subsidiary, being under-capitalised, is operating only some portions of the business of the parent or holding company there is no reason why it is not to be treated, so far as the liabilities incurred by it are concerned, as an agent of the parent company.

Position in USA and England.—Such is the law in U.S.A. There is no reason why the same principles should not be applied to the holding company-subsidiary relationships in this country. Where the separate corporate entity of a subsidiary is put to improper use, such as to defraud creditors, or evade the law or escape any legal obligation, there is no reason why for achieving the ends of justice the Courts in this country should not disregard the separate corporate entity of subsidiary and make the larger business entity comprising the parent company, and the subsidiary or subsidiaries as single business entity answerable for all the obligations of the group as a whole. As SANBORN J of the Supreme Court of the USA stated in *United States v. Milwaukee Refrigerator Transit Co.*, (1905) 142F ed 247 (quoted in various American Text Books on Corporate Law). "Where the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud or defend crime, the law will disregard the corporate entity and treat it as an association of persons".

Even in England the application of the rigid rule in *Salomon's* case has been departed from in several cases where the circumstances showed that the company was a mere facade concealing the true facts. GOWER in his book 'PRINCIPLES OF MODERN COMPANY LAW' (1979) 4th Edn. page 133 also observes that tendency of the Courts is to recognise enterprise "entity" rather than "corporate entity" and readily lift the veil where fraud or improper conduct is involved.

Doctrine of Economic Entity.—The modern tendency is that in the case of groups of companies, where there is identity and community of interest between companies in the

group, especially where they are related as holding company and wholly owned subsidiary or subsidiaries, to ignore their separate legal entity and look instead at the economic entity of the whole group. In *DHN Food Distributors Ltd. v. Tower Hamlets London Bourough Council,* (1976) 3 All ER 462 (CA), the DNH was the holding company in a group of three companies. One wholly owned subsidiary owned freehold property which was used in the business of the holding company but did not itself carry on business. The other subsidiary owned the vehicles used in the holding company's business. On the compulsory purchase of the property of the subsidiary company the holding company claimed compensation for disturbance of its business. The Court of Appeal upheld the claim LORD DENNING MR said, at p. 860:

"We all know that in many respects a group of companies are treated together for the purpose of general accounts, balance sheet, and profit and loss account. They are treated as one concern. Professor Gower in *Principles of Modern Company Law,* 3rd ed. (1969), p. 216 says: 'there is evidence of a general tendency to ignore the separate legal entities of various companies within a group, and to look instead at the economic entity of the whole group'. This is especially the case when a parent company owns all the shares of the subsidiaries—so much so that it can control every movement of the subsidiaries. These subsidiaries are bound hand and foot to the parent company and must do just what the parent company says..... This group is virtually the same as a partnership in which all the three companies are partners. They should not be treated separately so as to be defeated on a technical point. They should not be deprived of the compensation which should justly be payable for disturbance. The three companies should, for present purposes, be treated as one, and the parent company, DHN, should be treated as that one. So DHN are entitled to claim compensation accordingly." These observations and the bunch of cases have been cited with **approval** by the Madras High Court in *Hackbridge—Hewittic and Easun Ltd. v. GEC Distribution Transformers Ltd.,* (1992) 74 Com Cases 543, 555 (Mad). (Facts noted below). See also, *Prenn v. Simmonds,* (1971) 3 All ER 237 (HL); *Bird & Co. v. Thomas Cook & Sons Ltd.,* (1937) 2 All ER 227.

But apart from such special circumstances as were present in the above cases there is no general principle that all companies in a group should be regarded as a single economic unit and, on the contrary, each company in a group of companies is an independent entity. Accordingly there was no basis for finding in the present case that the parent English company was present in the United States for litigation purposes because its subsidiary marketing unit was present there. The fact that the subsidiary was set up to reduce the potential tortious liability of the parent company constituted a legitimate use of the corporate form and did not constitute a ground for piercing the corporate veil of the subsidiary so as to treat its activities as being those of the parent. There was no basis for finding that an earlier marketing unit of the parent company which went into liquidation was acting as an agent of the parent company since a substantial part of the business which it carried on was in every sense its own business and, in particular, it had no general authority to enter into contracts binding on the parent *Adams v. Cape Industries plc.,* (1990) BCLC 479 (CA) : (1991) 1 All ER 929: SLADE LJ **approved** the following passage in the judgment of ROBERT GOLF LJ in *Bank of Tokyo Ltd. v. Karoom,* (1986) 3 All ER 468 at 486:

"Counsel suggested beguilingly that it would be technical for us to distinguish between parent and subsidiary company in this context; economically, he said, they were one. But we are concerned not with economics but with law. The distinction between the two is, in law, fundamental and cannot here be bridged."

Apart from the exceptional situations in which the corporate veil is lifted, every company is entitled to organise and conduct its affairs in the expectation that the court will apply the principle of *Salomon v. A. Salomon & Co. Ltd.,* (1897) AC 22 : [1895-9] All ER Rep 33 in the ordinary way.

SLADE LJ further observed: "It is not surprising that in many cases such as *Holdsworth, Scottish Co-operative, Revlon and Commercial Solvents* the wordings of a word particular statute or contract has been held to justify the treatment of parent and subsidiary as one unit, at least for some purposes. The relevant parts of the judgments in the *DHN* case must, we think, likewise be regarded as decisions on the relevant statutory provisions for compensation, even though these parts were somewhat broadly expressed, and the correctness of the decision was doubted by the House of Lords in *Woolfson v. Strathclyde*

Regional Council, 1978 SLT 159 (HL)." Indeed, in the *Woolfson* case the House of Lords upheld a decision of the Scottish Courts delivered shortly after the *DHN* case in which the Scottish Judges had pointedly declined to follow the English case, although the facts were quite similar. In *Bank of Tokyo Ltd. v. Karoon,* (1986) 3 All ER 468 at 486, the Bank of Tokyo Ltd. carried on banking business in London. Its wholly owned subsidiary Bank of Tokyo Trust Co. (BTTC) carried on banking business in New York. A customer of both banks complained that details of his account with BTTC had been disclosed to its parent company without his permission in breach of a bank's duty of confidence, and sued BTTC in New York for damages. The disclosure was made for the purposes of legal proceedings in the High Court in London to which the customer and the parent company were parties. The parent company sought an order restraining the action against its subsidiary. ROBERT GOFF LJ said, at p. 486:

> The distinction between the two is, in law, fundamental and cannot here be bridged.

In *Smith, Stone and Knight Ltd. v. Birmingham Corpn.,* (1939) 4 All ER 116 a holding company was allowed to recover compensation for removal and disturbance of its business although the subsidiary carried on business in the premises. The court regarded them to be economically one unit or one enterprise. A holding company was allowed to sue a contracting party with one of its wholly-owned subsidiaries for causing loss by negligent breach of contract with the subsidiary. The contract was installation of equipment. The equipment installed was defective. The holding company claimed damages for loss of sales and increased operating costs of its subsidiaries. The defendant argued that such losses were not recoverable because a shareholder does not suffer any recoverable loss by diminution in the value of his shareholding. The Court of Appeal upheld the decision of the trial judge in favour of the holding company. The measure of damages was the loss caused to the subsidiary since a £ 1 loss to the subsidiary company as a result of the breach of contract would result in a £ 1 loss to the balance sheet or profit of the holding company. *George Fischer (Great Britain) Ltd. v. Multi Construction Ltd.,* (1995) 1 BCLC 260 (CA). The court referred to its own decision in *Lee v. Sheared,* (1955) 3 All ER 777. Lee was one of the two directors of and held 45% of the shares in a small private company which carried on business as textile merchants. Lee did both buying and selling for the company. He was injured in a car accident caused by the defendant's negligence. The company's business suffered and thus there was less profit for both the directors. It was held that the loss which Lee thus suffered was a head of damages for which he was entitled to claim and was not too remote. The judges agreed that this case was not affected by the rulings in *Foss v. Harbottle* and *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2).*

Subsidiary as agent of holding.—A subsidiary cannot always be considered as the agent of the holding company. *Kodak Ltd. v. Clark,* (1903) 1 KB 505 (CA); *I.R.C. v. Samsom,* (1921) 2 KB 492 (CA). In another case, the court refused to allow the holding company to force its subsidiaries to produce documents for the proceedings. *Lonrho Ltd. v. Shell Petroleum Co. Ltd.,* (1980) 1 WLR 627 : 1982 AC 173 (HL).

In the case of *I.C.I. v. E.C. Commission,* (1972) 11 CMLR 557 the European Court of Justice observed as follows: "The fact that the subsidiary has a distinct legal personality does not suffice to dispose of the possibility that its behaviour might be imputed to the parent company. Such may be the case in particular when the subsidiary, although being a distinct legal personality, does not determine its behaviour on the market in an autonomous manner but essentially carries out the instructions given to it by the parent company. When the subsidiary does not enjoy any real autonomy in the determination of its course of action on the market, the prohibition imposed by Article 85(1) may be considered inapplicable in the relations between the subsidiary and the parent company with which it then forms one economic unit. In view of the unity of the group thus formed, the activities of the subsidiaries may, in certain circumstances, be imputed to the parent company.

"In these circumstances, the formal separation between these companies arising from their distinct legal personality, cannot, for the purposes of application of the competition rules, prevail against the unity of their behaviour on the market. Thus it is indeed the applicant [ICI which was the holding company] which carried out the concerted practice within the Common Market.

"On the whole as regards the holding company—subsidiary relationship, the true legal position is that, though according to the trend of decisions of English Courts (our Supreme Court and High Courts generally follow them), the rule in *Solomon's* case is not departed from except in special circumstances, there is no reason why the courts in this country should worship at its altar and not take to the more vindicable course followed by the Courts in U.S.A., of disregarding the corporate veil, whenever necessary to achieve a just and equitable result".

Unlike in U.S.A., the Courts in England, though they have shown readiness to pierce the veil where in special circumstances a subsidiary company is found to be no more than a facade concealing the true facts, are rather hesitant to pronounce that a parent company is answerable for the debts of its subsidiary. The case of *ICI v. E.C. Commission* (*Supra*) was cited with **approval** in *Hackbridge Hewittic and Easun Ltd. v. GEC Distribution Transformers Ltd.,* (1992) 74 Com Cases 543, 555 (Mad).

The Supreme Court in *State of U.P. v. Renusagar Power Co.,* AIR 1988 SC 1737, 1757, 1758 : (1991) 70 Com Cases 127, observed that the doctrine of lifting the corporate veil is expanding in the context of modern jurisprudence. The court held on facts that the holding company and the subsidiary were to be treated as one and the same because the subsidiary was created to generate and supply energy and power to the holding company in order to enable it to maintain its production commitments to the State and therefore generation of power was considered for the purposes of excise to be the holding company's own source of supply and not supply from a separate company.

In another case the matter was remanded for considering whether an engineering corporation formed by a transport corporation was really an independent economic unit or was a colourable devise for reducing sales tax incidence. *Deputy Commissioner (CT) v. Cheran Transport Corpn. Ltd.,* (1992) 74 Com Cases 563 (Mad).

Group companies when to be regarded single economic unit.—In *Polly Peck International Plc. (In Administration) (No. 3), Re,* (1996) 1 BCLC 428 (Ch D), a company registered in England created a subsidiary in a foreign country to save itself from the listing rules of London Stock Exchange and also for tax advantages. The subsidiary company was used for issuing bonds to group of financing banks and the holding company would give a guarantee for the obligations of the subsidiary. The money thus collected was "on loaned" to the holding company. The loan bonds also provided that in certain circumstances the holding company would be substituted in the place of the subsidiary. The holding company went into administration. A scheme was prepared under which the creditors were to be paid in the same manner as if the company had gone into notional liquidation. The financing banks lodged their claims in respect of the loans to subsidiaries for which the company had given guarantees. The subsidiary company also lodged its claims in respect of the same transaction because it had "on loaned" whole amount to the holding company. The financing banks contended that the holding company and its subsidiary were one economic unit, the holding company using the subsidiary as a device for raising loans and therefore such a subsidiary would have no claim in the insolvency of its holding company. This would involve double proof. The court came to the conclusion that even if double proofs were involved the holding company and its subsidiary could not be regarded as one and the same entity. All companies in a group are separate legal entities and have to be so regarded unless there are compelling circumstances to make a departure from the *Saloman* principle. The court said that even if in certain circumstances the court may go behind the veil to examine the real substance of the transaction, it would still be looking at legal substance and not the economic substance.

In *Welsh Development Agency v. Export Finance Co. Ltd.*, (1992) BCLC 148 at 185 : 1992 BCC 270 STAUGHTON LJ said (in the context of deciding whether a commercial document effected a sale or a charge): 'The problem is not made any easier by the variety of language that has been used: substance, truth, reality, genuine are good words; disguise, cloak, mask, colourable device, label, form, artificial, sham, stratagem and pretence are "bad names", to adopt the phrase quoted by DIXON J in *Palette Shoes Pty. Ltd. v. Krohn*, (1937) 58 CLR 1 at 28. It is necessary to discover, if one can, the ideas which these words are intended to convey. One can start from the position that statute law in this country, when it enacts rules to be applied to particular transactions, is in general referring to the legal nature of a transaction and not to its economic effect. As ROBERT GOFF LJ put it in *Bank of Tokyo Ltd. v. Karoon*, (1986) 3 All ER 468 at 486, we are concerned not with economics but with law.

An important aspect is that whereas natural persons do not (since the abolition of slavery and the passing of the Married Women's Property Acts) own the persons or property of other human beings, commercial companies do have owners. Their shareholders have an economic interest in their commercial success. Although the shareholders do not own their company's assets, a wrong to the company (if uncompensated) may cause them economic loss. But in general the shareholders will have no direct right of action in respect of such loss (see *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)*, (1982) 1 All ER 354 at 367.

There are of course many cases in which it has been held, on the facts, that a company has acted as an agent or nominee, either for its principal shareholder or for some other party, (for instance *Canada Rice Mills Ltd. v. R.*, (1939) 3 All ER 991 and *Firestone Tyre and Rubber Co. Ltd. v. Lewellin (Inspector of Taxes)*, (1957) 1 All ER 561. But neither agency nor nomineeship—nor, still less, sham or something akin to sham—is to be inferred simply because a subsidiary company has a small paid-up capital and has a Board of Directors all or most of whom are also directors or senior executives of its holding company.

The arguments for considering a closely-integrated group of companies as a single economic unit were fully considered (principally in the context of corporate presence as founding jurisdiction) in *Adams v. Cape Industries plc.*, (1991) 1 All ER 929 at 965. The Court of Appeal stated that, save in cases which turn on the wording of particular statutes or contracts, the court is not free to disregard the principle of *Saloman v. Salomon* merely because it considers that justice so requires (1990) BCLC 479 at 513. The Supreme Court of Ireland has lent support to the consistent application of the *Salomon* principle in the context of a group of companies—*Allied Irish Coal v. Powell Duffryn International Fuels* [1998] 2 IR 519.

Grant of exclusive know how by subsidiary.—The Madras High Court in its decision in *Hackbridge Hewittic and Easun Ltd. v. GEC Distribution Transformers Ltd.*, (1992) 74 Com Cases 543, 557 (Mad) observed that whether a covenant of providing exclusive knowhow to a company would be breached if the providing company became the subsidiary of another company and which other company had another subsidiary in the same line of business, would depend upon whether the companies in the same group had independent existence as manufacturing units or whether they were merely marketing devices. Where after piercing the veil and removing the smoke-screen it is found that their activities stand apart and that the subsidiaries have not been functioning with the directing mind and the will of the holding company then it cannot be said that one subsidiary's manufacturing process is the process of the holding company, or that of another subsidiary of the same holding company. The matter came before the Court for adjudication of the question whether royality payable for exclusive use of know-how would cease to be payable when the company providing the know-how became the subsidiary of another company and that other company had another subsidiary in the same line of business in India and therefore the chances of that subsidiary receiving the benefit of knowledge could not be ruled out.

Diluting holding company's shareholding.—In *Freewheel (India) Ltd. v. Dr. Veda Mitra,* AIR 1969 Del 258 : (1969) 1 Comp LJ 138 a fifty-two per cent subsidiary company proposed to issue further capital which, following s. 81, was offered to the existing holders of equity shares. The holding company requested the court that its subsidiary should be restrained from going ahead with the issue as it would deprive its parent of their controlling interest and would also depreciate the value of its shares.

Refusing the injunction prayed for, KAPUR J said: "Here the parent holds only a nominal majority in the share capital of the subsidiary. With the meagre majority alone I am not prepared to hold, even if it were possible to do so for such a purpose, that the subsidiary company has lost its identity as a separate legal entity." *Id.* at 143 at Comp LJ. The court further said: A subsidiary company may, however, lose its separate identity to a certain extent in two cases. Firstly, the Legislature may brush aside the legal forms and require the companies in a group to present a joint picture. Thus, sections 212-214 contain provisions "designed primarily to give better information of the accounts and financial position of the group as a whole to the creditors, shareholders and public". *Id.* at 142 of Comp LJ. Secondly, the court may, on facts of a case, refuse to grant a subsidiary company an independent status. "It may not be possible to put in a straitjacket of judicial definition as to when the subsidiary company can really be treated as a branch, or an agent, or a trustee of the holding company. Circumstances such as the profits of the subsidiary company being treated as those of the parent company, the control and conduct of business of the subsidiary company resting completely in the nominees of the holding company... may indicate that in fact the subsidiary company is only a branch of the holding company."

Lifting the veil of small scale industry.—Where small scale industries were given certain exemptions only when the company owning an industry was not controlled by any group of persons or companies, it was held that it was permissible to lift the veil of the company to see whether it was the subsidiary of another company and, therefore, not entitled to the proposed exemptions. *Inalsa Ltd. v. Union of India,* (1996) 87 Com Cases 599 (Delhi).

Liability of holding company for insolvent subsidiary.—English company law possesses some curious features, which may generate various results. A parent company may spawn a number of subsidiary companies, all controlled directly or indirectly by the shareholders of the parent company. If one of the subsidiary companies turns out to be the runt of the litter and declines into insolvency to the dismay of its creditors, the parent company and the other subsidiary companies may prosper to the joy of the shareholders without any liability for the debts of the insolvent subsidiary. It is not surprising that when a subsidiary collapses, the unsecured creditors wish the finances of the company and its relationship with other members of the group to be narrowly examined, to ensure that no assets of the subsidiary company have leaked away; that no liabilities of the subsidiary company ought to be laid at the door of the other members of the group and that no indemnity from or right of action against any other company, or against any individual is by some mischief overlooked. The anxiety of the creditors will be increased where, as in the present case, all the assets of the subsidiary company are claimed by another member of the group in the right of a debentureholder. *Southard & Co. Ltd., Re,* (1979) 3 All ER 556 at 565 (CA).

In *Kleinwort Benson Ltd. v. Malaysia Mining Corporation Bhd.,* (1989) 1 WLR 379 CA the principle of non liability was applied even where the holding company had given a comfort letter to a creditor of the subsidiary. In *Reed v. Nova Securities,* (1985) 1 WLR 193 (HL). LORD TEMPLEMAN observed that the theoritical independent existence of every corporation enables a group of companies to escape liability at common law for the losses of an insolvent member of the group.

Corporate veil is normally lifted in cases of holding-subsidiary relationship with a view to making the holding company liable for the commitments of its subsidiary unless it has guaranteed the subsidiary's debts. But the question of piercing the veil was held to be

irrelevant where the holding company was sought to be held liable for the debt of a company in which the holding company's subsidiary had a substantial interest, particularly when it had not accepted any such liability. *SAE (India) Ltd. v. EID Parry (India) Ltd.*, (1998) 18 SCL 481 (Mad).

Transfer of assets to holding company under normal restructuring.—The plantiffs had taken the lease of a public house from a subsidiary company. They filed a case against the subsidiary claiming for damages for misrepresentation and breach of warranty. There was restructuring of the group of companies because of property losses. The subsidiary's assets were transferred at book-value to other companies in the group as a part of normal restructuruing. The plaintiffs applied for leave to substitute the parent company as its defendant in place of the subsidiary. The court did not permit it. Going by the most practical consideration the court said that the parent company was only a shareholder of the subsidiary company. Normally a person suing a company cannot seek permission that the principal shareholder should be substituted for the subsidiary only because the asset which was under lease was transferred to the parent company particularly when the subsidiary company was kept alive and not dissolved. *Ord v. Belhaven Pubs Ltd.*, (1998) 2 BCLC 447 : 1998 BCC 607 (CA). The court also rejected the proposition that the corporate veil could be pierced whenever it was necessary to do so in the interests of justice. The court said that such a proposition would be too broad. *Ibid,* citing SLADE L.J. in *Adams v. Cape Industries plc.*, (1990) Ch 333 (CA).

Piercing the veil in associated companies

For the purpose of considering whether a company which was a member of a group of companies was employing less or more than 20 persons, the employees of the whole group were not permitted to be taken into account. The court said that the Parliament was aware of the group phenomenon when it enacted the piece of legislation and could have drafted the statute in such away as to address itself to the matter but chose not to do so. *Colt Group Ltd. v. Couchman* [2000] I.C.R. 327. [PALMER IN COMPANY, October 20, year 2000].

Where, the companies are kept alive as separate legal entities for good commercial or historical reasons in order to keep the company's name fully alive and in order to maintain the loyalty of employees for example, and also probably to avoid redundancy and other problems, the court may see no reason why the veil should be pierced. On the facts the court said that it does indeed seem perhaps to be unseemly that the three companies working in the same geographical location of a dock should be allowed to unveil themselves in order to try to avoid the effect of the Dock Labour Scheme. *National Dock Labour Board v. Pinn & Wheeler Ltd.*, (1989) BCLC 647 (QBD).

Evasion of personal and statutory obligations

The court may disregard the separate existence of the company where it appears that the company was incorporated for evading contractual and statutory obligations. An observation about such cases is to be found in GOWER, PRINCIPLES OF MODERN COMPANY LAW, 126-127 (Fourth Edn. 1979): "Thus in *Gilford Motor Co. v. Horne,* (1933) Ch 935 (CA), Horne a former employee of the plaintiffs covenanted not to solicit its customers. He attempted to evade this obligation by forming a company which undertook the soliciting. An injunction was granted against both him and the company (notwithstanding that it was not a party to the covenant). The company was described in the judgment as "a device, a strategam", at 956, 961 and a "mere cloak or sham" *Ibid* p. 969. In *Jones v. Lipman,* (1962) 1 All ER 442; the defendant attempted to avoid completing the sale of his house to the plaintiff by conveying it to a company formed for the purpose. In ordering both the defendant and his company specifically to perform the contract with the plaintiff, RUSSEL J. described the company as "a devise and a sham, a mask which he holds before his face in an attempt to avoid recognition by the eye of equity." (*Ibid* p. 836, See also *Einhorn v. Westmount Investments Ltd.*, (1969) DLR (3d) 71, *Sask* Q.B. (*Affd.*), 73 WWR 161, (CA)) where it was held that directors who prevented a company from performing its contract by diverting its assets to an associated company might be liable for commit-

ting a breach of contract. They could not escape liability by "clothing themselves in a corporate veil of their own spinning". Per DISBERG J. at p. 75. But *Cf. Airlines Airspares Ltd. v. Handley Page Ltd.*, (1970) 1 All ER 29 : (1970) 40 Com Cases 604 where, there being no fraud or impropriety, a receiver and manager was held entitled to frustrate a contract by the company which was not binding on the company and which could not be specifically enforced against the company by causing the subject matter of the contract to be transferred to its subsidiary company incorporated for the purpose. In *Wallersteiner v. Moir*, (1974) 3 All ER 217, in which the Court of Appeal refused to allow Dr. Wallersteiner to put in a defence out of time to claims for misfeasance as a director in relation to breaches of the Companies Act, LORD DENNING M.R. was prepared to treat various companies through which he had operated as if they were "just the puppets of Dr. Wallensteiner". "He controlled their every movement. Each danced to his bidding. He pulled the strings. No one else got within reach of them. Transformed into legal language, they were his agents to do as he commanded. He was the principal behind them. I am of the opinion that the court should pull aside the corporate veil and treat these concerns as being his creatures for whose doings he should be, and is, responsible." (*Ibid*, p. 1013).

The properties of two companies were ordered to be attached in order to do justice to persons whom the promoter of the companies had duped by allotting a floor to more than one person. *Delhi Development Authority v. Skipper Construction Co. P. Ltd.*, (1997) 89 Com Cases 362 (SC).

An example of evasion of legal obligations by resorting to the devise of incorporation came before the Supreme Court in *Workmen of Associated Rubber Industry Ltd. v. Associated Rubber Industry Ltd.*, (1986) 59 Com Cases 134 (SC). A parent company incorporated a subsidiary company and transferred to it some of its investments and securities only for the purpose of splitting the profits into two hands and thereby to reduce the incidence of the obligation to pay bonus. The Supreme Court held that the separate existence of the new company would be disregarded for the purpose of working out the amount of bonus payable to workers. CHINAPPA REDDY J. noted that avoidance of welfare legislation is as common as avoidance of taxation and the approach in considering problems arising out of such avoidance has necessarily to be the same. He said (at p. 138) "If we look at the facts of the case, what do we find? A new company is created wholly owned by the principal company with no assets of its own except those transferred to it by the principal company, with no business or income of its own except receiving dividends from shares transferred to it by the principal company and serving no purpose whatsoever except to reduce the gross profits of the principal company." See further, *Chitra Kumar Basu v. Property Development Trust Ltd.*, (1988) 93 CWN 725 (Cal), where the doctrine of lifting the veil was not permitted to be resorted to so as to bring about evasion of welfare legislation. The court said that companies cannot be permitted to put off their veil at pleasure.

Where two persons who were the joint owners of leasehold rights in land attempted to circumvent an injunction against alienation of certain rights by transferring the leasehold rights to a private limited company (of which they alone were the shareholders and directors) which alienated the rights. The court held that the corporate veil was being used as a cloak to wilfully disobey the Court's orders. The court held that in these circumstances it was imperative to punish improper conduct by lifting the corporate veil. *Jyoti Ltd. v. Kanwaljit Kaur Bhasin*, (1987) 62 Com Cases 626 (Del).

Where by reason of an enactment an individual had to be put under prohibition order from carrying on business, the court said that since the applicant was in Hong Kong merely in his corporate capacity as a director, there was insufficient ground for making the prohibition order under the relevant section, on the basis that he was carrying on a business in Hong Kong. The phrase "carries on business" in that section referred to the individual's own personal business and did not extend to a business he was associated or concerned with, such as that of a company of which he was a shareholder or director. The legislature must be taken to have been aware of the fundamental distinction between a corporate personality and the personality of the individual corporators. *Abadi v. Chase Bank International*, (1987) LRC (Comm) 801 at 806 (Hong Kong HC).

Circumstances in which company's receipt is to be treated as individual's receipt

In *Trustor AB v. Smallbone,* (2001) 2 BCLC 436 : [2001] 1 WLR 1177 (Ch. D) the court had to consider whether in a given circumstance something received by a company could be considered to have been received by an individual inside the company. Explaining the approach to be adopted in such circumstances the court said : "The court is entitled to pierce the corporate veil and recognise the receipt of a company as that of the individual in control of it if the company has been used as a device or façade to conceal the true facts, thereby avoiding or concealing any liability of that individual. It is however, insufficient that the company has been involved in some impropriety, not linked to the use of the company structure to avoid or conceal that liability. Nor can the court pierce the corporate veil merely on the grounds that it was necessary to do so in the interests of justice and no unconnected third party was involved. The court **applied** *Adams v. Cape Industries plc.,* (1991) 1 All ER 929 and *Ord v. Belheaven Pubs Ltd.,* (1998) 2 BCLC 447 and **did not follow** *Re A Company,* (1985) BCLC 333 (337).

Using corporate structure for hiding criminal activities.—Where the defendant used the corporate structure as a device or facade to conceal his criminal activities (evasion of customs and excise duties effected through the company), the court could lift the corporate veil and treat the assets of the company as the realisable property of the shareholder. On the facts, there was a *prima facie* case that the defendants controlled the two companies, that the companies had been used for the fraudulent evasion of excise duty on a large scale, that the defendants regarded the companies as carrying on a family business and that they had benefited from companies' cash in substantial amounts; and further no useful purpose would have been served by involving the companies in the criminal proceedings. In all the circumstances it was therefore appropriate to lift the corporate veil and treat the stock in the companies' warehouses and the companies' motor vehicles as realisable property held by the defendants. The court said that the excise department is not to be criticised for not charging the companies. The more complex commercial activities become, the more vital it is for prosecuting authorities to be selective in whom and what they charge, so that issues can be presented in as clear and short a form as possible. In the present case, it seemed that no useful purpose would have been served by introducing into criminal proceedings the additional complexities as to the corporate mind and will which charging the companies would have involved. *H. and Others (Restraint Order: Realisable Property), Re,* (1996) 2 BCLC 500 at 511, 512 (CA).

Adverting to the general principle, the court observed as follows [at p. 511]: "As to the law, the general principle remains that which was enunciated in *Salomon v. Salomon & Co.,* (1897) AC 22, namely that a company duly formed and registered is a separate legal entity and must be treated like any other independent person with its own rights and liabilities distinct from those of its shareholders. But a succession of cases throughout the twentieth century show, as DANCKWERTS LJ said in *Merchandise Transport Ltd. v. British Transport Commission,* (1961) 3 All ER 495 at 518: '....where the character of a company, or the nature of the persons who control it, is a relevant feature the court will go behind the mere status of the company as a legal entity, and will consider who are the persons as shareholders or even as agents who direct and control the activities of a company which is incapable of doing anything without human assistance.' In *Adams v. Cape Industries plc.,* (1990) BCLC 479 at 517-518 SLADE LJ, giving the judgment of the Court of Appeal cited this passage and added: 'The correctness of this statement has not been disputed.' The court also assumed it to be the correct proposition that 'the court will lift the corporate veil where a defendant by the device of a corporate structure attempts to evade (i) limitations imposed on his conduct by law.....' (See (1990) BCLC 479 at 519).

Where companies are used as a vehicle for carrying on criminal activities, the Customs and Excise can lift the veil of corporate personality and use its power under section 77 of the Criminal Justice Act 1988 (British) to charge the assets of such individual shareholders directly who are responsible for that kind of use of the corporate form. *Hare v. Customs and Excise Commissioners,* The Times, February 29, 1996 (UK).

Using company for diversion of business opportunities

A director of a public company had a personally-held private company. He used his *alter ego* company for marketing the saleable materials of his public company. It was considered appropriate to lift the corporate veil of the marketing company to see whether it was a pretence for his own purposes. It was an offshore company wholly owned and controlled by the director. Everything that the company did was done on his directions alone. The company had no staff and was incapable of carrying on business. It was in substance the director's offshore bank account held in a nominee name. The company was simply a creature company used by the director to receive profits for which he was accountable to his public company. In such circumstances it was right for the court to regard it simply as the *alter ego* through which he enjoyed the profit which he earned in breach of his fiduciary duty. *Gencor ACP Ltd. v. Dalby,* (2000) 2 BCLC 734 (Ch D). The court **applied** the ruling in *H (restraint : realisable property Re,* (1996) 2 BCLC 500.

Company's lease and tenancy.—Where a lease of premises was granted to a company to be used for residence and personal use of directors for the purposes of the company, it was held that the purposes of the company would not mean in this context commercial purposes. Hence the lease was usable only for residential purposes. *Keshav Kumar Swarup v. Flowmore P. Ltd.,* (1996) 85 Com Cases 210 (SC). Where a company was the tenant of a property under a lease deed which prohibited sub-letting, it was held that merely because the company was attempting to induct new shareholders would not amount to an attempt to sublet the premises to the new shareholders under the cover of corporate veil. *Naga Brahma Trust v. Translanka Air Travels P. Ltd.,* (1997) 88 Com Cases 136 (Mad) : *Electrical Cable Development Assn. v. Arun Commercial Premises Coop. Housing Society Ltd.,* (1998) 94 Com Cases 53 (SC) : (1998) 4 Comp LJ 385 : (1998) 31 CLA 135. In considering the worthiness of a subsidiary company for the purposes of assignment of a lease, information about the way in which the holding company provided finance to the subsidiary may be taken into account. *Greater London Property Ltd., Re,* (1959) 1 WLR 503.

Where a suit was filed to evict a tenant from the company's property because the company had a personal need of the premises, it was held that the company's need was something different from the directors' need of occupying the premises and, therefore, the claim was not maintainable. *K.M. Basheer v. Lona Chackola,* (2003) 115 Com Cases 127 : (2004) 50 SCC 19 (Ker).

Matters of property and contracts.—In matters of property and contract the courts should surely be most hesitant to lift the veil in response to superficial considerations of "common sense" or "reality" or fairness. Those who adopt the corporate form should surely be expected to take the rough with the smooth. This was the point emphasised in *Tate Access Floors Inc. v. Boswell,* (1991) Ch 512, by Browne-Wilkinson V-C, at p. 531: "If people choose to conduct their affairs through the medium of corporations, they are taking advantage of the fact that in law those corporations are separate legal entities, whose property and actions are in law not the property or actions of their incorporators or controlling shareholders. In my judgment controlling shareholders cannot, for all purposes beneficial to them, insist on the separate identity of such corporations but then be heard to say the contrary when discovery is sought against such corporations." It is the company as a separate person that owns the company's property and enters into contracts and incurs debts. This has been affirmed in many different contexts. *Gas Lighting Improvement Co. Ltd. v. Commissioners of Inland Revenue* [1923] AC 723.

A company was the owner of a farm. Its principal shareholder disposed off company's property by means of a 'will' in favour of one of his sons. It was held that the 'will' was inoperative on the company's property and the shares of the principal shareholder would go to his two sons under intestate succession. *Lewis's willtrusts Re* (1985) 1 WLR 102.

Government company as separate legal entity.—Even if the entire share capital of the company is subscribed by the Union Government, it cannot be said that the Union Government owns its properties. *Bharat Aluminium Co. Ltd. v. Area Development Authority,* (1981) 51 Com Cases 184, 194 (MP). The Government and the company are two distinct entities *Lajpat Rai Mago v. Governor of Haryana,* (1971) 41 Com Cases 693, 706 (P & H). In *Western Coalfields Ltd. v. Special Area Development,* AIR 1982 SC 697, it was held that the property of the Government company did not belong to the Government of India. The company, therefore, could not escape liability to pay property tax under a statute which exempted "buildings and lands owned by or vesting in the Union Government", from such tax.

In reference to a Government company it has been held that whatever may be the extent, depth and sweep of control of the Government over its companies in connection with their affairs and functioning, the company remains a separate legal person as much distinct from the Government as any private sector company is distinct from its shareholders. It cannot be said that the company is carrying on its business under the authority of the Government. It carries on its business independently of the Government. Hence, the Central Government, by reason merely of its majority shareholding, cannot be regarded as the appropriate Government within the meaning of s. 2 (1)(*a*) in order to ask it to make reference of an industrial dispute under s. 10 of the Industrial Disputes Act. *Cotton Corporation of India Ltd. v. G. C. Odusumeth,* (1999) 225 CL-228 (Kar).

The assets of a Government company were held to be not exempt from payment of non-agricultural assessment under an A.P. legislation. The exemption given to the property of the Union from State taxation would not apply to a separate and distinct entity though created by the State. *Electronics Corpn. of India Ltd. v. Secretary, Revenue Department, Govt. of A.P.,* (1999) 97 Com Cases 470 : (1999) 3 Comp LJ 353 AIR 1999 SC 1734 (SC).

§ For further detail see notes under section 617.

Solicitor's duty to company—principal shareholder

A solicitor owes a duty to exercise all reasonable care and skill in connection with the client's business, the company in this case. The precise nature of this duty depends upon, *inter alia*, the experience of his client and therefore an incorporated client is entitled to expect a solicitor to take this into consideration in giving advice. The defendant was negligent in omitting to remind the plaintiffs of the need to initiate an application to obtain the protection of a new tenancy legislation. The court also added that a solicitor may owe a contractual duty of care not only to the company which retained him but also to the principal shareholder in the company where it is clear that the shareholder is also relying on the client to protect his interests. Alternatively, a duty may arise in tort where it is foreseeable that the share-holder would be injured by negligent advice given to the company. *R. P. Howard Ltd. S. Richard Alan Witchell v. Woodman Mathews & Co.,* 1983 BCLC 117 (QBD). In a case of the same kind before the New Zealand Court of Appeal, the shareholders of the company suffered loss because of professional negligence. It was held that the right of the shareholders, if it existed, was not affected by the fact that the company had chosen to settle its claim with the professionals. The plaintiff shareholders had based their claim on a direct duty owed to them personally by the defendants, irrespective of any duty which might have been owed to the company. If was a cause of action which was outside the settlement and therefore the plaintiffs were entitled to pursue it. *Christensen v. Scott,* (1996) 1 NZLR 273 (CA).

Loss of value in shareholding

The decision in *Johnson v. Gore Wood & Co.,* (1999) BCC 474 : (1999) 1 Lloyds Rep PN 91 (CA) was **affirmed** over this point by the House of Lords in *Johnson v. Gore Wood & Co.,* (2001) 1 BCLC 313 (HL) : (2001) 2 WLR 72 : (2001) 1 All ER 481, namely that a shareholder cannot complain of decline in share value where it is due to primary losses suffered by the company. The principle laid down in this case was **applied**

in *Giles v. Rhind,* (2001) 2 BCLC 582 (Ch. D). The company filed a claim against a former director-shareholder for compensation for breach of contractual duty of confidence by diverting an important contract which was the mainstay of the company to his new business. The company went into liquidation and discontinued the action. A shareholder brought his own proceedings against the director for his own losses consisting of deprivation of remuneration, reduction in value of shares and share conversion rights. It was held that the shareholder's losses merely reflected the company's losses. They were all linked with the loss to the company caused by the diversion of the contract. The court said that if the company had recovered in full for the director's breach of duty, the claiming shareholder would have been compensated in full for his losses. Accordingly, none of the heads of loss set out in the claimant's schedule was recoverable.

The principle of this case was **applied** by the Court of Appeal in *Day v. Cook,* (2002) 1 BCLC 1 (CA). A shareholder sued his solicitor for loss of investments made by his companies. The loss in value of share-holding was not recoverable beause it was reflective of merely the company's loss. The case was referred back to the trial court to record findings as to whether the loan was made by the claimant or the company and whether the defendant solicitor owed duties to the compay as well as the claimant and whether the claimant had suffered any loss separate from that of the company. Summarising the applicable principle, the court said that where there is a breach of duty to both the shareholder and the defendant and the loss which the shareholder suffered was merely a reflection of the company's loss, the shareholder could not recover. This principle does not apply where the duty is owed only to the shareholder so that the company has no claim or where the loss which the shareholder suffered is additional to or different from that suffered by the company.

In *Gerber Garment Technology Inc. v. Lectra Systems Ltd.,* [1997] RPC 443 at 471, HOBHOUSE LJ observed if the company chooses not to exercise its remedy, the loss to the shareholder is caused by the company's decision not to pursue its remedy and not by the defendant's wrongdoing. By a parity of reasoning, the same applies if the company settles for less than it might have done. Shareholders (and creditors) who are aggrieved by the liqidator's proposals are not without a remedy; they can have recourse to the Companies Court, or sue the liquidator for negligence.

It will thus be seen from the speeches in *Johnson v. Gore Wood & Co.,* (2001) 1 BCLC 313 : (2001) 2 WLR 72 (HL) that where there is a breach of duty to both the shareholder and the company and the loss which the shareholder suffers is merely a reflection of the company's loss there is now a clear rule that the shareholder cannot recover. That follows from the graphic example of the shareholder who is led to part with the key to the company's money box and the theft of the company's money from that box. It is not simply the case that double recovery will not be allowed, so that, for instance if the company's claim is not pursued or there is some defence to the company's claim, the shareholder can pursue his claim. The company's claim, if it exists, will always trump that of the shareholder. Acordingly the court has no discretion. The claim cannot be entertained. The English rule is therefore different from the position in New Zealand : see *Christensen v. Scott,* (1996) 1 NZLR 273. Even in the case of owner-managed companies, there is no discretion. Thus the position in English law differs from the position in the majority of States in the USA, where the courts exercise limited discretion to allow direct recovery by shareholders of closely-held corporations where the court is satisified that : 'to do so will not (i) unfairly expose the corporation or the defendants to a multiplicity of actions, (ii) materially prejudice the interests of creditors of the corporation, or (iii) interfere with a fair distribution of the recovery among all interested persons.' (PRINCIPLES OF CORPORATE GOVERNANCE, American Law Institute (1994) para 7.01).

Lawyers who failed to properly advise a company on the impact of the substantial property transactions rules in section 320 of the Companies Act, 1985 [British] were held to be negligent and liable for the resulting loss to the company. The chairman-director of the company was interested in the company whose shares were acquired. This required

approval of members. No approval was taken as the solicitors failed to advise the Board of Directors as to the need for approval. The members did not approve. This caused complications and resulting losses. *British Racing Drivers Club Ltd. v. Hexstall Erskine & Co.*, (1997) 1 BCLC 162 (Ch D).

Insurance broker's duty to principal shareholder.—In the case of a company composed of a man and his wife as the only shareholders and directors, the company's insurance broker took out a policy of insurance against theft in the name of one of them instead of in the company's name. The shareholder in whose name the policy was effected was not able to recover anything from the insurer when the most of the company's stock was stolen because he had no insurable interest in the company's property. Subsequently he sued the insurer and the broker seeking from the broker damages for: (i) the loss of the indemnity under the insurance policy, (ii) loss of their salaries as directors of the company, the company having ceased to trade as a result of losing its stock, (iii) anxiety, depression and inconvenience, and (iv) the costs of the abortive proceedings against the insurer. It was held that the brokers were under no duty of care to the shareholders for the kind of damages listed above. If such a duty were to exist it would pierce the corporate veil and have wide-ranging consequences including giving rise to claims for double recovery. *Verderame v. Commercial Union Insurance Co. plc.*, 1992 BCLC 793 (CA). In this respect the court **followed** the principles laid down in *Caparo Industries plc. v. Dickman*, 1990 BCLC 273 : (1990) 1 All ER 568 (HL).

No personal liability of managing director for company's dues.—A managing director was held to be not personally liable for unpaid dues to workers. *Rundan Singh v. Moga Transport Co. P. Ltd.*, (1987) 62 Com Cases 600 (P&H). Similarly, proceedings against managing director's and shareholders' personal assets for recovery of sales tax dues of the company were held to be void. *Surinder Nath Khosla v. Excise and Taxation Commissioner, Punjab*, (1995) 4 Comp LJ 343 (Punj).

Holding subsidiary and employees.—In *Dimbleby & Sons Ltd. v. National Union of Journalists*, (1984) 1 All ER 751 at 758 (HL) the House of Lords refused to disregard the separate personality of two wholly owned subsidiaries of a holding company. Both subsidiaries had the same directors and the same management. One subsidiary was an employer. It was party to a trade dispute with the National Union of Journalists. The House of Lords held that the other subsidiary was not a party to the trade dispute for the purposes of the Employment Act, 1980, s. 17(3), so that in the circumstances the union could not have immunity from an action for damages in tort in respect of industrial action taken against that other subsidiary. LORD DIPLOCK observed that the next sub-section of the Act, s. 17(4), specifically dealt with a situation in which action was taken against a company in the same group as a party to a dispute so that Parliament must be presumed to have definitely excluded such a situation from s. 17(3).

In *Manley Inc. v. Fallis*, (1977) 38 CPR (2d) 74, (Ontario Court of Appeal) the defendant had set up a business in competition with the plaintiff company. This would have been a breach of duty if he had been a senior employee of the plaintiff company but in fact he was a senior employee of a wholly owned subsidiary of the plaintiff and the business was not in competition with the subsidiary's business. The court said, at p. 76: "In our view, it would undermine the requirement of fidelity to allow an employee to successfully argue that, while his activities may have injured the parent company of his employer, they did not in fact injure his employer. This is a case where the court is not precluded from lifting the corporate veil, and, in effect, regarding the closely related respondent companies as essentially one trading enterprise, in the interests of the affiliated companies, in a circumstance where the refusal to do so would allow the appellant to escape the consequences of his breach of a fiduciary trust."

On an application for stay of proceedings, the House of Lords held in favour of South African miners who were employed by the local subsidiary of a U.K. multinational and who wished to sue the parent company for compensation for industrial diseases contacted

whilst working for the subsidiary. There was likely to be greater access to justice under English law, it being the more appropriate trial forum for a complex group action. *Lubbe v. Cape plc.* (2000) 1 W.L.R. 1545.

The lifting of corporate veil or piercing the corporate veil is permissible if public interest requires. This is also subject to considerations of permissibility as per the statute. If the company uses other concern; a firm, society or association, only to facilitate evasion of legal obligation like payment of direct or indirect taxes or denial of statutory benefits to workmen, the Court has to disregard the separate legal entity of the company. In such an event the question before the Court is one of company law, and the corporate personality of the company is of secondary importance. The important test is whether the method adopted for evasion of legal obligations would subvert public interest. In instant case it is no doubt true that undisputedly the subsidiary company was supplying its produce to the holding company. That, however, was not crucial. To start with, subsidiary was incorporated as private limited company and later converted as public limited company and made a subsidiary of the holding company. Board of Directors were different. The employees of the subsidiary company were recruited by the subsidiary company and there was no employment policy in the holding company to take employees from subsidiary either by transfer or deputation from the holding company. The stray cases where some employees were sent to holding company was not crucial unless there was any common cadre of service in both holding company and subsidiary company. Nothing was pleaded or proved to show that the holding company stood guarantee for any of the loans raised by the subsidiary company. It was not denied that the secured creditors of the holding company and subsidiary company were different. Financial investments were different. Therefore, while deciding the question whether workmen and employees of the subsidiary company could be treated as such of holding company, it was not permissible to pierce the corporate veil of subsidiary company. The subsidiary company had developed sickness, and was ordered to be wound up. Its holding company was also ordered to be wound up. The workers of the subsidiary, realising that it had no assets, staked their claim under s. 529A before the official liquidator of the holding company. Their claim was not allowed. They could not be treated as workers of the holding company. See at p. 561. *Krishi Foundry Employees Union v. Krishi Engines Ltd.*, 2003 CLC 547, 556-557 : (2003) 43 SCL 353 (AP).

S. 35. Conclusiveness of certificate of incorporation.—A certificate of incorporation given by the Registrar in respect of any association shall be conclusive evidence that all the requirements of this Act have been complied with in respect of registration and matters precedent and incidental thereto, and that the association is a company authorised to be registered and duly registered under this Act.

NOTES

Eng. Act, 1948 : Sec. 15
Eng. Act, 1985 : Sec. 13(7)

Previous Act : Sec. 24(1)

Conclusiveness of certificate

The certificate of incorporation is conclusive evidence that the requirements of the Act as regards registration have been complied with and prevents the reopening of matters prior and contemporaneous thereto, and it places the existence of the company as a legal person beyond doubt. This is so even if all the signatures of the subscribers are forged or all the signatories are minors. Such is the effect of the certificate of incorporation.

In *Peel's* case, (1867) LR 2 Ch 674, the memorandum of association had, after signature and before registration, been altered, without the privity of the signatories, so materially that, in the words of LORD CAIRNS, "the alteration entirely neutralised and annihi-

lated the original execution and registration of the document." The company was, however, registered, and the Registrar gave his certificate of incorporation; subsequently the question arose whether this certificate was conclusive, since according to the section as then in force, the memorandum before registration had to be subscribed "by seven or more persons associated for any lawful purpose," whereas here the signatures had been entirely annihilated. Nevertheless, it was held that the Registrar's certificate of incorporation *was* conclusive. LORD CAIRNS said at p. 681: "The certificate of incorporation .... is not merely a *prima facie* answer, but a conclusive answer to any such objection .... when once the certificate of incorporation is given, nothing is to be inquired into as the regularity of the prior proceedings." LORD CHELMSFORD L.C., dealing with the same point in *Oakes v. Turquand,* (1867) LR 2 HL 325, 354 said: "I think that the certificate prevents all recurrence to prior matters essential to registration, amongst which is the subscription of a memorandum of association by seven persons, and that it is conclusive in this case that all previous requisitions have been complied with." See also *Re, National Debenture, etc., Corporation,* (1891) 2 Ch 505 (CA). (Certificate would not be conclusive if the memorandum was inadequately signed); *Re, Northumberland, etc., Banking Co.,* (1886) 2 De G & J 357 (not conclusive if the company was one not authorised to be registered under the Act).

Even if the two signatures to a memorandum were written by one person, or were forged, the certificate would be conclusive that the company was duly incorporated. So, too, if the signatories were all minors, the certificate would still be conclusive. *Hammond v. Prentice Bros.,* (1920) 1 Ch 201 and *Bowman v. Secular Society Ltd.,* (1917) AC 406, 438 (HL).

Where only two adult persons signed the memorandum, one of them signing as a guardian of the other five members who were all minors at the time, in *Moosa Goolam Arif v. Ebrahim Goolam Ariff,* ILR (1913) 40 Cal 1 (PC), Lord MACNAGHTEN said: "Their Lordships will assume that the conditions of registration prescribed by the Indian Companies Act were not duly complied with; that there were no seven subscribers to the memorandum and that the Registrar ought not to have granted the certificate. But the certificate is conclusive for all purposes." "In England the question whether the Registrar's certificate is conclusive was decided so far back as 1867 by Lord CAIRNS.... In *Peel's* case, (1867) 2 Ch App 674, after signature and before registration a proposed memorandum of association had been altered without the authority of the subscribers so materially that the alteration entirely neutralised and annihilated the original execution and signature of the document. The company, however, was registered and the Registrar gave his certificate of incorporation. It was objected that the memorandum of association had not been signed by seven or indeed by any subscribers and that the provisions of the Act had not been complied with. To that proposition Lord CAIRNS assented. But "the certificate of incorporation", he said, "is not merely a *prima facie* answer, but a conclusive answer to such objection... When once the certificate of incorporation is given nothing is to be inquired into as to the regularity of the prior proceedings." The observations of Lord CHELMSFORD in *Oakes v. Turquand,* (1867) LR 2 HL 325 are to the same effect. "I think", said his Lordship, "the certificate prevents all recurrence to prior matters essential to registration... and that it is conclusive... that all previous requisites have been complied with. The same view was reiterated in *Ramasundari Roy v. Syamendra Lal Roy,* ILR (1947) 2 Cal 1. All these authorities were reviewed and **followed** by the Bombay High Court in *Salim Akbarali Nanji v. Union of India,* (2003) 43 Com Cases 141 (Bom). The court had to examine the validity of registration of a Cooperative Banking Society as a joint stock banking company under Part IX of the Act. Cooperative Societies are among the organisations mentioned in that Part as entitled to be registered. The court said that the definition of a "body corporate" in the Act is not applicable for the purposes of registration under Part IX. The society had fulfilled all the requirements of registration under Part IX of the Act.

The same view was reiterated in *Ramasundari Roy v. Syamendra Lal Roy,* ILR (1947) 2 Cal 1. All these authorities were reviewed and **followed** by the Bombay High Court in *Salim Akbarali Nanji v. Union of India,* (2003) 43 Com Cases 141 (Bom). The court had to examine the validity of registration of a Cooperative Banking Society as a Joint Stock Banking Company under Part IX of the Act. Cooperative Societies are among the organisations mentioned in that Part as entitled to be registered. The court said that the definition of a "body corporate" in the Act is not applicable for the purposes of registration under Part IX. The society had fulfilled all the requirements of registration under Part IX of the Act.

Further, a subscriber cannot, after the issue of the certificate of registration repudiate his subscription on the ground of misrepresentation, mistake or fraud, although he retains any claims for damages against the person who misled him. *Re, Metal Constituents Ltd., Lord Lurgan's* case, (1902) 1 Ch 707. The certificate is also conclusive that the company came into existence on the date of the certificate, and it must be taken to have been in existence during the whole of that day. *Jubilee Cotton Mills Ltd. v. Lewis,* (1924) AC 958. Where a company registered in England stated in its memorandum that the place of its registered office was a locality in Scotland and the English Registrar overlooked this discrepancy and granted his certificate of incorporation, HARMAN J held that the certificate was conclusive evidence that the company was an English company and that consequently the English court had jurisdiction to wind it up. *Re, Baby Moon (United Kingdom) Ltd.,* 1985 PCC 103.

The certificate is conclusive but not exclusive evidence. A fact to which the certificate refers can also be proved by evidence other than the production of the certificate.

The question whether the formation of the company is null and void cannot arise, in view of the conclusiveness of the certificate of incorporation once it is issued. *Cf.* PALMER'S COMPANY LAW 2193 (25th Edn., 1992, para 2.1302).

The certificate is conclusive evidence of the fact that each subscriber to the memorandum wrote opposite his name the number of shares he took. *Collector of Moradabad v. Equity Insurance Co. Ltd.,* (1948) 18 Com Cases 309, 314 : AIR 1948 Oudh 197.

Explaining the object of the section in the Australian case of *Stephenson & Son Ltd. v. Gillanders, Arbhuthnot & Co.,* (1931) 45 CLR 476 (High Court of Australia) E VATT J observed as follows : "[The] effect of formal incorporation is not regarded by the legislature as empowering the registrar to ignore compliance with the Act; but the legislature wishes to ensure that after the new legal entity has been brought into existence by the formal act of a State functionary, it will not be necessary for persons dealing with the company to ascertain at their peril whether the various statutory requirements have been complied with ... It is not so much a power given to the registrar by the legislature, as a protection given to the public who may be dealing with the company because of the assumption that the registrar will be careful in the matter...."

Power of review where object is unlawful

In view of the conclusiveness of the certificate of incorporation, irregularities relating to procedural matters pertaining to registration, such as defects in the signatures of subscribers or other prescribed particulars will not affect the legal status or personality of the company, though it does not prevent an aggrieved person prosecuting a claim against persons responsible for getting the company incorporated.

The conclusiveness of the certificate, however, does not warrant that all the objects of the company as set out in its memorandum are legal, nor will it validate what may otherwise be illegal objects. If a company with illegal objects happens to be registered, the effect will be that while the existence of the certificate precludes its corporate status from being questioned, the company is forbidden to carry on any business in furtherance of its illegal objects. *Bowman v. Secular Society,* 1917 AC 406 : nor does the fact of the Registrar issuing the certificate bind the Central Government, who may institute proceedings to

cancel the registration as improperly or erroneously allowed. *Cf. Bowman v. Secular Society Ltd.* (*Supra*); *Cotman v. Brougham*, 1918 AC 514. "In the same case LORD FINLAY L.C. said: "It was argued before us that the society could not have been properly incorporated if its objects were illegal, and that, as the certificate is conclusive to show that the company is one authorised to be registered and duly registered, it follows that it cannot for any purpose be contended that the objects are illegal. In my opinion this argument is an attempt to extend the effect of these enactments beyond their fair meaning and manifest object. What the legislature was dealing with was validity of the incorporation, and it is for the purpose of incorporation, and for this purpose only, that the certificate is made conclusive." It follows that even if all or some of the objects of the company are illegal but it has obtained registration, the certificate of incorporation prevents any doubt from being raised as to the legal *persona* of the company but it does not validate the illegal objects. A company pursuing illegal objects should not be registered, and the Registrar is entitled to refuse an application for registration.

Where the object of a company is unlawful, it has been held that the certificate of registration is not conclusive for this purpose, *Performing Right Society Ltd. v. London Theatre of Varieties*, (1922) 2 KB 433.

For illustrative cases on the conclusiveness of the certificate of incorporation. See *Peel's* case, (1867) 2 Ch App 674; *Oakes v. Turquand*, (1867) LR 2 HL 325; *Official Receiver and Liquidator of Jubilee Cotton Mills Ltd. v. Lewis*, (1924) AC 958; *T.V. Krishna v. Andhra Prabha (P.) Ltd.*, AIR 1960 AP 123. (For detail see Notes under section 33, *ante*).

Impeaching incorporation

Whether a company, once incorporated can be removed from the register and disincorporated was considered in *Princess of Reuss v. Bos*, (1871) LR 5 HL 176. Here the question arose as to the regularity of the constitution of a company called: "The General Company for the Promotion of Land Credit Limited." All the subscribers to the memorandum of this company were foreigners, and there was no intention to carry on business in England. The company was ordered to be wound up. Neither of these circumstances affected its validity, but the articles of association contained provisions contrary to the English Act of 1862, under which the company was incorporated, and LORD HATHERLEY LC, said at p. 193. "All we have to ask ourselves is this, my Lords. Has this company come into existence—has it been born? If it has been born, I think .... it ought to be, as speedily as possible, extinguished .... The question is therefore simple whether it has been created. If created, there is no power given in this Act of Parliament, nor in any other Act of Parliament that I am aware of, by which, through any result of a formal application, like an application for *scire facias* to repeal a charter, the company can be got rid of, unless by winding-up." The Act does not bind the Crown, and, accordingly, where a company has been registered for an illegal object, proceedings could be instituted by the Attorney-General (in Scotland, the LORD ADVOCATE) to have the registration cancelled. *Bowman v. Secular Society Ltd.*, (1917) AC 406, 439, 440 (HL) **followed** in *R. v. Registrar of Companies, ex parte, Attorney General*, (1991) BCLC 476.

A company could not be declared a nullity because it had been formed for the purpose of defrauding the creditors of one of its founding shareholders. *Marleasing SA v. La Commercial International de Alimentacion SA*, (1992) 1 CMLR 305 (Court of Justice of European Communities).

Provision as to voting and non-voting shares.—The articles of a company provided that non-voting shares would become voting shares if the family shareholding fell below 40% of issued voting shares for 14 consecutive days. An amendment was made to this provision for the purpose of calculating family shareholding. The amendment removed voting shares beneficially owned by family members for purpose of calculating family shareholding. The effect of this amendment had to be worked out with great difficulty

after interpolating words which ought to have been there. *Folkes Group plc. v. Alexander,* (2002) 2 BCLC 254 (Ch D).

Registration under Part IX

A Co-operative bank registered as a society under Multi-State Cooperative Societies Act, 1985, was registered as a joint stock banking company under Part IX of the Act. Requisite approvals for converting it into a banking company were obtained from the RBI and Central Government. The requirements of registration under Part IX were also satisfied. The registration was held to be valid and not allowed to be questioned by a writ petition. The court found that the banking company had rendered good public service since its conversion. The court said : joint stock banking company had made remarkable growth and progress after its conversion in 1995 and certain equities had also been created in favour of third parties after conversion and in view thereof it would not be proper, just and equitable to grant any reliefs to the petitioner. Allowing the writ petition would result in greater harm to the shareholders, borrowers and employees of respondent No. 11, the converted company. *Salim Akbarali Nanji v. Union of India,* (2003) 113 Com Cases 141 (Bom).

Effect of incorporation—Company a legal person but not a citizen

A company is a legal person just as much as an individual and has to be regarded in the same way as an individual as regards existence, powers, liabilities etc., except of matters where, being only a metaphysical entity, it cannot satisfy the conditions of physical existence that may be required. Thus it has been held by the Supreme Court that only an individual can be a citizen while a company cannot be. See *State Trading Corporation v. C.T.O.,* (1963) 33 Com Cases 1057 : AIR 1963 SC 1811.

§ For a full view of this aspect of incorporation, see Notes under section 34, *ante.*

S. 36. Effect of memorandum and articles.—(1) Subject to the provisions of this Act, the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed by the company and by each member, and contained covenants on its and his part to observe all the provisions of the Memorandum and of the Articles.

(2) All money payable by any member to the company under the memorandum or articles shall be a debt due from him to the company.

NOTES

Eng. Act, 1948 : Sec. 20
Eng. Act, 1985 : Sec. 14

Previous Act : Sec. 21

Scope of section

As between the memorandum and articles, the memorandum is the dominant instrument. It limits and restricts the company's powers to specified objects and to things incidental or conducive thereto. It effectually controls the articles in the sense that anything in the articles inconsistent with any provision in the Memorandum is invalid. "The memorandum is, as it were, the area beyond which the action of the company cannot go; inside that area, the shareholders may make such regulations for their own government as they think fit". *Ashbury Rly. Carriage Etc. Co. v. Riche,* (1875) LR 7 HL 653 (671). The articles may, however, be referred to explain any ambiguity appearing in the memorandum. *Guinness v. Land Corporation of Ireland,* (1882) 22 Ch D 349; or to supplement it upon any matter as to which it is silent. *Angostura Bitters Ltd. v. Kerr,* 1933 AC 550 : (1934) 4 Com Cases 1 (PC); *Re, Gilmour (Duncan) & Co. Ltd. v. Inman,* (1952) 2 All ER 871 (Ch D). For a view of full details as to memorandum, see under s. 13 and for articles under s. 26.

How far articles are a contract

Binding upon members.—The provisions of the articles are binding upon the company in reference to its members, and *vice versa*, to the same extent as if they have signed a contract to be bound by the articles. The legal analysis of the nature of an association of persons has always been in terms of a contract between the association and the associates. Even in the case of an unincorporated association the bond of union was regarded as contractual. *Conservative & Unionist Central Office v. Burrell,* (1982) 1 WLR 522, 525. There are dicta to the same effect in the case of incorporated associations also. *Tavarone Mining Co., Re,* (1873) LR 8 Ch App 956, 960 where MELLISH LJ said at p. 960: "...the articles of association are simply a contract as between the shareholders *inter se* in respect of their rights as shareholders. They are the deed of partnership by which the shareholders agree *inter se.* " Articles of association state the arrangement between the members. They are an agreement *inter socios* [that is, between partners]. *Eley v. Positive Security Life Assurance Co. Ltd.,* (1876) 2 Ex D 88, 89, 90.

One great example is *Borland's Trustees v. Steel Bros. & Co.,* (1901) 1 Ch 279. The articles of the company provided that in the event of a member's bankruptcy his shares would be sold by the directors at a fair price not exceeding the par value. Borland became bankrupt and his trustee tried to sell the shares without referring to the company by contending that he was not bound by the articles. He was however held bound to abide by the provisions of the company's articles. See also, *Amraoti Electric Supply Co. v. Chandak,* (1954) 24 Com Cases 465, 470 (Nag); *Imperial Hydropathic Co. v. Hampson,* (1883) 23 Ch D 1.

Statements and representations in a prospectus cannot be at variance with the provisions of the company's memorandum and articles. The later will prevail over the former. Shares are applied for and purchased and membership is granted on the basis of the company's memorandum and articles. The prospectus cannot be used for changing the terms of the contract already settled between the members and the company through the memorandum and articles. *Globe Motors Ltd. v. Globe United Engg. and Foundry Ltd.,* (1975) 45 Com Cases 429, 434 (Del).

A company was created under a joint venture agreement between certain partners. One of the terms of the agreement was that members of the company would not transfer their shares without the consent in writing of other members. This term of the agreement was not incorporated into the articles of association of the company. One member transferred his shares to another member. The transfer was held to be valid. There was no restriction against it in the company's articles. These members were free to exercise their right of transfer under the Companies Act. *Crompton Greaves Ltd. v. Sky Cell Communication Ltd.,* (2002) 39 SCL 704 (Mad—DB).

A share holders agreement which was incorporated in the company's articles provided that on the termination of an executive director's employment 'for whatever reasons', his shares would be transferred to the subscribers in accordance with company's articles. The employment was unlawfully terminated. The affected director contended that the clause in this article was not to apply to an unlawful termination. Rejecting his contention the court said that the words 'for whatever reasons' encompassed both lawful and unlawful termination of the employment and further that the provision for compulsory transfer after termination being a part of the company's articles, was binding on the share holders. *Holt v. Faulks,* (2001) BCC 50 (Ch. D).

Binding upon company.—A member can enforce articles against the company. In *Wood v. Odessa Water Works,* (1889) 42 Ch D 636 the directors proposed to pay dividend in kind by issuing debentures. The articles provided for payment of dividend. The court held that payment means payment in cash and therefore the company could be compelled to pay dividend in terms of the articles.

A member in his capacity as a member can enforce rights given to him by the articles such as impeaching any irregular forefeiture. *Johnson v. Lyttle's Iron Agency,* (1877) 5

Ch D 687; or prevent the company by an injunction restraining it from contravening the articles, *Wood v. Odessa Water Works Co., (Supra)*; insist upon the strict observance of the articles according to their construction. *Oak Bank Oil Co. v. Crum,* (1882) 8 App Cas 65.

Contractual terms by implication.—It has been held that there is no scope to imply in the contract so created between the company and its members any terms giving rise to contractual liability to members for the way in which the company carried out its functions. The defendant company in this case was created by all the race course owners with the object of protecting their interests. The articles conferred upon the directors the power of sole control of the business and affairs of the company. They could exercise all such powers and do all such acts and things as could be exercised or done by the company, and without prejudice to their general powers, the directors had power to make and impose rules and regulations for the administration and government of the company and for carrying its objects into effect. The company created a group for dealing with bidders for terrestrial rights. The owner of seven largest race course was appointed as the chairman of the group. The group recommended to the members that they should deal only with one of the two media bidders. A member refused to follow this advice. He alleged that the bidding was faulted because the chairman wanted consultancy arrangement with one of them which was declined and, therefore, that bidder was excluded. The member asked for an inquiry. The report of the inquiry panel constituted by the company was that the conduct of the chairman was inappropriate and unauthorised but it did not have any effect upon the outcome of the bidding process.

The member did not accept those conclusions and sought disclosure of appendices to the panel's report which included correspondence with bidders and transcripts of interviews with witnesses. The company refused to allow unrestricted access to that material on the ground that it was confidential. The member brought an action against the company alleging that the inquiry process was inadequate and seeking damages to compensate it for unnecessary legal and other expenses incurred as the result of the company failing properly to discharge its duties in conducting the inquiry.

The contention was that this duty was there on the part of the company by way of a necessary implication of contractual relationship in terms of the articles. The court did not agree that there could be any such contractual terms by implication. The court said : "The implied terms contended for by the claimant would be powers and duties of the company which, like all other such powers and duties, would be subject to the control of the directors and would be exercisable by the directors in the company's name in accordance with the articles. The effect of the implied terms therefore would be to make the company contractually liable to its members for the way in which it carried out its functions, while continuing to delegate control of those functions to the board. The directors would therefore be directly accountable to the members through the company for their actions, they would be subject to direct attack whenever a significant dispute arose between members about the running of the company, and they could be restrained at the suit of members from exercising the powers of the company in a particular way. If that were the case, the implied terms, far from being consistent with the terms of the articles, would in fact completely alter the express basis on which it was agreed that the company should be governed." *Towcester Racecourse Co. Ltd. v. Racecourse Association Ltd.,* (2003) 1 BCLC 260 (Ch D).

Articles how far binding between members.—The contractual force given to the articles by the section is limited to matters arising out of the company relationship of the members as members and does not extend to matters outside the company relationship *Khusiram Benarsi Lal v. Hanutmal Boid,* (1949) 53 CWN 505. The intention of the memorandum and articles is to fix the rights and liabilities of the shareholder as such in the company and not to restrain him in his individual capacity, *Bisgood v. Henderson's Transvaal Estate,* (1908) 1 Ch 743 (CA); *Baring-Gould v. Sharpington Combined Pick and Shovel Syndicate,* (1899) 2 Ch 80 (CA). The established position is that "the articles

constitute a contract between each member and the company and there is no contract in terms between the individual members of a company but the articles do not, any the less, in my opinion, regulate their rights *inter se*. Such rights can only be enforced by or against a member through the company or through the liquidator representing the company; but I think that no member has, as between himself and another member, any rights beyond that which the contract with the company gives." Per LORD HERSCHELL in *Welton v. Saffrey,* 1897 AC 299 (at 315) and this **followed** in *Re, Greene v. Greene,* (1949) 1 All ER 167 (Ch D). This view is however not quite accepted in a decision of the Bombay High Court, according to which the contractual application of the articles is not confined to the company relationship only but may extend to other dealings between members *inter se*. The entire case-law both English and Indian is reviewed, and discussed therein. See *Shiv Omkar Maheshwari v. Bansidhar Jagannath,* (1957) 27 Com Cases 255 : AIR 1956 Bom 459. *First National Bank Ltd. v. Seth Sant Lal,* AIR 1958 Punj 328 : (1958) 28 Com Cases 402. See also *Salmon v. Quinn & Axtens Ltd.,* (1909) 1 Ch 311, 318. In *Rayfield v. Hands,* (1958) 2 All ER 194 : (1958) 28 Com Cases 460 (Ch D), it was held that a provision in the articles that the directors would take at a fair value shares offered to them by members would be binding on them; and that the right could be enforced against them without joining the company as a party to the action.

The European Court of Justice found it easy to regard as a natural consequence of the nature of the company as an institution that its articles "known to European lawyers as its Statutes" form a contract between the members and the company as a separate person and between the members themselves. *Powell Duffryn Plc. v. Petereit* [Case C-214/89 [1994]-1 CEC 293].

Equality of treatment of members in the matter of allotment.—The articles of a company vested in the directors a power to allot, deal with or dispose of the company's shares 'on such terms as they think proper.' The company offered to the public for sale certain shares, half of which were made available to the existing shareholders on a preferential basis except those resident in the United States or Canada or their agents who were excluded from the offer because of the securities legislation in those countries. Such excluded shareholders commenced an action for damages alleging that the discrimination against them was a breach of the contract of membership as contained in the company's articles to treat all shareholders of the same class equally. The court dismissed the action saying that no term could be implied that the shareholders of the same class were to be treated equally either with respect to a resolution of the Board of Directors or of the shareholders in general meeting. The power of allotment was conferred by the articles on the directors in the widest terms and it was subject to only two implied conditions: (*i*) that the powers would be exercised by the directors in good faith and in the interest of the company, and (*ii*) that it would be exercised fairly as between different shareholders (which did not require that they be treated identically). There was no discrimination against the excluded shareholders because their exclusion was because of a difficulty resulting only from their own personal situation. *Mutual Life Insurance Co. of New York v. Rank Organisation Ltd.,* 1985 BCLC 11 Ch D. Among a large number of cases surveyed in the course of the judgment the court found a remark of LINDLEY MR in *Kerry v. Maori Dream Gold Mines,* (1898) 14 TLR 402 in relation to a complex transaction, that plainly it could not stand because the company had no right to stipulate for an advantage to one set of shareholders against another and that of ASTBURY J in *Fraser and Chalmers Ltd., Re,* (1919) 2 Ch 114 that all the shareholders are entitled to equal treatment unless and to the extent that their rights are modified by the contract under which they hold their shares. But these constraints apply when the company is voluntarily indulging in some discrimination and not, as here, due to external circumstances.

Arbitration Clauses.—In the case of *London Sack and Bag Co. Ltd. v. Dixon & Lupton Ltd.,* (1943) 2 All ER 763 a doubt had been raised as to whether an arbitration clause in the Articles constitutes a written agreement for submission to arbitration under the Arbitration Act. In this case the rules of a trade association, registered under the Compa-

nies Act, provided that all trading disputes between members should be submitted to arbitration. On an action on a trading dispute between two "members" the defendant asked for a stay. The Court of Appeal refused a stay, being not satisfied that there was a valid arbitration agreement. In *Hickman v. Kent or Romney Marsh Sheep Breeders' Association,* (1915) 1 Ch 881 the articles contained a provision for submission of disputes between a member and the company to arbitration. A member who had a dispute was threatened by the company with expulsion. He commenced legal proceedings to prevent the expulsion. The court stayed the proceedings and referred the matter to arbitration.

Where an existing member applied for a few more shares which were not allotted to him and the resulting dispute was referred to arbitration in terms of the company's articles, the company was not allowed to escape from the award by saying that the applicant was not a member in respect of the shares applied for. The court said that it was enough that he was a member otherwise. *Gauba (K.L.) v. Peoples Bank of Northern India Ltd.,* (1934) 4 Com Cases 156 (Lah).

An arbitration clause in the articles would not be binding as to matters not relating to membership of the company. An example is to be found in *Beattie v. Beattie (E. & F.) Ltd.,* (1938) Ch 708. Here, in an action by the plaintiff as a shareholder in a company, against the defendant, as director, alleging that he had made certain payments contrary to the regulations of the company, the defendant applied under the Arbitration Act for a stay and relied upon an arbitration clause in the articles of association, contending that by section 20 of the Companies Act, 1948 [s. 36 of our 1956 Act], this clause had the force of a written agreement to refer. It was held, however, that section 20 did not apply to directors in their capacity as such and so could not be relied on in this cases. The Calcutta High Court in its decision in *Khusi Ram Benarsilal v. Hanutmal Boid,* (1949) 53 CWN 505 held that a member having a dispute with another member under a commercial transaction between them and having no connection with company's business affairs, was not compellable to refer the dispute for arbitration in terms of the company's articles. A provision in a company's articles requiring disputes between the company and others to be referred to arbitration is not invalid merely because it is not under company's seal. *Ganges Sugar Works Ltd. v. Nuri Miah,* AIR 1915 All 234.

An arbitration clause in a company's articles could not be made use of for an order of reference under the Arbitration Act through a court situated in an area to which the Arbitration Act had not been extended *Sundar Mal Lakhu Mal v. Paris Business Corpn. Ltd.,* (1931) 1 Com Cases 141 (Lah).

There were also authorities to the effect that arbitration clauses in a company's articles would be enforceable throughout the courts in India whether or not Arbitration Act had been extended to the particular area in question. *Ruplal Agarwala v. Dhansor Coal Co.,* (1932) 2 Com Cases 217 (Pat); *Behari Lal Madho Prasad v. Sirsa Trading Co. Ltd.,* (1933) 3 Com Cases 1 (Lah—DB); *Attock Oil Company v. Abdul Majid,* (1929) 118 IC 533.

A provision in the company's memorandum and articles to the effect that the Board of directors would be competent to refer disputes to arbitration was held to be enabling provision and not such that the directors could be compelled to use it. There has to be an agreement in writing with the other party to refer a particular matter to arbitration. *Skypark Builders and Distributors v. Kerala Police Housing and Construction Corpn. Ltd.,* (2003) 114 Com Cases 425 (Ker).

§ For further study see JUSTICE RS BACHAWAT – LAW OF ARBITRATION AND CONCILIATION, 180, 181 (4th Edn., 2004).

Reference to arbitration under statutory provisions.—An example of statutory reference is to be seen in the provisions of Section 581 ZO brought in by the Companies (Amendment) Act, 2002 for resolution of disputes between members and producer companies. See Notes under the relevant section.

Arbitration with intervention of Court.—Even when arbitration with the intervention of the Court was possible under the Arbitration Act, 1940 [Not applicable under 1996 Act] the Court would hold that when reference was by the Court the Arbitration Act, 1940 was not applicable and that was so even if one of the parties was a company. *East Bengal Bank Ltd. v. Jogesh Chandra Banerjee,* (1939-40) 44 Cal. W.N. 828 (Cal).

Agreement outside articles.—It has been held by the Bombay High Court that the decision of the Supreme Court in *V.B. Rangaraj v. R. Gopalkrishna,* (1991) 6 CLA 211 is not confined only to a situation in which the right to transfer shares was in question. It is a general principle that effect cannot be given to a shareholders' agreement even in the matters of management unless the agreement has been incorporated in the company's articles of association. *IL & FS Trust Co. Ltd. v. Birla Perucchini Ltd.,* (2003) 52 CLA 35 (Bom). The court further held in this case that where the matters in question were under arbitration, the court would be justified in the exercise of its powers in granting such relief as would be necessary to ensure that pending the arbitration proceedings, the rights of the member (petitioner) in terms of the subscription-cum-shareholders' agreement are not abridged and are duly implemented.

Company-director relationship.—As regards the relationship between the company and its directors, though the articles do not have contractual force they may be evidence of the terms of service of the directors rendering service. See *Re, City Equitable Fire Insurance Co.,* (1925) Ch 407 (pages 520-521). In *New British Iron Co., In re, exp., Backwith,* (1898) 1 Ch 324 (Ch D) liability to pay a director in terms of the company's articles for his services was inferred from conduct. They cannot also be treated as constituting an agreement on the part of a director to take the qualification shares prescribed by the articles. *Re, Wheal Buller Consols,* (1888) 38 Ch D 42; *Bolton (R.) & Co., Re; Salisbury, Jones & Dale's* case (1895) 1 Ch 333.

It is possible to prove an implied contract in terms of the articles of association between the company and its managing director, even though the memorandum and articles are held not to constitute a contract in themselves. *Sardar Gulab Singh v. Punjab Zamindara Bank Ltd.,* (1941) 11 Com Cases 301, 306, 307 : AIR 1947 Lah 47 **affirming** (1940) 10 Com Cases 188, 192 (Lah). If on the basis of articles the directors were employed by the company, the terms of the articles are embodied in and form part of the contract between the company and its directors. *Indian Copper Corporation Ltd. v. CIT,* (1960) 30 Com Cases 200, 204 (Pat).

Where a director sued the company for costs in accordance with a provision in the articles, here is what the court said :

"The articles of association of a company are a statutory contract between a company and its members and are not automatically binding as between a company and its officers as such. However, the articles can be expressly or impliedly incorporated into the contract between the company and a director if the director accepted his appointment 'on the footing of the articles'. Although relatively little might be required to incorporate the articles by implication, there was in fact no evidence as to the basis on which the director in this case had accepted his appointment as a director of the company and there was nothing to suggest that he knew of article 18, or that there might be relevant provisions in the company's constitution, when he accepted his appointment. In those circumstances, where there was a real issue as to the incorporation of the article into any contract between him and the company, the court would confine itself to making such costs order as was appropriate in exercising its discretion under s. 51 of the Supreme Court Act 1981, leaving him to bring any claim under the article separately." *Globalink Telecommunications Ltd. v. Wimbury Ltd.,* (2003) 1 BCLC 145 (QBD).

But although the articles do not constitute a contract between the company and the directors, the directors are duty bound to act in accordance with and be guided by provisions in the articles as their powers are mostly derived from the articles. If they do not act

in conformity with the articles, they may render themselves liable to be proceeded against. (See PALMER'S COMPANY LAW, 24th Edn., 1987 paras 14-17, p. 179).

On the whole, the correct view seems to be that indicated in ***Beattie v. Beattie Ltd.,*** (1938) 3 All ER 214, *viz.*, that the contractual force given to the articles of association is limited to the relationship of members of a company in their capacity as members, and does not extend any further. In *Fertilizers Corporation of India v. Their Workmen,* AIR 1970 SC 867 at 873 the Supreme Court held that where the articles of association gave powers to the President of India to give directions regarding the working of the company, the exercise of the powers of the Board of Directors was, apart from other restrictions, subject to the directions issued by the President from time to time. See also *G. Karunakaran v. State of Kerala,* (1987) 61 Com Cases 334 (Ker).

In HALSBURY also, after a review of all the authorities, the view expressed is as follows: "The Articles constitute a contract between the company and a member in respect of his rights and liabilities as a shareholder; and the company may sue a member and a member may sue a company to enforce and restrain breaches of the regulations contained in the articles dealing with such matters. The purpose of the articles is to define the position of the shareholder, as a shareholder, not to bind him in his capacity as an individual. The articles do not constitute a contract between the company and a member in respect of rights and liabilities which he has in a capacity other than that of member, whether he becomes a member originally or subsequently; and where such rights and liabilities are the subject of a written agreement, the articles will not be imported unless they are referred to." HALSBURY'S LAWS OF ENGLAND, Fourth Edn., Reissue 1996 Vol. 7(1), Para 142]

A service agreement with a director which required for its validity under the articles of association that the remuneration would be fixed by the company in a general meeting and which neither fulfilled this requirement initially nor was subsequently ratified, was held to be determinable summarily. Even otherwise there were grave breaches of fiduciary duty and misfeasance on his part which also entitled the company to dismiss him summarily. His action for wrongful termination was dismissed. *Knopp v. Thane Investments Ltd.,* (2003) 1 BCLC 380 : (2002) EWHC 3139 (QB).

The articles of a producers' co-operative usually carry clauses to the effect that the members will trade only with the company in certain matters. A New Zealand Court has been of the view that such a clause is intimately connected with the very purpose of an incorporated producers' co-operative and therefore the provision deals with the members *qua members. Gore Bros. v. Newbury Dairy Co. Ltd.,* (1919) NZLR 205. But an Australian Court has been of the view that it is not necessary to consider the binding value of such a provision because it is already void as an unreasonable restraint of trade. *Heron v. Port Huon Fruitgrowers Co-operative Assn. Ltd.,* (1922) 30 CLR 315 (Aust). The House of Lords expressed a similar view in *McEllistrim v. Ballymacelligott Co-operative Agricultural & Dairy Society Ltd.,* (1919) AC 548.

These examples show that it is not safe to regulate any other relationship through articles than the simple relationship of company and its members—*qua members.*

§ The principles enunciated here have now become a part of the statute, having been incorporated in section 581ZO, brought in by the Companies (Amendment) Act, 2002 [1 of 2003] (w.e.f. 6-2-2003). For further Notes see under relevant section *post.*

Company and third parties

The memorandum and articles do not constitute a contract between the company and a third party though named therein. *Ramkumar Potdar v. Sholapur Spg. & Wvg. Co. Ltd.,* (1934) 4 Com Cases 481, 487 : AIR 1934 Bom 427; **dissenting** from *T.R. Venkatramana v. Coimbatore Mercantile Bank Ltd.,* (1934) 4 Com Cases 489, 491 : AIR 1924 Mad 126.

The articles do not constitute a contract between the company and any third party. No third party can acquire enforceable right by virtue of the articles. *Eley v. Positive Gov-*

ernment Security Life Assurance Co., (1875) 1 Ex D 20. For instance, a mere provision in the Articles that a certain person shall hold office as solicitor, secretary or wholetime director does not give such person a right to enforce the provision against the company, unless a contractual relationship has been created by offer and acceptance of the office. The articles can only be referred to as evidence of the terms of any agreement between the company and the officer concerned. *Doraisami Iyenger v. United India Life Assurance Co. Ltd.*, AIR 1956 Mad 316. See also *Shanta Shamsher Jung v. Kamani Bros.*, (1959) 29 Com Cases 501 : AIR 1959 Bom 201. Similarly in *Mothey Krishna Rao v. Grandhi Anjaneyalu*, (1953) 23 Com Cases 90 (Mad). The secretary was not allowed to question his removal on the basis of the company's articles. See *London Sack and Bag Co. Ltd. v. Dixon and Lugton Ltd.*, (1943) 2 All ER 763 (CA) as regards the scope of the contractual rights created by the articles.

But where a third party is dealing with the company on matters dealt with in the articles of the company, he will be taken to have contracted with the company on the terms of the memorandum and articles and the articles will in a proper case be incorporated into a contract with a third party. *Mell v. Atlanta*, (1894) 11 TLR 407; *Exparte, Beck*, (1898) 1 Ch 324; *Molineaux v. London, Birmingham & Manchester Insurance Co.*, (1902) 2 KB 589; *Read v. Astoria Garage (Streatham) Ltd.*, (1952) 2 All ER 292; *Royal British Bank v. Turquand*, (1856) 6 E&B 327. In *Ganges Sugar Works Ltd. v. Nuri Miah*, AIR 1915 All 234, it was held that a provision in a company's articles requiring disputes between the company and others to be referred to arbitration is not invalid merely because it is not under the company's seal.

In *Woodlands Ltd. v. Logan*, (1948) NZLR 230, the company's articles provided that in certain circumstances the personal representatives of the company's founder could appoint its managing director, and also define the powers of a managing director. It was held that when the personal representatives exercised the outsider right to appoint a managing director the appointment was valid giving the appointee all the powers of a managing director conferred by the articles. On the other hand, in a Singapore case, *Malayan Banking Ltd. v. Raffles Hotel Ltd.*, (1966) 1 MLJ 206 (Singapore) in which the landlord of a company was given by the company's articles a right to appoint a director: it was held that the appointment was invalid and of no legal effect.

Statutory power of alteration.—Another point to be remembered as regards contractual relationships created by the memorandum and articles is that such relationship is always subject to the provisions of the Act that the memorandum and articles are alterable. This means that the contractual relationships are liable to be altered from time to time according as circumstances may require.

Memorandum, articles and the rule of constructive notice

Members are deemed to be aware of the contents of the memorandum and articles. Other persons who have dealing with the company are also affected with notice of what is contained in them, but are not bound to make further inquiries and may assume that the internal management of the company has been regular and is being carried on in accordance with the memorandum and articles. In a Madras case, the articles required that all documents should be signed by the managing director, secretary and the working director on behalf of the company. A deed of mortgage was executed by the secretary and the working director only and the court held that no claim would lie under such a deed. The court said that the mortgagee should have consulted the articles before the deed was executed. Therefore, even though the mortgagee may have acted in good faith and the money borrowed applied for the purpose of the company, the mortgage was nevertheless invalid. *Kotla Venkataswamy v. Rammurthy*, AIR 1934 Mad 579; *Rajendra Nath Dutta v. Shibendra Nath Mukherjee*, (1982) 52 Com Cases 293 (Cal). See also, *Freeman & Lockyer v. Buckhurst Park Properties (Mangal) Ltd.*, (1964) 1 All ER 630 : (1964) 34 Com Cases 405. However, as stated above, the doctrine of indoor management protects third parties who have acted in good faith. The rule of constructive notice is confined only to the ex-

tent of powers under the memorandum and articles and there is no constructive notice as regards the manner in which the power is exercised. An outsider is entitled to presume that the procedural aspects of a transaction, have indeed been carried out. See *Sree Meenakshi Mills Ltd. v. Callianjee & Sons,* (1935) 5 Com Cases 103 (Mad); *Varkey Sourier v. Keraleeya Banking Co. Ltd.,* (1957) 27 Com Cases 591 (Ker); *Siva Sankara Panicker (C.K.) v. Kerala Financial Corpn. Ltd.,* (1980) 50 Com Cases 817 (Ker).

Persons dealing with incorporated companies or societies are bound to take notice of disabilities imposed on the corporation by the memorandum or other documents of constitution. They run a great risk in not acquainting themselves with such disabilities. Nevertheless they are entitled to assume that the director or other persons exercising authority on behalf of the company are duly functioning and performing their duties in accordance with the internal regulations of the constitution; *e.g.* the attestation in the pass book by the cashier-cum-clerk was held valid though the bye-laws prescribed the secretary or authorised officer. *K.S. Ramachandran v. Registrar of Co-op. Societies, Madras,* (1963) 33 Com Cases 807, 810 (Mad). But a third party who is aware that articles have not been followed cannot rely upon the presumption that internal rules would have been followed. *National Coal Co. Ltd. v. Gyan Ranjan Bhattacharya,* AIR 1927 Cal 299. Where a bank had been intimated as to the authorised signatories, any loss caused to the bank by unauthorised persons representing the company cannot be fastened on the company. *Bank of Montreal v. Dominion Gresham Guarantee & Casualty Co.,* AIR 1930 PC 278.

A further aspect of constructive notice is that persons dealing with the company are taken not only to have read those documents but also to have understood them according to their proper meaning. Persons dealing are presumed to have understood not only the company's powers but also its officers' powers. Furthermore, constructive notice extends not merely to memorandum and articles but also to all such documents as are required to be registered with the Registrar such as, special resolutions and particulars of charges. There is however no constructive notice of documents which are filed with the Registrar for the sake of record only, such as annual returns and accounts. It is suggested that there should be constructive notice of only such documents as are open to public inspection.

In reference to the "list of directors" it has been held by the Supreme Court of Malaysia that it becomes a 'public document'. Persons dealing with the company would be deemed to have constructive notice as to who are the directors of the company, where a document is required to be signed by a director and the person actually signing is not there in the list filed by the company, it would not be a properly signed document. The court said: "....the common law doctrine of constructive notice should apply to the form. To reiterate, the form is a public document which contains particulars of directors who are the mind and will of a company, as well as managers and secretaries who are responsible for the day-to-day running of the company. It is a document which affects the powers of the company and its agents. Certainly, its purpose must be more than just to provide information about the company's directors, manager and secretary. Therefore, persons dealing with the company should check with the registrar of companies who its directors, managers and secretaries are at any given time." *K.L. Engineering v. Arab Malaysia Finance,* (1995) 1 SCR 85 (Malaysia).

The impact of this doctrine on practical relations is thus stated in HALSBURY: "A company is subject to the rule that, where the conduct of a party charged with a notice shows that he had suspicions of a state of facts the knowledge of which would affect his legal rights, but that he deliberately refrained from making inquiries, he will be treated as having had notice, though he is not entitled to claim for his own advantage to be treated as having knowledge of the facts which inquiry would have disclosed, *Jones v. Smith,* (1841) 1 Hare 43; *Houghton & Co. v. Nothard, Lowe and Wills Ltd.,* (1927) 1 KB 246 (CA); **affirmed** in (1928) AC 1 (HL). Nevertheless, generally speaking the equitable doctrines of constructive notice are not applicable to purely commercial transactions", *Manchester Trust v. Furness,* (1895) 2 QB 539 (CA); *Greer v. Downs Supply Co.,* (1927) 2 KB 28 (CA). HALSBURY'S LAWS OF ENGLAND 726 (4th edn., Reissue Vol. 7(1) para 991).

See also Notes under section 610 under which doctrine of constructive notice operates and the right to inspection & copies of a company's public document is given.

Reform of the rule of constructive notice in England

Section 35A(1) of the English 1985 Act provides that:

"In favour of a person dealing with a company in good faith, the power of the Board of Directors to bind the company, or authorise others to do so, shall be deemed to be free of any limitation under the company's constitution."

This removes any restrictions imposed upon the authority of the directors, either to act themselves or to empower others to act, by the company's constitution if the third party is dealing in good faith. If section 35A(1) applies then the sole question is whether the agent was acting within his authority apart from the company's constitution.

The effects of this provision are: *First,* the section only applies in favour of a third party and not the company. *Second,* that person must be "dealing with a company." Section 35(2)(*a*) provides that anyone who is a party to any transaction or other act to which the company is a party is dealing with that company. See *T.C.B. Ltd. v. Gray,* (1986) 1 All ER 587 : (1986) BCLC 113 Ch D; *International Sales and Agencies Ltd. v. Marcus,* (1982) 3 All ER 551; *Re, Halt Garage, (1964) Ltd.,* (1982) 3 All ER 1016. *Thirdly,* the person dealing with a company must be acting in good faith. Section 35A(2)(*b*) provides that bad faith is not to be assumed simply because the third party knew that the act was contrary to the directors' powers under the constitution. If the outsider is dealing with the company in good faith, as defined in section 35A, [English Act, 1985] he will be able to enforce any contract made by an agent on the company's behalf if that agent was acting within his authority, irrespective of any limitations on his powers under the company's constitution. If the outsider is not acting in good faith, the position is different. An agent may bind his principal (in this case the company) if he has acted within his actual, implied or apparent authority.

"Person dealing with company in goodfaith.—A shareholder receiving bonus shares from a company has been held to be 'a person dealing with a company' within the ambit of s. 35A(1), and accordingly such a shareholder can in principle take advantage of the section which provides that, in favour of a person dealing with a company in good faith, the power of the Board of directors to bind the company, or authorise others to do so, shall be deemed to be free of any limitation under the company's constitution. The court said that the words 'a person dealing with a company' are not expressly fettered in any way. As a matter of ordinary language, a shareholder receiving bonus shares from the company is within the ambit of those wide words, and, in the absence of a powerful reason to the contrary, it is inappropriate to treat naturally wide words in a statute as subject to an implied limitation. *EIC Services Ltd. v. Phipps,* (2003) 3 All ER 804 : (2003) 1 WLR 360 : (2004) 118 Com Cases 443 (Ch. D).

A further attempt towards reform was made by the Companies Act, 1989 by inserting s. 711-A in C.A. 1985 for abolishing the doctrine of constructive notice altogether but that has not been implemented so far. This section provides that a person will not be taken to have notice of any matter merely because of its being filed with the Registrar of Companies and therefore available for inspection. Its implementation has become postponed because special care has to be taken in connection with registration of charges and its constructive notice.

A director-cum-chairman of a company was not allowed to take advantage of this provision. He called a meeting which he alone attended and also presided over it. He executed and approved an assignment of certain of the company's claims to himself. He entertained a mistaken belief that he had the power to act alone under the articles. The court held that the transaction was not proper. He was not a person dealing with the company from the outside. He was responsible to assure that the constitution of the company was properly applied. He could not rely on his own mistake in order to give validity to something which had no validity of any kind under the company's constitution. *Smith v. Henniker-Major & Co.,* (2002) 2 BCLC 655 (CA). There was a **dissenting** judgment also.

Internal rules and bye-laws

The rules or bye-laws made by the Board of Directors or committee of the Board or by the company in general meeting have not the same force as the articles. They are only directory and non-compliance with them will not make anything done invalid, and irregularities in administering them can always be regularised.

Money payable by members is a debt [Sub-section (2)]

Though all money payable under the memorandum or articles is a debt due, the liability on the debt is not enforceable, unless proper notice is given in accordance with the articles. *Pabna Dhana-Bhandar Co. Ltd. v. Foyezud Din Mia,* (1933) 3 Com Cases 41 : AIR 1932 Cal 716; *Viswanath Prasad Jallan v. Holyland Cinetone Ltd.,* (1939) 9 Com Cases 324 : AIR 1939 All 739.

Interpretation of memorandum and articles

Articles should be construed as a business document so as to give business efficacy in preference to a construction which will prove unworkable. *Holmes v. Keyes (Lord),* (1958) 2 All ER 129 (CA); *Rayfield v. Hands,* (1958) 2 All ER 194 : (1958) 28 Com Cases 460 (Ch D). Where the conduct of the parties reveals that there has been some practice in vogue for several years which was accepted by every one concerned without any challenge or question, then that practice in the course of long years in itself becomes an indication that the rules or articles which are framed by way of internal management were understood in that sense. *Krishnaswamy (S.) v. South India Film Chamber of Commerce,* AIR 1969 Mad 42; cited in *Sunil Dev v. Delhi and District Cricket Assn.,* (1994) 80 Com Cases 174 (Del).

Any provision in the memorandum or articles which is at variance with any provisions of the Act will have to be ignored as void (See section 9). But if it is in accordance with any regulations in Table A of Schedule I, it cannot be treated as void as Table A has statutory authority, *Lock v. Queensland Investments Etc., Co.,* 1896 AC 461 : (1896) 1 Ch 397.

The memorandum must like any other document be construed according to accepted principles applicable to the interpretation of all legal documents. No rigid canon of construction is to be applied to such a document. Like any other document, it must be read fairly and its import derived from a reasonable interpretation of the language which it employs. *A. Lakshmanaswami Mudaliar v. LIC of India Ltd.,* (1963) 33 Com Cases 420, 430 (SC) (**following** *Egyptian Salt & Soda Co. v. Port Said Salt Assn.,* AIR 1931 PC 182).

The memorandum and articles must be read together in the event of any ambiguity. In *Angostura Bitters & Co. Ltd. v. Kerr,* AIR 1934 PC 89 : (1934) 4 Com Cases 1 at 7; the Privy Council held: "Except in respect of such matters as must by statute be provided for by the memorandum, it is not to be regarded as the dominant document but is to be read in conjunction with the articles... The two documents must be read together at all events so far as may be necessary to explain any ambiguity appearing in the terms of the memorandum or to supplement it upon any matter as to which it is silent"—quoted with **approval** by the Supreme Court in *A. Lakshmanaswami Mudaliar v. LIC of India Ltd.,* (1963) 33 Com Cases 420, 429, 432 : AIR 1963 SC 1185. The Supreme Court also observed that if an object is not within the competence of the company, the directors cannot rely upon the articles to expend funds of the company to achieve that object.

For binding effect of the provisions in articles empowering both joint venturers to veto Board decisions see *IDL Chemicals Ltd. v. Astra Pharmaceuticals AB Sweden,* (1997) 88 Com Cases 649 (Kant).

§ See also, Notes under sections 1, 13 and 26.

S. 37. Provision as to companies limited by guarantee.—(1) In the case of a company limited by guarantee and not having a share capital, and registered on or after the first day of April, 1914, every provision in the memorandum or articles or in any resolution of the company purporting to give any person a right to participate in the divisible profits of the company otherwise than as a member shall be void.

(2) For the purpose of the provisions of this Act relating to the memorandum of a company limited by guarantee and of this section, every provision in the memorandum or articles, or in any resolution, of any company limited by guarantee and registered on or after the first day of April, 1914, purporting to divide the undertaking of the company into shares or interests, shall be treated as a provision for a share capital, notwithstanding that the nominal amount or number of the shares or interests is not specified thereby.

NOTES

Eng. Act, 1948 : Sec. 21
Eng. Act, 1985 : Sec. 15 CP 10

Previous Act : Sec. 27

Nature of guarantee company as distinguished from company limited by shares

The distinction between a guarantee company and a company limited by shares is that the liability to pay the share money can be enforced during the life time of the company, while the guarantee money can be recovered in the winding up of the company. Thus, it would seem that a guarantee company does not need any capital contribution at the initial stage from its members. It makes up its funds through donations, etc. It is a suitable choice for all kinds of educational, charitable, research, training, scientific development institutions. It is also extensively used for organising professionals, traders, etc., into an association for general and non-business purposes.

Guarantee company in essence a private company.—A guarantee company being generally in the nature of an association of members, it acquires the looks of a private company. Rights of admission to membership are generally reserved and the membership is generally not a transferable property.

Admission to membership and transfer of members' interest

Where the company is a guarantee company registered under section 25 of the Act, articles of association can make special provisions for expulsion of members, resignation of members, assignment of interest, and nomination of interest. Indeed provisions to this effect have been judicially upheld, and it has been held that such provisions made in the articles are not in any way inconsistent with Table C of Schedule I, the Form in Table C being only Form and not 'contents' as held in *Gaiman v. National Association for Mental Health,* (1971) 41 Com Cases 929 (Ch D). Where such specific provisions are made in the articles of association to deal with transfer of members' interest, the provisions of section 108(1) cannot be made applicable, as they relate to shares only. *Saroj Maloo (Smt.) v. Magadh Stock Exchange Assn.,* (1995) 4 Comp LJ 135 (CLB—Cal). The decision of the CLB was **not upheld** by the Patna High Court, the latter being of the view that there is no difference between transfer of shares and of membership. On appeal, the Supreme Court emphasised that the right of a guarantee company to refuse to accept the transfer by a member of his interest in the company is on a different footing than that of a company limited by shares. The guarantee company here was running a stock exchange. The right of an existing member to transfer his interest to another person would involve the question of that person's admission to the membership of the organisation. Such membership may carry privileges much different from those of ordinary shareholders. Accordingly, the Supreme Court characterised the decision of the High Court that the

same principles were applicable as much to transfer of membership as to shares, as wrong. The matter was remitted for reconsideration. *Narendra Kumar Agrawal v. Saroj Maloo,* (1996) 85 Com Cases 172 (SC). The Court noted the difference in the set of articles in Sch. I which are applicable to guarantee companies and companies limited by shares.

The Company Law Board in the case of *Saroj Maloo,* discussed above, rendered the unique service of reconnecting the various provisions of the Companies Act, which deal with a members' right to transfer shares or other interests listed at (1995) 4 Comp LJ 140, 141 and observed in conclusion that if the articles of association of the company have no provision regarding transfer of other interest of the company, we will have to examine whether the articles of association of the company are *inconsistent* with the provisions contained in the Form in Table C in Schedule I (section 29). A perusal of the Form in Table C in Schedule I shows that there is no provision in the format prescribing transferability of 'other interest'. Therefore, if the articles of association of a company limited by guarantee do not provide for transfer of 'other interest', it cannot be held that it is inconsistent with the provisions contained in the Form C in Schedule I.

In many instances guarantee companies, which satisfy the requirements of section 25 of the Act, do not add the word "Limited" to their names, but where this is not the case, a company limited by guarantee, like a company limited by shares, has to incorporate the word "Limited" as the last word of its name (S. 13(1)(a)). For memorandum and articles as applicable to guarantee companies, see Table C in Schedule I to the Companies Act, 1956.

Distribution of profits.—A company limited by guarantee may distribute its profits to its members unless its memorandum or articles otherwise provide, as invariably is the case where the company is exempt from the requirement of adding "Limited" as the last word in its name. (S. 25(1)(b)) (*Cf.* PALMER'S COMPANY LAW, 2015-6, para 2.009, 25th Edn., 1992). In *CIT v. Madras Stock Exchange Ltd.,* (1981) 130 ITR 184 (SC) it has been held that there is no prohibition against distribution of profits among the members. Articles in Table C (which apply to guarantee companies) neither enable nor prohibit distribution of dividends.

S. 38. Effect of alteration in memorandum or articles.—Notwithstanding anything in the memorandum or articles of a company, no member of the company shall be bound by an alteration made in the memorandum or articles after the date on which he became a member, if and so far as the alteration requires him to take or subscribe for more shares than the number held by him at the date on which the alteration is made, or in any way increases his liability as at that date, to contribute to the share capital of, or otherwise to pay money to, the company:

[1][*Provided* that this section shall not apply—

(a) in any case where the member agrees in writing either before or after a particular alteration is made, to be bound by the alteration; or

(b) in any case where the company is a club or the company is any other association and the alteration requires the member to pay recurring or periodical subscriptions or charges at a higher rate although he does not agree in writing to be bound by the alteration.]

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1. Subs. by Act 65 of 1960, s. 12.

NOTES

Eng. Act, 1948 : Sec. 22
Eng. Act, 1985 : Sec. 16

Previous Act : Sec. 20-A

Companies (Amendment) Act, 1960

The amendments were made in the section by the Amendment Act of 1960 with reference to the following observations of the Companies Act Amendment Committee: "It would appear that the section has no application to collateral obligation such as the liability for monthly or annual subscription payable by the members of a club or other association at such rates as may be fixed by the Articles from time to time for the privileges of enjoying the amenities provided by the club or association. In view of the increase in the general level of prices such recurring subscriptions have to be raised by an amendment of the Articles pursuant to a resolution of the company so as to be binding on all the members. Section 8 would have no application to such cases of recurring subscription. The Bombay High Court in a recent judgment, however, has taken a contrary view and construing the words "otherwise to pay money to the company" in their widest sense held that a resolution of the company (a Turf Club) amending its Articles so as to raise the rate of recurring subscriptions payable by members, would not be binding on the dissentient members and that they would be entitled to enjoy all the privileges of membership on payment of the rates of subscription current at the time when they became members of the club. Of course, persons who became members of the company subsequent to the amendment of the Articles would be bound to pay the increased rates of subscription." (*Report*, para 36).

Note that the section extends to all forms for increased liability to pay, and not merely in respect of share capital.

Members how far bound by alteration

The agreement of a member to be bound by any alterations in the memorandum or articles need not be in any special writing. If the member signs the minutes of any general meeting adopting the alteration, that will be sufficient agreement to bind him in respect of the alteration.

Alteration increasing members' liability to contribute capital

The limited liability clause is of the utmost importance for a shareholder. This section provides that save to the extent to which a member agrees in writing and anything in the memorandum or articles notwithstanding, the member shall not be bound by any alteration in the memorandum or articles requiring him to take or subscribe for more shares than he held at the date when he became a member, or to increase his liability to contribute to the share capital, or to pay money by any other means to the company. It is this that assures him of the extent of his liability subject to exceptions to be noted later. His liability being limited, he cannot be compelled to take more shares than he has already taken or contribute more than he has undertaken to do when he became a member. This right has been described as an "individual right of membership," *Edwards v. Halliwell*, (1950) 2 All ER 1064, 1067, *per* JENKINS LJ, and as "an individual membership right of the highest order because.... it cannot be overruled by a majority of even all the members other than the opposing one." PALMER'S COMPANY LAW, §10-02a, p. 114.

The protection of the section deals with the right of a member *qua* member of a company. It does not apply to the right of a member to take an additional liability from another member or a third party and such agreement need not be in writing. *Rayfield v. Hands*, (1960) Ch 1. But the section leaves untouched other devices for the compulsory raising of further capital which do not involve an alteration of the company's memorandum or articles. Thus, a company may by a reconstruction increase its members' liability to contribute share capital, and a similar increase may result from a reduction of share

capital approved by the court where the paid-up value of issued shares is reduced but their nominal value remains the same.

Increasing liability by implication

According to a decision of the Court of Appeal, it is not possible to imply into a company's articles on the basis of extrinsic evidence linked to surrounding circumstances requiring a member to make an additional financial contribution and, therefore, a member cannot be forced by such an implication to contribute sums to his company over and above his existing subscription. *Bratton Seymour Service Co. Ltd. v. Oxborough,* (1992) BCLC 693 (CA).

It may be noted that proviso (b) applies to all associations, clubs, chambers of commerce, trade associations, etc.

S. 39. Copies of memorandum and articles, etc. to be given to members.—(1) A company shall, on being so required by a member, send to him within seven days of the requirement and subject to the payment of a fee of one rupee, a copy each of the following documents, as in force for the time being—

(a) the memorandum;

(b) the articles, if any;

(c) [1][* * * *]

(d) every other agreement and every resolution referred to in section 192, if and in so far as they have not been embodied in the memorandum or articles.

(2) If a company makes default in complying with the requirements of this section, the company, and every officer of the company who is in default, shall be punishable, for each offence, with fine which may extend to [2][*five hundred rupees*].

NOTES

Eng. Act, 1948 : Sec. 24
Eng. Act, 1985 : Sec. 19

Previous Act : Sec. 25

Companies (Amendment) Act, 2000

The Amendment Act of 2000 has brought the following changes in the section :

1. Sub-section (1)(c).—In sub-section (1), clause (c) has been omitted by the Amendment Act, 2000. This amendment is of consequential nature. Before the omission clause (c) read as under : "(c) the agreement, if any, entered into or proposed to be entered into by the company with any person appointed or to be appointed as its managing agent or as its secretaries and treasurers; and"

2. Sub-section (2).—The Amendment Act of 2000 has enhanced the penalty amount from fifty rupees to five hundred rupees. Sub-section (2) was accordingly amended.

Notes on Clauses.—Clause 10 appended to the Bill stated thus : "*Clause 10* seeks to omit clause (*c*) in sub-section (*1*) of section 39 of the Act relating to managing agent,

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1. Clause (c) omitted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 10 (w.e.f. 13-12-2000).
2. The words "fifty rupees' substituted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 10 (w.e.f. 13-12-2000).

secretaries and treasurers and also seeks to enhance the fine specified in sub-section (2) of that section from fifty rupees to five hundred rupees." [*Clause* (10)].

Scope of section

The section requires that every agreement and every resolution referred to in section 192 should be embodied in the memorandum or articles and that on being required by a member and within seven days of such requirement a copy of each of them should be furnished to him, on payment of a fee of one rupee by the member. Similarly, a member is entitled to updated copy of Memorandum and Articles of Association on demand [See Section 40].

Section 391 also requires that a copy of the order of Court under that section approving of any compromise or arrangement with creditors and/or members or sanctioning the reconstruction or amalgamation should be annexed to every copy of the memorandum of the company issued after such order comes into effect [Section 391(4)].

The object is to give the agreements and resolution and orders the same importance as the articles of the company.

Penalty for default [Sub-section (2)].—The default is punishable with fine upto five hundred rupees and not only the company but every officer in default is made liable.

Compoundable Offence.—The offence is compoundable under section 621A.

Offence complete at Registered Office.—The failure to deliver documents constitutes an offence of which it has been held that the offence is complete at the registered office of the company and, therefore, the courts at that place alone would have jurisdiction to try the offence. *ICICI Ltd. v. H.V. Jayaram,* (1998) 94 Com Cases 409 (Kant). **Affirmed** by the Supreme Court in *H.V. Jayaram v. ICICI Ltd* (2000) 99 Com Cases 341 AIR 2000 SC-579 (SC); *Upendra Kumar Joshi v. Manik Lal Chaterjee,* (1982) 52 Com Cases 177 (Pat). The Supreme court **applied** the principle of law stated in *Hanuman Pd. Gupta v. Hiralal,* (1970) 40 Com Cases 1058 (SC) and **overruled** the decision in *Ranbaxy Laboratories Ltd. v. Indra Kala,* (1997) 88 Com Cases 348 (Raj). The ruling of the Supreme Court in *H.V. Jayaran* was **followed** in *Karnataka Bank Ltd. v. B. Suresh,* (2001) 105 Com Cases 110 : (2001) 2 Comp LJ 417 : (2001) 32 SCL 441 : (2001) 43 SCL 32 (Kant).

Secretarial Practice Notes

Ensure that members were supplied with updated copies of memorandum, articles, etc. within seven days of receipt of request from the members on payment of requisite fee. Check whether any complaints had been received? If so, whether corrective action taken?

S. 40. Alteration of memorandum or articles etc., to be noted in every copy.—(1) Where an alteration is made in the memorandum or articles of a company, [1][* * * * *] or in any other agreement, or any resolution, referred to in section 192, every copy of the memorandum, articles, agreement or resolution issued after the date of the alteration shall be in accordance with the alteration.

(2) If, at any time, the company issues any copies of the memorandum, articles, resolution or agreement, which are not in accordance with the alteration or alterations made therein before that time, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to [2][*one hundred rupees*] for each copy so issued.

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1. The words "in the agreement referred to in clause (c) of sub-section (1) of section 39 or in any other agreement" omitted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 11 (w.e.f. 13-12-2000).
2. The words "ten rupees" substituted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 11 (w.e.f. 13-12-2000).

NOTES

Eng. Act, 1948 : Sec. 25
Eng. Act, 1985 : Sec. 20

Previous Act : Sec. 25-A

Companies (Amendment) Act, 2000

The Amendment Act of 2000 has brought the following changes in the section :

1. The terms [in the agreement referred to in clause (*c*) of sub-section (1) of section 39] have been omitted by the Amendment Act, 2000. The amendment is of consequential nature.
2. The Amendment Act of 2000 enhanced the penalty amount from ten rupees to one hundred rupees. Sub-section (2) was accordingly amended.

Scope of section

Alterations made in the memorandum or articles of a company have to be incorporated in every copy of the memorandum or articles to be issued after the date of the alteration. Similarly, alterations made in any agreement or resolution referred to in s. 192 have to be incorporated in the copies of the agreement or resolution to be issued after the alteration. See section 2(1) for definition of 'alteration'.

An alteration of the memorandum pursuant to a reduction of capital should also be noted as per section 103(6).

Penalty for default [Sub-sec. (2)].—If a company issues any copies of memorandum, articles, resolution or agreement, which are not in accordance with the alterations made therein before that time, the company and every officer of the company who is in default, is punishable with fine which may extend to one hundred rupees for each copy so issued.

Compoundable Offence.—The offence is compoundable under section 621A.

Secretarial Practice Notes

Ensure that the alterations were noted in all copies of memorandum and articles issued after the date of alteration.

Membership of Company

S. 41. Definition of "member".—(1) The subscribers of the memorandum of a company shall be deemed to have agreed to become members of the company, and on its registration, shall be entered as members in its register of members.

(2) Every other person who [1][agrees in writing] to become a member of a company and whose name is entered in its register of members, shall be a member of the company.

[2][(3) Every person holding equity share capital of company and whose name is entered as beneficial owner in the records of the depository shall be deemed to be a member of the concerned company.]

NOTES

Eng. Act, 1948 : Sec. 26
Eng. Act, 1985 : Sec. 22

Previous Act : Sec. 30

1. Sub. by Act 65 of 1960, s. 13 for 'agrees'.
2. Ins. by the Depositories Act, 1996 (w.e.f. 20-9-1995).

Depositories Act, 1996

Sub-section (3) has been introduced as a consequential amendment made by the Depositories Act, 1996. It became necessary to expand the concept of membership through depositories. It provides a legal framework for establishment of depositories to record ownership details in book entry form. The sub-section, therefore, says that a person holding equity share capital of a company with an entry in the records of a depository as a beneficial owner shall be deemed to be a member of the company. Thus, an entry in the records of a depository is deemed to be an entry in the register of members.

Subscriber as member [sub-section (1)]

In the case of a subscriber, no application or allotment is necessary to become a member. By virtue of his subscribing to the memorandum, he becomes a member. *Babu Lal v. Naraina Sugar & General Mills Ltd.*, (1958) 28 Com Cases 155 (Punj). Entry in the register of members is not necessary to constitute him a member. *Official Liquidator v. Suleman Bhai*, AIR 1955 MB 166. See also LORD CAIRNS in *Evan's* case. *Re, London Hamburg* and *Continental Exchange Bank*, (1867) LR 2 Ch App 427, where it was pointed out that if allotment is made it must be regular to make him liable. In *Synemodelux Ltd. v. K. Vannamuthu Pillai*, AIR 1939 Mad 498 : (1939) 9 Com Cases 126, the court considered the allotment to be necessary to charge the subscriber with liability.

A subscriber becomes *ipso facto* a member on incorporation. This kind of automatic membership is considered necessary to create confidence in the investing public. *Collector of Moradabad v. Equity Insurance Co.*, (1948) 18 Com Cases 309, 315 : AIR 1948 Oudh 197. The subscribers are deemed to be the first members. Their membership is beyond revocation. *Universal Transport Co. v. Jagjit Singh*, AIR 1955 Punj 228 : (1956) 26 Com Cases 36; *Official Liquidator v. Sulemanbhai Kachi*, AIR 1955 MB 166. Neither repudiation, *Banwarilal v. Kundan Cotton Mills*, (1937) 7 Com Cases 345, 347 (Lah), nor any relief given to them from their obligation to pay for their shares, *Tufnell and Ponsonby's* case, (1885) 29 Ch D 421 (CA), nor allotment of fully paid shares nor transfer of shares by him will relieve him of his liability arising by virtue of subscription *Bombay Electric Co. Ltd., Elmore's* case, (1888) ILR 13 Bom 57. There is no relief even when he was the victim of a misrepresentation because he can sue those who deceived him. See, *Banwarilal's* case (*Supra*). Subscribers to the Memorandum of Association who are the first directors cannot escape their liability to pay for the shares they have agreed to take, by pleading their own default in not allotting shares to themselves. *Naraindas Lahoredas, Re*, (1934) 4 Com Cases 127 at 133 (Sind).

A subscriber to be liable must sign by his own hand or through an authorised agent. *Imperial Flour Mills Co. v. Lamb*, (1888) ILR 12 Bom 647.

Even when a subscriber is allotted fully paid shares for services rendered by him in the absence of a clear contract to the contrary, he will continue to be liable for the shares subscribed. *In Re, London & County Coal Co., Re, Bennett*, (1867) 16 LT 474. But see *In re, Hexford Co., Pell's* case, (1869) 39 LJ Ch 120 and *Re, Bosworthen & Penzance Mining Co., Jone's* case, (1870) 6 Ch App 48, where the subscribers were held not liable.

A subscriber ceases to be liable when all the shares have been allotted by the company to others, but in that case the subscriber will be liable again when the company has shares available for allotment. *Mackley's* case, (1876) 1 Ch D 247; *Kilpling v. Tood*, (1878) 3 CPD 350.

Directors as members by qualification shares

Section 266 provides that neither anybody's name will be mentioned among proposed directors nor will anybody act as a director of a public company unless he submits his consent in writing to the Registrar and agrees to take his qualification shares if any. When a director files an undertaking of this kind with the Registrar to take his qualification shares he also automatically becomes a member of the company, whether any shares have been allotted to him or not, though the Bombay High Court has held that if he does not

take his qualification shares within two months he vacates his office and incurs a penalty if he continues but that his name cannot be entered in the list of contributories unless the company had actually allotted him the requisite number of shares. *Zamir Ahmed Raz v. Dr. D.R. Banaji,* (1957) 27 Com Cases 634 : AIR 1958 Bom 198.

Agreement to become member [Sub-section (2)]

"Agrees in writing".—The words "in writing" have been added by Amendment Act (65 of 1960) on the following suggestion of the Companies Act Amendment Committee:—"It has been brought to our notice that in some cases on the verge of liquidation, entries are made in the register of members of the names of persons who never applied for shares, in order to fasten liability on these persons as contributories. To avoid this contingency, we suggest the addition of the words "in writing" after the word "agrees" in section 41 (2)." (*Report,* para 38.)

The Supreme Court has held that for any other person to become a member two conditions must be fulfilled (1) that there is an agreement to become a member (2) that his name is entered in the register of members. Both these conditions are cumulative. *Balkrishan Gupta v. Swedeshi Polytex Ltd.,* (1985) 58 Com Cases 563 : AIR 1985 SC 520; *Lalithamba Bai v. Harrisons Malayalam Ltd.,* (1988) 63 Com Cases 662 (Ker).

No one can become a member unless he has agreed in writing to become one. The words 'in writing' indicate, by necessary implication, that an application for allotment of shares should be made in writing. *Kumaran Potty v. Venad Pharmaceuticals Chemicals' Ltd.,* (1989) 65 Com Cases 246, 250 (Ker); *Manabendra Shah (H.H.) v. Official Liquidator,* (1977) 47 Com Cases 356 (Del). An agreement to become a member can no longer be inferred or implied from conduct.

The limited purpose of amending s. 41(2) by the incorporation of the words 'in writing' was to protect innocent persons from the demands of companies on the verge of going into liquidation. Under the sub-section a person must give his consent in unequivocal terms by applying in writing for allotment of shares. *Shri Balaji Textile Mills P. Ltd. v. Ashok Kavle,* (1989) 66 Com Cases 654, 666, 667 (Kar). The entering of a person's name in the register of members without there being any agreement on his part 'in writing' is contrary to section 41(2) and his name cannot be permitted to remain on the register. This requirement is based on public policy and cannot be waived by the investors. *Ram Kishan v. Kanwar Papers Private Ltd.,* (1990) 69 Com Cases 209, 219, 220 (HP). The company can be ordered to rectify the register under s. 111(4)(a)(i) (*ibid*).

As an agreement in writing is required for becoming a member, a person cannot be deemed to have become a member by means of estoppel, simply because his name is entered in the register. There can be no implied or constructive agreement to become a member.

The agreement should be with the company after incorporation. An agreement with promoters will not do. *Gujarat Spinning & Weaving Co. v. Girdharilal Dalpatram,* (1880) ILR 5 Bom 425. But in the case of a person whose name is entered in the register of members and who has in fact accepted the position and acted as a member, agreement in writing will be presumed until the presumption is rebutted by proof to the contrary. *Cf. Amar Singh v. Khalasa Bank Ltd.,* AIR 1933 Lah 108.

Under the English Act, where the words "in writing" are not used and the only words are: 'agrees to become a member', it has been held that this phrase is satisfied where a person assents to become a member and does not require that there be a binding contract between the person and the company. Accordingly, where the name of a person is entered in the register of members with his consent he is a member of the company within the meaning of statutory provisions. *Nuneaton Borough Association Football Club Ltd., Re,* 1989 BCLC 454 (CA).

Consideration necessary.—The agreement has to be for some consideration, otherwise the allotment would be void. Where the application was through stockinvest but that mode

of payment failed and the company received no consideration, it was held that the company had the right to call upon the allottee to make payment within the stipulated period. The company was bound to issue share certificates only on receiving payment. *American Remedies Ltd. v. Prakash Chandra Gupta,* (2001) 4 Comp LJ 138 : (2001) 44 CLA 36 : (2001) 32 SCL 295 : (2002) 111 Com Cases 777 (CLB).

Membership by oral agreement.—The words "in writing" indicate, by necessary implication, that an application for allotment of shares should be in writing and no oral application will be sufficient. Under the English Companies Act, no such writing is required. The observation in *Sree Ayyanar Spinning & Weaving Mills Ltd. v. Rajendran (V.V.V.),* (1973) 43 Com Cases 225 (Mad) that "the provisions of the Companies Act nowhere provide that there must be a written application for allotment of shares and, therefore, there can be an oral application for the purpose and an allotment made on the basis of an oral application", apparently has not taken note of the words "in writing" inserted by the Companies (Amendment) Act LXV of 1960.

Where there was no application in writing for an allotment nor any other form of request in writing and shares were allotted by converting loans into shares under an oral agreement, it was held that this was a non-compliance with the requirement of s. 41(2) and, therefore, the petitioner company, whose loan was converted, had a sufficient cause to seek rectification. *Indglobal Investment and Finance Ltd. v. Rajasthan Breweries Ltd.,* (2001) 3 Comp LJ 271 : (2001) 107 Com Cases 525 (CLB).

Rectification of register of members where name entered without agreement in writing.—Showing a person's name in a company's register of members without his agreement in writing to become a member is a wrongful entry and such wrongful entries are liable to be rectified by removing such a name. The court agreed that damages are payable to the person whose name is shown in a company's register of members without any justification, but that he would have to prove the damage suffered by him. In the present case, no such proof was offered and, therefore, the claim was rejected. The requirement of "agreement in writing" is a statutory requirement based on a principle of public policy and, therefore, cannot be waived by the parties. *Ram Kishan v. Kanwar Papers P. Ltd.,* (1990) 69 Com Cases 209 (HP).

No right in management before acquisition of membership.—Applicants for membership of a company do not acquire any right to interfere in the management of the affairs of the company. They have to wait till at least they are enrolled as members. Before that, they have the right to seek enforcement of their right to be members. They are not entitled to a court order that the company should not go ahead in election of directors till their applications for membership are disposed of. *Santosh Mani v. New Delhi Young Men Christian Assn.,* (1995) 19 Corpt LA 178 (Del).

Membership by transfer.—In the case of a person purchasing shares, registration of the transfer with the company is necessary to enable him to become a shareholder or member. As long as his name is not entered in the register of members he is not a member. *Balkrishan Gupta v. Swadeshi Polytex Ltd.,* (1985) 58 Com Cases 563 : AIR 1985 SC 520 : and *Life Insurance Corporation of India v. Escorts Ltd.,* (1986) 59 Com Cases 548 : AIR 1986 SC 1370. He does not acquire the status of a member merely by purchasing shares. Accordingly if the shares purchased by him have been forfeited by the company he cannot challenge the validity of the forfeiture. *Travancore Electro Chemical Industries Ltd. v. Alagappa Textiles (Cochin) Ltd.,* 1972 Tax LR 2192 at 2195 (Ker) where the court relied upon the following authorities: *Buckley on the Companies Act,* p. 808, (13th edn.) and judgment of HIDAYATULLAH J. in *Howrah Trading Co. v. CIT,* AIR 1959 SC 775 at 779.

Membership by transmission.—In the case of transmission of shares by operation of law, as the company will not register the name of a heir or other legal representative as a member unless intimation of the transmission is received by the company, such intimation, which must necessarily be in writing, will constitute an agreement in writing to be-

come a member. *Cf. Indian Chemical Products Ltd. v. State of Orissa,* (1966) 36 Com Cases 592 : AIR 1967 SC 253. **Affirming** *sub-nom,* (1962) 32 Com Cases 908 (Ori—DB). Membership arises when name is entered in the register of members. *James v. Buena Ventura Nitrate Grounds Syndicate Ltd.,* (1896) 1 Ch 456 (CA).

The legal representatives of deceased members have certain rights such as the right to present a petition under sections 397 and 398. *Worldwide Agencies v. Margaret T. Desor,* AIR 1990 SC 737 : (1990) 67 Com Cases 607 (SC). **Affirming** *Margaret T. Desor v. Worldwide Agencies P. Ltd.,* (1989) 66 Com Cases 5 (Del) and *Sub-nom,* (1990) 67 Com Cases 589 (Del).

Allotment in blank to unknown persons [Special Court].—Shares can be allotted only to persons who apply for them in writing. Where an allotment was made in blank to unknown persons, it was held that the Special Court constituted under the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992 was justified in holding that it was not a proper allotment and in directing the return of the money to the persons whose allotment would be so cancelled. *Rahul Subodh Windoors Ltd. v. A.K. Menon,* (1999) 96 Com Cases 597 : (1999) 33 CLA 468 (SC).

Admission to membership.—Admission to membership has to be in accordance with the articles of the company. Accordingly, where the admission to membership of the company required a decision of the company's council as to whether a person should be admitted as a member, persons taken in without following that procedure were held to be not properly constituted members. The court found that the procedure adopted by the company in practice was a virtual automatic admission on an administrative basis of any person who applied for membership and that was not sufficient to comply with the provisions of the company's articles of association. Hence, an extraordinary general meeting attended by such members was not validly constituted. *POW Services Ltd. v. Clare,* (1995) 2 BCLC 435 (Ch D).

A company was running a school. Under its Articles "management of business" was the function of the directors. A dispute arose as to whether the admission of new members was within the domain of the directors' powers. The court laid down that the directors had no power to admit members. The court could not ignore the limiting words of the Article which had to be construed, according to the natural meaning of the words, as conferring only such powers as were relevant to the management of the business. Though the expression "management of the business" could be given a very wide meaning, it did not extend to admission of members to the corporation. In the context of the common form Article the word "business" must be affected to some extent at least by the nature of the undertaking of the company. In the present case, the undertaking was a school whose business included the provision of facilities and personnel for instruction, the admission of pupils and the many matters directly concerned with its day-to-day operation. It did not go so far as to include the decision as to who should comprise the legal entity which was to be ultimately responsible, *Yau Kung School v. Tang Kemp Yip,* (1986) LRC (comm) 616 (Hong Kong CA).

Convertible Debentures.—Companies have been issuing debentures with a conversion clause, the company being under an obligation to issue fully paid equity shares for part of that amount with the condition that without any further act or application by the debenture holder the company is obliged to issue and allot such shares to the debenture holder. It is also stated in the application forms for issue of debentures that the applicant agrees to accept the debentures applied for and such other number as may be allotted to him subject to the terms of the conversion. Unless there is adequate compliance under terms of sub-section (2) of this section, there would be an irregularity committed by the company in allotting equity shares under the conversion clause without any further act or application by the debentureholder. The requirement of sub-section (2) must also be fulfilled in cases of conversion pursuant to the conversion clause in the debenture. When the company implements its obligations to allot shares in lieu of debentures and the applica-

tion for allotment of debentures contains recitals as to allotment of shares pursuant to the terms of issue of debentures, it may serve as an agreement in writing between the debentureholder and the company to become a shareholder on allotment of shares.

Effect of allotment contrary to sub-section (2)

The requirement of the sub-section is directory and not mandatory. The sub-section does not mean that the company cannot allot shares if a person has not complied with section 41(2). An allotment so made is not void but voidable. If a person is treated as a shareholder of the company, either by entering his name in the register of members or treating him as a member by any subsequent conduct, his right of membership cannot be questioned by the company on the ground that he has not complied with section 41(2). *Shri Balaji Textile Mills P. Ltd. v. Ashok Kavle,* (1989) 66 Com Cases 654, 667-668 (Kar).

A shareholder whose name is not in the register can be member

Even if the prescribed register of members of the company does not incorporate the names of all its shareholders as members of the company, a person may be a member, the particulars entered in the register being not conclusive. The shareholders in whose favour share certificates are issued, can exercise rights as members of the company notwithstanding the omission of their names from the register. *N. Satyaprasad Rao v. V.L.N. Sastry,* (1988) 64 Com Cases 492, 496 (AP). But otherwise it is difficult to conceive how a person can be a shareholder in the true and full sense of the term without being a member of the company whose name is borne by the register, *Hindustan Investment Corporation v. CIT,* (1955) 25 Com Cases 57, 63 (Cal). Absence of name from the register is only a *prima facie* evidence that the person concerned is not a member. *Murarka Paint & Varnish Works Ltd., Re,* (1948) 18 Com Cases 177 (Cal).

Member on depository record [Sub-section (3)]

Depositories Act, 1996.—This sub-section has been brought into the Companies Act, by the Depositories Act, 1996 (w.e.f. 20-9-1995). The effect of the new provision is that a person holding the equity share capital of a company and whose name is entered as beneficial owner in the records of the Depository, shall be deemed to be a member of the concerned company even though there is no agreement in writing with the company nor his name appears in the register of companies.

Definition of "member" under s. 2(27) *vis-a-vis* section 41

The difference in the language of section 2(27) of the Act which comes under the definition clause in the Act and section 41 dealing with the membership of the company should be noticed. In section 2(27) the word 'member' is defined in a very comprehensive manner. The definition of the word 'member' in section 41(2) will not control the meaning of the same word in other provisions such as sections 397 and 398. The compliance with section 41(2) would not be a mandatory requirement but only directory. *Shri Balaji Textile Mills (P.) Ltd. v. Ashok Kavle,* (1989) 66 Com Cases 654, 661, 662 (Kar).

'Member' and 'Shareholder'

In the case of a company limited by shares, a company limited by guarantee and having a share capital and an unlimited company whose capital is held in definite shares, the terms 'member' and 'shareholder' are synonymous and there can be no membership except through the medium of shareholding. See *Killick Nixon Ltd. v. Bank of India,* (1985) 57 Com Cases 831 (Bom); *Howrah Trading Co. v. CIT,* AIR 1959 SC 775 : (1959) 29 Com Cases 282; *Balkrishan Gupta v. Swadeshi Polytex Ltd.,* (1985) 58 Com Cases 563 : AIR 1985 SC 520; *CWT, West Bengal v. Sumitra Devi Jalan (Smt.),* (1974) 96 ITR 35 (Cal); *Jaluram Bhikulal Firm of Itwara v. IT Commissioner,* (1953) 23 Com Cases 103 (Nag). A shareholder can have only one legal connotation. He is the person who owns certain shares and who is shown as a shareholder in the register of the company. *Shree Shakti Mills Ltd. v. CIT,* (1948) 18 Com Cases 169, 172 (Bom); *Bikaner Trading Co. v.*

CIT, (1953) 23 Com Cases 409, 412 (Cal). In the case of a company limited by guarantee and not having a share capital, admission to membership is regulated by rules adopted by the company and there is no question of anybody holding shares or being a shareholder.

Whether a partnership firm can be member

Sub-section (2) provides that a person who has agreed in writing to become a member and whose name is entered in the register of members, shall be a member of the company. The provision speaks of a 'person'. An ordinary effect of the use of this expression is that only a person can be a member. Since a person means a natural person or a corporation, the question arises whether a partnership firm, which is not a person, can be a member. This was the question before the Calcutta High Court in *Bansidhar Durgadutt v. CIT*, 1975 Tax LR 900 (Cal). A partnership firm was allotted certain shares and its name was registered in the register of members of the company. The Income-tax authorities refused to recognise this as a valid allotment for tax purposes. The court overruled the objection and held that an allotment in favour of a firm is not inoperative. The Court said [at page 906]: "It appears to us that when shares are registered in the name of a firm such registration in effect would render all partners as joint holders of the shares. In PALMER'S COMPANY LAW, (51-04, p. 802, 24th ed. 1987) it is said: "A firm can be registered in England under its partnership name although it is not a legal entity. That a Scottish partnership which is regarded as a legal entity can be registered, under its firm name is not remarkable." Similar observations have also been made in BUCKLEY'S COMPANIES ACT, 75 (12th edn.). In HALSBURY'S LAWS OF ENGLAND, 109 (3rd edn., Vol. VI Art. 227), it is observed that "if a firm with the authority of the firm, has subscribed to a memorandum the partners are joint holders of the shares subscribed for. Therefore it cannot be said that any such registration is tainted with any illegality so as to vitiate it. Neither such registration is void, nor can it be treated as *non est*". In practice, however, the articles of association of most companies provide that only individuals, companies and registered associations will be accepted as members. The Madras High Court held in *Seth Mengraj v. SMES Corporation*, (1960) 2 Mad LJ 46 (Notes) that a partnership firm could not be a member as such.

Note that there is nothing in the law which prohibits a firm from being a debenture holder. However, in case the debenture is convertible into shares either automatically or at the option of the holder, it is advisable to restrict the same only to legal entities, as these debentures also involve contract or option to be a member of the company.

Before the department expressed its view in the circular given below [*Cir. No.* 4/72 of 1972], a company had a number of partnership firms on its register as members and was not able to drop their names by itself and the department launched prosecution under s. 150 for not keeping the register in accordance with the law. The company applied to CLB for an order. The CLB stayed the prosecution and directed the company to form a trust and to transfer the shares in question to trustees. *Amrit Banaspati Company Ltd., Ghaziabad, In Re*, (1995) 83 Com Cases 789 (CLB).

Department's views.—The Department is also of the view that "a firm, not being a person cannot be registered as a member of a company except when the company is licensed under section 25. Companies which have firms registered as members should be advised to take steps to rectify the position within a specified time. In case the irregularity persists, action can be taken under section 150(2) of the Companies Act, 1956." [*Circular No.* 4/72, dated 9-3-1972].

Company as member

A company can be a member of another company. There should be authority in the company's memorandum for investment in the shares of other companies, because, without such authority, the investment is likely to be struck down as *ultra vires*. See, under s. 13. Apart from this, the other restrictions are that a company cannot purchase its own shares outside the restrictions imposed by S. 77 and, subject to the extent as specified in s. 42, a subsidiary company cannot purchase the shares of its holding company.

Co-operative society as member

A co-operative society may become a member of a company provided it is a registered society and is recognised as a separate legal entity.

Position of shareholder in company

The true position of a shareholder is that when the company earns profits and declares a dividend as per its articles, he is entitled to participate in it and get his share of the dividend and in the event of a winding up, he has a further right to participate in the distribution of the company's assets in accordance with the rights given to him under the articles. Further than this he acquires no interest in the assets of the company, *Bacha F. Gazdar v. CIT,* AIR 1955 SC 74 : (1955) 25 Com Cases 1. See also, *Tata Engineering and Locomotive Co. Ltd. v. State of Bihar,* AIR 1965 SC 40 : (1964) 34 Com Cases 458; *Lalithamba Bai v. Harrisons Malayalam Ltd.,* (1988) 63 Com Cases 662 (Ker); *Perumal (R.T.) v. John Deavin,* (1960) 30 Com Cases 340 : AIR 1960 Mad 43; for position of directors also see *Prithvi Cotton Mills v. Broach Borough Municipality,* AIR 1968 Guj 124 at 128.

A member who has transferred his shares continues to be a member so long as his name continues in the register of members, and ceases only when the transfer is registered in the name of the transferee. This is so far as the company is concerned and does not affect the rights *inter se* between the transferor and the transferee.

Contributory and member

The terms 'contributory' and 'member' are not interchangeable, since under section 428, while every member would become a contributory the converse would not be true, unless the name of the contributory is entered in the Register of members. *Rajdhani Grains & Jaggery Exchange Ltd., In re,* (1983) 54 Com Cases 166 (Del).

The series of sections which follow and are headed "Winding up by court", "Official Liquidator" and "Ordinary powers of court", leave no doubt that the word 'contributories' is really used synonymous with the word 'members'. *Raja Surrindar Singh v. P.B. & A. Products Co. Ltd.,* (1956) 26 Com Cases 41, 44 (Pepsu). Mere striking off a subscriber's name for failure to pay calls does not affect his liability to pay as a contributory. *In re, U.P. Oil Mills Ltd. Co.,* (1931) 1 Com Cases 262, 265 (All).

A member does not cease to be a member merely because winding up of the company has commenced. He continues to be a member of the company so long as the requirements of section 41 read with section 150 are complied with. *National Steel and General Mills v. Official Liquidator,* (1990) 69 Com Cases 416 (Del).

Joint members

If more than one person jointly apply for and are allotted share in a company each one becomes a member. *Narandas Munmohandas Ramji v. Indian Manufacturing Co. Ltd.,* (1953) 23 Com Cases 335 : AIR 1953 Bom 433.

In the case of partners, a firm as such cannot be registered as a member, as a firm is not, in law, a person but the partners in their individual names may be registered as joint holders of the shares: if a change occurs in the partnership, and the shares are to continue to remain as assets of the firm, a transfer of the shares will have to be effected by means of a regular instrument of transfer in the names of the new partners and the procedure for transfer of shares required to be followed by the Act must be followed as in the case of transfers among other shareholders.

In the case of joint holders, they can insist on having their names registered in such order as they may require, and they may also require their holdings to be split into several joint holdings with their names in different orders, so that all of them may have a right to vote as first named holder in one or other of the joint holdings. See *Re, Saunders (T.H.) & Co.,* (1908) 1 Ch 415; *Burns v. Siemens Brothers Dynamo Works Ltd.,* (1919) 1 Ch 225. Where a man purchased shares jointly with his wife's name, she became entitled on

his death as a surviving joint owner to have the shares registered in her name. *Deputy Commissioner v. M.D. Aikman,* (1934) 4 Com Cases 218, 223 (Oudh).

The Department is of the view that there is no need of transfer deeds for transposition of names *i.e.* change in the order of names of joint shareholders provided such request is made by all shareholders jointly to the Company. However, where the change in the order of names is required in respect of a part of the holding, execution of a transfer deed will be required (*Letter No.* F1/24/SE/80, dated 5-9-1980).

In the case, however, of a private company, the private company, may refuse to split any holdings of shares if such splitting will cause an increase in the number of its members beyond the statutory maximum provided for a private company by section 3(1)(iii)(b).

Nominee joint members.—Where the shares of a company were registered in the joint name of the company and one of the directors, it was held that the director was a nominee of the company for that purpose. He could act jointly with the company and not individually. He had no rights of his own in respect of the shares and was not entitled to bring proceedings on the basis of being one of the registered holders. *Exchange Travel (Holdings) Ltd., Re,* (1991) BCLC 728 (Ch D).

Position of joint shareholders in relation to company

(1) Private company; oppression and mismanagement.—For purposes of determining whether the number of members of a private company does not exceed fifty as required by section 3(1)(iii), and for determining the number of members required for making application under section 397 or 398, joint holders of shares are counted as one member.

(2) Requisitioning meeting [S. 169].—For purpose of calculating the number of members required for signing a requisition or notice to call an extraordinary general meeting under section 169, the signature of any one of joint holders will be sufficient and be treated as good as the signature of all of them [Section 169(8)].

(3) Splitting up joint holdings.—Unless a company had adopted an article on the lines of Regulation 7(3) of Table A of Schedule I, joint shareholders will be entitled to have their holding of shares split into such number of smaller holdings as there are number of joint holders and have the names of all of them registered in such order as will entitle all of them to receive notice of general meetings of the company and exercise voting right.

The company cannot do so by itself or on the application of any one of the joint-holders. It would require the consent of all the joint-holders or under a partition. *Rajiv Das (Dr.) v. United Press Ltd.,* (2001) 44 CLA 268 : (2002) 1 Comp LJ 170 : (2002) 111 Com Cases 584 (CLB—Cal).

(4) Service of notices etc. [S. 53].—In the case of joint shareholders, notices and other documents required to be served by a company will be deemed to be properly served if the service is effected on the first named of the joint holders as entered in the register of members [Section 53(4)]. But this does not prevent the company from issuing notice or other document to the other joint holders also at its discretion, if the circumstances of any case require the same.

(5) Payment of dividends [S. 205].—As regards payment of dividend, section 205(5)(b) enables the company to make the payment to the first named of joint shareholders on the register unless instruction in writing signed by all the joint holders has been given to the company for making the payment to any other person. In this connection Regulation 92 of Table A of Schedule I may also be noted.

(6) Attendance and voting.—As regards the rights of joint holders to attend and vote at general meetings, it would seem that, in the absence of any provision in the Act relating thereto, a company may make its own provision in its articles of association, provided that such provision is not restrictive of any rights given to shareholders under the Act or

otherwise repugnant to any provision in the Act. In the absence of any such provision in the articles joint shareholders may properly claim the following rights:—

(i) **Notice of meetings [Table A, Art. 57].**—Although notices of general meetings and other documents are required to be served only on the senior or first named of joint holders, the joint holders are individually entitled to be present and take part in the debate at such meetings and vote on resolutions decided on a show of hands (except that where Regulation 57 of Table A of Schedule I or an Article similar thereto has been adopted by the company, the voting right is not exercisable otherwise than in accordance therewith); but on a poll the voting right can be exercised only by all of them acting together.

Proxy.—And proxy also can be appointed only by all of them acting jointly but see, Regulation 57, Table A which says that in the case of joint holders the vote of the senior joint holder whether in person or by proxy shall be accepted to the exclusion of the votes of other joint holders. For this purpose seniority shall be determined by the order in which the names stand in the register of members. This shows that the senior joint holder can appoint a proxy all by himself.

(ii) **Voting and quorum.**—Even if the articles do not make any specific provisions, any joint holder present at a meeting will be entitled to exercise voting power and will be counted for quorum. But only one of the several joint holders will be entitled to exercise voting power. For the purposes of the quorum, joint shareholders will be collectively regarded as one shareholder.

Joint shareholders must concur in voting unless the articles provide to the contrary. *Lumbers v. Fretz,* (1929) 1 DLR 51 (Canada). See also, Article 57, Table A.

§ See also Notes on this point under s. 174.

(7) Share qualification [S. 270].—Where the Articles of a company require any specified share qualification for appointment to the office of director, shares held jointly with others will be sufficient qualification unless the Articles require that the shares should be held exclusively in the director's own sole name (in this connection see also Notes under section 270).

(8) Transfer and transmission [Ss. 108, 109].—In the case of transfer of shares held by joint holders, the transfer will be effective only if it is made by all the joint holders.

As regards transmission of shares by operation of law, while under English Law the survivor or survivors of the joint holders are entitled to be recognised as exclusively entitled on the death of any of them, as joint tenants, in India the law is regulated by section 45 of the Contract Act and the right devolves on the representatives of the deceased person jointly with the survivor or survivors.

(9) Payment of calls [Table A, Art. 15].—Whether or not an article similar to Regulation 15 of Table A of Schedule I has been adopted by a company making joint holders jointly and severally liable to pay calls in view of the specific provisions of section 43 of the Contract Act, the English decisions based on the general rule of English Law, [*Maxwell's* case, *Hill's* case, (1875) 20 Eq 585 and other subsequent cases] holding that in the absence of any provision in the Articles as to several liability, there would be only joint liability among the joint holders is not applicable to joint holders of shares in Indian Companies. Under Indian Law joint holders are jointly and severally liable.

General permission to NRIs to subscribe to Memorandum and Articles

§ For RBI circular issued under the above subject see Notes under section 12 under the same heading.

Minor or trust as members

Companies Amendment Act, 1960.—*Recommendation of Company Law Committee.*—The word 'agrees' used in sub-section (2) was substituted by the words 'agrees in writing' by the Companies (Amendment) Act, 1960, based on the recommendations of the Company Law Committee, thus:

"It has been suggested that a specific provision should be made that minors cannot be members of a company. Under the Contract Act a minor is incapable of contracting and membership involves a contractual relationship between the company and the members as well as the members *inter se*. No further provision is necessary.

Under section 117 of the English Companies Act no notice of any trust, expressed, implied or constructive, can be entered in the register of members or debenture holders or be receivable by the Registrar. Section 153 of our Act is to the same effect. In a few cases, the Act has recognised the holding of shares in the names of a nominee or nominees of the real owner [See sections 4(3), 42, 49, 226(3) and 307]. It would be risky for a company to register transfers of shares and pay dividends to the transferees if it was obliged to take notice of equitable interests in its share capital and it was eventually proved that the transfers were in breach of trust. A trustee of shares who is on the register of members is personally liable to the company for any calls or other obligations attaching to the shares. This has been the settled law for a long time. We are, therefore, unable to accept the suggestion that the name of a minor who has inherited shares as heir or legatee should be entered in the register as the holder of the shares. There would, however, be no objection to having the name of the certificated guardian of a minor who has inherited the shares or the executor of a probated will, under which a legacy of shares is given to a minor, being entered in the register and dividends being paid to him.

Trust as member.—"We are also unable to accept the suggestion that the name of a trust owning shares should be entered in the register in order to avoid the necessity for a transfer of the shares by one trustee to a succeeding trustee. To do so would be a contravention of section 153." (*Report* : Para 38, page 33)

Minor as member

The Company Law Board held in *Nandita Jain v. Bennett Coleman & Co. Ltd.,* Appeal No. 27 of 1972, dated 17-2-1978, "Selected Decisions of the Company Law Board", 3rd Edn. 37 (published by Government of India) that a minor applying (through her natural guardian) for being registered as a member of a company, was entitled to be so registered if the shares were fully paid up. The Board relied upon observations made in PENNINGTON'S COMPANY LAW, 2nd Edition, and in BUCKLEY ON THE COMPANIES ACTS, 12th Edition and observed that:

(1) the minor's ability to exercise some of the rights of a member under the Act and under the Memorandum and Articles is not material in this context;

(2) the contractual obligation between a member and the company or between members *inter se* under section 36 of the Act is also not relevant in this context;

(3) where the shares are fully paid up no personal covenant to pay for the shares arose.

Under the Indian Law a minor's contract is void. Observations made by authors in the context of the English Law of Contract, under which such a contract is voidable are of little value. Under section 41(2) of the Companies Act, 1956, a member is defined as a person who 'agrees in writing' to become a member. The company, therefore, cannot register a person unless the person desiring to be a member applies in writing : a minor cannot agree to be a member of the company.

The CLB'S order **relied** upon two judgments of the Punjab High Court in *Diwan Singh v. Minerva Films Ltd.,* (1958) 28 Com Cases 191 (Punj) and *Diwan Singh v. Minerva Films Ltd.,* (1959) 29 Com Cases 263 (Punj) in which there is no reference to section 30 of the Indian Companies Act, 1913, nor to section 41(2) of the Companies Act, 1956, as giving rise to contractual obligations. The Board also **relied** upon its earlier decision in, *R. Balaraman v. Buckingham and Carnatic Co. Ltd.,* (1969) 1 Comp LJ 81 (CLB), where the Board directed the company to register a transfer of fully paid-up shares in favour of

the minor daughters of the petitioner. The Board, in arriving at its decision held that the provisions of S. 11 of the Indian Contract Act would not affect the transfer since the shares were fully paid. The Board further held that the transferee could sign as guardian of the minor daughters and that the minors themselves would be the owners of the shares. The guardian would not be the trustee and S. 153 would not apply. The minor's names cannot be entered on the register of members. The guardian's name may be entered on the register of members and he can give notice of trust to the company under S. 187-C (which was enacted in 1974) after these judgments were pronounced. But as far as the company is concerned only the guardian will be the shareholder. The CLB's view is also **contrary** to the decision in *Dalmia Jain Airways Ltd. v. Saroj Rani,* ILR (1956) Punj 41.

In *Karnataka Theatres Ltd. Re* (2000) 100 Com Cases 124 : (2000) 2 Comp LJ 130 : (2000) 36 CLA 245 (CLB—SB), **following** the CLB decision in *R Balaraman* (*supra*) it has been again held that there is nothing in the Companies Act prohibiting a minor from becoming the member of a company. Section 41(2) read with Regulation 19(1) of Table A indicates that the agreement in writing can be made by the guardian on behalf of minor. It will not be a case of trust because minor's name would be entered in the register. He would incur no liability because the shares were fully paid. The shares in question were obtained by transfer. *Gautam R. Padival (Minor) v. Karnataka Theatres Ltd.,* (2000) 37 CLA 244 : (2000) CLC 1765 (CLB—SB).

When a guardian of a minor applies to be a member of a company, the company cannot enter the name of a minor in the share register, because a person's name may be registered as a shareholder only if he agrees in writing to be a member of the company. If the shares are registered in the name of the guardian, the guardian alone is the shareholder by virtue of section 153 of the Companies Act. In *Fazalbhoy Jaffar v. Credit Bank of India,* AIR 1914 Bom 128; SCOTT, C.J., said: "On attaining majority the minor can repudiate his liability and the company cannot plead an estoppel on the ground of his having received dividends during minority or his having fraudulently misrepresented his age in his application for shares". In this case an infant was registered as a shareholder. After attaining majority he received dividends from the company. The Court observed: "Under these circumstances it cannot be doubted that he has intentionally permitted the company to believe him to be a shareholder and in that belief to pay him dividends since he attained majority. He is, therefore, estopped now by his conduct from denying that he is a shareholder." The company was in winding up. See also *Beharilal v. Official Liquidator,* AIR 1918 Lah 138; *In Re, Muslim Bank of India,* (1939) 9 Com Cases 309, 310 (Lah).

If, however, shares are issued and registered in the minor's name, the contract would be void and neither the minor nor her guardian would be liable on the calls. *Palaniappa Mudaliar v. Official Liquidator Ltd., Pasupathi Bank,* (1942) 12 Com Cases 89, 91 (Mad). But where the company transferred shares to a minor without being aware of this fact, the company can repudiate the transfer, and the transferor would be liable by being restored to the register of members, *In Re, Massey & Griffin,* (1907) 1 Ch 582.

Department's Clarifications.—As regard the subject of minors being admitted as members, the Department of Company Law Administration has expressed the following views:

Clarification I.—"This Department has been advised that the Judicial Committee of the Privy Council in the leading case *Mohori Bibi v. Dharmodas Ghosh,* (1903) 30 Cal 539 : 39 IA 114 (PC) held that in India a contract by a minor is *ab initio* void. Apart from the subscribers to the memorandum of association of a company a person can become a member of a company only when he agrees in writing to be a member and when, pursuant to such agreement the name of the person is entered in the register of members. Since a minor cannot enter into a contract or agreement except through a guardian, and since in view of section 153, no notice can be taken of the fact that the guardian, holds a share in trust for a minor, it follows that his name cannot be entered in the register of members and therefore, he cannot become a member of a company. A subscriber to the memorandum of association of a company also enters into an implied agreement to become a member of the company by acceptance of the number of shares of the company written against his name. Since a minor cannot enter into contract, it follows that he cannot subscribe his name to the memorandum of association of a company. There is, however, no objection in

law to the guardian of a minor entering into a contract on behalf of a minor or a minor entering into a contract by or through his guardian. In such an event, however, owing to the operation of section 153 of the Companies Act, the name of the minor cannot be entered in the register of members along with that of his guardian nor can the name of the guardian be entered in the register of members in a manner which will show that the person concerned (the guardian) is holding the shares in question on behalf of another person *viz.*, the minor. In view of the fiduciary relationship between the guardian and the minor as laid down in the Guardian and Wards Act, a guardian is responsible for his acts and dealings to the minor in respect of the 'ward' property. There is a distinction between an agreement for sale and the sale itself. Whereas, due to the provisions of section 10 of the Indian Contract Act, 1872 a minor is not competent to enter into any contract for the purchase of shares, there is no bar to a minor purchasing fully paid-up shares since in the event of such purchase there will be no covenant subsequent on the part of the minor. In view of the legal position explained above, the Government feels it desirable that in the case of shares owned by a minor the name of the guardian and not of the minor is shown in the register of members." [*Circular No.* 312(43)-CL-III/63, dated 30-9-1963].

Clarification II.—"In a reference from the Federation of Indian Chambers of Commerce & Industry, New Delhi, the question relating to the holding of shares in a company by a minor was examined in the Department and it has been decided that whereas due to the provisions of section 10 of the Indian Contract Act a minor is not competent to enter into any contract for the purchase of shares, there is no bar to a minor purchasing fully paid-up shares, provided the name of the guardian and not that of the minor is entered in the register of members." [*Circular No.* 8/18(41)/63-PR, dated 2-11-1963 *to all Regional Directors and Registrars of Companies*].

Clarification III.—"Registrars should not raise any objection to the allotment or registration of transfer/transmission of shares to a minor and the entry of the name of a minor in the register of members or in the return of allotment or in any other return." [*Department's Letter No.* 8/18(41)/63-PR, dated 31-3-1964].

HUF as member

HUF is not a juristic person for all purposes, although it is a person for purposes of the Income-tax Act. HUF is represented by its *Karta*. There is no legal bar on HUF to invest its money in shares and securities and the Companies Act does not prohibit membership of HUF. In the case of an HUF, the shares can be registered in the name of 'A' as Karta of HUF. *Vickers Systems International Limited v. Mahesh P. Keshwani,* (1992) 73 Com Cases 317 (CLB).

Trade Union as member

A trade union registered under the Trade Unions Act, can be registered as a member and can hold shares in a company in its own corporate name *All India Bank Officers Confederation v. Dhanlakshmi Bank Ltd.,* (1997) 90 Com Cases 225 : (1997) 3 Comp LJ 132 : (1997) 26 Corpt LA 33 : (1997) 13 SCL 6 (CLB—Mad).

Society as member

Department's Clarification.—"A society registered under the Societies Registration Act, 1860 should not be deemed to be a 'body corporate' within the meaning of the aforesaid provisions [Refer to Section 2(7)] of the Companies Act, although such a society can be treated as a 'person' having separate legal entity apart from the members constituting it and thereby capable of becoming a member of a company under section 41(2) of the Companies Act, 1956." [*Circular letter,* dated 24-11-1962].

Shares belonging to society held in names of trustees simpliciter

Department's Clarification.—"In 1957 the Department of Company Affairs was advised that the shares in a company, being the property of a charitable trust, can be held in the names of the trustees *simpliciter* without describing them as trustees and that if the trustees constitute a society registered under the Societies Registration Act, 1860, the shares can be held in the name of such a society (*vide U.O. No.* 21031/57. *Adv. (F),* dated 27-5-1957). This view was reiterated in the subsequent opinion bearing *U.O. No.* 21767/62-Adv.(F), dated the 16th July, 1962, wherein it was pointed out that though a society registered under the Societies Registration Act, 1860 is not a body corporate, it is a "person" capable of being a member of company under section 41(2) of the Companies Act, 1956. Such a society is also a 'person' as contemplated by section 153B." [*Extracts from Department's File No.* 1(43)-PT/67].

Shares to be held in the name of trustees

Department's Clarification.—"Goenka Charitable Trust although the name indicates so, is not a Trust created under the Indian Trusts Act, 1862. It is a Society registered under the Societies Registration Act, 1860 and as such the provisions of the Societies Registration Act shall apply. Under section 5 of the

said Act, moveable and immoveable properties of a Society so registered, if not vested in Trustees, shall be deemed to be vested for the time being in the governing body of such Society. Under the rules and regulations of the Goenka Charities Trust, the management of the Society is vested in a Board of Trustees. The Board of Trustees, therefore, is the governing body of the Society for the purposes of section 5 of the said Act irrespective of whether the trust properties have been transferred to the Trustees as required by section 6 of the Indian Trusts Act. The shares should therefore be held in the name of the Trustees.

Section 108 of the Indian Companies Act, 1956 *inter alia* requires that a company shall not register transfer of shares unless a proper instrument of transfer duly stamped and executed by and on behalf of the transferor and transferee has been delivered to the company. As the section under which the application has been made requires that the transfer should be on a proper instrument duly stamped and executed, the Company Law Board is, competent to advise the applicant that the share should be held in the name of the Trustees and not the Trust and that the application should be amended accordingly." [*Extracts from Department's File No.* 32/108/68-CL-V].

Shares in the name of 'Public Office'

Department's Clarification.—"There is no provision in the Companies Act, 1956 that the shares in a company may be held in the name of a public office. Section 41(2) provides how a "person" (other than a subscriber of the memorandum) becomes a member. The Collector of Central Excise or the Secretary, to the Government of India, as such, is not a legal entity. Shares cannot, therefore, be held in the name of such office. Similar observations apply to the holder of any other public office which is not a corporation sole constituted by statute (*e.g.*, the Administrator General constituted a corporation sole by the Administrators General Act, 1963). Hence shares in a company cannot be registered in the name of a public office which is not a corporation sole as understood in law.

The question raised is whether the Collector of a District is entitled to hold shares of a company incorporated under the Companies Act. A 'member' has been defined in section 41 of the Companies Act. According to that section, the subscribers to the Memorandum of Association of a company and other persons who agree in writing to become a member shall be deemed to be members of the company. The answer to the question raised will, therefore, depend on whether the Collector of a District is "a person" within the meaning of the Companies Act. The term "person" has been held to include among others a "corporation sole". The Collector of a District can only be entitled to be a shareholder as a corporation sole in case it is held that his office constitutes a corporation sole. A 'corporation sole' is a corporation constituted in a single person who in the right of some office or function has corporate status. The object of a corporation sole is to make it possible to distinguish the holder of an office or function in his official and in his private capacity. By this fiction of law, it is possible to attach rights and duties to the holder, for the time being, of the office or functions to convey real or personal property to him in his official capacity, and to sue him and for him to bring an action in his official name and style. In short, a 'corporation sole' has the same characteristics of perpetual succession and separation of rights and duties of the corporate body from those of the corporator as all corporations possess.

Illustrations of corporation sole in existence in the modern law are the sovereign, an archbishop, a minister or officer of the Crown who is given the status usually by statutes (see PALMER'S COMPANY LAW—21st Edition).

The Collector of a District is a civil servant of the Union/State. Under Article 299 of the Constitution of India, all contracts required to be in the name of the President or the Governor as the case may be and under Article 300 all suits by or against the Union/State Governments are required to be filed in the name of the President or the Governor as the case may be. A Collector has no power under the Constitution either to enter into contracts or to sue or to be sued in his capacity as a Collector. Therefore, the Collector cannot be said to be a Corporation sole.

In the circumstances, he is not competent to hold shares in a limited company incorporated under the Companies Act, as the Collector." [*Extracts from Department's File No.* 25851/67].

Termination or cessation of membership

A member is entitled to exercise all the rights of membership until he ceases to be a member in accordance with the provisions of the Act. *Balkrishan Gupta v. Swadeshi Polytex Ltd.*, (1985) 58 Com Cases 563 (SC). A person may cease to be a member of a company—

(1) by surrender of shares, *Trevor v. Whitworth*, (1887) 12 App Cas 409 : (1886-90) All ER Rep 46;

(2) by disclaimer of an insolvent member's shares;

(3) by transfer of shares and registration of transfer. After registration the transferor is still liable to be placed on the B list of contributories as a past member, if the company is wound up within a year. *Stanhope's* case, (1866) 1 Ch App 161; *Heritage's* case, (1869) LR 9 Eq 5;

(4) by rescission of membership *e.g.*, on the ground of fraud or misrepresentation;

(5) by sale of shares by the company in the exercise of a power reserved in the company's articles *e.g.*, lien;

(6) by forfeiture of shares, *Dawes'* case, (1868) LR 6 Eq 232;

(7) by death; *Heward v. Wheatley,* (1853) 3 De GM & G 628; *Baird's* case, (1870) 5 Ch App 725; *U.P. Oil Mills Co. Ltd. v. Jamna Prasad,* (1933) 3 Com Cases 256 (All);

(8) by expulsion from membership.

In the case of *Vasant Investment Corporation Ltd., In re,* (1982) 52 Com Cases 139 (Bom) the Court referred to Sec. 41(2) and Sec. 150(1)(a) to (d) and held that the applicants were shareholders of the original company as their names continued to be on the "register of members". At page 143 it was observed that "under Sec. 536 (2) any transfer of shares in the Company or alterations in the status of its members made after the commencement of the winding up, required sanction of the Court. This section goes to show that members do not cease to be members on a Company being wound up nor do they cease to be members on receiving a return of capital... because handing over of the share certificates to the official liquidator does not amount to a surrender of shares to the Company".

In the case of member becoming insolvent, the insolvency does not deprive him of his right to vote in the company's general meetings or to participate as a signatory in requisition under section 169 or an application to the Court under section 397 or section 398, so long as the Official Assignee or Official Receiver does not get himself substituted in the register of members of the company in the place of the insolvent or sell the shares in the course of the administration of the insolvent's estate and the purchaser gets his name registered in the place of the insolvent, in the register of members of the company.

In *Wise v. Lansdell,* (1921) 1 Ch 420 (Ch D), it was held that in the case of a bankrupt whose name was still on the register of members of a company, as between himself and the company, the bankrupt, so long as his name remained on the register, was entitled to vote in respect of the shares, though as between himself and the mortgagees, he could vote only as they dictated. But the right to vote was held to be unimpaired as long his name appeared on the register. See also observation at p. 426 in *National Steel and General Mills v. Official Liquidator,* (1990) 69 Com Cases 416 at 426 (Del—DB).

If there is neither forfeiture nor termination of the membership of a person, a mere appropriation of his share capital towards the amount due by him to the company will not bring about a termination of membership. *N.K. Venkatesan v. Official Liquidator,* (1935) 5 Com Cases 459, 460 (Mad).

Where a person's name is entered in the register of members of a company as a shareholder and no proceedings have been taken to have his name removed from the register, he is entitled to take part in the meetings of the company and a resolution for reduction of capital cannot be invalidated on the mere ground that he was not really qualified to be a shareholder and to vote in the meeting, *Marwari Stores Ltd. v. Gouri Shankar Goenka,* (1936) 6 Com Cases 285 at 294 : AIR 1936 Cal 327.

Expulsion from membership

In the case of company limited by guarantee such as a social club, a political party organisation, a school committee, a chamber of commerce or professional, cultural, religious or other association, there is nothing in the Companies Act, 1956, to prevent the company including in its articles or regulations a provision for the expulsion of any

member if his acts or conduct should be considered detrimental to the interest of the company.

It is one of the requisites of a proper expulsion that the power should be exercised in the interest of the company as a whole and not in the interest of a shareholder or a group of shareholders. This principle has been **reiterated** by the Andhra High Court in *Gothami Solvent Oils Ltd. v. Mallina Bharathi,* (2001) 105 Com Cases 710 : (2001) 31 SCL 178 : (2001) 42 CLA 267 : (2001) 3 Comp LJ 127 : (2001) CLC 1377 (AP). The court could not find any material on record to hold that the decision to expel the shareholder was with any reasonable prospect of advantage to the company as a whole nor was it established that the activity of the shareholder and her husband in sending out various complaints resulted in any tangible damage to the company. There was no assurance that the shareholder or her husband would be stopped from sending the complaints against the company as a result of the expulsion. In the circumstances, the action in cancelling the membership of the shareholder would achieve no benefit or advantage to the company as a whole; consequentially, the same must be held to be illegal. The court emphasised that the power of expulsion must be exercised in absolute good faith in the interest of the company, a principle which is applicable to alteration of articles also. The court **upheld** on this point, the CLB decision in *Mallina Bharathi v. Gowthami Solvent Oils Ltd.,* (2001) 105 Com Cases 700 : (2001) 41 CLA 188 : (2001) 31 SCL 60 (CLB—SR).

For Forms of such articles, see Forms Nos. 185, 186 and 187, PALMER'S COMPANY PRECEDENTS Part I, 17th Edn., Page 650 *et seq.* In a decision of the Court of Chancery in England, *Gaiman v. National Association for Mental Health,* (1970) 2 All ER 362 (Ch D), it has been held that if, under the articles the directors have been given the discretion to exercise the power to expel any member, they can do so, even without giving the member prior notice of the charge against him and giving him an opportunity to show cause against such expulsion. With great respect to the learned Judge who decided that case, it must be said that the power of expulsion, even though it may have been given under the articles which bind each member of the company as a contract made by him with the company, being of a confiscatory nature, cannot be exercised without first giving that member a 'show-cause' notice and also giving him an opportunity to be heard. Whatever might be the reason for the decision in the aforesaid case, it is certainly unjust and opposed to all principles of natural justice to deprive a person of his right of membership without hearing him.

It appears that articles in case of an association not for profit or a company limited by guarantee, having no share capital, may provide for expulsion of its members. However, any such provision in a company having a share capital will be against the principles of corporate democracy and in violation of sections 100-104.

Sachar Committee Views.—Sachar Committee's view on the point which is reproduced below also subscribe to the same view : "One or two cases have been brought to our notice in which public limited companies have altered their Articles of Association enabling the Board of Directors to expel one or more members in certain circumstances. We are firmly of the opinion that this is a trend which ought not to be encouraged. Even assuming that this is within the scope of a company's power to prescribe in its Articles of Association that a member may be expelled, we think that such a power ought not to apply to public companies. Accordingly, we would recommend the insertion of a suitable provision in the Act prohibiting a company from expelling one or more of its members. It should, however, be clarified that this prohibition would not be applicable either to private limited companies or to section 25 companies." [*Sachar Committee Report* p. 61].

Department's views.—As regards the power of a company limited by shares to expel a shareholder, the following clarification issued by the Department of Company Affairs (*Circular No.* 32 of 1975) dated 1-11-1975 gives the Department's view:—

"Recently a case has come to the notice of the Central Government where a public limited company has amended its Articles of Association by including a clause by a special resolution passed at the Extraordinary General Meeting of the company empowering the Board of Directors of the Company to expel a member in a case where the Board is *prima facie* of the view that activities or conduct of the member is detrimental to the interests of the company or that by reason of his continuance as a member, it would be prejudicial to the future of the company. The question whether such an amendment of the Articles of Association of a company is valid has been under consideration of the Department. After considering the scheme of the Companies Act, the Department is of the view that amendment of Articles of Association of a company providing for expulsion of a member by the management is opposed to the fundamental principles of the company's jurisprudence and is *ultra vires* of the company. Such a provision is repugnant to the various provisions in the Companies Act pertaining to the rights of a member in a public limited company and cuts across the scheme of the Act as it has the effect of rendering nugatory the very powers of the Central Government under section 111 of the Companies Act, 1956 and the powers of the courts under sections 107 and 395 of the Act and is, therefore, void by the operation of the provisions of section 9 of the Act. The Articles of Association is a contract between the company and its members setting out the rights of members *inter se* under the contract, and expulsion of a member is not only a violation of this contract but it is also opposed to the principles of natural justice. Moreover, under section 23 of the Indian Contract Act, any agreement which is contrary to any law or opposed to public policy would be deemed to be unlawful and void. The Supreme Court in the case of *Bajaj Auto Ltd. v. N.K. Firodia,* (1971) 41 Com Cases 1 : AIR 1971 SC 321 has laid down the law as to the conditions on the basis of which directors could refuse a person to be admitted as a member of the company. The principles laid down by the Supreme Court in this case, even though pertaining to the refusal of a company to the admission of a person as a member of the company, are applicable even with greater force to a case of expulsion of an existing member. As under Article 141 of the Constitution the law declared by the Supreme Court is binding on all courts within the territory of India, any provision pertaining to the expulsion of member by the management of a company which is against the law as laid down by the Supreme Court will be illegal and *ultra vires*. In the light of the aforesaid position, it is clarified that assumption by the Board of Directors of a company of any power to expel a member by amending its Articles of Association is illegal and void."

It has been held that the views expressed in the *Circular No.* 32/75, dated 1-11-1975 (*Printed above*) cannot be directly enforced by a member of a company by means of a writ petition and also that the view point that the members cannot be expelled will not apply to temporary suspension of membership. Departmental instructions cannot be enforced against field officers by means of a writ petition by any member of a company. *Leela Kumar (K.) v. Government of India,* (1997) 27 Corpt LA 145 (Mad).

Expulsion when justifiable and relief against.—On a careful consideration of the subject in all its aspects, it would appear that there is nothing illegal or *ultra vires* in the exercise of a power of expulsion of the shareholder, if it is exercised *bona fide* to protect the interests of the company where the shareholder's act or conduct is considered to be detrimental or injurious to the interests of the company. An article giving such power is not necessarily invalid or *ultra vires*. The case of *Bajaj Auto Ltd. v. N.K. Firodia* relied on by the Department does not decide or throw light on the question whether a shareholder can or cannot be expelled from the company for good cause. There is no reason why, where a shareholder's act or conduct is so repugnant as to be considered detrimental to the interest of the company by, say, 90% of the shareholders (both in number and value of shares held), he should not by resolution of such majority in general meeting be expelled and his shares compulsorily transferred either to other willing members or any other person designated by the company, at the face-value or market value of the shares, whichever is higher. It will be open to the expelled member to seek relief through court and it cannot be contended that expulsion is a mere matter of internal or indoor management as it deprives a member of his personal rights. *Cf. Sidebottam v. Kershaw Leese & Co.,* (1920) 1 Ch 154.

Government companies: President or Governor as member

Department's Circular.—The undersigned is directed to refer to this Department's Office Memorandum No. 15/32/65-IGC, dated the 13th October, 1965 on the above subject and to state that certain Ministries of the Government of India and State Governments have, on receipt of the above communication, raised a query as to whether the President or the Governor of a State will be deemed to be a corporation sole for purposes of holding shares in Government companies. This matter has, therefore, been examined in detail and the clarification as under is given for information and guidance of all concerned.

2. This Department had advised in the above Office Memorandum that shares in a Government company cannot be registered in the name of a public office which is not a corporation sole as understood in law. Thus the shares in a company cannot be held in the name of the Collector of Central Excise or a Secretary to the Government of India, etc. This position may be followed in the case of holders of all public offices save as mentioned below.

3. The President or the Governor of a State functioning under the constitution is not a corporate sole, just as the Administrator-General constituted under the Administrators-General Act, 1963, is. As provided by Articles 77(1) and 166(1) of the Constitution, all executive action of the Government of India or the Government of a State shall be expressed to be taken in the name of the President or the Governor, as the case may be. "Executive action" or "executive power" has been broadly stated to be "the residue of Governmental functions that remain after legislative and judicial functions are taken away". Further, it appears that the said articles are confined to cases where the executive action is required to be expressed in the shape of a formal order or notification or any other instrument. When an executive decision affects an outsider or is required to be officially notified or communicated, it should be normally expressed in the form mentioned in these Articles, that is, in the name of the President or the Governor, as the case may be.

4. The acquisition or holding of shares in a company by the Government of India or a State Government is "executive action" as contemplated by Articles 77(1) and 166(1) of the Constitution and can, therefore, be made in the name of the President of India or the Governor of the State as the case may be.

5. In view of the above, shares in a Government company can be held in the name of the President of India or the Governor of a State. [*DCA No.* 15/32/65-IGC, dated 30th September, 1966.]

S. 42. Membership of holding company.—(1) Except in the cases mentioned in this section, a body corporate cannot be a member of a company which is its holding company and any allotment or transfer of shares in a company to its subsidiary shall be void.

(2) Nothing in this section shall apply—

(a) where the subsidiary is concerned as the legal representative of a deceased member of the holding company; or

(b) where the subsidiary is concerned as trustee, unless the holding company or a subsidiary thereof is beneficially interested under the trust and is not so interested only by way of security for the purposes of a transaction entered into by it in the ordinary course of a business which includes the lending of money.

(3) This section shall not prevent a subsidiary from continuing to be a member of its holding company if it was a member thereof either at the commencement of this Act or before becoming a subsidiary of the holding company, but except in the cases referred to in sub-section (2), the subsidiary shall have no right to vote at meetings of the holding company or of any class of members thereof.

(4) Subject to sub-section (2), sub-sections (1) and (3) shall apply in relation to a nominee for a body corporate which is a subsidiary, as if references in the said sub-sections (1) and (3) to such a body corporate included references to a nominee for it.

(5) In relation to a holding company which is either a company limited by guarantee or an unlimited company, the reference in this section to shares shall, whether or not the company has a share capital, be construed as including a reference to the interest of its members as such, whatever the form of that interest.

NOTES

Eng. Act, 1948 : Sec. 27
Eng. Act, 1985 : Sec. 23

Companies Act, 1956

Restrictions upon subsidiary.—This section adopts the provisions of section 27 of the Engligh Act on the recommendation of the Company Law Committee, which was as follows: "We recommend that the provisions of section 27 of the English Companies Act, 1948, be adopted. Under the section of the English Act, no subsidiary or its nominee can in future become a member of its holding company, except as a personal representative or a trustee. In the latter case, neither the holding company nor the subsidiary may have any beneficial interest under the trust except by way of security for the purpose of a transaction entered into in the ordinary course of a business, which includes the lending of money. In regard to subsidiaries, which are already members of their holding companies, they are permitted to retain their membership but can exercise no voting rights in future, except where they are personal representatives or trustees. Further, any allotment or transfer of shares in a company to its subsidiary is declared to be void. These salutary provisions constitute an attempt to maintain the separate operational identity of a holding company and its subsidiary thereby to preserve the respective shareholders' control over them. In the absence of any such provision, the affairs of a holding company and its subsidiary may, in the hands of unscrupulous company managers become inextricably involved and confused to the serious detriment of shareholders." (*Report :* para 40).

Object of section

The object of the section is to maintain the separate operational identity of a holding company and its subsidiaries and thereby preserve the respective shareholders' control over them. *Asian Investments Ltd., Re,* (1992) 73 Com Cases 517, 523 (Mad).

Scope of section

A subsidiary company cannot hold shares in or be a member of its holding company, and if it was a member before the commencement of this Act or before it became subsidiary, it has no right of vote at meetings of the holding company and what applies to a subsidiary applies also to a nominee of it.

In case a subsidiary comes within the exception provided by sub-section (2), its right to vote is not taken away ; that is to say, if the subsidiary holds the shares as the legal representative of a deceased member or if it holds them in the capacity of trustee of some other person not being the holding company or any subsidiary of it.

It may be noted that the section does not prohibit Company A holding 49 per cent of shares in Company B and Company B holding 49 per cent of shares in Company A. In such cases, without there being any relationship of holding company and subsidiary company, both companies may remain under the same control. In such cases, this section will not bite.

As sub-section (1) prohibits any allotment of shares to a subsidiary company, allotment by way of bonus shares also will be invalid. Sub-section (3) only permits the subsidiary to continue as member of the holding company, if it had already been a member of it before it became its subsidiary. The expression 'shall not allot any shares' prohibits the allotment of any kind of shares—rights shares or bonus shares.

Subsidiary's subsisting holdings in its holding company [Sub-section (3)]

Where a company was already holding some shares or other interest in a company of which it subsequently became a subsidiary, or at the commencement of the Act, that interest may be maintained, subject to the restriction that the subsidiary would have no voting rights at a meeting of its holding company, or at meetings of any class of the holding company's members.

A subsidiary company can buy shares in its holding company where it is a part of a scheme of amalgamation sanctioned by the court. *Himachal Telematics Ltd. v. Himachal Futuristic Communications Ltd.,* (1996) 86 Com Cases 325 (Del).

"Subsidiary Company" includes sub-subsidiary also [*vide* section 4(1)(c) and illustration].

§ See also Notes under S. 394 under the heading "Amalgamation involving violation of Ss. 42 and 77".

Nominee [Sub-section (4)]

This expression is not defined in the Act. It apparently means a holder of shares, having no beneficial interest in the shares, the whole beneficial interest remaining in one or more other persons.

'Shares' means 'interest' where no share capital [Sub-section (5)]

In case where the holding company is an unlimited company or a guarantee company, strictly speaking, there can be no acquisition of shares of the holding company by its subsidiary nor allotment of shares by the holding company to its subsidiary. In such cases, however, sub-section (5) requires that the section shall be construed as including a reference to the interest of the members as such in such holding company whatever may be the form of that interest. Thus in cases of such holding company, its subsidiary company cannot acquire interest similar to that of other members of such holding company.

There is no legal impediment to two or more independent companies, being formed by a few persons and then each company becoming the subsidiary and holding company of the other or others.

It would appear that the word "shares" in sub-section (1) would also include preference shares of the holding company. This can be inferred from the words "of any class of members" in sub-section (3) of the section.

Convertible or non-convertible debentures not hit by the section

Since debentures are not shares, it is clear that holding of debentures by the subsidiary in the holding company is not hit by s. 42. Furthermore, even convertible debentures are not hit by the section since what are allotted initially are only debentures and not shares. However, when the debentures get converted into shares, it would appear that the section gets attracted whether the conversion is compulsory or optional.

Holders of convertible debentures are not members until their debentures have been converted into shares and they are duly registered as shareholders.

ICSI Guidance Note on Compliance Certificate (August 2003)

Membership of Holding Company*

Check List

Check whether:

(i) the company is a member of a company which is its holding company;

(ii) the company which is a member of its holding company has been allotted any shares or acquired further shares after it became a subsidiary, as such allotment or transfer is void.

For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

* This matter is not directly referred to in the 33 paragraphs appended to the Form prescribed under the Companies (Compliance Certificate) Rules. The Check List given by the ICSI under the heading 'Check List for Other Compliances' is for the guidance of CSP who may, in the course of his scrutiny, come across non-compliance with regard to this matter. CSP need not qualify such non-compliance.

Private Companies

S. 43. Consequences of default in complying with conditions constituting a company a private company.—Where the articles of a company include the provisions which, under clause (iii) of sub-section (1) of section 3, are required to

be included in the articles of a company in order to constitute it a private company, but default is made in complying with any of those provisions, the company shall cease to be entitled to the privileges and exemptions conferred on private companies by or under this Act, and this Act shall apply to the company as if it were not a private company :

Provided that the [1][*Central Government*] on being satisfied that the failure to comply with the conditions was accidental or due to inadvertence or to some other sufficient cause, or that on other grounds it is just and equitable to grant relief, may, on the application[2] of the company or any other person interested and on such terms and conditions as seems to the [1][*Central Government*] just and expedient, order that the company be relieved from such consequences as aforesaid.

NOTES

Eng. Act, 1948 : Sec. 29. Previous Act : Sec. 154(3).

Note : As and when the Companies (Second Amendment) Act, 2002 (11 of 2003) comes into force, the power under sections 17, 18 and 19 shall become transferred to the Central Government to be exercised by it in place of the Company Law Board. The commentary and procedure should be read keeping this changeover in mind.

Companies (Amendment) Act, 1988

The power to give relief from the consequences under this section was originally vested with the court. By the Companies (Amendment) Act, 1988, this power has been conferred on the Company Law Board w.e.f. 31-5-1991.

Companies (Second) Amendment Act, 2002 [11 of 2003]

The powers under s. 43 which were earlier with the CLB have been conferred on the Central Government by the Second Amendment Act, 2002. Companies (Amendment) Bill, 2001 had proposed to confer CLB's power on the Tribunal. Notes on Clauses stated:

Notes on clauses.—This clause seeks to amend sections 18, 19, 43, 49, 55A and 58A of the Companies Act, 1956 relating to alteration of memorandum of association to be registered within three months, effect of failure of such registration, consequences of default in complying with conditions constituting a company as private company, investments of company to be held in its own name, powers of Securities and Exchange Board of India so far as they relate to issue and transfer of securities and acceptance of deposits without issuing advertisement. It is proposed to confer the powers of the Company Law Board in the aforesaid sections upon the Tribunal. These amendments are of consequential nature. (*Clause* 8 of the Companies (Amendment) Bill, 2001).

Consequences of default

The immediate consequence of default in complying with provisions relating to a private company are that the provisions of the Act will apply to it as if it were not a private company and all the results flowing therefrom will follow.

One of the results which follows is that the formal requirements of a public company must be complied with. A failure to do so may involve penalties. *Laxman Bharmaji v. Emperor,* AIR 1946 Bom 18 : (1946) 16 Com Cases 31. When under this section a pri-

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1. **Subs. for "Company Law Board" by the Companies (Second Amendment) Act, 2002 (11 of 2003), s. 8. Earlier subs. by the Companies (Amendment) Act, 1988, (w.e.f. 31-5-1991) *vide* GSR dated 31-5-1991, for the word "Court".**
2. Application fee Rs. 200/- as per Company Law Board (Fees on Applications & Petitions) Rules, 1991. For the text, see *Appendix* 6.

vate limited company is converted into a public limited company the company's identity is not changed, but only its nature. A private limited company can be converted into a public limited company by merely changing two or three clauses of its articles of association, the original articles of association continuing to be operative. A company can alter some of its articles of association. Such an alteration does not affect the identity of the company. *All India Reporter Ltd. v. Ramachandra,* AIR 1961 Bom 292 at 298.

The section is very general, and it does not impose any time-limit, and there is no special penalty, except the penalties that may be imposed, by reason of default in complying with the provisions of the Act as applicable to a public company.

Petition before CLB

Petition praying for relief from consequences of failure to comply with conditions constituting it a private company be made to the Regional Bench of the Company Law Board in Form No.1 of Annexure II to the CLB Regulations, 1991 along with an application fee of Rs. 200/-and accompanied by the following documents:

(1) Copy of memorandum and articles of association;

(2) Copy of document showing that the default has been committed in complying with the conditions laid down in clause (iii) of sub-section (1) of Section 3;

(3) Affidavit verifying the petition;

(4) Bank draft evidencing payment of application fee;

(5) Memorandum of appearance, shall be filed in Form 5 of Annexure 1.

§ For text of the Company Law Board Regulations, 1991 refer *Appendix* 3.

Secretarial Practice Notes : Private Companies, consequences of default

Check whether the private company had committed default and came under this section ? If so, seek relief from CLB.

Documents involved are: (1) Memorandum and Articles of Association of the Company; (2) Certificate of incorporation; (3) Minutes of Board Meetings; (4) Register of Members; (5) Correspondence with the Registrar of Companies.

[1][**S. 43-A. Private company to become public company in certain cases.**— (1) Save as otherwise provided in this section, where not less than twenty-five per cent of the paid-up share capital of a private company having a share capital, is held by one or more bodies corporate, the private company shall,—

(a) on and from the date on which the aforesaid percentage is first held by such body or bodies corporate, or

(b) where the aforesaid percentage has been first so held before the commencement of the Companies (Amendment) Act, 1960, on and from the expiry of the period of three months from the date of such commencement unless within that period the aforesaid percentage is reduced below twenty-five per cent of the paid-up share capital of the private company,

become by virtue of this section a public company:

Provided that even after the private company has so become a public company, its articles of association may include provisions relating to the matters specified

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1. Ins. by Act 65 of 1960, s. 14.

in clause (iii) of sub-section (1) of section 3 and the number of its members may be, or may at any time be reduced, below seven:

Provided further that in computing the aforesaid percentage, account shall not be taken of any share in the private company held by a banking company, if, but only if, the following conditions are satisfied in respect of such share, namely:—

(a) that the share—

(i) forms part of the subject-matter of a trust,

(ii) has not been set apart for the benefit of any body corporate, and

(iii) is held by the banking company either as a trustee of that trust or in its own name on behalf of a trustee of that trust; or

(b) that the share—

(i) forms part of the estate of a deceased person,

(ii) has not been bequeathed by the deceased person by his will to any body corporate, and

(iii) is held by the banking company either as an executor or administrator of the deceased person or in its own name on behalf of an executor or administrator of the deceased person;

and the Registrar may, for the purpose of satisfying himself that any share is held in the private company by a banking company as aforesaid, call for at any time from the banking company such books and papers as he considers necessary.

[2][*Explanation.*—For the purposes of this sub-section, "bodies corporate" means public companies, or private companies which had become public com panies by virtue of this section.]

[3][(1-A) Without prejudice to the provisions of sub-section (1), where the average annual turnover of a private company, whether in existence at the commencement of the Companies (Amendment) Act, 1974, or incorporated thereafter, is not, during the relevant period, [4][*less than such amount as may be prescribed*[5]], the private company shall, irrespective of its paid-up share capital, become, on and from the expiry of a period of three months from the last day of the relevant period during which the private company had the said average annual turnover, a public company by virtue of this sub-section:

Provided that even after the private company has so become a public company, its articles of association may include provisions relating to the matters specified in clause (iii) of sub-section (1) of section 3 and the number of its members may be, or may at any time be reduced, below seven.

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2. Ins. by the Companies (Amendment) Act, 1988, s. 7(a) w.e.f. 15-6-1988 *vide* GSR No. 559(E), dt. 10-6-1988.
3. Ins. by the Companies Amendment Act (XL of 1974), s. 6 (w.e.f. 1-2-1975).
4. Subs. by the Companies (Amendment) Act, 1988, s. 7(b) w.e.f. 15-6-1988 *vide* GSR No. 559(E) dt. 10-6-1988 for the words "less than rupees one crore".
5. W.e.f. 23-2-1999 the average annual turnover shall be not less than Rs. 25 crores *vide* GSR No. 130(E), dt. 23-2-1999, earlier w.e.f. 18-9-1990 the average annual turnover was not less than Rs. 10 crores *vide GSR No. 795(E), dated 18-9-1990.* See R. 4C of the Companies (Central Government's) General Rules and Forms, 1956 (*Appendix* 1).

(1-B) Where not less than twenty-five per cent of the paid-up share capital of a public company, having share capital, is held by a private company, the private company shall,—

(a) on and from the date on which the aforesaid percentage is first held by it after the commencement of the Companies (Amendment) Act, 1974, or

(b) where the aforesaid percentage has been first so held before the commencement of the Companies (Amendment) Act, 1974, on and from the expiry of the period of three months from the date of such commencement, unless within that period the aforesaid percentage is reduced below twenty-five per cent of the paid-up share capital of the public company;

become, by virtue of this sub-section, a public company, and thereupon all other provisions of this section shall apply thereto:

Provided that even after the private company has so become a public company, its articles of association may include provisions relating to the matters specified in clause (iii) of sub-section (1) of section 3 and the number of its members may be, or may at any time be reduced, below seven.]

[6][(1C) Where, after the commencement of the Companies (Amendment) Act, 1988, a private company accepts, after an invitation is made by an advertisement, or renews, deposits from the public, other than its members, directors or their relatives, such private company shall, on and from the date on which such acceptance or renewal, as the case may be, is first made after such commencement, become a public company and thereupon all the provisions of this section shall apply thereto:

Provided that even after the private company has so become a public company, its articles of association may include provisions relating to the matters specified in clause (iii) of sub-section (1) of section 3 and the number of its members may be or may at any time be reduced below seven.]

(2) Within three months from the date on which a private company becomes a public company by virtue of this section, the company shall inform the Registrar that it has become a public company as aforesaid, and thereupon the Registrar shall delete the word "Private" before the word "Limited" in the name of the company upon the register and shall also make the necessary alterations in the certificate of incorporation issued to the company and in its memorandum of association.

[7][*(2A) Where a public company referred to in sub-section (2) becomes a private company on or after the commencement of the Companies (Amendment) Act, 2000, such company shall inform the Registrar that it has become a private company and thereupon the Registrar shall substitute the word "private company" for the word "public company" in the name of the company upon the register and shall also make the necessary alterations in the certificate of incorporation*

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6. Ins. by the Companies (Amendment) Act, 1988, s. 7(c) w.e.f. 15-6-1988 *vide* GSR No. 559(E), dt. 10-6-1988.
7. Ins. by the Companies (Amendment) Act, 2000 (53 of 2000), s. 12, (w.e.f. 13-12-2000).

issued to the company and in its memorandum of association within four weeks from the date of application made by the company.]

(3) Sub-section (3) of section 23 shall apply to a change of name under sub-section (2) as it applies to a change of name under section 21.

(4) A private company which has become a public company by virtue of this section shall continue to be a public company until it has, with the approval of the Central Government and in accordance with the provisions of this Act, again become a private company.

(5) If a company makes default in complying with sub-section (2), the company and every officer of the company who is in default, shall be punishable with fine which may extend to five hundred rupees for every day during which the default continues.

(6) [8][* * * *]

(7) [9][* * * *]

[10][(8) Every private company having a share capital shall, in addition to the certificate referred to in sub-section (2) of section 161, file with the Registrar along with the annual return a second certificate signed by both the signatories of the return, stating either—

(a) that since the date of the annual general meeting with reference to which the last return was submitted, or in the case of a first return, since the date of the incorporation of the private company, no body or bodies corporate has or have held twenty-five per cent or more of its paid-up share capital,] [11][* * * *]

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8. Omitted sub-section (6) by the Companies (Amendment) Act, 1988, s. 7(d) w.e.f. 15-6-1988 *vide* GSR No. 559(E) dt. 10-6-1988, the words "(6) Nothing in this section shall apply—
   (a) to a private company of which the entire paid-up share capital is held by another single private company or by one or more bodies corporate incorporated outside India; or
   (aa) to a private company in which shares are held by one or more bodies corporate incorporated outside India, which or each of which, if incorporated in India, would be a private company, within the meaning of this Act, if the Central Government, on an application made to it in this behalf by that private company, by order so directs; or
   (b) to any other private company if, but only if, each of the following conditions is satisfied, namely :—
      (i) that the body corporate or each of the bodies corporate holding shares in the private company is itself a private company (hereinafter in this section referred to as a shareholding company),
      (ii) that no body corporate is the holder of any shares in any such shareholding company,
      (iii) that the total number of shareholders of the shareholding company, or as the case may be, of all the shareholding companies together with the individual shareholders [not including the persons referred to in sub-clause (b) of clause (iii) of sub-section (1) of section 3], if any, of the private company, does not exceed fifty."
9. Omitted by the Companies (Amendment) Act, 1988, s. 7(d) w.e.f. 15-6-1988 *vide* GSR No. 559(E) dt. 10-6- 1988, the words "(7) Every shareholding company shall, as soon as may be, inform the private company referred to in clause (b) of sub-section (6) about every change in the membership of the shareholding company taking place by a change in the number of its individual shareholders or by any body corporate becoming the holder of any of its shares."
10. This sub-clause has been added by the Companies (Amendment) Act (31 of 1965) (w.e.f. 15-10-1965).
11. The word "or" omitted by the Companies (Amendment) Act, 1988 (w.e.f. 15-6-1988).

(b) [12][* * * *]

[13][(c) that the private company, irrespective of its paid-up share capital, did not have, during the relevant period, an average annual turnover of [14][such amount as is referred to in sub-section (1A) or more]

[15][*(d)* that the private company did not accept or renew deposits from the public.]

[16][(9) Every private company, having share capital, shall file with the Registrar along with the annual return a certificate signed by both the signatories of the return, stating that since the date of the annual general meeting with reference to which the last return was submitted, or in the case of a first return, since the date of the incorporation of the private company, it did not hold twenty-five per cent or more of the paid-up share capital of one or more public companies.

[15][(10) Subject to the other provisions of this Act, any reference in this section to accepting, after an invitation is made by an advertisement, or renewing deposits from the public shall be construed as including a reference to accepting, after an invitation is made by an advertisement or renewing deposits from any section of the public, and the provisions of section 67 shall, so far as may be, apply, as if the reference to invitation to the public to subscribe for shares or debentures occurring in that section, includes a reference to invitation from the public for acceptance of deposits.]

Explanation.—For the purposes of this section,—

(a) "relevant period" means the period of three consecutive financial years,—

(i) immediately preceding the commencement of the Companies (Amendment) Act, 1974, or

(ii) a part of which immediately preceded such commencement and the other part of which immediately, followed such commencement; or

(iii) immediately following such commencement or at any time thereafter;

(b) "turnover", of a company, means the aggregate value of the realisation made from the the sale, supply or distribution of goods or on account of services rendered, or both, by the company during a financial year.]

[17][(c) "deposits" has the same meaning as in section 58A.]

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12. Omitted clause (b), by the Companies (Amendment) Act, 1988, s. 7(e)(ii) w.e.f. 15-6-1988 *vide* GSR No. 559(E) dt. 10-6-1988, the words "(b) that though since the aforesaid date one or more bodies corporate have held twenty-five per cent, or more of its paid-up share capital, the provisions of this section do not apply to it because it is a private company referred to in clause (a) or clause (b) of sub-section (6)."
13. Ins. by the Companies (Amendment) Act, (XLI of 1974), s. 6 (w.e.f. 1-2-1975).
14. Subs. by the Companies (Amendment) Act, 1988, s. 7(e)(iii) w.e.f. 15-6-1988 *vide* GSR No. 559(E) dt. 10-6- 1988, for the words "rupees one crore or more."
15. Ins. by the Companies (Amendment) Act, 1988, s. 7(e)(iv) w.e.f. 15-6-1988 *vide* GSR No. 559(E), dt. 10-6-1988.
16. Ins. by the Companies (Amendment) Act (XLI of 1974), s. 6 (w.e.f. 1-2-1975).
17. Ins. by the Companies (Amendment) Act, 1988, s. 7(g) w.e.f. 15-6-1988 *vide* GSR No. 559(E) dt. 10-6- 1988.

[18][*(11) Nothing contained in this section, except sub-section (2A), shall apply on and after the commencement of the Companies (Amendment) Act, 2000*].

NOTES

Companies (Amendment) Act, 2000

A substantial change of far-reaching importance has been made by inserting sub-section (11) by the Amendment Act, 2000 to render the provisions of this Section inoperative on and after the commencement of the amendment. Accordingly, the concept of deemed public company under this section introduced by the Companies (Amendment) Act, 1974 has now been abolished, based on recommendations of the Working Group on the Companies Act, 1956.

Recommendations of Parliamentary Standing Committee[19]

Government's views.—Entire Section 43A may not be deleted. The provision of Section 43A(4) may be retained so that deemed public companies may submit the Certificate of Incorporation to Registrar of Companies for correction by adding the word "Private' before the word 'Limited' in the name as indicated in the Certificate of Incorporation. The Registrar will do so forthwith. No fee need be paid for this change as it is a statutory requirement on amendment of the Companies Act, 1956.

Committee's recommendation.—The Committee recommends the Clause 12 [of the Companies (Second Amendment) Bill, 1999] may be amended as agreed to by the Government [*Para 16.14*]. As regards granting of approval forthwith by the ROC for changing a deemed public company to private company, it may be prescribed in the rules that the said approval will be accorded within four weeks time [*Para 16.15*]. Sub-section (2A) reflects these recommendations.

Option of deemed Public Company to revert to Private Company [Sub-section 2A]

As per newly inserted sub-section (2A) by the Amendment Act, the procedure has been prescribed for change of character of a deemed public company to that of a private company. The company shall inform the Registrar that it has become a private company on the commencement of the Companies (Amendment) Act, 2000, and, thereupon, the Registrar shall make necessary changes in the certificate of incorporation and Memorandum of Association of the company within 4 weeks from the date of application made by the company. Sub-section (2A), as enacted, required the Registrar, to substitute the word "private company" for the word "public company", instead the word 'private' should have been added before the word 'limited' as part of the name of the company.

Private Companies Not reverting deemed as Public Company

Deemed public companies who do not exercise this option of reverting back to private companies are to be regarded as public companies. The Government has issued the following circular in this context:

Departments Circular No. 23/2002 dated 30-9-2002.—The Registrar of NCT of Delhi and Haryana has sought a clarification on the applicability of Section 43A(2A) on the erstwhile deemed public companies (when Section 43A was in operation prior to the Companies (Amendment) Act, 2000, which came into force w.e.f. 13.12.2000), to those public companies which are subsidiaries of foreign body corporates. The matter has been examined in the Department.

2. After amendment of the erstwhile Section 43A, since the provisions of Section 4 of the Companies Act are independent, a private company, being a subsidiary of a foreign body corporate, which, if incorporated in India, would not be a public company. As such, these deemed public companies are entitled to

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18. Sub-section 11 inserted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 12 (w.e.f. 13-12-2000).

19. 64th Report on Companies (Second Amendment) Bill, 1999.

revert back to their initial status of private limited companies as the effect of Section 43A has been nullified by the amendment referred to.

3. Section 4(7) of the Act was an exemption available to Indian private companies when foreign body corporates were holding 100% share in them to retain their "private" status. After amendment of Section 43A, such exemption is not required. Therefore, applications under Section 43A(2A) shall be dealt with independent of section 4(7) of the Act. The legal position in the above circumstances would be that a private company would be the subsidiary of another private limited company even if the holding company happens to be a foreign body corporate and these companies do not need the exemption provided in Section 4(7) of the Act. Therefore, the private company status of such companies is a statutory one, and takes effect automatically. All that the company is required to do is to make an application to the Registrar that the company has become a private company and there upon the Registrar shall substitute the words "private limited" in lieu of the words "public limited".

4. Since no time limit has been prescribed in the statute for the companies to revert back, the Department has already issued a departmental circular no. 3/2002 dated 24.7.2002 (F.No.17/4/2002-CL.V) (*Copy Enclosed*) wherein it has been clarified that those companies which do not approach the Registrar of Companies seeking reversion back to private company status, are deemed to have chosen to remain as public companies. [*F. No. 17/26/2002 – C : L.V. General Circular No. 23/2002 dated 30-9-2002*]

IMPORTANT NOTE

This section has been made inoperative by the Companies (Amendment) Act, 2000. [See sub-s. (11)]. This third category of companies, which the section had created would cease to exist after the enforcement of the Amendments [*w.e.f. 13-12-2000*]. However, the whole commentary has been retained 'for guidance as to pending' matters.

Companies (Amendment) Act, 1960

Committee Report on the need for S. 43-A.—The section was originally added by the Companies Amendment Act, 1960 and the object was thus stated in the Notes on the relevant clause of the Bill: "Clause 15.—The amendment proposed, implements the recommendation in para 23 of the report that private companies, which employ public money to an appreciable extent, should be subject to the same restrictions and limitations as to disclosure and otherwise, as apply to public companies. It is proposed to exempt a private company which is wholly owned either by another private company registered in India or by one or more foreign companies from the operation of the new requirement."

Para 23 of the *Report* of the Companies Act Amendment Committee, referred to above stated as follows : "Private companies are exempted from the operation of several sections of the Act and enjoy certain privileges, principally on the ground that they are family concerns in which the public is not directly interested. It is, however, well known that there are many private companies with large capital doing extensive business and controlling a number of public companies. This is made possible because funds of other companies, public and private, are invested in such private companies. As public money is invested in such companies there is no reason for treating such companies, as private companies. The problem of private companies has always been somewhat difficult. On the one hand, there are genuine private companies which are nothing but glorified partnerships and, on the other, there are private companies whose operations, financial and industrial, are far wider than those of many public companies. To meet this problem, *the Cohen Committee* created the category of exempted private companies but the relevant provisions in the English Act are very complicated. It was strongly urged upon us that the several exemptions granted to and the privileges enjoyed by private companies should be withdrawn, as they are abused. But to withdraw them from all private companies may cause hardship to genuine small private companies. At the same time, there is no doubt that private companies, which employ public money directly or indirectly to a considerable extent, should be subject to the same restrictions and limitations as to disclosure and otherwise as apply to public companies."

The section enacted by Parliament in 1960 was drafted by the Joint Committee on the Bill, and they reasoned as follows: "In respect of this clause it was contended that there was no justification for deeming a private company as a public one when twenty-five per cent or more of its shares were held by one or more private companies, because such a company might not employ any public money directly or indirectly particularly when the aggregate individual membership of the concerned company including the individual members of the shareholding private companies did not exceed 50. The Committee think that this contention is not without substance. They, therefore, feel that the restriction imposed under this clause should not apply to any private company if (i) the body corporate or each of the bodies corporate holding shares in the private company is itself a private company, (ii) no body corporate holds any shares in any of the shareholding companies and (iii) the total number of individual shareholders of the shareholding company or companies together with the individual shareholders of the private company does not exceed 50, which number should be computed in the same manner as is done in the case of a private company under section 3(1)(iii)(b) of the Act.

The Committee further feel that in computing the relevant percentage no account should be taken of any shares in the private company held by a banking company either as a trustee for any individual or as an executor or as an administrator of a deceased person.

The Committee also consider it unnecessary to require a private company which has become a public company to pass a resolution for the change of its name. The purpose will be served if the company informs the Registrar about the conversion within a period of three months." (*Report of Joint Committee*, para 22.)

These modifications by the Committee were accepted and incorporated in the section.

Companies (Amendment) Act, 1974

In the light of the experience gained from the application of the section since 1960, it was felt that some further amendments of the section were necessary for making it more effective in achieving its object and accordingly sub-sections (1-A), (1-B), clause (c) of sub-section (8), sub-section (9) and the *Explanation* at the end have been added by the Companies Amendment Act, 1974. The provisions in the original Bill were considered rather drastic by the Joint Committee of Parliament who felt that they would hamper the formation and growth of private companies in the private sector and so moderated them in the form in which they have been enacted as aforesaid.

As regards sub-section (1) the recommendation of the Committee, was that "the reduction of the percentage of shareholding from twenty-five to ten is likely to hamper the formation and growth of private limited companies in the small scale sector, especially in the rural areas and therefore the provisions of section 43-A (1) should not be disturbed. (*Report* : Para 21(a)).

As regards sub-section (1-A), "private companies which are less capital intensive but have a considerable consumer and employee interest because of its high turnover should be brought within the ambit of deemed public companies irrespective of its paid-up share capital. The Committee therefore recommend that a private company, irrespective of its paid-up share capital, shall become a public company if it has an average annual turnover of one crore of rupees. The Committee have therefore inserted new sub-section (1-A) after sub-section (1) to achieve these objectives" (*Report* : Para 21(a)).

Sub-section (1-B): As regards this, the Joint Committee said "The Bill, as originally introduced, sought to provide that a private company holding ten per cent or more of a paid-up share capital of a public company will be deemed to be a public company. The Committee felt that the fixation of the percentage at ten is likely to hamper the growth and formation of public companies. The Committee therefore recommend that the percentage be increased to twenty-five. The sub-clause has been amended accordingly." (*Report* : Para 21(b)).

Clause (c) of sub-section (8): "The Committee feel that private companies which do not have an average annual turnover of rupees one crore or more should file with the Registrar a certificate to that effect". (*Report* : Para 21(d)).

Sub-section (9): "The Committee feel that every private company, having share capital should file with the Registrar, along with the annual return, a certificate signed by both the signatories of the annual return, stating that since the date of the annual general meeting with reference to which the last annual return was submitted, or in the case of a first return, since the date of the incorporation of the private company, it did not hold twenty-five per cent or more of the paid-up share capital of one or more public companies". (*Report* : Para 21(e)).

The framers of the Amendment Act of 1974 overlooked the fact that the insertion of sub-section (1-A) without amending sub-section (6) created the following anomalies:—

(i) that the opening phrase of sub-section (6) ("nothing in this section shall apply .....") severely restricted in application of the new sub-section (1-A).

(ii) that sub-section (9) which was inserted by the same Act (41 of 1974) required every private company which held more than 25% of the paid-up share capital of a public company to solemnly make a declaration that, it did not hold more than 25% of the share capital of any public company, which would be patently false, if the company did hold more than 25% but continued to be a private company by virtue of sub-section (6).

Both these anomalies were removed by the deletion of sub-sec. (6) by the Amendment Act of 1988.

Companies (Amendment) Act, 1988

The *Sachar Committee* suggested that private companies be prohibited from accepting deposits or borrowing money from the members of the public, except from their own directors, shareholders and their relatives (Para 4.5). The said recommendation has been adopted in the Companies (Amendment) Act, 1988, besides others, as clarified in clause 7 of Notes on clauses:

"Sub-clause (a)—The value of average annual turn-over of rupees one crore as the ceiling for deeming a private company as public company in section 43A is being substituted to provide for a ceiling that may

be prescribed. Further the provision for laying down absolute monetary ceilings are being substituted by ceilings to be prescribed by rules.

Sub-clause (b)—This sub-clause provides that private company which accepts deposits from the public should be deemed to be a public company.

Sub-clause (c)—Sub-sections (6) and (7) of section 43A are sought to be deleted as the exemption contained therein have been found to render the other provisions of the section nugatory.

Sub-clauses (d), (e) and (f)—The amendments proposed in these sub-clauses are of consequential nature."

Explanation to sub-section (1) was inserted while moving official amendment before Rajya Sabha.

Scope of section

A deemed public company under section 43-A is not a public company for all purposes. The articles of a section 43-A company may continue to include provisions relating to restriction on transfer of shares, limitation on the number of its members to 50, and prohibition for invitation to the public to subscribe for its shares, which are typical characteristics of a private company. Therefore, the expression, 'public company' in section 3(1)(iv) cannot be equated with a 'private company which has become a public company by virtue of section 43-A ! The number of members of a public company cannot fall below 7 without attracting the serious consequences provided for by section 45 (personal liability of members for the company's debts) and section 433(d) (winding up in case the number of members falls below 7). A section 43-A company can still maintain its separate corporate identity *qua* debts even if the number of its members is reduced below seven and is also not liable to be wound up for that reason. A section 43-A company cannot be incorporated and registered as such under the Act. It is registered as a private company and becomes, by operation of law, a public company. The contingencies in which a private company becomes a public company by virtue of section 43-A [mentioned in sub-sections (1), (1A), (1B) and (1C)] read with the provisions of sub-section (4) of that section show that it becomes and continues to be a public company so long as the conditions in sub-section (1), (1A), (1B) or (1C) are applicable. The proviso to each of these sub-sections clarifies the legislative intent that such companies may retain their registered corporate shell of a private company but will be subjected to the discipline governing public companies. Section 43-A did not adopt the language either of section 43 or section 44. Under section 43, where default is made in complying with the provisions of section 3(1)(iii), a private company shall cease to be entitled to the privileges and exemptions conferred on private companies by or under the Act, and the Act shall apply to the company as if it were not a private company. Under section 44, where a private company alters its articles in such a manner they no longer include the provisions, which under section 3(1)(iii) are required to be included in the Articles in order to constitute it a private company, the company shall as on the date of the alteration cease to be a private company. If a section 43-A company were to be equated in all respects with a public company, that is a company which does not have the characteristics of a private company, Parliament would have used language similar to the one in section 43 or section 44. Sections 174 and 252, which deal respectively with quorum for meetings and minimum number of directors, recognise expressly the separate existence of public companies which have become such by virtue of section 43A, *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.*, (1981) 51 Com Cases 743 : AIR 1981 SC 1298.

Department's views.—A private company which becomes a public company under section 43-A, is required to comply with all the provisions of the Act except those expressly excluded. The provisions of sections 12(1) and 45 which require a public company to have at least 7 members will not apply and its articles of association may continue to contain a provision similar to that in section 3(1)(iii), which is applicable to private companies. Section 44 also is not applicable to such a company and it will not be required to file a statement in lieu of prospectus. The provisions of section 269/388 will not apply to a person holding the office of managing director or whole-time director or manager of such a company for a period not exceeding 5 years from the date of appointment, when it was private company, but the restrictions contained in sections 198, 309, 310 and 311 would automatically be applicable to such companies from the day they become deemed public companies. In case, the existing appointment of managerial personnel is for an indefinite period, then the appointment will be taken to be for 5 years from the date when the company becomes a public company. (*Circular No.* 32/13/73-CL-III, dated 25-6-1975). Full text of the Circular containing Queries and answers given by the department is reproduced hereunder:

Full text of Circular.—QUERIES: (i)(a) Consequent upon becoming a deemed public limited company under the amended section 43A will it be necessary for the company to get an approval from the Central Government for the continuation of the appointment of its Managing Director, whole-time Directors already in position, or on the analogy of the provisions contained in sub-section (2) of Section 269 applicable to an "existing company", the present tenure of the continuing directors may remain undisturbed and the approval of the Central Government will be necessary for any new appointment or reappointment only on expiry of the existing tenure of the continuing directors.

(b) What will be the position if the orders appointing them only say that their appointment is until further orders and no fixed tenure is indicated there against. In such a case, would it be correct to assume that in terms of Section 317 they can continue for a period of five years from the date of company becoming a deemed public company.

(ii) Have the companies, having losses or inadequate profits, on becoming deemed public limited under section 43A, to apply for approval for minimum remuneration to be paid to their Managing/Whole-time Directors. If so, what is the time-limit within which such applications should be submitted by such companies after their coming within the purview of Section 43A of the Act.

(iii) What would be the position of loans and advances already given in excess of the limits laid down in Section 370(1) of the Companies Act, 1956 in case of companies on becoming deemed public limited companies under Section 43A, of this Act. Would it be correct to assume that the past loans and advances would not be affected though for future loans and advances they will have to seek necessary approval from the Central Government apart from complying with other formalities as laid down.

Answers: (1) The existing appointment of Managing Director or the whole-time Director would not require the approval of the Central Government now, but it will be necessary at the time of the next appointment. In case the existing appointment is for an indefinite period, *i.e.*, until further orders, then, unless the appointment is terminated earlier, the period of appointment will be taken as five years from the date of the company becoming a public company. (Since the amendment of 1988 approval is necessary only where the terms and conditions prescribed by the Schedule XIII have to be departed from).

(2) In the event of inadequacy of profit, the company can pay the minimum remuneration after obtaining the approval of the Central Government under Section 198(3) of the Act and the application for the purpose has to be made within a reasonable time from the date of the company becoming a Public Company under Section 43A.

(3) Compliance with section 370(5).—On the principle underlying the provisions of section 370(5) of the Act, the company will have to recover the loans taken or withdraw the guarantee within a period of six months from the date of becoming a public company. [*Department's F. No.* 32/13/75-CL-III, dated 25-6-1975].

Deemed public company under sub-section (1) [25% or more holding by public company]

Prior to the Amendment Act of 1988, in case 25% or more of the paid-up capital of a private company was held by one or more public or private companies or other bodies corporate (such as, any foreign company as defined in section 592 or Indian or Foreign Corporations) the private company by reason of such holding, subject to the second proviso, became a public company from the date on which the aforesaid percentage was held. After the Amendment Act of 1988 (w.e.f. 15-6-1988), by virtue of the *Explanation* to sub-section (1), in case 25% or more of the share capital of a private company is held by another private company (which is not a deemed public company under section 43A) or by a foreign company, it will not change the status of the investee private company. Thus, now for purposes of sub-section (1), shareholding by a public company or a deemed public company is only relevant.

"The word 'held' used in sub-section (1) and elsewhere in section 43A does not mean "beneficially held" since companies are not permitted under section 153 of the Act to recognise trust or nominee holdings. Nominee holdings however are permissible to the extent they are provided for in sub-sections (2) and (3) of section 49 and companies which seek exemption from the provisions of section 43A under sub-section (6)(a) thereof would not be entitled to such exemption unless holdings by nominees of the patent company are restricted to what is permitted to under sections 49(2) and 49(3). For this limited purpose, the Department has construed the word 'company' appearing in these two sub-sections to include a 'Body Corporate'." (*Circular No.* 48 (50)-CL-IV/61, dated 12-2-1962).

In computing the aforesaid percentage of 25% account shall not be taken of any share held in the private company by a banking company subject to the conditions specified in the second proviso.

Computation of percentage of shareholding for purpose of s. 43A(I)

Department's Clarification

Query: According to section 43A, where not less than 25% of the paid-up share capital of a private company is held by one or more body corporate, the private company shall be deemed to be a public company subject to the other provisions of the section. The second proviso to clause (b) of sub-section (1) of the said section provides that in computing the said 25% share holding, account is not to be taken of any share in the private company held by a banking company if, *inter alia*, such share is held by the banking company either as a trustee of a trust or in its own name on behalf of a trustee of that trust. The Registrar of Companies should construe this proviso in such a manner that in computing the required percentage of share holding for the purpose of section 43A the shares held by a banking company on behalf of a trustee of a trust should not be taken into account even if there is no written trust deed in respect of such holdings.

Answer: The Department's view is that it is not possible to accede to the request mentioned above as the Registrar must have evidence to satisfy himself that the banking company is a trustee or that it is holding the shares on behalf of a person in his capacity as a trustee and that the share forms subject matter of the trust. (Extract from queries raised by the Indian Merchants Chamber in a memorandum submitted to the Department on 31-7-1962 and the Department's Views thereon. *Company News and Notes*, dated July 1, 1963).

Share Capital means both equity and preference capital.—For purposes of section 43A share capital means both equity and preference capital. Even if 25% or more of the preference capital of a private company is held by a public company or a deemed public company, the private company becomes a deemed public company. In the same way if 25% or more of the preference capital of a public company is held by a private company that private company becomes a "deemed public company". This holding of 25% or more can also be spread between equity capital and preference capital.

Formalties to be complied with on conversion

Department's view.—On a query to department: "There are no procedural details given in the new section 43A which made private companies/public companies in certain cases. Is it sufficient that the Registrar is intimated? What are the other formalities to be complied with?"

The Department of company affairs expressed the following views: "When a private company becomes a public company due to the provisions of section 43A(1), then by virtue of section 43A(2) the said company is required to:—

(i) file a declaration with the Registrar;

(ii) change its name;

(iii) bring its articles in consonance with the requirements applicable to a public company; and

(iv) take such other steps as would be necessary in regard to the number of its directors, members, etc." [*Letter No.* 8/16(1)/61-PR, dated 9-5-1961].

Deemed public company under sub-section (1A) [Turnover]

Department's explanation of 'Public Interest'.—It has been noticed that the term "public interest in companies" is being given a restricted meaning to cover only shareholdings of public institutions or the Government. Thus a private limited company or a closely-held company is said to involve no public interest. This is an outmoded concept of public interest in a company. Public interest is to be determined also on the basis of the interest of creditors, consumers, employees and the State in the undertaking of the company, in addition to the shareholdings as such. It is on this account, that "turnover" has been incorporated in the Companies (Amendment) Act, 1974 as a factor for converting a private company into a public company under section 43A. This point may be borne in mind while making observations regarding public interest in matters relating to companies. [*Letter No.* 7/9/74-CL-II, dated 13-5-1975].

The turn-over criterion.—In case the average annual turnover is not less than such sum as may be prescribed [w.e.f. 15-6-1988 the average annual turnover was prescribed as not less than Rs. 5 crores *vide GSR No.* 694(E), dated 10-6-1988 and w.e.f. 18-9-1990, the average annual turnover was prescribed as not less than Rs. 10 crores *vide GSR No.* 795(E), dated 18-9-1990. *W.e.f. 23-2-1999, the average annual turnover shall be not less than Rs. 25 crores vide GSR No. 130(E), dated 23-2-1999.* See, Rule 4-C in *Appendix* 1] during the relevant period, from the expiry of 3 months from that period, it will become a public company. The expression 'relevant period' has been defined in the *Explanation* to s. 43A.

Companies whose relevant period of three consecutive financial years having an average annual turnover of not less than Rs. 5 crores fall immediately after 15th June, 1988, will be covered under sub-clause (iii) of clause (a) of the *Explanation* to section 43A of the Act and shall become public companies by virtue of section 43(1A) on and from the expiry of a period of three months from the last date of the third financial year of the relevant period. [*Circular No.* 3 of 1989, dated 13-4-1989: (1989) 65 Com Cases 558 (St.)]

On the same analogy companies whose relevant period of three consecutive financial years having an average annual turnover of not less than Rs. 10 crores fall immediately after 18th Sept., 1990, will be covered under sub-clause (iii) of clause (a) of the *Explanation* to section 43A of the Act and shall become public companies by virtue of section 43(1A) on and from the expiry of a period of three months from the last date of the third financial year of the relevant period.

Revision of Turnover amount w.e.f. 23-2-1999.—The Turnover criterion has been revised and raised from Rs. 10 crores to Rs. 25 crores *vide* Rule 4C of the Companies (Central Govts.) General Rules & Forms, 1956 (w.e.f. 23-2-1999).

Department's Clarification.—As per sub-section (1A) of section 43A of the Companies Act, 1956 where the average annual turnover of a private company is not, during the relevant period *i.e.* during three consecutive financial years, less than such amount as may be prescribed, the private company shall become, on the expiry of three months from the last day of the period of three consecutive financial years

during which the private company had the said average turnover, a public company. This ceiling of average annual turnover under section 43A(1A) is prescribed by the Central Government from time to time under Rule 4C of the Companies (Central Government's) General Rules and Forms, 1956.

2. This ceiling criterion of Average Annual Turnover for the 'relevant period' which was Rs. 10 crores has been raised to Rs. 25 crores by this Department by amending the above-said Rule through Notification No. GSR 130(E), dated 23-2-1999.

3. Consequent on this upward revision of the Average Annual Turnover criterion a query has been raised as to the effect of the increase in the ceiling of average annual turnover with effect from 23-2-1999 on Companies whose average annual turnover for 3 consecutive financial years was beyond Rs. 10 crores or more (but was less than Rs. 25 crores) before it became a public company on the expiry of three months from the last day of the three consecutive financial years under the old criterion of Rs. 10 crores ceiling.

4. In this connection, it is to be noted that for determining the date from which a private company shall become a public company consequent upon increase in the ceiling of average annual turnover, 23-11-1998 which is three months earlier to 23-2-1999 will be the material date. It is, therefore, clarified that a private company whose last of the three consecutive financial years ended on any date during the period from 23-11-1998 to 22-2-1999 and its average annual turnover for three consecutive financial years was Rs. 10 crores or more but less than Rs. 25 crores, shall not become a deemed public company by virtue of sub-section (1A) of section 43A of the Companies Act, 1956. [*Issued by DCA vide F.No. 1/8/99-CL.V; General Circular No. 7/99, dated 25-5-1999*]

The basis for computing the turnover has evoked some controversy. Under explanation (b) to section 43-A, 'turnover' of a company, means the aggregate value of the realisation made from the sale, supply or distribution of goods or on account of services rendered, for purposes of section 43-A(1A) of the Act. Turnover means the amount representing the total sale of a trader during a period. The aggregate sale amount includes sales tax and excise duty. Thus, sales tax and excise duty will form part of turnover, whether the invoices issued by the company for sale of goods are inclusive or exclusive of sales tax and excise duty.

Similarly the in case of a travel agency business, although the commission which the travel agent gets is only a fraction of the amount of the bill consisting of recovery of railway/air fare already spent, the entire realisation made will be treated as the turnover.

The Department of Company Affairs has clarified that the gross freight collected from the customers by an agent of airlines carrier would constitute 'turnover' (*Letter No.* 32/15/88-CL-III, dated 7-7-1989). In case, however, the company books cargo on behalf of the carrier, as agent, the gross income is the commission of 5% paid by the Airlines and is its turnover, without taking into account the commission paid to sub-agents, which forms part of its expenditure. The Clarification issued by the Department of Company Affairs on 7-7-1989 and relied upon by the applicant is in order in respect of a air-freight company when it buys bulk space. (*Airlift India (P.) Ltd., Re, C.P. No. 2/1991*, Judgment dated 21-2-1992).

In respect of sale of film exhibition tickets, gross amount received on sale of tickets including entertainment tax would come within the purview of 'turnover', (*Circular No.* 4/1/80-CL-V, dated 2-9-1980). Since the turnover is linked up with the realisation, it refers only to the aggregate amount for which sales are affected and shown in the profit and loss account as having been realised or to be realised by a company by sale of goods produced or services rendered. Realisation against 'jobs-in-progress' would not be included in the turnover since it has not actually accrued to the company.

As per the decision in *George Oakes (Pvt.) Ltd. v. State of Madras,* AIR 1962 SC 1352; *State of A.P. v. East India Commercial Co. Ltd.,* AIR 1957 AP 83; *Sundaram Motors v. Jt. Commercial Tax Officer,* (1965) 16 STC 644 (Mad) turnover would include sales tax collected, and are relevant for the limited purpose of finding the incidence of sales tax that is payable and that beyond answering this question, the judgments have no accounting significance. The Expert Advisory Committee of the Institute of Chartered Accountants of India have expressed the opinion on the subject, as follows : "If a company makes a composite charge to its customer inclusive of freight and despatch, the charge so made should ordinarily be regarded as the invoice price of the goods sold and should accordingly be disclosed as the value of the turnover. It would not be proper to reduce the value of the turnover by reference to the approximate value of the service relating to freight and despatch. On the other hand, if the company makes a separate charge for freight and despatch, and for other similar services it would be quite proper to ignore such charges when computing the value of the turnover to be disclosed in the Profit and Loss Account. In other words, the disclosure may well be determined by reference to the company's invoicing and accounting policy and may, thereby, vary from company to company. For reasons of consistency, as far as possible, a company should adhere to the same basic policy from year to year and if there is any change in the policy, the effect of that change may need to be disclosed if it is material, so that a comparison of the turnover figures from year to year does not become misleading. For reasons discussed above, sales tax may also be segregated from the value of turnover if it is conveniently possible to do so in accordance with the ac-

counting system followed by the company; particularly if the company's billing procedures involve a separate charge to the customer for sales tax. This treatment, it may be noted, is also in accordance with the recommendations of the Institute of Chartered Accountants in England and Wales relating to the accounting treatment of the value-added tax which is a tax that corresponds, in many instances, to the sales tax in India-*vide* English Institute's statement M5 issued in April, 1974 in which it has been recommended *inter alia*, that 'turnover shown in the Profit and Loss Account should exclude VAT taxable outputs'.

While the foregoing treatment of sales tax is recommended as the approved method of accounting in a case where a company makes a separate charge on the invoice for sales tax, the question as to the appropriate method of accounting still remains to be resolved in a case where a company makes a composite charge to the customer which is inclusive of sales tax, without separately designating the sales tax on the invoice or in the contract with the customer. It was suggested that approximate adjustments to the value of turnover would not be proper in respect of various services which are not separately charged to the customer. The position with regard to sales tax is, however, somewhat different, since this is a statutory liability, the incidence of which can be calculated with a high degree of precision with reference to any given value of turnover. Accordingly, if sales tax is not separately charged to the customer, two alternative methods of accounting are available to the company, either of which may be adopted subject to consistency of application from year to year. The alternative methods are firstly, to disclose the entire value inclusive of sales tax as the value of the turnover, or secondly, to segregate the sales tax value by applying the appropriate sales tax rates to the gross value of the turnover so that only the net value after such adjustment is disclosed in the Profit and Loss Account as the value of the turnover. Incidently this raises the question as to how the accounting treatment should meet the situation where the invoice is inclusive of sales tax. Here there would appear to be two standard practices prevalent. One is (a) to ascertain the sales tax liability and make it as a deduction from the Sales Turnover. Even in the second alternative the gross invoicing should be shown as such and the sales tax liability deducted from the inner column and the net results extended to the outer column. COMPENDIUM OF OPINIONS—Vol. I of Institute of Chartered Accountants of India, p. 67, Views of ICAI do not seem to be in full accord with the Departmental views.

For purposes of sub-section (1A), it is not necessary that the 'turnover' is reflected in the accounts of the company duly audited and laid before an annual general meeting. Since the purpose of section 43-A is to introduce a fiction what is necessary is the availability of the accounts to the Board of Directors to satisfy the turnover criterion; the availability of accounts duly audited and laid before the annual general meeting is not a condition precendent. (*Circular No.* 32/17/75-CL-III, dated 9-9-1975.) The text of the Department's Circular is reproduced below:

Text of Circular.—"The turnover criterion brought in section 43A by the recent amendment for converting a private company into a public company contemplates an average over a period of three consecutive financial years. There is nothing in this context to import that the turnover as reflected in the accounts of the company as audited by an auditor appointed in terms of the requirement of the Companies Act or laid before an annual general meeting should only be taken into account. The definition of financial year in section 2(17) of the Act is applicable only if there is nothing repugnant to it as may be gathered from the context of the section where that expression occurs. Since the purpose of section 43A is to introduce a fiction whereby a private company becomes a public company, it has to be interpreted in a manner which will serve the concept of the public interest underlying it to the fullest extent possible. To that concept, the holding of the annual general meeting or the circumstances whether accounts are audited or not is not germane *stricto sensu*. What is germane is the availability of the accounts to the Board of Directors whereby they may determine for themselves whether they satisfy the turnover criterion or not. Given the accounts of the three financial years in the sense of the three accounting years of the company, a company would attract the provisions of section 43A".

According to *Departmental Clarification No.* 3/20/88-CL-V, dated 18-8-1988, the cases of companies becoming public company by virtue of sub-section (1A) of section 43A of the Act would fall under one of the 3 categories, as follows:

(i) Companies having the average annual turnover* of Rs. 5 crores and above during the relevant period consisting of three consecutive financial years and whose 3rd financial year does not end prior to 15-3-1988, *i.e.* where the 3rd financial year of the relevant period ended on 15-3-1988 or on any date thereafter but not after 14-6-1988 will be covered under sub-clause (i) of clause (a) of the *Explanation* to section 43-A of the Act and these companies will become public companies on and from the expiry of a period of three months from the last date of the 3rd financial year of the relevant period;

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* The average annual turnover prescribed was not less than Rs. 10 Crores *vide* GSR No. 795(E), dated 18-9-1990 and now w.e.f. 23-2-1999 the average annual turnover shall be not less than Rs. 25 crores *vide* GSR No. 130(E), dt. 23-2-1999.

(ii) Companies, whose first or the second financial year, as the case may be, of the relevant period having an average annual turnover* of Rs. 5 crores or above does not end prior to 15-3-1988 *i.e.* where either the first financial year or the second financial year of the relevant period is current on 15-6-1988, will fall under sub-clause (ii) of clause (a) of the *Explanation* to section 43-A and shall become public companies by virtue of the provisions of sub-section (1A) of section 43-A of the Act on and from the expiry of a period of three months from the last date of the third financial year of the relevant period;

(iii) Companies whose relevant period of three consecutive financial years having an average turnover of not less than Rs. 5 crores falls immediately after 15-6-1988 *i.e.* the third financial year of the relevant period ends after 15-6-1988, will fall under sub-clause (iii) of clause (a) of the *Explanation* to section 43-A of the Act and shall become public companies by virtue of section 43(1A) on and from the expiry of a period of 3 months from the last date of the third financial year of the relevant period. [*Vide F. No.* 3/20/88-CL-V, dated 18-8-1988].

Interpretation of 'relevant period' [Section 43A(1A) and Explanation of section 43A]

Department's Circular.—Several queries have been received relating to the interpretation of and the date of the applicability of the provision of Section 43A(1A) to private companies with reference to the explanation given at the end of the said section. The matter has been examined in consultation with the Department of Legal Affairs and it has been decided that the cases of companies becoming public companies by virtue of sub-section (1A) of Section 43A of the Act would fall under one of the three clauses as enumerated under Explanation to the said Section 43A, as follows:—

(i) Companies having the average annual turnover of Rs. 1 crore and above during the relevant period consisting of three consecutive financial years and whose 3rd financial year does not end prior to 31-10-1974 *i.e.*, where the 3rd financial year of the relevant period ended on 31-10-1974 or on any date thereafter but not after 31-1-1975 will be converted under sub-clause (i) of clause (a) of the Explanation to Section 43A of the Act and these companies shall become public companies on and from the expiry of a period of three months from the last date of the 3rd Financial year of the relevant period.

(ii) Companies, whose first or the second financial year, as the case may be, of the relevant period having an average annual turnover of Rs. 1 crore or above does not end prior to 31-10-1974 *i.e.*, where either the first financial year or the second financial year of the relevant period is current on 1-2-1975, will fall under sub-clause (ii) of clause (a) of the Explanation of Section 43A and shall become public companies by virtue of the provisions of sub-section (1A) of Section 43A of the Act on and from the expiry of a period of three months from the last date of the third financial year of the relevant period.

(iii) Companies whose relevant period of three consecutive financial years having an average annual turnover of not less than Rs. 1 crore falls immediately after 1-2-1975 *i.e.*, the third financial year of the relevant period ends after 1-2-1975, will fall under sub-clause (iii) of clause (a) of the Explanation to Section 43A of the Act and shall become public companies by virtue of Section 43(1A) on and from the expiry of a period of 3 months from the last date of the third financial year of the relevant period. (*Circular No.* 16/75, dated 23-6-1975).

Deemed public company under sub-section (1B) [Shares in public company]

In case a private company holds not less than 25% of the paid-up share capital of a public company, the private company becomes a public company from the date on which the aforesaid percentage is first held.

Deemed public company under sub-section (1C) read with Sub-sec. (10)

Acceptance or renewal of deposits.—Sub-section (1C) provides, with effect from 15-6-1988, that if a private company invites deposits from public by advertisement or renews deposits from public, other than its members, directors or their relatives, it shall become a public company. Sub-section (10) clarifies the reference made to the expression 'accepting, after an invitation is made by an advertisement or, renewing deposits from the public' used in sub-section (1C), by stating that the same shall be construed as including a reference made in section 67 to invitation to the public to subscribe for shares or debentures. Section 67(3) *inter alia* provides for private placement of shares, so that no offer or invitation shall be treated as made to the public if the offer or invitation can be properly regarded as not being calculated to result, directly or indirectly, in the shares or debentures becoming available for subscription or purchase by persons other than those receiving the offer or invitation. Therefore, by virtue of sub-section (10), acceptance or invitation of deposits not calculated to be accepted by persons other than those to whom the invitation is made, shall not be deemed to be from the public. In other words, for purposes of sub-section (1C) deposits invited from the public by advertisement will only be taken into account. However, in case the private company accepts deposits from its members, directors or their relatives (as defined in section 6), the same will not be taken into account.

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* The average annual turnover prescribed was not less than Rs. 10 Crores *vide* GSR No. 795(E), dated 18-9-1990 and now w.e.f. 23-2-1999 the average annual turnover shall be not less than Rs. 25 crores *vide* GSR No. 130(E), dt. 23-2-1999.

It may be noted that under Rule 2(b)(ix) of the Companies (Acceptance of Deposits) Rules, 1975 any amount received from a person who at the time of receipt of the amount was a director or any amount received from its shareholders by a private company or by a private company which has become a public company under section 43-A and continues to include in its Articles of Association provisions relating to the matters specified in section 3(1)(iii) is not treated as a deposit for purposes of section 58-A and the aforesaid Rules. Thus, the provisions of sub-section (1C) will only be attracted where the private company issues an advertisement in newspapers for inviting deposits from the public. Issue of Circulars/handouts by a private company or through its brokers to selected persons, subject to the conditions laid down in section 67, will not attract sub-section (1C).

Department's Clarifications.—"A private company which accepts deposits from public by way of invitation by advertisement, or renews deposits so accepted, will become a public company, and not otherwise. It is clarified that a private company which had accepted, after an invitation made by advertisement, deposits from the public prior to the 15th June, 1988, shall be deemed to have become a public company when any deposit so accepted is renewed, on and from the date of such renewal." [*Circular No.* 3 of 1989, dated 13-4-1989 : (1989) 65 Com Cases 558 (St.)]

In case of private companies, which have accepted deposits from their shareholders, such deposits come within the definition of 'public deposits' on the conversion of such private company into a public company under this section. The Department has clarified that such deposits even though within the meaning of 'Public deposits' may be repaid as per the terms of their acceptance. (*Letter No.* 4/2/76/CL-XIV, dated 18-6-1975).

Exemption under sub-section (6)/(7) [*Omitted* by Amendment of 1988]

Before the commencement of Amendment Act of 1988 *i.e.* 15-6-1988, the provisions of section 43-A were not applicable in case of a private company whose entire share capital was held by another single private company or by one or more bodies corporate incorporated outside India; or to a private company in which shares were held by a foreign company, subject to a declaration by the Central Government that the foreign company would be a private company under this Act; or a private company, whose shares are held by a private company and no company is holding shares in such shareholding company and that the total number of shareholders of the shareholding company do not exceed fifty. Sub-sections (6) and (7) were deleted w.e.f. 15-6-1988 by the Amendment Act of 1988 because exemption contained therein was found to render the other provisions of this section nugatory (Clause 7(c) of *Notes on clauses*). The provisions of section 43A were circumvented by allotting one or more shares by a private company to another private company, after satisfying the conditions laid in sub-section (6)(b). The exemption benefit will not be available to private companies after 15-6-1988, the commencement of the Amendment Act, 1988. The private companies presently availing such exemption will become deemed public companies, by operation of law and will have to intimate the position to the Registrar within 3 months from the date of commencement of the Amendment Act of 1988 (*i.e.* 15-6-1988) under sub-section (2).

Some general effects of conversion

(1) Where a private company becomes a public company by virtue of this section, any subsidiary of such company, if it was private company previously, will also become a public company.

(2) If any contract of appointment of any individual, firm or body corporate had been entered into by the private company which, if it was a public company, would have contravened the provisions of section 204 as regards the period of office of the person appointed, such contract would stand revoked if the company becomes a public company under this section unless and until such modifications as are required to satisfy the provisions of section 204 are effected. So also all other provisions such as those of sections 198, 268, 269, 309, 310 and 311 would have to be complied with.

(3) It may be noted that, where a private company becomes a public company, all the provisions of the Act except those where relaxation is permitted will have to be complied with.

(4) If loans had been given to directors within the meaning of s. 295 the approval of the Central Government should be obtained within a period of 6 months of change of status, failing which the company will have to recover the loans made or withdraw the guarantee within the aforesaid period of 6 months. Investments made by the company which could not have been made by the company under section 372 had it been a public company have to be disposed of within a reasonable period.

(5) A private company is entitled to commence business as soon as it is incorporated and the position remains the same even if it becomes a deemed public company before commencement of business. It is neither required to obtain commencement certificate under s. 149 nor to hold statutory meeting under s. 165.

Court proceedings to continue under its altered name.—The company has to change its name by dropping the word "Private". This will not affect the legal rights and liabilities of the company. It can continue its existing proceedings under its altered name. *Gur Narain Jagat Narain & Co. v. Motor & General Sales Ltd.*, 1980 All LJ 508 (All).

Filing of Statement in lieu of prospectus.—A private company which becomes a public company by virtue of section 43A is not required to file a prospectus or a statement in lieu of a prospectus, *Needle Industries (India) Ltd. v. Needles Industries Newey (India) Holding Ltd.*, (1981) 51 Com Cases 743 : AIR 1981 SC 1298.

Clarifications of various aspects of s. 43A—addressed to all recognised Chambers of Commerce and Trade Associations

(1) By virtue of the new section 43A, a number of private companies became public companies with effect from the 28th March, 1961. A company which was a private company before the enactment of section 43A will, however, continue to remain so, if it fulfils immediately before the 28th March, 1961 either of the conditions laid down under sub-section (6) thereof.

(2) *Application of the whole Act to deemed public companies except where exempted.*—All the provisions of the Act which are applicable to a public company will, after the 28th March, 1961, generally apply to a company which has become a public company by virtue of section 43A. However, the provisions of section 12(1) and 45 of the Act which require a public company to have at least seven members will not apply to a section 43A company. The articles of association of such company may continue to contain a provision similar to that in section 3(1)(iii) which is applicable to private companies. Section 44 also is not applicable to a private company, when it becomes a public company by virtue of section 43A and consequently such a company will not be required to file with the Registrar a statement in lieu of prospectus under section 44(1)(b) of the Act. When it intends to raise subscriptions from the public, the company must comply with the requirements of section 70.

(3) *Effect upon the appointment of managerial personnel and their remuneration.*—The provisions of sections 198, 269, 309, 310, 311, 387 and 388 etc. which govern *inter alia* the appointment and re-appointment and the payment of remuneration to managing and whole-time directors or managers apply to section 43A Companies. The provisions of section 269(1) of the Act will not, however, apply to a person holding the office of managing or whole-time director or manager of such a company for a period of not exceeding 5 years from the 28th March, 1961 provided he was holding the office immediately before it became a public company; but the restrictions contained in sections 198, 309, 310, 311 etc., would automatically be applicable to such companies from the date they became public companies. Some companies are under the impression that the amended provisions contained in sections 198 and 309 would not apply in cases where the terms of appointment were settled or approved before the Amendment Act was passed. This is not correct. It further appears that on the basis of the provisions contained in sub-section (8) of section 309 of the Act, some companies have taken the view that these sections are applicable to them only from the next financial year. Apparently, the words 'this Act' occurring in the sub-section have been taken to refer to the Companies (Amendment) Act, 1960 which came into force on the 28th December, 1960. This is not correct and it is pointed out for the information of all concerned that section 309 with all its existing sub-sections has been in force since the 1st April, 1956, when the Companies Act was promulgated. The Companies (Amendment) Act, 1960 has, brought about certain changes in the existing sub-sections. The words 'this Act' occurring in sub-section (8) of section 309, therefore, refer to the Companies Act which came into force on the 1st April, 1956, and not to the Companies (Amendment) Act, 1960. The provisions of sections 309 and 198 of the Act would therefore be applicable to public companies of the type referred to above with effect from the 28th March, 1961. Since the restrictive provisions of the Act relating to payment of remuneration to managerial personnel did not apply to private companies the remuneration had, in most cases, been fixed by the companies without reference to the modes of payment authorised under the Act or the ceilings prescribed thereunder. It would, therefore, be necessary for many of these companies to change the mode of payment of managerial remuneration and also seek the Central Government's approval, wherever necessary under sections 309, 310, and 198 of the Act as the case may be. Some companies have already sought the Central Government's approval in this behalf. Other companies which for some reason or other have not sought Government's approval so far should do so immediately in their own interest as otherwise they will be violating the law with its attendant consequences.

(4) For the purposes of calculating the total number of shareholders in terms of section 43A(6)(b)(iii), common shareholders of the private company and of the shareholding company should be counted separately. (This portion of Circular no longer applicable as sub-section (6) omitted by Amendment Act, 1988).

(5) The word "held" used in sub-section (1) and elsewhere in section 43A does not mean "beneficially held" since companies are not permitted under section 153 to recognise trust or nominee holdings. Nominee holdings, however, are permissible to the extent they are provided for in sub-sections (2) and (3) of section 49 of the Companies Act, 1956 and companies, which seek exemption from the provisions of section 43A under sub-section (6)(*a*) thereof, would not be entitled to such exemption unless holdings by nominees of the parent company are restricted to what is permitted to under sections 49(2) and 49(3). For

this limited purpose, the Department has construed the word "company" appearing in these two sub-sections to include a "body corporate".

(6) *Time period within which the company affairs should have been readjusted to save private character.*—In respect of the various representations made to the Central Government to the effect that a large number of private companies which had technically become public companies on 28-3-61 under the provisions of section 43A(1) could not, for one reason or the other, reorganise their shareholdings before 28-3-1961 so as to enable them to continue as private companies, Government has taken an administrative decision that no proceedings would be launched against such of those companies as were able to reorganise their shareholdings before 31-12-61 at the latest. All those companies which were able to avail of this administrative concession would be deemed to have continued as private companies and no insistence will be placed on them by the Department to comply with the requirements of sub-sections (2) and (4) of section 43A. Where, however, for its own protection any such company applies for the approval of Central Government under section 43A(4), it should first fulfil the obligations imposed on it under section 43A(2) and then only seek Central Government's approval under section (4).

(7) Companies which have failed to reorganise their shareholdings by 31-12-1961 would be deemed to have become and continued as public limited companies on and from 28-3-1961 and would become liable to penal proceedings as prescribed in law for failure to comply with the provisions of sub-section (2) of section 43A as well as other provisions of the Act applicable to public limited companies. [*Enclosure to Circular Letter No.* 48(50)-CL-IV/61, dated 12th February, 1962].

Effect on appointments, remuneration, etc. of managing directors.—"Where private companies convert into public companies, or come to be deemed to be public companies, and have pre-existing managing directors whose remuneration is in accord with sections 309 and 198, as amended, no permission of the Central Government would be necessary for the continuance of the existing appointment. But sections 268, and 317 will become applicable as from the date of conversion or change of character and Central Government's approval will be necessary for any amendment in the terms of appointment or at the time of re-appointment under section 269(2), as it will also be necessary for purposes of payment of minimum remuneration under section 198(4). [*Department's File No.* 8/16(1)/61-PR, dated 9-5-1961].

Department's Clarification regarding managerial remuneration in deemed public companies.—The general policy to be followed in regard to section 43A companies will be governed by the following considerations:—

(i) Section 43A companies should be treated at par with other public companies so far as managerial remuneration was concerned and except in the case of such companies which were primarily managing agency companies, no special treatment would be justified.

(ii) In the case of such companies where the existing remuneration itself could be considered reasonable having regard to the criteria adopted for fixation of remuneration of managerial personnel of public companies generally, such remuneration should be protected in full by issuing suitable orders under sections 198(4) and 309(3).

(iii) In cases where the existing remuneration consists of both salary and commission element and where the total remuneration exceeds 11 per cent of the current net profits of the company but the remuneration itself is not unduly high, the full amount of the salary and perquisites should be protected but the commission element should be protected (by being converted into salary) only to such extent that the total remuneration should not exceed 25 per cent of the average net profits of the company for the last three years.

(iv) In regard to cases where the remuneration is disproportionately high, no protection should be given to the commission element, if any, but the monthly salary payable in terms of existing contracts may be protected for a period not exceeding two or three years or for the remainder of the term of office, whichever is less. In such cases, it should be made clear to the company that Government would not be able to exercise its special powers to protect the salary for a longer period and that the company should reorganise their business and managerial set up so that the managerial remuneration should not exceed the ceilings prescribed under the Act. (*Department's F. No.* 1(125)-CL-I/61).

Section 43A and right of renunciation under section 81

The Supreme Court held in *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.*, (1981) 51 Com Cases 743 : AIR 1981 SC 1298 that a deemed public company which retains the restrictive clauses under section 3(1)(iii) would not be subject to the right of renunciation under section 81(1)(c) in the event of a "rights" issue of shares.

Investments under s. 49 and applicability of deeming provisions to foreign companies

Department's Circular.—A question was raised as to whether, in view of the fact that section 49 of the Act did not apply to a foreign company, it was open to such a company holding the entire paid-up share capital of an Indian private company, to hold these shares through nominee shareholders to the extent the company desired without thereby disturbing the private character of the Indian private com-

pany. Since, in view of the fact that a private company must have at least two members under the Act, it would, in effect, not be possible for the entire share capital of a private company to be held only by one company, the view has been taken that section 43A should be read with section 49 of the Act which allows nominees of a shareholding companies to hold the minimum number of qualification shares for the purpose of being appointed as directors or to hold shares solely for the purpose of complying with the requirement as to the minimum membership of two.

Section 49 of the Act not being applicable to foreign companies, they are not entitled even to the concession envisaged in that section. It has, however, been decided administratively that equal treatment should be given to foreign companies and they should have the benefit of section 49 of the Act. (*Department's F. No.* 8/16(1)/61-PR, dated 4-3-1961).

Pre-emptive agreements and deemed public companies

A pre-emptive agreement between the shareholders of a private company containing restrictions on transfer of shares whose terms have been incorporated in its articles, would be binding and enforceable as regards the company and its shareholders even when the company becomes a deemed public company but is retaining the clauses under section 3(1)(iii) of the Act. For further comments see Notes under section 3.

Directors' personal liability for private company's overdue taxes

The decision of the Kerala High Court in *N. Rajamoni Amma v. Dy. CIT,* (1991) 72 Com Cases 728 (Ker) was **reversed** by the Supreme Court in *sub-nom, N. Rajamoni Amma v. Dy. CIT,* (1992) 74 Com Cases 356, 359 (SC) holding that with effect from the conversion of the private company into a deemed public company, the directors' personal liability to pay arrears of income-tax under section 179 of the IT Act accumulating after the conversion would no longer arise and, therefore, the proceedings of the Department against the directors were quashed.

Reconversion [Sub-section (4)]

Department's Clarification.—The provisions of section 43A(1A) and (1B) are mandatory and the private company shall become a public company according to the said provisions and the company should comply with the provisions of sub-section (2) of section 43A of the Act within the stipulated period of 3 months. On the private company's disposing of the shares of the public company so as to reduce the percentage of its hold less than 25% of the paid-up share capital of the public company or its average annual turnover falling below rupees one crore, [*rupees ten crores* w.e.f. 18-9-1990] the company can convert itself into a private company by complying with the provisions of Section 43A(4) of the Companies Act, 1956. (*Letter No.* 32/21/75-CL-III, dated 20-10-1975.)

Reconversion of S. 43-A Company into Private Company.—After a private company becomes a deemed public company by virtue of operation of Section 43-A, it can be reconverted into private company only with the prior approval of the Central Government. It could not be treated as a private company till the approval was accorded. *V.R. Textiles Ltd., Re,* (CP No. 31 of 1991 decided on 20-4-1992 by CLB).

No automatic conversion of public company into private company by operation of law

Department's Clarification.—Under section 43A(1A), when the average annual turn-over of a private company for the last three years was Rs. one crore, it became a public company. The said monetary ceiling of Rs. one crore was raised to Rs. 5 crores w.e.f. 15-6-1988. The ceiling has since been raised to Rs. 10 crores w.e.f. 18-9-1990. There are many companies whose average annual turn-over is more than Rs. 5 crores but less than Rs. 10 crores; such companies are, accordingly, out of the net of section 43A(1A). Such companies are already public companies under these provisions and in view of the provisions of section 43A(4), such companies should seek approval of the Central Government (power delegated to Registrar of Companies) for their conversion as a private company. It is not correct to say that such a public company will be converted into a private company by operation of law, on 18-9-1990 when the notification amending the monetary ceiling from Rs. 5 crores to Rs. 10 crores was issued. (*Circular No.* 16/90, dated 22-10-1990 : [(1991) 70 Com Cases (St) 30)].

Approval under S. 43A(4) and 31(1)—Clarification regarding conversion of a public company under S. 43A(1) into a private company

Department's Circular.—When a deemed Public Company wants to get itself reconverted into a Private company by following the procedure laid down in section 43A(4) the provisions of section 31(1) will not be applicable, even if the reconversion necessitates a change in the Articles of Association [*Circular No.* 11/72(32/7/72-CL-III), dated 19-5-1972]. The question of passing a special resolution does not arise in case of those deemed public companies, which have retained in their articles the restrictions mentioned in section 3(1)(iii). But even in case of those who have shed these restrictions on becoming a deemed public company, the re-insertion of those restrictions or other changes in the articles to reconvert the company into a private company will not require the approval under section 31(1) as clarified by the above *Circular.* Text of the Circular is reproduced:

Text of Circular.—In terms of provisions in Section 43A(4) of the Companies Act, 1956 (hereinafter referred to as the Act) a private company which becomes a public company by virtue of provisions in Section 43A(1) shall continue to be a public company until it has with the approval of the Central Government and in accordance with the provisions of the Act again become a private company.

Question has been raised whether in the case of a company which having become a public company by virtue of the provisions of section 43A(1) of the Act approaches the Company Law Board for obtaining approval under section 43A(4) for a reversion to the status of a private company, two applications to the Central Government—one under section 43A(4) and the other under section 31(1) of the Act, with two separate application fees are required under the aforesaid provisions of the Companies Act or a single application fee is sufficient for the purpose.

The issue has been examined by the Company Law Board in consultation with the Ministry of Law and the Board has been advised that any company which becomes a public company by virtue of the provisions of Section 43A(1) of the Act can convert itself into a private company after obtaining the approval of the Central Government under section 43A(4) of the Act. Once the Central Government has granted its approval to convert a public company into a private one under section 43A(4) of the Act there is nothing left for further approval under section 31(1) of the Act. Therefore in such cases an application by the company under section 43A(4) is only required and the question of two applications accompanied by two application fees does not arise. Before making the said application the company should amend its Articles of Association, if necessary, so as to incorporate the requirements of Section 3(1)(iii) of the Act. This amendment will be necessary in those cases of companies which during their existence as a public company under section 43A(1) chose to get those clauses of the Articles of Association deleted, which had conformed to the requirements of section 3(1)(iii) of the Act, instead of retaining them under the proviso to section 43A(1). As for the obligation of companies in such cases to reinsert the said clauses in the Articles of Association in order that they might be regarded as private companies after their application under section 43A(4) of the Act is allowed, the said obligation may be fulfilled with the passing of a special resolution in pursuance of section 31 of the Companies Act, but no approval of the Central Government is required in that regard, because the special resolution would precede and be a step-in-aid of the application under section 43A(4) of the Act. This means that the requirement of Central Government's approval under the proviso to section 31 of the Act is solely applicable to the category of public companies which by the terms of their incorporation or by direct conversion (*i.e.*, without intervention of section 43A) from private to public have assumed the status of public companies and which seek to attain or recover the status of private companies [*Circular No.* 11/72, dated 19-5-1972.]

Delegation of powers under sub-section (4).—The powers of the Central Government under sub-section (4) have been delegated to the Registrar of Companies. (*Notification GSR No.* 507(E), dated 24-6-1985)

Penalty for default [sub-section (5)]

A private company which becomes a public company under this scheme is enjoined by sub-section (2) to inform the Registrar of this fact. If a company makes default in complying with this provision, the company and every officer of the company who is in default is punishable with fine which 'may extend to five hundred rupees for every day during which the default continues'.

The offence is compoundable under section 621A.

Annual submission of certificates by private companies [Sub-section (8)]

In addition to the certificate required to be submitted by private companies under section 161(2) along with the annual return, following certificates are also required by this section to be filed by such companies along with the annual return:

(i) under clause (a) of sub-section (8); as to any body corporate holding 25% of its paid-up share capital;

(ii) under clause (c) of sub-section (8) as regards its average annual turnover being during the relevant period of such amount as is referred to in sub-section (1A);

(iii) under clause (d) of sub-section (8) that it did not accept or renew deposits from public;

(iv) under sub-section (9) to the effect that during the period to which the annual return related, it did not hold 25 per cent, or more of the paid-up share capital of any public company.

Filing fees for information furnished to ROC under S. 43A(2)

Department's Circular.—It has come to the notice of this Department that some of the Registrars of Companies charge fees for recording the information referred to above while others do not charge any such fees. This Department has examined this point in consultation with the Ministry of Law and Justice and holds that the provisions contained in clause 6 of Schedule X of the Companies Act, 1956 apply to the making of an alteration in the Memorandum of Association under sub-section (2) of section 43A which has to be done when the Registrar is informed by a private company that it has become a public

company under sub-section (1) of the said section. Clause 6 of the Schedule X speaks of making a record of any fact and therefore making alteration by means of a formal writing in the Memorandum of Association registered with the Registrar showing that the private company has become a public company would be within the ambit of the said clause.

Appropriate fees are therefore to be paid by companies on the information furnished to the Registrar of Companies under sub-section (2) of section 43A of the Companies Act, 1956. (*Circular No.* 28/72, dated 2-8-1972.) The case of delay, additional fee is payable at prescribed rates *vide* Press Note No. 2/95, dated 21-3-1995. For the text of this Press Note see Notes under section 611 *post.*

Applicability of section 43A to Government Companies

Department's Circular.—Several Government Companies which were private companies until 1st February, 1975 have already become Public companies by virtue of the turnover criterion brought in by new sub-section (1A) of section 43A of the Companies Act, 1956. Representations have been received from some of the Government Companies etc. for exempting Government Companies incorporated as Private Limited Companies from the operation of sub-section (1A) of section 43A under section 620 so that they can preserve the *status quo ante* of a Government private company as on 1st February, 1975. While there is no bar to exempting Government Companies from the operation of sub-section (1A) of section 43A, there is no scope for exempting Government Companies which have become Public Companies by the operation of section 43A, with retrospective effect, so as to enable them to be re-converted into private company status. Hence, even if a notification under section 620 is issued granting such an exemption the same would not be available to all existing Government private companies, but may be available only to those companies which may become public companies by the turnover criteria adopted under section (1A) of section 43A in future or Government companies that may be incorporated as private in future.

2. The Department of Company Affairs have already notified exemptions in favour of Government companies generally, from the operation of some of the important sections and intend to give exemption from other important sections after complying with the provisions of sub-section (2) of section 620 of the Companies Act, 1956. These exemptions relate to inter-corporate investments, inter-corporate loans, contracts in which directors are interested, and investments, managerial appointments and remuneration and other provisions *viz.*, sections 187(C), 198, 259, 268, 269, 297, 309, 310, 311, 370, 372, 387 and 388 of the Companies Act, 1956. The question of granting exemption to the Government companies from the provisions of sections 255, 256, 257 and 258 is also under active consideration of the Department. Hence, it should not be so very important now whether a Government company becomes a public company or continues to remain a private company under section 43A in so far as the day-to-day operations are concerned. [*Circular, letter No.* 36/75 dated 3-12-1975.]

Government Companies exempted.—This section does not apply to wholly owned Government Companies. See Notes under section 620.

Relevant Rules and Forms.—The Companies (Central Government's) General Rules and Forms, 1956, Rule 4C is the relevant rule for amended s. 43-A. For text of the rule, see, *Appendix* 1.

§ For application for approval of the Central Government for conversion of a public company into a private company refer Form 1-B in *Appendix* 1.

ICSI Guidance Note on Compliance Certificate (August, 2003)

Conversion of a Public Company (Section 43A Company) into a Private Company*

Check whether:

(i) a public company (section 43A company) has become a private company after the commencement of the Companies (Amendment) Act, 2000 and if so, has it informed/applied to ROC that it has become a private company;

(ii) the ROC has made necessary alterations in the certificate of incorporation by substituting the word 'private limited' for the word 'public limited';

(iii) the company has filed Form No. 23 with the ROC and obtained new certificate of incorporation;

(iv) the private company's Articles contain provisions :

(a) restricting the right to transfer its shares;

(b) limiting the number of members to fifty;

(c) prohibiting any invitation to public to subscribe its shares/ debentures; and

(d) prohibiting an invitation or acceptance of deposits from persons other than its members, directors or their relatives.

Continuation of a Section 43A Public Company as a Public Company*

If a public company (section 43A company) intends to continue as a public company then check whether :

(i) it has altered its Articles by deleting provisions relating to matters specified in clause (iii) of sub-section (1) of section 3;

(ii) it has altered its Articles for increasing the number of its members to minimum seven;

(iii) it has altered its Articles for increasing the number of directors to at least three directors;

(iv) it has a minimum paid up capital of five lakh rupees or more on or before 12th December 2002 or such higher paid-up capital as may be prescribed;

(v) it has filed Form No. 23 with the ROC and obtained a fresh certificate of incorporation.

For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

* This matter is not directly referred to in the 33 paragraphs appended to the Form prescribed under the Companies (Compliance Certificate) Rules. The Check List given by the ICSI under the heading 'Check List for Other Compliances' is for the guidance of CSP who may, in the course of his scrutiny, come across non-compliance with regard to this matter. CSP need not qualify such non-compliance.

S. 44. Prospectus or statement in lieu of prospectus to be filed by private company on ceasing to be private company.—(1) If a company, being a private company, alters its Articles in such a manner that they no longer include the provisions which, under clause (iii) of sub-section (1) of section 3, are required to be included in the articles of a company in order to constitute it a private company, the company—

(a) shall, as on the date of the alteration, cease to be a private company; and

(b) shall, within a period of [1][thirty] days after the said date, file with the Registrar either a prospectus or a statement in lieu of prospectus, as specified in sub-section (2).

(2) (a) Every prospectus filed under sub-section (1) shall state the matters specified in Part I of Schedule II and set out the reports specified in Part II of that Schedule, and the said Parts I and II shall have effect subject to the provisions contained in Part III of that Schedule.

(b) Every statement in lieu of prospectus filed under sub-section (1) shall be in the form and contain the particulars set out in Part I of Schedule IV, and in the cases mentioned in Part II of that Schedule, shall set out the reports specified therein, and the said Parts I and II shall have effect subject to the provisions contained in Part III of that Schedule.

(c) Where the persons making any such report as is referred to in clause (a) or (b) have made therein, or have, without giving the reasons indicated therein, any such adjustments as are mentioned in clause 32 of Schedule II or clause 5 of Schedule IV, as the case may be, the prospectus or statement in lieu of prospectus filed as aforesaid, shall have endorsed thereon or attached thereto, a written statement signed by those persons, setting out the adjustments and giving the reasons therefor.

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1. Subs. by Act XXXI of 1965, s. 62 and Sch. for "fourteen" (w.e.f. 15-10-1965).

(3) If default is made in complying with sub-section (1) or (2), the company and every officer of the company who is in default, shall be punishable with fine which may extend to [2][*five thousand rupees*] for every day during which the default continues.

(4) Where any prospectus or statement in lieu of prospectus filed under this section includes any untrue statement, any person who authorised the filing of such prospectus or statement shall be punishable with imprisonment for a term which may extend to two years, or with fine which may extend to [3][*fifty thousand rupees*], or with both, unless he proves either that the statement was immaterial or that he had reasonable ground to believe, and did up to the time of the filing of the prospectus or statement believe, that the statement was true.

(5) For the purposes of this section—

(a) a statement included in a prospectus or a statement in lieu of prospectus shall be deemed to be untrue if it is misleading in the form and context in which it is included; and

(b) where the omission from a prospectus or a statement in lieu of prospectus of any matter is calculated to mislead, the prospectus or statement in lieu of prospectus shall be deemed, in respect of such omission, to be a prospectus or a statement in lieu of prospectus in which an untrue statement is included.

(6) For the purposes of sub-section (4) and clause (a) of sub-section (5), the expression 'included' when used with reference to a prospectus or statement in lieu of prospectus, means included in the prospectus or statement in lieu of prospectus itself or contained in any report or memorandum appearing on the face thereof, or by reference incorporated therein.

NOTES

Eng. Act, 1948 : Section 30 Previous Act : Sec. 154(1)

Companies Act, 1956

The whole of sub-sections (2) to (6) and Schedule IV follow the English section in all essential details.

Companies (Amendment) Act, 2000

The Companies (Amendment) Act, 2000 has enhanced the amount of penalty as follows:

1. Under sub-section (3), penalty amount has been enhanced from five hundred rupees to five thousand rupees.
2. Under sub-section (4), penalty amount has been enhanced from five thousand rupees to fifty thousand rupees.

Scope of section

This section applies to deliberate alteration of the articles, while section 43 deals with inadvertent or accidental non-compliance with or breach of the conditions required of a private company.

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2. The words "five hundred rupees" substituted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 13 (w.e.f. 13-12-2000).
3. The words "five thousand rupees' substituted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 13 (w.e.f. 13-12-2000).

Conditions of conversion of private into public company and *vice versa*

The name of a company is a condition contained in the memorandum within the meaning of section 13. If a private company is converted into a public company it involves a change of name, and the change can be effected only in the manner provided by section 21. So, where a private company wants to convert itself into a public company, a special resolution will be necessary.

Further, the following requirements also should be noted:—

(1) Alteration of articles so as to delete the restrictive clauses mentioned in section 3(1)(iii);

(2) If the number of members is less than seven, it must be raised at least to seven; [*Vide* sections 12(1) and 45.]

(3) If the number of directors is less than three it must be raised to not less than three (section 252).

As regards the personal liability of directors of private companies converted into public companies, in cases where the income-tax dues of such companies could not be recovered from the companies themselves, see Notes under section 291 under that heading.

No change in the legal personality of a company is brought about by conversion to a public company nor does the company cease to exist bringing into existence any new company. *Hindustan Lever Ltd. v. B.S. Factory,* AIR 1964 Mys 173; See also, *Oshkosh B'Ghos Inc. v. Dan Marbel Inc.,* (1989) BCLC 507 (CA).

Conversion of public company into private company

There is no express provision, except the reference in the proviso to section 31(1) and (2-A) for converting a public company into a private company. Such conversion will require : (1) a special resolution authorising the conversion and altering the Articles so as to contain the matters specified in section 3(1)(iii); (2) changing the name of the company by special resolution as required by section 21 read with Section 13(1)(a) and filing the same with the Registrar as required by section 23; (3) obtaining the approval of the Central Government as required by section 31 (1) proviso; and (4) after obtaining the approval of the Central Government, a printed copy of the articles as altered should again be filed with the Registrar within one month of the receipt of the approval, as required by section 31(2-A).

This section does not prevent conversion of public company into a private company by alteration of its articles. *Radiant Chemical Co. Ltd., In re,* (1943) 13 Com Cases 186, 188 : AIR 1943 Pat 278.

Penalty for default

A private company which ceases to be so on alteration of its articles is required to file with ROC a prospectus or a statement in lieu of prospectus within 30 days of such cessation [sub-section (1)], containing particulars specified in sub-section (2). If default is made in complying with sub-section (1) or (2), the company and every officer of the company who is in default, are punishable with fine which may extend to Rs. 5,000 for every day during which the default continues. [Sub-section (3)]. The offence is a continuing one and is not subject to any bar of limitation for filing prosecution. The offence is compoundable under section 621-A.

Where any prospectus or statement in lieu of prospectus filed under section 44 includes any untrue statement, any person who authorised the filing of such prospectus or statement will be punishable, with imprisonment for a term which may extend to two years, or with fine which may extend to Rs. 50,000 [sub-section (4)].

Compoundable offence.—The offence is compoundable under S. 621A.

Prescribed Form.—Form No. 1-B has been prescribed for application to the Central Government for approval of conversion of a public company into a private company. (See *Appendix* 1).

ICSI Guidance Note on Compliance Certificate (August 2003)

Conversion of a Private Company into a Public Company under Section 44*

Check List

Check whether:

(i) the company has increased the number of its directors to minimum three;

(ii) the company has increased the number of its members to minimum seven;

(iii) the company has secured shareholders' approval by special resolution for deletion of the Article containing restrictive provisions applicable to a private company [vide section 3(1)(iii)];

(iv) the company has altered other regulations in the Articles which are not applicable to a public company;

(v) the company has filed Form No. 23 with the ROC alongwith the special resolution and explanatory statement;

(vi) the company has filed prospectus/statement in lieu of prospectus with the ROC;

(vii) the company has received a fresh/modified certificate of incorporation after deleting the word "private" in its name.

§ For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

§ For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

* This matter is not directly referred to in the 33 paragraphs appended to the Form prescribed under the Companies (Compliance Certificate) Rules. The Check List given by the ICSI under the heading 'Check List for Other Compliances' is for the guidance of CSP who may, in the course of his scrutiny, come across non-compliance with regard to this matter. CSP need not qualify such non-compliance.

Secretarial Practice Notes : Private Companies ceasing to be private to file statement in lieu of prospectus

Check that the prospectus or a statement in lieu of prospectus has been filed with the Registrar within 30 days of ceasing to be a private company.

Documents involved: 1. Minutes of Board/General meeting of company; (2) Articles of association of the company; (3) Prospectus or statement in lieu of prospectus.

Reduction of Number of Members below legal minimum

S. 45. Members severally liable for debts where business carried on with fewer than seven, or in the case of a private company, two members.—If at any time the number of members of a company is reduced, in the case of a public company, below seven, or in the case of a private company, below two, and the company carries on business for more than six months while the number is so reduced, every person who is a member of the company during the time that it so carried on business after those six months and is cognisant of the fact that it is carrying on business with fewer than seven members or two members, as the case may be, shall be severally liable for the payment of the whole debts of the company contracted during that time, and may be severally sued therefor.

NOTES

Eng. Act, 1948 : Sec. 31
Eng. Act, 1985 : Sec. 24

Previous Act : Sec. 147

Scope of section and effects of reduction in membership

The section will apply only when a company carries on business for more than six completed months with members below the legal minimum. The directors of the company who may be actually carrying on the business during this period will not be personally liable unless they also happen to be the members.

The increased liability of a member under this section can be avoided by the existing members by transferring some of their shares to some nominees or other persons and thus increasing the number of members of the company, up to or more than the minimum number required within the time prescribed.

Liability for the payment of debts under this section extends to the liabilities under various tax statutes.

Whether the company in question carries on business or not, and whether its membership is above or below the legal minimum, a company so long as it exists, must comply with the obligations imposed by the Act *e.g.* holding annual general meetings, submitting annual returns to the Registrar, etc.

Reduction of the number of members below the legal minimum is one of the grounds upon which a company may be wound up. [See section 433(d).] It is important to note, that, by the reduction in number, the company does not automatically cease. It can cease to exist only through the process of a winding up or by being struck off. See section 433(d) and section 560. Even if the number of members is reduced below the minimum, the company as a legal person will continue to exist until it is dissolved.

Where there is an impossible situation *e.g.*, if there are no directors or shareholders, the Company Law Board may intervene by calling a meeting, either on application by any interested person or on its own motion as provided in section 186.

It is said that for the purposes of this section, a deceased or insolvent member, though his name may be on the register, cannot be counted. See *Re, Bowling and Welby's Contract,* (1895) 1 Ch 663. But there is no reason why the legal representative of a deceased member or the official receiver or assignee of the insolvent's estate, should not step into his shoes and be entered as member in his place. But so long as the shares are not registered in the name of the legal representative of other person, he cannot be counted in the number of seven or two. See *Morgan v. Gray,* (1953) 1 All ER 213 at 217 (Ch D).

Personal liability where membership below minimum

A member of a company became liable severally and jointly with the company for the debts incurred during the period when he was the sole member of the company. He had himself purchased the shares of the only other member of the company. *Nisbet v. Shepherd,* (1994) BCLC 300 (CA). HOFFMAN LJ observed: "I have considerable sympathy with the appellant, who has fallen into a trap created by an ancient and obsolete rule. Section 24 of the Companies Act, 1985 requires that a company should have at least two members. In default of compliance it strips the remaining member of the protection of limited liability. The rule goes back to section 48 of the Companies Act, 1862 when the minimum number of members was seven. This reflects the evolution of company law from partnership, but the reason why it has survived through successive Companies Act is obscure. It seems to serve no purpose in protecting the public or anyone else. It is not necessary that the second member should hold his share or shares beneficially. The appellant could have satisfied the requirement of the Act by transferring a single share to his wife, lawyer or accountant to hold in trust for himself. But he did none of these things. Since 1983, the appellant has been the sole member and is liable accordingly."

All the members would be necessary parties even if they contend that they would not be severally liable under the circumstances of the case. *Madanlal v. Himatlal,* (1997) 1 Comp LJ 399 : (2000) 37 CLA 273 (MP).

Decree against company

It is certainly impermissible for an executing Court under the pretext of acting under section 45 to convert a decree granted against a company into one granted against the director thereof and proceed to order the arrest of the director. It is open to the decree-holder to approach the Court that granted the decree and call upon it to review the decree in the light of section 45. But the executing Court has no jurisdiction whatsoever to re-mould the decree and direct the arrest of the director. *Selvamurugan Chit Fund v. Nalamaharajan,* (1975) 1 Mad LJ 3 (Short Notes) (Mad).

Position of erstwhile deemed public companies

Important Note.—The following commentary and Department's Circular was applicable only to S. 43-A Companies. This category of companies has ceased to exist with the enforcement of Amendment Act of 2000. The commentary and the clarification have been retained for guidance in respect of pending matters.

The section did not affect private companies consisting of less than seven members becoming public companies by virtue of section 43-A.

The Supreme Court had observed in the case of *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.,* (1981) 51 Com Cases 743 at 840 : AIR 1981 SC 1298 that if a private limited company having 3 members becames a deemed public company by virtue of the erstwhile s. 43A and retained in its articles of association, the restrictions of s. 3(1)(iii), it would "attract the rigour of s. 45" if it continued to function with 3 members. The court further observed that such a company would also be liable to be wound-up under the provisions of s. 433(d). The learned judges seemed to have proceeded on the basis that certain sections such as s. 174(1), s. 220 and s. 252(1) made specific exemptions in favour of the erstwhile s. 43A companies while this section and s. 433(d) did not. These observations were apparently inconsistent with what had been stated earlier in this judgment at p. 834 of the report) *viz.* ".....the number of members of a public company cannot fall below 7 without attracting the serious consequences provided for by s. 45 (personal liability of members for the company's debts) and s. 433(d) (winding up in case the number of members falls below). A s. 43A company can still maintain its separate corporate identity *qua debts* even if the number of its members is reduced below seven and it is not liable to be wound-up for that reason."

Department's Clarification.—All the provisions of the Act which are applicable to a public company will, after 28-3-1961, generally apply to a company which has become a public company by virtue of section 43A of the Companies Act, 1956. However, the provisions of sections 12(1) and 45 which require a public company to have at least seven members will not apply to a deemed public company. The articles of association of such a company may continue to contain a provision similar to that in section 3(1)(iii) which is applicable to private companies. Section 44 also is not applicable to a private company, when it becomes a public company by virtue of section 43A and consequently such a company will not be required to file with the Registrar a statement in lieu of prospectus under section 44(1)(b). When it intends to raise subscriptions from the public, the company must comply with the requirements of s. 70. [*Circular No.* 48(50)-CL-IV/61, dated 12-2-1962].

Secretarial Practice Notes : Members severally liable for debts

Ensure that the company did not carry on business for more than six months if membership was below the prescribed number.

Documents involved:—(1) Registers of members; (2) Minutes of Board/General Meeting, dealing with business of the company.

Contracts and Deeds, Investments, Seal, etc.

S. 46. Form of contracts.—(1) Contracts on behalf of a company may be made as follows:—

(a) a contract which, if made between private persons, would by law be required to be in writing signed by the parties to be charged therewith, may be made on behalf of the company in writing signed by any person acting under its authority, express or implied, and may in the same manner be varied or discharged;

(b) a contract which, if made between private persons, would by law be valid although made by parol only and not reduced into writing, may be made by parol on behalf of the company by any person acting under its authority, express or implied, and may in the same manner be varied or discharged.

(2) A contract made according to this section shall bind the company.

NOTES

Eng. Act, 1948 : Sec. 32
Eng. Act, 1985 : Sec. 36

Previous Act : Sec. 88

This section deals with the manner in which contracts can be made on behalf of the company.

As regards contracts in which the company is undisclosed principal, see section 416.

Requirements for company's contracts

The effect of this section is to render valid any contract made on behalf of a company, provided it is made in the manner laid down in the section. "A company can as a general rule contract without seal. It is sufficient if the contract is made by some person acting under the express or implied authority of the company, nor need the contract, as a general rule, be in writing even,... it is sufficient if it is made by word of mouth, provided the person who makes it has authority to make it on company's behalf. Whether a person is acting on the implied authority of the company must depend on the articles of the company." PALMER'S COMPANY LAW, 19th edition, page 244. Clause (b) of the section permits oral contracts to be made on behalf of a company in all circumstances in which a contract would otherwise be valid. Where the directors of a company verbally tendered their resignations at the annual general meeting and the resignations were accepted, the verbal acceptance was held good. *Latchford Premier Cinema v. Ennion,* (1931) 2 Ch 409 : (1932) 2 Com Cases 106.

A commercial company may, subject to restrictions specifically imposed upon it by its memorandum or articles, always enter into a contract for the purposes of its business (including arbitration agreements) subject, in the matter of form, to section 46 of the Companies Act, 1956. *Societe De Traction et D'electricite Societe, Anonyme v. Kamani Engineering Company Ltd.,* (1963) 33 Com Cases 869, 875: AIR 1964 SC 558, 562.

In all cases, the essential condition for the validity of a contract of a company is that it must be signed or made by a person acting under its authority, which may be express or implied.

Directors' power to sign contracts

Usually the articles of a company give the directors all the powers of the company and consequently authority to enter into contracts. The authority can be exercised in a Board meeting. If the Board approves the contract, the directors thereat can sign the contract on behalf of the company. PALMER'S COMPANY PRECEDENTS, 212 (17th Edn., Vol I).

Oral consent to arbitration by directors

Where an agreement in the nature of consent to arbitration could be made by a private individual by giving oral consent, the same mode can be employed by the managing director of the company also while acting on behalf of the company. The directors of the company are agents and the company acts through such directors as its agents and, therefore, even an oral consent given by the managing director on behalf of the company shall bind it. Besides these circumstances, the agreement in question was validly made and the same could not be disputed on that ground. *Jupiter Chit Fund P. Ltd. v. Som Nath Handa,* 1983 All LJ 704 at 707 (All). However, the agreement should be in writing. See S. 7(3)

of the Arbitration and Concliation Act, 1996. For detailed study out the subject see JUSTICE BACHAWAT'S LAW OF ARBITRATION AND CONCILIATION, 170 (3rd edn., 1999).

Delegation of authority

The articles of most of the companies provide for delegation of the directors' powers to committees or to managers or other persons. In such cases, the committees, managers or persons to whom the directors' powers are delegated can sign contracts on behalf of the company. The authority to act can be granted by an ordinary resolution in a general meeting. *Grant v. United Kingdom Switchback Railway Co.,* (1888) 40 Ch D 135 (CA).

***Ultra vires* contracts cannot be ratified**

The powers of a company incorporated under the Companies Act are bounded by the memorandum of association, and any contract made otherwise than in the exercise of such powers is *ultra vires* of the company and void, even if the whole body of shareholders assent to it and such a contract is incapable of ratification. *Ashbury Railway Carriage & Iron Co. v. Ricke,* (1875) LR 7 HL 653; *Attorney-General v. Great Eastern Railway Co.,* (1880) 5 App Cases 473; *Attorney-General v. Mersey Railway Co.,* (1907) 1 Ch 81 : (1907) AC 415; *London County Council v. Attorney General,* (1902) AC 165; *Re, Lee Behrens & Co.* (1932) 2 Ch 46 : (1932) 2 Com Cases 588.

Ratification of unauthorised acts.—Ratification is possible only where the contract is within the powers of the company but it has been entered into by its agents either without authority or otherwise irregularly. *Grant v. United Kingdom Switchback, etc.,* (1888) 40 Ch D 135 (CA); *Libertas-Kommerz Gmbtl,* 1978 SLT 223 : 1977 SC of Scotland 191.

A person dealing with a company can use the doctrine of ostensible authority to hold the company to the contract; the company can also ratify an unauthorised contract, provided that the act is otherwise lawful, so as to hold the other party bound by the contract but not where a ratification by resolution of the directors or members is no longer possible because, for example, a quorum cannot be found, *Re Qintex Ltd (No. 2)* (1990) 2 ASCR 479, (Aust.) or ratification will prejudice another person. *NM Superannuation Pty Ltd. v. Baker* (1992) 7 ACSR 1052 (Aust.).

Directors incur no personal liability

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. *Gadd v. Houghton,* (1876) 1 Ex D 357; *Newborne v. Sensolid (Great Britain) Ltd.,* (1953) 1 All ER 708 : (1954) 24 Com Cases 159; *Badgerhill Properties Ltd. v. Cottrell,* (1991) BCLC 805 (CA). 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 undertook personal liability. PALMER'S COMPANY PRECEDENTS *loc. cit.* p. 511.

Mode of signing contracts on behalf of company

Where, however, the words showing that the person who signs is signing for or on behalf of the company are omitted, it will nevertheless be the company and not the person so signing who can sue and be sued on the contract if the intention is clear that the signature shall only be that of the company, *Chapman v. Smethurst,* (1909) 1 KB 927, and *Newborne v. Sensolid (Great Britain) Ltd.,* (1953) 1 All ER 708 (CA). *Cf. The Swan,* [1968] 1 Lloyd's Rep 5, 13; *Bondina Ltd. v. Rollaway Shower Blinds Ltd.,* (1986) 1 All ER 564 : 1986 BCLC 177 (CA).

The company by its corporate name should be a party thus: Between the AB Company, Ltd. of the one part and CD of the other part.

The signing must show on the face of the contract that the person signing is acting for or on account of or on behalf of the company thus: "For and on behalf of AB Company

Ltd." This may be written or printed above or below or opposite signature. If the contract is sealed, it must end with the words:

> "As witness the common seal of the company and the hand [and seal] of— this day of the year."

As regards, contracts on behalf of a company, care must be taken to comply with the requirements of section 147 also, in respect of transactions covered by that section.

The section only says "contracts on behalf of company may be made ...." The section does not prevent a company providing by its articles the details of the form and other requirements as regards the making of contracts of any kind on its behalf.

The expression "may in the same manner, be varied or discharged" is only permissive and not compulsory. It does not mean that if a contract is in writing or under seal, the variation or discharge should likewise be only in writing or under seal. It may be varied or discharged in any other manner permitted by law.

Signing of International Contract

Where the terms and conditions of the contract showed that the English Law was applicable to the Contract and therefore it had to be signed in accordance with that Law but no evidence was produced to show the requirement of English Law on the point, the Court remanded the case for production of evidence on the point. *Rhodia Ltd. v. Neon Laboratories Ltd.,* AIR 2002 Bom 502 at 511.

Authority to act on behalf of company

Who has authority to act for and on behalf of the company is a question of frequent occurence in company matters. In many cases express authority is found in the articles. The articles usually empower the directors and also empower them to make the delegation of the directors' powers to committees, managers, managing directors, or other persons, and such delegation may be made either expressly, or by implication, as where an agent is permitted to exercise certain powers; or he may have ostensible authority to exercise such powers. If the person dealing with the officer can show that the officer had ostensible authority, or that such authority was within the ordinary scope of his duties, the company will be held liable for his acts even if he had been expressly forbidden to do such acts. *Freeman and Lockyer v. Buckhurst Park Properties (Mangal) Ltd.,* (1964) 1 All ER 630 (CA); *Rhodian River Shipping Co. SA v. Halla Maritime Corpn.,* (1984) BCLC 139 (QBD); *Egyptian International Foreign Trade Co. v. Soplex Wholesale Supplies Ltd.,* (1985) BCLC 404 (CA) (the Court explaining the proper approach in determining the scope of an agent's apparent authority).

This statement was **relied** upon by the High Court of Delhi in *Mohta Alloy and Steel Works v. Mohta Finance and Leasing Co. Ltd.,* (1997) 89 Com Cases 227 at 240 (Del). The court held that a lease agreement signed by a single director, even in the absence of a Board resolution authorising him to do so, bound the company. The position under the article was that directors and managing directors were given powers to enter into contracts. On facts, the chairman had authorised the director in question to execute the agreement and this was held to be a sufficient authorisation. An act by the directors or an officer in excess of authority may be ratified by the competent body. *Bamford v. Bamford,* (1969) 1 All ER 969 (CA); *Re, Land Credit Company of Ireland,* (1869) LR 4 Ch 460, 469.

Where a person was director in two companies of the same group and he himself signed an agreement on behalf of both companies acting in his capacity as a director of the respective companies, the court said that this was permissible. *Mohta Alloy and Steel Works v. Mohta Finance and Leasing Co.,* (1997) 89 Com Cases 227 at 241 : (1997) 3 Comp LJ 183 (Del). Furthermore, there was ratification as well as acquisance on the part of the petitioner company in respect of the lease agreement. The court **relied** upon the

Supreme Court decision in *LIC v. India Automobiles and Co.,* (1990) 4 SCC 286 and also referred to the doctrine of indoor management.

"The company will not be bound by any agreement if an agent of the company has entered into an agreement without actual authority, whether express or implied to enter into a contract. For any such agreement to be binding on the company that company should either accept the said agreement or ratify the same." *Deepa Anant Bandekar v. Rajaram Bandekar (Sirigao) Mines P. Ltd.,* (1992) 74 Com Cases 42, 53 (Bom).

Persons dealing in good faith.—Section 35(1) of the [English] Companies Act, 1985 which restricts the scope of the doctrine of constructive notice, gives this added protection to persons contracting with companies that if they deal in good faith, that is to say, without notice or any suspicion, about the authority of the directors through whom the dealing was finalised, the directors' authority would be deemed to be free of any limitation under the memorandum or articles. Section 35(2) of Act further provides that persons dealing with the company would be deemed to be acting in good faith till the contrary is proved. The protection of section 35(1) is only available if the director who purported to act for the company has either actual authority or ostensible authority. *Cartmell's* case, (1874) LR 9 Ch 691 [as to the authority of manager]; *Harold Holdsworth Ltd. v. Caddies,* (1955) 1 WLR 352 [managing director]. Where the circumstances are so unusual that the third party is put on inquiry and if he fails to inquire he cannot be said to have acted in good faith. *Cf. TCB Ltd. v. Gray,* (1986) BCLC 113 : (1986) 1 All ER 587 (CA).

Duty of those dealing with company to ascertain authority

As a company is not a living person and can only act through agents, any one entering into a contract or other transaction with it is bound to know or ascertain whether the person acting on behalf of the company has authority to do so. Such authority is ascertained both from the provisions of the Companies Act, and the constitution of the company as contained in its memorandum and articles.

The present section provides that a contract made on behalf of a company will be binding on it, if it is made by a person acting under its authority, either expressly given to him under the articles or in any manner provided by the articles such as by delegation, sub-delegation, etc., or exercisable by necessary implication from the office, position or other connection or relation of the person with the company. As in any case the authority of the company is necessary for acting on its behalf it behaves all those dealing with the company to ascertain whether such authority in fact exists.

Acts within usual authority

As a matter of business convenience, however, it has long been recognised that where officers of a company occupying position such as those of a managing director, or other director or manager or other officer to whom under the company's articles or agreements, or resolutions specified in section 192, of which third persons can have notice, any power or authority could be delegated or sub-delegated, and such person purports to exercise such power or authority, and person in his position usually exercises such power or authority, outsiders dealing with the company may reasonably assume that the person apparently or ostensibly exercising any such power or authority has been duly authorised to exercise it, whether in fact he is so authorised or not. This rule is based not only on the ground of estoppel but also business convenience. For otherwise, ordinary business dealing with companies will be intolerable if everybody in day-to-day business is required to examine the company's machinery in order to satisfy himself that the person he is dealing with has actual authority to enter into transactions on behalf of the company. For a thorough discussion of the subject. See *Freeman and Lockyer v. Buckhurst Park Properties (Mangal) Ltd.,* (1964) 1 All ER 630 : (1964) 2 Comp LJ 36 and *Hely Hutchinson v. Brayhead Ltd.,* (1967) 2 All ER 14 : (1967) 2 Comp LJ 67 and on appeal, (1968) 1 Comp LJ 263 : (1967) 3 All ER 98 (CA). See also, *Canjeevaram Hodgsonpet Thanarakshama Nidhi Co. v. Kandaswamy Naicker,* AIR 1916 Mad 496 and Notes under s. 290.

On an analysis of the relevant law, DIPLOCK LJ in *Freeman & Lockyer v. Buckhurst Parks Properties (Mangal) Ltd.*, (1964) 1 All ER 630 (CA) noted that there are four conditions which must be satisfied to entitle a contractor to enforce a contract entered into on behalf of the company by an agent who had no actual authority to do so. It must be shown that :

(1) A representation that the agent had authority to enter on behalf of the company into a contract of the kind sought to be enforced was made to the contractor.

(2) Such representation was made by person or persons who had 'actual' authority to manage the business of the company either generally or in respect of those matters to which the contract relates.

(3) The contractor was induced by such representation to enter into the contract, that is, that he in fact relied upon it.

(4) Under its memorandum or articles of association the company was not deprived of the capacity either to enter into a contract of the kind sought to be enforced or to delegate authority to enter into a contract of that kind to the agent.

His Lordship observed that the confusion which has sometimes crept into the cases is due to a failure to distinguish between these four separate conditions, and in particular to keep steadfastly in mind (a) that the only 'actual' authority which is relevant is that of the person making the representation relied upon, and (b) that the memorandum and articles of association of the company are always relevant (whether they are in fact known to the contractor or not) to the questions (i) whether condition (2) is fulfilled and (ii) whether condition (4) is fulfilled, and (but only if they are in fact known to the contractor) may be relevant (iii) as part of the representation on which the contractor relied.

In his judgement in the *Freeman's case* (*supra*), DIPLOCK LJ also referred to the cases where the contractor's claim failed, namely *Houghton & Co v. Nothard, Lowe & Wills Ltd.*, (1927) 1 KB 246, *Kreditbank Cassel GmbH v. Schenkers Ltd.*, (1926) 2 KB 450 and (1927) 1 KB 826 (CA); *Rama Co. Ltd. v. Proved Tex & General Advertisements Ltd.*, (1952) 1 All ER 554. These were all cases where the contract sought to be enforced was not one which a person occupying the position in relation to the company's business which the contractor knew that the agent occupied, would normally be authorised to enter into on behalf of the company. The conduct of the Board of directors in permitting the agent to occupy that position, upon which the contractor relied, thus did not of itself amount to a representation that the agent had authority to enter into the contract sought to be enforced, that is, condition (1) was not fulfilled. The contractor, however, in each of these three cases sought to rely upon a provision of the articles giving to the Board power to delegate wide authority to the agent as entitling him to treat the conduct of the Board as a representation that the agent had delegated to him wider powers than those usually exercised by persons occupying the position in relation to the company's business which the agent in fact was permitted by the Board to occupy. See also *Varkey Souvier v. Kerabeya Banking Co. Ltd.*, (1957) 27 Com Cases 591 (Ker.).

A person with actual authority to obtain quotations of prices has no implied authority to communicate acceptance of such quotes where no decision to purchase has been made by his principal—at most such a person may have apparent authority. *Crabree-Vickers Pty Ltd. v. Australia Direct Mail Advertising Co. Pty. Ltd.*, (1976) 5 A.L.J.R. 203 (Aust.).

The assignment by a director-manager of a decree obtained by a company in favour of a third party, though without valid authorisation of the Board of directors, was held to be valid, on the principle that a third party who deals with directors or managers acting under the powers of the Board of directors however irregularly is protected, if he acts in good faith in his dealing with them. *Ram Baren Singh v. Muffasil Bank* AIR 1925 All 141. Also see *Dehradun Mussorie Electric Transway Co. Ltd.*, (1931) 1 Com Cases 277 (All) wherein it was held that the mortgage security given by the managing director, though such power was not delegated to him by the Board of directors, was binding on

the company as the mortgage executed was *bona fide* necessary for meeting an emergency.

"Actual authority" and "apparent" or "ostensible" authority

The law on the subject of actual and apparent or ostensible authority is discussed at length by DIPLOCK, LJ, in the case of *Freeman v. Buckhurst Park Properties* referred to above, and is succinctly expressed by LORD DENNING MR in the later case, *Hely Hutchinson v. Brayhead Ltd.*, (1967) 3 All ER 98 (CA) as follows:

Actual authority may be express or implied. It is express when it is given by express words, such as when a Board of Directors, pass a resolution which authorises two of their number to sign cheques. It is implied when it is inferred from the conduct of the parties and the circumstances of the case, such as when the Board of Directors appoint one of their number to be managing director they thereby impliedly authorise him to do all such things as fall within the usual scope of that office. Actual authority express or implied, is binding as between the company and the agent and also as between the company and others, whether they are within the company or outside it.

Ostensible or apparent authority is the authority of an agent as it appears to others. It often coincides with actual authority. Thus when the Board appoints one of their number to be managing director, they invest him not only with implied authority, but also with ostensible authority to do all such things as fall within the usual scope of that office. Other people who see him acting as managing director are entitled to assume that he has usual authority of a managing director. But sometimes ostensible authority exceeds actual authority. For instance when the Board appoints the managing director, they may expressly limit his authority by saying he is not to order goods worth more than £ 500 without the sanction of the Board. In the case his actual authority is subject to the £ 500 limitation, but his ostensible authority includes all the usual authority of a managing director. The company is bound by his ostensible authority in his dealings with those who do not know of the limitation.

In the case of actual authority, it has to be noted, that either it may be express, as where authority is specifically given by the memorandum of articles or resolution of the company in general meeting or by the Board of Directors, or it may be implied from conduct such as the holding of a particular office or the delegation of a particular function or duty which carries with it authority to do certain things or enter into certain contracts or incur contractual obligations on behalf of the company. For instance, if a person is appointed as the manager of a branch office, he has implied authority to do everything connected therewith and which are normally required for the proper management of that office.

It sometimes happens that a person is allowed to act or continue to act as managing director or manager or in any other office without being formally appointed or re-appointed by the company. In such a case, his acts coming within the range of operation of the powers usually attached to the office and not inconsistent with the provisions in the company's articles will be binding on the company as he will be considered to be acting on the apparent authority to act in that capacity. The failure to make the appointment or re-appointment will only be an irregularity in the internal management of the company, with which, under the rule in *Turquand's* case (*Turquand v. Marshall*, (1869) 4 Ch App 376), outsiders are not concerned. See *Sorrell v. Finch*, (1976) 2 All ER 371 (HL). But any outsider having knowledge of the irregularity will not be protected.

Where the managing director of a company purports to do an act, the doing of which is under the articles of the company within the powers of his co-directors to delegate to him, persons dealing with him *bona fide* and in the ordinary course of business may assume that he has the power which he professes to have and are not bound to enquire whether or not such power has in fact been delegated to him. *Howard v. Rowatt's Wharf Ltd.*, (1896) 2 Ch 93.

A director cannot resort to the *Turquand* rule when he is representing the company for it is obligatory for him to know his position in the business. *Howard v. Patent Ivory Co.*, (1888) 38 Ch D 156. In *Morris v. Kanssen,* (1946) 1 All ER 586 (HL) a person was appointed director of a company and immediately thereafter there was an unauthorised allotment of shares to him, it was held that the director could not claim protection of ignorance under the *Turquand* rule.

Where under a company's articles the company's cheques had to be signed by two directors and the sole acting director falsely told the banker that his wife had been appointed as a co-director and the banker encashed cheques signed by the husband-wife duo, it was held that the banker was not protected against such encashments because the circumstances were suspicious and the banker had made no enquiry whether the director's wife had actually been appointed or not. *B. Liggett (Liverpool) Ltd. v. Barclays Bank Ltd.*, (1928) 1 KB 48.

As regards apparent or ostensible authority the point to be noted is that as a company can only act through the agency of its officers, and the objects and powers of the company are limited by its memorandum of association and the articles or regulations for the time being in force, any one dealing with the company has to see whether an act, contract, or other transaction of the company, with which he is concerned, is within the powers of the company and whether it is ordinarily or usually within the scope of authority of the particular officer or officers purporting to act on behalf of the company. If, from the nature of the transaction or other circumstances, there is anything to suggest that the exercise of a power or authority or the doing of a particular thing would be unusual or out of the ordinary and not within the normal ambit of the officer's powers, one dealing with him cannot assume that the officer would have been authorised by the Board of Directors or other competent authority to enter into the contract or transaction or do the act in question.

To bind a company for an act of an agent, it must be established that the transaction fell within the implied, actual or ostensible authority of the agent. *British Bank of Middle East v. Life Insurance Company of Canada, (UK) Ltd.,* 1983 BCLC 78 : (1985) 1 Comp LJ 27 (HL).

Unlike under the English Act, under the Companies Act of India, it cannot be assumed that the managing director of a company has any definite powers of management. The definition of "managing director" shows that he will have only such powers as may be entrusted to him. So it will be the duty of banks and others dealing with him to take care to know whether any particular contract or transaction will be within the ambit of his powers.

Commission agreement for business.—An employee was described as 'Director PSU Sales'. He was required by the terms of employment to perform such duties as may be reasonably associated with his job title. It was held that such power would give him authority to enter into a commission agreement for business introduced by a rival supplier. *SMC Electronics Ltd. v. Akhter Computers Ltd.*, (2001) 1 BCLC 433 (CA).

EEC Developments.—The following EEC Directives are relevant in this context:

The move in favour of security of transaction is required by the First Company Law Directive of the EEC (68/151/EEC). The preamble to that Directive states that :

".....the protection of third parties must be ensured by provisions which restrict to the greatest possible extent the grounds on which obligations entered into in the name of the company are not valid."

Article 9(2) of that Directive provides :

"The limits on the powers of the organs of the company, arising under the statutes or from a decision of the competent organs, may never be relied on as against third parties, even if they have been disclosed."

Article 9(2) of the Directive was implemented by CA 1985, ss. 35A and 35B. These sections provide as follows :

S. 35A(1) In favour of a person dealing with a company in good faith, the power of the Board of Directors to bind the company, or authorise others to do so, shall be deemed to be free of any limitation under the company's constitution.

(2) For this purpose—

(a) a person 'deals with' a company if he is a party to any transaction or other act to which the company is a party;

(b) a person shall not be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company's constitution; and

(c) a person shall be presumed to have acted in good faith unless the contrary is proved.

(3) The references above to limitations on the directors' powers under the company's constitution include limitations deriving—

(a) from a resolution of the company in general meeting or a meeting of any class of shareholders, or

(b) from any agreement between the members of the company or of any class of shareholders.

S. 35B. A party to a transaction with a company is not bound to enquire as to whether it is permitted by the company's memorandum or as to any limitation on the powers of the Board of Directors to bind the company or authorise others to do so.

§ For S. 35 of the English 1989 Act see under the heading "Persons dealing in good faith" (*supra*).

It has been held that sections 35A and 35B did not apply where the company was made a party to a transaction of the assignment of the company's cause of actions to the chairman-cum-director. Giving consent to such a transaction was outside the director's authority. The Board of directors could have ratified the transaction, but no valid. Board meeting was held for that purpose because he alone was present. The company's purported ratification was in essence a new transaction of assignment. It was not allowed to be added to the pending proceedings because it required an amendment of the plaintiff in a manner which was not permissible. *Smith v. Henniker Major & Co.*, (2002) BCC 544 (Ch. D). The court **followed** the decision in *Hendry v. Charlsearch Ltd.*, 1998 CLC 1382 : 1998 CLY 401. An appeal against the decision in the *Smith* case was **dismissed** in *Smith v. Henniker Major & Co.*, (2002) EWCA Civ. 762 (CA). It was held that the chairman-cum-director could not rely on his own mistake to transform his resolution, which was invalid under the company's constitution, into a decision of the Board of directors. Although s. 35A could apply to a director, it did not apply in the exceptional circumstances of the instant case. He was also the company chairman and therefore it was his duty to ensure compliance with the company's constitution. The subsequent deed could not retrospectively ratify the assignment as it included additional provisions.

Liability of company in case of forgery

It has been stated to be a "well established principle that strangers are entitled to assume that all things connected with the transactions and pertaining to the internal management of the company have been validly done has no application to fraud and forged instruments, as forged instruments are simply null and void. A secretary is a mere servant. His position is that he has to do what he is told and no person can assume that he has any authority to represent anything at all. If the secretary is shown to have either express authority to perform certain acts or implied authority by a course of dealing the company would be liable. In other words, if he is acting within the scope of his authority, the actions of the secretary will bind the company, even if done tortiously or fraudulently and even though they ensure not for the company's benefit but for the secretary himself." This observation occurs in a division bench decision of the Madras High Court in *Nagueri Peace Memorial Cooperative Urban Bank Ltd. v. Alamelu Ammal*, (1961) 31 Com Cases 705 at 711, 712 (Mad—DB). The court cited the following authorities on the subject at p. 712: "These established rules and principles will equally apply whether in the law of agency, or in the law of master and servant. In GOWER'S MODERN COMPANY LAW, at page 157, the learned author has put the whole proposition of law in a nutshell

thus: "If a document purporting to be sealed by or signed on behalf of the company is proved to be a forgery, it does not bind the company. But the company may be estopped from disclaiming the document as a forgery if it has been put forward as genuine by an official acting within his actual, usual, or apparent authority and if a transaction is binding on the company under the foregoing rules the company will be liable notwithstanding that the official has acted fraudulently or committed forgery." Similarly BOWSTEAD in his well known book, A DIGEST OF THE LAW OF AGENCY, has stated under article 82: "No principal is bound by any act of his agent which is not done within the agent's actual or implied authority unless the principal in fact authorised the agent to do the particular act." Dealing with the facts of the case the court found that the secretary exercised or purported to exercise an authority to bind the bank by committing a fraud and thereby he acted outside the scope of his ordinary ostensible authority. When he had no such authority, the deposit receipts signed by him were only a waste paper. Further, he had forged the signature of the directors and thereby committed a fraudulent act. Certainly the fraudulent act of the secretary of the bank would not bind the bank. Though the receipts were not valid, the company who held liable for the amount which it acknowledged it had actually received under those receipts.

Representation of authority should emanate from company

It is necessary that representation of authority should emanate from the company. A self representation by the officers as to the scope of his authority does not affect the company's position *e.g.*, an officer who was occupying the position of secretary and general manager taking a car on lease by representing himself to be the president of the company. The transaction did not bind the company. *First City Capital Ltd. v. 105383 BC Ltd.*, (1985) 28 BLR 274 (CA—Columbia). To be contrasted with *Panorama Developments (Guildford) Ltd. v. Fidelis Furnishing Fabrics Ltd.*, (1971) 2 QB 711 involving hiring of cars by the secretary of the company. Where a mortgage on company's land was executed by one out of three directors and by a person acting as the company secretary and they affixed the company's seal and the mortgage was given not to cover the company's debts but to cover the debts of other companies controlled by the directors, the mortgage was held to be a forgery which did not bind the company. *Northside Developments Pty. Ltd. v. Registrar-General,* (1990) 170 CLR 146 (Aust).

Validity of acts of directors

For Notes on validity of acts of directors, see comments under s. 290.

Contracts made before incorporation

According to the Common Law prevailing in England, a company cannot enter into a contract before its incorporation because it does not yet exist as legal person. Nor, for the same reason, it is bound by the contracts made by agents on its behalf before its incorporation. It is, however, open to the company to enter into a fresh contract after its incorporation. Under the general principles, it cannot even ratify such contracts made by the promoters before its incorporation. See *Kelner v. Baxter,* (1866) LR 2 CP 174 and *Newborne v. Sensolid (Great Britain) Ltd.,* (1953) 1 All ER 708 : (1954) 24 Com Cases 159. See also *Ramkumar Potdar v. Sholapur Spg. & Wvg. Co. Ltd.,* (1934) 4 Com Cases 481 (Bom). It makes no difference that the contract delimits the funds out of which the other contracting party is to be paid out of the company's paid up capital. *Scott v. Lord Ebury,* (1867) LR 2 CP 255. Nor does it make any difference if the contract were expressly made conditional on the company being incorporated. The position has, however, changed with the passing of the European Communities Act, 1972, under which it is provided by s. 9(2) (now incorporated in s. 36C of the English Act of 1989) that unless there is a clear exclusion of liability, a person who purports to contract on behalf of a company not yet incorporated, is personally liable on the contract. See *Phonogram Ltd. v. Lane,* (1981) 3 All ER 182 (CA); *Cotronic (UK) Ltd. v. Dezonie,* (1991) BCLC 721 (CA), where also the contracting agent was held liable and the court added that this liability would not by itself give him the right to sue the other side.

On its true construction, s. 36C(1) of the 1985 Act [English] not only entitles a party who has entered into a contract with an unformed company to enforce that contract against the person purporting to act for or as agent of the unformed company, but also entitles such a person or agent to enforce the contract against the other party unless such enforcement was otherwise precluded by the ordinary common law principles governing contractual arrangements. **Applying** this principle to the facts of *Braymist Ltd. v. Wise Finance Co. Ltd.*, (2002) 1 BCLC 415 : (2002) 111 Com Cases 402 (CA), the Court of Appeal held, B. Ltd.'s solicitors were entitled under s. 36C(1) to enforce the agreement against the purchaser as a party to it. In those circumstances, the solicitors were to be treated as having signed the agreement on their own behalf for the purposes of s. 2 of the Law of Property (Miscellaneous Provisions) Act, 1989. The solicitor had signed the contract on behalf of the unformed company for sale of its land.

The expression "pre-incorporate contract" does not include a contract entered into after a changeover of name, *Oshkosh B. Gosh Inc. v. Dan Marbel Inc.*, (1989) BCLC 507 (CA); *Vic Spence Associates v. Balchin*, 1990 SLT 10 (Scotland), nor a contract made after restoration of a company struck off the register earlier. *Cotronic (UK) Ltd. v. Dezonie*, (1991) BCLC 721 (CA), nor still a contract on which the name of the company was mis-described. *Badgerhill Properties Ltd. v. Cottrell*, (1991) BCLC 805 (CA). In *Cross v. Aurora Group Ltd.*, 4 NZCLC 64, 909 (New Zealand) the company was already in existence when the promoter contracted. It tried to ratify the contract after the promoter had taken it over as a running concern. The court said it was impossible.

Effect of Specific Relief Act.—In India there is a marked deviation from the principles of the common law. Under the provisions of S. 19(e) of the Specific Relief Act, 1963, specific performance may be enforced against a company where its promoters have, before its incorporation, entered into a contract for the purposes of the company and such contract is warranted by the terms of incorporation of the company, *e.g.* "by inclusion in the articles of association. It is, however, necessary that the company in such a case must have accepted the contract after its incorporation and communicated such acceptance to the other party to the contract. Section 15(h) of the same Act, which is identically worded, provides for obtaining of specific performance by a company. In view of these two provisions the decisions of the English courts stating that a pre-incorporation contract of a promoter on behalf of the company is a nullity and cannot be enforced by or against the company, must be considered in the light of Ss. 15(h) and 19(e) of the Specific Relief Act, 1963.

However, the Companies Acts of some commonwealth countries now contain a provision as to ratification. Where a person was appointed managing director before incorporation and after the incorporation the appointment was affirmed and he was informed accordingly, it was held that the appointment had become binding on the company and the mere fact that in the letter of confirmation the company had added certain definite terms to the appointment which were not there before, did not make any difference particularly because those terms were necessary to ensure conformity with the company's memorandum and articles. The company's attempt subsequently to remove him was held to be a breach of contract. *Cosmic Insurance Corpn. Ltd. v. Khoo Chiang POH*, [1980-1984] LRC (Comm) 577.

In the case of *Seth Sobhag Mal Lodha v. Edward Mills Co. Ltd.*, (1972) 42 Com Cases 1 (Raj) the High Court of Rajasthan followed the English decisions in holding that a contract entered into on behalf of a company before its incorporation as not binding on the company. Evidently the provisions of the Specific Relief Act, were not brought to the notice of the learned judges. There remains for consideration a class of cases in which a promoter enters into a contract on behalf of a company to be incorporated and the company does not ratify the contract. In such a case the question will arise as to whether the promoter is personally liable to the other contracting parties on the footing that he himself is the party to the contract.

Pre-incorporation contracts binding on persons contracting.—Although a contract made before a company's incorporation cannot bind the company, it is not wholly devoid of legal effect, even if all the persons who negotiated the contract are aware that the company has not yet been incorporated. *Phonogram Ltd. v. Lane,* (1981) 3 All ER 182 **applied** in *Cotronic (UK) Ltd. v. Dezonie,* 1991 BCLC 721 (CA). The contract takes effect as a personal contract with the persons who purport to contract on the company's behalf, *Kelner v. Baxter,* (1866) LR 2 CP 174, and they are liable to pay damages for failure to perform the promises made in the company's name; this is so despite the fact that the contract expressly provides that only the company's paid-up capital shall be answerable for performance. *Scott v. Lord Edury,* (1867) LR 2 CP 255.

It is open to doubt whether a person claiming to be an agent of a non-existent principal can be rendered personally liable on the contracts made by him on behalf of such principal. Under the terms of section 230 of the Indian Contract Act, in the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal nor is he personally bound by them. Such contract is presumed to exist in the following cases, *viz.*,

(1) where the contract is made by an agent for sale or purchase of goods for a merchant resident abroad;

(2) where the agent does not disclose the name of his principal and where the principle though disclosed cannot be sued.

An agent, therefore, is not personally liable, nor is he entitled to sue on a contract unless the contract so expressly provides or it is on behalf of the foreign principal or where the principal is disclosed but cannot be sued. The last branch of the rule cannot apply where there is no principal in law. It is submitted, therefore, that under the scheme of Indian Contract Act where a promoter of a company enters into a contract for and on behalf of the company to be incorporated and the company after its incorporation does not ratify the contract entered into on its behalf by its promoter, the promoter cannot sue on such contract nor can he be sued on such contract except on the principle of *quantum meruit* or for breach of warranty of authority. *Royal Bank of Canada v. Starr,* (1985) 31 BLR 124 (Canada).

Claim under *quantum meruit*.—An agent's personal liability under a contract which he makes in the name of a company not yet formed, does not enable him to sue the other party under the contract. But if he has rendered any services to the other party under the purported contract, he may sue for those services under a *quantum meruit* claim. Such claim as recognised by the Court of Appeal in *Cotronic (UK) Ltd. v. Dezonie,* (1991) BCLC 721 (CA), where the court added that section 34 of the 1985 Act does not have the effect of preventing such claims. This is now subject to section 36C brought in by 1989 Act [English Act].

How to make pre-incorporation contracts binding.—Promoters who want to bind the other party to contract must assume personal responsibility under the contract. They may, however, limit their liability. The promoter may obtain an option on the terms that the rights contained in the agreement may be assigned to the future companies. Alternatively the promoter may contract as trustees for the proposed company subject to this condition that on the company entering into a new contract on similar terms the promoter would be released from his liability. Still alternatively, the promoters may prepare only a draft agreement which is to be adopted by the company with an express provision in the objects clause for such adoption. It may be provided in a pre-incorporation contract that the person making the contract would be released from liability under it if the company, after incorporation, enters into a second contract with the contractor on the same terms as the pre-incorporation contract. This is called 'novation'. The problem for the contractor is to prove that the company did make a new contract after incorporation. The courts require very clear evidence *Bagot Pneumatic Tyre Co. v. Clipper Pneumatic Tyre Co.,* (1902) 1 Ch 146 (CA). Simply acting in the mistaken belief that a pre-incorporation con-

tract is binding is not enough *Re, Northumberland Avenue Hotel Co.,* (1886) 33 Ch D 16 (CA).

Property purchased by promoters.—In *Weavers Mills v. Balkis Ammal,* AIR 1969 Mad 462 at 470 Madras High Court held that where the defendants acting as the promoters of a company purchased certain properties expressly stating that they did so as representatives of the company to be formed, and that on incorporation the company assumed possession of the properties and improved them, these facts clearly showed that the company adopted the benefit of the purchase. The property therefore belonged to the company. The correctness of this decision is doubtful, since it appears to be clearly **contrary** to S. 54 of the Transfer of Property Act, 1882. The ruling in *Weavers Mills (supra)* was **relied on** in *Vali Pattabhirama Rao v. Sri Ramanuja Ginning & Rice Factory P. Ltd.,* (1986) 60 Com Cases (AP—DB). For detail, see Notes under section 575, *post.*

A similar approach was adopted by the Court of Appeal in *Banner Homes Group plc v. Luff.* (2000) 2 BCLC 269 (CA). There was an arrangement between certain developers to acquire a site as a joint venture. The joint venture company acquired the site before the agreement between the shareholders could be signed. The court followed the equitable principle laid down in *Pullant v. Morgan,* (1952) 2 All ER 951 : (1953) Ch. 43 and held that the kind of equity arose on the acquisition of the relevant property by one of the partners to a pre-acquisition arrangement or understanding. The arrangement was to the effect that the acquiring party would take steps to acquire the property, and that, if he did so, the other party would obtain some interest in the property. The pre-requisition arrangement coloured the subsequent acquisition by the defendant and led to his being treated as a trustee, if he sought to act inconsistently with the arrangement. It was not necessary for this purpose that the arrangement or understanding should be contractually enforceable. The judge was wrong in holding that a constructive notice could not be imposed in the circumstances because to do so would be, to remake the parties bargain.

In case the promoter had acquired the property after he became a promoter, the company would have had the option either to rescind the contract or affirm it in order to claim profits for itself. *Bank of London v. Tynell,* (1862) 10 HLC 26.

Where a company, after incorporation, takes possession of property transferred to it in a pre-incorporation contract, the court may be able to infer that the only possible explanation is that a new contract was made after incorporation. *Patent Ivory Manufacturing Co., Re,* (1888) 38 Ch D 156; *Heinhuis v. Blacksheep Charters Ltd.,* (1987) 46 DLR (4th) 67, (British Columbia).

Payments made under pre-incorporation contracts.—The Court of Appeal **reversing** the judgment of HARMAN J (1987) BCLC 540 held that the plaintiffs, *Rover International Ltd.,* were (i) entitled to recover the payments they had made subsequent to their incorporation on the grounds of failure of consideration and (ii) entitled to a *quantum meruit* for the services that they had rendered after their incorporation. *Rover International Ltd. v. Cannon Film Sales Ltd.,* 1988 BCLC 710 : (1989) 3 All ER 423.

Acquiring shares before incorporation.—A company cannot acquire shares prior to its incorporation. Where a company was named as the transferee in the share transfer forms prior to its incorporation, it was held that such transfers could not be registered. *Inlec Investment (P.) Ltd. v. Dynamatic Hydraulics Ltd.,* (1989) 3 Comp LJ 221, 225 (CLB).

Pre-incorporation agreement to subscribe for shares.—It may also be noted that any pre-incorporation share subscription, that is to say, any agreement by a person to take and pay for any shares of a company to be formed, cannot be enforced and is usually revocable unless accepted by the company after its formation.

Income-tax on pre-incorporation income.—The Supreme Court **did not approve** the idea of collecting income-tax from a company for any earnings accruing before the com-

pany was duly incorporated under the Companies Act. *CIT, T.N. v. City Mills & Distributors P. Ltd.*, (1996) 86 Com Cases 546 (SC).

Assignment of company contract to director.—For a discussion of the subject where such assignment is made without the consent of the other party to the contract, see the decision of the Court of Appeal in *Hendry v. Chartsearch Ltd., The Times* September 16, 1998 [PALMER IN COMPANY 1998 Oct] : 1998 CLC 1382 : 1998 CLY 401, here the contract was assigned without taking written consent as required by the contract. Consent could not have been unreasonably withheld if applied for, but this would require amendment of the plaint which was not granted.

Reimbursement of pre-incorporation expenses abroad

Under Rule 5 read with entry No. 17 of Schedule III of the FEM (Current Account Transactions) Rules, 2000, no entity in India shall draw foreign exchange for remittance exceeding US$ 100,000 by way of reimbursement of pre-incorporation expenses, except with prior approval of the RBI. The payment can, however, be made out of funds held in RFC Account of the remitter without such prior approval. [*Notification S.O. 301(E), dt. 30-3-2001*].

§ For text of the Rules refer *Appendix* 104.

Provisional contracts

As regards contracts made after the incorporation of the company and before it is entitled to commence business, see, section 149(4).

Model regulations regarding expenses before incorporation.—For model regulations authorising the directors to bear the pre-incorporation expenses of the company see Regulation 67 of the Table A. In the absence of a Regulation like this, the directors do not have any implied power to incur any expenses on behalf of the company.

Secretarial Practice Notes

Check (1) whether the contracts concluded by the company conform to the requirements of section 46 read with Articles of Association of the company. (2) Check whether approval of Central Government (Regional Director) is taken, if s. 297 involved. [*Circular No.* 5/93, dated 1-9-1993]

Documents involved: 1. Agreement/Contracts, 2. Articles of Association, 3. Register of Contracts, 4. Approval of Board of Directors.

S. 47. Bills of exchange and promissory notes.—A bill of exchange, hundi or promissory note shall be deemed to have been made, accepted, drawn or endorsed on behalf of a company if drawn, accepted, made, or endorsed in the name of, or on behalf of or on account of, the company by any person acting under its authority, express or implied.

NOTES

Eng. Act, 1948: Sec. 33.
Eng. Act, 1985 : Sec. 37.

Previous Act : Sec. 89.

Power to make Bills of exchange and promissory notes

A company cannot make promissory notes or other negotiable instruments unless it is expressly or impliedly empowered to do so by its memorandum of association. Such a power is implied only in the case of a trading concern. *Kerr v. University Press Ltd.*, (1923) 2 DLR 948 (Canada).

Mode of authenticating negotiable instruments on company's behalf

It may be noted that this section, unlike section 28 of the Negotiable Instruments Act, 1881 requires that the making, accepting or endorsing should be expressed to be or should indicate that it is on behalf or in the name or on account of the company. The matter will have to be decided on a true construction of the instrument as a whole. It is important to use some such words as "for" or "on behalf of" or "on account of" in order to convey the idea that the person making, accepting, etc., is acting under the authority of the company.

In the case of bills and promissory notes as in the case of contracts generally (*vide* section 46 of the Companies Act), the essential condition for their validity and enforceability is that they should be made, accepted, etc., by a person acting under its authority, express or implied.

It is very important to indicate that the person signing an instrument is signing it as agent or representative of the company. Otherwise personal liability will attach to him. If a bill of exchange or promissory note is signed by a director, then unless it states on the face of it that it is signed by him acting on behalf of the company, he will be personally liable. *Elliot v. Bax Ironside,* (1925) 2 KB 301 at page 309; and mere description of him in the body of the instrument as a director or officer of the company is not sufficient, (*Ibid*). See also *Britannia Electric Lamp Works Ltd. v. Mandler & Co., Ltd. and Mandler,* (1939) 2 All ER 469 (KB): (1940) 10 Com Cases 72. The mere fact that the company benefited by the borrowing will not be sufficient to bind the company. *Mangal Babu v. Jaitly & Co.,* (1946) 16 Com Cases 214 (All).

The general principle to be followed in cases of negotiable instruments is that the name of a person or firm to be charged upon a negotiable document should be clearly stated on the face or on the back of the document, so that the responsibility is made plain and can be instantly recognised as the document passes from hand to hand. It is not sufficient that the name of the principal should be in some way disclosed; it must be disclosed in such a way that on any fair interpretation of the instrument his name is the real name of the person liable on the bill. *Sadasuk Janki Das v. Sir Kishen Prasad,* (1913) ILR 46 Cal. 663 as cited in *Mangal Bahu (Mst.) v. Jaitly & Co.,* (1946) 16 Com Cases 214 (All).

Personal liability attaches not only to the persons who sign irregular documents but also to the person who authorises the signatures. *John Wilkes (Footwear) Ltd. v. Lee International Footwear Ltd.,* (1985) BCLC 444. A subsequent variation of the underlying transaction will not absolve the statutory liability of the signatory. *British Airways Board v. Parish,* (1979) 2 Lloyds Reports 361 (CA). The policy behind the imposition of personal liability on the company's officers and agents is to ensure proper publicity of the company's name. It is not an exception to the rule of the company's separate legal responsibility. The company in any case is liable and if the officer is compelled to pay, he may recover indemnity from the company. *Brooks Wharf & Bull Wharf Ltd. v. Goodman Bros.,* (1936) 3 All ER 696. For further details see notes under S. 147 and PENNINGTON'S COMPANY LAW, 107 (6th Edn., 1990) : (p. 130, 7th Edn., 1995). But where a promissory note or other negotiable instrument is executed by a person with added description indicating that he is the agent of another, that in substance means that he is acting as the agent of the other in executing the instrument. The absence of the formal expression "for and on behalf of" does not make the document not binding on the principal. See *Rangaswami Reddiar (P.) v. R. Krishnaswami Reddiar,* (1973) 43 Com Cases 232 : AIR 1973 Mad 251.

Where a pronote in favour of a company is endorsed by a branch manager, and as per the articles of the company, a branch manager could have been vested with the power and authority, a stranger is entitled to assume that the branch manager has the authority. *Surve Kedarappa v. Bhimappa,* (1960) 30 Com Cases 131 : AIR 1959 Mys 36. See also *Freeman and Lockyer v. Buckhurst Park Properties (Mangal) Ltd.,* (1964) 1 All ER 630 and *Hely Hutchinson v. Brayhead Ltd.,* (1967) 2 All ER 14. The company is not bound on a

promissory note drawn in the name of 'G' and signed by 'G' with the words "Managing Agent, Dehradun Company Limited". The words Managing Agent, etc. were merely descriptive of the maker of the note. *Sreelal Mangtulal v. Lister Antiseptic Dressing Co. Ltd.,* AIR 1925 Cal 1062 **followed** in *Thandumal & Sons v. Official Liquidator,* (1931) 1 Com Cases 17 : AIR 1930 All 778.

In *Poona Chitrashala Press v. Gajanan,* (1922) 24 Bom LR 355 : AIR 1925 Bom 29, a promissory note was signed on a letter paper of the company and a rubber stamp was used with the name of the company. The Court held that the requisite provisions had been properly complied with. A promissory note was signed by the chief executive of the company on the company's behalf. It was held to be the instrument of the company. It was considered to be immaterial that the accounts of the company did not reflect the borrowing in respect of the promissory note. Accounts are a part of the internal management of the company, outside creditors have no concern with them. The takeover of the management of the company did not affect the enforcement of the promissory note against the new management. *Kirlampudi Sugar Mills Ltd. v. G. Venkata Rao,* (2003) 114 Com Cases 563 : (2003) 42 SCL 798. On the other hand, in *New Fleming Spinning Co., Ltd., Re,* ILR 4 Bom 275, where a promissory note was signed by the secretary and treasurer and agents (since abolished) with the stamp of the company as "The New Fleming S. & W. Co., Limited" appended below, and it was held not to be a bill drawn on behalf of the company.

This rule, however, does not apply to cases where the document in question is a forgery. It applies only to irregularities that might otherwise affect a genuine transaction. *Ruben v. Great Fingall Consolidated,* 1906 AC 439 (HL).

The fundamental principle underlying the section is that a company is not to be bound in its corporate capacity in respect of a negotiable instrument unless the instrument on the face of it makes it clear that it is made, drawn or endorsed by the company itself. *Bombay Mercantile Bank Ltd. v. The Oriol Industries Ltd.,* (1955) 25 Com Cases 479 : AIR 1956 Bom 57: If the conditions imposed by the section are satisfied, any non-essential defects in drawing, accepting or endorsing will not invalidate the transaction. (*Ibid*). Again the principle of the section does not apply where the company itself enforces its rights under instruments defectively drawn on its behalf. (*Ibid*). **Affirming** the decision of High Court (AIR 1956 Bom 57) the Supreme Court expounded the principle as follows: Before a company can be bound by a negotiable instrument, one of the essential conditions is that the instrument must be shown to be drawn, accepted or endorsed by the company. This may be done either by showing the name of the company on the instrument or the statement of the person making it that he is doing so on behalf of the company. Therefore, an instrument purporting to be drawn by a company cannot be validly treated as such unless on its face it satisfies the requirements of this section. An instrument issued without complying with this requirement cannot be enforced against the company. This principle, however, cannot be extended to a claim made against a bank by a company on the ground that a cheque honoured by the bank was defective by reason of non-compliance with the requirement of this section and could not have been enforced against the company. *Oriol Industries Ltd. v. Bombay Mercantile Bank,* AIR 1961 SC 993 : (1961) 31 Com Cases 185.

A cheque with the company's name printed on it was signed by a director without any description as to his status. The cheque was dishonoured. It was held that the cheque was that of the company alone and the director incurred no personal liability since he had adopted all the printing and writing on the cheque and not merely the writing designating the payee and the amount of the cheque. *Bondina Ltd. v. Rollaway Shower Blinds Ltd.,* (1986) 1 All ER 564 : (1987) 3 Comp LJ 193 (CA). Where a director signs a cheque for and on behalf of the company, the company and not the director is the maker of the cheque. *Dilip Kumar Jaiswal v. Debapriya Banarjee,* (1992) 73 Com Cases 434, 440 (Cal). A director was also held personally liable for signing a promissory note intending to do so on behalf of the company, but on which the name of the company was not accu-

rately stated. *Lindholst & Co. A/S v. Fowler,* (1988) BCLC 166 (CA); *Blum v. OCP Repartition SA,* (1988) BCLC 170 (CA).

Use of trade name instead of registered name.—Where a bond or deed were executed in such manner that the body of the document referred to the company by its trade name rather than the registered name. The question was whether the bond was unenforceable by reason of non-compliance with the statutory requirement. The court said that there is nothing in s. 36 of the 1985 [English] Act which requires a company to use its registered name rather than its trading name in the body of a deed or bond. If there had been such a requirement, it would have abrogated the common law rule according to which extraneous evidence is admissible to identify a contracting party, when its identity was not clear from the face of the deed. The company's seal was also engraved with its trading name rather than its registered name. The bond was held to be enforceable. *OTV Birwel Co. Ltd. v. Technical & General Guarantee Co. Ltd.,* (2002) 2 BCLC 723 (QBD).

Criminal liability for dishonoured cheques under Negotiable Instruments Act

When a cheque issued by a company is dishonoured so as to constitute an offence under s. 138 of the Negotiable Instruments Act, 1881 then the director signing the cheque as well as the company can be prosecuted under s. 141 of that Act and no separate notice would be necessary to prosecute the director in question. *Dilip Kumar Jaiswal v. Debapriya Banerjee,* (1992) 73 Com Cases 434, 440 (Cal).

The dishonoured cheque was signed by the executive director of the company. The proceedings were instituted against the signatory as well as the managing director under the allegation that both of them were responsible for and incharge of the company's affairs. The managing director admitted that both of them had together established the company. It was held that the managing director was not entitled to have the complaint against him quashed. *Pankaj Jain v. Gyanendrapal Singh,* (1995) 82 Com Cases 578 (All). In another similar case, the fact that the person accused was the managing director of the company was held to be sufficient to sustain the complaint against him. *Jayalakshmi Nataraj v. Jeena and Co.,* (1996) 86 Com Cases 265 (Mad). So also where the director prosecuted was alleged to be incharge of and responsible for the company's affairs, the complaint against him was not quashed. *Sethuraman Thiagrajan Engineers P. Ltd. v. Cholamandalam Investments and Finance Co. Ltd.,* (1995) 83 Com Cases 484 (Mad). In order to make the officer-in-charge liable it is necessary that the company should also be prosecuted with him. *Alex v. Vijayan,* (1994) 81 Com Cases 910 (Ker).

§ See also Notes under s. 5 under the heading "Liability for dishonour of cheques under Negotiable Instruments Act".

Authority for signing negotiable instruments

Where a managing director signed a bill on behalf of the company without any authority to do so, it was held that the company was bound to a person taking the bill in due course, because the power might properly have been delegated to him. *Dey v. Pullinger Engineering Co.,* (1920) All ER Rep 591; **dissenting** from *Premier Industrial Bank v. Carlton Co.,* (1909) 1 KB 106. Where the managing director of a company certified and confirmed certain bills issued by it, the Gauhati High Court remanded the appeal for decision on facts whether the managing director had or had not the financial power for certification or confirmation of the bills which he was shown to have certified and confirmed. *Grindlays Bank v. Sham Lal,* (1989) 1 Gau LR (NOC) 8 (Gau).

The provisions of section 147 in so far as they apply to bills and promissory notes, should also be taken note of as auxiliary to this section.

Secretarial Practice Notes

Check to ensure that all Bills of Exchange, hundies and promissory notes made, drawn or endorsed on behalf of the company have been so done under proper authority?

Documents involved: 1. Counterfoils of Bills of Exchange, etc. made by the company or instruments accepted by the company. 2. Letters of authority or resolutions giving the relevant authority.

S. 48. Execution of deeds.—(1) A company may, by writing under its common seal, empower any person, either generally or in respect of any specified matters, as its attorney, to execute deeds on its behalf in any place either in or outside India.

(2) A deed signed by such an attorney on behalf of the company and under his seal where sealing is required, shall bind the company and have the same effect as if it were under its common seal.

NOTES

Eng. Act, 1948 : Sec. 34.
Eng. Act, 1985 : Sec. 38.

Previous Act : Sec. 90.

Writing under its Common Seal

Common Seal.—The seal is a relic of the days when mediaeval barons, who could not read or write, used their rings to make a characteristic impress. Though, with the growth of literacy, in the case of individuals it has given place to the signature by hand, in the case of corporate bodies, as they are not living persons who can sign, it has continued to serve as the physical impression made upon written documents executed by such bodies. The purpose is to supplement the signature of corporate officers and thereby authenticate the document, and under this Act it is required to be used on share certificates, and may be used on bonds, debentures and other formal contracts, power-of-attorney, etc. to authenticate them.

The seal is impressed upon a document as evidence of authenticity or attestation and in the case of a company or other corporate body the presence of the corporate seal on any document executed by it, is evidence that it was duly executed by authority of that corporate body. The seal usually consists of the words "corporate seal" and the corporate name and place of the company as well as the date of its incorporation. It need not be of a particular form, shape or substance. If, on behalf of such a body, a document is signed, bearing wax or water or other indication of a seal and the intention was to execute the document as a deed or other contract, this is sufficient proof of its due execution by that body. *Cf. Stromdale & Ball Ltd. v. Burden,* (1952) Ch 223 : (1952) 1 All ER 59 (Ch D).

Where the seal purports to be affixed as required by the company's articles, the presumption is that it was duly affixed by persons duly appointed and their signature were duly made, the burden of proving the contrary being upon the party alleging it. See *Re, County Life Assurance Co.,* (1870) 5 Ch 288.

Under English law a deed is deemed to have been duly executed by a company if its seal is affixed thereto in the presence of and attested by its clerk, secretary or other permanent officer or his deputy, and a member of the Board of Directors or other governing body, and where a seal purporting to be the seal of a company has been affixed to a deed, attested by persons purporting to be persons holding such offices as aforesaid, the deed is deemed to have been executed in accordance with the statutory requirements and to have taken effect accordingly. See HALSBURY'S LAWS OF ENGLAND, Fourth edition, Vol. 7, para 730, page 437 : [Vol. 7(1) Reissue Para 974 Page 713] referring to Law of Property Act 1925, Section 74 (1). See also *D'Silva v. Lister House Development Ltd.,* (1970) 1 All ER 858 at 866 (Ch D).

There is no similar statutory provision in India, but Regulation 84 (2) of Table A of Schedule I contains a more or less similar provision which requires authorisation by a

resolution of the Board of Directors or a committee of the Board authorised by the Board for the affixing of the seal to any instrument. In the case of companies which have not adopted Table A of the First Schedule but which by their Articles provide the manner of affixing the seal, the provision made by their own Articles will govern. Where, however, no provision is made by a company as regards the procedure for using the seal, it would appear that authorisation by a resolution of the Board of Directors will be sufficient, but in such case authentication of the affixing of the seal, if not in the manner provided by Regulation 84(2), should follow the procedure prescribed by section 54. In all cases the important point to be noted is that authorisation by a resolution of the Board is necessary for affixing the seal to any instrument. Where there is no such authorisation the affixing of the seal will not bind the company.

Seal of the company is not required to be affixed on promissory notes executed by directors on behalf of the company under this section. *Sundararaja Pillai, C. v. Sakthi Talkies Ltd.*, (1967) 37 Com Cases 463 (Mad.).

Whether attestation required for affixing common seal

The mere affixing of the seal of a corporation is sufficient without witness. Unless the articles of company provide that the directors shall attest, it is not necessary, although it is customary, for them to do so. Where the articles have such a provision the signature of the directors is not an attestation in the ordinary sense, but is part of the execution of the deed. *Shears v. Jacob*, (1866) LR 1 CP 513; *Deffel v. White*, (1866) LR 2 CP 144. Without such signatures the execution is not complete, but there is no direct judicial decision to this effect.

Presumption of validity

Where an instrument is apparently regular, persons dealing with the company have a right to presume that the seal was duly affixed, that the directors were duly appointed and their signatures duly made. *Re, County Life Assurance Co.*, (1870) LR 5 Ch 288; *Mahony v. East Holyford Mining Co.*, (1875) LR 7 HL 869. The burden of proving the contrary would be on those who allege it. *Clarke v. Imperial Gas, etc., Co.*, (1832) 4 B & Ad 315; *Hill v. Manchester, etc., Co.*, (1833) 5 B & Ad 866; *T.C.B. Ltd. v. Gray*, (1986) 1 All ER 587 : (1986) BCLC 113 (Ch D); *Royal British Bank v. Turquand*, (1856) 6 E & B 327. This principle was applied where the common seal was duly affixed, the irregularity being a part of the indoor management, *County of Gloucester Bank v. Rudry, etc., Co.*, (1895) 1 Ch 629 where the directors approved the way in which the seal was affixed, there being no provision in the articles, though the directors had adopted the practice of passing a resolution and that was not done, *Re, Barned's Banking Co.*, (1867) LR 3 Ch 105 where, unknown to the broker, share certificates which he was handling were stolen. *Yeung v. Hong Kong and Shanghai Banking Corp.*, (1980) 2 All ER 599 (PC). Fraud and forgery in the affixation of the seal give rise to different effects. In *Ruben v. Great Fingall Consolidated*, (1906) AC 439, a share certificate issued under seal on which directors' signatures were forged by the secretary, did not bind the company. *Cf.* PALMER'S COMPANY LAW, 234-35 [24th Edn., 1987, Para 20-12].

Irregularity in the use of common seal

Where the articles require the affixing of a seal on a particular document everyone dealing with the company is bound to take notice of it, but is not bound to ascertain that *de facto* directors have been duly appointed, or that the seal has been affixed with the authority of a meeting duly constituted, *County of Gloucester Bank v. Rudry, etc., Co.*, (*Supra*); *Davies v. Bolton & Co.*, (1894) 3 Ch 678; *Owen and Ashworth's Claim*, (1901) 1 Ch 115. Where there was no article as to the affixing of the seal it was held that the affixing by the managing director was sufficient: *Langley v. Delmonte & Patience Ltd.*, (1933) NZLR 77.

But in *Ruben v. Great Fingall Consolidated, (Supra)*; *Mayor, etc. of Merchants of the Staple of England v. Governor & Co. of Bank of England,* (1887) 21 QBD 160 (CA); *South London Grayhound Race Courses Ltd. v. Wake, (infra)*, it was established that the rule of indoor management as laid down in *Royal British Bank v. Turquand,* (1856) 6 E&B 327, did apply where the seal has been fraudulently affixed and the signatures are forged.

In *South London Geryhound Racecourses v. Wake,* (1931) 1 Ch 496 : (1931) 1 Com Cases 420 (Ch D) it was established that the rule does not apply even where the signatures are genuine but the seal has been affixed without authority. In *South London's* case the article provided that "in favour of any purchaser or person *bona fide* dealing with the company such signature shall be conclusive evidence of the fact that the seal has been properly affixed."

A departure from the provisions of a company's articles in respect of affixing the seal on a document and signing it may still leave the company liable depending upon the nature of the transaction and the authority of those who executed it. Thus, where the articles of a company required money to be borrowed on behalf of the company under the company's seal and signature of two directors, a loan on equitable mortgage taken under the seal of the company and under the signature of only one director was held to be sufficient to bind the company. *Probodh Chandra v. Roadoils (India) Ltd.,* AIR 1930 Cal 782 : (1929-30) 34 CWN 570. Similarly in *Dehradun Mussoorie Electric Tramway Co. Ltd. v. J. Das,* (1931) 1 Com Cases 227 (All) it was held that if a document under seal is not necessary then a mere defect in the manner of affixing the seal will not render the document invalid.

There is no obvious public policy reason for the court to decline to enforce the contractor's third party rights against the surety. Accordingly, the bond could be enforced by the contractor even though the company had sealed it with its common seal in a way that did not comply with s. 350, CA, 1985 (U.K.). *OTV Birwel Co. Ltd. v. Technical and General Guarantee Co. Ltd.,* (2002) 4 All ER 668 (QBD).

Execution of a lease by the managing director without affixing the common seal of the company which was in contravention of Article 42 of the Articles of Association and was accordingly unauthorised. It could not be validated by a subsequent resolution. *Rajendra Nath Dutta v. Shibendra Nath Mukherjee,* (1982) 52 Com Cases 293 (Cal).

Acting through attorney or agents

Where a deed is executed on behalf of a company by its attorney, empowered in accordance with sub-section (1), *i.e.* by writing under the common seal of the company, the deed will be binding on the company to the same extent, as would be, if executed by the company itself under its common seal.

A company has, by necessary implication, a general power to appoint and act by agents, as being a legal entity without physical body, it cannot act in its own person; but any third party dealing with an agent of a company cannot rely upon apparent authority but is bound to acquaint himself with the memorandum and articles, *Mercantile Bank of India v. Chartered Bank of India etc.,* (1937) 1 All ER 231 (KB).

A power-of-attorney executed by a company and the scope of operation of the power are strictly construed, *Danby v. Coutts & Co.,* (1885) 29 Ch D 500; *Jacobs v. Morris,* (1902)1 Ch 816; *Hambro v. Burnand,* (1904) 2 KB 10; and any person dealing on the basis of such power is put on inquiry, though not as to the existence of special circumstances. See *Bryant v. La Banque Du Peuple,* (1893) AC 170; *Montaignac v. Shitta,* (1890) 15 App Cases 357.

Proceedings against company and not by it

Section 48 is applicable when somebody wants to enforce obligations against the company arising under a contract and the company denies or disputes the execution of the

contract. The section was not allowed to be invoked in a case in which the company itself sought to enforce the clauses of a letter of appointment of a person as advisor to the company on retainership basis and not denying the company's own obligation arising under the letter. *Sociedade de Fomento Industrial Ltd. v. Ravindranath Subraya Kamat,* AIR 1999 Bom 158.

Common seal dispensed with in England

By the English Companies Act, 1985 S. 36A(3) inserted by the Companies Act, 1989 the possession and use of common seal by companies has been dispensed with. The resulting position is that common seal, though required formerly, is no longer necessary. Where a company has a common seal, it can execute documents without affixing common seal, though they are required by law to be executed by affixing common seal. Whether a company has a common seal or not, a document signed by directors in accordance with the requirements of the Act now has the same effect as a document executed under its common seal. If the document makes it clear that it is intended to be a deed, it has effect as a deed on its delivery though without seal.

Model regulations as per Table A.—For model regulations in the articles of association pertaining to common seal, see Regulation 84 of Table-A. For a company limited by guarantee and not having share capital, see Regulation 32 of Table-C.

ICSI Guidance Note on Compliance Certificate (August 2003)

The ICSI has issued a Check List for issue of Compliance Certificate under proviso to Sec. 383A(1) in respect of maintenance of registers. The relevant paragraph 1 of the Form prescribed under Rule 3 of the Companies (Compliance Certificate) Rules, 2001 states :

***"Paragraph 1.*— The company has kept and maintained all registers as stated in Annexure "A' to this certificate, as per the provisions and the rules made thereunder and all entries therein have been duly recorded."**

Register of Documents Sealed

Prescribed Check List

The register is optional register and should be maintained as good secretarial practice. However, if the register is not maintained, the CSP should not qualify his certificate.

Check whether:

(i) the company has maintained a register of documents sealed;

(ii) the register contains the following information :

(a) number and date of the minutes authorising the use of the seal;

(b) date of sealing;

(c) persons in whose presence the seal was affixed;

(d) document sealed;

(e) location of document.

§ For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

§ For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

S. 49. Investments of company to be held in its own name.—(1) Save as otherwise provided in sub-sections (2) to (5) [1][or any other law for the time being in force] and subject to the provisions of sub-sections (6) to (8),—

(a) all investments made by a company on its own behalf shall be made and held by it in its own name; and

(b) where any such investments are not so held at the commencement of this Act the company shall, within a period of one year

1. Ins. by Act 65 of 1960, s. 15.

from such commencement, either cause them to be transferred to, and hold them in, its own name, or dispose of them.

(2) Where the company has a right to appoint any person or persons, or where any nominee or nominees of the company has or have been appointed, as a director or directors of any other body corporate, shares in such other body corporate to an amount not exceeding the nominal value of the qualification shares which are required to be held by a director thereof, may be registered or held by such company jointly in the names of itself and of each such person or nominee or in the name of each such person or nominee. [2][* * * *]

(3) A company may hold any shares in its subsidiary in the name or names of any nominee or nominees of the company, if and in so far as it is necessary so to do, to ensure that the number of members of the subsidiary is not reduced where it is a public company, below seven, and where it is a private company, below two.

(4) Sub-section (1) shall not apply to investments made by a company whose principal business consists of the buying and selling of shares or securities.

(5) Nothing in this section shall be deemed to prevent a company—

(a) from depositing with a bank, being the bankers of the company, any shares or securities for the collection of any dividend or interest payable thereon; or

[3][(aa) from depositing with, or transferring to, or holding in the name of, the State Bank of India or a Scheduled Bank, being the bankers of the company, shares or securities, in order to facilitate the transfer thereof :

Provided that if within a period of six months from the date on which the shares or securities are transferred by the company to, or are first held by the company in the name of, the State Bank of India or a Scheduled Bank as aforesaid, no transfer of such shares or securities takes place, the company shall, as soon as practicable after the expiry of that period, have the shares or securities retransferred to it from the State Bank of India or the Scheduled Bank or, as the case may be, again hold the shares or securities in its own name; or]

(b) from depositing with, or transferring to, any person any shares or securities, by way of security for the repayment of any loan advanced to the company or the performance of any obligation undertaken by it.

[4][(c) from holding investments in the name of depository when such investments are in the form of securities held by the company as a beneficial owner.]

(6) The certificate or letter of allotment relating to the shares or securities in which investments have been made by a company shall, except in the cases re-

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2. The words "expressly described as a nominee of the company" omitted by Act 65 of 1960, s. 15.
3. Ins. by Act 65 of 1960, s. 15.
4. Ins. by the Depositories Act, 1996 (w.e.f. 20-9-1995).

ferred to in sub-sections (4) and (5), be in the custody of such company or [5][with the State Bank of India, or a Scheduled Bank], being the bankers of the company.

(7) Where, in pursuance of sub-section (2), (3), (4) or (5), any shares or securities in which investments have been made by a company are not held by it in its own name, the company shall forthwith enter in a register maintained by it for the purpose—

(a) the nature, value, and such other particulars as may be necessary fully to identify the shares or securities in question; and

(b) the bank or person in whose name or custody the shares or securities are held.

(8) The register kept under sub-section (7) shall be open to the inspection of any member or debenture-holder of the company without charge, during business hours, subject to such reasonable restrictions as the company may, by its articles or in general meeting, impose, so that not less than two hours in each day are allowed for inspection.

(9) If default is made in complying with any of the requirements of sub-sections (1) to (8), the company, and every officer of the company who is in default, shall be punishable with fine which may extend to [6][fifty thousand rupees].

(10) If any inspection required under sub-section (8) is refused, the [7][*Central Government*] may, by order, direct an immediate inspection of the register[8].

Nothing in this sub-section shall be construed as prejudicing in any way the operation of sub-section (9).

(11) In this section, "securities" include stock and debentures.

NOTES

General Note : As and when the Companies (Second Amendment) Act, 2002 (11 of 2003) comes into force, the power under this section shall become transferred to the Central Government to be exercised by it in place of the Company Law Board. The Commentary and the procedure should be read keeping this change in mind.

Companies Act, 1956

Investment of company in its own name

Recommendations of Company Law Committee.—This section is new and has been enacted on the recommendation of the Company Law Committee who felt that a provision like this "would reduce the temptation to misuse the investments of the company". (*Report,* page 291). The section in its present form was drafted by the Joint Committee with the following explanation : "The Committee consider that this clause which, requires a company to hold all investments in its own name, should not apply to an investment company whose business consists of the buying and selling of shares, stock, debentures or other securities. Deposits of securities in a bank for the collection of dividend or interest and deposits of transfers by way of security are permitted. In the case of investments

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5. Subs. by Act 65 of 1960, s. 15 "with a Scheduled Bank".
6. The words "five thousand rupees" substituted by the Companies (Amendment) Act, 2000, (53 of 2000) s. 14 (w.e.f. 13-12-2000).
7. **Subs. for "Company Law Board" by the Companies (Second Amendment) Act, 2002 (11 of 2003), s. 8. Earlier subs. by the Companies (Amendment) Act, 1988, (w.e.f. 31-5-1991) *vide* GSR dated 31-5-1991, for the word "Court".**
8. Application fee is Rs. 100/- vide GSR 219(E), dt. 2-3-2000, w.e.f. 1-4-2000 under CLB (Fees on Applications & Petitions) Rules, 1991.

held by a company at the commencement of this Bill, the period of six months, allowed by the Bill as introduced for compliance with the provisions of this clause, has been increased to one year. The Committee have also provided for the keeping of a register of all securities belonging to, but not held by, a company in its own name. (*Report,* para 24).

The section enjoins the maintaining of a register of investments wherein should be entered the particulars specified in sub-section (7), and the register is to be kept open for inspection of members and debenture-holders as provided in sub-s. (8).

Companies (Amendment) Act, 1960

Purchase of certain securities in the name of scheduled bank.—The reason for the insertion of clause (aa) of sub-section (5) by Amendment Act (65 of 1960) is thus given : "In the case of investments of the funds of a company in Government securities or debentures and shares it should be open to the company to have them bought in the name of a scheduled bank the advantage being the easy collection of dividends and the speedy disposal of such shares and securities at a slightly higher price. Till the shares or securities are disposed of the bankers of the company would be collecting interest and dividends and crediting them to the company's account. (Companies Act Amendment *Committee Report,* para 39).

The proviso to clause (aa) of sub-section (5) was added by the Joint Committee, as they thought that where a company transfers any shares to a bank to facilitate the disposal of these shares, then, if the shares are not disposed of within six months, the bank should retransfer them to the company". (*Report,* para 23).

Companies (Amendment) Act, 1988

The powers of the court have been conferred on the Company Law Board in sub-section (10) by the Companies (Amendment) Act, 1988.

Depositories Act, 1996

Sub-section (5) contains a few exceptions in which companies are permitted to hold investments in any other names than their own names. A fourth exception by introducing clause (c) to sub-section (5) has been inserted by Depositories Act, 1996 as a consequential amendment for introduction of depository mode of holding securities so as to enable companies to hold investments as beneficial owners in the name of a depository.

Companies (Amendment) Act, 2000

The Amendment Act of 2000 enhanced the penalty amount from five thousand rupees to fifty thousand rupees. Sub-section (9) was accordingly amended.

Companies (Second Amendment) Act, 2002 [11 of 2003]

The powers of the court were conferred on the Company Law Board under sub-section (10) by the Companies (Amendment) Act, 1988. These powers have now been vested in the Central Government by the Companies (Second Amendment) Act, 2002 (11 of 2003). The Companies (Amendment) Bill, 2001 had proposed transfer of CLB's power to the Tribunal. Notes on Clauses stated :

Notes on clauses.—This clause seeks to amend sections 18, 19, 43, 49, 55A and 58A of the Companies Act, 1956 relating to alteration of memorandum of association to be registered within three months, effect of failure of such registration, consequences of default in complying with conditions constituting a company as private company, investments of company to be held in its own name, powers of Securities and Exchange Board of India so far as they relate to issue and transfer of securities and acceptance of deposits without issuing advertisement. It is proposed to confer the powers of the Company Law Board in the aforesaid sections upon the Tribunal. These amendments are of consequential nature. (*Clause* 8 of the Companies (Amendment) Bill, 2001).

Scope of section

When the investment of a company consists of shares in another company the question arises whether shares held by the company in the name of its nominee must be deemed to be held by the company and whether the investments should be transferred to the name of the company. In considering this question, it is necessary to bear in mind the provisions of section 153 which provide that no notice of any trust, express, implied or constructive, shall be entered in the register of members or debenture holders. A company, therefore, is bound to treat the person in whose name the shares are entered in its register of members as a member. If a company holds shares in the name of its nominee it is not entitled to any of the rights in respect of the shares such as right to dividend, to allotment of rights shares under section 81, to exercise voting rights in relation to the shares and other privileges which shareholders have. It does not, therefore, appear to be an implication of the provisions of section 49 that if a company holds shares in another company in the name of its nominee, the shares must be deemed to be held by the company and not by the nominee. This would have practical importance in considering whether a company has become the holding company of another by virtue of acquiring more than 50% of the equity capital of the other company. Also under sections 81 and 43-A of the Companies Act and sub-section (3) of section 4, in determining whether one company is a subsidiary of another, any shares held by the company in fiduciary capacity shall be treated as not held. Under section 43-A, where not less than 25% of the paid-up share capital of a private company is held by one or more bodies corporate, the private company shall become a deemed public company. It is submitted that the holding of shares by a company is to be construed strictly in the light of sections 41 and 153 in order to determine whether a company has become a deemed public company. If, therefore, shares of a private company are beneficially held by another company but they are held in the name of its nominees who are individuals, in applying the provisions of s. 43-A, the holding of the nominees will not be taken into account. Under section 81(1) when shares are issued by a company it is required to offer the same to persons who on the date of the offer are holders of the equity shares of the company. This must mean an offer to registered holders of the shares and not to the beneficial holders. In view of these provisions even though penalties are attached under sub-section (8) of this section to the holding of investments by a company in the name of its nominee, it does not follow as a corollary that where shares are held by a company in the name of its nominee effect will be given for the purposes of sections 4, 43-A and 81 to the beneficial right of the company and not to the legal right of the nominee nor will the company be entitled to claim dividends on such shares or exercise voting rights, nor to bonus shares.

Where one company's money was invested for purchasing shares in another company's name and the transaction between the companies was treated as that of loan, it was held that section 49 was not violated. *Hemangiri Finance and Leasing P. Ltd. v. Tamilnadu Mercantile Bank Ltd.*, (1996) 86 Com Cases 875 (CLB—Mad).

Company Shareholding and Depository [Sub-section (5)(c)]

The Depositories Act, 1996.—This clause has been brought into the Companies Act by the Depositories Act, 1996 for the purposes of enabling the functioning of the depository system for transfer of shares. The sub-section contains the exceptional situations to which s. 49 does not apply. Clause (c) constitutes a fourth such exception. The resulting position is that nothing in s. 49 shall be deemed to prevent a company from holding investments in the name of a depository when such investments are in the form of securities of which the company is itself the beneficial owner.

Company's shares registered in joint name with director

Where the shares of a company were registered in the joint name of the company and one of its directors, it was held that the director was a nominee of the company for that purpose. He could act jointly with the company and not individually. He had no rights of his own in respect of the shares and was not entitled to bring proceedings on the basis of

being one of the registered holders. *Exchange Travel (Holdings) Ltd. Re,* (1991) BCLC 728 (Ch D).

Power of CLB to order inspection [Sub-section 10]

It may be noted that, if any inspection required under sub-section (8) is refused, the Company Law Board may direct an immediate inspection of the register. The jurisdiction of the Company Law Board has been vested with Central Government under the Companies (Second Amendment) Act, 2002 (11 of 2003).

Investment

The term means any outlay of a company's money or money's worth, with a view to obtain profit. See Notes under section 292.

Beneficial holdings

When section 187-C was in force the effect was that a company holding shares in any other name than its own name, the provisions of the section had to be complied with both by the beneficiary of the shares and the ostensible holder. The provisions of the section 187-C ceased to be operative on the commencement of the Companies (Amendment) Act, 2000.

Petition before Company Law Board

Petition under sub-section (10) by an aggrieved member/debenture-holder to direct the company to allow an immediate inspection of Register of investments, if the inspection is refused, be made in Form No. 1 of Annexure II of the CLB Regulations, 1991 before the Regional Bench of the Company Law Board along with an application fee of Rs. 100/-, and the following documents:—

(1) Documentary evidence, if any, showing the refusal on the part of the company to allow inspection.

(2) Affidavit verifying the petition.

(3) Bank draft evidencing payment of application fee.

(4) Memorandum of appearance to be filed in Form No. 5 of Annexure 1, with a copy of the Board resolution or the executed vakalatnama as the case may be.

(5) Any other relevant correspondence exchanged with the company.

(6) Acknowledgment of receipt from Registrar in token of receipt of the copy of the petition.

For text of the Company Law Board Regulations, 1991 refer *Appendix* 3.

Penalty for default [sub-section (9)].—If default is made in complying with any of the requirements of sub-sections (1) to (8), the company and every officer of the company who is in default are punishable with fine which may extend to Rs. 50,000/-.

Compoundable Offence.—The offence is compoundable under Section 621-A.

ICSI Guidance Note on Compliance Certificate (August 2003)

The ICSI has issued a Check List for issue of Compliance Certificate under proviso to Sec. 383A(1) in respect of maintenance of registers. The relevant paragraph 1 of the Form prescribed under Rule 3 of the Companies (Compliance Certificate) Rules, 2001 states :

***"Paragraph 1.*— The company has kept and maintained all registers as stated in Annexure "A' to this certificate, as per the provisions and the rules made thereunder and all entries therein have been duly recorded."**

Register of Investments under Section 49

Prescribed Check List

Check whether:

(i) all investments of the company are held in the name of the company;

(ii) if any investments are not held by the company in its own name as allowed by sub-sections (2), (3), (4) or (5); whether register of investments not held in company's name has been maintained and the particulars such as the nature, value and such other particulars as may be necessary fully to identify the shares or securities in question and the bank or person in whose name or custody the shares or securities are held have been entered therein;

(iii) the register is kept open for inspection by any member or debenture-holder without charge, during business hours, subject to reasonable restrictions as may be imposed by the Articles or in general meeting.

§ For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

§ For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

S. 50. Power for company to have official seal for use outside India.—(1) A company whose objects require or comprise the transaction of business outside India may, if authorised by its articles, have for use in any territory, district or place not situate in India an official seal which shall be a facsimile of the common seal of the company, with the addition on its face of the name of the territory, district or place where it is to be used.

(2) A company having an official seal for use in any such territory, district or place may, by writing under its common seal, authorise any person appointed for the purpose in that territory, district or place to affix the official seal to any deed or other document to which the company is a party in that territory, district or place.

(3) The authority of any agent authorised under sub-section (2) shall, as between the company and any person dealing with the agent, continue during the period, if any, mentioned in the instrument conferring the authority, or if no period is there mentioned, until notice of the revocation or determination of the agent's authority has been given to the person dealing with him.

(4) The person affixing any such official seal shall, by writing under his hand, certify on the deed or other document to which the seal is affixed, the date on which and the place at which, it is affixed.

(5) A deed or other document to which an official seal is duly affixed shall bind the company as if it had been sealed with the common seal of the company.

NOTES

Eng. Act, 1948 : Sec. 35.
Eng. Act, 1985 : Sec. 39.

Previous Act : Sec. 91.

Authorisation under the articles

The power under this section can be exercised only where the articles of the company authorise the use of an official seal outside India. In the absence of authority under the Articles the power under the section cannot be exercised.

Use of official seal

If the Official Seal is used upon any deed or document, it will be as binding upon the company as though the common seal itself has been used provided the following conditions are satisfied:—

(1) the person affixing the seal has the company's authority in writing under its seal;

(2) the deed or other document is one to which the company is party; and

(3) the person affixing the seal is acting in exercise of his authority in a place where the official seal was authorised to be used.

Seal necessary for appointing attorney

Section 48 expressly authorises a company to appoint attorneys to execute deeds on its behalf in India as well as outside India. The appointment has to be made under the company's common seal and may be a general or special power of attorney.

By the English Companies Act, 1985, S. 36A(3) inserted by the Companies Act, 1989, the possession and the use of common seal by companies has been dispensed with. The resulting position is that common seal, though required formerly, is no longer necessary under the English Companies Act, 1985.

For further details see, Notes under section 48.

Model Regulation as per Table A.—For model regulations in the articles of association pertaining to this section, see Regulation 68 of Table A.

Secretarial Practice Notes : Official seal for use outside India

Whether the company had used its Official Seal outside India ? If so, check whether:

(i) the articles authorised such use?

(ii) the seal was a facsimile of the common seal of the company with the addition on its face, the name of the place where it was to be used?

(iii) the person using the Official Seal was authorised in writing under the common seal of the company?

(iv) the person affixing such seal had certified in writing on the deed/document to which the seal was affixed the date on which and the place at which it was affixed?

Documents Involved: 1. Articles, 2. Minutes of Board/General Meeting, 3. Official Seal, 4. Document of authorisation to use the Seal, 5. Deeds/Documents bearing Official Seal, 6. Register of Documents sealed, if any.

Service of Documents

S. 51. Service of documents on company.—A document may be served on a company or an officer thereof by sending it to the company or officer at the registered office of the company by post under a certificate of posting or by registered post, or by leaving it at its registered office.

[1][*Provided* that where the securities are held in a depository, the records of the beneficial ownership may be served by such depository on the company by means of electronic mode or by delivery of floppies or discs.]

NOTES

Eng. Act, 1948 : Sec. 437. Previous Act : 148.
Eng. Act, 1985 : Sec. 725.

Depositories Act, 1996

Depositories Act, 1996 has, by inserting the proviso to s. 51, introduced a new method of service of documents on the company known as the electronic mode. The proviso says that where the securities are held in a depository, the records of the beneficial ownership

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1. Ins. by the Depositories Act, 1996 (w.e.f. 20-9-1995).

may be served by such depository on the company by means of an electronic mode or by delivery of floppies or discs.

Modes of service provided in this section

This has to be done, if sent by post, either by ordinary post under certificate of posting or by registered post. Previously under sections 148 and 149 of the 1913 Act, the obtaining of a certificate of posting, in the case of service by ordinary post, was not required.

Where the plaintiff in a suit sends notice of the suit by registered post or by certificate of posting and the same is not returned to him and neither is there anything to show that it has not been served, the plaintiff would be entitled to an *ex parte* decree, which would not be easily set aside even if the cover is later returned to the plaintiff. See, *Cathrineholm A/s. v. Nore Equipment Trading Ltd.,* (1972) 2 All ER 538 (CA); (Service rendered at the company's registered office building which was under demolition and not alternative address was provided—service was held to be good.) *Saga of Bond Street Ltd. v. Avalon Promotions Ltd.,* (1972) 2 All ER 545 (CA), **not following** *Thomos Bishop Ltd. v. Helmville Ltd.,* (1972) 1 All ER 365 (CA). On this point in *Madan and Co. v. Wazir Jaivir Chand,* AIR 1989 SC 630, the Supreme Court has reiterated that, when a summon was sent to the proper address of the addressee by registered post and tendered with the postal authority for service, then the presumption of service arises under section 27 of the General Clauses Act. Such presumption, even though rebuttable, has to be rebutted by the other side by leading sufficient evidence. However in *Harendra Nath Ghosal v. Super Foam P. Ltd.,* (1992) 74 Com Cases 740, 745-746 (Cal) where above-cited Supreme Court decision was referred to and the opinion expressed was that the provisions of s. 51 would prevail over Order 29, Rule 2 of CPC. But on facts the court was prepared to accept the possibility of the alternative modes of service. This appears from the fact that after stating that summons on a company must be served at its registered office, the court said that even if the service could have been made at branch office there was no proof to that effect. The Court accordingly set aside the *ex parte* decree.

The service of a High Court writ by posting it on company's registered office address was held to be good service. *Addis Ltd. v. Berkeley Supplies Ltd.,* (1964) 2 All ER 753; posting it by ordinary post or registered post *T.O. Supplies (London) Ltd. v. Jerry Creighton Ltd.,* (1952) 1 KB 42. Service by registered post on the registered office of the company was held to be good service under this section. There was a concurrent finding of two courts below that the petitioner company had received the notice enhancing the rent of the premises. The finding was not interfered with in a writ petition filed under Article 227 of the Constitution. *Indian Air Gases Ltd. v. Tarawati Sood,* (1999) 33 CLA 157 (Del).

Defective address

The letter should contain the address of the company in a substantially accurate form. The omission of the word "Private" will not vitiate the service of the document. Furthermore, the omission of the word "limited" shall not invalidate the service of document provided there is no other company with the same name at the same address—*Springate v. Questier,* (1952) 2 All ER 21. *Liverpool Marine Insurance Co. v. Haughton,* (1874) 23 WR 93, *Sarkar Estates P. Ltd. v. Kusumika Iron Works P. Ltd.,* AIR 1961 Cal 43 : (1962) 32 Com Cases 575.

Service where there is no registered office

Where there is no registered office, service at the office in fact used by the company is sufficient, *British and Foreign Generating Apparatus Co. Ltd., Re,* (1865) 12 LT 368. Where there was no office, the company having ceased to carry on business, service on some of the former officers was allowed, *Gaskell v. Chambers,* (1858) 26 Beav 252.

Service at address from which Company Corresponding.—Where the notice was served on the company not at its registered office but at the address from which the com-

pany was corresponding with the payee, the service was held to be valid. *RRJ Dass (Retd.) WG CDR v. Satya Bhama Lal,* (2003) 115 Com Cases 878 (Delhi).

Pollution notice.—It has been held that a service of a notice under the Environmental Protection Act 1990 [English] complaining that a statutory nuisance was being committed could be effected at the principal place of business of the company committing the nuisance. It was not necessary to lodge the notice at the registered office. As this legislation was meant to be used by lay persons the court was justified in adopting a commonsense and non-technical approach to statutory interpretation. *Hewlings v. McLean Homes East Anglia Ltd., The Times,* August 31, 2000.

Notice to company through directors and officers

A notice addressed to the company and served on the directors is good service. *Benabo v. Jay (William) and Partners Ltd.,* (1940) 4 All ER 196 : (1942) 12 Com Cases 92. In addition to serving a notice on the company which is complete when it is received by the company in the ordinary course of its business, it is also possible to give notice to the company through its proper officers. *Alletson v. Chicester,* (1875) LR 10 CP 319. Service of notice on a company, for the purpose of filing a suit, by service on the office assistant of the company was held to be not a good service. *Nicco Corporation Ltd. v. Cethar Vessels Ltd.,* (1998) 92 Com Cases 748 (Mad). Notice to a director or other officer in the course of a transaction in which he is concerned as such director or officer amounts to notice to the company. *Bank of Ireland v. Cogry Spinning Co.,* (1900) 1 IR 219; *European Bank, Ex p., Oriental Commercial Bank,* (1870) 5 Ch App 358.

A company will not be bound by a notice received by a director or other officer in the course of a transaction with which he is not concerned, *Societe Generale de Paris v. Walker,* (1885) 11 App Cas 20 (HL); *Kanhaiyalal Jhanwar v. Pandit Shirall & Co.,* (1953) 23 Com Cases 399 : AIR 1953 Cal 526; or where he received it while acting as a director of another company, *Re, Marseilles Extension Rly. Co., ex p., Credit Foncier and Mobilier of England,* (1871) 7 Ch App 161; *Sree Meenakshi Mills v. Ratilal Thakkar,* AIR 1941 Bom 108; *T.R. Pratt (Bom.) Ltd. v. E.D. Sasoon & Co. Ltd.,* AIR 1936 Bom 62 : (1936) 6 Com Cases 90; *Hudson v. Official Liquidator,* AIR 1929 All 826, or if it relates to a matter which he is not bound to disclose to the company and also does not do so. *Re, David Payne & Co. Ltd; Young v. David Payne & Co. Ltd.,* (1904) 2 Ch 608 (CA), where the same person was director of both contracting companies; *Deep Sea Fishery Co.'s (Ltd.) Claim,* (1902) 1 Ch 507; *Re, Hampshire Land Co.,* (1896) 2 Ch 743; *Lagunas Nitrate Co. v. Lagunas Syndicate,* (1899) 2 Ch 392 at 431, 432 (CA), or where he is acting fraudulently, *Re, European Bank, ex p., Oriental Commercial Bank,* (1870) 5 Ch App 358; *Ruben v. Great Fingall Consolidated,* (1906) AC 439 (HL); *Gluckstein v. Barnes,* (1900) AC 240 at 247 (HL); *Kwei Tek Chao (Trading as Zung fu Co.) v. British Traders and Shippers Ltd.,* (1954) 1 All ER 779; *Houghton & Co. v. Nothard, Lowe and Wills Ltd.,* (1928) AC 1 (HL); *Belmont Finance Corpn. Ltd. v. Williams Furniture Ltd.,* (1979) 1 All ER 118 (CA); *G.L. Baker Ltd. v. Medway Building and Supplies Ltd.,* (1958) 2 All ER 532; *VKRST Firm v. Oriental Investment Trust,* (1944) 14 Com Cases 231 (Mad); or irregularly, *Hampshire Land Co., Re, (infra).*

Where one person is an officer of two companies, his personal knowledge is not necessarily the knowledge of both the companies. The knowledge he has acquired as an officer of one company will not be imputed to the other company unless he has some duty imposed on him to communicate his knowledge to the company sought to be affected by the notice and some duty imposed on him by that company to receive that notice. *In Re, Hampshire Land Co.,* (1896) 2 Ch 743. *In Re, Fenwick, Stobart & Co. Ltd.,* (1902) 1 Ch 507.

Where a financial corporation wanted to effect recovery of its dues from the borrower company and it served a notice of its recovery petition on the managing director of the company who received the service for and on behalf of the company, it was held that that was a good service, the court saying that a managing director is entitled to accept notices on behalf of the company and that the notice having been accepted by him was a proper service on the company. *Maharashtra State Financial Corpn. v. Masvi & Co. P. Ltd.,* (1993) 76 Com Cases 168 at 182 (Bom). Where a director is duty bound to receive papers

on behalf of the company but does not do so and thereby plunges the company into ignorance, he will be personally liable for any consequential loss of the company. *Societe Generale de Paris v. Walker,* (1885) 11 App Cas 20 (HL).

Service of documents on Registered Office

§ For Notes see under section 146 as to service of documents on registered office.

Contrary provisions in articles not enforceable

The articles of a company containing any provisions contrary to this section are not enforceable nor can they limit the mode of service to one only of the modes provided by the statute. *Sadasiv Shankar Dandige v. Gandhi Seva Samaj Ltd.,* AIR 1958 Bom 247 : (1958) 28 Com Cases 137.

Other modes of service and manner of service under C.P.C.

In respect of the corresponding provisions, Section 14 of the old Act of 1913, it was observed by the Supreme Court in *Jute and Gunny Brokers Ltd. v. Union of India,* (1962) 32 Com Cases 845 : AIR 1961 SC 1214 that the provision is only an enabling provision and the method of service provided therein is not the only method of serving documents on a company and there is no reason why the manner of service provided for a summons by Order XXIX Rule 2 of the Code of Civil Procedure in the case of suits by or against corporations *viz.*, on the secretary or on any director or other principal officer, should not be adopted in appropriate cases.

Without taking note of the above-cited Supreme Court decision the Calcutta High Court held that the requirement of the section as to the mode of service prevails upon those of the Civil Procedure Code. The effect is that the requirement of the section would have to be satisfied even if it is in addition to that of the Civil Procedure Code. Where the directors proved that the premises of the company had remained closed during the time that summons were purported to have been served, the court held that there could be no inference that the summons were tendered by the postal authorities and refused by the company. The court did not draw any presumption as to valid service. The court further said that a court of revision cannot interfere with the finding of fact based on evidence by the appellate court which is the first court of fact. *Harendra Nath Ghosal v. Superfoam P. Ltd.,* (1992) 74 Com Cases 740 (Cal).

Service of Notice affixation with or without witnesses

§ See Notes under Rule 6 of Company Court Rules, 1959 in *Appendix* 4.

Service by electronic mode for depository purposes

The Depositories Act, 1996.—A special mode of service has been recognised under the Depositories Act, 1996 by inserting the proviso to s. 51. Where the securities are held in a depository, the records of beneficial ownership may be served by the depository on the company by means of electronic mode or by delivery of floppies or discs.

Oral notice.—An oral notice to Board of Directors while in meeting will suffice, *Worcester, Ex P., Agra Bank,* (1868) 3 Ch App 555, and also an oral notice to a company's clerk at its registered office in office hours and during the absence of the secretary, *Truman's* case, (1894) 3 Ch 272, or to a managing director or the secretary in the course of his duties as such, *Jaeger's Sanitary Woollen System Co. Ltd. v. Walker & Sons,* (1897) 77 LT 180 (CA).

Service of Notice by Fax.—In *Hastie & Jenkerson (A firm) v. McMahon,* (1991) 1 All ER 255 (CA), the issue was whether a list of documents is validly served when it arrives by fax. WOOLF LJ's starting point was one of principle: the purpose of serving a document is to ensure that its contents are available to the recipient. Since transmission by fax achieves this purpose, service by fax is good service. It was held, however, that a party who sends a document by fax but who cannot prove that it was received in a legible form will have failed to prove valid service. **Followed** by Federal Court of Australia in *Australian Securities Commission v. Bank Leumi Le-Israel,* (1995) 34 Aust LR 101 (FC—Aust).

The requirement of a notice of dishonour of acheque under section 138 of NI Act, in writing has been held by the Supreme Court to be satisfied when it is transmitted by fax. *SIL Import v. Exim Aides Silk Exporters,* (1999) 97 Com Cases 575 at 579 (SC).

Statutory recognition in England of Fax.—The matter is now governed by the new amendment to Ord. 65, r. 5, with effect from 1 February, 1991 [English]. For service by fax to be valid the following rules must be observed:

(A) Both parties must act by solicitors.

(B) To be affected on the same day, service of the document must be transmitted before 4 p.m.

(C) A copy of the transmitted document must be sent on the same day by traditional means.

Notice to agent.—Notice to an agent or his knowledge does not preclude the company from recovering its money paid under a mistake of fact, where the agent had no idea that his knowledge was relevant to the matter which was being acted upon. *Anglo-Scottish Beet Sugar Corpn Ltd. v. Spalding UDC,* (1937) 3 All ER 335; *Turvey v. Dentons (1923) Ltd.,* (1952) 1 All ER 1025.

§ As to when notice to an agent is regarded also as notice to his principal, see, section 229 of Indian Contract Act, 1872.

Service of notice on foreign company

§ See section 596 and notes thereunder.

S. 52. Service of documents on Registrar.—A document may be served on a Registrar by sending it to him at his office by post under a certificate of posting or by registered post, or by delivering it to, or leaving it for, him at his office.

NOTES

Previous Act : Sec. 149 and
Regulations 112 to 115 of Table A

Authorisation for making corrections in defective documents filed with ROC

Department's circular.—"It has come to the notice of this Department that the companies, which file defective documents with the Registrars of Companies, do not take appropriate steps to remove those defects. You are requested to prevail upon your constituents to ensure that the defective documents, pending with the Registrars of Companies, are corrected expeditiously, so that the same are taken on record. While it is necessary that the documents are corrected by the signatory of the document concerned, as a matter of administrative convenience, it has been decided that a duly authorised person, preferably a professional Chartered Accountant/Company Secretary/Cost Accountant or an Advocate, be allowed to make such corrections. The said authorisation should be by way of a Power of Attorney, duly executed on a requisite stamp paper and accompanied by a resolution of the Board of Directors, in this behalf.

2. You are also requested to advise your constituents that proper care is taken at the time of filing documents, so that the concerned Registrar of Companies has no difficulty in taking the documents on record. [*Circular No.* 8/90; No. 14/2/88-CL-V, dated 17-5-1990].

Filing of documents with Registrar of Companies

Regulation 17 of the Companies Regulation, 1956, as amended, provides that if any document is found to be defective or incomplete in any respect, the Registrar shall give notice in writing to the company to rectify the defect or complete the document or to file a revised document complete in all respects within 15 days from the date of such notice and on failure on the part of the company to rectify the defect, the document shall be registered, recorded or filed, as the case may be, by the Registrar and the company shall be informed accordingly. The defective document will be taken on record by the Registrar without prejudice to his powers to take such action as may be warranted under the law. [*Press Note No.* 12/92 (No. 14/3/87—CL-V), dated 21-12-1992, *issued by the Department of Company Affairs*].

Press Note, dated 12-3-1991.—The Government have taken a decision that all documents filed by companies with the concerned Registrar of Companies under the Companies Act, 1956, be taken on record, if the same are duly certified as correct by a chartered accountant/cost accountant/com-pany secretary in practice for the sake of expeditious registration of public documents filed under the said Act.

ICSI Guidance Note on Compliance Certificate (August 2003)

The ICSI has issued a Check List for issue of Compliance Certificate under proviso to Sec. 383A(1) in respect of the matters specified under Rule 3 of the Companies (Compliance Certificate) Rules, 2001.

Paragraph 2 under Rule 3 relates to filing of forms and returns with ROC, RD, etc. and reads as follows:

Paragraph 2.—**The company has duly filed the forms and returns as stated in Annexure "B" to this certificate, with the Registrar of Companies, Regional Director, Central Government, Company Law Board or other authorities within the time prescribed under the Act and the Rules made thereunder.**

Court/CLB Orders

Prescribed Check List

Check whether Form No.21 has been filed with the ROC along with certified copies of the following orders:

17(2)	Order of the Company Law Board* approving the shifting of the registered office from one State to another
79	Order of the Company Law Board** approving Issue of shares at discount
81(3)	Order of the Central Government approving the terms of issue of debentures relating to conversion of debenture or loan into shares
94A(2)	Order of the Central Government permitting public financial institution to convert debentures or loan into shares
102(1)	Order of the Court† confirming the reduction of capital
107(3)	Order of the Court† disallowing or confirming variation of the shareholders' rights
111(5) or 111A	Order of the Company Law Board† dismissing the appeal or rejecting the application in respect of refusal of registration of transfer and directing that the transfer or transmission shall be registered by the company/directing the rectification of the register of members
113	Order of the Company Law Board* granting extension of time for issue of debenture certificate
141	Order of the Company Law Board* extending time for filing particulars of registration, modification or satisfaction of charges or rectifying the register of charges
186	Order of the Company Law Board† for a meeting of the company to be called, held and conducted in terms of the Order
391(2)	Order of the Court† sanctioning any compromise or arrangement
394(3)	Order of the Court† making provisions for several matters specified in section 394(1) for implementing the compromise or arrangement
404(3)	Order of the Company Law Board† providing for change in Memorandum or Articles.

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* **Power transferred to the Central Government from the commencement of the Companies (Second Amendment) Act, 2002 (11 of 2003).**

** **Power transferred to the Central Government and in respect of Sick Industrial Companies power vested with National Company Law Tribunal from the commencement of the Companies (Second Amendment) Act, 2002 (11 of 2003).**

† **Power transferred to National Company Law Tribunal from the commencement of the Companies (Second Amendment) Act, 2002 (11 of 2003).**

§ For the text of the Companies (Compliance Certificate) Rules, 2001, see *Appendix* 38.

§ For the full text of the Guidance Notes on Compliance Certificate and for Specimen Compliance Certificate Form as issued by ICSI see *Appendix* 312.

Secretarial Practice : Service of documents on Registrar

Ensure that the documents served on the Registrar be as far as possible hand delivered and acknowledgment obtained or alternatively sent by registered post acknowledgment due or under certificate of posting alongwith bank draft towards payment of filing fee so as to reach him before the appointed day.

S. 53. Service of documents on members by company.—(1) A document may be served by a company on any member thereof either personally, or by sending it by post to him to his registered address, or if he has no registered address in India, to the address, if any, within India supplied by him to the company for the giving of notices to him.

(2) Where a document is sent by post,—

(a) service thereof shall be deemed to be effected by properly addressing, prepaying and posting a letter containing the document, provided that where a member has intimated to the company in advance that documents should be sent to him under a certificate of posting or by registered post with or without acknowledgment due and has deposited with the company a sum sufficient to defray the expenses of doing so, service of the document shall not be deemed to be effected unless it is sent in the manner intimated by the member; and

(b) [1][* * * *] such service shall be deemed to have been effected—

(i) in the case of a notice of a meeting, at the expiration of forty-eight hours after the letter containing the same is posted, and

(ii) in any other case at the time at which the letter would be delivered in the ordinary course of post.

(3) A document advertised in a newspaper circulating in the neighbourhood of the registered office of the company shall be deemed to be duly served on the day on which the advertisement appears, on every member of the company who has no registered address in India and has not supplied to the company an address within India for the giving of notices to him.

(4) A document may be served by the company on the joint-holders of a share by serving it on the joint-holder named first in the register in respect of the share.

(5) A document may be served by the company on the persons entitled to a share in consequence of the death or insolvency of a member by sending it through the post in pre-paid letter addressed to them by name, or by the title of representatives of the deceased, or assignees of the insolvent, or by any like description, at the address, if any, in India supplied for the purpose by the persons claiming to be so entitled, or until such an address has been so supplied by serving the document in any manner in which it might have been served if the death or insolvency had not occurred.

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1. The words "unless the contrary is proved" omitted by Act 65 of 1960, s. 16.

NOTES

Eng. Act, 1948 : Articles 131, 132 and 133 of Table A of Sch. I.

Eng. Act, 1985 : Sch. I Table A, Regns. 112, 115 and 116.

Companies (Amendment) Act, 1960

The amendment made in section 53(2)(b) is explained in the notes on clause, thus: "The expression 'unless the contrary is proved' in clause (b) of sub-section (2) of section 53, may be construed to mean that the presumption regarding the receipt of notice of a general meeting is rebuttable, and is likely to cause difficulty in practice in those cases where members receive the notice of a general meeting late due to delays in post but may nevertheless urge that the notice given to them is a notice of a period less than 21 days and goes against the provisions of section 171(1) of the Act. It is, therefore, proposed to delete the expression from clause (b) of section 53(2)" (*Clause* 17 of the Bill).

The compulsory Articles 112 to 115 of Table A of Schedule I of the previous Act of 1913 are with some modifications now incorporated in this section as a statutory provision.

Notice of general meeting

No notice need be given to a member who has not given his address in India.

In the case of notice of a general meeting sent to a member by post, service under the present section shall be deemed to have been effected at the expiry of 48 hours after it is posted. This means that even if it can be proved that in fact service was effected or could be effected only after the expiry of forty-eight hours, that will not affect the service being treated as good service. Previously the provision was that such notice should be deemed to have been effected 'at a time at which the letter would be delivered in the ordinary course of post.' The effect of this provision is that if notice of a general meeting is sent by post, it must be posted at such time as to give 21 clear days notice as required by section 171, plus 48 hours in addition. If for instance, a general meeting is to be held at 3 P.M. on the 5th April, service of the notice of the meeting will be deemed to have been duly effected if it had been despatched by post at any time before 3 P.M. on 13th March. This will satisfy the requirement of 21 days clear notice plus the 48 hours for transmission by post. A notice returned unserved cannot, however, be presumed to be good service where there are circumstances of suspicion negativing the presumption. Where a notice sent by registered post is returned unserved, the company is bound to enquire, especially in the case of a shareholder whose shares are to be forfeited, as to whether the shareholder's address has not changed. *Promila Bansal (Mrs.) v. Wearwell Cycle Co. (India) Ltd.*, (1978) 48 Com Cases 202 (Del).

The presumption as to deemed delivery was not raised when at the time of posting, the post office was, within the knowledge of the company, on strike. Any mode of service adopted by the company in sending out notices, although authorised by the articles of association, is likely to be held ineffective service, if not coming within the recognised means. *Bradman v. Trinity Estates Ltd.*, 1989 BCLC 757 (Ch D). The Court cannot extend the period of 48 hours laid down in clause (b)(i) of sub-section (2) [in order to give more time to members to enable them to file nominations, in this case] as by doing so the court will be extending the period which has purposely been limited to minimise the scope of mischief in holding of the AGM. *Maharaja Exports v. Apparels Exports Promotion Council*, (1986) 60 Com Cases 353 (Del).

Notice to shareholders residing abroad

It has been held in English cases that the Act refers only to shareholders who can be reached by post within the country. Service by post is not possible for shareholders who do not have an address for service within the country. See, SHACKLETON ON MEETINGS,

128 (9th Edn., 1997). Also see, *In re, Newcastle United Football Co. Ltd.,* (1932) WN 109. Where member's registered address was situate in an enemy territory, the court held that the company could carry on business without serving notices on such a member. *Anglo International Bank Ltd., In re,* (1944) 14 Com Cases 86, 90 : (1943) 2 All ER 88 (CA).

Service by post, when deemed effective [Sub-section (2)]

Service of notice of a meeting will be deemed to have been effected only when it is posted in a letter containing the same. The letter should carry the address noted in the register of members and the same should be substantially accurate though not literally the same. *Liverpool Marine Insurance Co. v. Haughton,* (1874) 23 WR 93. A notice sent to all the members of the company on the register at the date of sending out is good, even though the register is subsequently rectified with restrospective effect to a day prior to that date. *Sussex Brik Co., Re,* (1904) 1 Ch 598 (CA). Proof of posting must be given and entry in the despatch register is not sufficient. *Major Teja Singh v. Hindustan Petroleum Co. Ltd.,* (1961) 31 Com Cases 573 (Punj).

It is not stated at which post office or box the letter has to be posted. Presumably, it has to be posted at or near the place of the registered office of the company. The provisions in the section will not be satisfied if the posting is made deliberately at any far off place, with a view to delay delivery.

A notice duly addressed and stamped and sent under certificate of posting is deemed to have been duly served even if the notice does not in fact reach the addressee. *Ramdas v. Cotton Ginning Co.,* (1887) 9 All 366; *Jadabpore Tea Co. Ltd. v. Bengal Doars National Tea Co. Ltd.,* (1984) 55 Com Cases 160 (Cal) (DB). For other cases in which this presumption was taken note of see; *Bimal Singh Kothari v. Muir Mills Co. Ltd.,* (1952) 22 Com Cases 248 (Cal); *Bharat Bhushan v. H.B Portfolio Leasing Ltd.,* (1992) 74 Com Cases 20 (Del); *Shekhar Mehra v. Kilpest (P.) Ltd.,* (1986) 3 Comp LJ 234 (MP).

A notice of meeting for passing a resolution for curbing the powers of managing director despatched under "Certificate of Posting" was held to be good enough service and the presumption of service prevailed inspite of the allegation of the dislodged managing director that the notice was not received by him. *Mani (M.S.) v. M.S. Madhusoodan,* (1991) 5 Corpt LA 187 (Ker—DB). The court **followed** the principles laid down in : *Kanak Lata Ghose v. Amal Kumar Ghose,* AIR 1970 Cal 328; *Achamma Thomas v. E.R. Fairman,* AIR 1970 Mys 77; *Ramshankar Prasad v. Sindri Iron Foundry (P.) Ltd.,* AIR 1966 Cal 512 and *Jadabpore Tea Co. Ltd. v. Bengal Doars National Tea Co. Ltd., (Supra).* A notice of a meeting despatched under certificate of posting creates a presumption that it was served at the expiration of 48 hours. *Challa Rajendra Prasad v. Asian Coffee Ltd.,* (2000) 100 Com Cases 689 : (1999) 2 Comp LJ 46 : (1999) 20 SCL 414 (AP).

Notices of a meeting posted on Aug. 31 and Sept. 1 would be deemed to be delivered on Sept. 2 and 3. They are ineffective for a meeting to be held on Sept. 21. *Balwant Singh Sethi v. Sardar Zorawar Singh Hushnak Singh Anand,* (1988) 63 Com Cases 310 (Bom).

It has to be noted that under sub-section (2)(a) there may be special instructions given by any members for notices being sent to him by registered post or under certificate at his expense. See, *Abdul Karim Khan v. Sirpur Paper Mills Ltd.,* (1969) 39 Com Cases 33, 37 (AP). A letter sent by ordinary post duly stamped is sufficient unless the member had issued advance instructions that it should be sent by certificate of posting or by registered post and provided funds for that purpose. *Kuldip Singh Dhillon v. Paragaon Utility Financiers,* (1986) 60 Com Cases 1075, 1080 (P&H).

Rebuttable Presumption

The presumption of service which arises under the section by showing the fact of despatch is neither absolute nor irrebuttable. The question is one of fact. The fact of posting

has to be proved by the sender. On such proof, the addressee is presumed to have been served. Now it is up to him to show that there was no service. *M.S. Madhusoodanan v. Kerala Kaumudi P. Ltd.*, (2003) 4 Comp LJ 185 (SC).

Where the director in question attended the general body meeting as well as a Board meeting, his contention that he did not receive the notices of meetings and that he attended because he came to know the facts through an oral and a telephonic message was held to be unacceptable. *R. Khemka v. Deccan Enterprises P. Ltd.*, (1998) 5 Comp LJ 258 : (1998) 16 SCL 1 (AP).

The Company Law Board has expressed the view that service under certificate of posting creates a very weak presumption of service because a certificate of posting can be managed without actually putting the letters in the course of post. The presumption would therefore be rebuttable. *Akbarali A. Kalvert v. Konkan Chemicals P. Ltd.*, (1997) 88 Com Cases 245 (CLB). The CLB said [at p. 117]:

"While coming to this conclusion we have **relied** on our decision on this issue in *Stridewell Leathers (P.) Ltd. v. Shoe Specialities (P.) Ltd.*, (Company Petition No. 29 of 92) : (1996) 1 Comp LJ 426 (CLB). In that case we had occasion to consider the decisions in *Kanaklata Ghosh v. Anand Kumar Ghose*, AIR 1970 Cal 328 and *Achamma Thomas v. E.R. Fairman*, AIR 1970 Mys 77. In both these cases, it was held that in case of despatch under postal certificates a general presumption of posting could be drawn. However, in both the cases scope has been left to take the circumstances into account while drawing the presumption. Therefore, one will have to take into consideration the circumstances in determining the service of the letters sent under postal certificates. Even if it is presumed that the petitioners have suppressed the receipt of the notices since they were anticipating the payments it could not be said of notice of the extraordinary general meeting for additional share issue at which time the dispute assumed serious proportions. We have also noted that though the respondents have produced certificates of posting in respect of extraordinary general meetings, no such certificates were produced in respect of Board meetings. In fact, the respondents have admitted that at the Board meetings the petitioners were present though for a while. Thus, the grounds for vacation of office of directors have not also been conclusively established. The petitioners have also drawn our attention to the decision of the Supreme Court in *Parameshwari Prasad Gupta v. Union of India*, AIR 1973 SC 2389 to state that even if notice was not given to one of the directors, the resolution passed at such a Board meeting is not valid". In view of the above we are convinced that the board and the general body meetings of the company were not duly convened and all those meetings were invalid."

Notice of meetings sent to members under postal certificate creates a presumption of service, but the presumption is rebuttable. Where the company's despatch register which was supposed to show the despatch of the relevant notices, or account books supposed to show the postal expenditure incurred, were not produced and the members denied having received the notice, it was held that the presumption of service under S. 114 of the Evidence Act was not applicable. Thus, there was no presumption that notices were served on the members. *Bhankerpur Simbhaoli Beverages P. Ltd. v. P.R. Pandya*, (1996) 86 Com Cases 842 (P&H).

Where the addressee-member denies service through postal certificate, it would be for the company to prove by proper evidence that the notice had been properly despatched under certificate of posting, particularly when the circumstances pointed to a different inference. *Micromeritics Engineers P. Ltd. v. S. Munusamy*, (2002) 50 CLA 245 (Mad) : (2002) 38 SCL 846. Where the addressee denied receipt of the letter alleged to be sent to him under a certificate of posting, the onus to prove the posting shifted to the sender who had to produce corroborative records like postage account, despatch register, etc. *Ajit Singh v. DSS Enterprises P. Ltd.*, (2001) 45 CLA 102 : (2001) 34 SCL 547 : (2001) 4 Comp LJ 421 (CLB—N-Delhi).

Obligations not discharged by failure of communication

Where the documents were sent by Registered Post and for some reason they were not delivered to the addressee, it could not be said that the company becomes discharged from its obligations to send the documents again. *Inter Sales v. Reliance Industries Ltd.*, (1999) 35 CLA 370 (Cal).

Issue of refund orders, allotment letters/certificates, and letters of offer by registered post

Department's Circular I.—"The Government has been receiving complaints from the investing public regarding non-receipt of refund orders, allotment letters, share certificates, rights of offer and dividend warrants. In this connection, it may be stated that the Ministry of Finance, Department of Economic Affairs, *vide* their *Circular Letter No.* 8/15/SE/86-B, dated 3rd June, 1986, addressed to all stock exchanges, informed that the Government has decided that henceforth all companies listed or seeking enlistment on stock exchanges, shall issue refund orders, allotment letters/certificates only by registered post. It has now been considered necessary that with a view to protect the interests of investors, the letters of offer for rights issue be also issued to the shareholders by registered post, in future. You are, therefore requested to ensure strict compliance with these guidelines by your constituent member companies". [*Circular No.* 6 of 1992, dated 3-9-1992].

Department's Circular II.—"I am directed to invite your attention to this *Department's Circular No.* 6/92 (No. 17/8/89-CL-V), dated 3-9-1992, [*printed above*] on the above subject, and to say that your constituent member-companies were advised to ensure issue of refund orders only by registered post. The matter has been considered further, keeping in view the constraints faced by the companies in issuing the refund orders by registered post, as the Postal Department is not able to cope up with the work involved. It has, accordingly, been decided that it will be in order for the companies to issue refund orders for amounts exceeding Rs. 1500/-per refund order only by registered post and the refund orders below that amount be issued under Certificate of Posting. In case of delay in refund, interest for the delayed period be calculated 15% per annum and paid along with the refund order or while issuing the duplicate refund order, as the case may be upto the date of actual despatch. In this regard, attention is also invited to the penal provisions contained in section 73(2B) of the Companies Act, 1956." [*Circular No.* 1/93; *File No.* 17/8/89-CL-V, dated 16-3-1993].

Service by newspaper advertisement [Sub-section (3)]

The issue of a public advertisement under this sub-section does not obviate the necessity of sending individual notice to shareholders who have intimated to the company their registered addresses in India.

An advertisement in a newspaper in the neighbourhood of the registered office will be deemed to be due service of notice effective from the date of the advertisement on every shareholder who has not supplied to the company any address in India. *United Bank of India Ltd. v. United India Credit & Development Co. Ltd.,* (1977) 47 Com Cases 689 (Cal).

Service in case of joint shareholders [Sub-section (4)]

Sub-section (4) gives this latitude to companies that only the first mentioned joint holder need be informed. But this is only a privilege given to companies and they may at their choice inform all joint holders separately.

Communication through electronic media

The Government of UK has published a consultation document which contains proposals enabling companies to communicate elecronically with shareholders. Access to company accounts, proxy voting and incorporation procedures through electronic processes are all covered. *DTI Press Notice,* P/2000/98, [UK].

Personal delivery

The notice of a meeting of directors was claimed to have been handed over to the assistant of the director, but the despatch register did not show the details of the despatch. The court said that there could be no presumption of service. The meeting was invalidated and, therefore, the resolution passed at the meeting was of no effect. *M.S. Madhusoodanan v. Kerala Kaumudi P. Ltd.,* (2003) 117 Com Cases 19 (SC) : (2003) 55 CLA 372 : (2003) 46 SCL 695.

Effect of death and insolvency [Sub-section (5)]

When a shareholder dies it becomes the duty of the legal representatives to furnish their address for a notice to be sent and if they fail to send the intimation to the company, the

company would be entitled to serve at the address which is recorded with it. Such a notice would be deemed to have been served as if the death of the member had not occurred. *Canara Bank Ltd. v. T.P.R. Tampi,* (1972) 42 Com Cases 473 (Ker); *Tricumdas Mills v. Haji Saboo,* (1902) 4 Bom LR 215 (Bom).

Same is the effect of insolvency because the representatives or the assignee/receiver of the insolvent member have a right to register themselves as holders of the shares but as long as they do not do so the company can justifiably send notices to the registered address of the insolvent members.

§ See also Notes under s. 172(2) under the heading "Notice in case of death or insolvent member".

Jurisdiction for complaint against default

Section 53, which deals with service of documents on members by a company, makes it clear that the cause of action for non-compliance with the provision arises at the place where the registered office of the company is situate and from where documents are to be sent. The court which has jurisdiction to entertain a complaint for non-supply of the documents is the court within whose territorial jurisdiction the registered office of the company is situate. *Karnataka Bank Ltd. v. B. Suresh,* (2001) 105 Com Cases 110 : (2001) 2 Comp LJ 417 : (2001) 32 SCL 441 : (2001) SCL 32 (Kant).

Secretarial Practice Notes : Service of documents on members

(i) Whether documents were served on every member

(a) personally or by post, properly addressed and pre-paid ? and

(b) mode of posting was in accordance with request, if any, of a member,

(ii) Check sufficient sum to defray expenses had been received from such members and notice sent as desired by the members.

(iii) In case of a member with no registered address or any address in India whether documents were advertised in a newspaper circulating in the neighbourhood of the registered office?

(iv) In case of joint holders, whether served on first named holder in the Register of Members?

(v) In case of death or insolvency of a member, whether sent to representative, if any, or to the original address of the deceased/insolvent?

(vi) Ensure that the despatch register is properly maintained in the ordinary course of business.

Documents Involved: (1) Despatch register, (2) Members correspondence, (3) Newspaper cutting, (4) Register of members, (5) Postal receipts.

Authentication of Documents and Proceedings

S. 54. Authentication of documents and proceedings.—Save as otherwise expressly provided in this Act, a document or proceeding requiring authentication by a company may be signed by a director [1][* * * *] the manager, the secretary or other authorised officer of the company, and need not be under its common seal.

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1. The words "the managing agent, the secretaries and treasurers" omitted by the Companies (Amendment) Act, 2000 (53 of 2000), s. 15, (w.e.f. 13-12-2000).

NOTES

Eng. Act, 1948 : Sec. 36
Eng. Act, 1985 : Sec. 41

Previous Act : Sec. 150

Companies (Amendment) Act, 2000

The terms "managing agents, secretaries and treasurers" have been omitted by the Amendment Act, 2000. The amendment is of consequential nature.

Scope of section

A document or proceeding requiring authentication may be signed by a director, or manager, or secretary or other authorised officer. The named officers who sign by virtue of their office do not require any authorisation. But in the case of any other officer there must be actual authority. See *Calico Printers' Assn. Ltd. v. A.A. Karim & Bros.*, (1931) 1 Com Cases 58 : AIR 1930 Bom. 566. [Order 29, Rule 1, CPC, 1908].

By authentication of a document is only meant a certification of its genuineness or authorship. It has nothing to do with the truth or correctness of the facts or other matter contained in the document.

Signature of agent whether signature of company

The question was whether the signature of an agent on behalf of a company which contained misrepresentations could be regarded as the signature of the company. Accordingly if the Assistant Secretary of the defendant company was authorised to sign the representations then the defendant company would be bound. But this requires evidence on the scope of the assistant secretary's authority. A representation signed by a duly authorised agent or officer of a company acting within the scope of his authority and on behalf of the company in the course of its business may amount to a representation and signature of the company. *U.B.A.F. Ltd. v. European American Banking Corporation*, (1984) 2 All ER 226 : (1984) BCLC 112 (CA).