

UNIT 3

IMP TOPICS

- 1. Debt capital; Debentures**
- 2. Membership in company**
- 3. Directors**

Debt Capital: Debentures – Meaning and Kinds

1. Introduction

A company raises capital through two primary sources: equity (ownership capital) and debt (borrowed capital). Debentures are one of the most common instruments used by companies to raise debt capital. They represent a loan taken by the company and not an ownership stake.

Debenture-holders are creditors of the company, and not its members.

2. Meaning of Debentures

As per Section 2(30) of the Companies Act, 2013,

“Debenture includes debenture stock, bonds and any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.”

Thus, a debenture is a written instrument acknowledging a debt, issued under the company's seal and repayable with interest.

3. Features of Debentures

- Written Acknowledgement of Debt
- Fixed Interest Rate payable periodically
- Redemption after a fixed term
- May be secured or unsecured • Can be listed and traded on stock exchanges

4. Parties Involved

- Company: The borrower issuing the debentures
- Debenture-holders: Creditors of the company
- Debenture Trustee: Appointed to protect debenture- holders' interest (if the issue is public)

5. Kinds of Debentures

Debentures may be classified under several heads based on security, convertibility, tenure, registration, etc.

5.1 Based on Security

a) Secured Debentures

- Backed by a charge on the company's assets (fixed or floating).
- In case of default, assets can be sold to recover dues.

b) Unsecured Debentures (Naked Debentures)

- No security backing.
- Debenture-holders rank below secured creditors in case of liquidation.

5.2 Based on Convertibility

a) Convertible Debentures

- Can be converted into equity shares after a specified period.
 - Fully Convertible: Entire face value converted into shares.
 - Partly Convertible: Part is converted, and the rest is redeemed.

b) Non-Convertible Debentures (NCDs)

- Cannot be converted into shares. They are redeemed in cash.

5.3 Based on Redemption

a) Redeemable Debentures

- Repaid after a specific period, either in lump sum or instalments.

b) Irredeemable (Perpetual) Debentures

- No fixed repayment date. Rare under Indian law.

5.4 Based on Registration

a) Registered Debentures

- Details recorded in the Register of Debenture-holders.
- Transfer requires executed transfer deed.

b) Bearer Debentures

- Not registered in the company's records.
- Transferable by mere delivery, like cash.

6. Statutory Provisions and SEBI Guidelines

- Governed by Companies Act, 2013 (esp. Sections 71 & 77)
- SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021 applicable for listed NCDs
- Companies issuing public debentures must appoint a Debenture Trustee

7. Case Laws

a) IL & FS Financial Services v. Debenture Trustees (2020)

- Debenture Trustees must ensure protection of investor rights and proper enforcement of security.

b) Narandas M. Mehta v. Commissioner of Income Tax (1971)

- Defined nature of debentures as instruments of debt, not equity.

8. Conclusion

Debentures are an important source of long-term debt capital for companies. They allow companies to raise funds without diluting ownership and offer investors a fixed return. Understanding the types of debentures helps both companies and investors in making informed financial decisions while ensuring legal compliance and clarity in contractual obligations.

Membership in a Company – Modes of Acquiring Membership, Who Can Be a Member, Cessation of Membership, and Register of Members

1. Introduction

A member is a person whose name is entered in the Register of Members of a company. Under Section 2(55) of the Companies Act, 2013, a member includes:

- The subscriber to the Memorandum of Association;
- Any other person who agrees in writing to become a member and whose name is entered in the Register of Members;
- In case of a company without share capital, a person who agrees to become a member.

2. Modes of Acquiring Membership

2.1 By Subscription to Memorandum

- The original subscribers to the memorandum become members by default on incorporation.
- Their names appear in the Register of Members from the beginning.

2.2 By Application and Allotment

- A person applies for shares and, upon allotment, becomes a member once their name is entered in the Register.

2.3 By Transfer of Shares

- An existing shareholder may transfer shares to another person.
- The transferee becomes a member once the transfer is registered in the Register of Members.

2.4 By Transmission of Shares

- In case of death, insolvency, or legal disability, shares are transmitted to legal heirs or representatives.

2.5 By Acquiescence or Estoppel

- A person who acts like a member (e.g., receives dividends, attends meetings) may be considered a member by conduct (implied membership).

3. Who Can Be a Member?

3.1 Individual Persons

- Any competent person (not a minor or insolvent) may become a member.

3.2 Companies

- A company can hold shares in another company, subject to restrictions under Section 19 of the Companies Act, 2013.

3.3 Firms

- A partnership firm cannot be a member, as it is not a legal person.

3.4 Minor

- A minor cannot become a member directly, but shares can be held in their name through a guardian (only fully paid-up shares).

3.5 HUF (Hindu Undivided Family)

- HUFs can become members through the Karta.

3.6 Trusts

- Trusts are not legal persons, but trustees can become members in their capacity as trustees.

4. Cessation of Membership A person ceases to be a member in the following circumstances:

4.1 Transfer of Shares

- Upon valid registration of the share transfer to another person.

4.2 Forfeiture of Shares

- If shares are forfeited for non-payment of calls.

4.3 Surrender of Shares

- If a member voluntarily surrenders their shares, subject to company's acceptance.

4.4 Redemption of Shares

- Preference shares may be redeemed and canceled as per terms.

4.5 Death or Insolvency

- Legal heirs or assignees become members only upon registration.

4.6 Expulsion

- A company cannot expel a member unless specifically authorized by law.

5. Register of Members

5.1 Maintenance

- Every company must maintain a Register of Members under Section 88 of the Companies Act, 2013.

5.2 Contents

- The register must include:
 - Name, address, and occupation of members
 - Number and class of shares held
 - Date of becoming and ceasing to be a member

5.3 Location

- The register must be maintained at the registered office or another place with ROC approval.

5.4 Inspection

- The register is open for inspection by members on payment of prescribed fees.

5.5 Penalty

- Failure to maintain the register attracts a penalty under Section 88(5) and (6).

6. Case Law

Balkrishan Gupta v. Swadeshi Polytex Ltd. (1985)

- Clarified that a person becomes a member only when their name is entered in the Register of Members.

Bharat Insurance Co. Ltd. v. Kanhaiya Lal (1935)

- A firm is not a legal person and cannot be a member in its own name.

7. Conclusion

Membership forms the foundation of a company's legal structure, with shareholders exercising ownership rights. Understanding the modes of acquiring and terminating membership, as well as the importance of the Register of Members, is essential for ensuring compliance and protection of member rights.

Directors – Position, Appointment, Qualifications, Disqualifications, Powers and Duties; Director Identification Number (DIN)

1. Introduction

Directors are the key managerial personnel responsible for the governance, decision-making, and administration of a company. As per Section 2(34) of the Companies Act, 2013, a director is a person appointed to the board of a company.

2. Position of Directors

- Directors act as agents of the company when dealing with third parties.
- They are trustees of the company's property and funds.
- They are officers under the Companies Act and are liable for statutory compliances.
- The collective body of directors is called the Board of Directors.

3. Appointment of Directors

3.1 First Directors

- Named in the Articles of Association.
- If not named, all subscribers to the Memorandum become first directors.

3.2 Subsequent Appointment

- By shareholders in a general meeting through an ordinary resolution [Section 152].
- By the Board, in case of casual vacancies or additional directors [Section 161].

3.3 Independent Directors

- Mandatory in listed public companies [Section 149(4)].
- Must meet the criteria of independence as prescribed.

3.4 Proportional Representation

- Companies may adopt the method of proportional representation for board diversity [Section 163].

4. Qualifications of Directors

- A person must be competent to contract (sound mind, major, solvent).
- Should possess Director Identification Number (DIN).
- No specific academic or professional qualification is prescribed under the Act.
- Articles of Association may lay down additional criteria.

5. Disqualifications of Directors [Section 164]

A person is disqualified from being appointed as a director if:

- Declared insolvent or an unsound mind by a court.
- Convicted of an offence involving moral turpitude and sentenced to imprisonment for more than 6 months.
- Failed to file financial statements or annual returns for three consecutive years.
- Has been a director of a company which has defaulted in repayment of deposits or debentures.

6. Powers of Directors [Section 179]

The Board of Directors exercises all powers of the company, subject to the Act and Articles.

6.1 General Powers

- Power to manage the affairs and business of the company.
- Power to make decisions on policy and operational matters.

6.2 Specific Powers (by Board Resolution)

- Borrowing money.
- Investing funds of the company.
- Authorizing buy-back of securities.
- Approving financial statements.

6.3 Powers with Shareholder Approval

- Selling or leasing substantial company assets.
- Borrowing in excess of the paid-up capital and free reserves.
- Remuneration to directors beyond permissible limits.

7. Duties of Directors [Section 166]

7.1 Fiduciary Duties

- Must act in good faith in the interest of the company, its employees, shareholders, and community.

7.2 Duty of Care• Must exercise due diligence and reasonable care in decision-making.

7.3 Duty to Avoid Conflicts

- Must avoid situations where their interest conflicts with that of the company.

7.4 Duty Not to Achieve Undue Gain

- Should not make any undue personal gain or advantage.

7.5 Duty to Ensure Compliance

- Ensure the company adheres to all legal provisions and financial regulations.

8. Director Identification Number (DIN)

8.1 Meaning

- A unique 8-digit number issued by the Ministry of Corporate Affairs (MCA) to any individual intending to be a director.

8.2 Legal Requirement

- Under Section 153 & 154, no person shall be appointed as a director unless he holds a valid DIN.

8.3 Application Process

- Filed in Form DIR-3 with proof of identity and address.
- Must be verified and approved by the MCA.

8.4 Penalty for Non-Compliance

- Director or company is liable for penalty if any individual acts as a director without obtaining DIN.

9. Conclusion

Directors are the brain and nerve center of a company. Their role, from appointment to daily governance, is governed strictly under the Companies Act, 2013. Maintaining transparency, fiduciary integrity, and statutory compliance is essential for the credibility and success of a corporate entity.