

## Module 3: Companies Act

### 10 Introduction to Companies Act, 2013 - History of Company Acts in India

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#### Introduction

The Companies Act, 2013 forms the foundational legal architecture governing corporate entities in India. It regulates the entire lifecycle of a corporate entity—from initial promotion, incorporation, and capital structuring, to day-to-day operations, governance mechanisms, and eventual corporate liquidation or winding up.

#### Historical Evolution of Corporate Law in India

The history of corporate legislation in India mirrors changes in international trade standards and macroeconomic shifts, shifting from colonial models to contemporary corporate governance frameworks:

- **The Joint Stock Companies Act, 1850:** The first formal enactment establishing corporate registration in India. Based on the British Companies Act of 1844, it recognized companies as distinct entities but lacked the principle of limited liability.
- **The Joint Stock Companies Act, 1857:** Introduced the principle of **Limited Liability** into Indian corporate law for the first time, though it excluded banking and insurance enterprises from this protection.
- **The Companies Act, 1956:** Enacted post-Independence on the recommendations of the *Bhabha Committee*. It established a highly structured framework intended to align corporate operations with national economic priorities. It remained the primary corporate rulebook for over five decades.
- **The Companies Act, 2013:** Formulated following the recommendations of the **Dr. J.J. Irani Committee**. It replaced the 1956 Act to reduce red tape, improve minority shareholder protection, enforce Corporate Social Responsibility (CSR), and align Indian corporate structures with global digital standards.

# 11 Meaning and Definition of Company, Features of Company

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## Meaning and Statutory Definition

Etymologically, "company" is derived from the Latin terms "*com*" (together) and "*panis*" (bread), historically referring to an association of merchants cooperating over common business interests. Statutorily, **Section 2(20)** of the Companies Act, 2013 defines a company as: **"A company incorporated under this Act or under any previous company law."**

## Salient Legal Features of a Company

A corporation features several distinct legal characteristics that differentiate it from other business structures like sole proprietorships and partnerships:

- **1. Separate Legal Entity:** Upon incorporation, a company becomes a distinct legal persona independent of its individual shareholders or directors. It can hold property, open bank accounts, incur debts, and enter into contracts under its own name. \*(Landmark Case: Salomon v. A. Salomon & Co. Ltd.)\*
- **2. Perpetual Succession:** The existence of a company is not tied to the life, sanity, or solvency of its members. The membership may change continuously, but the legal entity endures until officially dissolved via statutory liquidation. As the phrase goes: *"Members may come and members may go, but the company goes on forever."*
- **3. Limited Liability:** The personal liability of shareholders is limited to any unpaid amount on the shares held by them. If a member's shares are fully paid up, their personal assets cannot be attached to satisfy corporate debts.
- **4. Artificial Legal Person:** It is created through a legal process and is recognized as an artificial person possessing legal rights, duties, and capacities, though it operates exclusively through human agents (Directors).
- **5. Separate Property:** Corporate assets belong to the company as a distinct entity, not to individual shareholders. A member has no direct insurable interest or proprietary claim over the company's land or inventory. \*(Macaura v. Northern Assurance Co. Ltd.)\*
- **6. Capacity to Sue and Be Sued:** As a legal person, the company can initiate civil litigation in its own name to protect its rights and can similarly be sued by third parties for breaches of contract or civil wrongs.

# 12 Kinds of Companies

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The Companies Act, 2013 classifies corporate entities based on liability, membership limits, control structures, and public accountability metrics.

## Core Categories of Corporate Entities

- **Public Company (Section 2(71)):** A company that is not private, features a minimum of 7 members, has no upper limit on membership, and allows unrestricted transfer of shares to the general public.
- **Private Company (Section 2(68)):** A company whose articles explicitly restrict the right to transfer shares, caps its maximum membership at **200 members** (excluding current/former employees), and strictly prohibits any public invitation to subscribe to its securities.
- **One Person Company (OPC) (Section 2(62)):** A private company structured with only **one individual member** as its founder. It provides sole proprietors with the benefits of corporate limited liability while reducing procedural compliance burdens. It requires a designated nominee to ensure business continuity.
- **Small Company (Section 2(85)):** A private company defined by specific financial thresholds: its paid-up share capital does not exceed ₹4 crores (or a higher prescribed amount up to ₹10 crores), and its turnover does not exceed ₹40 crores (or a higher prescribed amount up to ₹100 crores). It is eligible for simplified compliance paths.
- **Associate Company (Section 2(6)):** A company in which another enterprise exercises a **\*\*significant influence\*\***—defined as control of at least 20% of the total voting power or management of business decisions under an agreement—but which is not a direct subsidiary.
- **Dormant Company (Section 455):** Formed for a future project or to hold an asset/intellectual property without carrying out active accounting transactions. It can apply to the Registrar of Companies (ROC) for formal dormant status to preserve its legal identity with minimal compliance overhead.
- **Government Company (Section 2(45)):** Any company in which not less than **51% of the paid-up share capital** is held by the Central Government, any State Government(s), or jointly by central and state authorities. Its financial audits are overseen by the Comptroller and Auditor General (CAG) of India.
- **Producers Company (Part IXA / Section 378A):** Formed by a group of primary producers (farmers, artisans, fishermen) to handle the production, harvesting, procurement, grading, pooling, and marketing of their products. It applies cooperative principles within a corporate structure.

# 13 Lifting of Corporate Veil, Doctrine of Ultra Vires, Doctrine of Indoor Management

## 1. Lifting of the Corporate Veil

The corporate veil is a legal metaphor representing the separate legal personality that separates a company from its individual shareholders and directors. Under normal circumstances, this veil protects members from personal liability for corporate debts.

However, when this privilege is used for fraudulent purposes, tax evasion, or to evade legal obligations, the courts or statutes will look behind the corporate form to hold the individual bad actors directly liable. This is known as **Lifting or Piercing the Corporate Veil**.

### Key Grounds for Lifting the Veil:

- **Protection of Revenue:** Where corporate structures are created solely to evade taxes. \*(Dinshaw Maneckjee Petit Case)\*
- **Prevention of Fraud or Improper Conduct:** When a company is formed to bypass a restrictive contract or execute a scam. \*(Gilford Motor Co. v. Horne)\*
- **Determination of Enemy Character:** During wartime, to ascertain if the controlling minds behind the business belong to an enemy nation. \*(Daimler Co. Ltd. v. Continental Tyre & Rubber Co.)\*

## 2. Doctrine of Ultra Vires

The term "*Ultra Vires*" translates to "**Beyond the Powers.**" In corporate law, it states that a company can only execute activities that fall within the scope defined by the Objects Clause of its Memorandum of Association (MOA).

- **Legal Status:** Any transaction outside the scope of the MOA is completely ultra vires the company and is **\*\*void from the beginning\*\*** (\*void-ab-initio\*). It cannot be ratified or validated later, even if every shareholder votes in its favor. \*(Landmark Case: Ashbury Railway Carriage & Iron Co. v. Riche)\*
- **Purpose:** To protect shareholders by ensuring their capital is not invested in unapproved risks, and to protect creditors by defining the company's authorized line of business.

### 3. Doctrine of Indoor Management (Turquand's Rule)

The Doctrine of Indoor Management operates as a protective shield for external third parties dealing with a company, acting as an exception to the rule of *Constructive Notice* (which assumes outsiders have read the public documents, MOA, and AOA).

**The Core Rule:** Outsiders are bound to read public documents to ensure a transaction aligns with the company's authorized scope, but they are *\*not\** required to investigate the internal private procedures of the company to verify that regular internal approvals were met. They can assume that internal corporate actions are regular and compliant. \*(Landmark Case: Royal British Bank v. Turquand)\*

#### Statutory Exceptions (Where Indoor Management Fails to Protect Outsiders):

- **Knowledge of Irregularity:** If the outsider had actual knowledge that internal procedures were skipped.
- **Suspicion of Irregularity:** Where the nature of the transaction is unusual enough to put a reasonable person on inquiry.
- **Forgery:** The doctrine never applies to transactions built on forged signatures, as forgery is a complete nullity. \*(Ruben v. Great Fingall Consolidated)\*

## 14 Memorandum of Association, Articles of Association, Alteration of Memorandum and Articles of Association, Prospectus

### Memorandum of Association (MOA) vs. Articles of Association (AOA)

The MOA and AOA represent the constitutional framework of a company, defining its external boundaries and internal operations.

Feature	Memorandum of Association (MOA)	Articles of Association (AOA)
<b>Legal Status</b>	The primary constitution of the company; defines its foundational powers and object boundaries.	The secondary by-laws; subordinate to the MOA and contains rules for day-to-day operations.

Feature	Memorandum of Association (MOA)	Articles of Association (AOA)
<b>Core Focus</b>	Defines the company's relationship with the external world and public stakeholders.	Defines the internal relationship between the company, its members, and its directors.
<b>Mandatory Clauses</b>	Contains 6 clauses: Name, Registered Office, Objects, Liability, Capital, and Association.	Contains internal regulations regarding share transfers, dividends, voting, and board meetings.
<b>Ultra Vires Status</b>	Acts outside the MOA are completely void and cannot be ratified.	Acts outside the AOA are irregular but can be ratified by a shareholder vote.

## Alteration of MOA and AOA

Altering these constitutional documents requires adherence to strict corporate procedures to protect stakeholder interests:

- **Altering the MOA:** Requires passing a **Special Resolution** (75% majority vote) in a general meeting. Changing the \*Objects Clause\* requires filing details with the ROC. Shifting the \*Registered Office\* from one state to another requires additional approval from the Regional Director to protect local creditors.
- **Altering the AOA:** Requires a Special Resolution under Section 14. If the alteration converts a public company into a private company, it must also receive formal approval from the Regional Director.

## Prospectus (Section 2(70))

A prospectus is any formal document described or issued as a prospectus, including red herring or shelf prospectuses, notices, circulars, or advertisements that invite offers from the public to subscribe to or purchase the company's securities.

**Legal Liability:** A prospectus must contain accurate facts. Any material misstatement or active concealment can expose directors and promoters to civil liability for damages and criminal liability for fraud under **Section 447**.

## 15 Management of Companies - Directors: Appointment, Removal, Powers, and Duties

### Appointment and Removal of Directors

Directors serve as the primary human agents through whom an artificial corporate person acts. Every public company must have a minimum of 3 directors, private companies a minimum of 2, and an OPC at least 1, with a maximum cap of 15 directors across all types (extendable via special resolution).

- **Appointment (Section 152):** Directors are typically appointed by shareholders in a general meeting via an ordinary resolution. Every director must hold a valid **Director Identification Number (DIN)**. At least one director must be a resident of India (stayed in India for at least 182 days in the financial year).
- **Removal (Section 169):** Shareholders can remove a director before the expiration of their tenure by passing an **Ordinary Resolution**, provided the director is given a reasonable opportunity to be heard (principles of natural justice).

### Types of Directors

#### Independent Director

A non-executive director with zero material or financial interest in the company or its promoters, appointed to ensure neutral, objective oversight.

#### Executive Director

Includes Managing Directors (MD) or Whole-Time Directors (WTD) who handle day-to-day operations as full-time employees.

#### Additional / Alternate

Additional directors are appointed by the Board between AGMs. Alternate directors act in place of a director absent for over 3 months.

## Powers and Duties of Directors

Directors owe strict fiduciary obligations and duties of care to the company as an entity:

- **Statutory Duties (Section 166):** A director must act in good faith to promote the objects of the company, exercise reasonable care, skill, and diligence, avoid conflicts of interest, and ensure they do not achieve any undue gain or assign their office to another.
- **Corporate Powers (Section 179):** The Board is authorized to exercise all such powers as the company is authorized to do, including borrowing funds, investing surplus corporate capital, approving financial statements, and issuing securities. These powers must be exercised via formal resolutions passed at Board meetings.

## Key Managerial Personnel (KMP) (Section 2(51))

KMPs represent the core executive layer responsible for implementing the strategic directives approved by the Board. Under Section 203, specified classes of companies must appoint: a Chief Executive Officer (CEO) or Managing Director, a **Company Secretary (CS)**, and a Chief Financial Officer (CFO).

# 16 Company Secretary: Qualification, Appointment and Duties

## Role of a Company Secretary (CS)

The Company Secretary serves as the primary compliance officer, ensuring that the company follows all statutory legal guidelines, files corporate records accurately, and maintains transparent governance practices.

## Statutory Qualifications

Under the law, an individual cannot be appointed as a Company Secretary unless they satisfy specific educational requirements:

**The Standard:** For any company featuring a paid-up share capital of **₹10 crores or more**, it is mandatory to appoint a whole-time Company Secretary who is a member of the **Institute of Company Secretaries of India (ICSI)**.

## Appointment Protocol

The CS is classified as a Key Managerial Personnel (KMP). Consequently, their appointment must be approved via a formal Board Resolution outlining specific terms, conditions, and remuneration metrics, and the appointment details must be filed with the ROC within 30 days via Form MGT-14/DIR-12.

## Primary Duties of a Company Secretary

The duties of a CS are split between operational compliance and board support functions:

- **1. Statutory Filings:** Ensuring accurate preparation and timely submission of mandatory annual returns, financial disclosures, and share transfer data to the Registrar of Companies (ROC).
- **2. Secretarial Standards Compliance:** Ensuring that all corporate operations align with the Secretarial Standards issued by the ICSI under Section 205.
- **3. Meeting Coordination:** Managing the administration of Board Meetings and Annual General Meetings (AGMs). This includes issuing timely meeting notices, distributing agendas, and drafting the official minutes of the meetings.
- **4. Advisory Role:** Advising the Board of Directors on their legal liabilities, disclosure duties, and changes in corporate legislation to prevent compliance breaches.

End of Module 3 • Companies Act