**UNIT-I COMPANY**

* 1. **INTRODUCTION**

Company is a form of business ownership which overcome the limitations of all other forms of ownerships like sole trading concern, HUF, Partnership etc. It has emerged from the industrial revolution. Company needs huge capital and it operates in a very large scale. Generally, company means a joint stock company.

Company law is a legislation under which the formation, registration or incorporation, governance, and dissolution of companies is administered and controlled. It includes all business organizations which usually carry on some form of economic or charitable activity. A company is an artificial person with legal recognition. It means the company has separate legal personality. In India law relating to companies is contained in The Companies Act 1956 and 2013.

* + 1. **Definitions of company**

There is no definite and legal meaning of the term company. Some author points out that the term company is derived from the *Latin* word “*companies”,* which means a group of persons who gathered to fulfill their need together. Usually company means an association of persons joint together to attain a common goal social or economic.

***Section 3 (1) (i) of the Companies Act, 1956*** defines a company as “a companyformed and registered under this Act or an existing company”. Section 3(1) (ii) of theact states that “an existing company means a company formed and registered under any of the previous company’s laws”. This definition does not focus on the characteristics of a company.

**Other definitions of the company are**:

***Haney*** defines company as “Joint Stock Company is a voluntary association ofindividuals for profit, having a capital divided into transferable shares. The ownershipof which is the condition of membership”.

***Chief Justice Marshall of USA*** define company as “A company is a person, artificial, invisible, intangible, and existing only in the contemplation of the law. Being a mere creature of law, it possesses only those properties which the character of its creation of its creation confers upon it either expressly or as incidental to its very existence”.

A very comprehensive and clear definition of a company is given by *LordJustice Lindley,* “A company is meant an association of many persons who contributemoney or money’s worth to a common stock and employ it in some trade or business and who share the profit and loss (as the case may be) arising there from. The commonstock contributed is denoted in money and is the capital of the company. The personswho contribute it, or to whom it belongs, are members. The proportion of capital towhich each member is entitled is his share. Shares are always transferable although theright to transfer them is often more or less restricted”.

From the above definitions, it can be concluded that a company is registeredassociation which is an artificial legal person, having an independent legal, entity witha perpetual succession, a common seal for its signatures, a common capital comprisedof transferable shares and carrying limited liability.

Thus a company is a legal entity, allowed by law, which permits a group of people, as shareholders, to create an independent organization, pursuing set of objectives, and empowered with legal rights, such as to sue and be sued, own property, hire employees or loan and borrow money.

* + 1. **Features of Company**

A company has its own features; most of the features can be traced in the definitions mentioned in the above paragraph. The main features of the company are:

1. **Artificial Person**

In the eye of law, a company is a person. It enjoys all the privileges of law.It has the right, to enter into contract with third parties in its own name, to acquire and dispose of the property and can sue and be sued in its own name, it is responsible for its conduct.

However, it is not a natural person, it is an artificial person and it can’t act on its own, it has to operate through its board of directors i.e. management elected by the shareholders. It was observed *in Bates Vs Standard Land Co*. case that, “The board of directors are the brains and the only brains of the company, which is the body and the company can and does act only through them”. Further it is not a citizen as it cannot enjoy the rights under the Constitutionof India or Citizenship Act. It was held in the case of *State Trading Corporation of India Vs C.T.O* (1963 SCJ 705), that neither the provisions of the Constitution nor the Citizenship Act apply to it. Justice Hidayatullah once remarked that if all the members are citizens of India, the company does not become a citizen of India.

1. **Incorporated association**

A company is an incorporated association. It comes into being only after incorporated under The Companies Act of 1956. It exists from the date mentioned in the certificate of incorporation. It may be noted that any type of business must be registered under the Companies Act and if it is not so registered, it is deemed to be an illegal association.

Minimum number of persons required for the purpose of incorporation is seven in case of a public company and two in case of a private company. These persons need to subscribe their names to the Memorandum of association and also comply with other legal requirements of the Act in respect of registration to form and incorporate a company, with or without limited liability [Sec 12 (1)].

1. **Separate Legal Personality**

As a company is an artificial person in the eye of law, it has a separate personality and it is not dependent on its members. Of course it acts through its members i.e. board of directors but it is only responsible for its actions and not the members. This has several important consequences:

1. Company is liable for its liabilities - The shareholders have no obligations towards the liabilities of the company. They are not liable for the debts of the company and cannot be sued by the creditors of the company. Similarly, the company is not in any way liable for the individual debts of its members. However, a shareholder can be a debtor or creditor of the company and he/she can sue or be sued by the company.
2. Company owns Property- acompany has its own property - the shareholders have no direct right to this or any share of it. A shareholder has no legal interest in the company’s property and cannot insure it against theft, damage, etc. The property of the company is to be used for the benefit of the company and nor for the personal benefit of the shareholders.
3. Limited Liability of the members – As the company is distinct from its members, it makes the liability of the members limited. If any Person wishes to cease a membership, he/she is only entitled to whatever price he/she can get for the shares held.
4. Contractual Capacity- A Company has full contractual capacity - and only the company can enforce its contracts. At the same time the members of the company can enter into contracts with the company in the same manner as any other individual can. Further a Companies may also be liable for negligence and shareholder cannot be made liable for the negligence of the company, unless he was personally negligent.
5. Assesse for the purpose of Income Tax – Separate legal entity of the company is also recognized by the Income Tax Act. A company is required to pay Income-tax on its profits. When these profits are distributed to shareholders in the form of dividend, then the shareholders have to pay income-tax on their dividend of income. This proves that a company and its shareholders are two separate entities.
6. Crimes- A company can be convicted for the crime, regardless of whether its directors are also convicted. However, this has some limitations, they are:
7. A company cannot be convicted of a crime which requires the physical act of driving a vehicle: Richmond on Thames Borough Council v Pinn& Wheeler
8. A company cannot be convicted of any crime for which the only available sentence is imprisonment. There are particular problems with crimes which require *mensrea*("a guilty mind") - most common law crimes require *mensrea*, while many statutory offences involve strict criminal liability. In order to convict companies of common law crimes, courts may consider the *mensrea*of those individuals who control the company to be the *mensrea*of the company. However, the courts have been very restrictive in their use of this approach.

The principal of separate legal entity was explained and emphasized in the famous case of Salomon v Salomon & Co. Ltd. This case established that in the eyes of law a registered company is a distinct entity from its members, even if the person holds all the shares in the company. Further there is no difference in principle if a company has only two shareholders or two hundred members. In each case the company is a separate legal entity.

1. **Perpetual Existence**

Perpetual means permanent or eternal. A company is everlasting form of business organisation. A company will never end unless it is ended by the law. Law creates it and law alone can dissolve it. Its life does not depend upon the lives of its members or shareholders. The death, insolvency or retirement of any or all shareholders or directors will not affect the survival of the company. The company is like a river where the water keeps on changing continuously, but the river remains the same. Members may come and go but the company continues its operations until it is wound up. Thus, a company has a perpetual existence, irrespective of changes in its membership.

1. **Common Seal**

A company being an artificial person cannot sign documents for itself. But having a legal identity, it acts through natural persons who are called board of directors. Thus, the law has provided for the use of common seal, as a substitute for its signature. All contract entered into by the directors will be under the common seal of the company. Any document bearing the common seal of the company will be legally binding on the company.

1. **Limited Liability**

Limitation of liability is another important feature. The company, being a separate entity, the members are not liable for its debts. The liability of members is limited by shares or limited by guarantee; each member is bound to pay the nominal value of shares held by them and his liability ends there. For example, if the face value of a share in a company is Rs. 10 and a member has already paid Rs. 8 per share, he can be called upon to pay not more than Rs. 3 per share during the lifetime of the company. In a company limited by guarantee the liability of members is limited to such amount as the member may undertake to contribute to the assets of the company in the event of its being wound up.

1. **Transferable Shares**

Members of the company can easily transfer and sell their shares. The right to transfer share is a statutory right of members and it cannot be taken away by a provision in the articles. The articles shall prescribe the manner in which such transfer of shares will be made. However, it may contain bona fide and reasonable restrictions on the right of members to transfer their shares. However, in the case of a private company, the articles shall restrict the right of member to transfer their shares in companies with its statutory definition.

1. **Separate Property**

A company is capable of owning, enjoying and disposing of property in its own name. Although its capital and assets are contributed by its shareholders, they cannot claim ownership of any asset of company’s assets. The company is the real person in which all its property is vested and by which it is controlled, managed and disposed of.

1. **Delegated Management**

As already pointed out the company is an artificial person it cannot act on its own. It has to depend on its members for its operations. Since it has a large number of members, all of them cannot take part in the management of the affairs of the company. Therefore, the control and management is, delegated by the shareholders to their elected representatives, known as directors. They look after the day-to-day working of the company

1. **Share capital**

Company carries out its business in large scale. To do business in large scale it needs huge capital. Generally, the company mobilizes its capital by selling its shares. Those persons who buy these shares become its shareholders and thereby become members in it.

1. **Voluntary Association**

A company is voluntary association of persons who have come together for a common object i.e., earning profit. Activities of this association are governed by the law and are limited by its memorandum of association.

1. **Termination of Existence**

A company, being an artificial juridical person, does not die a natural death. It is created by law, carries on its affairs according to law throughout its life and ultimately is effaced by law. Generally, the existence of a company is terminated by means of winding up. However, to avoid winding up, sometimes companies adopt strategies like reorganisation, reconstruction and amalgamation.

1. **Capacity to Sue and Be Sued**

A company being a body corporate, can sue and be sued in its own name. To sue, means to institute legal proceedings against (a person) or to bring a suit in a court of law. All legal proceedings against the company are to be instituted in its name. Similarly, the company may bring an action against anyone in its own name. A company’s right to sue arises when some loss is caused to the company, i.e. to the property or the personality of the company. A company, as a person distinct from its members, may even sue one of its own members.

* + 1. **Kinds of companies**

Companies can be classified in the following manner.

1. On the basis of incorporation
2. On the basis of ownership
3. On the basis of liability
4. On the basis of number of members
5. On the basis of Incorporation companies are classified in to 3 categories

a. Chartered Company

b. Statutory Company

c. Registered Company

1. **Chartered company**

These companies are incorporated under the special charter granted by the King or Queen. A chartered company has wide powers. It can deal with its property and bind itself to any contracts like an ordinary person. The power and the affairs of these companies are mentioned in the charter under which they are incorporated. For example, East India Company and Bank of England. After independence such companies do not exist in India.

1. **Statutory companies**

These companies are incorporated by a special Act passed in the Parliament or any State legislature. For example, Reserve Bank of India, Life Insurance Corporation of India and Food Corporation on India, State Bank of India, Industrial Finance Corporation, Unit Trust of India, State Trading corporation etc. the functions and affairs of these companies are stipulated in the act creating them. Such companies do not have any memorandum or articles of association. The provisions of the Companies Act shall also apply to these companies except in so far as provisions of the Act are inconsistent with those of such Special Acts. These companies are generally formed to meet social needs and not for the purpose of earning profits.

1. **Registered companies**

Companies formed under the companies Act of 1956 or under any other companies Act passed earlier to this, are called registered companies. This is most common mode of incorporating a company especially after independence. Such companies come into existence only when they are registered and a certificate of incorporation is obtained from the Registrar of Companies.

1. On the basis of Liabilitythe companies are classified in to following types.

a. Companies limited by shares

b. Companies limited by Guarantee

c. Unlimited Companies

1. **Companies limited by shares**

In these types of company, the liability of the members is limited to the extent of face value of share subscribed by them. It means the liability of shareholder is limited to the amount if any unpaid on the shares held by them. The members can be called upon to pay the amount remaining unpaid during the existence of the company or in the event of winding up. A company limited by shares may be a public company or a private company. These are the most popular types of companies.

1. **Companies limited by Guarantee**

In these type companies the liability of the members is limited to a certain amount of money promises by them. in other words, eachmember promises to pay a fixed sum of money specified in the Memorandum in the event of liquidation of the company for payment of the debts and liabilities of the company. This amount promised by him is called ‘Guarantee’, and such a company is called a company limited by guarantee. These companies may or may not have share capital. If the company does not have share capital, it depends on entrance and subscription fees for its existence. if the company has a share capital, then the liability of the member is limited to the extent of the guarantee. If it has a share capital, it may be a public company or a private company.

Non-trading or non-profit companies formed to promote culture, art, science, religion, commerce, charity, sports etc. are generally formed as companies limited by guarantee.

1. **Unlimited companies**:

In case of these companies the liability of the members is unlimited. In other words, a company not having any limit on the liability of its members is called unlimited company. In an unlimited company every member is liable for the debts of the company in proportion to his interest in the company. An unlimited company may or may not have share capital. If the company has a share capital, the articles of an unlimited company should state the amount of share capital and also the number of member of the company. Such companies are not popular in India.

1. On the basis of members, company can beclassified into

a. Private Company

b. Public Company

1. **Private company**:

A private company is that company which by its articles of association:

1. Restricts the number of its members to 50 (excluding those members who are in the employment of the company)
2. Disallows the right to transfer its shares
3. Does not invites the public to subscribe any shares or debentures of the company
4. Provides where two or more persons hold one or more shares in the company jointly.

There should be at least two persons to incorporate a private company and it required to add the word “Private Ltd” at the end of its name.

**Characteristics or Features of a Private Company.** The features of a privateof a private company are as follows:

1. Restriction on share transfer:

The shares of the private company are not freely transferable. The articles of association generally states that when a shareholder wants to transfer his shares, first he has to offer them to the existing members of the company. The price of the shares is fixed by the directors of the company.

1. Limited number of members:

The maximum number of the members are fifty excluding employees who are working in the company. The minimum number of members are two. If two or more persons held the shares jointly they are considered as a single member.

1. Own capital:

A private company cannot invite the general public to purchase its shares and debentures. It has to make its own private arrangement for mobilizing capital.

**Special rights of a Private Company**

The private company enjoys certain special privileges under the provisions of companies Act 1956. These privileges can be listed as follows:

* 1. A private company may be started with only two persons as member. [Sec.12(1)]
  2. Before the minimum subscription is subscribed for or paid, it may commence allotment of shares (Sec. 69).
  3. Not required to issue a prospectus to the public. (Sec 70 (3)]
  4. Restrictions imposed on public companies regarding further issue of shares do not apply on private companies. [Sec 81 (3)]
  5. Provisions of Sections 114 and 115 relating to share warrants shall not apply to it. (Sec. 14)
  6. Need not keep an index of members. (Sec. 115)
  7. A certificate of commencement of business is not required to commence the business [Sec. 149 (7)]
  8. It need not hold statutory meeting or file a statutory report [Sec. 165 (10)]
  9. Unless the articles provide for a larger number, only two persons personally present shall form the quorum in case of a private company, while at least five member personally present form the quorum in case of a public company (Sec.174).

1. **Public company**

A company which is not a private company is called public company. Sec 3 (1) (iv) of the companies Act 1956 defines public company as “A public company which is not a Private Company”. i.e. the articles of the public company

1. Do not restrict the number of its members.
2. Does not disallows the transfer of its shares.
3. It invites the general public to subscribe the shares and debentures.

**Characteristics of Public company**

The public company has the following features

1. No restriction on transfer of shares

The shares of the public company are freely transferable. Whenever a shareholder wants to transfer his shares he can transfer them to whomever he wants. The price of the shares is determined in the share market by the demand and the supply factors.

1. No limit in the number of members

There is no restriction regarding the maximum number of members in the company. The minimum number is seven, and there is no limitation on the maximum number of the members.

1. Share capital

The public company invites general public to purchase its shares and debenture to mobilize the share capital. It means public company mainly depends on public for its capital requirement.

1. Regulated by Act

Unless a private company a public company is subject to a number of regulations and restrictions as per the requirements of Companies Act, 1956. It is done to safeguard the interests of investors or shareholders of the public company.

**DIFFERENCE BETWEEN PUBLIC COMPANY AND PRIVATE COMPANY**

|  |  |
| --- | --- |
| **Private Company** | **Public Company** |
| 1. The minimum number of persons required is 02 and the maximum is 50. | 1. The minimum number of persons required is 07 and the maximum is unlimited. |
| 1. It makes the use of the word Private limited after its name. | 1. It makes the use of the word limited after the name. |
| 1. It can commence its business operation immediately after getting certificate of incorporation. | 1. It requires both the certificate of incorporation and the certificate of commencement for starting its commencement. |
| 1. The memorandum of association and the articles of association is required to sign by at least two persons. | 1. Its memorandum and articles of association is required to sign by at least seven persons. |
| 1. The filling of both memorandum and article of association is obligatory. | 1. It may or may not have its own articles of association because it may adopt table ‘A’. |
| 1. It does not require the filling of the prospectus or statement-in-lieu of prospectus. | 1. It must file prospectus or statement in lieu of prospectus before allotment of shares. |
| 1. It cannot sell shares to the general public in the open market. | 1. It sell shares to the general public in the open market. |
| 1. Transfer of share is restricted in the articles of association. | 1. Transfer of shares is not restricted and as such shares are freely transferable and are quoted in the stock exchange. |
| 1. There are of least two directors and they need not retire by rotation. | 1. It has at least 3 directors and they are subject to retire by rotation. |
| 1. There is no legal restriction on director’s remuneration. | 1. The directors cannot draw remuneration more than 11 percent of the net profit of the company. |

1. **On the basis of Ownership companies are classified into**

**a.Government Companies**

**b. Non-government Companies**

1. **Government Companies**

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 jointly or partly by the Central Government and by one or more State Governments is called Government Company. The subsidiary of a Government company is also a Government company. In other words, a part or the whole of capital of the government company is owned by the government. The directors and the auditors are appointed by the government. Some of the examples of government companies are - National Thermal Power Corporation Ltd., State Trading Corporation Ltd. Hydroelectric Power Corporation Ltd. Bharat Heavy Electricals Ltd. Hindustan Machine Tools Ltd. etc.

1. **Non-Government Companies.**

All other companies, except the Government Companies, are called non-government companies.

1. **On the basis of Nationality (Domicile)companies are divided into following categories**

**a. Indian Companies**

**b. Foreign Companies**

1. **Indian Companies**

Companies registered under the provisions of the Companies Act 1956 and having their registered office in India are known as Indian Companies.

1. **Foreign Companies**

**C**ompanies incorporated outside India and having a place of business in India whether its own or through an agent, conducts any business activity in India physically or through electronic mode; and in any other manner are called Foreign Companies [Sec. 591 (I)]. A foreign company has a place of business in India if it has a specified place at which it carries on business such as an office, store house or other premises with some visible indication premises. Section 592 to 602 of Companies Act, 1956 contain provisions applicable to foreign companies functioning in India.

1. **On the basis of holding (Control)**

On the basis of control, a company may be classified into:

a. Holding companies, and

b. Subsidiary Company

1. **Holding Company [Sec. 4(4)].**

A company is called holding company of another company if it controls the other company. Sec 4(4) of the Companies Act specify that a company is deemed to be the holding company of another if, but only if that other is its subsidiary.

Though there are two companies, the affairs of both the companies are managed and controlled by the holding company. A holding company may have any number of subsidiaries. The annual report of the holding company is required to disclose full information about its subsidiaries.

A company may become a holding company in either of the following ways: -

1. By holding more than half in nominal value of its equity share capital or
2. By holding more than fifty per cent of its voting rights; or
3. By securing to itself the right to appoint, the majority of the directors of the other company, directly or indirectly.
4. **Subsidiary Company. [Sec. 4 (I)].**

A company is known as a subsidiary of another company when its control is exercised by the other company (called holding company).

1. **Other classifications of the company are**:
2. **One Person Company**

Means a company which has only one person as a member. This is a company in which one man holds practically the whole of the share capital of the company, and in order to meet the statutory requirement of minimum number of members some dummy members like his wife and son holds one or two shares each. As per section 3(1) (c), One-person Company is considered as a private company. Only a natural person who is anIndian citizen and resident in India is eligible to incorporate it. Many relaxations have been granted to One Person Company in compliances and procedural aspects. For example, One Person Company is not required to hold annual general meeting. Relaxation with regard to holding board meetings, preparation of financial statements (cash flow exempted), signing of annual return etc.

1. **Small company**

Small company is a new type of company defined under the companies Act 2013. A classification of a private company based on size of the paid up capital and turnover. As per sec 2(85) a small company means a private limited company, not being a subsidiary or holding company of a public company, having:

1. Paid –up share capital of which does not exceed fifty lakh rupees
2. Turnover of which as per its last profit and loss account does not exceed two crore rupees
3. **Associate company**

The concept of associate company is introduced to add more transparency and governance in the working of the company. According to sec 2(6) An associate company in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes joint venture company. Here significant influence means control of at least twenty percent of the total share capital.

1. **Dormant company**

Dormant company is type of an inactive company. As per sec 455(1) of the companies Act 2013, a company which formed and registered for a future project or hold an asset or intellectual property and has no significant accounting transactions is termed as dormant company.

* 1. **CORPORATE PERSONALITY**

The concept of corporate personality has been a significant issue in the study of corporate and commercial systems in general. In company law, the concept of corporate personality' signifies that a company is distinct from its shareholders. The company has the liability and not the shareholders. The company has a legal but not a physical existence. It is neither an agent nor a trustee for its shareholders. A company acquires certain attributes upon incorporation. It is treated as a 'person' in its own right.

After incorporation the company gets a unique identity. The certificate of incorporation having distinct registration number distinguishes it from other corporate entities. The certificate signifies the birth of the company. It can be likened to a human being, but it is a lifeless body dependent upon the support of others for its functional and operational existence. It has a 'directing mind and will' – the directors of the company, who protect the best interests of the company at all times. They act as a nerve center of the company, managing the day-to-day operations and functions, thereby protecting the company's assets and striving towards profit maximisation as one of the major objectives of the company.

Corporate personality is concerned with the company acquiring an existence which is independent in its own right from its shareholders. The independent existence of a company from its shareholders means that a company can own and dispose of property. It is subject to corporation tax. It can sue and be sued. It can enter into contracts. It may be subject to civil or criminal penalties.

Salomon v Salomon case is the leading case regarding independent existence, it identified that a company is not only an association of its members, but also a person separate from its members which is extremely significant as it carries many consequences. Once a company is legally incorporated it becomes a legal person with its own rights and liabilities separate from those of its members. Thus shareholders cannot be liable to indemnify the company’s debts.

Individuals are permitted to incorporate companies to separate their business and personal affairs, thereby avoiding further personal liability as mentioned in Salomon. This advantageous limited liability is consequential of members being separate persons from the company. Members’ liability is limited to their fully paid share amount or the fixed amount payable by guarantee. The company cannot insist on further contribution nor can the members be liable to cover debts which the company incurred as a separate person. Additionally, the debts were not incurred on behalf of the members since Salomon rendered that no agency relationship exists between them.

Salomon also distinguished that a company’s business is its own as a separate person. A company is hereby entitled to sue third parties, and even its own members, but the members cannot sue on behalf of the company since the legal rights belong to the company as a separate person.

Another consequence of this doctrine is that a company’s property is its own, hence neither members nor creditors have any legal or equitable interest in the company’s assets. Regardless if members have a profitable interest in the assets, the separate personality principle applies even to their detriment, enforcing that the company’s assets do not belong to its owners.

Further a company can enter into contracts and transactions, even with its members, as a result of separate personality, whether it is a contract of sale or contract of employment. Furthermore, companies have perpetual existence even after the death of all members emphasising the principle of separate personality. Thus ownership change and share trading will not affect its continuous existence.

* 1. **CORPORATE VEIL**

The term corporate veil refers to a legal concept that separates the personality of a corporation from the personalities of its shareholders and protects them from being personally liable for the company’s debts and other obligations. Thus, a veil of incorporation exists between the company and its members and due to this a company is not identified with its members. In order to protect themselves from the liabilities of the company, its members often take the shelter of the corporate veil. Sometimes this corporate veil is used as a vehicle of fraud or evasion of tax etc. To prevent unjust and fraudulent acts, it becomes necessary to lift the veil of the corporation or disregard the corporate personality to look into the realities behind the legal shell and to hold the individual member of the company liable for its acts or liabilities.

The Court will break through the corporate veil and apply the principle or doctrine of what is called as “lifting of or piercing the corporate veil”. The Court will look behind the corporate entity and take action as entity is not separate from the members and make the members or the controlling persons liable for debts and obligations of the company. The separate legal personality is only ignored for certain purposes, but the corporate entity still retains its status as a corporation.

* 1. **LIFTING OF THE CORPORATE VEIL**

Lifting of the corporate veil means disregarding the corporate personality and looking behind the real person who are in the control of the company. In other words, 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.

The circumstances under which the court may lift the corporate veil may be discussed under the following two categories.

1. Under statutory provisions
2. Under Judiciary provisions
3. **Under Statutory Provisions**

Under statutory provisions, the corporate veil may be lifted as per the provisions of the Companies Act 1956. This can happen in the following circumstances:

1. **Reduction of the number of members below statutory minimum:** In case the number of members fall below 7 in a public company and below 2 in a private company and the company carries on business for more than six months then every continuing member of the company who is aware of the fact, can be individually liable for the payment of the whole debts of the company contracted during that time, and may be severally sued.
2. **Establishing the relationship of holding and subsidiary company**: When one company controls the management of another company the former is called the holding company and the latter is called the subsidiary company. In this case the law can lift the corporate veil in order to determine whether there exists a relationship of holding and subsidiary between the two companies.
3. **Fraudulent Trading**- Under Section 542 of The Indian Companies Act, 1956, if any business of a company is carried on with the intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, who was knowingly a party to the carrying on of the business in that manner is liable to imprisonment or fine or both. This applies whether or not the company has been or is in the course of being wound up. This was upheld in Delhi Development Authority Vs Skipper Constructions Co. Ltd. (1997).
4. **Company not mentioned on a bill of exchange**- Section 147 (4) of The Indian Companies Act, 1956, provides that if any officer of the company or other person acting on its behalf signs or authorizes to be signed on behalf of the company any bill of exchange, promissory note, endorsement, cheque or order for money or goods in which the companies name is not mentioned in legible letters, he is liable to fine and he is personally liable to the holder of the instrument unless the company has already paid the amount.
5. **Premature Trading**- Another example of personal liability is mentioned in Section 117 (8) of The English Companies Act. Under this section a public limited company newly incorporated as such must not "do business or exercise any borrowing power" until it has obtained from the registrar of companies a certificate that has complied with the provisions of the act relating to the raising of the prescribed share capital or until it has re-registered as a private company. If it enters into any transaction contrary to this provision not only are the company and its officers in default, liable to pay fines but if the company fails to comply with its obligations in that connection within 21 days of being called upon to do so, the directors of the company are jointly and severally liable to indemnify the other party in respect of any loss or damage suffered by reason of the company's failure.
6. **Failure to Refund Application Money**-According to Section 69(5) of The Indian Companies Act, 1956, the directors of a company are jointly and severally liable to repay the application money with interest if the company fails to refund the money within 130 days of the date of issue of prospectus.
7. **Facilitating the task of an inspector appointed** under section 235 or 237 to investigate the affairs of a company: According to Section 239 of the Companies Act 1956 if it is necessary for the satisfactory completion of the task of an inspector appointed to investigate the affairs of a company for any mismanagement, fraud or wrong policies towards its members, he/she has can lift the corporate veil of another related company having the same management to investigate the affairs of the company.
8. **Investigation of ownership of Company:** According to Section 247 of the Companies Act the central government may order to lift the corporate veil by appointing one or more inspectors to investigate and report on the membership of any company for the purpose of determining the true persons who are financially interested in the company and who control and influence its policy.
9. **Under Judicial Interpretation**

**The cases where the court can lift the corporate veil are as follows:**

1. **Evasion of taxes**: If it is found that the company has been formed with the sole purpose of making money and the members are using unfair practices such as evasion of tax to amass wealth then the court has the power to lift the corporate veil to enquire about the real members of the company who are making financial gain through such unfair means.
2. **Fraud and unethical conduct:** The court has the power to lift the corporate veil if it finds that its members for defrauding its creditors and for avoiding contractual obligations are using the company and making personal gains.
3. **Enemy character of the company:** If there are reasons to believe that the company is being controlled and run by members who are alien enemies (citizens of countries with whom our country is at war) then the court can lift the corporate veil to identify those members.
4. **Where the Company is a Sham**- The Courts also lift the veil where a company is a mere cloak or sham (hoax).
5. **Company Avoiding Legal Obligations**- Where the use of an incorporated company is being made to avoid legal obligations, the Court may disregard the legal personality of the company and proceed on the assumption as if no company existed.
6. **Agency or Trust**- Where a company is acting as agent for its shareholder, the shareholders will be liable for the acts of the company. It is a question of fact in each case whether the company is acting as an agent for its shareholders. There may be an Express agreement to this effect or an agreement may be implied from the circumstances of each particular case.
7. **Avoidance of Welfare Legislation**- Avoidance of welfare legislation is as common as avoidance of taxation and the approach of the Courts in considering problems arising out of such avoidance is generally the same as avoidance of taxation. It is the duty of the Courts in every case where ingenuity is expended to avoid welfare legislation to get behind the smokescreen and discover the true state of affairs.
8. **Public Interest** the Courts may lift the veil to protect public policy and prevent transactions contrary to public policy. The Courts will rely on this ground when lifting the veil is the most ‘just’ result, but there are no specific grounds for lifting the veil. Thus, where there is a conflict with public policy, the Courts ignore the form and take into account the substance.
   1. **CORPORATIONS AS CITIZENS**

A company, though a legal person is not a citizen in the same way that "real" citizens are - they cannot hold passports or vote in elections. It has been recognized that they do share in some of the same or similar practices, such as paying taxes, engaging in free speech, and expecting certain protections from the state. There is concern, however, that extending the scope of citizenship to incorporated corporations may infringe upon democracy and equality given their access to substantial power and resources.

**IS COMPANY A CITIZEN?**

 A company, though a legal person, is not a citizen. This has been the conclusion of a special bench of the Supreme Court in ***State Trading Corporation of India v. CTO (AIR 1963 SC 1811)****.*

The State Trading Corporation of India is incorporated as a private company under the Companies Act, 1956. All the shares are held by the President of India and two secretaries in their official capacities. The question was whether the corporation was a citizen. One of the contentions put forth on behalf of the corporation was that “if the corporate veil is pierced, one sees three persons who are admittedly the citizens of India”, and, therefore, the corporation should also be regarded as a citizen.

 But it was held that, “neither the provisions of the Constitution, Part II, nor of the Citizenship Act, either confer the right of citizenship on or recognize as citizen, any person other than a natural person. In striking words the Supreme Court observed.

     “If all the members are citizens of India the company does not become a citizen of India any more than, if all are married the company would not be a married person.” A company can have the benefit of only such fundamental rights as guaranteed to every “person” whether a citizen or not. However, it has a nationality, domicile and residence. The hardship caused by the above pronouncement was later modified by holding that a citizen shareholder may petition, proceeding on behalf of the company, against violation of his company’s fundamental rights.

Movement aimed at encouraging companies to be more aware of the impact of their business on the rest of society, including their own stakeholders and the environment.

**CASE EXAMPLES**

1. **The case of Salomon v. Salomon and Co. Ltd*.,* (1897) A.C. 22**

This case has clearly established the principle of Separate Legal Entity, that once a company has been validly constituted under the Companies Act, it becomes a legal person distinct from its members and for this purpose it is immaterial whether any member holds a large or small proportion of the shares, and whether he holds those shares as beneficially or as a mere trustee.

In the case, Salomon had, for some years, carried on a prosperous business as leather merchant and boot manufacturer. He formed a limited company consisting of himself, his wife, his daughter and his four sons as the shareholders, all of whom subscribed to 1 share each so that the actual cash paid as capital was £7.

Salomon sold his business (which was perfectly solvent at that time), to the Company formed by him for the sum of £38,782. The company’s nominal capital was £40,000 in £1 shares. In part payment of the purchase money for the business sold to the company, debentures of the amount of £10,000 secured by a floating charge on the company’s assets were issued to Salomon, who also applied for and received an allotment of 20,000 £ 1 fully paid shares. The remaining amount of £8,782 was paid to Salomon in cash. Salomon was the managing director and two of his sons were other directors.

The company soon ran into difficulties and the debenture holders appointed a receiver and the company went into liquidation. The total assets of the company amounted to £6050, its liabilities were £10,000 secured by debentures, £8,000 owing to unsecured trade creditors, who claimed the whole of the company’s asset s, viz., £6,050, on the ground that, as the company was a mere ‘alias’ or agent for Salomon, they were entitled to payment of their debts in priority to debentures. They further pleaded that Salomon, as a principal beneficiary, was ultimately responsible for the debts incurred by his agent or trustee on his behalf.

Their Lordships of the House of Lords observed:

“…*the company is a different person altogether from the subscribers of the memorandum; and though it may be that after incorporation the business is precisely the same as before, the same persons are managers, and the same hands receive the profits, the company is not, in law, their agent or trustee. The statute enacts nothing as to the extent or degree of interest, which may, be held by each of the seven or as to the proportion of interest, or influence possessed by one or majority of the shareholders over others. There is nothing in the Act requiring that the subscribers to the memorandum should be independent or unconnected, or that they or any of them should take a substantial interest in the undertakings, or that they should have a mind or will of their own, or that there should be anything like a balance of power in the constitution of company.*”

1. **Lee V. Lee’s Air forming Ltd. (1961)**

Lee V. Lee’s Air forming Ltd. (1961) A.C. 12 of the 3000 shares in Lee’s Air Forming Ltd., Lee held 2999 shares. He voted himself the managing Director and also became Chief Pilot of the company on a salary. He died in an air crash while working for the company. His wife was granted compensation for the husband in the course of employment. Court held that Lee was a separate person from the company he formed, and compensation was due to the widow. Thus, the rule of corporate personality enabled Lee to be the master and servant at the same time.

The principle of separate legal entity of a company has been, in fact recognized much earlier than in Saloman’s case. In Re Kondoi Tea Co Ltd. (1886 ILR 13 Cal 43), (7) it was held by Calcutta High Court that a company was a separate person, a separate body altogether from its Shareholders. In Re. Sheffield etc. Society - 22 OBD 470), it has been held that a corporation is a legal person, just as much in individual but with no physical existence.

**Keywords**

**Limited liability**

Usually refers to limited companies where the shareholders’ liability to pay the debts of the company is limited to the value of their shares.

**Corporation**

An organization formed under state law for the purpose of carrying on a business enterprise is such a manner as to make the enterprise distinct from its owners.

**Citizen**

A person who is a member of a particular country and who has rights because of there or being born because of being given rights, or a personwho lives in a particular town or city.

**Veil**

A thin covering that hides something or stops you from seeing something clearly

**Company personality**

A company with such personality is an independent legal existence separate from its shareholders, directors, officers and creators

**Questions**

* 1. Define ‘Company’. What are its essential characteristics?
  2. Explain the special privileges of a private company as compared to a public company.
  3. Write notes on :

1. Chartered Companies
2. Government Companies
   1. Classify company form of organization on the basis of liability of members.
   2. Explain the classification of companies based on holding.
   3. Is company a citizen? Comment
   4. Explain the characteristics of private company.
   5. State the difference between public company and private company.

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