MODULE I
THE INDIAN COMPANIES ACT, 2013.

1

NATURE, FEATURES OF COMPANIES

Unit Structure

1.0 OBJECTIVES

After studying the unit, the students will be able to:

- Understand the characteristics of the Company
- Understand the Advantage and Disadvantage of Companies
- Explain how to form the company.
- Understand the meaning and effects Lifting of Corporate Veil
- Understand the Effects of Non- Registration.

1.1 INTRODUCTION

HIGHLIGHTS OF THE COMPANIES BILL, 2012 (as passed by the Lok Sabha on 18.12.12 and by the Rajya Sabha on 08.08.13) The Bill has 470 clauses as against 658 Sections in the existing Companies Act, 1956. The entire bill has been divided into 29 chapters. Many new chapters have been introduced,

Section 2 (20) of Companies Act, 2013" "Company" means a company incorporated under this Act or under any previous company law.

The word "company" has no strictly technical or legal meaning. A body corporate or corporation includes a company incorporated outside India, but does not include a co-operative society registered under the law relating to co-operative societies, and anybody corporate which the Central Government may, by notification, specify for this purpose.

Company" is derived from two words: "com"- group and "panies"- bread. Therefore, it means group that eat their bread together.

A company is: - an association or collection of individuals, whether natural persons, legal persons, or a mixture of both.

- Company members share a common purpose and unite
- in order to focus their various talents and organize their collectively available skills or resources to achieve specific, declared goals
- not merely a legal institution
- a legal device for attainment of social (Section 25/8) or economic end and to a large extent publicly and socially responsible

A company as an entity has many distinct features which together make it a unique organization. The essential characteristics of a company are following:

1.2 CHARACTERISTICS OF THE COMPANY

1. Voluntary association:

A company is a voluntary association formed by an individual or group of individuals. Most companies are formed with the motive of profit-making except the Section 8 companies that is Non-Governmental Organization . Profit earned is divided among the shareholders or saved for the future expansion of the company**.**

2. Separate Legal Entity:

A company becomes a separate legal entity as compared to its members when it registered with an appropriate authority that is ROC (Registrar of Company). The company is distinct and different from its members in law. It has its own seal and its own name; its assets and liabilities are separate and distinct from those of its members. It is capable of owning property, incurring debt, and borrowing money, employing people, having a bank account, entering into contracts and suing and being sued separately.

Case Law: Salomon v/s Salomon: Salomon had a business in leather and shoe manufacturing. Due to some circumstances, he created his own company and sells his previous business of shoe manufacturing to this company. Salomon gave one share each to his wife, daughter, sons, and the rest of the company's shares were held by him. After few years, the company was wound up and had some existing liabilities but did not have enough assets to pay off the liabilities. Unsecured creditors sued Salomon for repayment of their money, but the court held that the company was not an agent or a trustee for Salomon. The company is entirely different from the individual, and hence the contentions of the creditors could not be upheld.

3. Limited Liability:

The liability of the members of the company is limited to contribution to the assets of the company up to the face value of shares held by him. A member is liable to pay only the uncalled money due on shares held by him. If the assets of the firm are not sufficient to pay the liabilities of the firm, the creditors can force the partners to make good the deficit from their personal assets. This cannot be done in the case of a company once the members have paid all their dues towards the shares held by them in the company.

The liability of a company may be limited either by Shares or Guarantee.

Company limited by Guarantee: Liability of shareholders is limited to a certain amount of guarantee mentioned in the memorandum payable only at the time of wind up and losses occurred by the company.

Company limited by Shares: Liability of the members shall be limited to the extent of unpaid money or shares held by them.

4. Perpetual Succession:

"Perpetual Succession" in a company is best defined by this line - ***Members may come and go but the company goes on forever.*** It means company never dies If any member dies or leaves the company it does not make any difference to the corporate existence of the company. It is one of the fundamentals of a company's existence. Perpetual succession means that a company's life is not determined by the longevity of its members, shareholders, promoters, directors, employees or anyone else. If a shareholder dies, or hypothetically, all the shareholders die, only their shares in the company will be transferred to new people. If even a key director resigns, he/she will be replaced but the company will continue on.

5. Separate Property:

A company is a distinct legal entity. The company's property is its own. A member cannot claim to be owner of the company's property during the existence of the company.

6. Transferability of Shares:

Shares in a company are freely transferable, subject to certain conditions, such that no share-holder is permanently or necessarily wedded to a company. When a member transfers his shares to another person, the transferee steps into the shoes of the transferor and acquires all the rights of the transferor in respect of those shares.

7. Common Seal:

A company is an artificial person and does not have a physical presence. Thus, it acts through its Board of Directors for carrying out its activities and entering into various agreements. Such contracts must be under the seal of the company. The common seal is the official signature of the

company. The name of the company must be engraved on the common seal. Any document not bearing the seal of the company may not be accepted as authentic and may not have any legal force.

8. Capacity to sue and being sued:

A company can sue and be sued in its name and may even sue its members. It also has a right to seek damages where a defamatory matter is published about the company, which affects its business.

9. Separate Management:

A company is administered and managed by its managerial personnel i.e. the Board of Directors. The shareholders are simply the holders of the shares in the company and need not be necessarily the managers of the company.

1.3 DISADVANTAGE OF INCORPORATION OF COMPANY

1. Cumbersome Formalities and Cost
2. Separation of control from ownership
3. Greater Social Responsibility
4. Greater Tax Burden in Certain Cases
5. Winding Up Procedure is lengthy

Cumbersome Formalities and Cost:

Incorporation of a company is a very complex legal process and it involves a considerable amount of time and money. These elaborate procedures have been established so as to discourage people from doing business who not serious and passionate about it.

Even after the incorporation of the company, it has to be run and managed very strictly. In accordance with the legal provisions provided by the Companies Act. The returns and other documents have to be registered at the Registrar of Companies.

Certain particular events or activities such as accounts, corporate audits, meetings, borrowing, lending, investment and issue of capital, dividends etc, are necessarily required to be conducted and carried out by the provisions of the Companies Act.

Separation of control from ownership:

Members of small shareholders of a company do not have any effective control over the functions and decisions of the company because, the number of people in the company is large in number that an individual or even a small group of people cannot have a big effect on the functioning of the organisation.

Greater Social Responsibility:

Companies incorporated under Companies Act have to pay a higher tax. An incorporated company does not get any discounts and any minimum taxable limits. An incorporated company also has to pay income tax on the whole of its income at a fixed rate whereas other companies are charged at a gradual or slab rate.

Winding up Procedure is lengthy:

The Companies Act provides for a very much lengthy and complicated process to explain the winding up of a company. This process takes more time to complete the formalities, time consuming and expensive.

1.4 FORMATION OF COMPANIES

Introduction:

The formation and incorporation of a company are very much similar to the birth of a human like it also goes through various stages of formation of its body parts during the womb stage. Number of preliminary works are to be carried out to bring a company into existence. The process of an idea converting into a company includes various stages, these crucial stages of the pre-incorporation and formation stages are discussed in detail as under. This lesson explains the functions, duties and liabilities of a promoter along with providing in depth knowledge into cases regarding pre-incorporation contract.

Role of Promoters For Incorporation of Company:

"Promoter is the person who originates the idea for formation of a company and gives the practical shape to that idea with the help of his own resources and with that of others."

A person cannot be held as promoter merely because he has signed at the foot of the Memorandum or that he has provided money for the payment of formation expenses.

The promoters, in fact, render a very useful service in the formation of the company. A promoter has been described as "a creator of wealth and an economic prophet." The promoters carry a considerable risk because if the idea sometimes goes wrong then the time and money spent by them will be a waste.

A promoter may be an individual, a firm, an association of persons or even a company.

S. 2 (69) of Companies Act 2013 defines Promoter as:

(a) "who has been named as such in a prospectus or is identified by the company in the annual return referred to in section 92; or

(b) who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

(c) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act:

Provided that nothing in sub-clause (c) shall apply to a person who is acting merely in a professional capacity"

Preliminary Contracts/Pre-Incorporation Contracts Made by the Promoters:

Preliminary contracts are those contracts which are made by the promoters with different parties on behalf of the company yet to be incorporated. Such contracts are generally entered into by promoters to acquire some property or right for and on behalf of the company to be formed.

The promoters enter into preliminary contracts, generally as agents or trustees of the company. Such contracts are not legally binding on the company because two consenting parties are necessary to a contract whereas the company is non-entity before incorporation.

Functions of a Promoter:

The Promoter Performs the following main functions:

1. To conceive an idea of forming a company and explore its possibilities.

2. To conduct the necessary negotiation for the purchase of business in case it is intended to purchase as existing business. In this context, the help of experts may be taken, if considered necessary.

3. To collect the requisite number of persons (i.e. seven in case of a public company and two in case of a private company) who can sign the 'Memorandum of Association' and 'Articles of Association' of the company and also agree to act as the first directors of the company.

4. To decide about the following:

(i) The name of the Company,

(ii) The location of its registered office,

(iii) The amount and form of its share capital,

(iv) The brokers or underwriters for capital issue, if necessary,

(v) The select the bankers,

(vi) The selection of auditors of company,

(vii) The legal advisers.

5. To get the Memorandum of Association (M/A) and Articles of Association (A/A) drafted and printed.

6. To make preliminary contracts with vendors, underwriters, etc.

7. To make arrangement for the preparation of prospectus, its filing, advertisement and issue of capital.

8. To arrange for the registration of company and obtain the certificate of incorporation.

9. To defray preliminary expenses.

10. To arrange the minimum subscription.

Promoter of Company and his legal position towards Company:

The promoter is neither a trustee nor an agent of the company because there is no company yet in existence. The correct way to describe his legal position is that he stands in a fiduciary position towards the company about to be formed.

The promoters of a company stand undoubtedly in a **fiduciary position.** They have in their **hands the creation and molding** of the company. They have the power of defining how and when and in what shape and under what supervision, it shall start into existence and begin to act as a trading corporation."

From the fiduciary position of promoters, the two important results follow:

(1) A promoter cannot be allowed to make any secret profits. If it is found that in any particular transaction of the company, he has obtained a secret profit for himself, he will be bound to refund the same to the company.

(2) The promoter is not allowed to derive a profit from the sale of his own property to the company unless all material facts are disclosed. If he contracts to sell his own property to the company without making a full disclosure, the company may either repudiate/rescind the sale or affirm the contract and recover the profit made out of it by the promoter.

A promoter who wishes to sell his own property to the company must make a full disclosure of his interest.

The disclosure may be made:

(i) To an independent Board of Directors, or

(ii) In the articles of association of the company, or

(iii) In the prospectus, or

(iv) To the existing and intended shareholders directly.

If the promoter fails to discharge the obligation demanded of his fiduciary position the company may rescind the contract or may in the alternative choose to take advantage of the contract and sue the promoter for damages for breach of his duty to the company.

Secret profits on the sale of property can be recovered from a promoter only when the property was bought and sold to the company while he was acting as a promoter.

Rights of Promoter:

The rights of promoters are enumerated as follows:

1. Right of indemnity:

Where more than one person act as the promoters of the company, one promoter can claim against another promoter for the compensation and damages paid by him. Promoters are severally and jointly liable for any untrue statement given in the prospectus and for the secret profits.

2. Right to receive the legitimate preliminary expenses:

A promoter is entitled to receive the legitimate preliminary expenses which he has incurred in the process of formation of the company such as cost of advertisement, fee of solicitor and surveyors. The right to receive the preliminary expenses is not a contractual right. It depends upon the discretion of the directors of the company. The claim for expenses should be supported by vouchers.

3. Right to receive the remuneration:

A promoter has no right against the company for his remuneration unless there is a contract to that effect. In some cases, articles of the company provide for the directors paying a specified amount to promoters for their services but this does not give the promoters any contractual right to sue the company. This is simply an authority vested in the directors of the company.

However, the promoters are usually the directors, so that in practice the promoters will receive their remuneration.

The remuneration may be paid in any of the following ways:

(i) A commission may be paid to the promoter on the purchase price of the business or property taken over by the company through him.

(ii) The promoters may be granted by the company a lumpsum amount.

(iii) The promoters may be given fully or partly paid shares in consideration of their services rendered.

(iv) The promoter may be given a commission at a fixed rate on the shares sold.

(v) The promoter may purchase the business or other property and sell the same to the company at an inflated price. He must disclose this fact.

(vi) The promoters may take an option to subscribe within a fixed period for a certain portion of the company's unissued shares at par.

Whatever be the nature of remuneration, it must be disclosed in the prospectus if paid within the preceding two years from the date of prospectus.

Duties of Promoter:

The duties of promoters are as follows:

1. To disclose the secret profit:

The promoter should not make any secret profit. If he has made any secret profit, it is his duty to disclose all the money secretly obtained by way of profit. He is empowered to deduct the reasonable expenses incurred by him.

2. To disclose all the material facts:

The promoter should disclose all the material facts. If a promoter contracts to sell the company a property without making a full disclosure, and the property was acquired by him at a time when he stood in a fiduciary position towards the company, the company may either repudiate the sale or affirm the contract and recover the profit made out of it by the promoters.

3. The promoter must make good to the company what he has obtained as a trustee:

A promoter stands in fiduciary position towards the company. It is the duty of the promoter to make good to the company what he has obtained as trustee and not what he may get at any time.

4. Duty to disclose private arrangements:

It is the duty of the promoter to disclose all the private arrangement resulting him profit by the promotion of the company.

5. Duty of promoter against the future allottees:

When it is said the promoters stand in a fiduciary position towards the company then it does not mean that they stand in such relation only to the company or to the signatories of memorandums of company and they will also stand in this relation to the future allottees of the shares.

Liabilities of Promoter:

The liabilities of promoters are given below:

1. Liability to account in profit:

As we have already discussed that promoter stands in a fiduciary position to the company. The promoter is liable to account to the company for all secret profits made by him without full disclosure to the company. The company may adopt any one of the following two courses if the promoter fails to disclose the profit.

(i) The company can sue the promoter for an amount of profit and recover the same with interest.

(ii) The company can rescind the contract and can recover the money paid.

2. Liability for mis-statement in the prospectus:

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

The promoter may also be imprisoned for a term which may extend to two years or may be punished with the fine up to Rs. 5,000 for untrue statement in the prospectus.

3. Personal liability:

The promoter is personally liable for all contracts made by him on behalf of the company until the contracts have been discharged or the company takes over the liability of the promoter. The death of promoter does not relieve him from liabilities.

4. Liability at the time of winding up of the company:

In the course of winding up of the company, on an application made by the official liquidator, the court may make a promoter liable for misfeasance or breach of trust. Further where fraud has been alleged by the liquidator against a promoter, the court may order for his public examination. (Sec. 478).

Registration Process:

The Companies Act, 2013 provides for the kinds of companies that can be promoted and registered under the Act.

Section 3(1) of the Companies Act 2013 states that a company may be formed for any lawful purpose by—

1. Minimum Members Required:

(a) **seven** or more persons, where the company to be formed is to be a public company;

(b) **two or more persons,** where the company to be formed is to be a private company; or

(c) **one person**, where the company to be formed is to be One Person Company that is to say, a private company, by subscribing their names or his name to a memorandum and complying with the requirements of this Act in respect of registration

A company formed under Section 3(1) may be either:

(a) a company limited by shares; or

(b) a company limited by guarantee; or

(c) an unlimited company.

2. Approval of the Proposed Name of the Company:

Before the company is registered, it is essential to obtain the approval of the Registrar to its proposed name. There is a specific application form for this purpose that is FORM INC-1. The promoter generally selects a few suitable names in order of preference and apply to the National Company Law Tribunal through the Registrar of the State in which the company is to be registered in with a fee of Rs.1000. On hearing about the available name, the promoter has to decide the name for the company. As per Section 4 (5) the name reserved shall be valid for a period of 60 days from the date on which the application has made.

3. Documents to be Filed with the Registrar during registration

The promoter should then prepare and file the following documents with the Registrar of Companies. He should also pay the necessary filing and registration fees.

A. Memorandum of Association:

The Memorandum is the heart of any company. It is the Constitution of the company and Primary document which is rigid in form. A Memorandum of Association (MoA) represents the charter of the company. It is a legal document prepared during the formation and registration process of a company to define its relationship with shareholders and it specifies the objectives for which the company has been formed. The company can undertake only those activities that are mentioned in the Memorandum of Association. As such, the MOA lays down the boundary beyond which the actions of the company cannot go. It should be printed and signed by the subscriber whose names are there in the Memorandum.

B. The Articles of Association:

Articles of association form a document that specifies the internal rules and regulations for a company's operations and defines the company's purpose. The document lays out how tasks are to be accomplished within the organization, including the process for appointing directors and the handling of financial records.

4. First Directors:

Minimum 02 directors in case of Private company and 3 in case of public company are required to be appoint. The names of first director have to be mentioned. Once the company name has been approved by MCA and registered, the next step is procuring a Digital Signature Certificate for private limited company. Digital Signature Certificate is a form of a digital key, which holds all the vital information about the registered signatory like name, address, email, phone number, and the authority which has provided the certificate. Further an intending directors must have an DIN (Directors Identification Number by filling up the Form No DIR-3. This DIN must be obtained by the director before commencing the procedure for incorporation of the company.

5. Consent of the Directors:

When Directors of a Company are appointed by the or named in the prospectus, a written consent to act as directors and also a written undertaking to take up and pay for the qualification shares if any are mandatory in Incorporation of a Company.

6. Statutory Declaration from the professionals:

A statutory declaration by any one of the following persons stating that all the requirements of the Act regarding Registration have been duly complied with:

a) An Advocate of the Supreme Court or High Court.

b) An Attorney or Pleader who is entitled to appear before a High Court.

c) A Chartered Accountant who is engaged in formation of the company and also practicing in India.

d) Any individual who is named in the Articles of Association as the Company's Director, Manager or Secretary.

7. An Affidavit:

Subscriber of Memorandum of Association required to file an affidavit stating that he/she is not convicted in any offence in relation with the formation or management of an affairs of any company.

8. Notices of the Address of the Registered Office:

The notice for the address of the registered office of the company should be given within 30 days after its incorporation or on the date from which the company commences its business whichever is earlier.

9. Payment of Fees and Stamp Duty:

After submitting the document to the Registrar of Company, Fees and Stamp duty has to be paid by the proposed company the said fees are depends upon the authorized capital of the company.

Final Procedure:

1. Certificate of Incorporation of the Company:

After the above documents are filed with the Registrar and the prescribed fees are paid and the Registrar is satisfied that all the requirements of the Act regarding the registration have been complied with, he will register the documents and retain them.

The Registrar will then issue a certificate known as **Certificate of Incorporation** and enter the name of the company in the Register kept in his office. This Certificate of Incorporation entitles the company as a legal person. In other words, the company is born upon the issue of Certificate of Incorporation. (Form No INC 11) and Rule 18 of Companies (Incorporation) Rules 2014.

Conclusiveness of the Certificate of Incorporation:

According to Companies Act, the certificate is conclusive evidence that all the requirements of the Act in regard to the formation and registration of the company have been complied with. The effects of the certificate of incorporation can be summed up as follows:

1. Neither the Court nor the Registrar can cancel the Certificate of Incorporation even if the company is formed for an illegal purpose.
2. The validity of the Certificate of Incorporation cannot be debated or argued upon on any grounds whatsoever.
3. When a certificate is issued, the new company is born. In other words, a legal person has come into existence through a legal process.
4. The date mentioned in the certificate is the date of incorporation of the company.

Effect of Certificate of Incorporation:

1) The company is born on the day on which it receives its certificate of incorporation.

2) It is conclusive evidence that all the requirements of the Act in relation to registration have been complied with. The validity of the certificate cannot be challenged on any ground.

Effect of Pre-incorporation contracts:

Often contracts are entered into on behalf of the company even before it is duly incorporated. Such pre-incorporation contracts are not binding on the company after it comes into existence. This is because at the time of making of the contract, the company is a non-entity. A company cannot even ratify these contracts, after it comes into existence for the simple reason that ratification relates back to the date on which the contract was made. So, the person entering into the contract incurs personal liability on such contracts.

Advantages of Incorporation:

The advantages of incorporation are

i) The company acquires an independent corporate personality.

ii) It becomes the owner of its capital, assets and other property.

iii) It is capable of perpetual succession.

iv) It can use a common seal.

v) It can sue in its own name.

vi) The liability of the members is limited.

vii) Shares of the company are easily transferable.

Disadvantages of Incorporation:

i) Social Responsibility:

Many companies have billions of dollars in assets and employ hundreds of thousands of people. They have a significant impact on society, and these companies often participate in social activities that are part of their corporate social responsibility (CSR) campaigns. These incorporation companies are so influential that they must adhere to certain social norms and contribute to the development of society.

ii) Formality and expenses:

Incorporation of a company is not only expensive but it also involves a number of formalities. Several requirements hare to be complied with - both as to the formation of a company as well as the administration of its affairs. Whereas, constituting a firm is a relatively easy and inexpensive affair.

iii) Lifting the veil of Corporation:

Personality of a company is a legal myth. It ignores reality. And the reality is that a company is an association of persons who are in fact the beneficial owners of corporate property. So in some cases, the courts ignore the legal personality of the company, pierce the veil of corporation and look at persons behind it. Thus, some of the advantages of incorporation may become illusory.

Following are the circumstances in which the courts may lift the veil of corporation:

a) When the company assumes an enemy character:

In Daimler Co. Ltd. v. Continental Tyre and Rubber co. (1916)2A C 307, the House of Lords, while determining the character of a company registered in England, held that though the company was registered in England it would assume enemy character if the persons in de facto control of its affairs are residents in an enemy country (Germany).

b) When the company is formed for evasion of taxes:

Where the company is formed only for the purpose of evasion of taxes, the court has the power to disregard the corporate personality of the company (Re Sir Dinshaw Maneckjee Petit).

c) Where the company is formed for fraudulent purposes:

The courts can pierce the corporate personality if the company is formed for a fraudulent purpose, or for an unlawful object (Gilford Motor Co. v. Horne)

d) Where the company is an agent or trustee:

Courts will refuse to uphold the separate and independent existence of a company where it is an agent of its, members or of another company.

e) Under Statutory Provisions:

The courts will crack the shell of corporate personality where, because of the fall in the number of members below the prescribed legal minimum (seven in case of a public company and two in case of private company) the liability has become unlimited.

f) Any other just case:

The courts may, in the interest of truth and justice, set aside the cloak of corporate personality so as to determine liability.

1.5 LIFTING OF CORPORATE VEIL / PIERCING OF CORPORATE VEIL

Lifting the corporate veil, in simple words means disregarding the corporate personality and looking behind the real person who are in the

control of the company and where a fraudulent and dishonest use is made of the legal entity, the individuals concerned will not be allowed to take shelter behind the corporate personality. In this regards the court will break through the corporate veil.

Corporate personality of a company should ordinarily be respected. The whole law of corporations is still based on this basic principle of corporate entity. There are umpteen instances in which the courts have upheld this principle and resisted the temptation to break through the veil. But when the benefit is misused, the court is not powerless and it can lift the veil of corporate personality to see the realities behind the veil. In doing so, the court sub serves the important public interest, namely, to arrest misuse or abuse of benefit conferred by law. 27 Thus, it is quite evident that 'Piercing the veil' law exists as a check on the principle that, in general, investor shareholders should not be held liable for the debts of their corporation beyond the value of their investment.

Statutory Provisions for Lifting the Corporate Veil:

1. Reduction of Number of Members:

If an organization carries on business for over a half year after the number of its members has been diminished to seven if there should arise an occurrence of a public company and two in the event of a privately owned business, each individual who knows this fact and is a member during the time that the organization so carries on business after the half year, becomes liable severally and jointly with the organization for the payment of debts contracted following a half year. It is just that part who stays after a half year who can be sued.

2. Fraudulent Trading:

If any business of an organization is gone ahead with the aim to defraud creditors of the organization or creditors of some other individual or for any deceitful reason, who was intentionally a party to the carrying on of the business in that way is subject to imprisonment or fine or both

3. Misdescription of the Company:

If any officer of the organization or other individual acting on its benefit signs or approves/authorized to be signed by the organization any promissory note, bill of exchange, order or cheque for money or goods, endorsement in which the organization's name is not specified in readable letters, he is obligated to fine and he is personally liable to the holder of the instrument unless the organization has effectively paid the sum.

4. Failure to Refund Application Money:

If the executives of an organization are mutually and severally at risk to reimburse the application cash with premium if the organization neglects to refund the cash within 130 days of the date of issue of the prospectus.

5. Failure to deliver Share Certificate etc. within stipulated time:

If the Company fails to deliver the share or debentures stipulated within the period of 3 months of allotment or within 2 months of application for transfer, then the company as well as every officer of the company who is at fault shall be punishable with fine up to Rs.5000/- per day till such default continues.

6. Investigation of ownership of Company:

Central Government if deems fit may order to evaluate or check who are the persons who are financially interested and also control its decision making, appoint one or more investigators for investigation and reporting in respect of membership of the company.

7. Liability for Ultra Vires acts:

The Directors and other officers of the company may be held personally liable under the provisions of other statues for example, for the recovery of tax arrears of a Private Company while being wound up, every director jointly and severally liable for the tax during the tenure for which the arrears is due.

1.6 EFFECTS OF NON-REGISTRATION

Company gets the status of body corporate on immediate effects of its registration with ROC which mandatory under Companies Act 2013 and any other previous Act. On registration company gets a status of Separate Legal Entity and carries Perpetual Succession. Company can enjoy all the rights as the common man enjoys the rights conferred by the constitution. Likewise when the company is registered with the ROC can enter into number of contracts, can acquire and disposed off the movable or immovable property with its own. Company can sue and can be sued in its corporate name.

When company is not registered with appropriate authority that is Registrar of Company will not enjoy the benefits of companies which are registered . **For Example :** Unregistered Company can not enjoy the Perpetual Succession status, Such companies will be treated as illegal association and Director or the Members are personally Liable for tortious acts. Such association can not enter into any contract with any other companies lawfully.

1.7 SUMMARY

Characteristics of the Company:

Voluntary association. Separate Legal Entity :.Limited Liability: Perpetual Succession Separate Property: Transferability of Shares: Common Seal:.

Capacity to sue and being sued: Separate Management:

Functions of Promoter:

1. To conceive an idea of forming a company and explore its possibilities.
2. To conduct the necessary negotiation for the company.
3. To collect the requisite number of persons to form the company.

Rights of Promoter:

Right of indemnity: Right to receive the legitimate preliminary expenses:

Right to receive the remuneration:

Duties of Promoter:

The duties of promoters: To disclose the secret profit: To disclose all the material facts: The promoter must make good to the company what he has obtained as a trustee: Duty to disclose private arrangements:

Duty of promoter against the future allottees:

Liabilities of Promoter: Liability to account in profit: Liability for mis-statement in the prospectus: Personal liability: Liability at the time of winding up of the company:

1.8 QUESTIONS

1. Define Company and Explain the features of company
2. What do you understand by lifting up of corporate veil ?
3. What do you understand by pre incorporation or preliminary contracts?
4. Explain the role of Promoter in formation of Company.

Write Short Notes

1. Body corporate
2. Government company
3. Subsidiary company
4. Promoter
5. Pre incorporation contract

*****

2

TYPES OF COMPANIES

MEMORANDOM OF ASSOCIATION AND ARTICLES OF ASSOCIATION - I

Unit Structure

2.0 OBJECTIVES

After studying the unit, the students will be able to:

- Understand the different types of Companies
- Understand the difference between Public and Private of Companies
- Understand the procedure for conversion of Public company into Private and Private Company in to Public Companies.
- Understand the advantages and disadvantages of Public and Private Companies.

2.1 INTRODUCTION

Classification of companies are essential for smooth understanding the functions and procedures. Companies are classified according to the Nature, Formation, Place of registration, Managerial Control, Liability Number of Shares held, Number of Directors etc.

2.2 TYPES OF COMPANY

Kinds of Companies:

For better understanding the body corporate of the companies are broadly divided in to number of classes on the following grounds:

A. Modes of formation.

B. On the basis of liability of members

C. Allowed number of members.

D. Management Control.

E. Miscellaneous Category

A. On The Basis of Mode of Formation/ Incorporation:

There are two modes under which a corporate body may be formed; one, through a special Act of parliament, and two, through registration under the Companies Act.

Based on Incorporation:

- Statutory Company
- Chartered Company
- Registered Company

Statutory Companies: Corporations created under the special legislations of parliament or state legislatures may be called statutory companies**;**

A statutory company are companies created to provide public service and has limited liability; they are not always required to utilize limited title. Such companies can be approved can by either the Central or State Legislature Statutory Company. A statutory company is usually created with the intention of serving people rather than the traditional business goal of creating profits. Further The provisions of the Companies Act applies to statutory companies except where the said provisions are inconsistent with the provisions of the Act creating them.

They are required, however, to provide annual reporting to the Legislature-Parliament. A few well-known statutory companies include the following:

- Reserve Bank of India (RBI)
- Life Insurance Corporation of India (LIC)
- Industrial Finance Corporation (IFC)
- State Bank of India (SBI)
- Food Corporation of India (FCI)
- Unit Trust of India (UTI)

2. Chartered Companies:

Companies which are established under a special charter or by order of monarch or kings or a queen. Such companies are come into in an existence under Royal Chartered Act. The nature and powers of a ventures are specified by the charter. Following are the examples of Chartered Companies.

- **British Broadcasting Corporation,**
- **Bank of England**
- **East India Company**

3. Registered Companies:

Such companies incorporated or registered under the Companies Act passed by the government of the country are termed as a registered company. These companies can come into existence after they have registered themselves by observing the necessary procedures laid down under Indian Companies Act from the time to time. Companies Act and the registrar of companies (ROC) has granted a certificate of incorporation/Certificate of Commencement of Business which are known to be conclusive evidence that the company has observed all the necessary formalities of incorporation and later on such certificates cannot be challenged on the ground whatsoever.

Example: Google India Pvt Ltd is a registered or an incorporated company.

(B) On the Basis of Liability:

On the basis of liability, the company can be classified into:

i. Companies limited by shares

ii. Companies limited by guarantee

iii. Unlimited companies.

i. Companies limited by shares:

When there is the liability of the members of a company is limited up to the amount unpaid on the shares if any, such a company is termed as a company limited by shares. In a company limited by shares the liability of the members is restricted to the unpaid amount on the shares held by them. The liability can be enforced during existence or life time of the company as well as during the winding up. Where the shares are fully paid up, no further liability leviable on them.

ii. Companies limited by guarantee:

These are the companies whereby the liabilities of members are limited up to the amount that they have agreed by the memorandum to contribute in the companies' assets at the time of liquidation. Therefore, it is a companies registered under Companies Act. In the case of such companies the liability of its members is limited to the amount of guarantee undertaken by them. Trade Associations, Research Associations, Clubs are examples of such companies. They promote various objects are various examples of guarantee companies.

iii. Unlimited Companies:

A company not having a limit on the liability of its members is known as unlimited company. In case of such a company every member is liable for the debts of the company as in an ordinary partnership in proportion to his interest in the company. As far as popularity is concerned, such companies are not so popular in India.

(C) On the basis of number of members.

(Allowed number of members)

i. Private Company

ii. Public Company

iii. One Person Company

(i) Private company:

A private company means a company which by its articles of association:

(i) It Restricts the right to transfer shares.

(ii) There is Limits the number of its members to fifty (excluding members who are or were in the employment of the company) and

(iii) Prohibits any invitation to the public to subscribe for any shares or debentures of the company.

(iv) Where two or more persons hold one or more shares in a company jointly, they are treated as a single member. There should be at least two persons to form a private company and the maximum number of members in a private company cannot exceed 50. A private limited company is required to add the words "Private Ltd" at the end of its name.

ii. Public company:

A public company means a company which is not a private company. A company the ownership of which is open to the public is a public company. In other words, anyone can purchase the shares of this company. There is no restrictions to the number of members or to the transferring right of its shares. There must be at **least seven** members to form a public company. It is of the basics fundamental of a public company that its articles do not contain provisions restricting the number of its members or excluding generally the transfer of its shares to the public or prohibiting any invitation to the public to subscribe for its shares or debentures. Only the shares of a public company are capable of being assigned in on a stock exchange.

iii. One Person Companies (OPC):

The Companies Act, 2013 completely transformed corporate laws in India by introducing many new concepts that did not there previously. One person company is also one of new concept introduced by companies act 2013. One person company (OPC) means a company formed with only sole or single person as a member, unlike the traditional manner of having at least two members. In one person company there is no mandatory requirement of minimum share capital. It is recognition of single person economic entity lightens a path for small traders, service providers to venture into business by expanding their opportunities through corporate existence.

D. Companies on the basis of Control or Holding. (On the basis of Management Control):

i. Holding and Subsidiary Companies:

Some companies', shares shall be held fully or partly by another company. In this case, the company controlling these shares becomes the holding company. Likewise, the company whose shares the parent company controls known as its subsidiary company. Holding companies exercise control over their subsidiaries by governing the composition of their board of directors. Further, parent companies also exercise control by controlling more than 50% of their subsidiary companies' shares.

ii. Associate Companies:

In such companies other companies have significant or important influence. This "significant influence" amounts to ownership of at least 20% shares of the associate company. The other company's control can exist in terms of the associate company's business decisions under an agreement. Associate companies can also exist under joint venture agreements.

iii. Government Company:

It means any company in which not less than 51 percent of the paid-up share capital is held by the Central Govt, and/or by any State Government or Governments or partly by the Central Government and partly by one or more State Governments. The subsidiary of a government company is also a government company.

E. Miscellaneous Category:

I. Foreign Companies:

Definition of Company under Companies Act, 2013 Section 2(20): "Company means a company incorporated under this Act or under any previous company law."

In General, a foreign company is a company which is incorporated outside India which,

- has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
- conducts any business activity in India in any other manner.

II. Dormant Company:

In common parlance, the word "Dormant" means inactive or inoperative.

When a Company is formed and registered for future project or to hold any intellectual property or an asset and not having any significant accounting transaction, such company apply for obtaining the status of Dormant Company. The provisions regarding Dormant Company has been given in Section 455 of Companies Act, 2013 read with Rule 3 to 8 of Companies (Miscellaneous) Rules, 2014 under Chapter XXIX. The Act prescribed lesser compliances for dormant companies in these provisions and rules.

iii. Small Company [S. 2(85)]:

A New concept has introduced by the Companies Act, 2013 that is 'small company'. Its just a type of Private Company but with less capital and turnover size. It was proposed initially that the minimum paid-up capital requirement in such companies will be Rs 50 lakh and the minimum turnover of Rs 2 crores. Therefore, as per the latest amendment in Companies Act, 2013 the definition of Small Company is as follows: paid up share capital of not more than 50 lakhs or such higher amount as may be prescribed which shall not be more than 10 crores; AND annual turnover of not more than 2 crores or such higher amount as may be prescribed which shall not be more than 100 crores. here to become a small company both the conditions are required to be fulfilled.

2.3 ADVANTAGE AND DISADVANTAGES OF PUBLIC AND PRIVATE COMPANY

Advantages and Disadvantages of Private Company:

A Private Limited Company is a company which held privately by small businesses enterprises. The liability of the members of a Private Limited Company is limited to the number of shares respectively held by them. Shares of such companies are not publicly traded Shares of Private Limited Company cannot be publicly traded.

1. Separate Legal Entity:

A Private Limited Company is a separate legal identity in the court of the law, meaning assets and liabilities of the business are not the same as the assets and liabilities of the Directors. Both are different form each other.

2. Limited Liability:

If the company undergoes financial crises because of any reasons, the personal assets of members will not be liable for payment of the debts of the company as the liability of members of the companies are limited.

3. Easy formation:

A Private Limited Company can be formed and registered easily, It does not requires cumbersome procedures of formation. Secondly no need to wait for certificate of commencement of business.

4. Transferability of shares:

Shares of a company limited by shares are transferable by a shareholder to any other person if articles permit, without taking any permission or authorization from any of the higher authority.

5. Existence is uninterrupted:

As companies are featured with Perpetual Succession, means company never dies, which is continued existence until it is dissolved legally . A company, being a separate legal person, is unaffected by the death or other departure of any member but continues to be in existence irrespective of the changes in membership. 'Perpetual Succession' is one of the most important characteristics of a company.

Disadvantages of a Private Limited Company:

1. There is a restricts to transferability of shares by its Articles:

Articles of Association is the internal rules and regulations of the company which restricts the transferability of the shares if no provisions are in this regard.

2. Restriction on maximum number of memberships:

Companies Act 2013 provides that in any case number of members should not increase exceed 200. This leads to less financial liquidity.

3. It cannot issue prospectus to the public:

Private companies cannot issue prospectus to the public and hence it cannot use public money. Private companies are raising the capital by their internal sources.

Advantages and Disadvantages of Public Company:

Advantages:

Public Company Registration is done under the Companies Act, 2013. The registration of Public Company is subject to strict compliances. Further, such companies are required to have huge capital investment, Companies intend to have huge capital investment it can go for Public Company Registration.

1. Limited Liability of the members:

In Public Company the liability of the shareholder and Directors is limited to the extent of the shares they hold in the company or they can be called for any unpaid shares. **For example**, if the company suffers from any financial irregularities because of primary business activity, then in such case personal properties of shareholders and Directors will not be liable by the Banks, creditors, and government**.**

2. Separate Legal Entity:

Members of the company, Directors may come and go, but the existence of the company continues to exist. i.e., the absence or movement of any shareholder in the company will not affect the existence of the company.

3. Unlimited source of raising fund:

Public Company has a great advantage of an unlimited source of raising fund through Public which results in carrying out new projects and for getting the new market.

1. Easy Transferability

There is an easy transferability of share in Public Company. Shares of the company are listed on a stock exchange; the shareholders find it is easy to transfer the share in the company.

Disadvantages:

1. Difficult Legal Requirements and High cost of formation:

Setting up and maintaining a public company is much more difficult than setting up and maintaining a private company. Public Companies are subject to many legal requirements that do not apply to private corporations. Further the registering the company as a Public Company requires a huge cost. To come up with the formation of a public company huge investment, time and procedural things are required to be complied with. The returns of the company relied upon the investment you have done.

2. Increased Governmental Interference:

Public Companies are subject to a high level of government interference that does not apply to private companies held. Such interference has increased over the last 15 years in the wake of the many public corporations mismanagements that caused harm to people at large. The government intervention, though often required, slow down and decrease the flexibility of the operations of public companies.

3. Lack of secrecy:

To maintain the transparency and trust of the shareholders, the company provides full disclosure to the public due to which secrecy cannot be

maintained. The Public is involved in decision making, the company cannot maintain the secrecy.

2.4 DIFFERENCE BETWEEN PUBLIC COMPANY AND PRIVATE COMPANY

Criteria	Public Company	Private Company
Meaning:	The public company refers to a company that is listed on a recognized stock exchange.	A private company is one that is not listed on a stock exchange and its securities are restricted or held privately by its members only
Name:	A public company need not affix the word "private"	private company, it is mandatory to affix the words "private limited" at the end of its name
Number of Members:	There must be minimum seven members to start with a public company and no maximum number of members restricted.	Private company can be started with a minimum of two members. Private companies can have a maximum of 200 members.
Transfer of Shares	The shares of a public company are freely transferable.	The shares of a private company are not freely transferable. Transferability is allowed subject to the provisions in the Articles of Association.
Issue of Prospectus	Public Company issues the Prospectus for public subscription.	A Private Company is restricted from issuance of prospectus as these companies cannot invite public for subscription.
Statutory Meeting	Compulsory to hold statutory meeting to obtain the certificate of commencement	Not required to hold statutory meeting.
Place of Holding AGM	Annual General Meeting can be held at the registered office or any other place where the registered office is situated	Place of Holding AGM

2.5 [1]CONVERSION OF PRIVATE COMPANY INTO PUBLIC COMPANY

Most of the business concern most of the time preferred for formation of Private Limited Company because the advantages and special privileges offered by it. Such companies don't issue the prospectus and invites from the near and dear and close friends of the directors and other members Capital is sourced Therefore, the Companies Act, 2013 does not impose stringent rules and regulations as those imposed on Public limited companies. In certain circumstances, a private limited would become a public company.

In the following circumstances a Private Limited Company can becomes a Public Limited Company

1. Conversion by default
2. Conversion by operation of law
3. Conversion by choice or by option

Once a private company becomes a public company under any of the above-mentioned circumstances, it would lose the privileges it enjoyed as a private company. On conversion, the rules and regulations applicable to public limited companies would become applicable.

1. Conversion by default:

A private company prohibits the right to transfer shares. There is a limit of the maximum number of members to 200 and prohibits invitation to the public for subscription of shares or debentures. In violation of any of these conditions laid down Private Company would become a public Company by default.

2. Conversion by operation of law:

In the following cases, a private company becomes a public company by the operation of law: When not less than 25% of the paid-up share capital of a private company is held by one or more public companies,

a. When the average total turnover of the private company is not less than Rs.25 crores for three consecutive years,
b. When the private company holds not less than 25% of the paid up share capital of a public company.
c. When the private company invites, accepts or renews deposits from the public.

[1] https://accountlearning.com/under-what-circumstances-a-pvt-company-be-converted-to-public-company/

The Companies Amendment Act 2000 has given an option to these companies, either to continue as public limited companies or convert themselves into private limited companies by making the necessary changes in their articles.

3. Conversion by Choice or Option:

A private company out of its own free will can choose to convert itself into a public company. Generally, when private companies plan to expand and require more capital resources, they would convert themselves into public companies.

By becoming public companies, they can issue shares or debentures to the public and get the required amount of capital. In India, many organizations which commenced operations as private companies have got themselves converted into public limited companies in order to expand and diversify.

Any private company which desires to get converted into a public company should make the necessary changes in the Articles and follow the below mentioned steps:

a. It should convene a general meeting and pass a special resolution duly altering the Articles.

b. The copy of the resolution along with the amended Articles should be filed with the Registrar within 30 days of passing the special resolution.

c. The number of members should be increased to seven.

d. The company has to apply to the Registrar for obtaining a fresh certificate of incorporation with the words 'Private' deleted from its name.

2.6 SUMMARY

Modes of formation. On the basis of liability of members. Allowed number of members Management Control. Miscellaneous Category.

i. Types of Companies: A. Statutory Company ,Chartered Company, Registered Company . Chartered Companies: Registered Companies: Companies limited by shares, Companies limited by guarantee, Unlimited companies. Companies limited by guarantee, Private Company, Public Company, One Person Company, Holding and Subsidiary Companies, Associate Companies, Government Company, Foreign Companies, Dormant Companies.

Advantages and disadvantages of private company:

I **Separate Legal Entity. Easy formation**: Transferability of shares. Existence is uninterrupted.

1. There is a restricts to transferability of shares by its Articles. Restriction on maximum number of memberships: It cannot issue prospectus to the public:

Advantages and Disadvantages of Public Company:

I Limited Liability of the members, Separate Legal Entity, Unlimited source of raising fund.

II Difficult Legal Requirements and High cost of formation: Increased Governmental, Interference: Lack of secrecy

2.7 QUESTIONS

1. What are the types of Company?
2. What is the procedure for converting public company into private company?
3. What is the procedure for converting private company into public company?
4. Distinguish Between Public Company and Private Company
5. Define the following terms:

a. Chartered Company

b. Private Company

c. Public Company

d. One man Company

e. Holding Company

f. Subsidiary Company

*****

3

MEMORANDUM OF ASSOCIATION AND ARTICLES OF ASSOCIATION - II

Unit Structure

3.0 OBJECTIVES

After studying the unit, the students will be able to:

- Understand the Meaning of Memorandum of Association and Articles of Association and their contents.
- Understand the Doctrine of Ultra Vires, Constructive Notice and Indoor Management
- Understand the Distinction between Memorandum of Association and Articles of Association.
- Understand the Provisions for Alteration of Memorandum of Association and Articles of Association.

3.1 INTRODUCTION

Memorandum of Association is the fundamental and most important document as to the formation of the company. A company is formed where number of members come together for achieving a specific purpose. This objective is usually commercial in nature. Companies are generally formed to earn profit from business activities. To incorporate a company, an application has to be filed with the Registrar of Companies (ROC). This application is required to be submitted with a number of documents. One of the fundamental documents that are required to be submitted with the application for incorporation is the Memorandum of Association.

3.2 DEFINITION AND MEANING

As per Section 2(56) of the Companies Act,2013 "memorandum" means the memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this Act. Memorandum Of Association: Section 4 of the Companies Act, 2013 deals with MOA.

A Memorandum of Association (MOA) represents the charter of the company. It is a legal document prepared during the formation and registration process of a company to define its relationship with shareholders and it specifies the objectives for which the company has been formed.

3.3 CLAUSES UNDER MEMORANDUM OF ASSOCIATION

Memorandum of every company shall state:

1. Name of the company with "Limited" as the last word of the name in case of a public company and "Private Limited" in case of a private company.
2. Registered office of the Company
3. Objects of the Company
4. Liability of the members
5. Details of Share Capital of the Company
6. Subscription or Association Clause.

1. Name Clause:

The name gives a personal existence; therefore, every company must have its own name. Company is a legal person possessing a separate identity; it must have a name with which it can be identified. Promoters of the Company have to make an application to the Registrar of Companies for the availability. The company can adopt any name if:

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

ii. The name should not be considered undesirable and prohibited by the Central Government. A name which misrepresents the public is prohibited by the Government under the Emblems & Name (Prevention of Improper Use) Act,1950, for example, Indian National Flag, name and pictorial representation of

Mahatma Gandhi and the Prime minister of India, name and emblems of the U.N.O., and W.H.O., the official seal and Emblems of the Central Government and State Governments.

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 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. The Central Government, before deeming a name as undesirable, may consult the Registrar of Trade Marks.

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

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

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

b. If the liability of the members is limited the words "Limited" or" Private Limited" as the case may be, shall be added to the name

c. The name and address of the registered office shall be mentioned in all letter-heads, business letters, notices and Common Seal of the Company.

d. However, the Central Government has the power to grant a license to a company to drop the word "limited" from its name. The license is granted if:

i. The company is formed for the promotion of commerce, art, religion, science, charity or any other useful object, and

ii. The company intends to apply its income, if any, in promoting its objects and prohibits the payment of dividends to its members.

Alteration of Name Clause:

Section 13 of the Companies Act, 2013 associated with change of name which states that.

- The name of the company can be changed by a passing a special resolution and with the approval of the Central Government. Approval of Central Government is not required if the change relates to the addition/deletion of the words "private" to the name.

- Sub Section- 2 of Section 4 of the Companies Act, 2013 provides further that "no company shall be registered by name which: Is identical with or resemble too nearly to the name of an existing company registered under this Act or any previous company law

Alteration of Name shall not allow to following Companies:

- Company who has not filed annual returns or financial statements due for filing with the Registrar or
- Companies who has failed to pay or repay matured deposits or debentures or interest thereon

On the alteration of the name of the company, the Registrar must enter the new name of the company in the register and issue a fresh certificate of incorporation. Change of name becomes effective only on the issue of the new certificate

Alteration of name does not, in any way, affect the rights and obligation of the company.

2. Registered Office Clause:

The memorandum of Association must contain the name of state in which the registered office of the company is to be situated. Every company must have registered office. The company shall from the date on which it commences its business or[2] within thirty days of incorporation, whichever is earlier, have a registered office. Intimation should be given to Registrar within thirty days of incorporation. All communication and notices are to be sent to its registered office. All the important documents and books of the company such as the Registrar of Members, Minutes and book are kept at the registered office.

Where the securities are held in a depository, the records of the beneficial ownerships may be served by such depository on the company by means of electronic mode or by delivery of floppies or disk.

Alteration of Registered Office Clause:

a) Registered office if shifts from one place to another within the same city, town, or village it can be made by passing a resolution by Board of directors.

b) Where registered office shifts from one place to another within the same state and is within the same office of Registrar of Companies it could be done by passing a special resolution at the shareholders meeting. Even if the change is within the state it may fall within the jurisdiction of another Registrar of Companies, in which the change shall not be effective unless approved by Regional Director. Intimation of the change is to be filed with the Registrar within 30 days of the change.

c) But, shifting of registered office from one state to another state involves alteration of memorandum itself.

[1] Proposed amendment under companies (Amendment Bill 2016 S. 12 (1) for the words " on and from the fifteenth day of its incorporation " the words, " within thirty days of its incorporation" can be substituted.

The alteration comes into force only when it is registered with the Registrar of Companies of both the States i.e. the State in which the registered office was originally situated and the state to which the office is being situated.

A change in the registered office of the company is permitted from one state to another on the following grounds: Substantive Limits:

i) To enable the company to carry on business more economically or more efficiently

ii) To attain its main purpose by new or improved means (E.g. by new scientific discoveries); or

iii) To enlarge or change the local area of its operations; or

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

v) To restrict or abandon any of the objects specified in the memorandum; or

vi) To sell or dispose of the whole, or any part of the undertaking, or of any of the undertakings of the company; or

vii) To amalgamate with any other company or body of persons.

3. Object Clause:

The third clause in the memorandum states the object which the company, on its incorporation will pursue. The objects clause, also called the objective clause, is considered the most important in the MOA. It defines and limits the scope of the company's operations. It details the company's scope of activity for the members and explains how the members' capital will be used.

The object clause explained why the company has come into in existence. Companies aren't lawfully permitted to do any kind of business other than the kind of business that is specifically stated in the object clause of MOA. An object clause should contain:

- A list of the main objects the company will be pursuing after it's Incorporation
- Incidental objects or the relative objects that are necessary to achieve the main object
- Any other objects that which are not included in the main objects or incidental object
- Nothing that's against the public interest and nothing that's against the country's general rule of law

The object clause to be divided into:

i) Main objects of the company to be pursued by company on its incorporation

ii) Objects incidental or ancillary to the attainment of the main objects; and

iii) Other objects

Alteration of Object Clause:

The procedure for alteration of the Object clause is the same as the alteration of registered office from one state to another.

4. Liability clause:

The liability of the members is limited to the extent of the shares subscribed by the members if the company is formed with share capital or to the extent of the guarantee given by the members if the company is formed with guarantee. In the absence of this clause it is deemed that liability of its members is unlimited.

Alteration of liability clause:

The liability of the members cannot be altered so as to increase the liability of the members, or prejudice their interests. The alteration can be affected only with the consent of the members in writing, either before or after a particular alteration is made by passing a special resolution and to file **form No.MGT 14**.

5. Capital Clause:

In case of a company having share capital unless the company is an unlimited company, memorandum shall also state the amount of share capital with which the company is to be registered and division thereof into shares of a fixed amount.

Alteration of Capital Clause:

The capital can be increased by passing a ordinary resolution in the general body meeting and shall not require to be confirmed by the court. It should be noted that cancellation of shares shall not be deemed to be a reduction of share capital. A notice of alteration of capital must be filed with the registrar within 30 days of such alterations.

6. Subscription or Association Clause:

It is a declaration made by the subscribers who have signed the memorandum of their intention to form a company. The signature of the subscribers shall be attested by at least one witness.

3.4 DOCTRINE OF ULTRA VIRES

Object Clause is the heart of Memorandum of Association of the company. It lays down the objectives which the company has to observe on incorporation of the company under this Act. It is expected that the company must observe and work within the object set by the object clause under MOA. If the company acts beyond the objective set such act is termed as an Ultra Vires and nether Board or any highest authority can justify or confirm such act as, it is void ab initio in nature.

Anything that a company does which is beyond the scope of the object clause is called ultra vires the object clause and is null and void. Since the Act is void it cannot be ratified by the shareholders either. When the company does an act in furtherance of its objects, it is intra vires (intra vires means within; and vires means power) the company. But, where the company does an act which is outside the scope of the object clause, it is ultra vires (outside the powers of) the company. This rule was first time laid down by the House of Lords in Ashbury Railway, Wagon Co. v/s Riche (1875), The objects of the Ashbury Company were: -

a. To manufacture and sell railway carriages etc. and

b. To act as mechanical engineers and general contractors.

The directors of the company entered into a contract with Riche to finance the construction of railway line in Belgium. Subsequently, they repudiate the contract, claiming it to be ultra vires the company. Riche brought an action for damages for breach of contract. The House of Lords held that the contract was ultra vires the company and hence null and void.

3.5 EFFECTS OF ULTRA VIRES TRANSACTION

1. Ultra Vires Contracts:

A contract that is ultra vires the company is absolutely null and void. Such a contract cannot become intra vires by reason of estoppels, ratification, acquiescence, delay or lapse of time. The company is not liable on such contract however:

a. If the company has lent money and this lending is ultra vires the company, it can recover the money from the debtors. The debtors would be stopped from contending that the company had no power to lend.

b. If the company has rendered any particular service which is ultra vires, it is entitled to receive the charges for the service rendered.

c. If the property of the company has been delivered to an outsider through an ultra vires act, the company has a right to retrieve its property provided it existing specie or if it can be traced.

2. Ultra Vires Property:

If a company's money has been utilized in acquiring some property and such an act is ultra vires the company, the company is entitled to the ownership of that property. This is because; the property through wrongly acquired represents the capital of the company.

3. Personal Liability of Directors:

If the director of a company makes an ultra vires payment, he becomes personally liable, for that amount, to the company. He can be compelled to refund the money.

4. Breach of Warranty of Authority:

If the directors induce, however innocently, an outsider to contract with the company in a matter that is ultra vires the company the directors shall be personally liable to the outsider for any loss caused to him, provided he has no knowledge of the fact that the act was ultra vires the company.

5. A company is liable for any tort, if the following conditions are fulfilled:

i) The activity, in the course of which the tort has been committed, falls within the scope of the memorandum of association; and

ii) The servant of the company must have committed the tort within the course of his employment

(A tort is a civil wrong, not arising out of a contract, and the remedy for which is damages)

3.6 ARTICLES OF ASSOCIATION

Definition and Meaning:

As per Section 2(5) of the Companies Act,2013 "articles" means the articles of association of a company as originally framed or as altered from time to time or applied in pursuance of any previous company law or of this Act.

Articles of association is a document containing rules and regulation for the administration of the company. The following companies are required to file with the Registrar, their articles along with the memorandum:

a. Unlimited companies

b. Companies limited by guarantee; and

c. Private companies limited by shares

In case of public company limited by shares, articles of association may be submitted along with the Memorandum of Association. But in other case namely unlimited company, company limited by guarantee and private

company limited by shares, articles of association must be submitted along with the memorandum of association.

Schedule I of the Act sets out several tables containing model forms of articles applicable to different companies. The model set out in Table A applies to a public company limited by shares. Thus, if a company limited by shares does not frame its own articles, the form set out in Table A will automatically apply to it.

Contents of Articles of Association:

Articles of a public company limited by shares usually provide for the following rules:

i. Share Capital and alteration thereof

ii. Meetings of company

iii. Rights of shareholders

iv. Accounts & audit

v. Dividends

vi. Indemnity

vii. Winding up

viii. Appointment, remuneration, qualification, powers, etc. of Board of Directors

ix. Share Certificates and warrants

x. Payment, calls, transfer, lien, transmission, forfeiture, etc. of shares

xi. Votes to members

xii. Capitalization of profits.

xiii. Seal

xiv. Adoption to preliminary contracts

Alteration of Articles of Association:

A company can, at any time, alter its articles subject to the following conditions or restrictions:

i. Alterations of Articles can be made only by a Special Resolution of the shareholders of the Company to that effect. Even if, the articles prescribe an ordinary resolution for its alteration or even if the members agree.

ii. No alteration of Articles will be allowed, which will violate the provisions of the Companies Act, or any other provisions of general law which may be applicable

iii. No alteration of Articles will be allowed, which will violate the conditions, contained in the Memorandum of Association of the Company.

iv. Alteration must not contain anything illegal.

v. An alteration cannot require a member, or any class of members, to purchase more shares or increase his/their liability without his/their consent in writing

vi. Alteration of certain provision of Articles, such as provisions relating to the number of directors and their remuneration, etc. requires the previous consent of the Central Government.

vii. An alteration must not constitute a fraud on the minority. In other words, an alteration must not affect the interests of the minority shareholders.

viii. An alteration of Articles which has the effect of converting a public company into a private company shall have effect only if the alteration is approved by the Central Government.

ix. Alteration must be made bonafide in the interest of the company as a whole, even though the private interests of some members may be affected.

x. Lastly, Articles of Associations may be altered with retrospective effect.

3.7 DISTINCTION BETWEEN MEMORANDUM AND ARTICLES OF ASSOCIATION

i. The Memorandum is the character of the company which defines its objects and powers. The Articles are bye laws of the company for the internal management of the affairs for achieving the objects set out in the Memorandum

ii. The Memorandum is the supreme document of the company while the Articles are subordinate to the memorandum. In case of inconsistency between the memorandum and articles, the provision of the memorandum will override the provisions of the articles.

iii. The Memorandum of Association should not contain any provision contrary to the Companies Act. The Articles must not include any provisions contrary to Companies Act as well as the Memorandum of Association.

iv. Every company must have its own Memorandum. But a public company limited by shares may or may not have its own Articles. It may adopt Table A of Schedule I of the Act.

v. The Memorandum defines the relationship between the company and the outsiders while the Articles defines the relationship between the company and its members and among the members themselves.

vi. A new company must prepare its Memorandum and file it with the registrar before the registration of the company is affected. But the Articles are not required to be filed for the purpose of registration. The company can adopt Table 'A' if it does not prepare its own Articles.

vii. Any act of the company which is *ultra vires* the Memorandum is wholly void and cannot be ratified, even by the whole body of shareholders. But any act which is ultra vires the Article but intra vires the Memorandum can be ratified by the shareholders by passing a special resolution.

viii. The Memorandum cannot be altered easily. The procedure laid down in the Act must be followed for altering the various clauses of the Memorandum. In some cases the approval of the Central

Government is required. But the alteration of Articles is not difficult. The Articles can be altered by passing a special resolution and the approval of the Central Government is not necessary.

3.8 DOCTRINE OF CONSTRUCTIVE NOTICES

Memorandum and articles of association of a company are public documents. These documents are pre-requisite for registration of a company. These documents are available for public inspection either in the office of the company or in the office of the Registrar of Companies on the payment of fee.

Any person who is dealing with a company is presumed to have read and understood the proper meaning of the documents. Every person, dealing with the company must inspect these documents to ensure whether they are in conformity with the respective provisions. A party cannot take a plea that he was ignorant of what has been stated in memorandum or articles of association.

It comes to the aid of a company vis-à-vis the outsiders. If a person deals with the company, and the transaction is beyond the powers of the company, he cannot enforce it against the company and he shall be personally liable to bear the consequences of such dealings. If a person deals with the company in good faith and the person with whom he is dealing has 'Ostensible authority' to deal on behalf of the company.

The above doctrine is subject to one exception that is, so far as the internal proceedings of the company are concerned the outsiders dealing with the company, can assume that everything has been regularly done. This is known as the "Doctrine of indoor management".

3.9 DOCTRINE OF INDOOR MANAGEMENT / TURQUAND (AND RULE)

The principle of constructive notice operates against the person dealing with the company by protecting the latter against the former. Whereas the doctrine of indoor management protects the outsider against the company.

It is the duty of every person to read the memorandum and Articles of the company, but he is not bound to inquire into the internal affairs of the company whether they are being conducted in accordance with the Articles of the Company. He has a right to assume that internal proceedings and affairs of the company are being regularly carried on in accordance with the rules and regulations. The limitation to doctrine of constructive notice is called 'indoor management'

The directors of a company (Royal British Bank), borrowed a sum of money from Turquand and issued a bond to him. The articles of the company provided that the directors might borrow on bonds such sums, as may, from time to time, be expressly authorized by resolutions of shareholders. The shareholders claimed that there had been no such resolution authorizing the loan.

The company was held bound by the loan because Turquand, the plaintiff, had the right to assume that the necessary resolution must have been passed.

Exception to the Rule of Indoor management:

The doctrine of indoor management is subject to five exceptions:

a) Knowledge of internal irregularities of the company:

Where the third person dealing with the company has actual or constructive notice regarding the non-compliance and irregularity of the internal procedure prescribed by the articles of association, they cannot claim protection under this rule.

b) Suspicion of irregularity:

The doctrine also does not apply when the circumstances are so suspicious that an inquiry is invited by the person dealing with the company.

c) Acts void ab initio:

This doctrine does not apply to acts that are void ab initio. Eg:.Where the documents is a forged one.

d) Acts, outside the apparent authority of the company:

Where the acts of an officer do not fall within the apparent authority of such an officer, the contract is not binding on the company.

e) No knowledge of articles:

A person who at the time of entering into a contract with a company, has no knowledge of the company's articles of association, cannot be saved or protected by the doctrine.

3.10 SUMMARY

Clauses under Memorandum of Association

Name Clause, Registered Office Clause, Object Clause: Liability clause: Capital Clause: Subscription Clause.

Effects of Ultra Vires Contracts: Ultra Vires Property: Personal Liability of Directors: Breach of Warranty of Authority: A company is liable for any tort, -

Contents of Articles of Association: Meetings of company, Rights of shareholders, Accounts & audit, Dividends, Indemnity, Winding up procedures etc.

Exception to the Rule of Indoor management: Knowledge of internal irregularities of the company: Suspicion of irregularity: Acts void ab initio: Acts, outside the apparent authority of the company: No knowledge of articles:

3.11 QUESTIONS

1. What are articles of association? Compare the relation of the articles to memorandum of association.

2. Answer the following

a. To what extent and how are the articles of association amended.

b. What is the binding force of memorandum and articles of association?

3. Discuss fully the Doctrine of Indoor Management.

4. Critically examine the principle of the Constructive notice.

5. Examine the Effects of Doctrine of Constructive Notice and Indoor Management

3. Define the following terms:

a. Memorandum of association

b. Articles of Association

c. Doctrine of Ultra vires

*****

4

PROSPECTUS AND PRIVATE PLACEMENT (SECTIONS. 2.23, 26 TO 32 AND S. 42)

Unit Structure

4.0 OBJECTIVES

After studying the unit students will be able to:

- Define the various terms like prospectus, statement in lieu of prospectus and Shelf prospectus.
- Explain the contents of Prospectus.
- Discuss about the legal requirements of prospectus.
- Explain the liabilities against misstatement and how to defence against this liability.

4.1 INTRODUCTION

Chapter III of the Act deals with "Prospectus and allotment of securities", the chapter is divided into two parts, Part I deals with Public Offer and Part II deals with Private Placement. Section 23 of the Act provides that a company whether public or private may issue securities. A public company may issue securities:

a) To public through prospectus ("public offer") by complying with the provisions of Part I of Chapter III of the Act; or

b) Through private placement by complying with the provisions of Part II of Chapter III of the Act; or

c) Through a rights issue or a bonus issue in accordance with the provisions of this Act and in case of a listed company or a company which intends to get its securities listed also with the provisions of the SEBI Act, 1992 and the rules and regulations made thereunder.

For a private company the section provides that a private company may issue securities (a) by way of rights issue or bonus issue in accordance with the provisions of this Act; or

The section deals with issue of securities, which is a wider term not restricted to equity, preference or debentures. Securities has been defined under section 2(81) to mean the securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956.

The relevant section says that securities include:

Shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

a) Derivative;

b) Units or any other investments issued by any collective investment scheme to the investors in such schemes;

c) Government securities;

d) Such other instruments as may be declared by the Central

e) Government to be securities; and

f) Rights or interest in securities.

PROSPECTUS:

"Prospectus means any document described or issued as a prospectus and includes any notice, circular, advertisement or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of any shares in, or debentures of a body corporate"

Definition of prospectus includes any invitation to the public to subscribe to shares or debentures. A document by which an invitation is issued to the public to take shares or debentures of the company is called a prospectus. Prospectus is thus a document described or issued as a prospectus. Even inviting offers from the public for subscription to shares or debentures is a prospectus.

4.2 TYPES OF PROSPECTUS

Abridged Prospectus: [S. 2(1)]:

Section 2(1) of the Indian Companies Act, 2013 described an abridged prospectus as a memorandum that has all the salient features of the prospectus as specified by the SEBI.

It is a summary of a prospectus filed before the registrar of the companies. It includes all the features of a prospectus. An abridged prospectus has all the information of the prospectus in short form so that it should be easy

and quick for an investor to know all the useful information in short and to arrive at the investment decision.

There is a provision under section 33(1) of the Companies Act, 2013 that when any form for the purchase of securities of a company is issued, it must be accompanied by an abridged prospectus.

Deemed Prospectus [S. 25(1)]:

A deemed prospectus has been stated under section 25(1) of the Companies Act, 2013. When any company to offer securities for sale to the public, allots or agrees to allot securities, the document will be considered as a deemed prospectus through which the offer is made to the public for sale. The document is deemed to be a prospectus of a company for all purposes and all the provision of content and liabilities of a prospectus will be applied upon it.

Red Herring Prospectus: – [**S.32]:**

Red herring prospectus does not contain all information about the prices of securities offered and the number of securities to be issued. According to the act, the firm should issue this prospectus to the registrar at least three before the opening of the offer and subscription list.

Shelf prospectus – [**S.31]:**

Shelf prospectus is described under section 31 of the Companies Act, 2013. Shelf prospectus is issued when a company or any public financial institution offers one or more securities to the public. The validity period of such prospectus will be not more than 1 year. The validity period starts with the commencement of the first offer. There is no need for a prospectus on further offers. The organization must provide an information memorandum when filing the shelf prospectus

4.3 CONTENTS OF THE PROSPECTUS

For filing and issuing the prospectus of a public company, it must be signed and dated and contain all the necessary information as stated under section 26 of the Companies Act,2013:

- Name and registered address of the office, its secretary, auditor, legal advisor, bankers, trustees, etc.
- Date of the opening and closing of the issue.
- Statements of the Board of Directors about separate bank accounts where receipts of issues are to be kept.
- Statement of the Board of Directors about the details of utilization and non-utilization of receipts of previous issues.
- Consent of the directors, auditors, bankers to the issue, expert opinions.

- Authority for the issue and details of the resolution passed for it.
- Procedure and time scheduled for the allotment and issue of securities.
- The capital structure of the company in the manner which may be prescribed.
- The objective of a public offer.
- The location of the business and its objectives
- Particulars related to risk factors of the specific project, gestation period of the project, any pending legal action and other important details related to the project.
- The details of the acts of material frauds committed against the company in the last five years, if any
- The related party transactions entered during the last five financial years immediately preceding the issue of prospectus.
- Minimum subscription and what amount are payable on the premium.
- Details of directors, their remuneration and extent of their interest in the company.
- The aggregate amount proposed to be raised through all the stages of offers of specified securities made through the shelf prospectus,
- Reports for the purpose of financial information such as auditor's report, report of profit and loss of the five financial years, business and transaction reports, statement of compliance with the provisions of the Act and any other report.

4.4 MISSTATEMENT IN THE PROSPECTUS

Every person authorizing the issue of prospectus has a primary responsibility to see that the prospectus contains the true states of affairs of the company and does not give any fraudulent picture of the public. People invest in the company on the basis of information published in the prospectus. They have to be safe guarded against all wrong or false statement in prospectus. Prospectus must therefore make full and honest declaration of material facts without concealing or omitting any relevant fact. This is known as the golden rule for framing prospectus. The true nature of companies venture should be disclosed. The statement which does not qualify to the particulars mentioned in the prospectus, or any information is intentionally and willfully concealed by the director of the company, would be constructed as misstatement. They are in other words, either false or untrue statement in the prospectus or information which ought to have been disclosed is concealed, or omission of any material fact. Statements which produce wrong impression of actual facts would also be constructed as misstatements.

Misstatements includes:

i. Untrue statements

ii. Statements which produce wrong impression

iii. Statement which are misleading

iv. Concealment of material fact

v. Omission of facts

The prospectus must make all statements with absolute accuracy and not state the facts which are not strictly correct. A statement may be false not only because of what it states but also because of what it conceals or omits.

A statement included in prospectus shall be deemed to be untrue if:

i. Statement is misleading in the form and context in which it is included

ii. The omission from prospectus of any matter is calculated to mislead

The prospectus which contains misstatements or misleading statements is called "Misleading Prospectus"

Example:

1. A statement in the prospectus that share capital has been subscribed when it has only been allotted in fully paid shares to the company's contractor. It was held that it is a misstatement in prospectus.

Liability:

The liability may be civil or criminal.

I. CIVIL LIABILITY:

1. Compensation:

The above person shall be liable to pay compensation to every person who subscribes for any shares or debentures for any loss or damage sustained by him by reason of any untrue statement included therein.

2. Damages for deceit or fraud:

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

3. Rescission of the Contract for misrepresentation:

It means avoiding the contract. Any person can apply to the court for rescission of the contract if the statement on which he has taken the shares are false or caused by misrepresentation whether innocent or fraudulent. It must be of material fact and not of law. It should be noted that a person cannot claim rescission of contract on misrepresentation, if he had the means of discovering the truth with ordinary diligence.

4. Liability under general law:

Any person responsible for the issue of prospectus may be held liable under the general law or under the Act for misstatements or fraud.

II. CRIMINAL LIABILIY:

Section 63 of the Companies Act deals with criminal liability for misstatements in prospectus.

Where a prospectus issued, circulated, or distributed includes any statement that is untrue or misleading in any form in which it is included or where any inclusion or omission of any matter is likely to mislead, every person who authorises such issue of the prospectus shall be liable for fraud.

"**Fraud" under Sec. 447** comprises of an act, omission, concealment of any fact with an intent to deceive, gain undue advantage, or to injure the interests of the company, its shareholders, its creditors or any other person. It is not necessary that such an act involve any wrongful profit or wrongful loss. If a person commits abuse of position, then that shall also be considered fraud under this section.

Punishment for mis-statement:

If a person is found to be guilty of the offence of fraud, then that person shall be punished with imprisonment for a term that shall not be less than six months and may extend to ten years. He shall also be liable to fine, which shall not be less than the amount involved in the fraud and may extend to three times the amount involved in the fraud.

If the fraud so committed involves public interest, the term of imprisonment shall not be less than three years.

4.5 LEGAL RQUIREMENTS OF PROSPECTUS

[3]Following are the legal requirements of prospectus:

1. A prospectus is required to be issued only after the incorporation of the company.
2. The prospectus must contain all the particulars, listed in Schedule II to the Companies' Act.
3. The prospectus must be dated.

4. A prospectus must be signed by every person, mentioned therein as a director or a proposed director, or his agent.

5. Every application form for shares, issued by the company, must be accompanied by a copy of the prospectus except (a) application form, issued for bona fide invitation to a person to enter into an underwriting agreement, and (b) application forms, issued to existing members and debenture holders.

6. A statement, relating to the affairs of the company by an expert, may be included in the prospectus.

7. Consent of the expert must be obtained in writing and this fact must be stated in the prospectus.

8. No deposit can be invited without issuing an advertisement in a daily newspaper. The said advertisement must be containing a statement, reflecting the company's financial position issued by the Company and in such a form or in such a manner, as may be prescribed.

9. Before a prospectus is issued, a copy of it must be registered with the registrar of companies.

10. Prospectus shall be issued within 90 days of its registration.

Penalty for Non-Compliance of Section 26:

If a prospectus is issued by non-observance of the provisions of Section 26 of this Act, shall be punishable with fine which shall not be less than Rs. 50,000/- which may extend to Rs. 300,000/- and every person who is knowingly a party to the issue of such prospectus, shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than Rs. 50,000/- and may extend to Rs. 3,00,000/- or both.

4.6 PRIVATE PLACEMENT

Private placement by companies means offering its securities or inviting to subscribe its securities for a select group of persons other than by way of a public issue through a private placement offer letter.

[3] Vipul Publication .Business Law kalaivani venkatesh page no 78-79

Private placement of securities can be made only to select persons or identified persons (as identified by the board of the company). A company making a private placement cannot offer its securities through any public advertisements or utilise any marketing, media, or distribution agents or channels to inform the public about such an offer. If the offer is advertised or marketed, it will be considered a public offer and not a private placement by the company.

Rules for Private Placement:

1. Each Private Placement offer should be previously approved by the shareholders of the company, by a Special Resolution.

2. No fresh offer can be made unless the allotments with respect to any offer or invitation made earlier have been completed or that offer or invitation has been withdrawn or abandoned by the company.

3. All money received under private placement to be made by cheque or demand draft only. In any circumstances no cash can be accepted.

4. Qualified Institutional buyers and employees of the company being offered securities under a scheme of employees' stock option are excluded in calculating the number.

5. Company shall not expected to utilise monies raised through private placement unless allotment is made and the return of allotment is filed with the Registrar.

6. Company should be restricted to from making any advertisement of the offer to public.

7. A company shall issue private placement offer cum application letter only after the relevant special resolution or resolution from the Board has been filed with the Registrar.

8. The value of such offer or invitation per person shall be with an investment size of less than Rs.20,000/-of face value of the securities.

9. The company shall maintain a complete record of private placement offers in Form PAS-5. A copy shall be filed with the Registrar along with the requisite fee within 30 days of circulation of private placement offer letter.

10. Allotment of securities shall be done within 60 days of receipt of the application failing which the application money shall be refunded within 15 days of the expiry of 60 days otherwise interest at the rate of 12% per annum shall be required to be aid from the 60th day.

Procedure for Private Placement:

A private placement shall be made only to a selected group of persons who have been identified by the Board, whose number shall not exceed fifty or such higher number i.e., not more than 200, excluding the qualified institutional buyers and employees of the company being offered securities under a scheme of employees' stock option, in a financial year.

1. A resolution must be passed by the Board of Directors for private placement of securities.

2. Preparation of notice of board meeting along with draft resolution to be passed in the board meeting.

3. A General Body meeting must be convened, where in the proposed offer of securities has been previously approved by the shareholders of the company, by a special resolution, for each of the offers or Invitation.

4. Opening of separate bank account for maintaining subscription money and ensure that money received from only those persons whose name is addressed in form.

5. Open separate bank account for keeping subscription money and ensure that money received from only those persons whose name is addressed in form.

Penalty for Non-Compliance of Private Placement:

A company, its directors and promoters will be liable for a penalty if the company accepts monies or makes an offer in contravention of the Act and Rules. The penalty may extend to the amount involved in the invitation or offer or Rs.2 crore, whichever is lower. The company should also refund all monies to the subscribers within thirty days of the order imposing the penalty.

4.7 SUMMARY

Types of Prospectus: Abridged Prospectus: Deemed Prospectus Red Herring Prospectus: Shelf prospectus

Legal Requirements of the Prospects:

Misstatement in the prospectus: Untrue statements, Statements which produce wrong impression, Statement which are misleading, Concealment of material fact. Omission of facts

Civil Liability for Misstatement in the prospectus Compensation: Damages for deceit or fraud: Rescission of the Contract for misrepresentation:

Rules for Private Placement:

Each Private Placement offer should be previously approved by the shareholders of the company, by a Special Resolution. No fresh offer can be made unless the allotments with respect to any offer or invitation made earlier have been completed or that offer or invitation has been withdrawn or abandoned by the company.

Procedure for Private Placement:

Open separate bank account for keeping subscription money and ensure that money received from only those persons whose name is addressed in form.

Penalty for Non-Compliance of Private Placement