UNIT 1
IMP TOPICS
Incorporation and Promotors
Certification of incorporation
Doctrine of constructive notice

Company: Meaning, Definition, and Kinds of Companies

1. Introduction

• A company is one of the most widely used forms of business organization, especially for large-scale enterprises.
• It is a legal entity separate from its members, formed under law to carry out lawful business activities.
• The concept of company law is governed primarily by the Companies Act, 2013 in India.

• **2. Meaning of a Company**

• A company is a voluntary association of persons formed to carry out a business with the aim of earning profit.
• It is a juristic person with legal rights and duties, and a perpetual succession, unaffected by changes in membership.
• A company has a distinct legal identity, can own property, sue or be sued in its own name, and is capable of entering into contracts.

3. Essential Features of a Company

1. <u>Separate Legal Entity</u>
◦ The company has an identity distinct from its members.
◦ Established in Salomon v. Salomon & Co. Ltd.
2. <u>Limited Liability</u>
◦ Members are liable only up to the nominal value of shares held by them.
3. <u>Perpetual Succession</u>
◦ Company continues to exist despite changes in membership or death of members.
4. <u>Artificial Legal Person</u>
◦ It exists only in the eyes of law, acts through human agents (directors).
5. <u>Transferability of Shares</u>
◦ Shares are freely transferable (in public companies), enhancing liquidity.
6. <u>Common Seal (Optional)</u>
◦ It may have a common seal used as its official signature.
7. <u>Separate Property</u>
◦ The company can own, enjoy, and dispose of property in its own name.

4. Kinds of Companies (Classification)

Companies may be classified based on various criteria under the Companies Act, 2013:

A) On the Basis of Incorporation

1. Chartered Companies
◦ Formed under a Royal Charter (e.g., East India Company – historical relevance).
◦ No longer prevalent in India.

2. Statutory Companies
◦ Formed by a Special Act of Parliament or State Legislature.
◦ E.g., RBI, LIC – governed by their own statutes.

3. Registered Companies
◦ Incorporated under the Companies Act, and are most common.

B) On the Basis of Liability

1. Company Limited by Shares
◦ Liability of members is limited to the amount unpaid on their shares.
◦ Most common form.

2. Company Limited by Guarantee
◦ Members guarantee to contribute a fixed amount in case of winding up.
◦ Common for non-profit organizations.

3. Unlimited Company
◦ Members have unlimited liability. Rare in practice.

Memorandum of Association (MOA)

1. Introduction• The Memorandum of Association (MOA) is the legal document that lays the foundation of a company's existence.
• It acts as the company's charter, setting out its powers, limitations, and fundamental conditions under which it operates.
• Section 2(56) of the Companies Act, 2013 defines MOA as the document originally framed or altered, which governs the external affairs of the company.
• It is submitted at the time of incorporation and registered with the Registrar of Companies (ROC).
• Without a valid MOA, a company cannot be formed.

2. Purpose and Importance

• The primary purpose is to define the scope of the company's activities and to ensure that it operates within the legal and permitted boundaries.
• Acts as a contract between the company and its members, and between the company and outsiders.
• Helps protect creditors and investors by declaring the company's objectives and limitations.

- Ensures that resources of the company are not misused for activities not intended by its founders.
- Forms the basis for the doctrine of ultra vires, under which acts beyond the MOA are void.

3. Clauses of Memorandum of Association

Section 4 of the Companies Act, 2013 mandates the inclusion of the following six clauses in the MOA:

a) Name Clause

- Specifies the legal name of the company.
- Must end with "Limited" for a public company or "Private Limited" for a private company.
- Name should not be identical or similar to an existing company's name (as per Rule 8, Companies Incorporation Rules, 2014).

b) Registered Office Clause

- States the location of the company's registered office, including the state where it is situated.
- Determines jurisdiction for legal matters and the ROC applicable.

c) Object Clause

- The most important clause, as it defines the main and ancillary objects for which the company is formed.
- Activities beyond this clause are ultra vires and hence void.
- Divided into:
- Main Object: The principal activity or purpose of incorporation.
  - Ancillary/Incidental Object: Activities necessary to carry out the main object.
  - Other Objects (for some companies): Optional or non-core objectives.

d) Liability Clause

- States whether the liability of members is limited or unlimited.
- In companies limited by shares, the liability is limited to the amount unpaid on shares held.

e) Capital Clause

- Details the authorized share capital, types of shares, and their nominal value.
- Helps determine the company's financial structure.

f) Subscription Clause

- Contains the declaration by initial subscribers, agreeing to take a certain number of shares.
- Must be signed by at least two persons (for private companies) and seven (for public companies).

4. Alteration of MOA

- Section 13 of the Companies Act, 2013 governs the alteration process.

• Requires a special resolution passed by shareholders in a general meeting.
• In some cases, Central Government or Tribunal approval is required (e.g., for shifting registered office from one state to another).
• The alteration becomes effective only after registration with the ROC.
• Object Clause alteration requires:
◦ Special resolution.
◦ Filing with ROC using Form MGT-14.
◦ In some cases, approval from Regional Director (if change involves shifting jurisdiction).

5. Doctrine of Ultra Vires
• Actions or contracts beyond the powers conferred by the object clause are considered ultra vires.
• Such acts are void ab initio and cannot be ratified, even with unanimous consent of all shareholders.

• Purpose: Protect shareholders and creditors from unauthorized business activities.

Important Case Laws:
• Ashbury Railway Carriage Co. Ltd. v. Riche (1875):
◦ Company entered into a financing contract not covered in its object clause.
◦ Held ultra vires and void.

• A. Lakshmanaswami Mudaliar v. LIC of India (1963):
◦ Company donated to a trust not aligned with its objectives.
◦ Supreme Court held the action ultra vires the MOA.

6. Legal and Practical Significance
• MOA acts as the backbone of the company's legal identity.
• Used by courts and tribunals to determine if the company is operating within its permitted powers.
• Guides the Board of Directors and shareholders in business decision-making.
• Helps potential investors understand the company's purpose and risk level.

7. Conclusion
• The Memorandum of Association is not a mere formality; it is a legal charter that defines the scope and limitations of a company's existence.
• It plays a crucial role in corporate governance by setting boundaries for company operations.
• A proper understanding of MOA ensures legal compliance, minimizes disputes, and enhances the company's credibility and transparency.

Incorporation of Companies under the Indian Companies Act, 2013

The incorporation of a company under the Companies Act, 2013, is a legal process through which a company becomes a separate legal entity, distinct from its members. This process is governed primarily by **Chapter II (Sections 3 to 22)** of the Companies Act, 2013, and involves several procedural and compliance requirements. Below is a detailed explanation of the incorporation process:

1. Types of Companies (Section 3)

Under Section 3 of the Act, a company may be formed for any lawful purpose by:

- **One Person Company (OPC):** By one person.
- **Private Limited Company:** By two or more persons.
- **Public Limited Company:** By seven or more persons.

These individuals subscribe their names to the Memorandum of Association (MoA) and comply with the registration requirements.

2. Preliminary Requirements

a) Digital Signature Certificate (DSC):

Every proposed director must obtain a DSC to sign electronic documents.

b) Director Identification Number (DIN):

DIN is mandatory for every individual intending to become a director.

c) Name Reservation (RUN/SPICe+ Part A):

The proposed company name must be reserved through the **RUN (Reserve Unique Name)** service or **SPICe+ (Simplified Proforma for Incorporating Company Electronically Plus)**. The name must comply with the **Companies (Incorporation) Rules, 2014**, and not be identical or similar to an existing company or trademark.

3. Preparation of Incorporation Documents

The following documents are necessary:

- **Memorandum of Association (MoA):** Defines the company's scope of activities.
- **Articles of Association (AoA):** Defines internal rules and regulations.

- **Declaration by Professionals (Form INC-8):** That all legal requirements have been complied with.
- **Affidavits/Declarations (Form INC-9):** From subscribers and directors.
- **Proof of Registered Office (Form INC-22):** Including ownership documents or rent agreement and utility bill.
- **Consent to Act as Director (Form DIR-2).**

4. Filing of Incorporation Forms

The **SPICe+** form (INC-32) is an integrated web form used for the incorporation of companies. It includes:

- **Part A:** For name reservation.
- **Part B:** For all other incorporation details including:
    - DIN allotment
    - PAN and TAN application
    - GST, EPFO, ESIC registration
    - Bank account opening

Additionally, the **AGILE PRO-S form** is used for obtaining mandatory registrations like GSTIN, EPFO, ESIC, and Profession Tax (in applicable states).

5. Payment of Fees

Fees must be paid for the MoA, AoA, and stamp duty based on the state and authorized capital. The Registrar of Companies (ROC) requires payment through the MCA portal.

6. Verification and Certificate of Incorporation (Section 7)

Upon submission, the ROC verifies the documents. If found satisfactory, a **Certificate of Incorporation** is issued, which includes:

- Company Identification Number (CIN)
- Date of incorporation
- PAN and TAN details

The company becomes a legal entity from the date of incorporation.

7. Post-Incorporation Compliances

- **Board meeting:** First meeting within 30 days of incorporation.
- **Opening of bank account.**
- **Appointment of Auditor (Form ADT-1):** Within 30 days.
- **Commencement of Business (Form INC-20A):** Filed within 180 days if the company is limited by shares.

8. Legal Effects of Incorporation (Section 9)

Upon incorporation, the company becomes:

- A body corporate with perpetual succession.
- Capable of owning property, suing, and being sued in its own name.
- Separate from its members and directors (principle of corporate personality).

9. Penalties for Non-Compliance

Section 10A mandates filing of a declaration of commencement of business. Non-compliance may lead to penalties and possible striking off of the company by the ROC.

Conclusion

Incorporation under the Companies Act, 2013, is a structured and digitized process aimed at promoting ease of doing business in India. It ensures that all companies are brought under a common legal framework, providing legal recognition and credibility. Compliance with the incorporation provisions also ensures transparency, investor confidence, and corporate governance.

Promoters, Position of Promoters, Pre-incorporation and Provisional Contracts under the Companies Act, 2013

The formation of a company involves various stages, and one of the key persons during the pre-incorporation stage is the **promoter**. The Companies Act, 2013 recognizes the role and responsibilities of promoters, especially in relation to contracts entered into before incorporation.

1. Who is a Promoter? [Section 2(69)]

The **Companies Act, 2013** defines a promoter under **Section 2(69)** as a person:

- **(a)** Named as such in the prospectus or identified by the company in its annual return;
- **(b)** Who has control over the affairs of the company, directly or indirectly, whether as a shareholder, director, or otherwise;
- **(c)** In accordance with whose advice, directions, or instructions the Board of Directors is accustomed to act (excluding those acting in a professional capacity).

Promoters are instrumental in:

- Conceiving the idea of the business
- Gathering initial capital
- Assembling the board
- Taking steps for incorporation

2. Functions of Promoters

- Selection of name and registration of the company.
- Drafting the **Memorandum of Association (MoA)** and **Articles of Association (AoA)**.
- Appointing directors and professionals.
- Entering into preliminary contracts.
- Procuring initial capital and assets for the company.

3. Legal Position of Promoters

Although promoters play a critical role, they are **not agents or trustees** of the company in the legal sense since the company does not exist during the promotion stage. However, **they are in a fiduciary relationship** with the company they promote.

Fiduciary Duties of Promoters:

- **Duty to disclose** any personal interest in transactions (e.g., profits made while selling personal property to the company).
- **Duty not to make secret profits.**
- **Duty to act in good faith** and in the best interest of the proposed company.

Key Case Law:

- **Erlanger v. New Sombrero Phosphate Co. (1878):** Held that promoters must disclose material facts to an independent board or shareholders.

4. Pre-Incorporation Contracts

These are contracts entered into **by the promoters on behalf of the company before it is incorporated**.

Legal Status:

- **Not binding on the company** because the company does not exist as a legal entity at that point.
- **Promoters remain personally liable** for such contracts unless:
    - A new contract is signed post-incorporation by the company adopting the same terms.
    - The company, after incorporation, **ratifies** the contract (technically, ratification is not valid in law since the company did not exist when the contract was made, but courts may uphold it through novation or fresh agreement).

Relevant Provision:

- **Section 15 of the Specific Relief Act, 1963**: Allows enforcement of pre-incorporation contracts if they are warranted by the terms of incorporation and are adopted by the company post-incorporation.

5. Provisional Contracts

Provisional contracts are those **entered into after incorporation but before the company is entitled to commence business** (especially relevant for public companies under the earlier Companies Act, 1956).

Key Features:

- The company exists, but the contract is **provisional** until the **certificate of commencement of business** is obtained.
- If the company fails to commence business, such contracts become void and unenforceable.

Companies Act, 2013 Context:

- Under **Section 10A** (inserted by the Companies (Amendment) Act, 2019), a company with share capital must file a **declaration of commencement of business** within 180 days.
- Until this declaration is filed, the company cannot borrow or commence operations, hence contracts made in this period are **treated as provisional**.

6. Promoters' Liability

- **Personal liability** for contracts entered into before incorporation, unless novated.
- **Liability for misstatements** in the prospectus (Section 35).
- **Liability for fraud and breach of fiduciary duty.**

7. Remuneration and Indemnity

Promoters are **not automatically entitled to remuneration** unless:

- There is an express agreement with the company post-incorporation.
- The Articles or Board approves it.
- They may be indemnified for expenses incurred **only if ratified** by the company after incorporation.

8. Conclusion

Promoters are crucial in shaping a company at its formation stage, but their actions before incorporation are not legally binding on the company unless explicitly adopted. The Indian legal framework ensures that while promoters have a key role, they are also bound by fiduciary responsibilities and may be held liable for misconduct or misrepresentation. Both **pre-incorporation and provisional contracts** are treated with caution under the law to protect the interests of the company and third parties.

Certificate of Incorporation and its Consequences; Commencement of Business (Companies Act, 2013)

I. Certificate of Incorporation [Section 7(2), 7(3), 7(4) of the Companies Act, 2013]

The **Certificate of Incorporation (CoI)** is a legal document issued by the **Registrar of Companies (RoC)** upon successful registration of a company under the Companies Act, 2013. It signifies the birth of a company as a separate legal entity.

Process of Incorporation:

Under **Section 7**, a company is incorporated after:

- Filing of SPICe+ form (INC-32) with necessary documents:
  - Memorandum and Articles of Association
  - Proof of registered office
  - Declaration by professionals
  - Identity/address proof of subscribers and directors
- Verification and approval by the RoC.

If the RoC is satisfied, it registers the company and issues the **Certificate of Incorporation** under **Section 7(2)**.

II. Legal Status of the Certificate of Incorporation

The Certificate of Incorporation is **conclusive evidence** of:

- Valid incorporation of the company.
- Compliance with all requirements of the Act.
- The company's existence from the date mentioned on the certificate.

Section 7(3) clearly states that once the certificate is issued, the company comes into legal existence as a **body corporate** under **Section 9**.

III. Consequences of the Certificate of Incorporation

1. Separate Legal Entity:

The company becomes a **distinct legal person**, capable of owning property, entering into contracts, suing, and being sued.

2. Perpetual Succession:

The company continues to exist regardless of changes in membership or death of its members.

3. Common Seal (optional):

If adopted, it serves as the company's official signature.

4. Limited Liability:

Members' liability is limited to the amount unpaid on shares or guaranteed.

5. Binding Effect of MoA and AoA (Section 10):

Once incorporated, the Memorandum and Articles become binding between the company and its members.

6. Conclusive Proof (Case Law):

Moosa Goolam Arif v. Ebrahim Goolam Arif (1913):
Held that once the Certificate of Incorporation is issued, its validity cannot be challenged, even if there were irregularities in the incorporation process.

Jubilee Cotton Mills Ltd. v. Lewis (1924):
A company was held validly formed even though one of the signatories was dead at the time of registration.

7. Commencement of Legal Operations (with conditions):

While the CoI brings the company into legal existence, commencement of business is a separate compliance requirement under Section 10A.

IV. Commencement of Business [Section 10A of the Companies Act, 2013]

Introduced by the **Companies (Amendment) Act, 2019**, Section 10A applies to companies incorporated after **2nd November 2018** and having a share capital.

Requirement:

A declaration must be filed by a director in **Form INC-20A** within **180 days** of incorporation, stating that:

- Every subscriber to the memorandum has paid the value of the shares agreed to be taken.
- The company has verified its registered office (as per Section 12).

This declaration is submitted along with a bank statement showing the receipt of share application money.

V. Consequences of Non-Compliance with Section 10A

If the declaration is **not filed within 180 days**, the following consequences apply:

1. Penalties:

- Company: ₹50,000
- Every officer in default: ₹1,000 per day (maximum ₹1 lakh)

2. Restriction on Business Activity:

The company **cannot commence any business** or exercise borrowing powers until Form INC-20A is filed.

3. Strike-off by RoC [Section 248(1)(d)]:

If the declaration is not filed and the company fails to begin operations, the RoC may remove the name of the company from the register of companies.

VI. Distinction: Certificate of Incorporation vs. Commencement of Business

Basis	Certificate of Incorporation	Commencement of Business
Legal Reference	Section 7	Section 10A
Meaning	Legal recognition of a company	Permission to begin business operations
Applicability	All companies	Only to companies with share capital
Filing Requirement	Automatic upon registration	Form INC-20A within 180 days
Consequences of default	Company doesn't come into existence	Penalty + possible strike-off

VII. Conclusion

The **Certificate of Incorporation** is the foundational document that marks the legal birth of a company, ensuring its separate identity and legal status. However, under the Companies Act, 2013, companies with share capital must also fulfill an additional obligation under **Section 10A** to commence business. This dual-layer compliance mechanism ensures that shell companies are discouraged and genuine commercial activity is verified through actual capital contribution.

Doctrine of Constructive Notice

1. Introduction

• The Doctrine of Constructive Notice is a legal concept in Company Law that protects companies from the claims of outsiders who act without proper diligence.
• It is based on the principle that certain company documents are public documents, and therefore, it is assumed that everyone dealing with the company has read and understood them.

- The doctrine ensures transparency and accountability in corporate transactions and protects the company from fraudulent or negligent dealings.

2. Legal Basis

• The doctrine arises from Section 399 of the Companies Act, 2013, which allows public access to the documents filed with the Registrar of Companies (ROC).

- Key documents like the Memorandum of Association (MOA) and Articles of Association (AOA) are considered to be "constructively known" by outsiders, even if they have not actually read them.

3. Meaning of Constructive Notice

• "Constructive notice" means presumed knowledge, not actual knowledge.
• Any person dealing with a company is presumed to have inspected the public documents of the company and to have known the content of those documents.

- This presumption is irrefutable in law and applies to all persons dealing with the company.

4. Purpose and Justification

• The doctrine is meant to ensure that third parties exercise due diligence before entering into contracts with a company.
• It helps protect the company from being bound by unauthorized acts or actions taken outside the scope defined in the MOA or AOA.

- It also discourages negligence and prevents outsiders from pleading ignorance of the company's internal rules.

5. Application of the Doctrine

- This doctrine applies to all documents filed with the ROC, especially:

◦ Memorandum of Association (MOA) – which defines the scope and object of the company.
◦ Articles of Association (AOA) – which lay down the internal rules of management.

• Outsiders dealing with the company are expected to verify whether:
◦ The person acting on behalf of the company has the authority to do so.
◦ The company is legally empowered to enter into the contract.

6. Legal Effect

• If an outsider enters into a contract that goes beyond the powers in the MOA or is inconsistent with the internal regulations in the AOA, the company is not bound by that contract.

- The outsider cannot claim ignorance and is presumed to have constructive notice.
- This doctrine favors the company and may operate harshly against third parties.

7. Landmark Case Laws

i) Kotla Venkataswamy v. Ramamurthy (1934)

• A secretary of a company signed a contract without the signatures of the two required directors as per the Articles.

• Held: The company was not bound by the contract because the plaintiff was deemed to have constructive notice of the requirement of two directors' signatures.

ii) Ernest v. Nicholls (1857)• A third party was presumed to have knowledge of restrictions placed in the company's Articles.

- The company was held not liable for unauthorized acts.

8. Criticism of the Doctrine

• The doctrine is considered unfair to outsiders, especially when internal irregularities are not easily discoverable.

• It imposes an unrealistic burden on third parties to verify not only public documents but also compliance with internal processes.

- It is sometimes regarded as rigid and outdated, particularly in modern commercial transactions.

9. Exceptions: Doctrine of Indoor Management

• To soften the harshness of the constructive notice doctrine, the courts have evolved the Doctrine of Indoor Management, which protects outsiders dealing in good faith.

• According to this exception, outsiders are not expected to verify internal proceedings of the company, only public documents.

- Thus, if the act is within the MOA/AOA but there is a lapse in internal procedure, the company is still bound.

10. Conclusion

• The Doctrine of Constructive Notice plays a crucial role in safeguarding companies against unauthorized or ultra vires transactions.

• However, it must be balanced with the Doctrine of Indoor Management to ensure fairness to external parties.

- While it promotes diligence, modern business practices may demand a more equitable application of the doctrine to avoid injustice.

Doctrine of Indoor Management

1. Introduction

• The Doctrine of Indoor Management is an important exception to the Doctrine of Constructive Notice.

• While constructive notice assumes that an outsider knows the contents of public documents like the MOA and AOA, the doctrine of indoor management protects outsiders from being adversely affected by internal irregularities of the company.

• First laid down in the landmark case Royal British Bank v. Turquand (1856), this doctrine facilitates fair and secure dealings with companies.

2. Meaning and Rationale

• The doctrine states that people dealing with a company in good faith are entitled to assume that the internal requirements or procedures laid down in the company's Articles have been properly complied with.

• Outsiders are not expected to investigate the internal management processes of the company.

• This rule promotes commercial convenience and fairness.

3. Origin: Royal British Bank v. Turquand (1856)

• In this case, a company borrowed money and issued bonds without passing the resolution required by its Articles.

• The outsider relied on the apparent authority of directors.

• The court held that the outsider was not bound to verify internal resolutions and that the company was liable.

• This case established the foundation of the indoor management doctrine.

4. Purpose and Utility

• Protects innocent third parties who deal with companies in good faith.

• Ensures that internal lapses or procedural defaults by officers do not unfairly penalize outsiders.

• Encourages smooth and secure commercial transactions.

• Balances the strictness of constructive notice with fairness in company dealings.

5. Scope of the Doctrine

• Applies where:

◦ The outsider has acted in good faith.

◦ The outsider has relied on apparent authority.

◦ The act is not ultra vires the company.

• Not applicable where the outsider is aware of the irregularity, or should have suspected it.

6. Examples of Application

• If the Articles state that a document must be signed by two directors and it is signed by one director and the company secretary, the outsider may presume proper internal authorization, unless they had reason to doubt it.

• If a board resolution is required for a transaction, the outsider is not bound to confirm that it was actually passed, unless suspicion exists.

7. Exceptions to the Doctrine

The Doctrine of Indoor Management does not apply in the following situations:

a) Knowledge of Irregularity

• If the outsider knows that the internal procedure was not followed, they cannot claim protection.

• Example: If a person knows that no resolution was passed but still enters into a contract, the doctrine won't apply.

b) Suspicion of Irregularity

• If the circumstances are suspicious, the outsider is expected to make proper inquiry.

• Failing to do so disqualifies them from protection.

• Case: Anand Bihari Lal v. Dinshaw & Co. – a company manager transferred property, which he had no authority to do. The transaction was held invalid.

c) Forgery

• The doctrine does not apply to forged documents or signatures.

• Forgery is a nullity in law and cannot bind the company.

• Case: Ruben v. Great Fingall Consolidated (1906) – a company secretary forged the signature of directors. Held: Company was not liable.

d) Acts Ultra Vires the Company

• If the act is beyond the powers of the company as per the MOA, this doctrine will not apply.

8. Landmark Case Laws

i) Royal British Bank v. Turquand (1856)

• Established the principle that outsiders can presume compliance with internal procedures.

ii) Lakshmi Ratan Cotton Mills v. J.K. Jute Mills (1957)

• Company manager borrowed money for the company.

• It was presumed that proper authorization existed, and the company was held liable.

iii) Ruben v. Great Fingall Consolidated (1906)• Forged signature case; court held the company not liable as indoor management doesn't apply to forgery.

9. Comparison with Constructive Notice

Aspect	Constructive Notice	Indoor Management
Favours	The company	Outsiders
Presumption	Outsiders must know MOA/AOA.	Internal rules are followed
Purpose	Protects company from unauthorized acts	Protects outsiders from internal lapses
Effect	Strict, harsh on outsiders	Liberal, fair to third parties

10. Conclusion

• The Doctrine of Indoor Management is a vital protective measure for outsiders transacting with companies.

• It helps balance the harshness of constructive notice by ensuring that companies are liable for their internal failures when third parties act in good faith.

• While the doctrine has its exceptions, it remains a cornerstone of fair corporate dealings and is essential for the security and efficiency of commercial transactions.