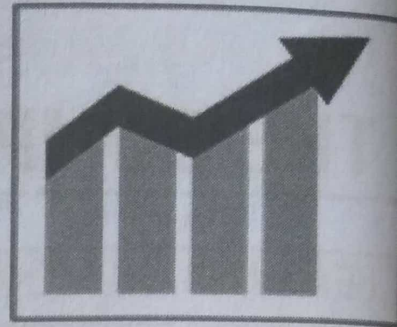


INTRODUCTION

The Companies Act, 2013 was enacted to consolidate and amend the law relating to the companies. The Companies Act, 2013 was preceded by the Companies Act, 1956.

Due to changes in the national and international economic environment and to facilitate expansion and growth of our economy, the Central Government decided to replace the Companies Act, 1956 with a new legislation. The Companies Act, 2013 contains 470 sections and seven schedules. The entire Act has been divided into 29 chapters. A substantial part of this Act is in the form of Companies Rules. The Companies Act, 2013 aims to improve corporate governance, simplify regulations, strengthen the interests of minority investors and for the first time legislates the role of whistle-blowers and provisions relating to class action suit. Thus, this enactment seeks to make our corporate regulations more contemporary.



Applicability of the Companies Act, 2013:

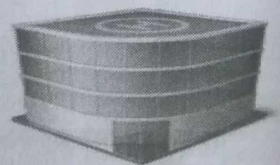
The provisions of the Act shall apply to-

- 1 ♦ Companies incorporated under this Act or under any previous company law.
- 2 ♦ Insurance companies (except where the provisions of the said Act are inconsistent with the provisions of the Insurance Act, 1938 or the IRDA Act, 1999)
- 3 ♦ Banking companies (except where the provisions of the said Act are inconsistent with the provisions of the Banking Regulation Act, 1949)
- 4 ♦ Companies engaged in the generation or supply of electricity (except where the provisions of the above Act are inconsistent with the provisions of the Electricity Act, 2003)
- 5 ♦ Any other company governed by any special Act for the time being in force.
- 6 ♦ Such body corporate which are incorporated by any Act for time being in force, and as the Central Government may by notification specify in this behalf.



1. COMPANY: MEANING AND ITS FEATURES

Meaning: According to Chief Justice Marshall, "a corporation is an artificial being, invisible, intangible, existing only in contemplation of law. Being a mere creation of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as accidental to its very existence."



In the words of professor Haney "A company is an incorporated association, which is an artificial person created by law, having a separate entity, with a perpetual succession and a common seal." This definition sums up the meaning as well as the features of a company succinctly.

However, the Act defines the term company a bit differently. Section 2(20) of the Companies Act, 2013 defines the term 'company'. "Company means a company incorporated under this Act or under any previous company law". As we shall progress under the chapter, the meaning of the term company will be understood by the students.

Features of a Company

Separate Legal Entity

- ♦ Legally separate from the members

Perpetual succession

- ♦ Change in members does not affect existence of Company

Limited Liability

- ♦ Liability of Company different from liability of members

Artificial Juridical Person

- ♦ Company can act through human agency only
- ♦ Company can contract, sue and be sued in its own name

We have seen the definition given to company from a layman's point of view and legal point of view. But the company form of organization has certain distinctive features that help us to understand the realms of a company. Following are the main features:

↓ **Separate Legal Entity:** There are distinctive features between different forms of organisations and the most striking feature in the company form of organisation vis-à-vis the other forms of business organisations is that it acquires a unique character of being a separate legal entity. In other words, when a company is registered, it is clothed with a legal personality. It comes to have almost the same rights and powers as a human being. Its existence is distinct and separate from that of its members. A company can own property, have bank account, raise loans, incur liabilities and enter into contracts. MCA 21

- (a) It is at law, a person which is different from the shareholders subscribers to the memorandum of association. Its personality is distinct and separate from the personality of those who compose it.
- (b) Even members can contract with company, acquire right against it or incur liability to it. For the debts of the company, only its creditors can sue it and not its members. A company is capable of owning, enjoying and disposing of property in its own name. Although the capital and assets are contributed by the shareholders, the company becomes the owner of its capital and assets. The shareholders are not the private or joint owners of the company's property.

[A member does not even have an insurable interest in the property of the company. The leading case on this point is of Macaura v. Northern Assurance Co. Limited (1925).]

Fact of the case

shareholder → Macaura (M) was the holder of nearly all (except one) shares of a timber company. He was also a major creditor of the company. M insured the company's timber in his own name. The timber was lost in a fire. M claimed insurance compensation. Held, the insurance company was not liable to him as no shareholder has any right to any item of property owned by the company, for he has no legal or equitable interest in them.

- II **Perpetual Succession:** Members may die or change, but the company goes on till it is wound up on the grounds specified by the Act. The shares of the company may change hands infinitely but that does not affect the existence of the company. 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 1: Many companies in India are in existence for over 100 years. This is possible only due to the fact that the company has perpetual existence. 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.

- III **Limited Liability:** The liability of a member depends upon the kind of company of which he is a member. We know that company is a separate legal entity which is distinct from its members.

- (i) Thus, in the case of a limited liability company, the debts of the company in totality do not become the debts of the shareholders. The liability of the members of the company is limited to the extent of the nominal value of shares held by them. In no case can the shareholders be asked to pay anything more than the unpaid value of their shares.
- (ii) In the case of a 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.
- (iii) However, if it is an unlimited company, the liability of its members is unlimited as well.

IV **Artificial Legal Person:**

- (1) A company is an artificial person as it is created by a process other than natural birth. It is legal or judicial as it is created by law. It is a person since it is clothed with all the rights of an individual.
- (2) Further, the company being a separate legal entity can own property, have banking account, raise loans, incur liabilities and enter into contracts. Even members can contract with company, acquire right against it or incur liability to it. It can sue and be sued in its own name. It can do everything which any natural person can do except be sent to jail, take an oath, marry or practice a learned profession. Hence, it is a legal person in its own sense.
- (3) As the company is an artificial person, it can act only through some human agency, viz., directors. The directors cannot control affairs of the company and act as its agency, but they are not the "agents" of the members of the company. The directors can either on their own or through the common seal (of the company) can authenticate its formal acts.
- (4) Thus, a company is called an artificial legal person.

- V **Common Seal:** (A company being an artificial person is not bestowed with a body of a natural being. Therefore, it works through the agency of human beings. 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 common seal is a seal used by a corporation as the symbol of its incorporation.)

The Companies (Amendment) Act, 2015 has made the common seal optional by omitting the words "and a common seal" from Section 9 so as to provide an alternative mode of authorization for companies who opt not to have a common seal. Rational for this amendment is that common seal is seen as a relic of medieval times. Even in the U.K., common seal has been made optional since 2006. This amendment provides that the documents which need to be authenticated by a common seal will be required to be so

2 Directors
10 Directors &
1 CS

done, only if the company opts 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.

2. CORPORATE VEIL THEORY

Curtain
 Corporate Veil: Corporate Veil refers to a legal concept whereby the company is identified separately from the members of the company.

The term Corporate Veil refers to the 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. In other words, they enjoy corporate insulation.

Thus, the shareholders are protected from the acts of the company.

The Salomon Vs. Salomon and Co Ltd. laid down the foundation of the concept of corporate veil or independent corporate personality.

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 £ 1 share each. Subsequently, the company went into liquidation due to general trade depression. The unsecured creditors to the tune of £ 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. It was held by Lord Mac Naughten:

"The Company is at law a different person altogether from the subscribers to the memorandum, and though it may be that after incorporation the business is precisely the same as it was before and the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustees for them. Nor are the subscribers, as members, liable, in any shape or form, except to the extent and in the manner provided by the Act."

Thus, this case clearly established that 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.

Now, the question may arise whether this Veil of Corporate Personality can even be lifted or pierced.

Before going into this question, one should first try to understand the meaning of the phrase "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 or managers, the corporate veil may be said to have been lifted. Only in appropriate circumstances, the Courts are willing to lift the corporate veil and that too, when questions of control are involved rather than merely a question of ownership.

(ii) Lifting of Corporate Veil: The following are the cases where company law disregards the principle of corporate personality or the principle that the company is a legal entity distinct and separate from its shareholders or members:

(1) To determine the character of the company i.e. to find out whether co-enemy or friend: In the law relating to trading with the enemy where the test of control is adopted. The leading case in this point is Daimler Co. Ltd. vs. Continental Tyre & Rubber Co., if the public interest is not likely to be in jeopardy, the Court may not be willing to crack the corporate shell. But it may rend the veil for ascertaining whether a company is an enemy company. It is true that, unlike a natural person, a company does not have mind or conscience; therefore, it cannot be a friend or foe. It may, however, be characterised as an enemy company, if its affairs are under the control of people of an enemy country. [For this purpose, the Court may examine the character of the persons who are really at the helm of affairs of the company.]

(2) To protect revenue/tax: In certain matters concerning the law of taxes, duties and stamps particularly where question of the controlling interest is in issue. [S. Berendsen Ltd. vs. Commissioner of Inland Revenue]

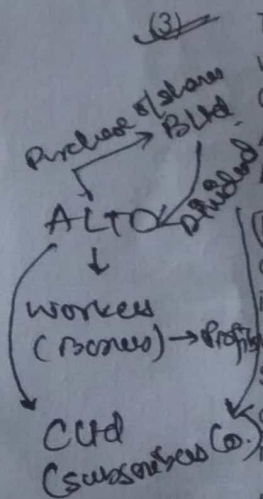
(i) Where corporate entity is used to evade or circumvent tax, the Court can disregard the corporate entity [Juggilal vs. Commissioner of Income Tax AIR (SC)].

(ii) In [Dinshaw Maneckjee Petit], it was held that the company was not a genuine company at all but merely the assessee himself disguised under the legal entity of a limited company. The assessee earned huge income by way of dividends and interest. So, he opened some companies and purchased their shares in exchange of his income by way of dividend and interest. This income was transferred back to assessee by way of loan. The Court decided that the private companies were a sham and the corporate veil was lifted to decide 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 Supreme Court upheld the piercing of the veil to look at the real transaction (The Workmen Employed in Associated Rubber Industries Limited, Bhavnagar vs. The Associated Rubber Industries Ltd., Bhavnagar and another).

Workmen of Associated Rubber Industry Ltd., v. Associated Rubber Industry Ltd. The facts of the case are that "A Limited" purchased shares of "B Limited" by investing a sum of ₹ 4,50,000. The dividend in respect of these shares was shown in the profit and loss account of the company, year after year. It was taken into account 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. Thus, the Supreme Court brushed aside the separate existence of the subsidiary company. 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 so as 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.)

In the case of Merchandise Transport Limited vs. British Transport Commission (1982), a transport company wanted to obtain licences for its vehicles, but could not do so if applied in its own name. It, therefore, formed a subsidiary company, and the application for licence 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 licences 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*]

