Incorporation of Company

- Before a Company is formed certain preliminary Decisions are necessary.
- For example whether it should be a Private Company or a Public Company
- What should be it's Capital etc.
- All these decisions are taken by the group of people known as promoters.
- They do all the necessary preliminary work incidental to the formation of a Company

Mode of forming incorporated Company

- A Company Limited by Shares
- A Company Limited by Guarantee
- An Unlimited Company

Incorporation of Company

- The following documents have to be filed with the Registrar of Companies under whose jurisdiction the registered office of the Company falls
- The memorandum and articles of association
- A declaration by an advocate, CA or CS in practice in prescribed format along with Director or Secretary of the Company that all the requirements relating to the formation of the Company has been complied with.

- An affidavit by the subscribers to the memorandum that they are not convicted of any offence.
- The address for correspondence till the regd. office is formed
- The particulars of name, surname, address, nationality etc. of the subscriber to the Memorandum
- The Particulars relating to the first directors of the Company
- And the particulars of the first Directors in the Company.

- The registrar on the basis of the documents and information filed as mentioned before issue a certificate of incorporation in the prescribed form to the effect that the proposed company is incorporated under the act.
- A Certificate of incorporation issued by the Registrar of Companies is a conclusive evidence that all the requirements of the Companies Act have been complied with in respect of registration.

Memorandum of Association

- Memorandum means the Memorandum of Association of a Company as originally framed or as altered from time to time in pursuance of any previous company law or of this act [Sec.2(56)]

Contents of Memorandum

- Name Clause
- Registered office Clause
- Objects Clause
- Capital Clause
- Liability Clause
- Association Clause

Doctrine of Ultra Vires

- A Company has the power to do all such things as are-

1. Authorised to do by the Companies Act,2013
2. Essential to the attainment of its objects specified in the Memorandum
3. Reasonably and fairly incidental to it's objects

4. Everything else done by the Company is ultra vires the Company

5.Ultra means beyond and vires means powers

The purpose of these restrictions is to protect

1.Investors in the Company so that they may know the in which their money is to be employed, and

2.Creditors by ensuring that the Company's funds are not wasted in unauthorized activities

Leading Case

- Ashbury Rly.Carriage & Iron Company Ltd. Vs. Riche

Articles of Association

- Contents of Articles

1.Share Capital and variation of Rights
2.Lien
3.Call on shares
4.Transfer of Shares
5.Forfeiture of Shares
6.Transmission of Shares
7.Alteration of Capital
8.Capitalisation of Profits

9. Buy Back of Shares
10. General Meetings
11. Proceedings at Meetings
12. Adjournment of Meetings
13. Voting Rights
14. Proxy
15. Board of Directors
16. Proceedings of the Board
17. Chief Executive Officer, Manager, Company Secretary and CFO

18.The Seal

19 .Dividends & Reserves

20 . Accounts

21.Winding-up

Relation between Articles and Memorandum

- 1. The Articles are Subordinate to Memorandum
- 2.The Memorandum must be read in conjunction with Articles
- 3.The terms of Memorandum cannot be modified or controlled by the Articles

- **1.Relation between Members and Company**: The Memorandum and the Articles create a binding contract between the members and the Company.
- In the case of **Borland's Trustee v. Steel Bros.& Co. Ltd.** the Articles of the Company as altered provided that the shares of any member who become bankrupt should be sold to certain persons at a fair price. B, a shareholder, became bankrupt and his trustee in bankruptcy claimed that he was not bound by the altered Articles. It was held that as the Articles were a personal contract between B and the rest of the members hence B and his trustees were bound.

- **2.Rights of Members for Ultra Vires Act:** A Company is bound to the members for their individual rights. A Company can exercise its rights only in accordance with the provisions of the Memorandum and Articles. A member can obtain an injunction restraining the Company from doing an Ultra Vires Act.
- In the case of **Wood v Odessa Waterworks Co.**, the Articles of the Company provided that the directors may, with the sanction of the Company at general meeting, declare a dividend to be paid to the members. A resolution was passed to give the shareholders debenture bonds instead of paying the dividends in cash. It was held that the words to be paid, meant to be paid in cash and a shareholder can restrain the company from acting on the resolution on the ground that it contravenes the Articles.

- **3.Relation between Members**: The Memorandum of Association and the Articles of Association constitute a Contract between the members. Each member is bound to the other members through these documents.

- **4.Relation between Company and Outsiders**: As per the law of contract a stranger to a contract cannot acquire any right under the contract. Hence an outsider cannot take advantage of the Article and make a claim against the Company.
- In the case of **Eley v. Positive Govt. Security Life Ass.Co.,** the Articles of a Company provided that Eley should be the solicitor of the Company for life and could be removed from office only in case of misconduct. Eley accepted the offer and later on became a Shareholder. As a shareholder he could have access to the Articles. After a period of time Eley was removed from the office without any misconduct. Eley sued the company based on the provisions of the Articles. It was held that the Articles do not create a contract between the Company and the outsider and hence no action lies against the Company.

- **Constructive Notice of Memorandum and Articles**: Memorandum of Association and the Articles of Association assume the character of public document as soon as they get registered with the Registrar. Hence every outsider dealing with the Company is expected to be aware of the contents of the Memorandum of Association and Articles of Association. This is known as the constructive notice of Memorandum and Articles.

The Doctrine of Indoor Management is an exception to the rule of Constructive Notice. As per this doctrine if an outsider enters into a transaction with the Company without contravening the provisions of the Memorandum and the Articles, he can presume that everything is regular in his transaction and there is no irregularity. The Company cannot escape the liability arising from the outside party because of internal irregularity.

Royal British Bank Vs. Turquand: In the case of Royal British Bank v. Turquand the directors of the Company had issued a bond to Turquand. They were empowered by the articles to issue such bonds provided they were authorised by a resolution passed by the shareholders at a general meeting of the Company. However, no such resolution was passed by the Company. It was held that Turquand could recover the amount of the bond from the Company as he could assume the resolution to have been duly passed regarding issuance of such bond to him.

Exceptions to the Doctrine of Indoor Management

- **1.Knowledge of Irregularity**: Where an outsider dealing with a Company had the actual or constructive notice of the irregularity regarding internal management, he is not entitled to the benefits under the rule of indoor management.
- **2.Negligence**: Where it is possible on the part of an outsider to have knowledge of the internal management but he fails to enquire the Doctrine of indoor management is not applicable in such case.

- **3.Forgery**: This doctrine is not applicable in those cases where the person entering into a contract with the Company relies on the basis of a forged document. Thus, a Company can never be held responsible for the forgery committed by any of its officers.
- **4.Acts outside the scope of apparent authority**: If an outsider enters into a contract with an officer of a Company for a transaction, which is beyond the authority bestowed on the officer the Company will not be held responsible for such acts.

Lifting of the Corporate Veil

- A company is incorporated as a separate legal entity and is distinct from the members forming such company. It means the company has a corporate personality as different from the members. This is confirmed by the courts in the case of Salomon v Salomon & Co. Ltd.

- Thus, there lies a fictional veil between the company and its members. However, in order to find the real culprit when a fraud is committed or a tax evasion takes place or for any other improper conduct made by a company it may become necessary for the courts and other relevant authorities to lift the corporate veil and to look at the persons responsible for such fraud or improper conduct

- Thus, in the following cases the corporate veil may be lifted.
- **(i)Protection of revenue:** The courts may ignore the principle of separate entity where the objective of the company is the evasion of tax. In the case of **Sir Dinshaw Maneckjee Petit**, Dinshaw the assessee, formed four private companies to which the dividend income and interest income received by him was transferred in order to evade taxes. Later on, these companies were transferring these amounts to Dinshaw and was showing as loan amount. It was held that these companies were nothing but the assessee himself as they had no other business but to receive dividends and to transfer it to assessee.

- **(ii) Prevention of Fraud or improper Conduct**: The veil of the company may be pierced where such veil is used for some fraudulent purposes like defrauding the creditors or avoidance of law.
- **(iii) To determine the enemy characteristics of a Company**: At times the corporate veil is lifted to find out whether the persons having the controlling stake in the company are the residents of an enemy country.

- **(iv) Where the Company formed is a Sham**: The courts can lift the veil, when they are of the opinion that the main objective of the company is to create a cloak around the members forming it. In the case of **Gilford Motor Co Ltd. V Horne**, Horne was a former employee of the company and as per the terms of employment, he was not allowed to solicit its customers after the service period. In order to override this clause, he formed a company through which he solicited the customers of the company. It was held that Horne is not allowed to do so as the company is nothing but a sham or cloak.

- (v) Where the main objective of company formation is to avoid legal obligation in such cases the court may lift the corporate veil.
- (vi) Further the court may lift the veil, where the objective is to avoid welfare legislation

The court may also lift the corporate veil where there is violation of statutory obligation. Some of these reasons are as follows:

- **(i) Where the number of members fall below statutory minimum:** As per section 45 of the companies act,2013 where the number of members of a company falls below the statutory minimum, i.e., two in case of a private limited company and seven in case of a public limited company and the company carries on it's business for a period of more than six months ,then such members who have the information regarding this fact and continue as members will be liable for the debt conducted during such period.

- (ii) **Failure to refund the application money**: As per section 69(5) of the companies act,2013 the directors of the company shall be liable personally for the repayment of application money, if the company fails to repay the application money to the persons who have not been allotted shares in the company within 130 days from the date of the issue of prospectus.
- (iii**) Misdescription of Company name**: Where an officer or an agent of the company enters into a contract without properly and fully writing the name of the company, such officer or agent will be personally liable in such cases.

- (iv) **For fraudulent trading**: As per section 542 of the companies act, where in the course of winding up of a company it comes to the notice that some business or transaction of the company has been carried out with the sole objective of defrauding the creditors, then in such cases the court may held such person liable who knowingly were parties to such business.
- (v) **In case of Subsidiary Company**: In case of violation of the provisions the court may treat a subsidiary company as a branch or department of the holding company.