

# **CA FOUNDATION NOTES PART- 3**

## **The Companies Act, 2013**

### **Other Companies:**

- Government Company
- Foreign Company
- Section 8 Company
- Dormant Company
- Nidhi Company
- Public Financial Institutions (PFIs)

### **1. Government Company [Section 2(45)]:**

Government Company means any company in which not less than 51% of the paid-up share capital is held by –

- (i) the Central Government, or
- (ii) by any State Government or Government, or
- (iii) partly by the Central Government and partly by one or more State Government, and the section includes a company which is a subsidiary company of such a Government Company.

### **2. Foreign Company [Section 2(42)]:**

“Foreign Company” means any company or body corporate incorporated outside India which—

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

### **3. Section 8 Company – Formation of a Company with charitable objects:**

Deals with the companies formed to –

- has in its objects the promotion of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of the environment or any such other object.
- intends to apply its profits, if any, or other income in promoting its objects; and

- intends to prohibit the payment of any dividend to its members.
- **Examples:** FICCI, ASSOCHAM, CII, National Sports Club of India.
- **Power of Central Government to issue a license:**
  - (i) Section 8 allows the Central Government to register such a person or association of persons as a company with limited liability without the addition of words 'Limited' or 'Private Limited' to its name.
  - (ii) On receiving such an application, the Registrar shall register such person or association of persons as a company under this section.
  - (iii) On registration, the company shall enjoy all the privileges of a limited company.
- **Revocation of License:** The Central Government may by order revoke the license of the company where the company -
  - Contravenes any of the conditions of this Section subject to which a license is issued.
  - Violate the objects of the company.
  - Where the affairs of the company are conducted fraudulently.

On revocation, the Registrar shall put the word Limited or Private Limited against the name of the company.

Before revocation, The Central Government must give it a written notice of its intention to revoke the license and opportunity to be heard in this matter.

- **Order of the Central Government:**

When a license is revoked then Central Government may order this company registered under Section 8 to –

1. Amalgamate with another company registered under this section with similar objects
2. Form a single company with such constitution, properties, powers, rights, interest, authorities and privileges and with such liabilities, duties and obligations as may be specified in the order.
3. Company be wound up.

- **Penalty or Punishment in Contravention:**

If the company fails to comply with any of the requirements of this Section, the Company shall be punishable with a fine which shall not be less than ten lakh rupees but which may extend to one crore rupees and the director and every

officer of the company who is in default shall be punishable with a fine which shall not be less than twenty five thousand rupees and can extend upto twenty five lakh rupees.

#### **4. Dormant Company (Section 455):**

Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

Explanation, For the purposes of this section –

- i. "Inactive Company" means a company which has not been carrying on any business or operation or has not made any significant accounting transaction during the last two financial years or has not filed financial statements and annual returns during the last two financial years.
- ii. "Significant Accounting Transaction" means any transaction other than –
  - a. payment of fees by a company to the Registrar.
  - b. payments made by it to fulfil the requirements of this Act or any other law
  - c. allotment of shares to fulfil the requirements of this Act; and
  - d. payments for maintenance of its office and records.

#### **5. Nidhi Company [Section 406(1)]:**

- Nidhi Company is also called the 'Mutual benefit society'.
- These kinds of companies are mostly found in the southern part of the Country.

##### **Objectives of Nidhi Company:**

- To lend and borrow money to the members, for the purpose of their mutual benefits.
- To cultivate the habits of savings among the members.

#### **6. Public Financial Institutions (PFI):**

As per Section 2(72) of the Companies Act 2013, following institutions are considered as PFIs:

- i. The Life Insurance Corporation of India, established under Life Insurance Corporation Act, 1956
- ii. The Infrastructure Development Finance Company Limited
- iii. Specified company referred to in the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002
- iv. Institutions notified by the Central Government under Section 4A(2) of the Companies Act, 1956 so repealed under section 465 of this Act
- v. Such other institution as may be notified by the Central Government in consultation with the Reserve Bank of India:

Provided that no institution shall be so notified unless —

- (A) It has been established or constituted by or under any Central or State Act other than this Act or the previous company law; or
- (B) Not less than fifty-one per cent of the paid-up share capital is held or controlled by the Central Government or by any State Government or Governments or partly by the Central Government and partly by one or more State Governments.

### **Mode of Registration or Incorporation of a Company:**

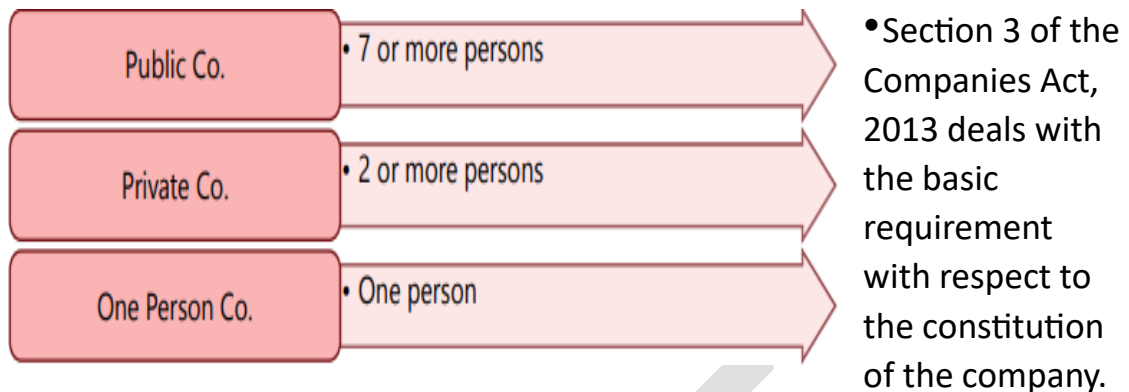
**Promoters:** The Companies Act, 2013 defines the term “Promoter” under section 2(69) which means a person—

- 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.

In simple terms we can say,

- Persons who form the company are known as promoters.
- It is they who conceive the idea of forming the company.
- They take all necessary steps for its registration.
- It should, however, be noted that persons acting only in a professional capacity e.g., the solicitor, banker, accountant etc. are not regarded as promoters.

- **Formation of a Company:** Minimum persons required –



## Incorporation of a Company

Section 7 of the Companies Act, 2013 provides for the procedure to be followed for incorporation of a company.

1. **Filing of the documents and information with the registrar:** For the registration of the company following documents and information are required to be filed with the registrar within whose jurisdiction the registered office of the company is proposed to be situated –
  - the memorandum and articles of the company duly signed by all the subscribers to the memorandum.
  - a declaration by person who is engaged in the formation of the company (an advocate, a chartered accountant, cost accountant or company secretary in practice), and by a person named in the articles (director, manager or secretary of the company), that all the requirements of this Act are duly complied.
  - a declaration from each of the subscribers to the memorandum and from persons named as the first directors, if any, in the articles stating that –
    - he is not convicted of any offence in connection with the promotion, formation or management of any company, or
    - he has not been found guilty of any fraud or misfeasance or of any breach of duty to any company under this Act or any previous company law during the last five years,
    - and that all the documents filed with the Registrar for registration of the company contain information that is correct and complete and true to the best of his knowledge and belief.
  - the address for correspondence till its registered office is established;

- the particulars (names, including surnames or family names, residential address, nationality) of every subscriber to the memorandum along with proof of identity, and in the case of a subscriber being a body corporate, such particulars as may be prescribed.
  - the particulars (names, including surnames or family names, the Director Identification Number, residential address, nationality) of the persons mentioned in the articles as the subscribers to the Memorandum and such other particulars including proof of identity as may be prescribed; and
  - the particulars of the interests of the persons mentioned in the articles as the first directors of the company in other firms or bodies corporate along with their consent to act as directors of the company in such form and manner as may be prescribed.
2. **Issue of certificate of incorporation on registration:** The Registrar on the basis of documents and information filed, shall register all the documents and information in the register and issue a certificate of incorporation in the prescribed form to the effect that the proposed company is incorporated under this Act.
  3. **Allotment of Corporate Identity Number (CIN):** On and from the date mentioned in the certificate of incorporation, the Registrar shall allot to the company a corporate identity number, which shall be a distinct identity for the company and which shall also be included in the certificate.
  4. **Maintenance of copies of all documents and information:** The company shall maintain and preserve at its registered office copies of all documents and information as originally filed, till its dissolution under this Act.
  5. **Furnishing of false or incorrect information or suppression of material fact at the time of incorporation (i.e. at the time of Incorporation):** If any person furnishes any false or incorrect particulars of any information or suppresses any material information, of which he is aware in any of the documents filed with the Registrar in relation to the registration of a company, he shall be liable for action for fraud under section 447.

**6. Company already incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact (i.e. post Incorporation):** Where, at any time after the incorporation of a company, it is proved that the company has been got incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company, or by any fraudulent action, the promoters, the persons named as the first directors of the company and the persons making declaration under this section shall each be liable for action for fraud under section 447.

**7. Order of the Tribunal:** Where a company has been got incorporated by furnishing false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants —

- pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or
- direct that liability of the members shall be unlimited; or
- direct removal of the name of the company from the register of companies; or
- pass an order for the winding up of the company; or
- pass such other orders as it may deem fit:

**Provided that before making any order:**

- the company shall be given a reasonable opportunity of being heard in the matter; and
- the Tribunal shall take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.

## **Effect of Registration:**

Section 9 of the Companies Act, 2013 provides for the effect of registration of a company.

- According to Section 9, from the date of incorporation (mentioned in the certificate of incorporation), the subscribers to the memorandum and all other persons, who may from time to time become members of the company, shall be a body corporate by the name contained in the memorandum.
- Such a registered company shall be capable of exercising all the functions of an incorporated company under this Act and having perpetual succession with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued, by the said name.
- From the date of incorporation mentioned in the certificate, the company becomes a legal person separate from the incorporators; and there comes into existence a binding contract between the company and its members as evidenced by the Memorandum and Articles of Association.
- It has perpetual existence until it is dissolved by liquidation or struck out of the register.
- It may be noted that under the provisions of the Act, a company may purchase shares of another company and thus become a controlling company.

## **Classification of Capital –**

- In relation to a company limited by shares, the word capital means share-capital, i.e., the capital or figure in terms of so many rupees divided into shares of fixed amount.
  - In other words, the contributions of people to the common stock of the company form the capital of the company.
  - The proportion of the capital to which each member is entitled is his share.
  - A share is not a sum of money; it is rather an interest measured by a sum of money and made up of various rights contained in the contract.
- a. Nominal or Registered or Authorized Capital –**
- This form of capital has been defined in section 2(8) of the Companies Act, 2013.



- “Authorized capital” or “Nominal capital” means such capital as is authorized by the memorandum of a company to be the maximum amount of share capital of the company.
- Thus, it is the sum stated in the memorandum as the capital of the company with which it is to be registered being the maximum amount which it is authorized to raise by issuing shares, and upon which it pays stamp duty.

**b. Issued Capital –**

- Section 2(50) of the Companies Act, 2013 defines “issued capital” which means such capital as the company issues from time to time for subscription.
- It is that part of authorized capital which is offered by the company for subscription and includes the shares allotted for consideration other than cash.
- Schedule III to the Companies Act, 2013, makes it obligatory for a company to disclose its issued capital in the balance sheet.

**c. Subscribed Capital –**

- Section 2(86) of the Companies Act, 2013 defines “subscribed capital” as such part of the capital which is for the time being subscribed by the members of a company.
- It is the nominal amount of shares taken up by the public.
- Where any notice, advertisement or other official communication or any business letter, bill head or letter paper of a company states the authorised capital, the subscribed and paid-up capital must also be stated in equally conspicuous characters.
- A default in this regard will make the company and every officer who is in default liable to pay penalty extending Rs 10,000 and Rs 5,000 respectively. [Section 60].

**d. Called-up capital:**

- Section 2(15) of the Companies Act, 2013 defines “called-up capital” as such part of the capital, which has been called for payment.
- It is the total amount called up on the shares issued.

**e. Paid-up capital:**

- Paid-up capital is the total amount paid or credited as paid up on shares issued.
- It is equal to called up capital less calls in arrears.

## Shares –

- Section 2(84) of the Companies Act, 2013 defines the term ‘share’ which means a share in the share capital of a company and includes stock.
- A share thus represents such proportion of the interest of the shareholders as the amount paid up thereon bears to the total capital payable to the company.
- It is a measure of the interest in the company’s assets to which a person holding a share is entitled.
- **Shares are a movable property:** According to section 44 of the Companies Act, 2013, the shares or debentures or other interests of any member in a company shall be movable property transferable in the manner provided by the articles of the company.
- **Shares shall be numbered:** Section 45 provides, every share in a company having a share capital, shall be distinguished by its distinctive number. This implies that every share shall be numbered.  
*However, this shall not apply to a share held by a person whose name is entered as holder of beneficial interest in such share in the records of a depository.*

## Kinds of Share Capital –

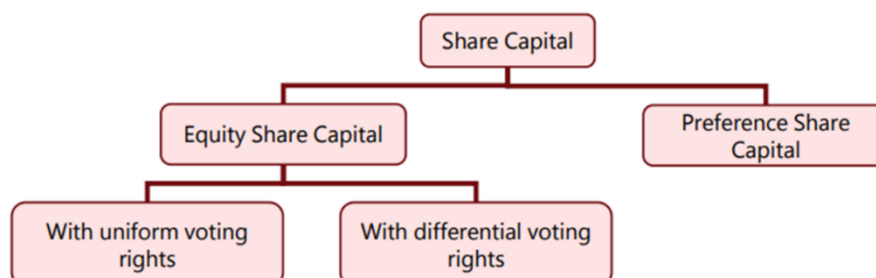
### 1. Equity Share Capital:

Equity share capital is that part of issued share capital which has –

- Voting rights
- Differential rights as to dividend, voting or otherwise in accordance with prescribed rules.

### 2. Preference Share Capital:

With reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to –



- **Payment of Dividend**, either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax.
- **Repayment**, in the case of a winding up or repayment of capital, of the amount of the share capital paid-up or deemed to have been paid-up, whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company.

### **Memorandum of Association –**

- The Memorandum of Association of company is in fact its charter.
- It defines its constitution and the scope of the powers of the company with which it has been established under the Act.

### **Objective of framing MOA:**

- It contains the object for which the company is formed and therefore identifies the possible scope of its operations beyond which its actions cannot go.
- It enables shareholders, creditors and all those who deal with company to know what its powers are and what activities it can engage in.
- A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering a contract with the company is presumed to have the knowledge of the conditions contained therein.
- The shareholders must know the purposes for which his money can be used by the company and what risks he is taking in making the investment.
- ***It cannot enter into a contract or engage in any trade or business, which is beyond the power confessed in it by the memorandum. If it does so, it would be ultra vires the company and void.***

**As per Section 4, Memorandum of a company shall be drawn up in such form as is given in Tables A, B, C, D and E in Schedule I of the Companies Act, 2013.**

- **Table A** is a form for memorandum of association of a company limited by shares.
- **Table B** is a form for memorandum of association of a company limited by guarantee and not having share capital.

- **Table C** is a form for memorandum of association of a company limited by guarantee and having share capital.
- **Table D** is a form for memorandum of association of an unlimited company.
- **Table E** is a form for memorandum of association of an unlimited company and having share capital.

## **Contents of MOA –**

### **a. Name Clause:**

- The name of the company with the last word “Limited” in the case of a public limited company, or the last words “Private Limited” in the case of a private limited company.
- This clause is not applicable on the companies formed under section 8 of the Act.
- The name including phrase ‘Electoral Trust’ may be allowed for Registration of companies to be formed under section 8 of the Act.
- A Government company’s name must end with the word “Limited”.
- In the case of One Person Company, the words “One Person Company”, should be included below its name.

### **b. Registered Office Clause:**

The State in which the registered office of the company is to be situated.

### **c. Object Clause:**

- The objects for which the company is proposed to be incorporated, and any matter considered necessary in furtherance thereof.
- If any company has changed its activities which are not reflected in its name, it shall change its name in line with its activities within a period of six months from the change of activities after complying with all the provisions as applicable to change of name.

### **d. Liability Clause:** The liability of members of the company, whether limited or unlimited, also state –

- In the case of a company limited by shares, that the liability of its members is limited to the amount unpaid, if any, on the shares held by them; and
- In the case of a company limited by guarantee, the amount up to which each member undertakes to contribute.

**e. Capital Clause:**

- The amount of authorized capital divided into share of fixed amounts and the number of shares with the subscribers to the memorandum have agreed to take, indicated opposite their names, which shall not be less than one share.
- A company not having share capital need not have this clause.

**f. Association clause:**

- The detail of the subscribers to be formed into a company. Every subscriber to the Memorandum shall take at least one share, and shall write against his name, the number of shares taken by him.
  - In the case of OPC, the name of the person who, in the event of death of the subscriber, shall become the member of the company.
- The memorandum must be printed, divided into paragraphs, numbered consecutively, and signed by at least seven persons (two in the case of a private company and one in the case of One Person Company) in the presence of at least one witness, who will attest the signatures.
  - The particulars about the signatories to the memorandum as well as the witness, as to their address, description, occupation etc., must also be entered.
  - It is to be noted that a company being a legal person can, through its agent, subscribe to the memorandum.
  - However, a minor cannot be a signatory to the memorandum as he is not competent to contract. The guardian of a minor, who subscribes to the memorandum on his behalf, will be deemed to have subscribed in his personal capacity.

**Doctrine of Ultra Vires –**

- The meaning of the term ultra vires is simply “beyond (their) powers”.
- The legal phrase “ultra vires” is applicable only to acts done in excess of the legal powers of the doers.
- It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act, thus far and no further.
- In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the

company is wholly void and inoperative in law and is therefore not binding on the company.

- The impact of the doctrine of ultra vires is that a company can neither be sued on an ultra vires transaction, nor can it sue on it.
- Since the memorandum is a “public document”, it is open to public inspection. Therefore, when one deals with a company one is deemed to know about the powers of the company. If in spite of this you enter into a transaction which is ultra vires the company, you cannot enforce it against the company.

### **Case Law – Ashbury Railway Carriage and Iron Company Limited v. Riche-(1875).**

The main objects of a company were:

- i. To make, sell or lend on hire, railway carriages and wagons;
  - ii. To carry on the business of mechanical engineers and general contractors.
  - iii. To purchase, lease, sell and work mines.
  - iv. To purchase and sell as merchants or agents, coal, timber, metals etc.
- The business's directors signed a contract with Riche to finance the building of a railway line in Belgium, and the company further approved the directors' action by adopting a special resolution.
  - The company however, repudiated the contract as being ultravires. And Riche brought an action for damages for breach of contract. His contention was that the contract was well within the meaning of the word general contractors and hence within its powers. Moreover, it had been ratified by a majority of shareholders.
  - However, it was held by the Court that the contract was null and void. It said that the terms general contractors were associated with mechanical engineers, i.e. it had to be read in connection with the company's main business.
  - If, the term general contractors was not so interpreted, it would authorize the making of contracts of any kind and every description, for example, marine and fire insurance.

An ultra vires contract can never be made binding on the company. It cannot become “Intravires” by reasons of estoppel, acquiescence, Lapse of time, delay or ratification.

The whole position regarding the doctrine of ultra vires can be summed up as:

- (i) When an act is performed, which though legal in itself, is not authorized by the object clause of the memorandum, or by the statute, it is said to be ultravires the company, and hence null and void.
- (ii) An act which is ultravires, the company cannot be ratified even by the unanimous consent of all the shareholders.
- (iii) An act which is ultravires the directors, but intravires the company can be ratified by the members of the company through a resolution passed at a general meeting.
- (iv) If an act is ultravires the Articles, it can be ratified by altering the Articles by a Special Resolution at a general meeting.

### **Articles of Association –**

- The articles of association of a company are its rules and regulations, which are framed to manage its internal affairs.
- Just as the memorandum contains the fundamental conditions upon which the company is allowed to be incorporated, so also the articles are the internal regulations of the company.
- The articles play a part subsidiary to memorandum of association. They accept the memorandum as the charter of incorporation, and so accepting it the articles proceed to define the duties, the rights and powers of the governing body as between themselves and the company and the mode and form in which the business of the company is to be carried on, and the mode and form in which changes in the internal regulation of the company may from time to time be made.

Section 5 of the Companies Act, 2013 seeks to provide the contents and model of articles of association. The section lays the following law-

1. **Contains regulations:** The articles of a company shall contain the regulations for management of the company.
2. **Inclusion of matters:** The articles shall also contain such matters, as are prescribed under the rules. However, a company may also include such

additional matters in its articles as may be considered necessary for its management.

3. **Contain provisions for entrenchment:** The articles may contain provisions for entrenchment (to protect something) to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.
4. **Manner of inclusion of the entrenchment provision:** The provisions for entrenchment shall only be made either on formation of a company, or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by a special resolution in the case of a public company.
5. **Notice to the registrar of the entrenchment provision:** Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed.
6. **Forms of articles:** The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company.
7. **Model articles:** A company may adopt all or any of the regulations contained in the model articles applicable to such company.
8. **Company registered after the commencement of this Act:** In case of any company, which is registered after the commencement of this Act, in so far as the registered articles of such company do not exclude or modify the regulations contained in the model articles applicable to such company, those regulations shall, so far as applicable, be the regulations of that company in the same manner and to the extent as if they were contained in the duly registered articles of the company.

### **Memorandum of Association Vs Articles of Association:**

1. **Objectives:** Memorandum of Association defines and delimits the objectives of the company whereas the Articles of association lays down the rules and regulations for the internal management of the company.



2. **Relationship:** Memorandum defines the relationship of the company with the outside world and Articles define the relationship between the company and its members.
3. **Alteration:** Memorandum of association can be altered only under certain circumstances and in the manner provided for in the Act. In most cases permission of the Regional Director, or the Tribunal is required. The articles can be altered simply by passing a special resolution.
4. **Ultra Vires:** Acts done by the company beyond the scope of the memorandum are ultra-vires and void. These cannot be ratified even by the unanimous consent of all the shareholders. The acts ultra-vires the articles can be ratified by a special resolution of the shareholders, provided they are not beyond the provisions of the memorandum.

### **Doctrine of Constructive Notice –**

- Section 399 of the Companies Act, 2013 provides that any person can inspect by electronic means any document kept by the Registrar, or make a record of the same, or get a copy or extracts of any document, including certificate of incorporation of any company, on payment of prescribed fees.
- The memorandum and articles of association of a company when registered with Registrar of Companies, become public documents, and they are available for inspection to any person, on the payment of a nominal fees.
- It is therefore, the duty of every person dealing with a company to inspect its documents and make sure that his contract is in conformity with their provisions but whether a person reads them or not, it will be presumed that he knows the contents of the documents.
- This kind of presumed/implied notice is called constructive notice.

### **By Constructive Notice is meant:**

- i. Whether a person reads the documents or not, he is presumed to have knowledge of the contents of the documents.
- ii. Every person dealing with the company not only has the constructive notice of the memorandum and articles, but also of all the other related documents, such as Special Resolutions etc., which are required to be registered with the Registrar.

Thus, if a person enters into a contract which is beyond the powers of the company as defined in the memorandum, or outside the authority of directors as per memorandum or articles, he cannot acquire any rights under the contract against the company.

### **Doctrine of Indoor Management –**

- The Doctrine of Indoor Management is the exception to the doctrine of constructive notice.
- The doctrine of constructive notice does in no sense mean that outsiders are deemed to have notice of the internal affairs of the company.
- For instance, if an act is authorised by the articles or memorandum, an outsider is entitled to assume that all the detailed formalities for doing that act have been observed.

### **Case Law - The Royal British Bank vs. Turquand**

- **FACTS** of the Royal British Bank vs. Turquand Mr. Turquand was the official manager (liquidator) of the insolvent Cameron's Coalbrook Steam, Coal and Swansea and Loughor Railway Company.
- It was incorporated under the Joint Stock Companies Act, 1844. The company had given a bond for £ 2,000 to the Royal British Bank, which secured the company's drawings on its current account.
- The bond was under the company's seal, signed by two directors and the secretary. When the company was sued, it alleged that under its registered deed of settlement (the articles of association), directors only had power to borrow up to an amount authorized by a company resolution.
- A resolution had been passed but not specifying how much the directors could borrow.
- Held, it was decided that the bond was valid, so the Royal British Bank could enforce the terms. He said the bank was deemed to be aware that the directors could borrow only up to the amount resolutions allowed.
- Articles of association were registered with Companies House, so there was constructive notice.
- But the bank could not be deemed to know which ordinary resolutions passed, because these were not registrable.
- The bond was valid because there was no requirement to look into the company's internal workings.

- This is the indoor management rule, that the company's indoor affairs are the company's problem.

The Turquand Rule is inapplicable in the following cases –

**a. Actual or constructive knowledge of irregularity:**

- The rule does not protect any person when the person dealing with the company has notice, whether actual or constructive, of the irregularity.
- In *Howard vs. Patent Ivory Manufacturing Co.* where the directors could not defend the issue of debentures to themselves because they should have known that the extent to which they were lending money to the company required the assent of the general meeting which they had not obtained.
- Likewise, in *Morris v Kanssen*, a director could not defend an allotment of shares to him as he participated in the meeting, which made the allotment. His appointment as a director also fell through because none of the directors appointed him was validly in office.

**b. Suspicion of Irregularity:**

- The doctrine in no way, rewards those who behave negligently. Where the person dealing with the company is put upon an inquiry, for example, where the transaction is unusual or not in the ordinary course of business, it is the duty of the outsider to make the necessary enquiry.
- The protection of the "Turquand Rule" is also not available where the circumstances surrounding the contract are suspicious and therefore invite inquiry.
- Suspicion should arise, for example, from the fact that an officer is purporting to act in matter, which is apparently outside the scope of his authority.

**c. Forgery:**

- The doctrine of indoor management applies only to irregularities which might otherwise affect a transaction but it cannot apply to forgery which must be regarded as nullity.
- Forgery may in circumstances exclude the 'Turquand Rule'. The only clear illustration is found in the *Ruben v Great Fingall Consolidated*.

- In this case the plaintiff was the transferee of a share certificate issued under the seal of the defendant's company.
- The company's secretary, who had affixed the seal of the company and forged the signature of the two directors, issued the certificate.
- The plaintiff contended that whether the signature was genuine or forged was apart of the internal management, and therefore, the company should be estopped from denying genuineness of the document.
- But it was held, that the rule has never been extended to cover such a complete forgery.

DEECE