

# **CA FOUNDATION NOTES**

## **The Companies Act, 2013**

### **Introduction:**

- The Companies Act, 2013 was enacted to consolidate and amend the law relating to the companies. The Companies Act, 2013 was preceded by Companies Act, 1956.
- The Companies Act, 2013 contains 470 sections, 7 schedules and is divided into 29 chapters.

### **Applicability of the Companies Act, 2013:**

- Companies incorporated under this Act or under any previous law.
- Insurance companies (subject to the provisions of the Insurance Act or IRDA Act, 1999).
- Banking companies (subject to the provisions of the Banking Regulation Act, 1949).
- Companies engaged in the generation or supply of electricity, (subject to the provisions of the Electricity Act).
- Any other company governed by any special act for the time being in force,
- Such body corporate, incorporated by any act for the time being in force, as the Central Government may, by notification, specify in this behalf.

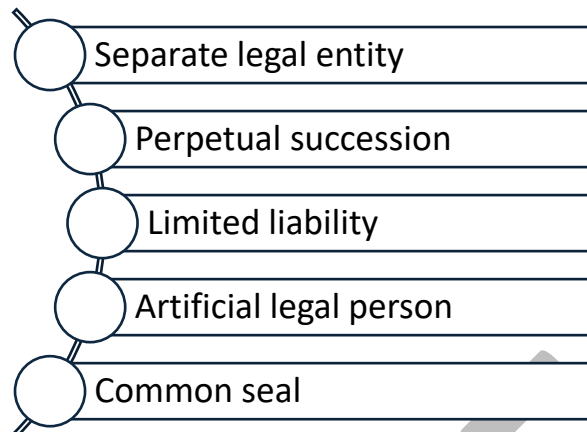
### **Meaning of a Company:**

**Section 2(20)** of the Companies Act, 2013 defines, A company is a company incorporated under this Act or under any previous company law.

**Chief Justice Marshall** – “A corporation is an artificial being, invisible, intangible, existing only in contemplation of the law. Being a mere creation of law, it possesses only the properties which the Charter of its creation confers upon it, either expressly or as incidental to its very existence.”

**Prof. Haney** – “A company is an incorporated association which is an artificial person created by law, having separate entity, with a perpetual succession and common seal.”

## Features of a Company:



### 1. Separate legal entity:

- When a company is registered, it is clothed with a legal personality.
- This feature provides the company with all the rights that a human being of that country enjoys.
- Its existence is distinct and separate from that of its members.
- The company gets the power to sue any company individually, can also acquire property, can open a bank account in their name, also can get loans from banks in their name.
- A company is capable of owning, enjoying, and disposing of property on its own name. Although the capital and assets are contributed by the shareholders, the company becomes the owner of its capital and assets.
- A member does not even have any insurable interest in the property of the company.

- ***Case Law: Macaura Vs. Northern Assurance Co. Ltd (1925)***

Fact of the Case:

- The owner of a timber estate sold the timber to a company in exchange for stock in the company.
- As a result, M (Macaura) was the major shareholder of the timber company and was also its creditor to a large extent.
- He obtained a policy on the timber in his own name. He made a claim for the loss to the insurance company after the fire burned the timber.
- But the insurance company refused to settle the claim.

Issue:

Is the insurance company liable to pay compensation to M for the loss incurred?

Court Judgement:

- Since the timber was not insured under the company's name, the insurance company was found to be exempt from liability towards M.
- The timber belonged to the company, and therefore, only the company could obtain an insurance policy for it.

## 2. Perpetual succession:

- Members may die or change, but the company goes on till it is wound up on the grounds specified by the Act.
- Since a company is an artificial person created by law, law alone can bring an end to its life.
- Its existence is not affected by the death or insolvency of its members.
- Example: There was a company which has 7 members and all of them died in an aircraft. Despite this, the company still exists unlike partnership form of business.

## 3. Limited liability:

The liability of a member depends on the kind of company of which he is a member.

- a. **Limited liability company:** The liability of the members of the company is limited to the extent of the nominal value of the shares held by them.
- b. **Company limited by guarantee:** The members are liable only to the extent of the amount guaranteed by them and that too only when the company goes into liquidation.
- c. **Unlimited company:** The liability of the members is unlimited in the case of an unlimited company.

#### 4. Artificial legal person:

- A company is called an artificial person by law.
- It is also called a legal person because it can enter into a contract, own property in its own name, sue and be sued by others, etc.
- It can do everything which any natural person can do except be sent to jail, take an oath, marry or practice a learned profession.
- Also, it is not human, but it acts through human beings.
- It is called an artificial person because it is invisible, intangible and exists only in the eyes of the law.

#### 5. Common seal:

- Since a company is an artificial person, it cannot act on its own. It acts through its Board of Directors.
- The common seal is the official signature of a company, which is affixed by the officers and employees of the company on its every document.
- The Companies (Amendment) Act 2015 has made it optional for the companies to have a common seal.
- In case a company does not have a common seal, the authorization shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.

#### Corporate Veil:

- The term Corporate Veil refers to a legal concept that members of a company are shielded from liability connected to the company's actions.
- If the company incurs any debts or contravenes any laws, the corporate veil concept implies that members should not be liable for those errors.

#### ***Case law: The case of Salomon v. Salomon and Co. Ltd***

- In Salomon vs. Salomon & Co. Ltd. the House of Lords laid down that a company is a person distinct and separate from its members.
- In this case one Salomon incorporated a company named "Salomon & Co. Ltd.", with seven subscribers consisting of himself, his wife, four sons and one daughter.
- This company took over the personal business assets of Salomon for £ 38,782 and in turn, Salomon took 20,000 shares of £ 1 each, debentures worth £ 10,000 of the company with charge on the company's assets and

the balance in cash. His wife, daughter and four sons took up one of 1 share each.

- Subsequently, the company went into liquidation due to a general trade depression. The unsecured creditors to the tune of f 7,000 contended that Salomon could not be treated as a secured creditor of the company, in respect of the debentures held by him, as he was the managing director of one-man company, which was not different from Salomon and the cloak of the company was a mere sham and fraud.
- This case clearly established that the company has its own existence and as a result, a shareholder cannot be held liable for the acts of the company even though he holds virtually the entire share capital. The whole law of corporation is in fact based on this theory of separate corporate entity.

**Lifting the veil:** It means looking behind the company as a legal person, i.e., disregarding the corporate entity and paying regard, instead, to the realities behind the legal facade. Where the Courts ignore the company and concern themselves directly with the members, the corporate veil is said to be lifted.

**1. To determine the character of the company i.e. to find out whether co-enemy or friend:**

*Daimler co. Ltd v/s Continental Tyre & Rubber co. Ltd.*: It was held that a company will be regarded as having enemy character if the persons having de facto control of company are residents of enemy country or wherever they maybe they are acting on instructions of enemy.

**2. To protect revenue/tax:**

*Dinshaw Maneckjee Petit:*

- The assessee was receiving huge dividend and interest income, and he created three companies to reinvest the income for reducing the tax burden.
- The companies were having no business other than receiving investment and giving back to assessee as a pretended loan.
- It was held that company was not more than the assessee himself and the assessee was held liable to pay the tax.
- The Court decided that the private companies were a sham and corporate veil was lifted to find out the real owner of the income.

**3. To avoid a legal obligation:** Where it was found that the sole purpose for the formation of the company was to use it as a device to reduce the amount to be paid by way of bonus to workmen.

*The Workmen of Associated Rubber Industries Limited vs. The Associated Rubber Industries Ltd.:*

- The facts of the case are that "A Limited" purchased shares of "B Limited" by investing a sum of 450,000.
- The dividend in respect of these shares was shown in the profit and loss account of the company, year after year. It was considered for the purpose of calculating the bonus payable to workmen of the company.
- Sometime in 1968, the company transferred the shares of B Limited to C Limited, a subsidiary, wholly owned by it. Thus, the dividend income did not find place in the Profit & Loss Account of A Ltd., with the result that the surplus available for the purpose for payment of bonus to the workmen got reduced.
- Here a company created a subsidiary and transferred to it, its investment holdings in a bid to reduce its liability to pay bonus to its workers.
- The new company so formed had no assets of its own except those transferred to it by the principal company, with no business or income of its own except receiving dividends from shares transferred to it by the principal company and serving no purpose except to reduce the gross profit of the principal company to reduce the amount paid as bonus to workmen.

**4. Formation of subsidiaries to act as agents:** A company may sometimes be regarded as an agent or trustee of its members, or of another company, and may therefore be deemed to have lost its individuality in favour of its principal. Here the principal will be held liable for the acts of that company.

*Merchandise Transport Limited vs. British Transport Commission (1982):*

- A transport company wanted to obtain licenses for its vehicles but could not do so if applied in its own name.
- It, therefore, formed a subsidiary company, and the application for license was made in the name of the subsidiary.
- The vehicles were to be transferred to the subsidiary company.

- Held, the parent and the subsidiary were one commercial unit and the application for licenses was rejected.

**5. Company formed for fraud/improper conduct or to defeat law:** Where the device of incorporation is adopted for some illegal or improper purpose, e.g., to defeat or circumvent law, to defraud creditors or to avoid legal obligations. [Gilford Motor Co. vs. Horne]

### **Classes of Companies:**

**Private Company [Section 2(68)]:** Private company means a company having a minimum paid-up share capital as may be prescribed, and which by its articles,

- i. restricts the right to transfer its shares.
- ii. except in case of One Person Company, limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member:

Provided further that—

- a. persons who are in the employment of the company; and
- b. persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased, shall not be included in the number of members; and
- iii. prohibits any invitation to the public to subscribe for any securities of the company

### **Important points:**

- no minimum paid up capital required.
- Minimum members 2, maximum members 200. (excluding present and past employees)
- Right to transfer shares restricted.
- Prohibition on invitation to subscribe for shares to the public.
- Small company is a private company.
- OPC can be only formed as private company.

**Small company [Section 2(85)]:** A company other than a public company whose:

- i. Paid up share capital does not exceed 4 crores.
- ii. And annual turnover should not exceed 40 crores.

This clause shall not apply to:

- a. Holding or subsidiary companies
- b. Companies registered under Section 8
- c. A company or a body corporate governed under a special act.

**Public company [Section 2(71)]:** Public company means a company which is –

- i. Not a private company
- ii. Has a minimum paid up share capital as may be prescribed.

Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.

**Important points:**

- Not a private company
- Shares freely transferrable
- No minimum paid up share capital required
- Minimum members 7
- Maximum members – unlimited
- Subsidiary of a public company is deemed to be public company.