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UNIVERSITY OF JAMMU

JAMMU

SELF LEARNING MATERIAL

PGDBM - Ist SEMESTER

PAPER : IV **UNIT : I - VI**

Subject : LEGAL ASPECTS OF BUSINESS

Course Co-ordinator

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LEGAL ASPECTS OF BUSINESS

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PGDBM SEMESTER-I

Course Title : Legal Aspects of Business **Total Marks : 100**
Paper: IV **Internal Assessment : 20**
Contact Hours: 45 **Semester Examination : 80**
Duration of Examination : 3 hours

Objective :
The course has been design to know about business laws in the country

UNIT I

a) Business Industry and Commerce; Forms of Business
b) Business Ethics

UNIT II

a) Business Laws in India. The Indian Contract Act
b) Law of sale of Goods; Contract of Sale; Formation of the Contract

UNIT-III

a) Company Law; Types of Companies; Incorporation of Companies; Memorandum of Association; Article of Association

b) Prospectus; Issue of Capital, Shares and Share Capital; Kinds of Share

UNIT IV

a) E-Filling; Company Law in a computerise environment; Digital Signature Certificate; Director Identification Number; Corporate Identity Number

b) The Limited Liability Partnership Act, 2008; Meaning and Nature of Limited Partnership Formation of LLP

UNIT-V

a) Consumer Protection Act; Consumer Rights

b) Securities and Exchange Board of India; Stock Exchanges

NOTE FOR PAPER SETTER:

The Question Paper shall contain two questions from each Unit (Total 10 Questions) and the candidates shall be required to answer one question from each unit (total number of questions to be attempted shall be five, i.e. there shall be internal choice within each unit)

SUGGESTED READINGS:

1. N. D. Kapoor, Elements of mercantile Law, Sultan Chand and Company, India.
2. P. K. Goel, Business Law for Managers, Bizentra Publishers, India
3. Akhileshwar Pathack, Legal Aspects of Business, 4th Edition, Tata McGraw Hill
4. Kuchhal, M.C. and Deepa Parkash, Business Legislation Management, Vikas Publishing House Pvt. Ltd.
5. Kuchhal, M.C. Business Law, Vikas Publishing House, New Delhi.

LEGAL ASPECTS OF BUSINESS

SEMESTER - I **UNIT-1**
PAPER -IV **LESSON-1**

STRUCTURE

1.1 INTRODUCTION

Business, like any human body, has its own problems which have to be understood, analysed and resolved by those responsible for managing it, we may proceed in the fashion of the physician who has to understand the structure and working of human body before he can venture to diagnose ills and prescribe remedies.

Before a person starts practicing medicine and surgery, he has to acquire sufficient knowledge about the structure of the body, the functions of different organs, the processes by which these organs perform their functions in co-ordination with others, the inter-relationship among different body organs, the external conditions in which the human body is to survive and grow and the responses which are made by the body to adapt itself to its environments. Similarly, a person can hope to understand and tackle problems of business properly only if he has some knowledge of the business world, business activity and its organisation and the relationship of business with the world around it.

Human Occupations

Human life is built around work. Whether one likes it or hates it, work is an essential part of life. Numerous and varied are the activities that a man undertakes during his life-time and long indeed is the list of the roles that he has to play in the theatre of life. We may well leave it to the students of sociology and psychology to go into these and mark the various patterns of human behaviour. But we know it from our experience as also from that of others around us that all activities of man fall into two categories.

In the first category come all those acts and activities of man which are inspired by love, patriotism, sympathy, humanity and similar sentiments. A housewife's cooking for her family, a man's sacrifice for the country, his work for the uplift of Harijans and his visits to the temple for the day's prayers are all examples of human actions of the first type. Though important, these are outside the scope of the present discussion. Here, we are concerned with the second category of human activities which is related to the production and exchange of wealth. In Economics, we call these economic activities. All of them involve working to earn a livelihood and are usually called occupations. A lawyer goes to the court, a teacher to the school or college, a government servant to his office, an employee to his work-place, a factory worker to his factory, and a factory owner to his office in the factory to earn a living by producing wealth in different forms. These are all instances of human occupations. If we look at the whole range of human occupations, we can classify these under the following categories

Profession

Professions are those occupations which involve the rendering of personal services of a special and expert nature. A lawyer who practises the legal profession takes up cases and offers his technical advice and specialised services for suitable payment. So do the chartered accountant and the medical practitioner. Since specialised services have to be rendered by professional persons, they have to satisfy the minimum academic and other qualifications prescribed by law or by the association to which they must belong in order to be able to practise their profession. Such requirements exist for lawyers, engineers, doctors, etc., who practise professions as their occupation.

Employment

In this class of occupations, a person has to work under an agreement or rules of service and perform such work as may be assigned to him by the employer. Remuneration for such work takes the form of wages or salaries and allowances. Sometimes people belonging to professions take up employment with the Government or private agencies. Firms employ chartered accountants and hospitals engage doctors and in regular services.

Business

As an economic activity, business is so familiar to us that it seems almost funny to go back to its literal meaning of 'being busy'. All occupations require a person to be busy but what really matters for a proper understanding of business is what keeps him busy. Business is known to us by the institutions that conduct it and, therefore, we may try to mark its essential characteristics by examining the nature of work performed by some of them. The village farmer who tills his land and sells his produce, the village shoe-maker who makes shoes to order, the various kinds of shops in the market in the rural and urban areas dealing in various articles and commodities in demand, the restaurants that cater to the needs of different classes of population, the banks, insurance companies, transporters' cold storage companies, theatres and the line-selling services, the factories turning out manufactured goods of all kinds required by consumers

and producers are some examples of business firms familiar to us all. Some of them are working on a small scale and making both ends meet. Some others are functioning on a large scale and are providing livelihood to thousands. Some are owned and controlled by individuals, some others by groups of private individuals, and yet others by the Government.

1.2 OBJECTIVES

After going through this lesson, you should be able to:

- Understand the concept of business
- Identify the various components of business

1.3 CHARACTERISTICS OF BUSINESS

(i) Sale, transfer or exchange for the satisfaction of human needs: It will be noted that all business activities are, directly or indirectly, concerned with the transfer or exchange of goods and services for value. Production or purchase of goods or services for personal consumption or presentation ex-gratia (free of charge) are obviously outside the scope of business, for there is no sale or transfer for value involved in them. If, for instance, a person cooks at home for personal consumption, if is not business, for it does not entail any transfer for value or exchange. But when a person cooks for those who patronize his restaurant and pay for their meals, it becomes his business. The ultimate object of production and sale is to meet some felt need of the people in the community

(ii) Dealings in goods and services: Business consists in dealings in goods and services. The goods produced or acquired for business purposes may be consumers' good like cloth, shoes, crockery, etc., or producers' goods like tools and machinery. Services are those intangible and invisible goods supplied by business concerns which cannot be stored by the consumer. Concerns supplying electricity, water or gas, or those engaged in transportation of goods and passengers, deal in services and are business concerns like those dealing in tangible goods.

(iii) Recurrence of transactions: Properly speaking, the term business should be reserved for the exchange of goods and services undertaken continually or at least recurrently. If a person sells his radio set and gains thereon, it does not constitute business. But, if he keeps a stock of such sets and conducts a series of such deals it will be his business. The profit motive is an important distinguishing feature of business. Business is a human activity directed towards the acquisition of wealth. All business consists in an attempt on the part of men to reap more than what has been expended or invested. If a business enterprise despairs of making a profit in a particular line or dealing, it is likely to turn to another field which brings back something over and above what was initially invested. This will be true even of Government-run business in the long run. This is not to undermine or be little the importance of the element of service in business activity. In fact, business activity will flourish and its object will be realised only when it is able to serve the community to its satisfaction

(v) Element of risk. Risk means the possibility of loss. It arises out of the uncertainty that goes with the profit expected from a business activity. Profit generally depends not only upon the efforts of the business enterprise but also upon a number of other factors over which it has little or no control. These factors include:

(a) Changes in technology,

(b) Changes in consumer tastes and fashions,

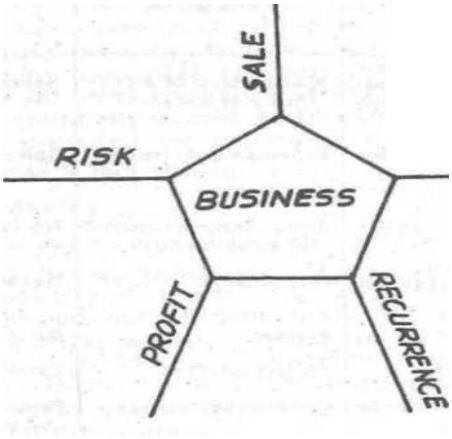
(c) Wrong management decisions about use of capital and other resources,

(d) Labour trouble,

(e) Shortage of raw materials,

(f) Increase in competition in the market.

(g) Fire, theft or natural causes (these can be shifted to insurers)



Characteristics of Business

Thus, business may be defined as the organised production of sale of goods undertaken with the object of earning profits through the satisfaction of human want

Business , Profession and Employment

FACTORS	BUSINESS	PROFESSION	EMPLOYMENT
Formal basis for establishment or commencement.	Individual decision plus registration formalities where required by law	Membership of a professional body	Service contract
Qualification	Specialized knowledge not found in all cases	Expertise and training in a specific field necessary	Specialised knowledge not necessary in all cases
Capital	Capital requirement varies according to scale	Some amount required for establishment	No capital required
Transfer of interest	Transfer possible with required formalities	Not possible	Not transferable
Individual risk	Present	Present	None
Return	Profit or a share thereof	Professional fee	Salary
Nature of work	Goods and services provided to individuals and groups	Personalised service	Performing work assigned by superiors

Interrelationship of Business, Profession and Employment

Although business as an activity is distinguished from profession and employment mainly on account of factors of investment and risk, yet one cannot forget the important role played by professional experts and employees in the success of modern business. Professionals of various types like consulting engineers, chartered accountants, cost accountants, management consultants, legal experts, doctors, architects and the like are retained by business firms for tackling a variety of complicated technical problems that go with modern large-scale business. Besides, large business firms employ a large number of specialists and experts in different areas on a regular basis. In fact, considering the expert knowledge that the conduct of modern business requires, management of business is becoming a professional job. As an economic institution of recognised importance, business provides employment to a large number of persons in the country. The prosperity of a business concern depends not merely on the foresight and the resources of businessmen, but is equally determined by the availability of the right type of employees with positive attitude towards work. Thus, while business provides opportunities for employment, the employees provide the organised and devoted effort which is essential for any business house to make the best of its investment..

1.4 DIVISIONS OF BUSINESS

Business activities may be classified into two broad categories : (a) Industry, and (b) Commerce. Industry involves the production of goods and materials, while commerce is concerned mainly with their distribution. Accordingly, then, a business concern the agency through which business is regularly conducted, may be an industrial/enterprise or a commercial one.

INDUSTRY

The term 'industry' refers to that part of business activity which concerns itself with the raising, production, processing or fabrication of products. The products of an industry may be used either by the final consumers or by another industrial undertaking for further production. Accordingly, these will be called

consumers' goods if used by final consumers, and producers 'goods or capital goods if used in the production of other goods. When a concern engages in the production of cloth or toothpaste, or when it processes cheese, it may be said to be producing consumers' goods. On the other hand, an engineering concern manufacturing machine tools and machinery is said to be producing producers' goods for the simple reason that these products will be used by factories for the production of certain other products. In some cases, an industrial concern may produce materials which will be further processed by yet other concerns, for conversion into finished consumers' goods. Such materials are generally placed in the category of intermediate goods.

Type of Industry

The broad sphere of industry may be divided into four distinct types :

(1) *Extractive industries:* These industries include activities whereby various forms of wealth are drawn out, extracted, or raised from the soil, air or water or obtained from beneath the surface of the earth. The commodities raised by such industries are produced with comparatively little assistance from man. The productsof extractive industries are generally meant to be used by the manufacturing and construction industries for producing finished goods though these may be used directly in some cases. These include hunting, fishing, mining, fruit-gathoring, agriculture, afforestation, etc.

(2) *Genetic industries:* These industries engage in reproducing and multiplying certain species of plants and animals with the object of earning profit from their sale. Examples of this type are nurseries multiplying and selling plants, cattle- breeding farms, poultry farms and commercial kennels.

(3) *Construction industries:* These industries involve construction of buildings, roads, dams, bridges, canals. The distinctive characteristic of these industries is that their products are not marketed in the

ordinary sense of being taken to the markets to be sold ; they are erected, built, or fabricated at a fixed site. These industries use the products of manufacturing industries, especially cement and iron and steal, as also those of extractive industries like quarries, etc.

(4) *Manufacturing industries:* Ordinarily, the term industry is used to refer to manufacturing industries. Though that is not correct, it cannot be denied that the bulk of our requirements is fulfilled by such industries. Manufacturing industries are engaged in the conversion or transformation of raw materials or semi-finished products into finished products. In this process, these industries create 'form utility.' The products of extractive industries generally becomathe raw materials of manufacturing industries. The cotton textile industry is an example of a manufacturing industry that makes use ot the- cotton produced by farms which are engaged in an extractive industry. Likewise, the iron and steel industry is concerned with the conversion of iron ore produced by mines (extractive industry) into pig iron, steel and various other products. Manufacturing industries may be divided further into the following categories :

(a) *Analytical:* In this type of industry, many types of products may be manufactured by analysing and separating different elements from the same material. For example, in the oil refinery industry, the crude oil is analysed and separated into petrol, diesel, gasoline, kerosene and lubricating oil.

(b) *Synthetic:* In synthetic industries various ingredients are put together and combined in the manufacturing process so as to manufacture a new product. For instance, cement is produced by combining and mixing concrete, gypsum, coal, etc.

(c) *Processing:* In this category are included those industries wherein the raw material is processed through different stages of production resulting in the fnal product. Textiles, paper and sugar are examples of this type.'

(d) *Assembly line* : 'Assembly line' type of industries include the industries where different instruments or component parts already manufactured are assembled to turn out new useful products, e.g., car, scooter, bicycle, television, etc.

Industries are also classified on the basis of size and investment as follows :

(e) *Heavy industries*: Tha term heavy industries is generally used to refer to those industries which call for big capital investment and have a longer production cycle. Such investment cioes mostly into" machinery and equipment of sophisticated and expensive type. Industries like iron and steel, aeronautics, ship-building and aluminium are included in this category.

(f) *Light Industries*: Light industries are those which involve a comparativelysmaller capital investment and have a short duration production cycle. This may bebecause of the less costly machinery required for the manufacture of certain types of products or because of the use of less sophisticated process of production.

Industries are also classified as large-scale and small-scale according to the capital employed, number of workers employed, materials and tools used and volume or value of output produced over certain periods.

Industries by the Type of Product (Official Classiflcatson)

Industries may also be classified by the type of product. Although the number of products manufactured by various industries is very large a standard classification of industries on this basis is given by the Government of India in the First Schedule to Industries (Development and Regulation), Act, 1951 for purposes like licensing and reporting of production and other statistics. This is as follows :

(i) Metallurgical industries including :

(a) Ferrous goods, e.g., iron and steel and ferro-alloys ; and between producers and consumers and, therefore, embraces all those functions which are essential for maintaining a free and uninterrupted flow of goods and services between them. The stream of goods and services starting from industry is beset with a number of hindrances, some of which are discussed below :

i) *Hindrances of person*: The basic problem of the producers is to find persons who will be interested in picking up for a fair price whatever has been produced by them. Commerce is primarily concerned with the establishment of contacts between producers and sellers'through trade. Trade on local and international markets may, therefore, be regarded as the core commerce.

ii) *Hindrances of exchange*: The goods produced by various industries are exchanged by them for money. Dealing in goods will naturally involve the question of the time and place of payment. When is money to be paid and how or in what form is it to be paid will be the important questions to be settled before transactions in goods can be completed. Commerce makes exchange of goods and services possible by removing these hindrances and solving these problems through the agancy of banks and other financial institutions. Banking should, therefore, be regarded as an important function of commerce and banks as essentia! commercial institutions.

iii) Hindrances of place. Producers and consumers are generally separated by varying distances. Commerce being concerned with establishing a contact between them naturally involves arranging for the transportation of goods from the production end to the consumption end. Not merely this, proper arrangements have to be made to cover the risks to which goods are exposed while in transit. Besides, proper packing will also have to be

arranged to protect products against possibilities of damage. Transportation, insurance and packing are, therefore, important functions of commerce concerned with the removal of difficulties relating to the transfer of goods from places where they are produced to the places where they are needed. Transport agencies (including railways, airlines, shipping companies, bus companies, etc.) as well as insurance companies (fire, marine and general) are, therefore, commercial institutions of no mean significance.

iv) *Hindrances of time*: Production and consumption, particularly in modern times, are separated not only by long distances but also by varying intervals of time. Since goods are produced in anticipation of demand, it becomes necessary to make suitable arrangements for their storage so that they can be made available o as and when needed by consumers. For this reason, warehousing is recognised, as yet another important function of commerce. Agencies and institutions operating warehouses are, therefore, commercial undertakings which form an integral part of the network of modern commerce.

v) *Hindrances of knowledge*: Exchange of goods which is the central function of commerce can be performed well only if the producers have opportunities of bringing their products to the notice of potential customers. This requires the proper organisation of advertising, publicity and selling campaigns. For this reason, advertising and publicity can also be included among functions of commerce. Therefore, advertising agencies are commercial concerns of importance.

To sum up, commerce may be defined as that part of business activity which seeks to facilitate ' exchange of goods by removing hindrances of person (through trade), hindrances of exchange (through banking), hindrances of place (through transportation, insurance and packing), hindrances of time (through warehousing) and hindrances of knowledge (through advertising, etc.). It could well be described as the sum total of all such activities and processes as make trade possible.

The important commercial activities revolving around trade are: (i) banking, (ii') transport, (iii) insurance, (iv) warehousing, (v) packing, and (vi) advertising

TRADE

Trade is not only an important part of commerce but is its nucleus. Trade refers to the sale, transfer or exchange of goods. It does not include the ancillary functions like transportation, insurance, banking, etc. which along with it, form part of commerce.

Types of Trade

Trade may be classified broadly into two categories :

(i) *Internal trade*: Also called horns trade, this consists in the sale and exchange of goods wihin the bounds of a nation. Payments for such sale are made in national currency directly or through the national banking system and the internal transportation system is utilised for the movement of goods. Internal or home trade may be conducted on either of the following bases :

(a) *Wholesale trade*: This involves the sale of goods in comparatively larger quantities to those traders who are in direct contact with the consumers. It serves as a link between the producers or manufacturers and the retail traders who sell direct to the consumers.

(b) *Retail trade*: This type of trade consists in the supply of the requirements of the consumers in the sm.ill quantities needed by them It provides the link between the wholesalers and the consumers.

(ii) International or foreign trade. This refers to the supply of the goods to buyers located in foreign countries. When goods are moved from one country to another, payments have to be converted into the currency of the other country and means of international transportation have to be used. Such trade is conducted mostly on wholesale basis. Foreign trade may be further divided into :

(a) Import trade, which consists in the procuring of foreign goods for home use.

(b) Export trade, which consists in the supply of home goods for foreign use.

(c) Entrepot trade, which effects the exchange of goods between foreign producers and foreign consumers the textile industry.

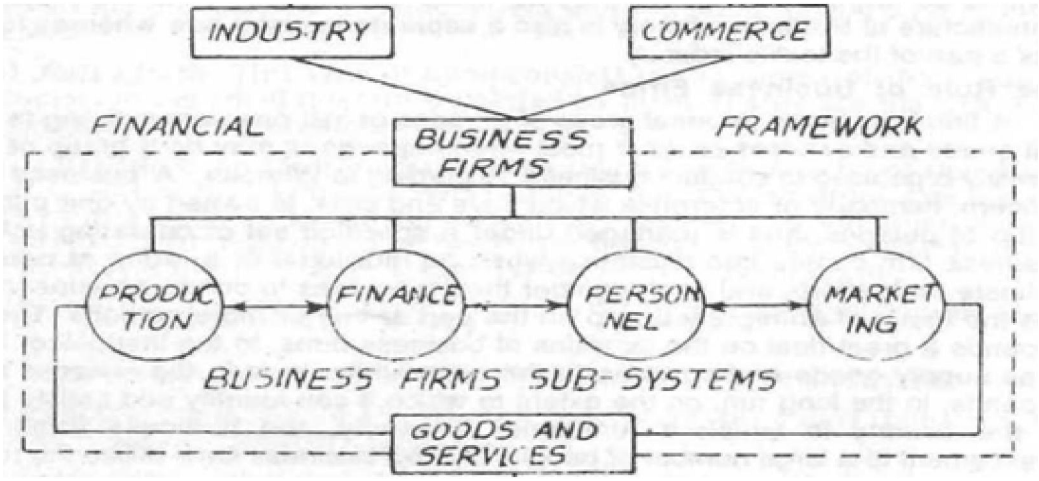
The Role of Business Firms

A firm may be an informal group of persons or just one person trying to buy and sell goods and services or, as it most often happens, it may be a group of persons formally organised to conduct business. According to Wheeler, "A 'business firm' is a concern, company or enterprise which buys and sells, is owned by one person or a group of persons, and is managed under a specified set of operating policies." A business firm comes into existence when an individual or a group of persons coordinate their efforts and pool together their resources to conduct business activity. It is the result of entrepreneurship on the part of one or more persons. The society depends a great deal on the activities of business firms. In the first place, business firms supply goods and services to the community. In fact, the success of a firm depends, in the long run, on the extent to which it can identify and satisfy the need of the society in which it functions. Secondly, the business firms provide employment to a large number of people. Thirdly, business firms utilise the resources of the community for production of goods and services and are thus responsible for capital formation. Fourthly, a business firm provides opportunities for gain to other firms dependent on it for their business (say, as suppliers of materials, goods, fuels, etc.) Lastly, business firms provide tax revenues to the government of the country and enable it to undertake projects and programmes for the welfare of the people. Keeping the importance of business firms in view, Wheeler describes an individual firm as "the atom of business, the basic source of productive economic energy." It is the firm that turns the wheel of business and economic activity in any society.

1.5 BUSINESS SYSTEM

Meaning of System

Even though the word 'system' is a very old one, it has gained currency in scientific literature comparatively recently. The term has acquired such popularity that it can be anything that one wants it to be. Simply stated, a system may be described as a set of interrelated parts. In studying a system, we address ourselves not only to a study of the different parts as such, but what is more important, to the way these parts are integrated and inter-related and these contribute to the functioning of a whole being. Thus, a system is a whole entity consisting of parts, each of which may be called a sub-system. To understand the functioning of a system, one has to integrated. This approach to the study of phenomena is called 'systems approach' or 'system analysis'. A character in a play by the Italian playwright Moliere expressed surprise and delight when he was told that he had been speaking prose all through his life. Our reaction will perhaps be no different if we are told that "we are entirely surrounded by, live within, and we ourselves are systems."In fact the best example of a system is provided by the human body which has organic, muscle and skeletal sub-system-all highly inter-related to. form an integral whole. The human society is also a system and so is our economy. An interesting feature of systems study is that there are sub-systems within systems, and the solar and other systems; the solar system consists of different planetary and other systems, and so on. In studying any system, therefore, we have to study it internally by identifying its sub-systems and also externally as a part (sub-system) of some larger system. This is the approach of modern science and it is, this that we propose to adopt in our study of business organisation and management in this book.



An Outline of Business System

BUSINESS AS A SYSTEM

Let us now see how the systems approach of analysis can be used to study and understand business. If we look upon business as a system, it may be regarded as an entity functioning in the social, economic, political and cultural environment of a country or even of the world. The structure of the business system consists of subsystems of industry and commerce. These sub-systems are made up of various forms of enterprises which are engaged in the production and supply of goods and services to the community. Each firm or enterprise is itself a system comprising subsystems like production, marketing, financing, personnel, etc, and of course, each of these functions or systems has its own sub-systems. The behaviour of the business system as a whole depends on the functioning of and inter-relationship among these sub-systems. However, these sub-systems are the direct parts of the business system and these constitute the structure of business. The structure of business being a sub-system of the society is tied up with the environment in which it has to function. The environment of the business system consists of the natural resources, government and law, monetary system, consumers, workers ; in short, the whole social, economic

and political set-up in which the business system has to operate. In undertaking a study of the modern business system, we shall concern ourselves not merely with the structure of business but also with the environmental factors which have a direct bearing on the smooth and efficient functioning of business. Our focus will, of course, be on the firm, the core of the business system, and its functional sub-systems like production marketing, finance, personnel, etc., Since the working of a firm is influenced by the environmental elements like its competitors, suppliers, government, consumers, workers, financiers, owners, etc., the responsibilities of a business firm towards all these will also engage our attention in this book. The Feedback

To engage in any type of business activity, a business unit has to gather various resources like finance, materials, machines (called factors of production by economists). The society, consisting of various sections like the government, suppliers, the financiers, customers and the workers, agrees to provide the required resources on the understanding that the needs of the various sections will be met by the business unit through the production of goods and services, payment of taxes, payment of suitable wages and payment of suitable returns on the financial resources invested in the unit. If the needs of the various sections of the society are satisfied, these sections continue to supply the desired support and resources. If, however, these needs are not satisfied or are partly satisfied, they react by cutting down the supply of resources required by the business unit. This process of increasing or reducing the support to a business unit in response to its performance is known as the process of 'feedback". The word 'feedback' means that which is fed back to the original giver or that which is given in return for something. Thus, in a business system, the concept of feedback refers to the arrangement by which society gets various outputs from business in return for the inputs and increases or reduces the inputs provided to the business system depending upon the satisfaction provided on the outputs of business.

MANAGEMENT OF BUSINESS

Since we are concerned with the management of business, it will be useful to start with a working definition of management too. The management of

business firm or enterprise consists in guiding and directing its operations towards fulfilment of its objectives, the most important of them being the production and supply of goods and, services needed by the community. To realise this objective of maintaining a continuous supply of goods and services of a specific type for meeting the needs of the community, a business firm makes use of the four basic resources-Men, Materials, Money and Management. With the aid of money (capital), the management makes use of human (man) and physical resources (materials to convert ideas into achievements). Given money, men and materials, it is the quality of management that determines how well and how far will a firm succeed in its work. Management is the'critical' factor in business operations that is responsible for the utilisation of the resources through proper planning, direction and supervision. The following chart shows how the management of a business firm performs this function in the conduct of its operations.

It is the function of those responsible for the management of a firm to lay down objectives and policies fcr the firm, plan its operations, organise the resources and allocate duties among the staff, issue directions and guide and co-ordinate their work and then check on the operations to make sure that these contribute to the realisation of objectives. The operations of a firm are generally sub-divided as production, finance, marketing, personnel, research and development, etc. Generally, the functioning of an enterprise is conditioned by the availability of finance. Therefore, subject to the available financial resources, the enterprise has to function in pursuit of its goals. Business management, then, refers to the guidance and diiection of business operations, including production, marketing, finance, personnel (people), research and development, etc., within the framework of financial resources. The function of production is concerned with the creation of utility, particularly form utility Marketing consists in catering to consumer needs by arranging for the supply of goods and services to the members of the community. Management of finance consists in utilising the available finances so as to meet the requirements of the firm for money most effectively and efficiently. Management of personnel involves

the functions of hiring, firing, compensating and motivating the people in the enterprise to work for the realisation of enterprise objectives. Management of research and development consists in conducting research investigations into markets and what is more into product design and production processes so that the enterprise can render better service to the community. We have included this function under the production sub-system.

Inter-relation of Business Activities

It must be borne in mind that all the functions of an enterprise are inter-related. Production depends upon the information gathered from the market. The personnelor staff requirements depend upon the level or scale of production and financial requirements will depend upon the personnel and production requirements. Marketing will, in turn, depend upon the pattern and scale of production.

1.6 OBJECTIVES OF BUSINESS

It is generally believed that business activity is carried on only for profit. Businessmen themselves proclaim that the main object of business is to earn profits. This is true to an extent; but it has been found that a truly successful business cannot afford to keep profits as its sole objective. As Urwick puts it, 'Earning of profits cannot be the objective of a business any more than eating is the objective of living." Similarly, Henry Ford declared in his autobiography that "mere money-chasing is not business." He built his business on the basis of service and set out to manufacture cars which would be within the means even of low-income groups and which, therefore, would serve the general mass of people. He declared that business consists in manufacturing those goods which the community wants, at a price which the community can pay. The same kind of missionary zea! marked the efforts of the Indian pioneer in industry, Jamshetjf Nausherwanji Tata. Thus, a truly great business can be built up only if the objective of "service to the community" is constantly kept in view. If this is done, profits will come automatically; but if the whole emphasis is on profits, business may not succeed for long. As Appleby puts it, “The enterprise that is

coldly and solely motivated by the making of money seldom fares well in the long run."

Business is essentially an economic activity but it cannot be carried on in isolation from the society. In fact, it is an activity carried on by the people (entrepreneurs and managers), through the people (employees), for the people (consumers and the society at large). A business enterprise may, therefore, be viewed as. an economic institution functioning in social, political and cultural environment. The objectives of business will have to be set in relation to this survival and growth in its environment. It will be seen that while on the one hand the environment dictates certain objectives to the enterprise, the enterprise in its own turn also influences the environment. For example, the environment may require that an enterprise provides employment to people. Having accepted this objective, the business enterprise may create products Or services for the distribution of which facilities may have to be created in the economy. This may set new objectives for the environment including the Government, the community and the financial institutions. Thus, the objectives of business are determined through an interaction between the enterprise and its activities on the one hand and the environmental needs and responses on the other.

Against the above backdrop, the objectives of business activity may be broadly categorised under the following heads :

1. Organic Objectives
2. Economic Objectives
3. Social Objectives
4. Human Objectives
5. National Objectives.

1. Organic Objectives

A business enterprise consists of people organised to conduct business activity to meet and satisfy the needs of society. It is essentially an organic entity which has its own infancy, childhood, adulthood and maturity. In

this position, the first concern of a business enterprise is to ensure its own survival for the continuance of business activity. Once the enterprise is assured of its survival it will aim at growth and expansion. To achieve this, it will try to gain prestige and win recognition from the society in which it functions. If it is unable to establish its goodwill in the community by rendering useful service, it will aim at further growth and expansion. In this respect the behaviour of an enterprise is similar to that of an individual human-being. A man like an enterprise first works towards the objectives of survival. If this objective is achieved in a reasonable measure, he looks forward to growth through and with goodwill, prestige and recognition. It will be seen that the economic, social, human and national objectives of business are all means to the achievement of a business enterprise and its activities because an enterprise, which does not fulfil these objectives, cannot hope to survive for long leave apart growing or creating goodwill .

2. **Economic Objectives**

Since business is basically an economic activity, its primary objectives are economic. The main economic objectives of business may be described as under:

(i) **Profit :**

Business activity is undertaken for earning profits. In privately-owned business enterprise, profit may be earned to provide means for wealth accumulation or growth and expansion of business activity through ploughing back of earnings. In a State-owned business enterprise, profit may be aimed at generating sufficient resources to finance expansion of the same business or other important social and economic needs.As has been stated earlier, profit is not the sole objective of business but is certainly an important measure to the success of business activity. However, an enterprise does not work for the so-called maximum profit. What is necessary is that a firm must try to avoid losses so that it can

continue to function. As Peter F. Drucker puts it, "The problem of any business is not the maximisation of profit but the achievement of sufficient profit to cover the risks of economic activity and thus to avoid loss."

The objective of business is then to earn as much of profits as will cover its own future risks. To quote Drucker again, it must have "A profit required to enable it to stay in business and to maintain intact the wealth-producing capacity of its resources."

(ii) **Creation of customers :**

Business involves transfer, sale or exchange of goods and services to satisfy the needs of customers. It follows that business activity can be sustained only if there are enough people to buy the products and services offered by an enterprise. Without a body of customers, a business enterprise cannot survive. That is why Peter Drucker asserts, "There is only one valid definition of business purpose : to create a customer.... it is the customer who determines what a business is...the customer is the foundation of the business and keeps it in existence...and it is to supply the customer that society entrusts wealth-producing resources to the business enterprise". Customers collectively constitute the market. Thus business amounts to creating a market for its products and services by meeting the needs of the customers. Who would be the customers of a business will depend upon the way the business defines itself. For example, furniture may be bought by people for their homes and, therefore, the customers may be individuals and families. Furniture could also be made for the house building contractors who construct furnished apartments. It is by identifying new categories of potential customers that a business enterprise is able to achieve the objective of extending the market for its products and services.

(iii) **Innovation :**

Business is an order of growth, expansion and change in the

economy. This dynamic function is performed by a business enterprise through innovation. Whether it is the objective of earning profits or expanding the market, it can be achieved only when business provides newer and better products and services. Sometimes innovation may take the form of adaptation to a change taking place in the society. For example, if consumers do not have enough time for household activities like cooking, business may offer new gadgets for the purpose and thus meet the need. But it is also possible for business to innovate and lead the society towards change. Innovation has its part to play. In all branches of business, it is the means by which an enterprise that has reached the stage of maturity and is beginning to decay can renew itself by introduing new designs using new techniques and tools, adopting new processes and suggesting new uses for its products. Through innovation a business enterprise can increase competitive strength and improve its image in the minds of the customers.

3. Social Objectives :

Since business operates in society it cannot survive and grow unless it meets the needs of the society. Business activity has to be rooted deep in the society and its culture. It is an important part of its objectives to fulfil its obligations to the society. In its turn, it is also likely to influence the need and expectations of the society and its culture. Some of the important social objectives of business are as under:

(i) Supply of the desired quality of goods: Business thrives on the goodwill of the com.r unity in which it is carried out. A business enterprise can hope to have a good image only if it is alive to its responsibility for producing and supplying goods and ; ervices of standard quality. If business fails to maintain a continuous and sufficient supply of unadulterated goods and articles of standard quality, it will be failing in fulfilling its social objects and is likely to incur the wrath of the society.

(ii) Avoidance of profiteering and anti-social practices: While it is legitimate for a business enterprise to work for reasonable profit, it is necessary that it does not over- charge the customers and profiteer at their cost. It is also a social obligation of business enterprises not to indulge in such malpractices as hoarding, black-marketing, etc.

(iii) Providing employment: One of the important objectives of business is to create opportunities for gainful employment for the people in the society. Sometimes this objective may conflict with the economic objective of cutting down costs and increasing profits by introducing automatic or semi-automatic machines. In a country like India, conflict may have to be settled in favour of employment considerations and programme for the introduction of automatic equipment may have to be deferred or implemented in phases without causing loss of job to anyone.

4. Human Objectives

Business activity can be conducted only through the medium of human beings working as individuals or groups in organisations. If the human factor is overlooked by a business enterprise, it will be difficult for him to achieve any of its other objectives. In fact, the efficiency and success of an enterprise depends ultimately on the ability and zeal of the people working in it. For this reason, business has to consciously seek the willing co-operation of people engaged in different tasks consciously seek the willing co-operation of people engaged in differen ttasks. The human objective of business arises from the expectations of the human beings performing business operations. Some of the important human objectives of business are:

(i) Fair deal to employees: The first prerequisite for getting the best out of people is providing a fair deal to employees at different levels in the form of fair wages and other incentives.

(ii) Development of human resources: Business can perform its function of innovation and customer creation only when the employees

are given opportunities for developing new skills and abilities and have work climate in which they will grow as mature and productive beings.

(iii) *Participation*: A business enterprise can get the best consideration from its employees if they have an opportunity to participate in making such decisions as affect them.

(iv) *Job satisfaction* : A business enterprise owes to its employees to provide them job satisfaction by making the job interesting and challenging and by reducing the unpleasantness of work.

In short, a business enterprise that pays sufficient attention to its human objectives,i.e., objectives in relation to the people working in it, can hope to benefit from their active participation in its activities

5. National Objectives

While social objectives are reflected in the general responsibilities of business to observe some moral code and serve the society in various ways, national objectives are the more specific obligations of business towards fulfilment of national needs and aspirations and implementation of national plans and policies in accordance with the accepted priorities. Keeping in view the national goal of establishing a democratic socialist society and achieving growth with stability and social justice, business in India has the following major national objectives:

(i) Ensuring social justice: It should be the objective of business to remove in-equalities of opportunities and provide a fair opportunity to all to work and progress. In pursuit of this objective, special attention has to be paid to neglected and weaker sections of the society.

(ii) Development of small enterpreneurs: In keeping with the accepted national policy, large business has the responsibility of encouraging the growth and development of small-scale entrepreneurship by patronising small-scale ancillary units and also by desisting from assuming monopolistic position.

(ii) Production according to national priorities: Business has the objective of producing and supplying goods which are needed in the country for its development. Development of industries to supply inputs for agriculture also one of the national objectives of business in India to manufacture and distribute cheaper varieties of essential goods like cloth, soap, edible oils, etc., so as to help the poorer sections.

(iv) National self-sufficiency and export development: To help the country to become self-reliant and avoid dependence on other nations, business has special responsibility to produce such articles as have hitherto been imported. In the case of machinery, equipment and processes, business should aim at import substitution.

Thus, the above mentioned are few obligations that business owes to the nation.

1.7 SUMMARY

Thus, in this lesson we have discussed about the basis characterstics of business along with different divisions of business . Industry and commerce are the two basic divisions of business which supports the economy of a country. The different objectives of a business which have been identified are organic, economic, social , human and national objectives.

1.8 GLOSSARY

i) Profession: occupation which involve the rendering of personal service of a special and expert nature.

ii) Employment: It is the action of employing someone or something

iii) Business: An organization or economic system where goods and service are exchanged for one another or for money.

iv) Commerce: The activity of buying or selling, especially on large scale.

v) System: It is defined as a set of interrelated parts.

1.9 SELF ASSESSMENT QUESTIONS

1. Differentiate between trade, commerce and Industry, explaining the main characterstics of each.

2. “Business firm is the hub of business activity.” Elucidiate

3. “In the present -day business world, an educated person can be more successful than an uneducated one” comment.

4. Explain all the objectives of business in detail.

1.10 LESSON END EXERCISE

1. What is meant by business system? What are the main elements of this system and how are these interrelated?

Ans. _____

_____

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_____

2. What is meant by 'Business'? What are its important divisions? How far can profit be regarded as the sole motive of business?

Ans. _____

_____

_____

_____

3. Distinguish between Business, Profession and Employment.

Ans. _____

_____

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_____

1.11 SUGGESTED READING

1. Business Environment by Francis Cherunilam
2. Fundamental of Business organization and management by Y.K. Bhushan
3. Business organization and management by C.B.Gupta
4. Business Management by Dinkar Pagare

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-1**

PAPER -IV **LESSON-2**

MEANING AND DIFFERENT FORMS OF ORGANISATION

STRUCTURE

2.1 INTRODUCTION

FORMS OF OWNERSHIP ORGANISATIONS

The first question to be settled in organising business operations is that of the ownership organisation. Ownership of business is represented by the right of an individual or a group of individuals to acquire legal title to assets for the purpose of controlling them and to enjoy the gains or profits from such possession and use. This right to acquire, enjoy and dispose property of business vests in private individuals or groups for firms in the private sector and in Government or other public bodies in the public sector. From this point of view, there are four main alternative possibilities for a business unit. It may be organised by an individual as sole proprietorship, or by an association of persons by mutual agreement as a partnership firm, or by an association of persons who form a co-operative society for the purpose, or else, it may be organised by a number of persons as a joint stock company. Besides these, Hindu undivided families also undertake business in India. The importance of the Hindu undivided family, or the joint Hindu family, as it is/known, is declining. For business purposes, therefore, the chief forms of ownership organisation are :

(a) Sole proprietorship,

(b) Partnership,

(c) Co-operative society and

(d) Joint stock company.

Before these forms are taken up for detailed discussion and evaluation, it must be noted that this classification of business units is based only on their ownership.

2.2 OBJECTIVES

The main objectives of this lesson is to:

- Understand the concept of different business forms
- Distinguish between sole proprietorship and partnership
- Understand the concept of cooperative societies

2.3 CHARACTERSTICS OF AN IDEAL FORM OF ORGANISATION

Before undertaking a description of the various forms of organisation and their respective merits and weaknesses, it will-be desirable to refer to the features which make for an ideal form of business organisation. These characteristics will be found applicable to the various forms of organisation . In choosing a particular form of organisation, an entrepreneur will try to find out how far his requirements will be met by a particular form of organisation. The following factors will generally be considered by him while making this type of an assessment :

(1) **Ease of formation**: From the point of view of the entrepreneur, the first consideration, though not the only one, in the choice of a proper form of organisation is as to which one can be formed with the greatest ease. An ideal form of organisation is, therefore, one which can be brought into existence with the least difficulty. A good form of organisation, as judged from the point of view of ease of formation, is one which involves the least expense in formation and minimum of legal formalities Besides, it should involve the least difficulty in the choice of proper associates for running the business.

(2) **Base of raising capital** : Another important feature of a good form of organisation is the facility of raising the required amount of capital. Where a large amount of capital is needed, it is desirable to ensure that investors in the business concerned are assured of safety of investment, fair return on investment and transferability of investment. The entrepreneur will do well to consider the comparative ease (or difficulty) with which capital can be raised for the various forms of organisation.

(3) **Limit to liability**: From the point of view of risk, the entrepreneur will prefer limited liability. This would mean that in case of insolvency or winding up, the owner or owners will be held responsible only up to the amount of capital agreed to be contributed by them. Unlimited liability (making the personal estates of the owners liable for losses) is preferred

in some cases just because it provides the necessary incentive to the owners to work for the success of the chosen form of organisation.

(4) **Direct relationship between ownership, control and management** : As a rule, control should lie where ownership lies. This will lead the management and the entrepreneurs to take active interest in the efficient running of the enterprise. If the responsibility for management or the control of management does not lie with the owners, the management may not have a direct personal interest in maximising profits through increase in efficiency. However, sometimes, close association of ownership with management may discourage adventure and enterprise on the part of the management. If the owners are all the time worried about the safety of their investment in the enterprise, as they naturally would be, it will be difficult for them to take big risks or follow a bold or adventurous business policy.

(5) **Flexibility of operation**: A good form of organisation offers the maximum flexibility and adaptability. This means that the organisation should lend itself to change and adjustment without much difficulty as the need be. In choosing a form of organisation, the entrepreneur will consider as to whether it will add to the flexibility and efficiency of management to associate some more persons as part owners or as employees.

(6) **Continuity or stability**: An ideal form of organisation enjoys uninterrupted existence over a long period of time. From the point of view of the entrepreneur, it is important that he should be able to formulate plans for the future and to make investments paying for considerable periods of time. From the social point of view also, it is desirable that there should be an agency which meets its economic needs continuously and provides continued employment to a section of the society. "The organisation must both be able, when undisturbed, to last through a long period of time, and also to resist temporary disturbing influences, that is, be stable."

(7) Retention of Business Secrets: The entrepreneur will also have to be careful to ensure that the form of organistaion chosen by him will allow

vital. Business secrets to be retained without being leaked out to the competitors. This will naturally mean that he will have to select his associates with utmost care.

(8) Lighter tax liability: Various forms of business organization are assessed to income-tax on different bases. Obviously, other things being equal, the ideal form of organization will be that which attracts the minimum amount of tax liability.

Choice of a Suitable Form of Organization

The various characteristics of an ideal form of organisation indicated above are not to be considered in isolation from each other. The choice of the entrepreneur will, in actual practice, be dictated by the peculiar requirements of the enterprise proposed to be started.

Some requirements which guide entrepreneurs in making this choice are :

(a) Type of business-trading, manufacturing, commercial or service.

(b) Expected volume of business.,

(c) Area of operation.

(d) Degree of direct control over management desired by management.

(e) Finance required for initial requirements and expansions.

(f) Willingness of owners to assume personal liability for business risks.

(g) Arrangement for sharing profits.

(h) Expected life-span of business.

(i) Tax advantage under different types of ownership.

(j) Degree of Government regulation and the freedom desired by the entrepreneurs.

2.4 SOLE PROPRIETORSHIP

Sole proprietorship is a form of business organisation in which an individual introduces his own capital, uses his own skill and intelligence in the management of its affairs and is solely responsible for the results of its operations. The individual may run the business alone or may obtain the assistance of employees. It is the first stage in the evolution of the forms of organization and is, thus, the oldest among them.

Also known as individual entrepreneurship, it is the easiest to form and is also the simplest in organization. All that is required is that the individual concerned should decide to carry on some particular business and find the necessary capital. For this purpose, he may depend mostly on his own savings, or else, he may borrow part or whole from his friends or relatives. The business may be started either in a portion of the proprietor's own house or in rented premises. There are no legal formalities to be gone through except those required for a particular type of business. For example, if one wants to start a restaurant one has to obtain a licence from the Health Department of the Municipal Corporation, but for setting up the firm as such no legal formalities are necessary.

The law makes no distinction between the firm and the proprietor. If 'A' starts business, then, as far as the law is concerned, 'A', the businessman, and 'A', the individual, are one and the same person. In other words, the owner's personal property is also liable for the liabilities of the firm. This makes his liability unlimited. If the business prospers, he gets the whole profit; if it does not do well, he bears the whole loss. For this reason, he enjoys full control over the affairs of the firm. He decides everything for the firm and carries out his own plans without fear of any opposition, but, of course, at his own risk. In short, the entrepreneur is his own master in this form of organisation.

The following features of individual or sole-proprietorship emerge from the foregoing account of this form :

1. Single ownership.
2. One-man control.

3. Undivided risk.

4. Unlimited liability.

5. No Government regulation.

6. No separate entity of the firm

Evaluation : This form of organisation is quite popular for a small-scale business, though for a large business the other forms are generally preferred. The reasons for this can be found in its merits and limitations.

Merits

1) Ease of formation and dissolution: As has been pointed out no legal formalities are necessary for setting up the business in this form. It is, thus, the most easily formed of all the forms of business organization. Any person enjoying the capacity to contract can set up such an organization. As Lundy puts it, "Becoming a proprietor is as simple as buying newspapers for 3 cents and selling them on a street corner for a nickel (5 cents)." Dissolution, termination, or sale of the business is equally simple in the case of a sole-proprietorship. There are no legal formalities in this regard and all that the businessman has to arrange for is the satisfaction of creditors' claims.A sole proprietor may wash his hands off his business selling his interest to another person or association of persons.

2) **Direct motivation**: The direct relationship between effort and reward serves as a powerful incentive to the proprietor to manage the concern efficiently. It encourages and induces him to put forth his best in the management of the business. He knows that any lapse on his part will mean loss of profits.

3) **Facility of co-ordination** : There is no problem of co-ordination. The proprietor himself has to decide everything and, therefore, he will not take a decision by which the various interests of the firm clash.

4) **Promptness in decision -making** : Promptness in decision is another advantage of this firm. As pointed above ,an individual entrepreneur need not consult others while deciding the affairs of his concern. This makes for quicker decisions by which he can take advantage of the opportunities of gain arising from time to time.

5) **Flexibility in management**: if any change in business is called for, he doesnot have to consult anyone and , therefore, he will be able to make the change without delay. This give flexibility to this type of organization.

6) **Secrecy** : Secrecy can be maintained about business matters, therefore, the proprietor will be able to take full advantage of any new ideas that occur to him.

7) **Freedom from Government regulations**: Sole proprietorship is the least regulated form of business organization.

Limitations

1) **Limited finance**: The individual proprietor suffers from the limitation of financial resource. He can depend only on his own savings, and it is neither safe nor easy for him to borrow much money from banks or other financial institutions.

2) **Limited managerial skill**: The managerial ability of the proprietor is limited. Modern business is full of complications especially due to the ever - changing nature of market, and the various laws that are being enacted. An individual may not be an expert all matters and, therefore, sometimes his decisions may be unbalanced.

3) **Uncertainty of duration**: The proprietorship business comes to an end if anything happens to the proprietor. If the business is rendering useful service to the society the closure of such a business will be a social loss.

4) **Unlimited liability**: The liability of the owner is unlimited . Not only the assets of the business but also his private assets will be used to pay off

the f irm's debts. Therefore, when a man starts a business he may not really know the extent to which he is committing his private property

2.5 JOINT HINDU FAMILY FIRM

The joint Hindu family business represents a business organisation owned by the co-owners or co-parceners of an estate belonging to a Hindu family which has no' yet been partitioned. Such business can exist only under the Mitakshara law which governs Hindu succession in all parts of India except Bengal and Assam, where the Dayabhaga system of inheritance is in vogue. Under the Mitakshara system of inheritance, joint Hindu family technically comprises those who hold coparcenary interest in it.: Such interest belongs to three successive generations in the male line who can inherit an interest in the ancestral property immediately on their birth. After the passage of the Hindu Succession Act of 1956, a female relative of a deceased male co-parcener will have a share in the co-parcenary interest after the death of the co-parcener 'in question.The privilege is open even to male relative of the deceased who claims through certain specified female relatives of the deceased.

The ancestral property is that which is inherited by a Hindu from his father, grandfather or great grandfather. Likewise, a son, his son, and his son's son become members of the joint Hindu family with co-parcenary interests by virtue of being born in the family. Since business is regarded as a part of the heritable property, the coparcenary interests arise even in the case of family business. Joint Hindu family property and business are governed by the accepted rules of Hindu law

2.6 PARTNERSHIP ORGANIZATION

The individual proprietorship organization, with all its limitations, proved unequal to the requirements of expanding business. Expansion of business called for more capital, enhanced the risk, and required more managerial ability than could be expected of a single individual. A wealthy man may lack managerial capacity, and an able manager might not have money

enough to finance a big concern. This made some kind of an association among individual businessmen necessary. Partnership organization is one form of such association. It grew essentially out of the failures and limitations of the individual proprietorship and represents the second stage in the evolution of the forms of business organization. Generally when a sole trader finds it hard to cope with the problems created by the expansion of business, he takes an able employee, or some other capable and well-to-do person, as his associate in business and converts his sole-proprietary business into a partnership.. The formation and management of partnership organisation is governed by the provisions of the Indian Partnership Act of 1932.

Section 4 of the Act defines partnership as "the relation between persons who have agreed to share profits of a business carried on by all or any of them acting for all."

The following characteristics of partnership emerge from this definition :

1. Existence of business. An association of persons will become a partnership only when it is meant to do some kind of business. If the purpose is to carry on some charitable work, it will not be a partnership.

2. Plurality of persons. At least two persons must join together for business. One person cannot enter into partnership with himself.

3. Contractual relationship. The business is set up by an agreement between persons concerned called partners. Persons who are not competent to contract (e.g., minors) cannot be partners. Moreover, a Hindu family business does not automatically become a partnership business.

4. Profit motive. The purpose of partnership should be to earn profits and there must be an agreement to share them.

5. Principal-agent relationship. The business must be carried on by all or one or more acting on behalf of all the partners. Thus every partner is an agent of the other members of the firm.

All these conditions must be satisfied to constitute partnership. If the manager of a firm is given a share in profits, he is not to be treated as a partner, because business is not carried on on his behalf. The chief test of whether a person is a partner or not is Whether the business is conducted on his behalf, i.e. whether or not the element of agency exists. Every partner has the right to participate in the management of the firm's business though any of them may give up this right by agreement.

The minimum number of persons required to make a partnership is two. The Partnership Act does not mention the upper limit but under the Companies Act, 1956. a partnership consisting of more than 20 persons for a general business and 10 partners for a banking business would be illegal. Hence, these should be regarded as the maximum limits to the number of partners in a partnership firm.

Other Legal Characteristics: It will be useful here to take notice of some other notable features of partnership organisation also :

1. **Unlimited liability:** Each partner has an unlimited liability in respect of the firm's debts. The creditors can recover their dues from the property of any or all partners in case the firm's assets are insufficient.

2. **Utmost good faith:** A partnership agreement rests on utmost good faith.The partners must, therefore, be just and honest to one another. They must disclose every information and present true accounts to one another.

3. **Implied agency:** Every partner has an implied authority, to act on behalf of his fellow-partners and the firm in the ordinary course of business. Thus, he is an agent of the firm and the other partners.

4. **Restriction on transfer of interest:** A partner cannot transfer his share to an .outsider without the consent of the other partners!. This is so because partnership is a contract between individual partners and contract resting on utmost good faith at that.

FEATURES OF PARTNERSHIP

1. **Formation** : Since partnership resets on a contract among persons,

its formation does not involve any special legal problems. Generally, the partnership agreement is reduced to writing and a Partnership Deed laying down the terms and conditions of partnership and the rights, duties and obligations of partners is drafted. Since there can be possibility of bad blood and disagreements developing among partners in future (money is a great divider I) legal assistance may be sought from a lawyer in drafting the Deed.Law does not make it compulsory for a partnership firm to be registered but registration becomes necessary in view of the fact that certain disabilities attach to the firm if it is not registered. The most serious of these is that unregistered firm cannot file a suit to enforce rights against outside parties if such (rights arise out of a contract. Likewise, a partner cannot file a suit to enforce his rights against the firm and other partners under the Partnership Deed. For these reasons, registration with the registrar of Firms may well be regarded as a part of the formation procedure for partnership organisation.

2. **Financing** : The capital of partnership firm consists of ,the amounts contributed by different partners. The capital contributions of partners need not necessarily be in proportion to their profit-sharing ratio. Sometirmes, a partner may be admitted to partnership without any capital contribution. This is usually accepted for those partners who bring special skills, abilities or' contacts into the partnership organisation. A partnership may augment its initial finances by borrowing from Outsiders but such borrowing will be on the strength of the security of the'firm's property and of the private estates of partners.

3. **Control** : In a partnership firm where all the partners are active, control vests with all of them. No major business decision can be taken without the unanimous will of all the partners. In some firms, only one or two partners are active and the rest are sleeping or dormant. The sleeping or dormant partners do not take an active part in the operations of the firm. But the right of even such partners to control the functioning of the firm cannot be denied. In short, then, control is shared by the partners in a firm.

4. **Management** : Law confers on every partner the right to take an active part in the management of the firm's affairs. Each partner has the authority to

bind the firm and other partners through his acts in the ordinary course of business. Each firm is free to choose a pattern of management according to agreement among partners. In many cases a managing partner looks after the work of the firm (and its departments, if any) as the chief executive. In some others, the partners allocate areas of management among themselves, e.g., one partner may look after the factory, the other may take care of purchases, the third may be put in charge of sales, and so forth. Where a firm has ranches in the same or other towns, each partner may be put in charge of each branch. Of course, decisions on major issues of objectives, policies and programmes, will be taken by them jointly.

5. **Duration** : The partnership firm continues at the pleasure of the partners. Legally, a partnership comes to an end if any of insolvent. However, if the remaining partners agree to work together under tho original firm name and style, the firm will not be dissolved and will continue its business after settling the claim of the outgoing partner. The Indian Partnership Act lays down the circumstances in which a firm will be dissolved, e g., when the business Becomes illegal or when all partners (or all except one) become insolvent. The Court is also empowered to order dissolution of the firm in certain circumstances, e.g., when the business cannot be carried on except at a loss or partner becomes incapacitated, etc.

6. **Taxation** : Like an individual's income, the income of a partnership is taxed on slab system The rate of tax rises progressively as the income goes up. If the firm is registered under the Income Tax Act (as distinct from registration under the Indian Partnership Act), the income of the firm will be divided among partners and each partner will be assessed to income-tax separately. But if the firm is not registered, the firm will have to pay tax on its profits as distinct from the incomes of partners.

Types of Partners

Although all the partners are entitled to conduct the business of the firm, yet, in practice, the management and operation of business is left to a few active

partners. These partners carry on the business on behalf of the rest. The others, who may be partners and yet may not participate in management, ma/ by classified as follows :

(a) Sleeping partners or dormant partners are those who agree not to participate in the management: Such partners only invest their capital and take a share of profits which is usually smaller than that of active partners. To the third parties they are equally liable as other partners, that is to say, their liability, too, is unlimited.

(b) Nominal partners: Some people only lend their name to the firm as partners. They do not invest, do not get a share of profit, and are not entitled to take part in the management. They are partners only nominally. But, they are liable, like other patners, to third parties.

(c) Partners by estoppel: If a person behaves in such a fashion that he is mistaken to be a partner by third parties, he will be held liable to those third parties who extend credit to the firm on the reputation of his being a partner. Such a person is known as partner by estoppel because, having behaved as a partner, he cannot deny the liabilities attaching to the position of a partner.

(d) Partners by holding out: If a person is declared (by word or deed) t o be a partner by another person, the person concerned should deny it immediately on coming to know of such a declaration. If he does not, he will be liable to those third parties who lend money or otherwise give credit to the firm on the basis of his being a partner. Such a partner is known as a partner by holding out.

Minor partners

Since a minor does not enjoy the capacity to enter into contracts in his own right, he cannot be a full fledged partner in a partnership firm. He can, however, be admitted to the benefits of partnership. The minor concerned will be a minor partner. His liability in the firm will be limited to the extent of his share in the firm. His estate cannot be called upon to contribute anything beyond

what is already invested in the firm. On attaining majority, or on his coming to know of his admission as a partner, he has to choose whether he will continue as a partner or not. If he does not give a public notice of his choice within six months, he will be treated as having decided to continue as a partner. In case he chooses or is deemed to be a partner, his liability will become unlimited with effect from the date of his original admission to the benefits of the partnership.

IDEAL PARTNERSHIP

One should choose one's partner with as much care as one would use while choosing one's wife. A wrong choice in both cases can be ruinous. A partner can act on behalf of all his partners without consulting them as far as third parties are concerned. He can enter into commitments which the other partners will have to honour; the other partners will be responsible even for frauds committed by a partner in the course of the business. A partner may, out of foolishness, recklessness or sheer mischief, land the whole firm in trouble. One must, therefore, be extremely careful in entering into a partnership. There are a large number of firms which fail because the partners cannot work harmoniously. The following can be said to be the requisites of an ideal partnership :

(a) Mutual understanding : Only such people as know one another thoroughly over a fairly long period should become partners. Moreover, the number of partners should be small-five seems to be the maximum ; otherwise, the partnership will become unwieldy.

(b) Common approach : The partners should have common views regarding conduct of business. If one partner takes a legalistic view of things, and wishes to drive hard bargains while another partner takes a generous view of things-the two may not pull on together for long. To take another example, one partner may be extremely cautious and may play absolutely safe, whereas another may like to take risks. Such a partnership, too, cannot work for long.

(c) Good faith: The partners should work in absolute sincerity and

good faith. They must contribute their best in terms of knowledge, time, attention and finance. Each partner should feel that his interest is being well looked after. No partner should try to take an unfair advantage over other partners.

(d) Balancing of skills and talents: There should be balance in the firm. This means that the partners should possess talents of different types so that all the problems that come before the firm are properly solved. The skills should be complementary. If a firm consists only of financial experts, marketing and production problems will go by default and the firm will work in a iop-sided manner. Balance is required in another sense also. There should be partners who think out new schemes for business-new ideas often turn out to be extremely fruitful-but there should also be partners who are capable of making exact calculations on paper about the implications of the schemes.

(e) Adequate long-term capital : The funds that the firm will need should be available either by capital raised from partners or as long-term loans. The drawings of partners for private purposes should be kept as low as possible and in no case must they exceed the profits. As far as possible profits should be ploughed back into the firm in order to enable it to develop further.

(f) Long duration : The term of partnership should be sufficiently long. Short-term partnership cannot obviously undertake a business which takes long to establish and consolidate.

(g) Written agreement: The mutual rights of partners and their obligations must be discussed in all details before the partnership is entered into. No mental reservations should be there when a partner gives his assent to the details when they are being worked out. The agreement should be put in black and white.

(h) Registration : The partnership should be registered as soon as

it is formed. In the absence of registration, the firm will not be able to enforce its legal remedies £3ainst outsiders.

(i) Partnership Deed : The partnership deed is a must for a partnership. The Partnership Act defines certain rights and duties of a partner, but mostly the provisions of the Act come into operation only when there is no agreements among the partners. If there is no agreement, differences may develop. For example, one partner may demote all his time while another may give little of his time to the firm. The first partner may legitimately ask for a salary but cannot get it in the absence of an experts agreement to this effect. It is for this reason that before the partnership is formed, all mutual rights, powers and obligations should be discussed and incorporated in a written agreement. The services of a lawyer should be utilised for drafting the agreement. The Deed has to be stamped in accordance with the Indian Stamps Act. Each partner should have a copy of the Deed.

Distinction between Partnership and Joint Hindu Family Firm : Both partnership and joint Hindu family firm are owned and run by groups -of persons But there are some basic points of distinction arising from the different laws governing them. These may be summed up as under :

1. Legal basis : Partnership arises out of a contract between the partners and a partnership business can, therefore, be brought into existence by mutual agreement. A joint Hindu family co-partnership is, however, the result of the operation of law. The- membership of a joint Hindu family business is based on the status of an individual in the sense that every male child born in the family becomes a coparcener right from the moment he is born. In a partnership, a minor who are not enjoy the legal capacity to bind himself by contracts is not recognised as a full-fledged partner, but minority of age does not affect the rights and status of a coparcener (or co-sharer) in a joint family business.

2. The position of females: Under the partnership law, women can.

enter. into contract with men or among themselves for stating a partnership business. They will, in such cases, enjoy the same rights and privileges as male members. In a joint Hindu family business, however, the membership is generally restricted to male members. In fact, prior to the enactment of the Hindu Succession Act of 1956, females were denied coparcenary interests altogether. Under this Act, however, a female relative of a deceased male member gets a coparcenary interest at the time of the death of such a coparcener.

3. Management : Partnership business is run on the basis of implied authority vested in every partner. Any partner can bind his other partners by acts done in the ordinary course of the partnership business. The Indian Partnership Act, 1932, provides that every partner has a right to manage the affairs of the partnership business. In a joint Hindu family business, however, the management vests only in Karta, the senior most member of the family, who alone has the implied authority to bind the joint family business for the ordinary purposes of business. No other, member can participate in the management of the business and bind the joint business by his acts. In fact, no coparcener can question the judgment of the Karta in the conduct of family business.

4. Mode of dissolution : The death of a partner automatically dissolves , the partnership, but a joint Hindu family business is not affected by the death of a coparcener. Both partnership and joint Hindu family business can be dissolved through mutual agreement. In case of a joint Hindu family business, an ault'-member can demand partition of the joint property.

5. Members' liability : The liability of every partner in a partnership firm is unlimited inasmuch as their personal estates will also be liable for the debts and obligations incurred by the firm.

6. Right to accounts: On leaving a firm,a partner can ask for the accounts of the firm but a coparcener is not entitled to do so.

2.7 CO-OPERATIVE SOCEtIES

The co-operative organization is different from other organizations as they are not set up with profits as the guiding motive but with the fundamental object of organizing and rendering service for the organization and its members. A co-operative society is essentially an association of persons who join together on a voluntary basis for the furtherance of their common economic interests. It may be described as a protective device used by the relatively less strong sections of society to safeguard their economic interests in the face of exploitation by producers and sellers working solely for maximizing profits.

Features

As a form of organization , the cooperatives association is marked by the following distinctive characterstics:

(i) Voluntary Association: 'A cooperative society is a voluntary association of persons and not of capital.' Any person , irrespective of his caste or creed , can join a cooperative society of his free will and can leave it at any time after giving due notice to the society.

(ii) Finance : The capital of a co-operative society is raised from members by way of share capital. Since co-operatives are organized by relatively weaker sections of society, the share capital is generally limited.

(iii) Control and management: Democracy is the key note of the management of a co-operative society. Since most of these societies operate on a local scale, the meetings of the members are generally well attended. At these meetings, the members elect the managing committee and lay down the policy which it must follow to promote their common interests. Each member, whatever be his stake in the society, has one vote and hence an equal right to participate in the management of the society.Members cannot vote by proxy.

(iv) Service motto: A co-operative society is organized primarily with the object of rendering maximum service to its members in certain field. It doesnot aim at profit at the cost of its members, for it is formed basically for providing certain essential facilities to members.

(v) Disposal of surplus: It is usual for commercial concerns to distribute profit among the owners in the ratio of their capital contribution, or in an agreed ratio. A co-operative society differs from the trading companies in this respect.under the co-operative form of ownership and organization , the surplus arising out of a year's working is given to the members not directly as dividend on shares held by each of them,but in the form of a bonus which need to proportionate to their respective capital contributions.

(vi) Fixed return on capital: One of the basic principles of co-operative organization , laid down by the pioneers of the co-operative movement like Rochdale and Owen, was that a fixed or limited return on capital subscribed the society must be paid out of the surplus to the members.

(vii) State control and corporate status: Although voluntary in their basic character , the co-operative societies are subject to considerable state control and supervision. In India , the co-operative societies are registered under the Co- operative Societies Act,1912 or the relevant State Co-operative Societies Act, as the case may be.

2.8 JOINT STOCK COMPANY

The word 'company' has no strict or technical or legal meaning. A company in the normal sense means an association of persons united for a common object. Accordingly the term is used to represent associations formed to carry on some business for profit or to promote art, science, education or some charitable purpose. Such an association may or may not be incorporated according to the law of the land.

Section 2(20) of the Companies Act 2013 provides that company

means a company incorporated under this Act or, under any previous company law."

According to Chief Justice Marshall of USA, "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".

Thus, a company is a voluntary association of persons formed for the purpose of doing business having a distinct name and limited liability .It is a juristic person having a separate legal entity distinct from its members who constitute it, capable of rights and duties of its own and endowed with the potential of perpetual succession.

CHARACTERISTICS OF A COMPANY

The main characteristics of a company are :

1. **Incorporated Association** : An incorporated company or a 'corporation' is a single person distinct from the individuals constituting it, whereas an unincorporated company, such as a partnership, is a mere collection or aggregation of individuals. Therefore, unlike a partnership, a company is a corporate body and a legal person having status and personality distinct and separate from that of the members constituting it.

   Section 2(20) of the Companies Act 2013 provides that company means a company incorporated under this Act or, under any previous company law.

   Company is a voluntary association of persons formed for the purpose of doing business having a distinct name and limited liability It is a juristic person having a separate legal entity distinct from its members who constitute it, capable of rights and duties of its own and endowed with the potential of perpetual succession. When the member dies, the

company continues to exist. His share and in the assets of the company vest in his personal representatives;

2. **Limited liability** : "Limited Liability" means "you have to pay as much as you have agreed to pay."

"Unlimited Liability" means "you have to pay as much as you owe."

It is the liability of a member to a company, which is limited. The company's liability is always unlimited. A company itself is always fully liable to pay its debts so long as there are assets available to pay the debts. When a company goes into liquidation, the debts must be paid in a strict order to the extent of availability of assets.

- Limited liability of members is another most important characteristic of a company. It is the reason why a great many people invest their money in limited companies.
- The contribution of a member in winding up towards debts and liabilities and costs shall not exceed the amount unpaid on the shares.
- A Company is a separate person, having its own name, identity, common seal and capacity to se and be sued in its own name.
- A Company's liability may be limited by shares or guarantee or unlimited as per its MOA.
- ln some cases, however, the limited liability of members may be rendered unlimited.

From the above, It is clear that the liability of the Company is also its own and not that of its members.

3. **Separate property** : Another characteristic of the company is that it is capable of owning, enjoying and disposing of property in its own name. It is a consequence of the fact that the company is a legal person. The property of the company will not be considered as the joint property of

the members constituting the company, although the capital and assets of the company are contributed by members. A member does not even have an insurable interest in the property of the company.

4. **Perpetual succession** : Unlike a natural person a company never dies. Under Section 9 of the Companies Act, 2013. It is an entity with a perpetual succession. This means that the company being an entity separate and distinct from its shareholders, the life of a company is not measured by the life of any member; it is independent of the lives of its members.

The death or insolvency of a member does not affect the corporate existence of the company. A company is an immortal person. Members may come and members may go, but the company continues its operations unless it is wound up. A company is created by the process of law and can be put to an end only by the process of law. The existence of the company is not affected by the death of all the shareholders.Thus where all the members of a company were killed by a bomb, the company was deemed to survive. In such a case, the legal heirs of the deceased shareholders will become members.

5. **Transferability of shares**: Under Section 56 of the Companies Act, 2013. The shares of a company are freely transferable and can be sold or purchased in the share market. This is one of the reasons why people prefer to form companies than partnerships. A shareholder is therefore no permanently wedded to a company.

The Companies Act recognises the right of transferability shares and provides that, the shares or other interest of any member shall be movable property transferable in the manner provided for in the articles of the company. However, any change in membership does not affect the working of the Company. Hence, members may come and go, but the Company goes on forever. In a Private Company, there are certain restrictions and not prohibition on transfer of Shares.

6. **Common seal** : As a company is an artificial person it cannot sign its name on a contract. So it functions with the help of a seal. Common seal

is used as a substitute for its signature. Every company must have a seal with its name engraved on it. A rubber stamp does not serve the purpose. Anything done under an agreement between the company and the third party requires recognition of the company in the Form of an official seal unless exempted by the Act. A document not bearing the common seal of the company is not authentic and as such is not binding on the company.

W.e.f 29/5/15. The World "Common Seal" have been omitted from sec. 9. Therefore use of common seal is now optional and no more mandatory. If the company does not have a common seal, the authorization u/s 22(2) shall be made by 2 directors or by one director & CS where ever company has appointed a company secretary.

7. **Capacity to sue and be sued** : On incorporation a company acquires a separate and independent legal personality. As a legal person it can sue and be sued in its own name. A company may be sued for infringement of copyrights, negligence and contempt of court. A company may sue for an injury done to its business reputation by defamation.

2.9 SUMMARY

In this lesson, different forms of ownership organization have been discussed. Ownership is represented by the right of an individual or a group of individuals to acquire legal title to assets for the purpose of controlling them. The chief forms of ownership organization are Sole proprietorship, Partnership, Co-operative societies and Joint Stock Company.

2.10 GLOSSARY

1. *Ownership*: A person who owns something.
2. *Commerce*: It is an organized system for the exchange of goods between the members of the industrial world.
3. *Liability*: It is defined as the state of being legally responsible for something
4. *Stability*: It is the state of being stable.
5. *Existence*: It is defined as the fact of existing.

2.11 SELF ASSESSMENT QUESTIONS

1. Discuss the preliminary considerations which a businessman should keep in mind when selecting a form of business organization.

2 . Discuss the advantages and disadvantages of sole trading business.

3. "One man control is the best in the world if that one man is big enough to manage everything." Explain this statement.

4. Explain salient features of a partnership firm.

5. Discuss the various kinds of partners in partnership firm and discuss their rights and liabilities.

2.12 LESSON END ACTIVITIES

1. Elaborate the concept of cooperative societies in detail.

Ans. _____

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72 Discuss the essential features of a joint Hindu family business and state its advantages and disadvantages.

Ans. _____

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3. Describe the various kinds of partners in a partnership firm and discuss their rights and liabilities.

Ans. _____

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4. Explain the meaning of the terms (3) firm, (6) limited partnership, (c) sleeping partners in connection with a partnership organisation.

Ans. _____

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5. Under what circumstances, might you be considered by law to be a partner against your wishes? Explain the duties and responsibilities of such partners. Is it a popular form of business ownership?

Ans. _____

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2.13 SUGGESTED READINGS

1. Business Environment by Francis Cherunilam
2. Fundamental of Business organization and management by Y.K. Bhushan
3. Business organization and management by C.B.Gupta
4. Company law by N.D .Kapoor
5. Indian Company Law by Avtar Singh

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-1**

PAPER -IV **LESSON-3**

STRUCTURE

3.1 INTRODUCTION

The word 'Ethics' has been derived from the ancient Greek word 'Ethikes'- meaning of which is essence of values and habits of a person or group. The term ethics describes a set of principles that provide a framework for conduct. Ethics is all about rules governing the way in which we determine what is 'right' or 'wrong', 'good' or 'bad. In other words, Ethics is about our actions and decisions. When we act in a way which is consistent with our beliefs ,we will characterize that as acting ethically. When our actions are not consistent with our values - our sense of right, good and just - we will view that as acting unethically. Ethics is perceived as a set of societal standards of conduct and moral judgment that encompasses the norms of a given community. Ethics are a personal set of values used by an individual a group or a profession, so as to guide them in their action and help them fulfill or carry out their obligation. Its subjective rather that objective and its relative to our perception of reality dependent on circumstances and life experiences of the individual or group, thus making it a continuously evolving code of conduct. It addresses issues pertaining to morality, i.e. good and bad; right or wrong etc.

No doubt, ethics is a subjective topic that may mean different things to different; people, it's still very important in all types of corporate settings.

GOLDEN RULE OF ETHICS

The golden rule of ethics is often terms as 'Ethics of Reciprocity'. The golden rule states "Do unto others as you would have them to unto you." In other words, "treat others as you would like to be treated, if you were them." The golden rule is an example of normative theory which establishes a single principle against which we can judge all action (i.e. whether any possible action is right or wrong).

3.2 OBJECTIVES

After going through this lesson, you should be able to:

- Understand the concept of ethics and business ethics

- Identify the various characterstics of business ethics
- Elaborate different types of ethics
- Identify the different factors highlighting the importance of business ethics

3.3 IMPORTANCE OF ETHICS

Highly educated, successful and business savvy corporate professionals at Enron, Tyco, WorldCom, and Satyam got themselves into a big mess mainly because of profound lack of ethics. Ethics are important in all aspects of life , because it is an essential part of the foundation on which a civilized society is built. To exist in the business ethics are essential. Ethics encourage true and fair practices in place of malpractices, promotes truth in place of false and misleading actions, prefers fair means in place of unfair means. Ethics is important to businesses for several reasons:

(i) Ethics create good relationship among various stakeholders.

(ii) Ethics is an index for development

(iii) Ethics reduces the corruption level and mistrust.

(iv) Ethics creates investor friendly atmosphere and minimizes risk.

(v) Ethics corresponds to basic human needs.

(vi) Ethics create creditability with the public and with the employees.

(vii) Ethics and profit go together.

(viii) Rules and regulations can control or minimize the corruption, but can't prevent it fully, whereas ethics can do this wonder.

(ix) Law can't protect society, while ethics can

3.4 BUSINESS ETHICS

Business Ethics is concerned with the application of ethics to the business

activities. Business ethics are moral values and principles that determine our conduct in the business world. Business ethics is the application of general ethical ideas to business behaviour. All in all the ethical issues existed since ages but ethics in business became more relevant in the present era of cut throat competition

Ethical business behaviour facilitates and promotes good to society, improves profitability, fosters business relations and employee productivity. The concept of business ethics has come to mean various things to various people, but generally it's coming to know what it right or wrong in the workplace and doing what's right - this is in regard to effects of products/services and in relationships with stakeholders. Business ethic are structured around values as fairness and honesty.

Business ethics is concerned with the behavior of a businessman in doing a business. Unethical practices creating problems to businessman and business units. The life and growth of a business unit depends upon the ethics practiced by a businessman. Business ethics are developed by the passage of time and customs. A custom differs from business to another. If custom is adopted and accepted by businessman and public, that custom will become an ethic. Business ethics is applicable to every type of business. The social responsibility of a business requires the observing of business ethics. A business man should not ignore the business ethics while assuming social responsibility. Business ethics means the behaviour of a businessman while conducting a business, by observing morality in his business activities. The ethos of business ethics should be a part and parcel of every business.

DEFINITION OF BUSINESS ETHICS

1. **According to Wheeler** :Business Ethics is an art and science for maintaining harmonious relationship with society, its various groups and institutions as well as reorganizing the moral responsibility for the rightness and wrongness of business conduct.

2. **According to Velasquez**: Business ethics examines three particular subjects: the systemic issues that are considered as the ethical concerns focusing

on the economic, legal, politic and social structures in which companies perform, the corporate issues which are particular to a specific company and the individual issues which refer to the concerns of an individual working in a specific company.

Business Ethics or Ethical standards are the principles, practices and philosophies that guide the business people in the day today business decisions. It relates to the behaviour of a businessman in a business situation. They are concerned primarily with the impacts of decisions of the society within and outside the business organizations or other groups who keep interest in the business activities . Business ethics can be said to begin where the law ends. Business ethics is primarily concerned with those issues not covered by the law, or where there is no definite consensus on whether something is right or wrong.

3.5 CHARACTERISTICS OF BUSINESS ETHICS

The following are the important features of business ethics :-

1. Business ethics are the principles, norms and standards that guide an organization's conduct of its activities, internal relations and interactions with external stakeholders.
2, It is considered both as a science and an art.
3. It continuously test the rules and moral standards and is dynamic in nature
4. It is based on theological principles such as sincerity, human welfare, service, good behaviour etc.
5. It is based on reality and social customs prevailing in business environment.
6. It studies the activities, decisions and behaviour which are related to human beings
7. It has universal application because business exists all over the world

8. Many of the ethical principles develop the personal dignity

9. Business ethics keeps harmony between different roles of businessman, with every citizen, customer, owner and investors.

3.6 TYPES OF ETHICS

The following are the major types of ethics:

1. **Individual Ethics :** Individual Ethics includes practices in private life of an individual and covers the consistent behaviour according to the beliefs of an individual. The ethical duties and responsibilities can be listed such as not to tell lies, to keep one's word, try not to hurt others. These listed duties and responsibilities may change from an individual to another. For this reason, no single universal right decision exists.

2. **Institutional ethics :** Institutional ethics includes democratic management. Besides that, economic and social development, mutual assistance, equal treatment, volunteering, solidarity, justice and peace are also the main elements of institutional ethics. If responsibilities aren't generally shared, institution may create unethical pressure on in unethical pressure on individuals. When humans share their expectations, mutual aims and values, moral leaders and working people form a team and a family.

3. **Social ethics :** Social ethics stems from the relations of the institutions with society. The responsibilities of the managers are beyond the boundaries of the institutions. Managers have relations with public offices, unions, wholesalers, customers and even competitors. Managers are responsible for environmental pollution, unsafe product and unjust competition. Besides, managers have to abide by the standards determined by professional organizations or chambers, which they are attached.

4. **Global Ethics :**The growth of international business urged the MNCs to develop universal ethical standards. Buller and Mc Evoy suggest that ethical capabilities can be an important source of sustainable advantage in addition to

strategic, technological, financial, and organizational capabilities as source of competitive advantage. A MNC must try to identify and respond effectively to ethical issues in a global context. Business ethics behaviour of firms in a global context can be described in two different frameworks: relativism or absolutism. Relativism refers to behave which is applicable to the saying "when in Rome, do as the Romans do". On the other hand absolutism argues that "home country cultural (and ethical) values must be applied everywhere as they are home".

3.7 IMPORTANCE OF BUSINESS ETHICS

1. **Good Reputation :** Good corporate reputation is built on a solid foundation of ethical culture. Business ethics helps to create mutual trust and confidence in relationship.The public trust is an essential aspect allowing firms to gain the satisfaction of customers.Satisfied consumer will certainly come back and portrays a positive image of the company and its products.Good reputation in the mind of customers will certainle pay in the long run.In a similar fashion, a customer cheated only once by unethical practices adopted'by th£ company is likely to share negative information about a through word of mouth as well as through social networking sites like Facebook,Twitter etc

2. **Cornerstone of Corporate Governance :**Ethics are the cornerstone of corporate governance, in order that firms can meet these ethical expectations Good ethical standard helps the business to face the challenges of corporate governance more effectively.Moreover, A company known for dealing honestly with all the stakeholders is likely to be more successful in business.

3. **Ethical decision making :** Business ethics can help to improve ethical decision making by providing managers with the appropriate knowledge and tools that allow them to correctly identify, diagnose, analyse, and provide solutions to the ethical problems and dilemmas they are confronted with.

4. **Long term sustainability of a business** : Ethical conduct allow companies to achieve a long term liaison with the clients, their assistance and high esteem are essential for success. It helps them to retain the business for long years.

5. **Increased employees commitment :**Employees believe that ethics is an essential instrument encouraging them to keep working for their employer. When a company believes in and practices ethical culture in the company,the employees will certainly feel attached and will be ready to make individual sacrifices for the well being of the company.

6. **Prevention of Fraud :** Ethics play a major role in the prevention of fraud. Fraud prevention becomes a shared responsibility among all the members of the organisation .Business ethics can provide us with the ability to assess the possibility of frauds in organizations and to take effective safeguards to prevent such frauds.

7. **Competitive Advantage** : Business ethics allow companies to have a competitive advantage. Investors well know that an ethical conduct on the part of company contributes to effectiveness and profit earning capacity of the company.

3.8 FACTORS HIGHLIGHTING THE IMPORTANCE OF BUSINESS ETHICS

In the present scenario, we can cite a few factors which highlight the importance of business ethics.

1. **Long-term growth :** Sustainability comes from an ethical long-term vision which takes into account all stakeholders. Smaller but sustainable profits long-term must he better than higher but riskier short-lived profits. Large profits are always attractive, potentially allowing faster achievement of strategic goals, a greater provision against risk and a greater sense of success and stability. However, there are countless examples in corporate history of dramatic boom and bust cycles (both on a micro, corporation level and macro-economic level). Now, more than ever, we need to re-evaluate our endless search for bigger and bigger profits with the bigger and bigger risks that entails. The financial crisis which began in 2008 is painful evidence of that. Whole countries have gone to the brink of bankruptcy as a result of an unwillingness or inability to plan long-term.

More and more organisations are recognising what most owner-run businesses have always known: that stable profits are a better bet in the long run than large profits now and an uncertain future. Even the largest remaining investment banks like Goldman Sachs are having to recognise this (if only to try and fend off more aggressive regulation) and attempting to make their bonus allocations more dependent on longer term value than the current year's performance. One can only hope that the heads of such organisations recognise the importance of business ethics and the resulting need to change to a more sustainable model of growth. Certainly the only way to change the huge, unwieldy vessel that is global business is to focus on the business benefits. While it may seem contradictory and hypocritical to place self-interest at the heart of change for the better, it is the only conclusion that seems to offer hope. Fundamentally the importance of business ethics is driven by personal ethics and morality and most people are fundamentally self-interested. But, if it is in people's best interest to be ethical, this has the potential to drive real change. It is already happening in several consumer markets where demand is shifting to ethical products and social networks are instrumental in spreading stories about unethical practices.

2. **Cost and risk reduction** : Companies which recognise the importance of business ethics will need to spend less protecting themselves from internal and external behavioural risks, especially when supported by sound governance systems and independent research. A precedent which argues the case made above is the Quality Management industry. In the West, this sprung up in the early 1980s, when products began to be inspected before leaving the factory in an attempt to reduce the amount of costly customer complaints. Now, most products come with at least a one-year warranty and in the case of some car manufacturers, up to five years. What started off as a self-interested need to reduce costs has led to more reliable products. Just as widespread bribery and corruption in society are recognised as being inimical to the development of a healthy economy, similarly the lack of a high standard of ethical behaviour in a company is inimical to trust and loyalty, which in turn has a detrimental effect on the health of the company over the longer term.

It may be argued that an owner can run a business in whichever way he or she wishes, and at first glance there would appear to be a case for this so long as no other shareholders are involved, and only his or her money is at risk, and of course with the acquiescence of the employees and trading partners. However, in many years of observing different standards of behaviour in different business circumstances, one recognises the relationship between the perception of ethics which permeates an organisation and the degree of trust and loyalty present among employees and between staff and management. The conclusion one reaches is that loyalty and trust have a significant value in terms of the efficiency and effectiveness with which a business can be run, and the concomitant cost of control systems needed.

In other words, a highly ethical operation is likely to spend much less on protecting itself against fraud and will probably have to spend much less on industrial relations to maintain morale and common purpose. This should be motivation in itself to recognise the importance of business ethics and instil good corporate governance in any organisation.

3. **Core values** : A company's core values are those beliefs and principles that provide the ultimate guide in the company's decision-making. Core values of a company play a very important part in ethical behaviour of a company. In simple terms, core values are set conceptions that you decide to follow in your life or in a business. Core values can be used for living a transparent life and coordinating with other people. Core values are the very significant components of the identity of any business. They are specialized standards set by a company regarding the method of its functioning; decision making, problem solving, and customer service.

4. **Leadership :** It is important for leaders to set the tone by reinforcing a strong ethical culture. The ethical leader understands that cordial relationships germinate and grow in the deep rich soil of fundamental principles: trust, respect, integrity, honesty, fairness, equity, justice and compassion. Maintaining universal ethical values and being sensitive to the laws and customs of a diverse global customer environment can be a competitive advantage.

5. **Culture in the company :** Organization culture represents the common perception shared by members of an organization. Individuals with different backgrounds in an organization altogether have a tendency to describe the organization culture in almost similar terms. The strength of an organization culture has an influence on ethical behaviour of managers. If the culture is strong and supports high ethical standards, it should have a very powerful positive influence on a manager's ethical behaviour, In a weak culture managers are more likely to rely on sub cultural norms to guide their behaviour.An effective organizational culture should encourage ethical behaviour and discourage unethical behaviour.

6. **Influence of co-workers and managers :** Coworkers and management team exert significant control the choices at work through authority and example. In fact, the activities and examples set by coworkers, along with rules and policies established by the firm, are critical in gaining consistent ethical compliance in an organization. If the company fails to provide good examples and direction for appropriate conduct, confusion and conflict will develop and result in the opportunity for misconduct.

8 **Culture in the country :** Culture prevailing in the country also affect business ethics.Individuals in a hard working country(like Japan) will be ethical. On the other hand,in a country where there is rampant corruption, it will have negative influence on ethical behaviour of managers. If the culture is strong in a country, it should have a very powerful positive influence on a manager's ethical behaviour. In Canada or the United States, for example, it would be inappropriate for a businessperson to bring an elaborately wrapped gift to a prospective client on their first meeting-the gift could be viewed as a bribe, hi Japan, however, it is considered impolite not to bring a gift. In Africa or Latin America non-governmental organizations (NGOs), is often a key player within the arena of business ethics. The following table shows the regional differences from a business ethics perspective: the example of Europe, North America, and Asia

TABLE 1: Showing Regional differences from a business ethics perspective : the example of Europe, North America, and Asia.

Query/Continent	Europe	North America	Asia
Who is responsible for ethical conduct in business?	Social control	The individual	Top management
Who is the key actor in business ethics?	Government, trade unions, corporate associations	The corporation	Government, corporations
What are the key guidelines for ethical behaviour?	Negotiated legal framework of business	Corporate codes of ethics	Managerial discretion
What are the key issues in business ethics?	Social issues in organizing the frame work of business	Misconduct and immorality in single decisions situations	Corporate governance and accountability.
What is the dominant Stakeholder manage-ment approach?	Formalized multiple Stakeholder approach	Focuson share-holder value	Implicitmultiple stakeholder approach, benign managerialism

9. **Moral values of a person** : Morals are a person's inner and peculiar character. It may be different between even two human beings. An act regarded as wrong by one person may be regarded as perfectly by another one. Morals are the faith of a person. One good example is of abortion which is totally legal and allowed in the medical ethics whereas it is against the morality of human kind.

Morals are values which we attribute to a system of beliefs, typically a religious system, but it could be a political system of some other set of beliefs. These values get their authority ftom something outside the individual- a higher being or higher authority (e.g. society). In the business world we often find ourselves avoiding framing our ethical choices in1 moral terms for fear that doing

so might prove offensive (lacking in respect or compassion) to some. Many of us find our values are strongly influenced by our sense of morality - right as defined by a higher authority.

10. **Environment in the country :** Economic environment prevailing in a country also has an impact on the business ethics. Ethical differences are often seen in a developed and a Under Developed Country. One of the reasons for this lies in the fact that governments in various African and Latin American countries often are underfunded or even corrupt, and therefore provide limited guidance or legal frameworks for ethical issues.

11. **Formal ethics program :** A survey by the US Ethics Resource Center on attitudes toward and knowledge of ethics and ethics programs indicated that employees' personal ethics improve when their organization has a comprehensive ethics training program. In addition, the study found that individuals in companies that have ethics training programs believe that their business ethics have improved during the course of their careers.

12. **Tolerance level :** The tolerance level of the higher officers also affects business ethics. Tolerance of small lapses in the beginning may create major ethical lapses in future.

13. **Lapse on the part of professionals :** Unethical professionals make a compromise with the dignity of their profession and alter company financial records and man oeuvre numbers to paint false pictures of company successes.

14. **Anti-capitalist sentiment :** The financial crisis marked another blow for the credibility of capitalism, with resentment towards bank bailouts at the cost of fundamental rights such as education and healthcare. The eye-watering profits of some of the world's largest corporations attract a lot of negative sentiment from those outside the world of business and finance. While clearly a result of the scale of these organisations, there is always a suspicion that these profits have been achieved through not entirely ethical means - and in some cases downright uneth downright unethical means, often resulting in major

public failures. Banks in particular receive a lot of bad publicity over profits and executive pay (especially bonuses), and while not always justified, the fact is, an industry at the centre of the credit crunch and resulting economic and financial crisis continued to produce hefty profits and bonuses even while making large numbers redundant. This is, of course, a huge generalisation and simplification of the issue but it is the natural reaction of the general public, who lack such detailed information and understanding. Public sentiment cannot be ignored. This situation makes the importance of business ethics all the more pressing in the 21 st century.

15. **Limited resources :** The planet has finite resources but a growing population; without ethics, those resources are repleted for purely individual gain at huge cost both to current and future generations. One irrefutable fact is that this planet has limited resources. Probably the biggest failure in human development over the last three hundred years has been in recognising that and attempting to minimise use and maximise re-use and recycling. While there are now global initiatives to try and reverse this trend, and much progress has been made, there is still a long way to go. In the major developing economies, especially, history is repeating itself on a massive scale. With notable exceptions, this applies not only to specific environmental and sustainability issues but to corporate governance generally and the importance of business ethics to the new high growth regions and corporations. This is another example of short-term ism prevailing over long-term vision and preservation of limited resources for future generations - and in some cases the same generation, as in deforestation driving native peoples and animal species to the point of extinction. Just as basic financial management requires planning to ensure capital reserves and so solvency, the same principles should clearly apply to the extraction and usage of natural resources.

3.9 PRINCIPLES OF BUSINESS ETHICS

The Principles of business ethics developed by well known authorities like Cantt, J. S.Mill, Herbert Spencer, Plato, Thomas Garret, Woodrad, Wilson etc are as follows

1. **Sacredness of means and ends :** The first and most important principles of business ethics emphasize that the means and techniques adopted to serve the business ends must be sacred and pure. It means that a good end cannot be attained with wrong means, even if it is beneficial to the society.

2. **Not to do any evil :** It is unethical to do a major evil to another or to oneself, whether his evil is a means or an end.

3. **Principle of proportionality** : This principle suggests that one should make proper judgment before doing anything so that others do not suffer from any loss or risk of evils by the conducts of business.

4. **Non co-operation in evils**: It clearly points out that a business should with any one for doing any evil acts.

5. **Co-operation with others**:This principles state that business should help others only in that condition when other deserves for help.

6. **Publicity** : According to W. Wilson, anything that is being done or to be done, should be brought to the knowledge of everyone. If everyone knows, none gets opportunity to do an unethical act.

7. **Equivalent price**: According to W. Wilson, the people are entitled to get goods equivalent to the value of money that he will pay.

8. **Universal value** : According to this principle the conduct of business should be done on the basis of universal values.

9. **Human dignity** : As per this principle, man should not be treated as a factor of production and human dignity should be maintained.

10. **Non violence** : If businessman hurts the interests and rights of the society and exploits the consumer by overlooking their interests this is equivalent to violence and unethical act.

3.10 SUMMARY

Ethical behaviour is one of the essential personal skill that a businessman must possess in addition to competence, confidence, integrity and objectivity.

A company can never succeed if it ignores ethics. Ethical standards should never be compromised while doing business. The company following unethical business practices is bound to fail sooner or later. In short ethics are the highway to success for companies all over the world. Senior professionals must encourage an ethics-based culture in their organisations and among younger professionals because a company following ethical business practices can ultimately survive and thrive in the long run.

3.11 GLOSSARY

1. *Ethics* : It is defined a set of moral principles.
2. *Reputation*: The beliefs or opinion that are generally held about someone or something.
3. *Fraud*: The crime of deceiving someone to gain or personal advantage.
4. *Core* : The central or most important part of something.
5. *Business* : It is defined as a person's regular occupation.

3.12 SELF ASSESSMENT QUESTIONS

1. Discuss scope of business ethics.
2. Define ethics. How is ethics different from morality?
3. Define business ethics. Why ethics must be in business? What are the consequences , if ,any , of not applying ethics in business?
4. Why is the concept of ethics seen negatively in the context of business?

3.13 LESSON END ACTIVITIES

1. "Ethical conduct of business does not impair profitability instead improves it".Discuss in the light of Business Ethics.

Ans. _____

_____

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2. Write a descriptive note on ethical issues related to Top Management . Discuss its usefulness for the company

Ans. _____

_____

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_____

3. Discuss Major ethical issues related to environment protection.

Ans. _____

_____

_____

_____

4. What are the ethical problems that lead to unethical behavior in business?

Ans. _____

_____

_____

_____

3.14 SUGGESTED READING

1. Business Environment by Francis Cherunilam
2. Business Ethics by Sanjeev K. Bansal, Sandeep K. Bansal and Rama Bansal
3. Business Ethics: An Indian Perspective by A. C. Fernando

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LEGAL ASPECTS OF BUSINESS

SEMESTER - I **UNIT-1**

PAPER -IV **LESSON-4**

STRUCTURE

4.1 INTRODUCTION: ETHICAL THEORIES

Theories of business ethics enable a business to do activities which are considered to be desirable and right and avoid various undesirable and wrong activities.In fact, various theories of Business Ethics have been divided into two major categories. These are:

1. Teleological theories

2. Deontological theories

A brief ideas about these is as under:

1. **Teleological theories**:The word Teleological is based on term, teleology which is derived from the greek word, telos which means goal or end purpose. A theory is regarded as teleological when the actions finally bring about happiness. This theory is also considered as consequentiality theory. The main theories covered under it are utilitarianism, universalism, theory justice and virtue theory.

2. **Deontological theories** : The word deontology is based on greek word, deon which means duty. This theory says when people ad here to their obligations, their acts are regarded as ethically right. But the main drawback of this theory is that sometimes even the duties of a person may conflict. Theory of Right and Theory of Duty are covered under .

4.1 OBJECTIVES

After going through this lesson, you should be able to:

- Understand different theories of business ethics.
- Classify the Teleological theories
- Classify the Dentological theories

A brief description of various theories covered under teleological and deontological aspects are as under:

4.2 TELEOLOGICAL THEORIES

- Utilitarianism theory
- Universalism theory
- Virtue theory
- Theory of Justice

UTILITARIANISM

This approach was developed by Jeremy Bentham (1748-1832) and John Stuart Mi!l(1806-1873). It is based on the greatest happiness principle. According to the utilitarian view, the decision that produces the greatest good for the greatest number of people is the best. The business managers should choose the course of action that provides the maximum benefits, or conversely, the course of action that does the least harm, to stakeholders.

It suggests that the morality of an act is determined by its consequences, because of this reason it is also sometimes known as consequential principle also. According to thit theory people should select that option which provides the greatest utility (the highrst degree of satisfaction) to the greatest number affected by a given situation. Here it is believed that actions are right if they are useful to a majority of people. The main concentration is on the consequences of actions, and not on how these consequences are being achieved. Here results are more important than the means adopted to get those results.lt is really a theory of balancing which aims at resolving ethical dilemmas by having maximum benefit to majority of affected people.

FORMS OF UTILITARIANISM

According to David Lyons, there are two forms of utilitarianism defined as under:

1. **Act-Utilitarian** : It denotes that an action is justified if it provides the maximum benefits , or conversely, the course of action that does the least harm, to stakeholders.

2. **Rule-Utilitarian** : It denotes that an action is justified if it confirms to a set of rules the general acceptance of which would provide the maximum benefits , or conversely, the course of action that does the least harm, to stakeholders.

STRENGTHS OF THIS THEORY

The following are the major strengths of this theory:

1. In this theory, it is believed that actions are right if they are useful to a majority of people. That is because of its simple premise, it is most commonly applied ethical theory.

2. In this theory, the worth of each action is judged primarily on its own merits.

MAIN POINTS OF CRITICISM OF THIS THEORY

The following are the major criticisms of this theory:

1. The notion of utility is very vague. It is very difficult to accurately determine what the maximal utility would be for all affected by a situation. Hence, utility, the very foundation of this .theory is not quantifiable and cannot be compared on measurable scale.

2. There are doubts regarding what is the 'majority'. Sometimes its action may benefit the majority at the cost of exploitation of the minority.

3. Utilititarian approach may sometimes result in unethical and immoral choices as it judges morality by the results only,and not by the means.

4. It is very much difficult to foresee the consequences with accuracy.

5. The ethical dilemma for managers is to measure the benefits and harms that will be done to each stakeholder group.

(B) CONCEPT OF UNIVERSALISM

Universalism refers to religious, theological, and philosophical concepts with universal application or applicability. Universalism is a term used to identify particular doctrines considering all people in their formation.

(C) THEORY OF JUSTICE

The main proponent of the theory of justice is John Rawls(1921-2002), a contemporary Philosopher. Rawls' most famous work, A Theory of Justice (1971), provides an introduction to this body of thought as well as some of its

implications for ethics. He focused upon justice because of its substantive importance for organizing and governing society. According to him, justice is the first virtue of social institutions, as truth is of systems of thought. There are basically two theories of defining justice-Merit Theory and Need theory.

1. According to "merit theory" of justice, each individual must be treated exactly as one deserves. He will be rewarded or punished on the basis of merit of his conduct whether it was useful or harmful to society.

2. The "need theory" of justice, which assumes that individual members of society should help those other members who are most in need so as to redress their disadvantages. In this view, "doing good" dictates that every member of society recognize that need entitles the most disadvantaged to some sort of special consideration and that the more advantaged must compensate the disadvantaged with the goal of bringing them up to an acceptable level of advantage.

In simple parlance, justice means to give what is ones due. lt must be noted that dignity of each and every person should be respected. Every individual should be treated in a fair or appropriate manner. For ensuring it, even government intervention is legitimate. Disputes among individuals in business are often interlaced with references to justice or fairness. Resolving disputes requires that we compare and weigh the conflicting claims of each of the parties and strike a balance between them. Justice and fairness are essentially comparative. They are concerned with the comparative treatment given to the members of a group when benefits and burdens are distributed, when rules and laws are administered, when members of a group cooperate or compete with each other, and when people are punished for the wrongs they have done or compensated for the wrongs they have suffered. Standards of justice are generally taken to be more important than utilitarian considerations. If a society is unjust to some of its members, then we normally condemn that society, even if the injustices secure more utilitarian benefits for everyone.

If we think that slavery is unjust, for example, then we condemn a society that uses slavery even if slavery makes that society more productive. Greater benefits for some cannot justify injustices for others. Nonetheless, we also seem to hold that if the social gains are sufficiently large, a certain level of injustice may legitimately be tolerated. In countries with extreme deprivation and poverty, for example, we seem to hold that some degree of equality may be traded off for major economic gains that leave everyone better off. The principle "equal pay for equal work" is also based on Rawls' theory of justice.

Standards of justice do not generally override the moral rights of individuals because justice itself is based on individual moral rights. The moral right to treat each and every person in an equal way is the basic idea behind theory of justice. It must be remembered that generally moral rights of some individuals cannot be sacrificed merely in order to secure, a somewhat better distribution of benefits for others. However, correcting extreme injustices may justify restricting some individuals' rights.

THE CONCEPT OF ORIGINAL POSITION AND VEIL OF IGNORANCE

According to Rawls, cooperation among members of society is very much necessary to make life better .Rawls believes that desires of the members of society may be considered as primary social goods which include among others: health, rights, income, and the social' bases of self-respect. Rawls further remarks that the members of the society will often times disagree about what constitutes the good and how the benefits and burdens within society will be distributed. Some believe that the good consists in virtuous conduct while others may believe that the good is discovered in the pursuit of individual happiness. As far as distribution is concerned, some members may believe that an individual's merit should determine how one will participate in society's benefits while others may believe that society must provide the least advantaged extra assistance so that they will be able to share equally in.

If society is to exist and to endure despite these and other such differences, its members must derive a consensus regarding what minimally constitutes the good.

What consensus requires in actual practice is that the members of society agree upon the rules which will govern them as a society and that these rules will be applied consistently. But the important questions arise: what constitutes a "fair" principle? what is "reasonable" for every member to agree with?

Rawls responded to this challenge by invoking the original position. He has used a thought experiment called "the original position" from which agents behind a "veil of ignorance" select principles of justice to govern society in which representative members of a society would determine, the answers to these difficult questions. The chief task of these representatives would not be to protect individual rights but to promote the welfare of society. The representatives do not know which place in society they will occupy. In fact, every factor which might bias a decision (e.g., one's tastes, preferences, talents, handicaps, conception of the good) is kept away from the representatives. However, they possess knowledge of those factors which will not bias one's decision (e.g., social knowledge, scientific knowledge of the issue etc). From this original position covered by a veil of ignorance about their place in society, Rawls argued the representatives ultimately would select the principle of justice rather than other principles (e.g. natural law, utilitarian principles) to organize and govern society in a rational way.

Rawls argued that this is precisely what would occur in the original position when the representatives operated from behind the veil of ignorance. Freed from focusing upon one's self-interest to the exclusion of others' self-interests, the society which the representatives would design determines what will happen to its members and how important social matters like education, health care, welfare, and job opportunities will be distributed throughout society. The idea is that the representatives operating from behind the veil of ignorance would design a society that is fair and acceptable to all of its members because no individual member would be willing to risk ending up in an intolerable position that one had created for others but had no intention of being in oneself.

Rawls claimed that the representatives to the original position would invoke the principle of rational choice. He supports it with a wonderful example, suppose there is one piece of cake that two persons want to eat. They equally desire to eat the cake and each wants the biggest piece possible. To deal with this dilemma, both agree that one will cut the cake while the other will choose one of the two pieces. The consensus derived guarantees that the cake will be shared fairly, equating justice with fairness. The reason the representatives in the original position and operating from behind the veil of ignorance would agree upon the difference principle is not due to the existence of a social contract but mainly due to ethical considerations.

CLASSIFICATION OF JUSTICE

Issues involving questions of justice and fairness have been divided into following three categories.

1. Distributive Justice

It is the first and basic category. It is concerned with the fair distribution ofsociety's benefits and burdens among its members. Generally different people put forth conflicting claims on society's benefits and burdens and all the claims cannot be satisfied. The claims may relate to issues such as jobs, food, housing, medical care, income, and wealth etc. where a number of participants are there. On The other hand, there may be some areas say unpleasant work, drudgery, substandard housing, health injuries of various sorts, here not enough people will be willing to help. If there were enough goods to satisfy everyone's desires and enough people willing to share society's burdens, then conflicts between people would not arise and distributive justice would not be needed. The real problem arises when people's desires exceed the adequacy of their resources. Then principles for allocating scarce benefits and undesirable burdens in a just and equitable ways are needed to be developed. The fundamental principle of distributive justice is that, equals should be treated equally and unequal treated unequally. Another opinion put forward is that a society's benefits should be distributed in proportion to what each individual contributes to a society and/or to a group.

2. Retributive Justice : It is concerned with just imposition of punishments and penalties on those who do wrong: A just penalty is one that in some sense is deserved by the person who does wrong. It must be noted that a wrongdoer must be punished only under the valid conditions under which it is just to punish a person him for doing wrong. Penalising anybody on the basis of flimsy or incomplete evidence will surely be a case of injustice. Another point to be kept in mind is that the punishment must be consistent and proportioned to the degree of offence wrong. Punishment will be considered just and consistent only when everyone is given the same penalty for the same wrong/offence.

3. Compensatory Justice : Compensatory justice concerns the justice of restoring to a person what the person lost when wronged by someone else. When one person wrongfully harms the interests of another person, the wrong doer has a moral duty to provide some form of restitution to the aggrieved person. A just compensation is one that in some sense is proportional to the loss suffered by the person being compensated. There are no hard and fast rules for determining how much compensation a wrong doer owes the victim. Justice requires that the wrong doer should restore whatever was taken from the victim. The main conditions involved in this case are: the action that inflicted the injury was really wrong ,the wrongdoers action was the real cause of the injury and he inflicted the injury voluntarily.

PRINCIPLES GOVERNING JUSTICE

Rawls argued that two principles serve to organize society, the liberty principle and the difference principle. The liberty principle and the difference principle apply to the basic structure of society i.e. society's fundamental political and economic arrangements rather than to particular conduct by governmental officials or individual laws. The brief details of these principles is as under:

1. The Liberty Principle

The liberty principle requires society to provide each citizen with a fully adequate scheme of basic liberties. It states that every persons basic liberties

must be protected from interferences by others. Moreover, each member of society must be entitled to an equal right of liberties available to others. The liberties include:

- political liberty (the right to vote and to be eligible for public office).freedom of speech and assembly.
- Right to live and right to personal privacy.
- Freedom of conscience and freedom of thought.
- Rule of law to get protection.

2. The Difference Principle

The difference principle requires that inequalities in wealth and social position be arranged so as to benefit society' least advantaged group. All possible steps must be taken to improve the conditions of least advantaged section of society in order to maintain justice, fairness and welfare.

IN CASE OF CONFLICT BETWEEN TWO PRINCIPLES

According to Rawls, in case of a conflict between these two principles, the liberty principle must always take precedence over the difference principle because society cannot justify a decrease in liberty by increasing any member's social and economic advantage.

CRITICISM OF THEORY OF JUSTICE

The theory of justice has been criticised by a number of thinkers on the following grounds:

1. The theory has been criticised on which members of society constitute the "least advantaged"? Rawls definition has ignored the truly least advantaged rnembers of society, namely, those citizens of some permanently unemployed underclass, who depend entirely upon government aid and we fare measures to subsist.

2. Rawls over emphasis on primary social goods has been criticised by a number of modern thinkers.

3. Rawls" concept of original position and the veil of ignorance to elaborate the theory of justice are not acceptable to all. Maclagan is of the opinion that the parties who are not in the original position and who are not operating from behind a veil of ignorance. Can also move forward adjudicate their differences amicably and for the benefit of both. The best example here is that of collective bargaining.

4. Rawls' states that inequalities are permissible but only if they better the lot of the least advantaged members of society. Whereas in original position Rawl claim that the representatives to the original position must not take an interest in anyone's particular interests, it is really contradictory.

5. Rawls has neglected to consider the market forces unleashed in a capitalist society where seeking one's self-interest is arguably the primary motivating principle. Critics argue that even the least advantaged, if they so choose, can take advantage of the minimal benefits society offers them by virtue of citizenship.

6. The difference in earnings of individuals may be due to their qualifications, experience and personality factors. There is no justification in it that everybody earning more should distribute his/her hard earned money among the needy and underprivileged.

FURTHER DEVELOPMENTS

Keeping in mind the criticisms, Rawls modified the principles of liberty and difference. Rawls considered how a society ordered by the two principles of liberty and difference might endure. In Political Liberalism (1996), Rawls introduced the idea that stability can be found in an overlapping consensus between citizens who hold diverse religious and philosophical views or conceptions about what constitutes the good to be sought. In Justice as Fairness

(2001), Rawls introduced the idea of public reason, that is, the reason possessed by all citizens which contributes to social stability.

CONCLUDING REMARKS

The theory of justice is broad as well as rational. The rights secured by justice are not subject to political bargaining. Rawls maintained that inequalities in society can only be justified if they produce increased benefits for the entire society. His concern towards least advantaged members of society is really praiseworthy. The principle of equal pay for equal work is based on the theory of justice. All must be treated in an equal way and no special treatment should be given to anyone in violation of theory of justice .In addition, every member of the society must be given opportunity to pursue their choice so that he may give his whole hearted contribution towards the betterment of the society.

(D) VIRTUE THEORY

The word Virtue has been translated from the Greek word Arete which means to be the best at something one can be. Virtue is a quality of an individual and expressed in his behaviour. Good virtues like honesty, integrity and courage etc are really helpful in ethical behaviour. Virtues are really embedded in the personality of an individual, and are not the forced one and it is not a one time affair. For example, all of us know that honesty is a virtue of a person, but we will say an individual honest if he act in an honest way as a general practice, we will not call an individual honest if he act in an honest way once in a year or if he is forced to be honest in a particular casein other words, virtue ethics is concerned with the whole of a person's life, rather than particular episode. According to Socrates, knowledge is equal to virtue and virtue is equal to happiness. Plato discussed four key virtues: wisdom, courage, temperance and justice. The first systematic description of virtue ethics was written down by Aristotle in 350 BC and it was dedicated by him to his son Nicomachus. According to him, there are two types of virtues viz. Intellectual virtues and Moral virtues. He further says that when people acquire good habits of character, they are better able to regulate their emotions and their reason. It helps in reach

morally correct decisions even when we are faced with difficult choices. Even various religions of the world provides a mention of these virtues. For example, in Hinduism, the following virtues have been enshrined:

1. Honesty
2. Universality
3. Peace
4. Non-Violence
5. Reverence
6. Altruism
7. Restraint

BENJAMIN FRANKLIN 'S LIST OF VIRTUES

Benjamin Franklin, one of the greatest citizens and thinkers the world has given the following list of virtues:

1. Temperance - eat not to dullness; drink not to elation.
2. Silence - Speak not but what may benefit others or yourself; avoid trifling conversation.
3. Order - Let all your things have their places; let each part of your business have its time.
4. Revolution - Resolve to perform what you ought; perform without fail what you resolve.
5. Frugality - Make no expense but to do good to others or yourself; that is, wast nothing.
6. Industry - Lose no time; be always employed in something useful; cut off all unnecessary actions.
7. Sincerity - Use no hurtful deceit; think innocently and justly; speak accordingly.

8. Justice - Wrong none by doing injuries; or omitting the benefits of your duty.

9. Moderation - Avoid extremes; forbear resenting injuries so much as you think they deserve.

10. Cleanliness - Tolerate no un cleanliness in bocy, clothes, or habitation.

11. Tranquility - Be not disturbed at trifles or at accidents common or unavoidable.

12. Chastity - Rarely use venery but for health or offspring, never to dullness, weakness, or the injury of your own or another's peace or reputation.

MAJOR ELEMENTS OF VIRTUE ETHICS THEORY

The following are the major elements of virtue ethics theory:

Eudaimonism: This is mainly an agent focussed theory. Eudaimonia means happiness and fulfilment. Aristotle is of the opinion that all the things that are ends in themselves also contribute to a wider end, an end that is the greatest good of all. He further says that the good man is the man who reasons well. This is the life of excellence. Eudaimonia is the life of virtue-activity in accordance with reason, man's highest function. Rosalind Hursthouse has further developed eudaimonist virtue ethics. It claims that the good life for an individual is the life of virtue and therefore it is in the interest of an individual to be virtuous.

1. Agent Based Theory: Agent based theory was developed by Michael Slote. This theory concentrates that virtues are mainly determined by common sense intuitions which we find admirable & and which are often there in the traits of other people whom we really admire.

2. Ethics of Care: Annette Baier has contributed a lot towards this theory. This theory states that while performing our duty we should not only consider justice and autonomy but also other factors like taking care of others, having patience, having ability to nurture and making self-sacrifice etc.

IMPORTANCE OF VIRTUE ETHICS

Virtue ethics is relevant and important for business world. It emphasises on the whole life of an individual and not any particular episode of his life. Virtue ethics really play an important contribution in our understanding of morality because they emphasize the central role played by motives in moral questions. To act from virtue is to act from some particular motivation; thus to say that certain virtues are necessary for correct moral decisions is to say that correct moral decisions require correct motives. Virtue Ethics claims that a virtuous person is most likely to make correct moral decisions.

KEY QUESTIONS OF VIRTUE ETHICAL SYSTEMS

In fact ,the following are the various key questions that virtue ethical systems ask :

- What kind of person do I want to be?
- What virtues are characteristic of the person I want to be?
- What actions will cultivate the virtues I want to possess?
- What actions will be characteristic of the sort of person I want to be?
- with the practicalities of how we should behave.

CONCLUSION

Virtue ethics should be treated as ways to understand how to become moral creatures and how to develop the means by which we may be able to make moral decisions, and the process by which moral attitudes may be developed. No doubt, there are a number of valid objections against virtue ethics but at the same time it is also true that in the initial years, these may be able to teach us how morals themselves should be taught.

4.4. DEONOTOLOGICAL THEORIES

(E) THEORY OF RIGHTS

The first person credited with developing a comprehensive theory of rights was British philosopher John Locke (1632-1704). Locke wrote that people form societies, and societies form governments, in order to assure the enjoyment of "natural" rights. Locke defined government as a "social contract" between rulers and ruled. Locke was of the opinion that citizens should give allegiance only to a government that protects their human rights. Government must systematically protect the human rights of its citizens.

The main limitations of Locke's theory is that he did not consider the claims of all people. In fact, his actual focus was the protection of the rights of European men owning property. Women, along with indigenous peoples, servants, and wage labourers, were not recognized as full rights-holders. Still, it can be remarked that the theory of Locke was an important breakthrough.

GENERAL CLASSIFICATION OF RIGHTS

The following is a general classification of rights:

1. **Positive rights** : Positive rights are those rights that others have a duty to supply. In a welfare state government should provide certain benefits (positive rights) to the citizens. For example, if an individual has a right to education, then the government has a duty to fulfil individuals needs.

2. **Negative rights**: Negative rights are the rights free from interferences by others in pursuing ones right of life, liberty and property,

3. **Moral Rights** :Moral Rights are the rights which are based on moral norms entitling all persons to do something or to have something to be done for them.

4. **Legal Rights** :A right provided by the legal system or the constitution of the country is known as a legal right. In India, a number of rights are provided by our constitution. Important being right of constitutional remedies etc.

5. **Human rights** : Human rights are those moral rights of humans as such, rights that humans have in virtue of being human.

6. **Natural rights**: Natural rights are moral rights that humans (in the moral sense) have because of their nature, or in virtue of being human. But this is simply a consequence of the fact that they are moral rights that humans have because of their nature, as opposed not only to legal and other conventional rights, but also to civil rights.

7. **Civil rights** : Civil rights are moral rights of citizens as such. In moral and political philosophy, they are often further defined as the rights that constitute free and equal citizenship in a liberal democracy.

8. **Inalienable right** : An inalienable right is one that cannot be transferred. And in moral philosophy, the term is often used more broadly to refer to a right that cannot be lost or given up either by transfer, forfeiture, or waiver.

CLASSIFICATION OF RIGHTS GIVEN BY HOHFELD

Hohfled has classified the rights into four basic categories viz. Claim , liberty, power, and immunity. The brief description of these is as under:

(1) **Claim** : It is entitlement of a person to get something from another person.

(2) **Liberty** : It means privileges, licenses or permissions/freedom to do something.

(3) **Power** : It means the authority given to someone. In other words, it is the legitimate power.

(4) **Immunity** : It means some special legitimate power to thwart others power in some circumstances.

(F) CONCEPT OF CONSENT, WAIVER, AND FORFEITURE

One does not violate a person's rights if one acts with that person's consent. Sometimes a right may be waived. It means giving it up voluntarily. To Forfeiture of a right may result from wrongdoing.

(G) OTHER RELEVANT THEORIES

A few other relevant theories in this context have been described as under:

Constraint Theory : It states that rights are constraints or restrictions on what we may do to promote good ends or optimal outcomes-limits on what it is permissible to do, even to achieve noble ends or the greater good. It provides rights a non-instrumental status but may take them to be derivative of other sorts of constraints, including obligations or duties.

Instrumental Theory : It claims that moral rights are instruments either for promoting valuable ends or outcomes or for acknowledging the moral status of persons. Such theories assign rights and respect for rights a derivative status. For a few practical purposes, rights function as if they were constraints.

End-state Theory : This is also known as goal-rights theory. According to this theory, if the duties are fulfilled and the rights are not violated and if they are respected ,then these are valuable ends in itself and, therefore contribute towards the overall value of states of affairs. It assigns rights and respect for rights a non-derivative status, as intrinsic goods and ends to be promoted. This theory does not consider rights as constraints.

Concluding Remarks : Generally a theory of rights is a complete moral theory. Because by knowing what the rights of the relevant parties are ,we are not in a position to say what one ought or ought not do. It is also important to know that all duties or obligations do not entail correlative rights. One thing must be kept in mind that it is always presumptively wrong , immoral and unethical to infringe a claim right of other party. But this presumption is rebuttable where the right in question is not absolute, and any claim that a right is absolute will be controversial.

(H) ETHICS OF CARE

Ethics of care approach to has been developed primarily by feminist ethicists. It originated in the claim of psychologist Carol Gilligan that women and men approach moral issues from two different perspectives. Man lays

emphasis on justice and impartiality, whereas women concentrates mostly on aspects of care. But now it is not so, ethic of care is not for women only. In fact, caring is a moral imperative for both men and women. Annette Baier has also contributed a lot towards this theory. This theory states that while performing our duty we should not only consider justice and autonomy but also other factors like taking care of others, having patience, having ability to nurture and making self-sacrifice etc. Ethics of care addresses what I know and who I am as well as how to act toward others. Like in business, a company has a responsibility towards the workers, both blue-collar and white-collar. An equal responsibility is there towards community. All human beings are a part of society. Moreover, all of us are bound by a social system and family values. Traditional approaches to ethics are inadequate to address the challenges of our diverse social existence. In a number of circumstances, it is found that a company had no legal obligation to continue to pay his workers while they were not working, but still a few glaring examples are there which signifies the ethics of care. In fact, ethics of care motivated such companies to take care of their workers precisely because they were their workers and had built concrete relationships with him, helping them build their business empire in the past and to enable the company to get competitive advantage in the industry.

Ethics of care theory is characterized by the notion of caring for others and attention paid to the others. Other approaches to ethics lays emphasis on the fact that ethics should be impartial and therefore any special relationships with relatives, friends, or one's employees, should be set aside when determining what one should do. But ethics of care approach believes that the earlier approach is perverse and mistaken. Ethics of care pre-supposes that special relationship of love and caring that an individual has with your parents(and a businessman has towards his workers) gives him a special obligation to care for them in a way that overrides obligations he may have toward strangers.

FEATURES OF ETHICS OF CARE

Ethic of care is a theory that revolves around the interdependence of all individuals. The following are its distinguishing features:

1. Ethic of care is concerned with caring for someone in the way as a mother cares for toward her child. Such caring is focused on persons well-being, not on things. Here, it is to be mentioned that ethics of care does not promote dependence, but nurtures the development of the person to enable him to live his own life. Ethic of Care supports a relationship of interdependence and mutual benefits, and to help in enabling other party to live an

2. Ethics of care highlights the importance of a lack of universal truth. It concentrates on taking into account contextual details of each place such as the local customs, cultural heritage and traditions, economy, history and language etc. to promote the needy.

3. Ethic of Care supports giving the best and most considerate services to the needy.

4. Ethic of Care pre-supposes that if you are qualified and has the skills necessary to meet the needs of the local community, you can serve the needy in a better way.

BASIC PREMISES OF ETHICS OF CARE

The basic premise of the ethics of care can be understood well from the following points:

1. Ethics of care is based on the premise that we have an obligation to exercise special care toward those particular persons with whom we have valuable close relationships, particularly relations of dependence. We should preserve and nurture those concrete and valuable relationships we have with specific persons.

2. A morality of care "rests on an understanding of relationships as response to another in their terms." In such cases, the moral task is not to follow universal and impartial moral principles, but instead to attend and respond to the good of particular concrete persons with whom we

are in a valuable and close relationship. Compassion, concern, love, friendship, and kindness ate all sentiments or virtues that normally manifest this dimension of morality.

3. Ethics of care emphasises on special care for those with whom we are concretely related by attending to their particular needs, values; desires, and concrete well-being as seen from their own personal perspective, and by responding positively to these needs, values, desires, and concrete well being, particularly of those who are vulnerable and dependent on our care.

4. This requirement to take care of specific group of individuals personally known is more significant than any moral requirement to care for strangers in other countries.

5. Ethics of care is not restricted to concrete relationships between two individuals or to relationships between an individual and a specific group. In fact, ethic of care should also encompass the larger systems of relationships that make up concrete communities. Such broader relationships should be preserved and maintained. The theory pre-supposes that an individual cannot exist, cannot even be who he or she is, in isolation from caring relationships with others. Initially he needs others feed and care for him. Parents, friends, relatives and other well wishers are needed. Such relationship and value should be maintained and nurtured. The value of the self, then, is ultimately derived from the value of the community.

6. Ethics of care are concerned with the relationships that are really having value. It must be noted that all kind of relationships do not have value, and such relationships are not covered by the ambit of ethics of care. Relationships characterised by hatred, violence, disrespect, domination, oppression, injustice, exploitation, and resulting in harm to others lack the value that ethics of care requires. Ethics of care implies that relationship of love, compassion, concern, friendship, and loyalty are very valuable and such relationships should be nurtured.

CONFLICTING POINTS IN ETHICS OF CARE

It is important to recognise that the demands of caring are sometimes in conflict with the demands of justice. For example, in some cases where the Boss who has been controlling a number of subordinates, and say one of his subordinates is his close friend also, then there will be a conflicting situation for the Boss to recommend the name of a subordinate for promotion. It may happen too often in real life. There is no fixed rule to resolve all conflicts. We may imagine situations in which the Senior Managers obligations of justice towards the company would clearly override the obligations he has towards his friend. His first and foremost duty is duty to protect the resources of the company and abide by company policy. This clause of his appointment letter will stop him from showing some favouritism towards his friend in violation of the company policies The institutional obligations we voluntarily accept and to which we voluntarily commit ourselves, then, can require that we be impartial toward our friends and that we pay more attention to the demands of impartial justice than to the demands of the ethics of care.

OBJECTIONS TO ETHICS OF CARE

The ethics of care approach to ethics has been criticised on the following grounds:

1. It has been claimed that an ethic of care can degenerate into unjust favouritism. Being partial, for example, to members of one's own ethnic group, to members of one's own race, or to members of one's own nation can all be unjust forms of partiality. Proponents of an ethic of care, however, can respond that, although the demands of partiality can conflict with other demands of morality, this is true of all approaches to ethics. Morality consists of a wide spectrum of moral considerations that can conflict with each other. Utilitarian considerations can conflict with considerations of justice, and these can conflict with moral rights. In the same way, the demands of partiality and caring can also conflict with the demands of utility, justice, and rights. What morality requires is not that we get rid of

all moral conflicts, but that we learn to weigh moral considerations and balance their different demands in specific situations. The fact that caring can sometimes conflict with justice, then, does not make an ethic of caring less adequate than any other.

2. Its demands can lead to "burnout." In demanding that people exercise caring for children, parents, siblings, spouses, lovers, friends, and other members of the community, an ethic of care seems to demand that people sacrifice their own needs and desires to care for the well-being of others. However, proponents of caring can respond that an adequate view of caring will balance caring for the caregiver with caring for others.

CONCLUDING REMARKS

In these respects, an ethic of care provides an important correction to the other approaches to ethics which all emphasise impartiality and universality. An ethic of care, with its focus on partiality and particularity, is an important reminder of an aspect of morality that cannot be ignored. The advantage of an ethic of care is that it forces us to focus on the moral value of being partial toward those concrete persons with whom we have special and valuable relationships and the moral importance of responding to such persons as particular individuals with characteristics that demand a response to them that we do not extend to others. Care theory needs to be more than an academic pursuit. It is gaining popularity but only among some academics. Care needs to be a social and political value that helps repair our world. This theory is based on individuals moral sensivity. Moral sensivity is more applicable to intimate relationship than a far anonymous relationship. Thus ethics of care provides a long run vision of the interdependent relationships.

4.5 SUMMARY

In this lesson a detailed study has been conducted on ethical theories. The business ethical theories are divided into two major categories i.e teleological

and Deontological theories and these further are further subdivided into various theories. These theories of business ethics enables a business to identify those activities which are correct and avoid those which are wrong and undesirable.

4.6 GLOSSARY

1. *Virtue*: It is a behavior showing high moral standard.
2. *Morality*: The extent to which an action is right or wrong
3. *Veil*: It is a thing that hides or disguise.
4. *Dilemma*: It is referred as a difficult situation or problem

4.7 SELF ASSESSMENT QUESTIONS

1. "An action is right if anyone produces the greatest balance of pleasure over pain foe everyone." Elaborate.
2. Elaborate with examples the utilitarian theory of ethics.
3. Discuss the right theory of ethics and its implications in present business scenario
4. Discuss the salient features of theory of virtue ethics
5. What is more important, law or ethics? Discuss

4.8 LESSON END ACTIVITIES

1. Compare and contrast between 'Rights Theory' and 'Justice Theory'.

Ans. _____

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2. Write a detailed note on Teleological Theories and Deontological Theories.

Ans. _____

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3. Explain teleological theories in detail.

Ans. _____

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4. Describe the classification of Theory of Justice.

Ans. _____

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4.9 SUGGESTED READING

1. Business Environment by Francis Cherunilam
2. Business Ethics by Sanjeev K. Bansal, Sandeep K. Bansal and Rama Bansal
3. Business Ethics: An Indian Perspective by A. C. Fernando

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-II**

PAPER -IV **LESSON - 5**

STRUCTURE

5.1 INTRODUCTION

The essence in the evolution of the human and humane is in the ability of its learning, observing and introspecting the ethics and values. Ethics and values denote something's degree of importance with the aim of determining what action is the best to live or to do or at least attempt to describe the value of different actions. The fundamentals of living are being learnt on none other than through the acquisition of language, and the widely developed literature universally. The introspection of the self and the retrospection only always create room for further development in any dimension in general and in ethical point of view in particular. The development of the universal culture solely depends up on the development of the language. For Indian life style, philosophy and for the nurturing of ethical values, the epics like Ramayana, Mahabharatha and Bhaagavatha and various forms of literature like Upanishads, Aaranyakas have laid the corner stone, and given the continuous renaissance through their language with a splendid stature and enriched with affluent literature.

The very widely discussed issue all over the world is the inclination of ethical values and morals. It is being perceived by most of the intellectual and spiritual masters that the culture is slipping into red with a quick evasion of the standards as suggested by our ancestors. It is the need of the hour to introspect ourselves and retrospect the globe around with a deep analysis to know about the rich heritage of humane of the world in general and of India in specific. To the credit of our nation we do have lot of guiding literature to us from ages back to thousands of years and that provides the rays of light for each and every walk of our life. The introspection and retrospection can be done by even by an average intelligent person or even a lay man by going through the Itihas as and epics

5.2 OBJECTIVES

After going through this lesson, you should be able to:

- Understand the relevance of ethical values
- To be familiar with the concept of ethics and Indian value system

- Understand the Indian value system in relation to business ethics
- Explain the characterstics of Indian value system and ethic

5.3 RELEVANCE OF ETHICAL VALUES OVER SUCCESS IN BUSINESS

Success in business depends not only on the way that the objectives are established and achieved, but also on the manner in which values and moral practices are cultivated which encouraged honesty, correctness, responsibility of each employee. Without cultivating the environment to create and respect values, a company will be faced with challenges like bribe, corruption, deceit, favouritism etc. Strong companies do not exclusive relay on rational instruments of scientific management (strategy, system, structure) for obtaining performance. They promote values like honesty, correctness, trust on all levels of their activity. These values are cultivated at the level of the entire organization and permit making a unique vision for achieving the major objective. A high level of trust among employees towards ethical values promoted by company's management is very much necessary.

If an organization values profit, productivity and quality it will prefer to operate in a way that prioritizes action and behaviour that reflects those values. Another organization that values innovation, research and learning will prefer to operate in a way that prioritizes action and behaviour that reflects those values. For either organization, if the values that are influencing daily behaviour and actions are not aligned with the strategies then their performance and results will suffer. For success in business the following points should be considered.

1. ETHICAL VALUES FOR INDIAN MANAGERS

Indian managers are moving away from the concept of values and ethicsj The lure for maximizing profit is deviating them from the value based managerial behaviour. (There is a need for our managers today both in private and public sectors to develop a set of values and believes that will help them attain the ultimate goals of profits and survival and growth. They need to develop the following values: Optimum utilization

of resources; Attitude towards work- Managers have to develop the visionary perspective in their work. They have to develop a sense of larger vision in their work for the common good.; Work commitment; and Vision- Managers have a long term vision. The visionary managers must be practical, dynamic and capable of translating dreams into reality.

2. ETHICAL VALUES FOR WESTERN MANAGERS

Western managers are highly professionals with excellent analysis power, high professional education and specialization. Western managers follow a proper code of conduct and work in the structured formal atmosphere with no place of modesty in their behaviour. Professional efficiency and work disciplines are the conditions under which western managers perform. They consider rules as sacred in their value system. Western value system teaches contractual obligations. Managers honour their contracts. Western managers value principles above its privilege and they consider this as the best strategy to win

Remember that for making your business stand in the competitive market and leading it to success, you should create core values that would speak out in accordance with the quality of services your provide.

3. ETHICS FOR SENIOR MANAGEMENT

Top Management has the responsibility to create a work environment that helps an organization in maintaining ethical business relationships while achieving its primary objectives. Ethics should be the topmost priority for all members of the senior management of the company management in all of their dealings on behalf of or with the Company.

Environmentalism is at first a concern of top management since its principles must be adopted at corporate level, as policy, before an organisation can properly adopt them throughout. Top Management has always been expected by staff, investors and all other stakeholders to

maintain high ethical standards. Top Management must ensure that the company conducts business in full compliance with all applicable laws of the land. The company must deal fairly with suppliers, customers, business partners and others with integrity and honesty. The old saying "Yatha Raja Tatha Praja" meaning thereby that the conduct below is the reflection of the conduct of the ruler, must be remembered and therefore the Top Management should try to set examples by differentiating values from disvalues.

Top Management must act as per professional ethics depending on their position and training. Fiduciary duty is an example that applies to some managerial roles. The compliance and ethics program should strive to deliver tangible benefits and outcomes to the organization. First, managers are responsible for upholding ethical standards themselves. Additionally, managers may be responsible for creating and/or implementing changes to the ethical conduct of the organization.

4. ETHICAL DUTIES TOWARS BUSINESS PARTNERS

As far as selection of business partner is concerned, only a trustworthy partner practising Good Personal and Business Ethics and having good reputation in the market place should be selected. A poorly chosen business partner may end up hijacking your innovative ideas or valuable clients to start their own business in the same line of business, or breaking laws that could get your company into legal trouble.

A company must appreciate that it is supported in the business activities by their business partners. There may exist companies making short-term revenues by cheating their business partners, but in the long run this will certainly turn against the company. Therefore the companies must work with these partners for mutual gains. It becomes first and foremost duty of a company to act in the utmost good faith while dealing with the business partners. A company should build fair and equitable partnerships with business partners and keep the following points in mind:

- The company must obey Legal Compliance issues regarding partnership.
- It should promote fair and equitable procurement activities that comply with each country's laws and respect international standards or conduct.
- The business partner should be provided with an opportunity for equitable competition.
- Every possible effort must be made to have better co-operation and co-ordination with Business Partners.
- Along with educating its own staff, the company should hold briefings for their major business partners viz. raw materials suppliers, manufacturing licensees, and distributors/suppliers and conduct surveys among them regarding relevant issues.
- A company must receive Feedback from Business Partners and on the basis of this feedback, it must improve in the areas where there is a need and scope for improvement.
- Apart from daily interactions with business partners, the company should hold regular dialogues with their business partners at briefing sessions, conferences and quality workshops.
- The company must prefer Safe and Eco-friendly Distribution. The companies well versed in a particular field say safety issues, may guide them and help them in enhancing Safety at their premises.
- Like a good friend, a company should help their business partners in case of emergencies and adverse business circumstances. The old saying, a friend in need is a friend indeed must be practised by the company in true spirit.

5. ETHICAL DUTIES TOWARDS COMPETITORS

A company must keep in mind that its competitors are just the competitors. However, company's behaviour towards them may affect company's own customers. Company's behaviour towards them will show company's ethics. Each and every step by the company will be watched by the media and cosumer bodies. That is why it is suggested that competitors should be tackled very carefully. Companies should try to develop a good relationship with competitors. When customers see you have strong ethics in dealing with your competitors, they will really honolir you and it will be in the long term interest of the company. The following aspects must be adopted while dealing with the competitors:

1. **Dont be Jealous of their Success** : When a competitors performs well, the company should congratulate them and should not be jealous of their success.But it is also important that the company must introspect itself and find out the major points of viations. Recognising others success hows strong ethics followed by the company and will certainly havea positive impact on the mind of prospective customers.

2. **Co-Operation along with Competition** : A company should not mind giving a small portion of its not so successful business to a competitor whom the company thinks is in a better position to serve customers of thar area. In this way,your image in the eyes of customer will improve and in future,the competitors may also do the same for you resulting in a win-win situation for both the parties.

3. **Evolve Fair Competitive Strategies** : The companies should not blindly criticise the competitors, rather it should inform the prospective customers about positive and negative points of competitors products. Even when the competitors services are far from satisfactory, the company should act tactfully towards competitors while addressing as well as attracting the prospective customers. The company negative issues, the company should also appreciate their problems. It will demonstrate strong ethics of your company

4. No Tit for Tat Policy : When a company comes to know about something insulting and unethical said by a competitor, it must behave in a cool and calm manner. A well developed strategy must be used to give the competitor an answer while remaining within four walls of ethical considerations. By directly adopting tit for tat policy, the public image and reputation of the company will be adversely affected to a large extent.

It must be noticed that if the competition is fair, it meets the requirements of high ethics, and then it will be one of the fundamental sources of economic development.

6. ETHICAL ISSUES REGARDING GLOBAL BUSINESS

As a result of globalization cross-border exchange of goods, services, capital, technology, ideas, information and people has taken place. Now as a result of globalisation, the world has become a global village. The following are the major ethical issues in the context of global economy:

A code of ethics in the light of prevailing environment in the host country must be developed and this code of ethics must be made clear to all concerned with the company.

- A global company should not adopt malpractices like corruption, bribery, misrepresentation, and tax evasion etc. All the staff members must be sensitized about the hard penal provisions for induldging in unethical business conduct.

- All the responsible officer must be made familiar with governmental rules and regulations applicable to the industry in the country in which the MNC operate.

Everyone in the MNC must be instructed to comply with federal, state and local laws.

In a similar way, they must be made aware of the local culture, and everyone in the MNCs must be instructed to respect the tradition and culture of the host country.

It must try to transfer the best ethical practices learnt from one country to all the other MNCs operating in a group. It must collaborate with local people to improve understanding of the expectations of the local residents from the company, and in this way chalk out the strategies to help less advantaged people.

The MNC must follow the guidelines of various international agreements and it must follow general principles for business practice framed by various international organisations like OECD.ILO etc.

MNC managers must try to protect the environment of the host country in the long run. In order to tackle the problem of scarcity of natural resources in the host country, they must look for alternate raw materials. They should try to devise new methods of recycling or disposing of used materials and expanding the use of by-products.

7. ETHICS IN FINANCIAL MARKETS

This can be defined as the general action that the financial markets adhere to in the daily conduct of business. It affects how the financial markets deals with the investors. Companies raise money from the investors through the mechanism of financial markets. That is why, an ethical behaviour on the part of companies is needed. While working through the financial markets, the companies must maintain honesty, be fair and human ,and must set an example as far as ethical considerations are concerned.

Financial Markets worldwide have shown increased connectivity and interdependence due to improvement in the information communication technology, internet and electronic banking .Increased proliferation of the multinational corporations has resulted into the liberalization, extension and internationalization of the financial markets of the financial markets worldwide. Now capital inflows from the wealthier parts of the globe can be expected, promoting savings ,investments and employment. But liberalization of financial markets has raised a number of ethical issues as

well. The unethical practices like corruption have also increased manifold. As a result of global financial liberalisation, poor nations will be forced to open their markets to financial corporations that will offer undue competition to their local firms and create financial crisis. Financial market instability in the global world pose the greatest danger to developing countries than to the developed countries. There is an urgent need for a global code of ethics to rectify the structural inequalities which may be created by transnational financial institutions planning to operate globally.

5.4 UNETHICAL BUSINESS PRACTICES

In common parlance 'unethical' refers to an activity in which a company has acted exclusively in its own self-interest and, at the same time causing or trying to cause some harm to others. But it is also true that the use of unethical business practices has become very rampant, particularly in Indian Corporate Sector. In the long run, these unethical business practices often fizzle out by putting the business in legal complications and an environment of general mistrust. Following are some of the activities that come under the ambit of unethical practice:

1. Cheating the customers by selling substandard or defective.
2. Duplication and piracy.
3. Resorting to dishonesty or deception.
4. Distortion of facts to mislead or confuse the buyer.
5. Manipulating people emotionally by exploiting their vulnerabilities.
6. Hoarding and black marketing to earn excessive profits.
7. Tax evasion and voiding penalty or compensation for unlawful act.
8. Manipulation of business records and lack of transparency.
9. Adopting unfair trade practices
10. Harming the environment by exceeding the government prescribed norms for pollution

5.5 ETHICAL PROBLEMS FACED BY MANAGERS

The ethical problems faced by managers can be divided into two categories:

1. In various departments
2. In General

1. IN VARIOUS DEPARTMENTS

Basically, all the activities of a company are performed by five departments viz. Production, Marketing, Finance, Personnel and Research & Development. The following are the major ethical issues involved in each of the department.

(i) Production Department : Major concerns are procuring raw material in best possible way and no hoarding should be made the factory where production is being made is located at a place having no/minimum adverse impact on local community.try its best to control environmental pollution.

(ii) Marketing Department : Giving fair treatment to customers. Truthful and realistic claims to be made in advertising.

(iii) Finance : Protection of the interest of investors and trying our best for appreciation of investor's capital.

(iv) Personnel : No discrimination with the workers and just and equitable treatment to all employees without any favourtism.

(v) R&D: Making all R& D efforts in an environment friendly way and to have a human touch while testing the results of R&D, especially drugs etc.

2. IN GENERAL

(i) Privacy : Privacy is always a delicate matter for an FIR manager. Though a company culture may be friendly and open and encourage

employees to freely discuss personal details and lifestyles, the HR manager has an ethical obligation to keep such matters confidential. This particularly comes into play when the competing company calls for a reference on an employee. To remain ethical, FIR managers must stick to the job-related details and leave out knowledge of an employee's personal life.

(ii) Compensation and Skills : HR managers can recommend compensation. While these recommendations may be based on a salary range for each position, ethical dilemmas arise when it comes to compensating employees differently for the same skills. For example, a highly sought-after executive may be able to negotiate a higher salary than someone who has been with the company for several years. This can become an ethical problem when the lower-paid employee leams of the discrepancy and questions whether it is based on characteristics such as gender and race.

Employee Behavior

From large corporations to small businesses, individuals involved in all types of business often face ethical issues stemming from employee behavior. For example, whether an employee can spend work time checking personal email accounts, how a manager deals with claims of harassment and to what extent a manager can "groom" a certain employee for a promotion are all examples of ethical issues regarding employee behavior. There are legal consequences for some unethical employee behavior. For example, if a supervisor discriminated against an employee based on her gender, religion or ethnicity when making recommendations for a promotion, legal action could be sought. Small business owners can help to prevent ethical problems stemming from employee behavior by drafting a clear, attorney-reviewed set of standards that dictate behavior policies for employees at all levels.

Employee Working Conditions

In addition to employee behavior, there are a number of ethical issues business people must consider about employee working conditions.

For example, employers must be aware of the safety of their work environment and if they have compensated employees for all the time they have worked. The must also consider if they have required an employee to work an unreasonably long period of time or if they have him doing an unusually difficult task. Just like there are legal consequences for some unethical issues regarding employee behavior, there are also legal consequences for unethical working conditions. For example, an employer who requires an employee to work without pay or who creates an unsafe working environment can face legal action.

Supplier/Customer Relations

In addition employees and business owners must consider the ethical issues involved with their relationships between suppliers and customers. Business owners in particular must consider whether it is ethical to do business with suppliers who have unethical practices. When dealing with customers or clients, business people must ensure that they use their information correctly, do not falsely advertise a product or service, and do not intentionally do sub-standard work.

Small Business Ethics

Although there are ethical issues like discrimination that apply to all areas of business, each business area has its own ethical concerns. For example, business people who act as consultants must ensure they are giving sound advice. In the area of small business, some major ethical issues result from hiring, firing and dealing with employees. For example, conflicts of interest may cause ethical issues in small businesses, especially if they are family run. When personal family issues interfere with business decisions, this is a conflict of interest and an ethical concern.

5.6 ARGUMENTS AGAINST BUSINESS ETHICS

1. Some people object to the entire notion that ethical standards should be brought into business organizations. According to these, the following are the

general objections against business ethics. People's ethical values are set during childhood, in their families, and little can be done after that. The managers are not in a position to change the habits of their subordinates by way of orders/ instructions. Habits acquired in the childhood die hard. A good person generally remains a good person throughout his life unless some extremely bad experience is there. Moreover it is not company's duty to make their employees ethical.

2. The pursuit of profit in perfectly competitive free markets will, by itself, ensure that the members of a society are served in the most socially beneficial ways. Even more, there are several ways of increasing profits that will actually harm society. Producing what the buying public wants may not be the same as producing what the entirety of society needs. Thus, although the argument tries to show that ethics does not matter, it can do this only by assuming an unproved moral standard that at least appears mistaken.

3. Another main argument is that the ethical company cannot be competitive and viable. In the modern era, how can one pay the right taxes and remain competitive if their competitors are under-declaring their incomes and gaining a lot.

4. Managers are loyal agents and they should pursue the interests of their firms and should ignore ethical considerations. Employees have a duty to serve their employers single-mindedly. The manager has a duty to serve his or her employer as the employer would want to be served (to promote self-interests). Therefore, the manager has a duty to serve his or her employer in whatever ways will advance the employer's self-interests. But the conflicting view is also there, even in employment agreements, there is no clause to justify doing wrong on another's behalf.

5. It is sufficient if business firms obey law. Obeying the law is sufficient for businesses and that business ethics is, essentially, nothing more than obeying the law.

5.7 PREVENTING UNETHICAL PRACTICES IN ORGANIZATIONS

Addressing unethical behaviour and practices is essential to maintain an ethical climate in an organization. An appeal process must be in place so that

any unethical practice can be brought into light. Ethical or unethical behaviour of individual employees is influenced in the workplace both by their own moral development and the influence that the organization culture exerts on them. They are influenced by a group of forces that surround them such as their peers, their supervisors, and superiors, the reward system, group norms, company values and policies and the manner of their implementation. Ethical behaviour can be developed and managed in a number of ways. The pivotal role to manage and develop ethical behaviour among employees lies with the Top Management of an organization. Incorporation of ethical norms and conduct into all levels of the organization can be done in the following ways.

- Codes of corporate ethics must be formulated so that employees are.aware of the Organization's expectations regarding ethical norms and conduct.
- An appeal process must be in place so that any unethical practice can be brought into light. Whistleblower must be protected and rewarded in the company.
- Seminars on business ethics should be conducted for employees. This will help them in understanding the importance of ethical work culture.
- Compliance officers must be appointed to keep a check on fraud, corruption, and abuse within the organization.
- Performance management system of the organization must be modified to incorporate ethical behaviour as a parameter for appraisal and rewards.

Business houses that comply with ethics to determine their conduct are shrinking in number. The lack of business ethics in the market is a big reason to worry. Organizations now recognize the positive effects and outcomes of being ethical, humane and considerate. They have a competitive edge in the market, because of the honesty they show in their services. Their morally upright reputation attracts better staff and helps in retention. Though ethics are legally

binding in most cases, self-monitoring, transparency and accountability will go a long way in establishing trust of the people. Besides this, it makes sense to change, before you are penalized.

5.8 INDIAN VALUE SYSTEM AND ETHICS

True, ethical behavior and ethics as a science do not necessarily presuppose a religious-philosophical creed. However, not only does every activity presuppose some knowledge of pragmatic matters, it also involves ideas or beliefs regarding the nature of the objective world and the subject. In ethical behavior man has to be conscious of himself as a moral agent, and this presupposes some definite concepts of the human self, as also of the goal(s) or value(s) which man has to realize through his conduct. Hinduism as a religion is both a view of life and a way of life which are related as the theoretical and practical guides of the same spiritual life. Any study of Hindu ethics ought to take into account innumerable discussion on ethical matters, scattered throughout ancient Indian literature. Jainism and Buddhism as two branches of larger Hindu philosophical thought gives detailed accounts of ethical and unethical behavior and also talks in great lengths about the duties of man.

1. Ethics in Indian value system is conscious living within the frame of certain principles of conduct laid down by those regarded as authorities. In general, therefore, the ethical institutions of life or the moral point of view, consists in the awareness of an important distinction between what is and what ought to be.

2. In Indian philosophy ethical behavior may be both social and personal. Ethics as an institution of life has been recognized here from the very early age of the Vedas. Rather it has been recognized as the most basic element in human life. But then it has not necessarily been recognized as a social enterprise in the sense of being an instrument of the society to help guide the people living in the society. It is rather engrained in the very being of the universe.

3. Ethics has a divine origin. Man has simply to adopt it from there. The Vedic distinction between Rju (straight) and Vran (crooked) and the Upanisadic

distinction between Sreyah (desirable) and Preyah (pleasurable) have much to do with the origin of the sense of right and wrong and hence can be related to ethical and unethical behavior in the context of modern day business ethics.

4. The Indian philosophy the origin of ethics does not come from the contingent agency like the society, but it has a divine origin. The concept of ethics is not necessarily tied up here with the concept of society. Furthermore, it is not the case here that ethics in Indian philosophy has meaning only in the context of society.

5. An individual may behave ethically or unethically in relation to other members of his society as also in relation to himself. Man by virtue of being what he is has to follow certain obligations, even if he is not a member of any society. There is talk of both social and individual morality in Indian ethics, Social ethics refers to questions of morality in relation to others, and where as individual ethics refers to the question of morality in relation to oneself. One is adopting a moral point of view not only making judgments about the conduct and character of some towards other members of the society, but also in his behaviour to himself as a man.

6. The concept of social and individual ethics can .be analyzed in the context of business ethics. While social ethics can be seen from the point of view of organizational behavior individual ethics could be the ethical codes for individual members of the corporation which can guide them to indulge in ethical business. The recognition of both social and individual ethics constituting the parts of the ethical life of man corresponds to the acceptance of the ethics of doing and the ethics of being as part of the Indian concept.

7. The ethics of doing refers to the DO's and DON'Ts and the ethics of being refers to the virtues and vices. Social ethics is predominantly the ethics of doing and individual ethics is the ethics of being. It can be said that where as social ethics has its root in a sense of duty towards others, individual ethics or subjective ethics has its root in a sense of inculcating inner virtue

8. The institution of ethics has for its basic concern the regulation of man's lower inclinations and promotion of the higher ones in realization of his aspirations as a man. It is in such a concern that the transition from 'is' to 'ought' is involved. The natural inclinations of man go in favour of his own egoistic interest and therefore it is the concern of ethics to instruct him to feel, think and do for others also. The scarifies of one's egoistic interests does not always mean giving up one's egoistic interests for the sake of others, but also for the sake of the higher ones.

9. The Vedas in general seem to give an ethics of overt duties rather than inner virtues, an ethics of doing rather than being, and all duties are clearly directed towards worldly end. The Dharmasastras also preach an externalist ethics where inner motive or intention of the doer does hardly seem to constitute the Tightness and wrongness of the action done by him. Dharmashhstra are more or less given to us in the form of a legal code. Although at times it talks about inner purification.

10. Purity of motive and intention is also necessary for doing moral acts; only overt acts will which prompt the acts.

11. Sin is not merely failure to do the right, but failure to let good.

5. 9 INDIVIDUAL ETHICS ACCORDING TO INDIAN VALUE SYSTEM

Indian philosophy elucidates in detail about the ethical character of man. Every man should try to incorporate these ethical codes. If every individual follows a moral life then any organization can uphold utmost ethics. A man of character strives to practice Truth, non-stealing, fearlessness and such other vows. He is ready to give up his life, but not truth. He is prepared to die, but will not kill. He is willing to accept suffering, but not inflict it on others. He does not steal, not takes bribes. He does not waste his time or that of others, goes on doing his duty fearlessly. Below a brief account of the basic principles found in Indian philosophy regarding individual ethics are been given.

1. Doing one's duty : Performing one's duty is fundamental concept of work ethics. One should fulfill one's commitment and be accountable for results.

He should be dedicated to hard work. He should protect the interest of the organization he works for.

2. Building a character foundation for society : Everyone has goal for society. To get society in high gear, every member of society needs to understand the role for societal wellness.

3. Honesty : Wise persons are held to the highest standards of conduct which includes ethics, integrity, character, trustworthiness, truthfulness, morality, Tightness. They show high consistency between word and deed.

4. Vision : They have ability to "see the future" and perceive an improved reality for the community. They have competence of leading through work, action and deed. They communicate their vision and provide direction to follow the vision. They encourage risk taking.

5. Balance : They are integrated or well-balanced spiritually, mentally, emotionally and physically. This gives good vibration to others, thereby elevating their spirits in addition to their confidence and passion for excellence.

6. Self-learning: They continuously learn of new knowledge and skills and develop cultural awareness and sensitivity.

7. Self-confidence: They have self-confidence in order to convince their followers of the Tightness of goals and decisions.

8. Patience : A wise man has patience; he controls his emotions. He quietly ignores an insult. He will not be provoked into meaningless fight, choosing instead to hold back his anger and to use his intellect to seek peace and reconciliation.

9. Self-control and restrain in speech : The wise are especially noted by their skill with words. First, they show self-control and restrain in their use of language. Realizing the power of words, they speak with great caution. When they do speak, what they say is true and relevant. Moreover, their words are both dignified and astute.

10. Differentiate between right and wrong : The wise understand the true difference between right and wrong, good and evil. They know the real

meaning of justice and red fair play. They do not judge by appearance only, but they also see in depth. They have insights and foresight, enabling them to perceive both the underlying dynamics of things while accurately anticipating results and consequences. Therefore, they show good judgment and make correct decisions. Wise men are able to successfully perceive ahead because they have faith in the ultimate value of wisdom. And so the wise are law-abiding. They can see far ahead to know the benefits of right living. A man of character expresses all ethical and human values. He is called a Wiseman. He has wisdom and wisdom is born of contact with the divine. He has purity of mind/heart; higher consciousness is also called spiritual state of mind and combines in wisdom and values. In Indian wisdom, material and spiritual aspects of human existence or life are given emphasis and there is very close inter-relationship between worldly life and spiritual life. Both are manifestations or expressions of the divine or pure consciousness the wise are law-abiding. They can see far ahead to know the benefits of right living. A man of character expresses all ethical and human values. He is called a Wiseman. He has wisdom and wisdom is born of contact with the divine. He has purity of mind/heart; higher consciousness is also called spiritual state of mind and combines in wisdom and values. In Indian wisdom, material and spiritual aspects of human existence or life are given emphasis and there is very close inter-relationship between worldly life and spiritual life. Both are manifestations or expressions of the divine or pure consciousness.

5.10 ETHICAL VALUES AND A FEW MNC'S

1. **Ethical values and business ethics of cadbury :** Cadbury is one of the world's largest confectionary manufacturers. Cadbury believes that good ethics and good business go together naturally to produce the best long-term results for all the stakeholders. Cadbury's vision is to be the biggest and the best confectionery company in the world. Its success is sustained by understanding and responding to the needs of consumers, customers, suppliers, colleagues and citizens. Its values are based upon performance, quality, respect, integrity and responsibility, honesty, openness and courtesy. This means

everyone in Cadbury acts in an ethical way to protect and promote the company and its reputation among the people and communities it does business with. Cadbury maintains ethical sourcing standards and develops sustainable agriculture programmes such as the 'Cadbury Cocoa Partnership'. Cadbury recognizes its environmental responsibilities. It reduces environmental impact, in particular targeting carbon, packaging and water use, within its broad 'Purple Goes Green' environmental programme.

2. **Ethical values and business ethics of nestle :** Nestle is the world's leading nutrition, health and wellness company. With over 276,000 employees, the company has operations in almost every country in the world. The, people know more by brands and the portfolio covers practically all food and beverage categories, with market leaders like Nestle, DRUMSTICK, NESCAFE, STOUFFERS, KITKAT, Nestle GOODSTART, Nestle PURE LIFE and PURINA , to name, a few. Since its founding, Nestle's business practices have been governed by integrity, honesty, fair dealings andxfull compliance with all applicable laws. Nestle's employees worldwide have upheld and lived this commitment in their everyday responsibilities ever since, and Nestle's reputation remains one of the Company's most important assets today. The Nestle Corporate Business Principles prescribe certain values and principles which Nestle has remained committed worldwide.

3. **Ethical values and business ethics of other MNCS (Tate,Sail, Maruti , ONGC, Wipro , Relliance , Infosys, Canon, Johson & Johson , Ford Motor Company, IBM)** : The Tata Group has always sought to be a value-driven organization. These values continue to direct the Group's growth and businesses. The five core Tata values underpinning the way we do business are: Integrity; Understanding; Excellence; Unity; and Responsibility. SAIL (Steel Authority of India) is To be a respected world Class Corporation and the leader in Indian steel business in quality, productivity, profitability and customer satisfaction. Maruti Udyog: We believe our core values drive us in every endeavour: Customer obsession; flexible and first mover; innovation and creativity; networking and partnership; openness and learning. ONGC: To be a world-class Oil and Gas

Company integrated in energy business with dominant Indian leadership and global presence. The Spirit of Wipro is the core of Wipro. Spirit is rooted in current reality, but it also represents what Wipro aspires to be - thus making it future active. The Spirit is an indivisible synthesis of all three statements: Manifesting intensity to win; Acting with sensitivity; and being unyielding on integrity all the time. Reliance Industries: Reliance believes that any business conduct can be ethical only when it rests on the nine core values of: Honesty; Integrity; Respect; Fairness; Purposefulness; Trust; Responsibility; Citizenship; and Caring. Growth is care for good health. For Reliance Industries: Growth is care for safety; Growth is care for the environment; Growth is conservation; Growth is betting on our people; and Growth is thinking beyond business. Infosys Technologies is a globally respected corporation that provides best-of-breed business solutions, leveraging technology, delivered by best-in-class people and achieves its objectives in an environment of fairness, honesty, and courtesy towards our clients, employees, vendors and society at large.

4. **Ethical values of Infosys Technologies** : It's ethical values are customer Delight; Leadership; Integrity and Transparency; Fairness; and Pursuit of Excellence. Ethical values of Canon include: To foster good relations with customers and communities; to maintain good relation with nations and environment; and to bear responsibility for the impact of their activities on society.

5. **Ethical values of Johson & Johson Include** : High quality and prompt service at reasonable price with a view to making fair profit; to respect individuality of employees keeping in mind their job security and means of fulfilling family responsibility; Informal communication; Just and ethical action; and to encourage community service.

6. **Ford Motor Comapny's Ethical values Include :** Doing right thing for the customer, people, environment and society; Providing superior returns to the shareholders; and The customer is job 1.

7. **Ethical values of IBM Include** : Respect for individual; IBM anthem; Devotion to customers; Lifetime employment; and Open door program. For

IBM Ethics matters because it makes good business sense to "do the right thing". Additionally good corporate ethics results in: Attracting better talent; Retaining employees; attracting new customers; Retaining customers; Positive effect on Corporate Reputation.

5.11 SUMMARY

To conclude it can be said that ethical values really act as a vital tool for removing unethical practices and business. However, the idea of values, when it comes to management, relates much more importance to practical matters. There is a huge correlation between correct value alignment and success. Only a business following ethical practices can survive in today's competitive world.

The holistic approach of Indian Wisdom is needed for modern management to integrate matter/spirit or skills/values or object/subject. Modern management must incorporate Indian ethos to perfect the truncated model of man and recognize man as a whole man to assure wholesome human progress. Spirituality as well as material progress to satisfy the hunger of mind and soul as well as the hunger of physical and vital human being. Value-based holistic approach to management will assure such all round wholesome human development and prosperity. As per Indian ethos, the inner mind and inner aspects of man are emphasized. Focus is on developing inner mind. Faith and sincerity are two needs of management philosophy. Work must be done in right spirit and right attitude and in perfect way. A management with proper combination of values and skills can assure harmony and progress of organization as well as society. This is unique contribution of Indian ethos.

5.12 GLOSSARY

1. Teleology: which is derived from the greek word, telos which means goal or end purpose
2. Derivatives: It is something which is based on or comes from something else
3. Coherence: It means logical and consistent

4. Repercussions: It is defined as the consequences of an event or action

5. Stemming: It is to slow down the progress of something

5.13 SELF ASSESSMENT QUESTIONS

1. What is the role of Indian value system in business ethics?

2. What are the features of Indian value system in relation to business ethics?

3. What is the role of Indian value system in setting the business ethics? Do these values affect the business policies?

4. What types of ethical practices are followed by the various MNC's

5.14 LESSON END ACTIVITIES

1. Discuss major ethical problems related to top management. Discuss its usefulness for the company.

Ans. _____

_____

_____

_____

2. What are the ethical problems that lead to unethical behavior in business?

Ans. _____

_____

_____

_____

3. “Ethics are desirable for ever business.” Comment.

Ans. _____

_____

_____

_____

4. Discuss the significance of ethics in business.

Ans. _____

_____

_____

_____

5.15 SUGGESTED READING

1. Business Environment by Francis Cherunilam
2. Business Ethics by Sanjeev K. Bansal, Sandeep K. Bansal and Rama Bansal
3. Business Ethics: An Indian Perspective by A. C. Fernando

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-1I**

PAPER -IV **LESSON: 6-10**

BUSINESS LAWS IN INDIA, THE INDIAN CONTRACT ACT, THE LAW OF SALE OF GOODS, FORMATION OF CONTRACT

OBJECTIVES

The lesson will help you to:

- Understand the concept of Business Laws in India
- Explain the concept of the Indian Contract Act
- Understand the concept of the Law of Sale of Goods
- Explain the Concept of formation of Contract

STRUCTURE

2.1 INTRODUCTION

Business laws provide the authoritarian schemes on how commerce should be conducted. Every country has its own regulations, laws and regulatory bodies or agencies governing various processes of the country.Indian contract Act, 1872 was passed by British India and is based on the principles of english common law. It is applicable to all the state of jammu and kashmir. It determines the circumstance of legally binding parties . When one person sigifies to another his willingness to do or to abstain form doing any thing, with a view to obtaining the assent of that other to such act or abstinence ,he said to make proposal .Further ,The first reqiusite for the formation of any contract is an agreement (consisting of an offer and acceptance)At least two parties are required ,one of them ,is called offeree ,who accepts the offer. An offer is an emperission of willingness to contract made with the intension that it shallbecome binding on the offer oras it is accepted by the offeree.

2.2 BUSINESS LAWS IN INDIA

Business Law in India :

Business law and commercial law are the two laws that deal with the business and commercial transactions. It encompasses the formation of business management, commerce and consumer transaction. The commercial law consists of debtor Law, creditor law, sales and secured transaction. It also has the regulations and rules for the land cargo, sea cargo, merchant shipping, marine and accident insurance. There are various laws, which describe how the commerce should be taken care with the compliance, privacy laws, safety laws, foods and drugs law. Negotiable instruments and Secured transaction are the two most important areas of commercial and business law. In secured transaction,

borrower agrees on the collateral, which is owned by the borrower will be taken by lender. If in any business, party borrows money from the bank or from any other financial institution. In this case, the lender needs more than just promise to repay the loan amount. Hence, the law of collateral interests formed between borrower and lender.

Importance of Business Law Regulations in India

Business law refers to the laws which are applied to business entities such as partnerships and corporations. These are used as reference when putting up businesses whether big or small - from sole proprietorship to corporation. Business laws specify how different business can be set up, how taxes apply to them, registrations, documentations and requirements; define different terms pertaining to business, making by-laws, and articles of organization among many others.

These also provide the authoritarian schemes on how commerce should be conducted. Every country has its own regulations, laws and regulatory bodies or agencies governing the manufacturing, sales, marketing and distribution of products within the country. Laws and regulations are intentionally made for human beings and other institutions as a guide to bring order and sanity into the society. Because of this, it is likely that their application will impact upon the plans of firms; their effects on a given firm are also inevitable.

An attempt would be made to confer specified regulations and laws with particular reference to aviation and airline, environmental regulations, stock market regulations, banking regulations, research (and development) co-operation regulations, stock options regulations, labour regulations, intellectual property and social security regulations industry by industry and effects on the plans of firms where necessary.

Many business laws in India precede the country's independence in 1947. For example, the Indian Contract Act of 1872 is still in force, although specific contracts such as partnerships and the sale of goods are now covered by newer

laws. The Partnership Act of 1932 covers partnership firms in India. Business laws regulating chartered accountants and cost accountants were passed in 1949 and 1959, respectively. The Banking Regulation Act of 1949 continues to regulate private banking companies and manage banks in India. In 2012, it was amended by the Banking Law (Amendments) Act. Under these amendments, the Reserve Bank of India (RBI) was given power to restrict voting rights and shares acquisition in a bank. The RBI established the Depositor Education and Awareness Fund. Banks are now able to issue both equity and preference shares under RBI guidelines.

While India is often criticized for complex regulations, it is important to keep in mind that that in some cases, these laws are simpler than those of the U.S. Furthermore, most regulations are consistent across the country, and attorneys in India can practice in any state. Filing lawsuits is seldom productive in most commercial disputes since court cases can drag on for decades and collection can take even longer. For large deals, binding third-country arbitration can be the best way to resolve disputes.

Following India's economic development in the 21st century, the Ministry of Corporate Affairs passed the Competition Act of 2002 and the Limited Liability Act in 2008. These promote sustainable competition in markets, prohibit anti-competitive business practices, and protect consumer interests while ensuring free trade.

The Parliament of India passes and amends regulations for both businesses and investors. In addition to provisions from the Companies Act of 1956, theCompanies Act of 2013 features provisions regarding mergers and acquisitions, board room decision-making, related party transactions, corporate social responsibility, and shareholding.The act was further amended through the Companies Act of 2015 which eliminated the procedural common seal, declarations for commencement of businesses, and minimum paid-up capital requirements. The amendment also relaxed governing-related party transactions while limiting access to strategic corporate resolutions in India.

As a member of the International Labor Organization, India offers protections for employees. These include the Payment of Wages Act of 1936, the Industrial Employment Act of 1946, the Industrial Disputes Act of 1947, the Payment of Bonus Act of 1965, and the 1972 Payment of Gratuity Act. Protections include annual bonuses of 8.33% and separation fees of about 15 days per year of employment. Other labor laws such as the Building and Other Construction Workers Acts of 1996 and the Workmen's Compensation Act of 1923 (amended in 2000) are in effect. Passed in 1926, the Trade Unions Act deals with the registration, rights, liabilities, and responsibilities of trade unions. The Industrial Disputes Act of 1946 regulates trade unions and matters between industrial employers and employees.

Business laws in India include consumer protection. The Consumer Protection Act, 1986 mandates Consumer Dispute Redressal Forums at local and national levels. Older laws, such as the Standards of Weights & Measures Act of 1956, ensure fair competition in the market and free flow of correct information from providers of goods and services to consumers.

Due to the growth of trade, the Indian government passed the Foreign Trade (Development and Regulation) Act of 1992 to facilitate imports and augment exports. The latest EXIM Policy, known as the Foreign Trade Policy, was issued for April 2015 to March 2020. The Service Exports from India Scheme (SEIS) replaced the Served from India Scheme. The SEIS extends the duty-exempted scrip to Indian service providers and provides notified services in a specified mode outside the country. Under the Export Promotion Capital Goods Scheme, the export obligation requires six times the duty saved on imported capital goods; in the case of local sourcing of capital goods, the export obligation is reduced by 25%. Beyond goods and services, the Foreign Exchange Management Act of 1999 regulates foreign exchange transactions including investments abroad.

As a founding member of the World Trade Organization in 1995, India has updated business laws regarding copyrights, patents, and trademarks to

meet the Agreement on Trade Related Aspects of Intellectual Property Rights. Indian companies and the federal government honor global IP rights. However, because music copyrights are different in India, both Indian and Western IP owners in the entertainment industry have suffered due to digital piracy. Even so, there are few IP-related disputes outside of several celebrated pharmaceutical industry cases. In 2013, India's Supreme Court denied Novartis an extension to update its cancer drug Glivec due to "evergreening" charges.

E-commerce and online expansion of companies prompted India to create regulations to cover cyber law and security compliances, such as the techno legal regulatory provisions in the Companies Act of 2013. The Information Technology Act of 2000 is the primary law for e-commerce regulation in India. In 2008, the IT Act was amended to provide explicit legal recognition of electronic transactions.

2.2 THE INDIAN CONTRACT ACT

Meaning of Contract Act :

What is Law? Law means a 'set of rules' which governs our behaviours and relating in a civilized society. So there is no need of Law in a uncivilized society. Why Should One Know Law? One should know the law to which he is subject because ignorance of law is no excuse. Commencement and applicability:- Short Title Extent and commencement ¾ Prior to this English law of contract was followed in India. ¾ It has XI chapter. ¾ Law of contract creates jus in personem and not in jus in rem. ¾ The Indian Contract Act consists of the following two parts: (a) General principals of the Law of Contract. (b) Special kinds of contracts. ¾ The general principals of the Law of Contract are contained in Sections 1 to 75 of the Indian Contract Act. These principles apply to all kinds of contracts irrespective of their nature. ¾ Special contracts are contained in Sections 124 to 238 of the Indian Contract Act. These special contracts are Indemnity, Guarantee, Bailment, pledge and Agency. Note: In our discussion on this part of the book, unless otherwise stated, the sections mentioned are those of the Indian Contract Act, 1872. English Mercantile Indian Status Law Judicial

Decisions Customs and Usages The Indian contract Act 1872 Applicable to whole Indian except the state of Jammu & Kashmir First day of September 1872(1st Sept. 1872) Contracts as Defined by Eminent Jurists 1. "Every agreement and promise enforceable at law is a contract." - Pollock 2. "A Contract is an agreement between two or more persons which is intended to be enforceable at law and is contracted by the acceptance by one party of an offer made to him by the other party to do or abstain from doing some act." - Halsbury 3. "A contract is an agreement creating and defining obligation between the parties" -

1. Salmond Section : "All agreements are contracts, if they are madeby free consent of the parties, competent to contract, for a lawful consideration and with a lawful object, and not here by expressly declared to be void." - Sec.10. Offer + acceptance = Promise + consideration = Agreement + enforceability By Law Contract ESSENTIALS OF A VALID CONTRACT ESSENTIALS OF VALID CONTRACT 1. Proper offer and proper acceptance with intention to create legal relationship. Cases;- A and B agree to go to a movie on coming Sunday. A does not turn in resulting in loss of B's time B cannot claim any damages from B since the agreement to watch a movie is a domestic agreement which does not result in a contract. In case of social agreement there is no intention to create legal relationship and there the is no contract (Balfour v. Balfour) In case of commercial agreements, the law presume that the parties had the intention to create legal relations. [an agreement of a purely domestic or social nature is not a contract]

2. Lawful consideration : consideration must not be unlawful, immoral or opposed to the public policy.

3. Capacity : The parties to a contract must have capacity (legal ability) to make valid contract. Section 11:- of the Indian contract Act specify that every person is competent to contract provided. (i) Is of the age of majority according to the Law which he is subject, and (ii) Who is of sound mind and (iii) Is not disqualified from contracting by any law to which he is subject. Person of unsound mind can enter into a contract during his lucid interval.

An alien enemy, foreign sovereigns and accredited representative of a foreign state. Insolvents and convicts are not competent to contract.

4. Free consent : Consent of the parties must be genuine consent means agreed upon samething in the same sense i.e. there should be consensus - ad - idem. A consent is MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 4 9213188188 said to be free when it is not caused by coercion, undue influence, fraud, misrepresentation or mistake.

5. Lawful object : The object of agreement should be lawful and legal. Two persons cannot enter into an agreement to do a criminal act. Consideration or object of an agreement is unlawful if it

(a) is forbidden by law; or

(b) Is of such nature that, if permitted, would defeat the provisions of any law; or

(c) Is fraudulent; or

(d) Involves or implies, injury to person or property of another; or

(e) Court regards it as immoral, or opposed to public policy.

6. Possibility of performance: The terms of the agreement should be capable of performance. o An agreements to do act, impossible in itself cannot be enforced. Example : A agrees to B to discover treasure by magic. The agreement is void because the act in itself is impossible to be performed from the very beginning. 7. The terms of the agreements are certain or are capable of being made certain Example : A agreed to pay Rs.5 lakh to B for ultra-modern decoration of his drawing room. The agreement is void because the meaning of the term " ultra - modern" is not certain. 8. Not declared Void o The agreement should be such that it should be capable or being enforced by law. o Certain agreements have been expressly declared illegal or void by the law. 9. Necessary legal formalities o A contract may be oral or in writing. o Where a particular type of contract is required by law to be in writing and registered,

it must comply with necessary formalities as to writing, registration and attestation. If legal formalities are not carried out then the contract is not enforceable by law. Example : A promise to pay a time. Barred debt must be in writing. ™ Agreement is a wider term than contract where as all contracts are agreements. All agreements are not contracts. All Contracts are Agreements, but all Agreements are not Contracts The various agreements may be classified into two categories: Agreement not enforceable by law Agreement enforceable by law Any essential of a valid contract is not available. All essentials of a valid contract are available MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 5 9213188188 Conclusion: Thus we see that an agreement may be or may not be enforceable by law, and so all agreement are not contract. Only those agreements are contracts, which are enforceable by law, In short. Contracts = Agreement + Enforceability by Law Hence, we can conclude "All contracts are agreement, but all agreements are not contracts." Distinction between Contract & Agreement Basis Contract Agreement 1. Section : 2. Definition : 3. Enforceability : 4. Interrelationship 5. Scope : 6. Validity : 7. Legal : Obligation Sec. 2(h) A contract is an agreement enforceable by law. Every contract is enforceable A contract includes an agreement. The scope of a contract is limited, as it includes only commercial agreements. Only legal agreements are called contracts. Every contract contains a legal obligation. Sec. 2(e) Every promise or every set of promises forming consideration for each other is an agreements. Every promise is not enforceable. An agreement does not include a contract. Its scope is relatively wider, as it includes both social agreement and commercial agreements. An agreement may be both legal and illegal. It is not necessary for every agreement to have legal obligation.

Types of contracts :

On the Basis of creation validity execution of Liability:

a. Valid contract

b. Void contract

c. Voidable contract

d. Bilateral contract

e. Unilateral contract

f. Executed contract

g. Executed contract

h. Partly executed and

i. Unenforceable party executory contract

j. Illegal contract

k. Express contract

l. Implied contract

m. Tacit contract

n. Quasi contract

o. E contract

(p) Others

(a) **Valid contract**:- An agreement which satisfies all the requirements prescribed by law On the basis of creation

(b) **Void contract 2(j)** :- a contract which ceases to be enforceable by law because void when of ceased to be enforceable When both parties to an agreement are:- Under a mistake of facts Consideration or object of an agreement is unlawful. Agreement made without consideration; Agreement in restrain of marriage. Restraint of trade, restrain legal proceeding; Agreement by wage of wager.

(c) **Voidable contract 2(i)** :- an agreement which is enforceable by law at the option of one or more the parties but not at the option of the other or others is a voidable contract. Result of coercion, undue influence, fraud and misrepresentation.

(d) **Bilateral contract**:- A contract in which both the parties commit to perform their respective promises is called a bilateral contract. Example : A

offers to sell his fiat car to B for Rs.1,00,000 on acceptance of A's offer by B, there is a promise by A to Sell the car and there is a promise by B to purchase the car there are two promise.

(e) **Unenforceable contract**: - where a contract is good in substance but because of some technical defect i.e. absence in writing barred by imitation etc one or both the parties cannot sue upon but is described as unenforceable contract. Example: Writing registration or stamping. Example: An agreement which is required to be stamped will be unenforceable if the same is not stamped at all or is under stamped. MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 7 9213188188.

(f) **Executed contract** :- A contract in which both the parties have fulfilled their obligations under the contract. Example: A contracts to buy a car from B by paying cash, B instantly delivers his car.

(g) **Executory contract** : A contract in which both the parties have still to fulfilled their obligations. Example : D agrees to buy V's cycle by promising to pay cash on 15th July. V agrees to deliver the cycle on 20th July.

(h) **Partly executed and partly executory** : A contract in which one of the parties has fulfilled his obligation but the other party is yet to fulfill his obligation. Example : A sells his car to B and A has delivered the car but B is yet to pay the price. For A, it is excuted contract whereas it is executory contract on the part of B since the price is yet to be paid. On the basis of liability for performance:-

(i) **Unilateral contract** : A unilateral contract is a one sided contract in which only one party has to perform his promise or obligation party has to perform his promise or obligation to do or forbear. Example :- A wants to get his room painted. He offers Rs.500 to B for this purpose B says to A " if I have spare time on next Sunday I will paint your room". There is a promise by A to pay Rs 500 to B. If B is able to spare time to paint A's room. However there is no promise by B to Paint the house. There is only one promise.

(j) **Illegal contract**: It is a contract which the law forbids to be made. All illegal agreements are void but all void agreements or contracts are not necessary illegal. Contract that is immoral or opposed to public policy are illegal in nature.Unlike illegal agreements there is no punishment to the parties to a void agreement. Illegal agreements are void from the very beginning agreements are void from the very beginning but sometimes valid contracts may subsequently becomes void.

Difference Between Void and Voidable Contract Matter Void contract Voidable contract Definition It means contract which cease to be enforceable. It means an agreement enforceable by law by one or more parties. Nature Valid when made subsequently becomes unenforceable. It remains voidable until cancelled by party. Rights or remedy No legal remedy. Aggrieved party has remedy to cancel the contract. Performance of contract Party can't demand performance of contract If aggrieved party does not cancel it within reasonable time, performance MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 8 9213188188 can be demanded. Reason Due to change in law or circumstances If consent is not obtained freely. Damages Not available Can demand in certain cases. Difference between Void and illegal Agreement Matter Void agreement Illegal agreement What Void agreement is not prohibited by law. It is prohibited by law. Effect on collateral transaction Enforced Not enforced. Punishment No Yes Void ab initio May not be void ab initio Always void initio Contract of record: It is either a judgment of a court of a Recognizance. A Judgment is an obligation imposed by a Court upon one or more persons in favour of another or others. In real sense, it is not a contract, as it is not based upon any agreement between two parties. Recognizance is a Bond by which a person undertakes before a Court of Magistrate to observe some condition e.g. to appear on summons. Contracts of record derive their binding force from the authority of the Court. Contract under Seal: (a) A contract under Seal is one which derives its binding force from its form alone. (b) It is in writing and signed, sealed and delivered by the parties. (c) It is also called a Deed or a Specialty contract. MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 9 9213188188 Offer(i.e.

Proposal) [section 2(a)]:-When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other person either to such act or abstinence, he is said to make a proposal. OFFER To form an agreement, there must be at least two elements - one offer and the other acceptance. Thus offer is the foundation of any agreement. "When one person signifies to another his willingness - o to do or to abstain from doing anything, o with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal." The person who makes an offer is called "Offeror" or " Promisor" and the person to whom the offer is made is called the Offeree" or "Promisee". Example Mr. A says to Mr. B, "Will you purchase my car for Rs.1,00,000?" In this case, Mr. A is making an offer to Mr. B. Here A is the offeror and B is the offeree.

Essentials elements of an offer:-

(1) There must be two parties.

(2) The offer must be communicated to the offeree.

(3) The offer must show the willingness of offeror. Mere telling the plan is not offer.

(4) The offer must be made with a view to obtaining the assent of the offeree.

(5) A statement made jokingly does not amount to an offer.

(6) An offer may involve a positive act or abstinence by the offeree.

(7) Mere expression of willingness does not constitute an offer.

A tells B' that be desires to marry by the end of 2008, if does not constitute an offer of marriage by A' to B' A further adds will you marry me. Then it become offer. Legal Rules as to valid offer:- 1. Offer must be communicated to the offeree: The offer is completed only when it has been communicated to the offeree. Until the offer is communicated, it cannot be accepted. Thus, an offer accepted without its knowledge, does not confer any legal rights on the acceptor.

Example: A's nephew has absconded from his home. He sent his servant to trace his missing nephew. When he servant had left, A then announced that anybody who discovered the missing boy, would be given the reward of Rs.500. The servant discovered the missing boy without knowing the reward. When the servant came to know about the reward, he brought an action against A to recover the same. But his action failed. It was held that the MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 10 9213188188 servant was not entitled to the reward because he did not know about the offer when the discovered the missing boy. [Lalman Shukla v. Gauri Datt (1913) All LJ 489] 2. The offer must be certain definite and not vague unambiguous and certain. Example: A offered to sell to B. 'a hundred tons of oil'. The offer is uncertain as there is nothing to show what kind of oil is intended to be sold. 3. The offer must be capable of creating legal relation. A social invitation is not create legal relation. Example: A invited B to a dinner and B accepted the invitation. It is a mere social invitation. And A will not be liable if he fails to provide dinner to B. 4. Offer may be express and implied The offer may be express or implied; An offer may be express as well as implied. An offer which is expressed by words, written or spoken, is called an express offer. The offer which is expressed by conduct, is called an implied offer [Section 9]. 5. Communication of complete offer Example: A offered to sell his pen to B for Rs.1,000. B replied, "I am ready to pay Rs.950". On A's refusal to sell at this price, B agreed to pay Rs.1,000. held, there was not contract at the acceptance to buy it for Rs.950 was a counter offer, i.e. rejection of the offer of A. Subsequent acceptance to pay Rs.1,000 is a fresh offer from B to which A was not bound go give his acceptance. 6. Counter offer - A counter offer amounts to rejection of the original offer 7. Cross offer do not conclude a contract 8. An offer must not thrust the burden of acceptance on the offeree. Example: A made a contract with B and promised that if he was satisfied as a customer he would favorably consider his case for the renewal of the contract. The promise is too vague to create a legal relationship. ¾ The acceptance cannot be presumed from silence. ¾ Acceptance is valid only if it is communicated to the offeror. 9. Offer must be distinguished

from invitation to offer. Example: Menu card of restaurant is an invitation to put an offer. Example ; Price - tags attached with the goods displayed in any showroom or supermarket is also an invitation to proposal. If the salesman or the cashier does not accept the price, the or the cashier does not accept the price, the interested buyer cannot compel him to sell, if he wants to buy it, he must make a proposal. Example: Job or tender advertisement inviting applications for a job or inviting tenders is an invitation to an offer. Example: MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 11 9213188188 An advertisement for auction sale is merely an invitation to make an offer and not an offer for sale. Therefore, an advertisement of an auction can be withdrawn without any notice. The persons going to the auction cannot claim for loss of time and expenses if the advertisement for auction is withdrawn. 10. Offeror should have an intention to obtain the consent of the offeree. 11. An answer to a question is not a offer. Offer Invitation to offer ¾ Show his readiness to enter into a contract, it is called as an offer ¾ Purpose of entering contract ¾ Results in a contract Example Application filled in by a prospective applicable to the Institution, a student seeking admission in educational Institution. ¾ Person invites offer to make an offer to him. ¾ Purpose of enter offer ¾ Results in offer. Example Issue of prospectus by a Company, an education Institution. KINDS OF OFFER Express offer Implied offer Specific offer General offer Cross offer Counter offer Standing Open and Continuous offer I. Express offer - When the offeror expressly communication the offer the offer is said to be an express offer the express communication of the offer may be made by Spoken word Written word II. Implied offer - when the offer is not communicate expressly. An offer may be implied from:- The conduct of the parties or The circumstances of the case III. Specific:- It means an offer made in (a) a particular person or (b) a group of person: It can be accepted only by that person to whom it is made communication of acceptance is necessary in case of specific offer. IV. General offer: - It means on offer which is made to the public in general. o General offer can be accepted by anyone. o If offeree fulfill the term and condition which is given in offer then offer is accepted. o Communication of acceptance is not necessary is case of

general offer MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 12 9213188188 Example Company advertised that a reward of Rs.100 would be given to any person who would suffer from influenza after using the medicine (Smoke balls) made by the company according to the printed directions. One lady, Mrs, Carlill, purchased and used the medicine according to the printed directions of the company but suffered from influenza, She filed a suit to recover the reward of Rs.100. The court held that there was a contract as she had accepted a general offer by using the medicine in the prescribed manner and as such as entitled to recover the reward from the company. Carlill v Carbilic Smoke Ball Co. 1893 V. Cross offer:- When two parties exchange identical offers in ignorance at the time of each other's offer the offer's are called cross offer. Two cross offer does not conclude a contract. Two offer are said to be cross offer if 1. They are made by the same parties to one another 2. Each offer made in ignorance of the offer made by the 3. The terms and conditions contained in both the offers' are same. Example : A offers by a letter to sell 100 tons of steel at Rs.1,000 per ton. On the same day, B also writes to A offering to buy 100 tons of steel at Rs.1,000 per ton. When does a contract come into existence: - A contract comes into existence when any of the parties, accept the cross offer made by the other party. VI Counter offer :- when the offeree give qualified acceptance of the offer subject to modified and variations in the terms of original offer. Counter offer amounts to rejection of the original offer. Legal effect of counter offer:- (1) Rejection of original offer (2) The original offer is lapsed (3) A counter offer result is a new offer. In other words an offer made by the offeree in return of the original offer is called as a counter offer. Example: A offered to sell his pen to B for Rs.1,000. B replied, " I am ready to pay Rs.950." On A's refusal to sell at this price, B agreed to pay Rs.1,000. Held, there was not contract as the acceptance to buy it for Rs.950 was a counter offer, i.e. rejection of the offer of A. Subsequent acceptance to pay Rs.1,000 is a fresh offer from B to which A was not bound to give his acceptance. VII Standing, open and continuous offer:- An offer is allowed to remain open for acceptance over a period of time is known as standing, open or continually offer. Tender for supply

of goods is a kind of standing offer. Example: When we ask the newspaper vendor to supply the newspaper daily. In such case, we do not repeat our offer daily and the newspaper vendor supplies the newspaper to us daily. The offers of such types are called Standing Offer. MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 13 9213188188 LAPSE OF AN OFFER An offer should be accepted before it lapses (i.e. comes to an end). An offer may come to an end in any of the following ways stated in Section 6 of the Indian Contract Act: 1. By communication of notice of revocation: An offer may come to an end by communication of notice of revocation by the offeror. It may be noted that an offer can be revoked only before its acceptance is complete for the offeror. In other words, an offeror can revoke his offer at any time before he becomes before bound by it. Thus, the communication of revocation of offer should reach the offeree before the acceptance is communicated. 2. By lapse of time; Where time is fixed for the acceptance of the offer, and it is not acceptance within the fixed time, the offer comes to an end automatically on the expiry of fixed time. Where no time for acceptance is prescribed, the offer has to be accepted within reasonable time. The offer lapses if it is not accepted within that time. The term 'reasonable time' will depend upon the facts and circumstances of each case. 3. By failure to accept condition precedent: Where, the offer requires that some condition must, be fulfilled before the acceptance of the offer, the offer lapses, if it is accepted without fulfilling the condition. 4. By the death or insanity of the offeror: Where, the offeror dies or becomes, insane, the offer comes to an end if the fact of his death or insanity comes to the knowledge of the acceptor before he makes his acceptance. But if the offer is accepted in ignorance of the fact of death or insanity of the offeror, the acceptance is valied. This will result in a valid contract, and legal representatives of the deceased offeror shall be bound by the contract. On the death of offeree before acceptance, the offer also comes to an end by operation of law. 5. By counter - offer by the offeree: Where, a counter - offer is made by the offeree, and then the original offer automatically comes to an end, as the counter - offer amounts to rejections of the original offer. 6. By not accepting the offer, according to the prescribed or usual mode:

Where some manner of acceptance is prescribed in the offer, the offeror can revoke the offer if it is not accepted according to the prescribed manner. 7. By rejection of offer by the offeree: Where, the offeree rejects the offer, the offer comes to an end. Once the offeree rejects the offer, he cannot revive the offer by subsequently attempting to accept it. The rejection of offer may be express or implied. 8. By change in law: Sometimes, there is a change in law which makes the offer illegal or incapable of performance. In such cases also, the offer comes to an end. MS EDUCONZ PVT. LTD. LAW& AUDIT

(k) **Express contract** :- A contract made by word spoken or written. According to sec 9 in so for as the proposal or acceptance of any promise is made in words, the promise is said to be express. Example : A says to B 'will you purchase my bike for Rs.20,000?" B says to A "Yes".

(l) **Implied contract**:- A contract inferred by ™ The conduct of person or ™ The circumstances of the case. MS EDUCONZ PVT. LTD. LAW& AUDIT SUJEET JHA 6 9213188188 By implies contract means implied by law (i.e.) the law implied a contract through parties never intended. According to sec 9 in so for as such proposed or acceptance is made otherwise than in words, the promise is said to be implied. Example: A stops a taxi by waving his hand and takes his seat. There is an implied contract that A will pay the prescribed fare.

(m) **Tacit contract**: - A contract is said to be tacit when it has to be inferred from the conduct of the parties. Example obtaining cash through automatic teller machine, sale by fall hammer of an auction sale.

(n) **Quasi Contracts** : are contracts which are created - o Neither by word spoken o Nor written o Nor by the conduct of the parties. o But these are created by the law. Example: If Mr. A leaves his goods at Mr. B's shop by mistake, then it is for Mr. B to return the goods or to compensate the price. In fact, these contracts depend on the principle that nobody will be allowed to become rich at the expenses of the other. (e). e - Contract: An e - contract is one, which is entered into between two parties via the internet.

Indian Contract Act, 1872

The law relating to contracts in India is contained in INDIAN CONTRACT ACT, 1872. The Act was passed by British India and is based on the principles of English Common Law. It is applicable to all the states of India except the state of Jammu and Kashmir. It determines the circumstances in which promises made by the parties to a contract shall be legally binding on them. All of us enter into a number of contracts everyday knowingly or unknowingly. Each contract creates some rights and duties on the contracting parties. Hence this legislation, Indian Contract Act of 1872, being of skeletal nature, deals with the enforcement of these rights and duties on the parties in India.

The Act as enacted originally had 266 Sections, it had wide scope and included.

General Principles of Law of Contract- Sections 01 to 75

Contract relating to Sale of Goods- Sections 76 to 123

Special Contracts- Indemnity, Guarantee, Bailment & Pledge- Sections 124 to 238

Contracts relating to Partnership- Sections 239 to 266

Indian Contract Act embodied the simple and elementary rules relating to Sale of goods and Partnership. The developments of modern business world found the provisions contained in the Indian Contract Act inadequate to deal with the new regulations or give effect to the new principles. Subsequently the provisions relating to the Sale of Goods and Partnership contained in the Indian Contract Act were repealed respectively in the year 1930 and 1932 and new enactments namely Sale of Goods and Movables Act 1930 and Indian Partnership act 1932 were re-enacted.

At present the Indian Contract Act may be divided into two parts:

- deals with the General Principles of Law of Contract Sections 1 to 75
- deals with Special kinds of Contracts such as

(1) Contract of Indemnity and Guarantee

(2) Contract of Bailment and Pledge

(3) Contract of Agency

In simple words, the law of contract is contained in the Indian Contract Act, 1972. This Act is based mainly on English Common Law which is to a large extent made up of judicial precedents. (There being no separate Contract Act in England). It extends to the whole of India except the State of Jammu and Kashmir and came into force on the first day of September 1872. The Act is not exhaustive. It does not deal with all the branches of the law of contract. There are separate Acts which deals with contracts relating to negotiable instruments, transfer of property, sale of goods, partnership, insurance, etc. Again the Act does not affect any usage or custom of trade (sec. 1). A minor amendment in section 28 of the Act was made by the Indian Contract (Amendment) Act, 1996.

Scheme of the Act may be divided into two main groups:

1. General principles of the law of contract (Secs. 1-75).

2. Specific kinds of contracts, Viz.:

a) Contracts of Indemnity and Guarantee (Secs. 124-147).

b) Contracts of Bailment and Pledge (Secs. 148-181).

c) Contracts of Agency (Secs. 182-238).

Before 1930 the Act also contained provisions relating to contacts of sale of goods and partnership. Sections 76-123 relating to sale of goods were repealed in 1930 and a separate Act called the Sale of goods Act was enacted. Similarly, Sections 239-266 relating to partnership were repealed in 1932 when the Indian Partnership Act was passed.

BASIC ASSUMPTIONS UNDERLYING THE ACT

Before we take up the discussion of the various provisions of the Indian Contract Act, it will be proper to see some of the basic assumptions underlying the Act. These are:

1. Subject to certain limiting principles, there shall be freedom of contract to the contracting. parties and the law shall enforce only what the parties have agreed to be bound. The law shall not lay down only absolute rights and liabilities of the contracting parties. Instead it shall lay down only the essentials of a valid contract and the rights and obligations it would create between the parties in the absence of anything to the contrary agreed to by the parties.

2. Expectations created by the promises of the parties shall be fulfilled and their non-fulfilment shall give rise to legal consequences. If the plaintiff asserts that the defendant undertook to do a certain act and failed to fulfil his promise, an action at law shall lie.

1. **Offer 2(a)**: When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal.

2. **Acceptance 2(b)**: When the person to whom the proposal is made, signifies his assent there to, the proposal is said to be accepted.

3. **Promise 2(b)** : A Proposal when accepted becomes a promise. In simple words, when an offer is accepted it becomes promise.

4. **Promisor and promisee 2(c)** : When the proposal is accepted, the person making the proposal is called as promisor and the person accepting the proposal is called as promisee.

5. **Consideration 2(d)**: When at the desire of the promisor, the promisee or any other person has done or abstained from doing or does or abstains from doing or promises to do or to abstain from doing something such act or abstinence or promise is called a consideration for the promise. Price paid by one party for the promise of the other Technical word meaning QUID-PRO-QUO i.e. something in return.

6. **Agreement 2(e)** : Every promise and set of promises forming the consideration for each other. In short,

(agreement=Offer+Acceptance)

7. **Contract 2(h)** : An agreement enforceable by Law is a contract.

Therefore, there must be an agreement and it should be enforceable by law.

(Contract=Agreement+Enforceability)

8. **Void agreement 2(g)**:- An agreement not enforceable by law is void.

9. **Voidable contract 2(i)**: An agreement is a voidable contract if it is enforceable by Law at the option of one or more of the parties there to (i.e. the aggrieved party), and it is not enforceable by Law at the option of the other or others.

10. **Void contract 2(j)** : A contract which ceases to be enforceable by Law becomes void when it ceases to be enforceable.

According to Section 2(b), "When the person to whom the proposal is made signifies his assent there to, the proposal is said to be accepted."

Rules:

1. Acceptance must be absolute and unqualified. If the parties are not in ad idem on all matters concerning the offer and acceptance, there is no valid contract. For example, "A" says to "B" "I offer to sell my car for Rs.50,000/-. "B" replies "I will purchase it for Rs.45,000/-". This is not acceptance and hence it amounts to a counter offer.

2. It should be Communicated to the offeror. To conclude a contract between parties, the acceptance must be communicated in some prescribed form. A mere mental determination on the part of offeree to accept an offer does not amount to valid acceptance.

3. Acceptance must be in the mode prescribed. If the acceptance is not according to the mode prescribed or some usual and reasonable mode(where no mode is prescribed) the offeror may intimate to the offeree within a reasonable time that acceptance is not according to the mode prescribed and may insist that the offer be accepted in the prescribed

mode only. If he does not inform the offeree, he is deemed to have accepted the offer. For example, "A" makes an offer to "B" says to "B" that "if you accept the offer, reply by voice. "B" sends reply by post. It will be a valid acceptance, unless "A" informs "B" that the acceptance is not according to the prescribed mode.

4. Acceptance must be given within a reasonable time before the offer lapses. If any time limit is specified, the acceptance must be given within the time, if no time limit is specified it must be given within a reasonable time.

5. It cannot precede an offer. If the acceptance precedes an offer it is not a valid acceptance and does not result in contract. For example, in a company shares were allotted to a person who had not applied for them. Subsequently when he applied for shares, he was un aware of the previous allotment . The allotment of share previous to the application is not valid.

6. Acceptance by the way of conduct.

7. Mere silence is no acceptance. Silence does not per-se amounts to communication- Bank of India Ltd. Vs. Rustom Cowasjee- AIR 1955 Bom. 419 at P. 430; 57 Bom. L.R. 850- Mere silence cannot amount to any assent. It does not even amount to any representation on which any plea of estoppel may be found, unless there is a duty to make some statement or to do some act free and offer er must be consent

8. Acceptance must be unambiguous and definite.

Lawful consideration

According to Section 2(d), Consideration is defined as: "When at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or abstain from doing something, such act or abstinence or promise is called consideration for the promise". Consideration means

'something in return'.In short, Consideration means quid pro quo i.e. something in return. An agreement must be supported by a lawful consideration on both sides. Essentials of valid considerations are: It must move at the desire of the promisor. An act constituting consideration must have been done at the desire or request of the promiser. If it is done at the instance of a third party or without the desire of the promisor, it will not be good consideration. For example, "A" saves "B"'s goods from fire without being ask him to do so. "A" cannot demand payment for his service. Consideration may move from the promisee or any other person. Under Indian law, consideration may be from the promisee of any other person i.e., even a stranger. This means that as long as there is consideration for the promisee, it is immaterial, who has furnished it.

Consideration must be an act, abstinence or forebearance or a returned promise.Consideration may be past, present or future. Past consideration is not consideration according to English law. However it is a consideration as per Indian law. Example of past consideration is, "A" renders some service to "B" at latter's desire. After a month "B" promises to compensate "A" for service rendered to him earlier. When consideration is given simultaneously with promise, it is said to be present consideration .. For example, "A" receives Rs.50/- in return for which he promises to deliver certain goods to "B". The money "A" receives is the present consideration. When consideration to one party to other is to pass subsequently to the maker of the contract, is said to be future consideration. For example. "A" promises to deliver certain goods to "B" after a week. "B" promises to pay the price after a fortnight, such consideration is future.

Consideration must be real. Consideration must be real, competent and having some value in the eyes of law. For example, "A" promises to put life to "B"'s dead wife, if "B" pay him Rs.1000/-. "A"'s promise is physically impossible of performance hence there is no real consideration.

Consideration must be something which the promiser is not already bound to do. A promise to do something what one is already bound to do, either by law, is not a good consideration., since it adds nothing to the previous existing legal consideration.

Consideration need not be adequate. Consideration need not be necessarily be equal to value to something given. So long as consideration exists, the courts are not concerned as to adequacy, provided it is for some value.

The consideration or object of an agreement is lawful, unless and until it is:

- Forbidden by law: If the object or the consideration of an agreement is for doing an act forbidden by law, such agreement are void. for example,"A" promises "B" to obtain an employment in public service and "B" promises to pay Rs one lakh to "A". The agreement is void as the procuring government job through unlawful means is prohibited.
- If it involves injury to a person or property of another: For example, "A" borrowed rs.100/- from "B" and executed a bond to work for "B" without pay for a period of 2 years. In case of default, "A" owes to pay the principal sum at once and huge amount of interest. This contract was held void as it involved injury to the person.
- If courts regards it as immoral: An agreement in which consideration ir object of which is immoral is void. For example, An agreement between husband and wife for future separation is void.
- Is of such nature that, if permitted, it would defeat the provisions of any law: is fraudulent, or involves or implies injury to the person or property of another, or
- Is opposed to public policy. An agreement which tends to be injurious to the public or against the public good is void. For example, agreements of trading with foreign enemy, agreement to commit crime, agreements which interfere with the administration of justice, agreements which

interfere with the course of justice, stifling prosecution, maintenance and champerty.

- Agreements in restrained of legal proceedings: This deals with two category. One is, agreements restraining enforcement of rights and the other deals with agreements curtailing period of limitation.
- Trafficking in public offices and titles: agreements for sale or transfer of public offices and title or for procurement of a public recognition like Padma Vibhushan or Padma Shri etc. for monetary consideration is unlawful, being opposed to public policy.
- Agreements restricting personal liberty: agreements which unduly restricts the personal liberty of parties to it are void as being opposed by public policy.
- Marriage brokerage contact: Agreements to procure marriages for rewards are void under the ground that marriage ought to proceed with free and voluntary decisions of parties.
- Agreements interfering marital duties: Any agreement which interfere with performance of marital duty is void being opposed to public policy. An agreement between husband and wife that the wife will never leave her parental house.
- Consideration may take in any form-money, goods, services, a promise to marry, a promise to forbear etc.
- Contract Opposed to Public Policy can be Repudiated by the Court of law even if that contract is beneficial for all of the parties to the contract- What considerations and objects are lawful and what not- Newar Marble Industries Pvt. Ltd. Vs. Rajasthan State Electricity Board, Jaipur, 1993 Cr. L.J. 1191 at 1197, 1198 [Raj.]- Agreement of which object or consideration was opposed to public policy, unlawful and void- - What better and what more can be an admission of the fact that the consideration or object of the compounding agreement was abstention

by the board from criminally prosecuting the petitioner-company from offense under Section 39 of the act and that the Board has converted the crime into a source of profit or benefit to itself. This consideration or object is clearly opposed to public policy and hence the compounding agreement is unlawful and void under Section 23 of the Act. It is unenforceable as against the Petitioner-Company.

COMPETENT TO CONTRACT

Section 11 of The Indian Contract Act specifies that every person is competent to contract pro

1. He should not be a minor i.e. an individual who has not attained the age of majority i.e. 18 years in normal case and 21 years if guardian is appointed by the Court.

2. He should be of sound mind while making a contract. A person who is usually of unsound mind, but occasionally of sound mind, can make a contract when he is of sound mind. Similarly if a person is usually of sound mind, but occasionally of unsound mind, may not make a valid contract when he is of unsound mind.

3. He is not disqualified from contracting by any other law to which he is subject

There are other laws of the land that disqualify certain persons from contracting. They are:-

-Alien enemy

-Foreign sovereigns, diplomatic staff etc.

-Artificial persons i.e. corporation, companies etc.

-Insolvents

-Convicts

-Pardanashin Women

Free Consent

According to Section 13, " two or more persons are said to be consented when they agree upon the same thing in the same sense (Consensus-ad-idem). According to Section 14,Consent is said to be free when it is not caused by coercion or undue influence or fraud or misrepresentation or mistake.

Elements Vitiating free Consent

1. **Coercion (Section 15)**: "Coercion" is the committing, or threatening to commit, any act forbidden by the Indian Penal Code under(45,1860), or the unlawful detaining, or threatening to detain, any property, to the prejudice of any person whatever, with the intention of causing any person to enter into an agreement. For example, "A" threatens to shoot "B"if he doesn't release him from a debt which he owes to "B". "B" releases "A" under threat. Since the release has been brought about by coercion, such release is not valid. Explanation.-It is immaterial whether the Indian Penal Code (45 of 1860) is or is not in force in the place where the coercion is employed. Illustrations A, on board an English ship on the high seas, causes B to enter into an agreement by an act amounting to criminal intimidation under the Indian Penal Code (45 of 1860). A afterwards sues B for breach of contract at Calcutta. A afterwards sues B for breach of contract at Calcutta." A has employed coercion, although his act is not an offence by the law of England, and although section 506 of the Indian Penal Code (45 of 1860) was not in force at the time when or place where the act was done. A has employed coercion, although his act is not an offence by the law of England, and although section 506 of the Indian Penal Code (45 of 1860) was not in force at the time when or place where the act was done."

2. **Undue influence (Section 16)**: "Where a person who is in a position to dominate the will of another enters into a contract with him and the transaction appears on the face of it, or on the evidence, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall lie upon the person in the position to dominate the will of the other."

(Section 16(2) States that "A person is deemed to be in a position to dominate the will of another;

- Where he holds a real or apparent authority over the other. For example, an employer may be deemed to be having authority over his employee. an income tax authority over to the asessee.

- Where he stands in a fiduciary relationship to other, For example, the relationship of Solicitor with his client, spiritual advisor and devotee.

- Where he makes a contract with a person whose mental capacity is temporarily or permanently affected by the reason of age, illness or mental or bodily distress.

- Further, A contract is said to be induced by 'undue influence' where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other. '(2) In particular and without prejudice to the generality of the foregoing principle, a person is deemed to be in a position to dominate the will of another-

    (a) where he holds a real or apparent authority over the other, or where he stands in a fiduciary relation to the other; or

    (b) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness, or mental or bodily distress.

Where a person who is in a position to dominate the will of another, enters into a contract with him, and the transaction appears, on the face of it or on the evidence adduced, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall be upon the person in a position to dominate the will of the other. Nothing in the sub-section shall affect the provisions of section 111 of the Indian Evidence Act, 1872 (1 of 1872). Illustrations

(a) A having advanced money to his son, B, during his minority, upon B's coming of age obtains, by misuse of parental influence, a bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence."

(b) A, a man enfeebled by disease or age, is induced, by B's influence over him as his medical attendant, to agree to pay B an unreasonable sum for his professional services, B employes undue influence."

(c) A, being in debt to B, the money-lender of his village, contracts a fresh loan on terms which appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence."

(d) A applies to a banker for a loan at a time when there is stringency in the money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

3. **Fraud (Section 17)**: "Fraud" means and includes any act or concealment of material fact or misrepresentation made knowingly by a party to a contract, or with his connivance, or by his agent, with intent to deceive another party thereto of his agent, or to induce him to enter into the contract. Mere silence is not fraud. a contracting party is not obliged to disclose each and everything to the other party. There are two exceptions where even mere silence may be fraud, one is where there is a duty to speak, then keeping silence is fraud. or when silence is in itself equivalent to speech, such silence is fraud.

In other words 'Fraud' means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent1, with intent to deceive another party thereto or his agent, or to induce him to enter into the contract\:-"

(1) the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;

(2) the active concealment of a fact by one having knowledge or belief of the fact;

(3) a promise made without any intention of performing it;

(4) any other act fitted to deceive;

(5) any such act or omission as the law specially declares to be fraudulent. Explanation.-Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence, is, in itself, equivalent to speech. Illustrations

(a) A sells, by auction, to B, a horse which A knows to be unsound. A says nothing to B about the horse's unsoundness. This is not fraud in A."

(b) B is A's daughter and has just come of age. Here the relation between the parties would make it A's duty to tell B if the horse is unsound."

(c) B says to A-"If you do not deny it, I shall assume that the horse is sound". A says nothing. Here, A's silence is equivalent to speech."

(d) A and B, being traders, enter upon a contract. A has private information of a change in prices which would affect B's willingness to proceed with the contract. A is not bound to inform B."

4. Misrepresentation (Section 18): " causing, however innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement".

Misrepresentation" means and includes:

(1) the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;

(2) any breach of duty which, without an intent to deceive, gains

an advantage of the person committing it, or any one claiming under him, by misleading another to his prejudice, or to the prejudice of any one claiming under him;

(3) Causing, however innocently, a party to an agreement, to make a mistake as to the substance of the thing which is the subject of the agreement.

5. Mistake of fact (Section 20): "Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void". A party cannot be allowed to get any relief on the ground that he had done some particular act in ignorance of law.Mistake may be bilateral mistake where both parties to an agreement are under mistake as to the matter of fact.The mistake must relate to a matter of fact essential to the agreement.

Agency

In law, the relationship that exists when one person or party (the principal) engages another (the agent) to act for him, e.g. to do his work, to sell his goods, to manage his business. The law of agency thus governs the legal relationship in which the agent deals with a third party on behalf of the principal. The competent agent is legally capable of acting for this principal vis-à-vis the third party. Hence, the process of concluding a contract through an agent involves a twofold relationship. On the one hand, the law of agency is concerned with the external business relations of an economic unit and with the powers of the various representatives to affect the legal position of the principal. On the other hand, it rules the internal relationship between principal and agent as well, thereby imposing certain duties on the representative (diligence, accounting, good faith, etc.).

Under section 201 to 210 an agency may come to an end in a variety of ways:

(i) By the principal revoking the agency - However, principal cannot revoke

an agency coupled with interest to the prejudice of such interest. Such Agency is coupled with interest. An agency is coupled with interest when the agent himself has an interest in the subject-matter of the agency, e.g., where the goods are consigned by an upcountry constituent to a commission agent for sale, with poor to recoup himself from the sale proceeds, the advances made by him to the principal against the security of the goods; in such a case, the principal cannot revoke the agent's authority till the goods are actually sold, nor is the agency terminated by death or insanity. (Illustrations to section 201)

(ii) By the agent renouncing the business of agency;

(iii) By the business of agency being completed;

(iv) By the principal being adjudicated insolvent (Section 201 of The Indian Contract Act. 1872)

The principal also cannot revoke the agent's authority after it has been partly exercised, so as to bind the principal (Section 204), though he can always do so, before such authority has been so exercised (Sec 203).

Further, as per section 205, if the agency is for a fixed period, the principal cannot terminate the agency before the time expired, except for sufficient cause. If he does, he is liable to compensate the agent for the loss caused to him thereby. The same rules apply where the agent, renounces an agency for a fixed period. Notice in this connection that want of skill continuous disobedience of lawful orders, and rude or insulting behavior has been held to be sufficient cause for dismissal of an agent. Further, reasonable notice has to be given by one party to the other; otherwise, damage resulting from want of such notice, will have to be paid (Section 206). As per section 207, the revocation or renunciation of an agency may be made expressly or impliedly by conduct. The termination does not take effect as regards the agent, till it becomes known to him and as regards third party, till the termination is known to them (Section 208).

When an agent's authority is terminated, it operates as a termination of subagent also. (Section 210).

What agreements are contracts.-All agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void. -All agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void." Nothing herein contained shall affect any law in force in 1[India], and not hereby expressly repealed, by which any contract is required to be made in writing 2or in the presence of witnesses, or any law relating to the registration of documents.

- **Voidability of agreements without free consent :** When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused. A party to contract, whose consent was caused by fraud or misrepresentation, may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representations made had been true.

If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of section 17, the contract, nevertheless, is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence. Explanation.-A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practised, or to whom such misrepresentation was made, does not render a contract voidable. Illustrations

(a) A, intending to deceive B, falsely represents that five hundred maunds of indigo are made annually at A's factory, and thereby induces B to buy the factory. The contract is voidable at the option of B."

(b) A, by a misrepresentation, leads B erroneously to believe that five hundred maunds of indigo are made annually at A's factory. B examines the accounts

of the factory, which show that only four hundred maunds of indigo have been made. After this B buys the factory. The contract is not voidable on account of A's misrepresentation."

(c) A fraudulently informs B that A's estate is free from incumbrance. B thereupon buys the estate. The estate is subject to a mortgage. B may either avoid the contract, or may insist on its being carried out and mortgage-debt redeemed."

(d) B, having discovered a vein of ore on the estate of A, adopts means to conceal, and does conceal the existence of the ore from A. Through A's ignorance B is enabled to buy the estate at an under-value. The contract is voidable at the option of A."

(e) A is entitled to succeed to an estate at the death of B; B dies: C, having received intelligence of B's death, prevents the intelligence reaching A, and thus induces A to sell him his interest in the estate. The sale is voidable at the option of A."

- **Power to set aside contract induced by undue influence :** When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused. 2[19A. Power to set aside contract induced by undue influence.-When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused." Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just. Illustrations

(a) A's son has forged B's name to a promissory note. B under threat of prosecuting A's son, obtains a bond from A for the amount of the forged note. If B sues on this bond, the Court may set the bond aside.

(b) A, a money-lender, advances Rs. 100 to B, an agriculturist, and, by undue influence, induces B to execute a bond for Rs. 200 with interest at

6 per cent. per month. The Court may set the bond aside, ordering B to repay the Rs. 100 with such interest as may seem just.] (b) A, a money-lender, advances Rs. 100 to B, an agriculturist, and, by undue influence, induces B to execute a bond for Rs. 200 with interest at 6 per cent. per month. The Court may set the bond aside, ordering B to repay the Rs. 100 with such interest as may seem just.]"

- **Agreement void where both parties are under mistake as to matter of fact :** Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement the agreement is void. Explanation.-An erroneous opinion as to the value of the thing which forms the subject-matter of the agreement, is not to be deemed a mistake as to a matter of fact. Illustrations

(a) A agrees to sell to B a specific cargo of goods supposed to be on its way from England to Bombay. It turns out that, before the day of the bargain the ship conveying the cargo had been cast away and the goods lost. Neither party was aware of these facts. The agreement is void."

(b) A agrees to buy from B a certain horse. It turns out that the horse was dead at the time of the bargain, though neither party was aware of the fact. The agreement is void."

(c) A, being entitled to an estate for the life of B, agrees to sell it to C, B was dead at the time of agreement, but both parties were ignorant of the fact. The agreement is void."

- **Effect of mistakes as to law :** A contract is not voidable because it was caused by a mistake as to any law in force in India; but a mistake as to a law not in force in India has the same effect as a mistake of fact." Illustration A and B make a contract grounded on the erroneous belief that a particular debt is barred by the Indian Law of Limitation; the contract is not voidable. A and B make a contract grounded on the erroneous belief that a particular debt is barred by the Indian Law of Limitation; the contract is not voidable."

- ***Contract caused by mistake of one party as to matter of fact :*** A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact."

What consideration and objects are lawful, and what not.-

The consideration or object of an agreement is lawful, unless-" it is forbidden by law; or is of such a nature that, if permitted, it would defeat the provisions of any law; or is fraudulent; or involves or implies, injury to the person or property of another; or the Court regards it as immoral, or opposed to public policy. In each of these cases, the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful is void. Illustrations

(a) A agrees to sell his house to B for 10,000 rupees. Here, B's promise to pay the sum of 10,000 rupees is the consideration for A's promise to sell the house and A's promise to sell the house is the consideration for B's promise to pay the 10,000 rupees. These are lawful considerations."

(b) A promises to pay B 1,000 rupees at the end of six months, if C, who owes that sum to B, fails to pay it. B promises to grant time to C accordingly. Here, the promise of each party is the consideration for the promise of the other party, and they are lawful considerations.

(c) A promises, for a certain sum paid to him by B, to make good to B the value of his ship if it is wrecked on a certain voyage. Here, A's promise is the consideration for B's payment, and B's payment is the consideration for A's promise, and these are lawful considerations."

(d) A promises to maintain B's child, and B promises to pay A 1,000 rupees yearly for the purpose. Here, the promise of each party is the consideration for the promise of the other party. They are lawful considerations."

(e) A, B and C enter into an agreement for the division among them of gains

acquired or to be acquired, by them by fraud. The agreement is void, as its object is unlawful.

(f) A promises to obtain for B an employment in the public service and B promises to pay 1,000 rupees to A. The agreement is void, as the consideration for it is unlawful.

(g) A, being agent for a landed proprietor, agrees for money, without the knowledge of his principal, to obtain for B a lease of land belonging to his principal. The agreement between A and B is void, as it implies a fraud by concealment, by A, on his principal.

(h) A promises B to drop a prosecution which he has instituted against B for robbery, and B promises to restore the value of the things taken. The agreement is void, as its object is unlawful."

(i) A's estate is sold for arrears of revenue under the provisions of an Act of the Legislature, by which the defaulter is prohibited from purchasing the estate. B, upon an understanding with A, becomes the purchaser, and agrees to convey the estate to A upon receiving from him the price which B has paid. The agreement is void, as it renders the transaction, in effect, a purchase by the defaulter and would so defeat the object of the law."

(j) A, who is B's mukhtar, promises to exercise his influence, as such, with B in favour of C, and C promises to pay 1,000 rupees to A. The agreement is void, becuase it is immoral."

(k) A agrees to let her daughter to hire to B for concubinage. The agreement is void, because it is immoral, though the letting may not be punishable under the Indian Penal Code (45 of 1860).

- **Agreements void, if considerations and objects unlawful in part :**

If any part of a single consideration for one or more objects, or any one or any part of any one of several considerations for a single object, is unlawful, the

agreement is void." Illustration A promises to superintend, on behalf of B, a legal manufacturer of indigo, and an illegal traffic in other articles. B promises to pay to A a salary of 10,000 rupees a year. The agreement is void, the object of A's promise, and the consideration for B's promise, being in part unlawful.

Agreement without consideration, void, unless it is in writing and registered or is a promise to compensate for something done or is a promise to pay a debt barred by limitation law.-An agreement made without consideration is void, unless- -An agreement made without consideration is void, unless-"

(1) it is expressed in writing and registered under the law for the time being in force for the registration of 1[documents], and is made on account of natural love and affection between parties standing in a near relation to each other; or unless

(2) it is a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, or something which the promisor was legally compellable to do; or unless.

(3) It is a promise, made in writing and signed by the person to be charged therewith, or by his agent generally or specially authorized in that behalf, to pay wholly or in part a debt of which the creditor might have enforced payment but for the law for the limitation of suits. In any of these cases, such an agreement is a contract. Explanation 1.-Nothing in this section shall affect the validity, as between the donor and donee, of any gift actually made. Explanation 2.-An Agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate; but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent of the promisor was freely given. Illustrations

(a) A promises, for no consideration, to give to B Rs. 1,000. This is a void agreement. (a) A promises, for no consideration, to give to B Rs. 1,000. This is a void agreement."

(b) A, for natural love and affection, promises to give his son, B, Rs. 1,000. A puts his promise to B into writing and registers it. This is a contract."

(c) A finds B's purse and gives it to him. B promises to give A Rs. 50. This is a contract.

(d) A supports B's infant son. B promises to pay A's expenses in so doing. This is a contract."

(e) A owes B Rs. 1,000, but the debt is barred by the Limitation Act. A signs a written promise to pay B Rs. 500 on account of the debt. This is a contract."

(f) A agrees to sell a horse worth Rs. 1,000 for Rs. 10. A's consent to the agreement was freely given. The agreement is a contract notwithstanding the inadequacy of the consideration."

(g) A agrees to sell a horse worth Rs. 1,000 for Rs. 10. A denies that his consent to the agreement was freely given." The inadequacy of the consideration is a fact which the Court should take into account in considering whether or not A's consent was freely given.

- **Agreement in restraint of marriage, void :** Every agreement in restraint of the marriage of any person, other than a minor, is void."

- **Agreement in restraint of trade, void** : Every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void. -Exception 1.-Saving of agreement not to carry on business of which goodwill is sold.-One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the goodwill from him, carries on a like business therein, provided that such limits appear to the Court reasonable, regard being had to the nature of the business.

- **Agreements in restraint of legal proceedings, void.** ***Every agreement***

  (a) by which any party thereto is restricted absolutely from enforcing his rights under or in respect of any contract, by the usual legal proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights; or

  (b) which extinguishes the rights of any party thereto, or discharges any party thereto, from any liability, under or in respect of any contract on the expiry of a specified period so as to restrict any party from enforcing his rights, is void to that extent.

  Exception 1.- Saving of contract to refer to arbitration dispute that may arise. -This section shall not render illegal a contract, by which two or more persons agree that any dispute which may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable in respect of the dispute so referred.

  Exception 2.- Saving of contract to refer questions that have already arisen. -Nor shall this section render illegal any contract in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration. 19

- **Agreements void for uncertainty :** Agreements, the meaning of which is not certain, or capable of being made certain, are void. Illustrations

  (a) A agrees to sell B "a hundred tons of oil". There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty."

  (b) A agrees to sell B one hundred tons of oil of a specified description, known as an article of commerce. There is no uncertainty here to make the agreement void."

(c) A, who is a dealer in coconut-oil only, agrees to sell to B "one hundred tons of oil". The nature of A's trade affords an indication of the meaning of the words, and A has entered into a contract for the sale of one hundred tons of coconut-oil."

(d) A agrees to sell B "all the grain in my granary at Ramnagar". There is no uncertainty here to make the agreement void."

(e) A agrees to sell to B "one thousand maunds of rice at a price to be fixed by C". As the price is capable of being made certain, there is no uncertainty here to make the agreement void."

f) A agrees to sell to B "my white horse for rupees five hundred or rupees one thousand". There is nothing to show which of the two prices was to be given. The agreement is void."

- **Agreements by way of wager, void**: Agreements by way of wager are void; and no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to any person to abide the result of any game or other uncertain event on which any wager is made. -Agreements by way of wager are void; and no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to any person to abide the result of any game or other uncertain event on which any wager is made." Exception in favour of certain prizes for horse-racing.-This section shall not be deemed to render unlawful a subscription or contribution, or agreement to subscribe or contribute, made or entered into for or toward any plate, prize or sum of money, of the value or amount of five hundred rupees or upwards, to be rewarded to the winner or winners of any horse-race. Section 294A of the Indian Penal Code not affected.-Nothing in this section shall be deemed to legalize any transaction connected with horse-racing, to which the provisions of section 294A of the Indian Penal Code (45 of 1860) apply.

- **“Contingent contract” defined :** A “contingent contract” is a contract to do or not to do something, if some event, collateral to such contract, does or does not happen. -A “contingent contract” is a contract to do or not to do

something, if some event, collateral to such contract, does or does not happen." Illustration A contracts to pay to B Rs.10,000 if B's house is burnt. This is a contingent contract. A contracts to pay to B Rs.10,000 if B's house is burnt. This is a contingent contract."

- **Enforcement of contracts contingent on an event happening :** Contingent contracts to do or not to do anything if an uncertain future event happens, cannot be enforced by law unless and until that event has happened. - Contingent contracts to do or not to do anything if an uncertain future event happens, cannot be enforced by law unless and until that event has happened." If the event becomes impossible, such contracts become void. Illustrations

  (a) A makes a contract with B to buy B's horse if A survives C. This contract cannot be enforced by law unless and until C dies in A's lifetime."

  (b) A makes a contract with B to sell a horse to B at a specified price, if C, to whom the horse has been offered, refuses to buy him. The contract cannot be enforced by law unless and until C refuses to buy the horse.

  (c) A contracts to pay B a sum of money when B marries C. C dies without being married to B. The contract becomes void."

- **Enforcement of contracts contingent on an event not happening :**

Contingent contracts to do or not to do anything if an uncertain future event does not happen, can be enforced when the happening of that event becomes impossible, and not before." Illustration A agrees to pay B a sum of money if a certain ship does not return. The ship is sunk. The contract can be enforced when the ship sinks. A agrees to pay B a sum of money if a certain ship does not return. The ship is sunk. The contract can be enforced when the ship sinks."

When event on which contract is contingent to be deemed impossible, if it is the future conduct of a living person.-

If the future event on which a contract is contingent is the way in which a person will act at an unspecified time, the event shall be considered to become impossible when such person does anything which renders it impossible that he should so act within any definite time, or otherwise than under further contingencies." Illustration A agrees to pay B a sum of money if B marries C, C marries D. The marriage of B to C must now be considered impossible, although it is possible that D may die and that C may afterwards marry B.

When contracts become void, which are contingent on happening of specified event within fixed time.

Contingent contracts to do or not to do anything, if a specified uncertain event happens within a fixed time, become void if, at the expiration of the time fixed, such event has not happened, or if, before the time fixed, such event becomes impossible. When contracts may be enforced, which are contingent on specified event not happening within fixed time.

Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when the time fixed has expired, and such event has not happened, or before the time fixed has expired, if it becomes certain that such event will not happen. - Contingent contracts to do or not to do anything, if a specified uncertain event does not happen within a fixed time, may be enforced by law when the time fixed has expired, and such event has not happened, or before the time fixed has expired, if it becomes certain that such event will not happen." Illustrations

(a) A promises to pay B a sum of money if a certain ship returns within a year. The contract may be enforced if the ship returns within the year; and becomes void if the ship is burnt within the year."

(b) A promises to pay B a sum of money if a certain ship does not return within a year. The contract may be enforced if the ship does not return within the year, or is burnt within the year.

- **Agreements contingent on impossible event void :** Contingent agreements to do or not to do anything, if an impossible event happens, are void, whether the impossibility of the event is known or not to the parties to the agreement at the time when it is made. Illustrations

(a) A agrees to pay B 1,000 rupees if two straight lines should enclose a space. The agreement is void."

(b) A agrees to pay B 1,000 rupees if B will marry A's daughter C. C was dead at the time of the agreement. The agreement is void."

Obligation of parties to contract-The parties to a contract must either perform, or offer to perform, their respective promises, unless such performance is dispensed with or excused under the provisions of this Act, or of any other law. Promises bind the representatives of the promisors in case of the death of such promisors before performance, unless a contrary intention appears from the contract. Illustrations

(a) A promises to deliver goods to B on a certain day on payment of Rs.1,000. A dies before that day. A's representatives are bound to deliver the goods to B, and B is bound to pay the Rs. 1,000 to A's representatives."

(b) A promises to paint a picture for B by a certain day, at a certain price. A dies before the day. The contract cannot be enforced either by A's representatives or by B."

38. Effect of refusal to accept offer of performance. Where a promisor has made an offer of performance to the promisee, and the offer has not been accepted, the promisor is not responsible for non-performance, nor does he thereby lose his right under the contract." Every such offer must fulfil the following conditions:-

(1) it must be unconditional;

(2) it must be made at a proper time and place, and under such circumstances that the person to whom it is made may have a reasonable

opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do;

(3) if the offer is an offer to deliver anything to the promisee, the promisee must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver. An offer to one of several joint promisees has the same legal consequences as an offer to all of them. Illustration A contracts to deliver to B at his warehouse, on the 1st March, 1873, 100 bales of cotton of a particular quality. In order to make an offer of performance with the effect stated in this section. A must bring the cotton to B's warehouse, on the appointed day, under such circumstances that B may have a reasonable opportunity of satisfying himself that the thing offered is cotton of the quality contracted for, and that there are 100 bales.

- **Effect of refusal of party to perform promise wholly :** When a party to a contract has refused to perform, or disabled himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance. Illustrations

(a) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night A wilfully absents herself from the theatre. B is at liberty to put an end to the contract."

(b) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during next two months, and B engages to pay her at the rate of 100 rupees for each night. On the sixth night A wilfully absents herself. With the assent of B, A sings on the seventh night. B has signified his acquiescence in the continuance of

the contract, and cannot now put an end to it, but is entitled to compensation for the damage sustained by him through A's failure to sing on the sixth night."

- **Person by whom promise is to be performed :** If it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such promise must be performed by the promisor. In other cases, the promisor or his representative may employ a competent person to perform it." Illustrations

(a) A promises to pay B a sum of money. A may perform this promise, either by personally paying the money to B or by causing it to be paid to B by another; and, if A dies before the time appointed for payment, his representatives must perform the promise, or employ some proper person to do so."

(b) A promises to paint a picture for B. A must perform this promise personally."

- **Effect of accepting performance from third person :** When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

- **Devolution of joint liabilities :** When two or more persons have made a joint promise, then, unless a contrary intention appears by the contract, all such persons, during their joint lives, and, after the death of any of them, his representative jointly with the survivor or survivors, and, after the death of the last survivor, the representatives of all jointly, must fulfil the promise."

Any one of joint promisors may be compelled to perform. When two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any 1[one or more] of such joint promisors to perform the whole of the promise." Each promisor may compel contribution. Each of two or more joint promisors may compel every other joint promisor to contribute equally with himself to the performance of the promise, unless a

contrary intention appears from the contract." Sharing of loss by default in contribution.-If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares. -If any one of two or more joint promisors makes default in such contribution, the remaining joint promisors must bear the loss arising from such default in equal shares." Explanation.-Nothing in this section shall prevent a surety from recovering, from his principal, payments made by the surety on behalf of the principal, or entitle the principal to recover anything from the surety on account of payment made by the principal. Illustrations

(a) A, B and C jointly promise to pay D 3,000 rupees. D may compel either A or B or C to pay him 3,000 rupees."

(b) A, B and C jointly promise to pay D the sum of 3,000 rupees. C is compelled to pay the whole. A is insolvent, but his assets are sufficient to pay one-half of his debts. C is entitled to receive 500 rupees from A's estate, and 1,250 rupees from B.

(c) A, B and C are under a joint promise to pay D 3,000 rupees. C is unable to pay anything, and A is compelled to pay the whole. A is entitled to receive 1,500 rupees from B."

(d) A, B and C are under a joint promise to pay D 3,000 rupees. A and B being only sureties for C. C fails to pay. A and B are compelled to pay the whole sum. They are entitled to recover it from C."

- **Effect of release of one joint promisor** : Where two or more persons have made a joint promise, a release of one of such joint promisors by the promisee does not discharge the other joint promisor or joint promisors, neither does it free the joint promisors so released from responsibility to the other joint promisor or joint promisors.

- **Devolution of joint rights**: When a person has made a promise to two or more persons jointly, then, unless a contrary intention appears from the contract, the right to claim performance rests, as between him and then, with

them during their joint lives, and, after the death of any of them, with the representative of such deceased person jointly with the survivor or survivors, and, after the death of the last survivor, with the representatives of all jointly. Illustration A, in consideration of 5,000 rupees lent to him by B and C, promises B and C jointly to repay them that sum with interest on a day specified. B dies. The right to claim performance rests with B's representative jointly with C during C's life, and after the death of C, with the representatives of B and C jointly.

Time for performance of promise, where no application is to be made and no time is specified.-Where, by the contract, a promisor is to perform his promise without application by the promisee, and no time for performance is specified, the engagement must be performed within a reasonable time. Explanation.-The question "what is a reasonable time" is, in each particular case, a question of fact.

Time and place for performance of promise, where time is specified and no application to be made. When a promise is to be performed on a certain day, and the promisor has undertaken to perform it without application by the promisee, the promisor may perform it at any time during the usual hours of business on such day and at the place at which the promise ought to be performed. Illustration A promises to deliver goods at B's warehouse on the first January. On the day A brings the goods to B's warehouse, but after the usual hour closing it, and they are not received. A has not performed his promise. A promises to deliver goods at B's warehouse on the first January.

Application for performance on certain day to be at proper time and place.-When a promise is to be performed on a certain day, and the promisor has not undertaken to perform it without application by the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business. Explanation.-The question "what is a proper time and place" is, in each particular case, a question of fact.

Place for the performance of promise, where no application to be made and no place fixed for performance.-When a promise is to be performed

without application by the promisee, and no place is fixed for the performance of it, it is the duty of the promisor to apply to the promisee to appoint a reasonable place for the performance of the promise, and to perform it at such a place. Illustration A undertakes to deliver a thousand maunds of jute to B on a fixed day. A must apply to B to appoint a reasonable place for the purpose of receiving it, and must deliver it to him at such place. A undertakes to deliver a thousand maunds of jute to B on a fixed day.

Performance in manner or at time prescribed or sanctioned by promisee. The performance of any promise may be made in any manner, or at any time which the promisee prescribes or sanctions." Illustrations

(a) B owes A 2,000 rupees. A desires B to pay the amount to A's account with C, a banker. B, who also banks with C, orders the amount to be transferred from his account to A's credit, and this is done by C. Afterwards, and before A knows of the transfer, C fails. There has been a good payment by B."

(b) A and B are mutually indebted. A and B settle an account by setting off one item against another, and B pays A the balance found to be due from him upon such settlement. This amounts to a payment by A and B, respectively, of the sums which they owed to each other."

(c) A owes B 2,000 rupees. B accepts some of A's goods in reduction of the debt. The delivery of the goods operates as a part payment."

(d) A desires B, who owes him Rs.100, to send him a note for Rs.100 by post. The debt is discharged as soon as B puts into the post a letter containing the note duly addressed to A."

- **Promisor not bound to perform, unless reciprocal promisee ready and willing to perform :** When a contract consists of reciprocal promises to be simultaneously performed, no promisor need perform his promise unless the promisee is ready and willing to perform his reciprocal promise. Illustrations

(a) A and B contract that A shall deliver goods to B to be paid for by B on delivery. A need not deliver the goods, unless B is ready and willing to pay for the goods on delivery." B need not pay for the goods, unless A is ready and willing to deliver them on payment. B need not pay for the goods, unless A is ready and willing to deliver them on payment."

(b) A and B contract that A shall deliver goods to B at a price to be paid by instalments, the first instalment to be paid on delivery." A need not deliver, unless B is ready and willing to pay the first instalment on delivery. B need not pay the first instalment, unless A is ready and willing to deliver the goods on payment of the first instalment."

- **Order of performance of reciprocal promises :** Where the order in which reciprocal promises are to be performed is expressly fixed by the contract, they shall be performed in that order; and where the order is not expressly fixed by the contract, they shall be performed in that order which the nature of the transaction requires. Illustrations

(a) A and B contract that A shall build a house for B at a fixed price. A's promise to build the house must be performed before B's promise to pay for it."

(b) A and B contract that A shall make over his stock-in-trade to B at a fixed price, and B promise to give security for the payment of the money. A's promise need not be performed until the security is given, for the nature of transaction requires that A should have security before he delivers up his stock."

- **Liability of party preventing event on which the contract is to take effect** : When a contract contains reciprocal promises, and one party to the contract prevents the other from performing his promise, the contract becomes viodable at the option of the party so prevented and he is entitled to compensation 23 from the other party for any loss which he may sustain in consequence of the non-performance of the contract. Illustration A and B

contract that B shall execute certain work for A for a thousand rupees. B is ready and willing to execute the work accordingly, but A prevents him from doing so. The contract is voidable at the option of B; and, if he elects to rescind it, he is entitled to recover from A compensation for any loss which he has incurred by its non-performance.

Effect of default as to that promise which should be performed, in contract consisting of reciprocal promises. When a contract consists of reciprocal promises, such that one of them cannot be performed, or that its performance cannot be claimed till the other has been performed, and the promisor of the promise last mentioned fails to perform it, such promisor cannot claim the performance of the reciprocal promise, and must make compensation to the other party to the contract for any loss which such other party may sustain by the non-performance of the contract." Illustrations

(a) A hires B's ship to take in and convey, from Calcutta to the Mauritius, a cargo to be provided by A, B receiving a certain freight for its conveyance. A does not provide any cargo for the ship. A cannot claim the performance of B's promise, and must take compensation to B for the loss which B sustains by the non-performance of the contract."

(b) A contracts with B to execute certain builder's work for a fixed price, B supplying the scaffolding and timber necessary for the work. B refuses to furnish any scaffolding or timber, and the work cannot be executed. A need not execute the work, and B is bound to make compensation to A for any loss caused to him by the non-performance of the contract."

(c) A contracts with B to deliver to him, at a specified price, certain merchandise on board a ship which cannot arrive for a month, and B engages to pay for the merchandise within a week from the date of the contract. B does not pay within the week. A's promise to deliver need not be performed, and B must make compensation."

(d) A promises B to sell him one hundred bales of merchandise, to be

delivered next day, and B promises A to pay for them within a month. A does not deliver according to his promise. B's promise to pay need not be performed, and A must make compensation."

- **Effect of failure to perform at a fixed time, in contract in which time is essential :** When a party to a contract promises to do a certain thing at or before a specified time, or certain things at or before specified times, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the intention of the parties was that time should be of the essence of the contract." Effect of such failure when time is not essential.-If it was not the intention of the parties that time should be of the essence of the contract, the contract does not become voidable by the failure to do such thing at or before the specified time; but the promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure. Effect of acceptance of performance at time other than that agreed upon.-If, in case of a contract voidable on account of the promisor's failure to perform his promise at the time agreed, the promisee accepts performance of such promise at any time other than that agreed, the promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless, at the time of such acceptance he gives notice to the promisor of his intention to do so.

2.3 THE LAW OF SALE OF GOODS AND CONTRACT OF SALES

- **Law of Sale of Goods :** Indian Sale of Goods Act 1930 is a Mercantile Law. The Sale of Goods Act is a kind of Indian Contract Act. It came into existence on 1 July 1930. It is a contract whereby the sellers transfers or agrees to transfer the property in the goods to the buyer for price. It is applicable all over India, except Jammu and Kashmir.A contract where by the seller transfers or agrees to transfer the property or the goods to the buyer for price.A contract to transfer the ownership of goods from seller to the buyer is known as contract of sale.

Definition

According to section 4(1) of the Indian sales of goods act, a contract of sales means such contract by which by which the seller transfer the title or ownership of the goods to the buyer or makes an agreement to transfer it against a fixed price."

1. *Buyer*: A person who buys or agrees to buy goods.
2. *Seller*: A person who sells or agrees to sell goods.
3. *Goods*: Every kind of movable property other than actionable things and money.
4. *Existing goods*: Goods which are in existence at the time of contract of sale.
5. *Future goods*: Goods which are to be manufactured /produced by seller after making contract of sale.
6. *Specific goods*: Goods which are identified & agreed upon at the time of contract of sale has been made.

Section 4 of the Sales of Goods Act, 1930 de?nes a sale of goods as a "contract of sale whereby the seller transfers or agrees to transfer the property in goods to the buyer for price". The term 'contract of sale' includes both a sale and an agreement to sell. A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer by the other party. The contract may be oral or in writing. A contract of sale may be absolute or conditional.

Formalities of a contract of sale

Section 5 of the Act speci?cally provides for the following three steps or formalities in a contract of a sale:

1) *Offer and Acceptance*: A contract of sale is made by an o?er to buy or sell the goods for a price and acceptance of such o?er.

2) *Delivery and Payment*: It is not necessary that the payment for the goods to the seller and delivery of goods to the buyer must be simultaneous. They can be made at different times or in instalments - as per the contract.

3) *Express or Implied*: The contract can be in writing, oral or implied. It can also be partly oral and partly written.

Essentials

The five essential features of a contract of sale are as discussed below:

1) Two partied

2) Subject matter to be goods

3) Transfer of ownership of goods

4) Consideration is price.

5) Essential elements of a valid contract

1) **Two parties**: A sale has to be bilateral because the goods have to pass from one person to another. There must be a buyer - a person who buys or agrees to buy the goods and a seller - a person who sells or agrees to sell goods. The seller and the buyer must be different persons. A part owner can sell to another part owner. A partner may, therefore, sell to his firm or a firm may sell to a partner. But if joint owners distribute property among themselves as per mutual agreement, it is not sale'. A person cannot be the seller of his own goods as well as the buyers of them. However, when a bankrupt person's goods are sold under an execution of decree, the person may buy back his own goods from his trustee.

2) • **Subject mater to be goods:** The term 'goods' is defined in Section 2(7). It states that 'goods' "means every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale". However, when a bankrupt person's goods are sold under an execution of decree, the person may buy back his own goods from his trustee.

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Money cannot be sold because money means legal tender and not the old coins which can be sold and purchased as goods. Actionable claims are things that a person cannot make use of, but which can be claimed by him by means of legal action such as a debt.

Sale of immovable property is not covered under this Act. As per Section 3 of the Transfer of Property Act, 1882, 'immovable property' does not include standing timber, growing crops or grass. They are considered movable property and thus goods. Standing timber is taken as movable property while trees are immovable property.

Things like goodwill, copyright, trademark, patents, water, gas, electricity are all goods. In the case of Commissioner of Sales Tax vs. Madhya Pradesh Electricity Board [AIR 1970 SC 732], the Supreme Court observed - "...electricity...can be transmitted, transferred, delivered, stored, possessed, etc., in the same way as any other movable property...If there can be sale and purchase of electric energy like any other movable object, we see no di?culty in holding that electric energy was intended to be covered by the de?nition of "goods".

In the case of H. Anraj vs. Government of Tamil Nadu [AIR 1986 SC 63], it was held that lottery tickets are goods and not actionable claims. Thus, sale of lottery tickets is sale of goods. Sugarcane supplied to a sugar factory is goods within the meaning of Section 2(7) of the Act as held in the case of UP Cooperative Cane Unions Federation vs. West UP Sugar Mills Assn. [AIR 2004 SC 3697]

3) **Transfer of ownership of Goods :** There must be transfer of ownership or an agreement to transfer the ownership of goods from the seller to the buyer - not the transfer of mere possession or limited interest as in the case of pledge, lease or hire purchase agreement). If goods remain in possession of seller after sale transaction is over, the 'possession' is with seller, but 'ownership' is with buyer. The Act uses the term 'general property' implying that sale involves total ownership and not a specifc right limited by conditions.

Delivery of goods refers to a voluntary transfer of possession of goods from one person to another. Delivery may be constructive or actual depending upon the circumstances of each case. A contract may provide for the immediate delivery of the goods or immediate payment of the price or both. Alternatively, the delivery or payment may be made by instalments or be postponed.

4) **Consideration is Price :** The consideration in a contract of sale has to be price i.e., money. If goods are offered as the consideration for goods, it will not amount to sale. It will be barter. If there is no consideration, it will be called gift. But where the goods are sold for de?nite sum and the price is paid partly in kind and partly in cash, the transaction is a sale.

Consideration is an essential for a valid contract as per the Indian Contract Act, 1872. It is the duty of a buyer who has received and appropriated the goods to pay a reasonable price. According to Section 2(10) 'price' means the money consideration for the sale of goods. If the price is not fixed, the contract is void ab initio.

Section 9 lays down how the price may be fixed in a contract of sale

a) It can be fixed by the contract itself; or

b) It can be fixed in a manner provided by the contract, such as appointment of a valuer; or

c) It can be determined by the course of dealings between the parties; or

d) If the price is not capable of being fixed in any of the ways

mentioned ways, the buyer is bound to pay reasonable price. What is a reasonable price is a question of fact dependent on the circumstances of each particular case. It is not necessary that reasonable price should be equal to the market price.

Section 10 makes it clear that if the third party appointed under the agreement to fix the price cannot or does not make such valuation, then the agreement to sell goods will become void. If the third party is prevented in his valuation due to the buyer or the seller, the party not at fault can file a suit for damages against the party in fault.

5) Essential elements of a valid contract : All the essentials of a valid contract must be present. viz.,competent parties, free consent, legal object and so on. The transfer of possession and ownership under the Act has to be voluntary and not be tainted with fraud or duress.Time: Any stipulation with respect to time is not deemed to be of essence to a contract of sale unless adi?erent intention appears from the terms of the contract.

SALE & AGREEMENT TO SELL

A contract of sale is a generic term and includes both an actual sale and an agreement to sell provides that if the property in goods is transferred from the seller to the buyer under a contract, the contract is called a sale. Where the transfer of the property in the goods will take place at a future time or is subject to some condition which has to be fulfilled, the contract is called an agreement to sell. Such an agreement to sell becomes a sale when the prescribed time lapses or the conditions are fulfilled.

Basis of Distinction	Sale	Agreement to Sell
Transfer of property	The property in the goods sold passes to the buyer at the time of contract. It passes immediately.	The property passes when it becomes sale on the expiry of prescribed time or the fulfilmentof certain condi tions. It takes place at a future time or subject to

		fulfilment of conditions.
Conveyance of property	It creates a right to enjoy the goods against the whole world including the seller.	It creates a right in per sonam -right against the seller
Transfer of risk	The transfer of risk takes place immediately. It is related to ownership and when ownership is transferred, the risk also passes to the person. If there is loss of goods, it will fall on the buyer even though the goods maybe in the possession of the seller.	There is no transfer of risk of loss of goods as owner shipis not transferred. The loss will be borne by the seller even though the goods are in possession of the buyer.
Right of seller in case of breach	Since the property has passed to the buyer, the seller can sue the buyer for price of the goods.	The seller can only sue for damages, unless the price was payable at a particular date.
Right of buyer in case of breach	He can sue the seller for damages. He can also sue the third party who bought those goods for the goods.	He can sue the seller for damages, unless the price payable at a particular date.
Insolvency of seller in possession of goods	He can claim the goods from the Oficial assignee or Receiver.	He cannot claim the goods but only a rateable dividend for the money paid.
Insolvency of buyer before paying the price	The seller has to deliver the goods tothe Official assignee except where he has a lien over the property.	The seller can refuse to deliver the goods to the Offcial Assignee or Receiver

The question of paying sales tax arises only in case of a completed sale and not where there is only agreement to sell.

SALE & HIRE PURCHASE AGREEMENT

A Hire purchase agreement is an agreement for hire of goods where the person who hires the goods has an option to purchase the goods at the end. The possession of the goods is delivered to such a hirer and he has to pay via instalments. The property in the goods passes to the hirer on the payment of the last instalments.

The Hire purchase agreements are treated as bailment and the parties have the same rights as a bailor and bailee. The hirer has a right to terminate the agreement at any time before the property passes. The test whether an agreement is sale or hire purchase was given in the case of Lee vs. Butler [1893 2 QB 318] - If a person taking the goods has no option to terminate the agreement, is a contract of sale irrespective of where the price is paid in instalments.

Essentials of a Contract of sales of Goods

"A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price." [Sec. (4) 1]. Important features of a contract of sale

1) **Two Parties**: The first essential is that there must be two distinct parties to a contract of sale, viz, a buyer and a seller, as a person cannot buy his own goods. However, there may be a contract of sale between one part-owner and another part-owner [Section 4(1)]. A partner may, therefore, buy the goods from the firm in which he is a partner and vice-versa.

2) **Mutual Consent**: Just the presence of two parties is not sufficient. The parties must agree on the transfer of property.

3) **Transfer of Property**: What a contract of sale stipulates is the transfer of property i.e. the ownership of the goods and not the possession of the goods.

4) **Goods**: Goods means every kind of movable property other than actionable claims and money. But it includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale. [Sec. 2(7)]. Since the price of the goods is expressed in terms of the money, money itself cannot be bought, and hence, money is not considered as goods.

5) **Price**: Under a contract of sale, property in the goods is transferred to the buyer for a price. Price is the money consideration for the goods.

(6) **Varied requirement as to delivery and payment**: The contract may provide for the immediate delivery of goods or immediate payment of the price or both,

7) **Requires no formalities**: (Sec.5) The sale of goods act does not provide for a valid contract; mere offer and acceptance thereof forms a contract; it can be made either of the two and accepted by the other. Neither the payment nor delivery is necessary at the point of making the contract. It can either be verbal or in writing or both or understood through the conduct of parties involved.

8) **Absolute or Conditional**: An absolute contract of sale is technically called a 'sale'. Thus "where under a contract of sale the property in the goods is transferred from the seller to the buyer, the contract is called a sale" [Sec 4 (3)]. Thus a contract of sale is a generic term including 'Sale' as well as 'an agreement to sell.'

Express and Implied Conditions / Warranties in a contract of a Sale

Conditions and warranties may be express or implied.

Express conditions and warranties are which, are expressly provided in the contract. Implied conditions and warranties are those which are implied by law or custom; these shall prevail in a contract of sale unless the parties agree to the contrary.

i) **Condition as to title**: In every contract of sale, unless the circumstances of the contract are such as to show a different intention, there is an implied condition on the part of the seller, that :

   a. In case of a sale, he has a right to sell the goods, and

   b. In case of an agreement to sell, he will have a right to sell the goods at the time when the property is to pass.

   The words 'right to sell' contemplate not only that the seller has the title to what he purports to sell, but also that the seller has the right

to pass the property. If the seller's title turns out to be defective, the buyer may reject the goods.

ii) **Condition as to Description** : In a contract of sale by description, there is an implied condition that the goods shall correspond with the description. The term ' sale by description' includes the followingsituation ;

a. Where the buyer has not seen the goods and buys them relying on the description given by the seller.

b. Where the buyer has seen the goods but he relies not on what he has seen but what was stated to him and the deviation of the goods rom the description is not apparent.

c. Packing of goods may sometimes be a part of the description. Where the goods do not conform to be method of packing described (by the buyer or the seller) in the contract, the buyer can reject the goods.

iii) **Condition as to Quality or Fitness** : Where the buyer, expressly or by implication, makes known the seller the particular purpose for which goods are required, so as to show that the buyer relies on the seller's skill or judgment and the goods are of a description which it is in the course of the seller's business to supply (whether or not as the manufacturer of producer), there is an implied condition that the goods shall be reasonably fit for such purpose. In other words, this condition of fitness shall apply, if:

a. The buyer makes known to the seller the particular purpose for which the goods are required,

b. The buyer relies on the seller's skill or judgment,

c. The goods are of a description which he sellers ordinarily supplies in the course of his business, and

d. The goods supplied are not reasonably fit for the buyer's purpose.

iv) **Condition as to Merchantability** : Where the goods are bought by description from a seller, who deals in goods of that description (whether or not as the manufacturer or producer) there is an implied condition that the goods shall be of merchantable quality.

Merchantable quality ordinarily means that the goods should be such as would be commercially saleable under the description by which they are known in the market at their full value.

v) **Condition as to Wholesomeness** : In case of sale of eatable provisions and foodstuff, there is another implied condition that the goods shall be wholesome. Thus, the provisions or foodstuff must not only correspond to their description, but must also be merchantable and wholesome. By 'wholesomeness' it means that goods must be for human consumption.

vi) **Condition Implied by Custom or Trade Usage:** An implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of trade. In certain sale contracts, the purpose for which the goods are purchased may be implied from the conduct of the parties or from the nature or description of the goods. In such cases, the parties enter into the contract with reference to those known usage. For instance, if a person buys a perambulator or a medicine the purpose for which it is purchased is implied from the thing itself; the buyer need not disclose the purpose to the seller.

vii) **Conditions in a Sale by Sample** : A contract of sale is a contract for sale by sample where there is a term in the contract, express or implied to that effect. Usually, a sale by sample is implied when a sample is shown and the parties intend that the goods should be of he kind and quality as the sample is.

viii) **Conditions in a sale by Sample as well as by Description**: A vast majority of cases where samples are shown, are sales by sample as well as by description. In a contract for sale by sample as well as by description, the goods supplied must correspond both with the sample as well as with the description.

IMPLIED CONDITIONS

Whether any express condition is made or not law presumes certain standards which are to be ensured by the seller before selling the any product .These presumptions as to nature, quality, and rightful ownership of the product are termed as implied conditions. The implied conditions in sale of goods are laid down in sections 14 to 17.

1) CONDITION AS TO TITLE

It is presumed in law that in the case of sale, the seller has the right to sell the Goods, and in the case of an agreement to sell the, the seller will have the right to sell the goods at the time of sale. In case a seller sells without the right to sell them, the buyer has the right to repudiate the contract. The term "right to sell" infers that the seller should have a valid title to the Goods. According to section 14 of the Act, In a contract of sale, unless the circumstances of the contract are such as to show a different attention, there is an implied condition on the part of the seller that-

(a) in the case of a sale, the seller has the right to sell.

(b) in the case of an agreement to sell the seller will have a right to sell at the time of sale.

In Rowland v. Divall, {1923}2K.B.500, B bought a second hand car from S a car dealer. After few months the car was taken away by the police as it was a stolen one. The court observed that it was a breach of condition as to title as S had no right to sell the car. It was held that B could recover full price from S. In Niblett v. Confectioners Material Co

[.1921] 3 KB 387,B bought 3000 tins of condensed milk from S. Out of these 1000 tins were labeled as Nissly Brand.N, another manufacturer of the milk under the brand name of Nestle, claimed that this was an infringement of his trademark. Consequently B had to remove all the labels from the tins and had to sell them at loss. The court held that the seller had breached the implied condition that he had a right to sell.

When a person sells the goods by infringing the copyright or trademark of the others, he is considered as not having the right to sell the goods.

Where a seller having no title to sell the goods acquires a valid title to the goods after the sale, but before the buyer seeks to terminate the contract, the implied condition as to title is considered to be complied with.

B buys a stolen car from S without knowing this fact .By the time B came to know about it S had compensated the true owner and acquired a legal ownership of the car. Now B cannot terminate the contract on the ground of breach of implied condition.

In Butterworth V. Kingsway Motors 1954 1 W.L.R.1286. Where a seller having no title to the goods at the time of the sale, subsequently acquires a title, that title feeds the ,that title feeds the defective titles of both the original buyer and the subsequent buyer.

2. SALE BY DESCRIPTION

"If you contract to sell peas, you cannot oblige a party to take beans." This is the rule laid down in section 15, where there is a contract for the sale of goods by description, there is an implied condition that the goods shall correspond with the description. In Bowes v. Shand, 1877 App.Cas.455, it was held that if the description of the article tendered is different in any respect, it is not he article bargained for and the other party is not bound to take it. Goods are sold by description when they are described in the contract, as farm wheat, Australian Apple, Indian silk etc and the buyer contracts in reliance

on that description. In Shepherd v. Kane (1821)5b&Ald.240, A ship was contracted to be sold as "copper fastened vessel" to be taken with all faults, without any allowance for any defects whatsoever. The ship turned to be partially Copper fastened .The court held that that the buyer was entitled to reject the goods.

When a descriptive word or phrase is used in a contract of sale to describe the product it creates an implied condition that the goods will correspond to the description. For example a sale of Seedless Grapes, signifies that the fruit will have no seeds. If it turns that the fruit is with seeds the buyer can reject the goods.

Sale of Goods by description may include the following situations

(1) Where the buyer has not seen the goods and relies on their description given by the seller.

In Varley v. Whipp,1900Q.B.513,W bought a reaping machine which he had never seen V the seller described " to have been new the previous year and used to cut only 50 to 60 acres" .W found the machine to be extremely old .It was held that W could return the machine as it did not answer to the description.

(2). Where the buyer had seen the goods but relies not on what he had seen but on what was stated to him by the seller.

In Nicholson & Vennv.Smith Marriot,(1947) 177 L.T.189, in an auction sale of a set of Napkins and table clothes, these were described as dating from the seventh century; the buyer bought the set after seeing it. Subsequently it was found that the set was not of the seventh century but of the eighteenth century, it was held that he could reject the goods.

(3). Packing of goods may sometimes be part of the description.

In Moore &Co v. Landauver &Co, (1921),2K.B. 519, M sold to L 300 TINS OF Australian Apple packed in cases containing 30 tins.M

tendered a substantial portion in case containing 24 tins. It was held that l could reject all the tins as the goods were not packed according to the description given in the contract as the method in which the fruit was packed was an essential part of the description.

(4) Sale by description as well as by sample.

Section 15 further provides that if the sale is by sample as well as by description then it is not sufficient that it corresponds to the description but it should also correspond to the sample.

In Wallis v. Pratt, (1911) A.C .394, in a contract for the sale of a quantity of the sale of seed described as "common English Sainfoin", the seed supplied was of a different kind, though the defect was not discoverable except by sowing the defect also existed in the sample. Held the buyer was entitled to recover damages for the breach of contract.

3. CONDITION AS TO QUALITY OR FITNESS

Ordinarily there is no implied condition that the goods supplied by the seller should be fit for the particular purpose of the buyer. The rule Caveat emptor applies instead It means that while buying it is the responsibility of the buyer to ensure that the goods corresponds to the particular purpose he want to meet. However in the following situation the responsibility of the fitness as to Goods falls on the seller.

(a) the buyer make known to the seller the particular purpose for which he requires goods.,

(b) The buyer and seller relies on the skill and judgment of the buyer.

(c) The sellers business is to supply such goods whether he is the manufacturer or producer or not.

Firstly the particular purpose for which goods are required must be known to the seller The purpose may be made known explicitly or by implication

If the goods can be used for many purposes, the buyer should make known the specific purpose to the seller; otherwise the condition as to fitness would not apply.

In Re Andrew Yule &Co, AIR 1932Calcutta879, a buyer ordered for Hessian cloth which is generally used for packing purposes the cloth was supplied accordingly, on receiving the cloth, the buyer found that the cloth was not suitable for packing food products as it had unusual smell He wanted to reject the cloth. The court observed that the buyer had no right to reject the cloth because although it was not fit for the specific purpose, it was fit for the purpose of packing otherwise for which it was commonly used. There was no breach of condition of fitness in this case. In this case had the buyer have informed to the seller that he needs the cloth for the packing of food products, situation would have been different.

It is not necessary that the purpose should be expressed in words only. If the goods could only be used for one purpose only, it is implied that the seller had knowledge about the purpose for which the buyer need the goods.

In Priest v Last (1903)2K.B.148,B went to S a chemist and demanded a hot water bottle from him, S gave a bottle to him telling that it was meant for hot water, but not boiling water. after few days while using the bottle B's wife got injured as the bottle burst out, it was found that the bottle was not fit to be used as hot water bottle. The court held that the buyer's purpose was clear when he demanded a bottle for hot water bottle, thus the implied condition as to fitness is not met in this case.

Secondly, the buyer must have relied upon the skill and judgment of the seller. B asked S, he need a car for touring purpose, S supplies a car which is not fit for touring. A breach of condition has been committed here.

However mere mention of a particular trade name by the buyer doesnot mean that he has ordered for the product of that trade name only. He may still rely upon the skill and judgment of the seller.

Thirdly, the seller should be a dealer of the kind of products transacted.

4. CONDITION AS TO MERCHANTABILITY

Section 16 (2)-Where goods are bought by description from a seller who deals in goods of that description whether he is not the producer or manufacturer or not, there is an implied condition that the goods shall be of merchantable quality

The above provision reveals that the condition of merchantability is applicable when,

a) The goods are sold by description

b) The seller deals with such goods

Thus when Mohan a blacksmith sells to Das his old car, no implied condition as to merchantability applies.

Merchantable means that the goods must be fit for the ordinary purpose for which such goods are used. For example, when shoes are sold, merchantability requires that the shoes have their heals attached well enough, that they will not break of under the normal use.

In Jones v. Just, 1868LR 3 QB 197, B&Co a firm of merchants contracted to buy from S some bales of Manila Hemp. This was to arrive from Singapore. The hemp arrived wetted with sea water. It was so damaged that it was not possible to sell it as Manila hemp in the market. The court held that the hemp was not of merchantable quality and it was entitled to be rejected.

But where the buyer examines the goods and the defects are such which can be revealed by ordinary examination, the condition of merchantability does not apply to the extent of such defects.

Where the product has some latent defects which cannot be revealed by ordinary examination, the condition of merchantability would apply when even if the buyer has examined the goods.

In Thornet v. Beers, (1919) 1 KB 486, B wanted to purchase some glue. The glue was stored in the seller's warehouse in barrels. B was given every facility to open the barrels and inspect them but B did not open the barrels. Liter on the glue was found to have defects which B could have noted if he had opened the Barrels. The court held that there is no breach of implied condition as to merchantability in this case and B was not entitled to any relief.

In Grant v. Australian Knitting Mills AIR1936PC34, B bought underwear from S, B examined it while purchasing .Later on it turned out to be harmful for his skin because of the presence of hidden sulphites in the underwear which could not have been revealed by ordinary examination. The court held that the implied condition of merchantability is applicable in this case.

Now what amounts to an examination is a question of fact in each case. In Thornet's case the buyer had the product before him to examine but he chose not to examine it. Here as against the seller the examination is deemed to be made by the buyer.

Packing of goods is an equally important consideration in judging their merchantability.

In Morreli v Fitch &gibbons (1928)2K.B.636, M asked for a bottle of Stones Ginger Wine at S's shop. Which was licensed for the sale of wines.while M was drawing the cork, the bottle broke and M was injured. Held the sale was by description and M was entitled to recover damages as the bottle was not of merchantable quality.

5. CONDITION AS TO WHOLESOMENESS

In the case of food products the condition of fitness or merchantability requires that the goods should be wholesome, that is it should be fit for

consumption. In Chapronier v. Mason,(1905)21 TLR633, C brought a Bun from a baker's shop .The bun contained a stone which broke of C's teeth. The court held that the seller was liable to pay damages as he breached the condition of wholesomeness.

6. CONDITION IMPLIED BY CUSTOM

An implied condition as to quality or fitness for a particular may be annexed by the usage of trade. Section 16(3), there are instances where the purpose of purchasing goods may be ascertained from the conduct of parties to the sale. Or from the nature of description of the thing purchased. For, example if a water bottle is purchased the purpose for which it is bought is implied in it; in that case the buyer need not tell the seller the purpose for which he buys it.

In Dr.Baretto v. T.R.Price, AIR 1939 Nag 19, A bought a set of false teeth from a dentist. The set did not fit into A's mouth. Held A could reject the set as the purpose for which anybody would buy it was implicitly known to the seller, here the dentist.

In Priest v Last (1903)2K.B.148,P asked for a hot water bottle to S ,retail chemist ,he was supplied one which burst after few days use and injured P's wife. The court held that S was liable for the breach of implied condition because P had made known to the Chemist the purpose for which he buys the goods.

7. SALE BY SAMPLE

A contract of sale by sample is a contract for sale by sample where there is a term express or implied in the contract, to that effect. (Section 17).In the case of contract of sale by sample, there is an implied condition.

1. That the bulk shall correspond to the sample in quality.

2. That the buyer shall have a reasonable opportunity of comparing the bulk with the sample.

3. That the goods shall be free from any defect, rendering them unmerchantable.The defect should not however be apparent on a reasonable examination of the sample.

In the case of patent defect there is no breach of implied condition as to merchantability.

In Mody v. Gregson, L.R.4E.X.49, in a contract for the sale of brandy, by sample brandy colored with a dye was supplied. The court held that the buyer was not bound to the contract even though the goods supplied were equal to the sample. As the defects were not apparent on the reasonable examination of the sample.

In E&SRuben Ltd v.Fair Bros, 1949 1K.B.254.A agreed to buy some rubber material from B. The sample of the rubber was shown to A .On receiving the rubber material, A found that the measurement of the rubber material was different from that of the sample. The court held that measurement of the rubber material was part of its quality. It was held that the goods did not correspond to the sample.

In Lorymer V. Smith, (1822) 1 B&C1., Two parcels of wheat were sold by sample. The buyer went to examine the wheat a week later. One parcel was shown to him but the seller refused to show the other parcel as it was not there. In this case the buyer was not given reasonable opportunity to test the bulk with the sample. The court held that the buyer was entitled to reject the contract of sale.

EXCLUSION OF IMPLIED CONDITIONS

Section 62 of the sale of Goods Act, reads as-"Where any right, duty or liability would arise under a contract of sale by implication of law, it may be negatived or varied by express agreement or by the course dealing by the parties or by usage, if the usage is such as to bind both the parties to the contract"

The rule of law is that in a contract of sale the parties are free to make any bargain they feel like. The seller can exclude his liability by expressly providing in a contract of sale that he will not be liable for the breach of any condition. Similarly the buyer can waive any condition in a contract.However, the seller cannot exclude his liability to perform the Fundamental aspects of the contract. As quoted by Lord Harbinger ,"if a seller contract to sell a horse, and expressly excluded all conditions and warranties, express or implied, could he escape liability ,if he delivered a pig? He would be met by the simple and sufficient answer that he had failed the one fundamental obligation.

S sold a horse to B with the stipulation, that there is no condition or warranty as to the fitness of the horse. The horse dies on the third day after the sale. In this case the seller is not liable to compensate the buyer.

- **Remedy for Breach of Condition :** On breach of a condition by the seller, the buyer's remedy is that he can reject the transaction and return the goods to the seller On the breach of a warranty by the seller the buyer is provided with a remedy to claim damages suffered because of the goods bought under the transaction, but he cannot return the goods. When certain condition is not fulfilled, the buyer may not put an end to the contract by rejecting the goods and recover damages from the seller for breach of warranty. But once the buyer exercises his option to treat a breach of condition as a breach of warranty, he cannot afterwards insist on the fulfillment of the condition. This rule is laid down in Section 13 (1) of the Act.

Where the contract of sale is not severable and the buyer has accepted the goods or any part of the goods the breach of any condition by the seller can only be treated as a breach of a warranty, unless there is a term of the contract, express or implied to the contrary. This rule is laid down in Section 13(2) of the Sale Goods Act.

1) Implied Warranties : A condition becomes a warranty when -

a) the buyer waives the conditions or opts to treat the breach of the condition as a breach of warranty ; or

b) The buyer accepts the goods or a part thereof, or is not in a position to reject the goods.

i.) Implied Warranty of Quiet Possession -- In every contract of sale, unless there is a contrary intention, there is implied warranties that the buyer's shall have and enjoy quiet possession of the goods. If the buyer's right to possession and enjoyment of the goods is in any way disturbed as consequences of the seller's defective title, the buyer may sue the seller for damages for breach of this warranty.

ii.) Implied Warranty of Freedom from Encumbrances - The buyer is entitled to a further warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to buyer before or at the time when the contract is made. If the buyer is required to discharge the amount of the encumbrance it shall be a breach of this warranty and the buyer shall be entitled to damages for the same.

2.4 FORMATION OF THE CONTRACT

INTRODUCTION

- A contract may be defined as an agreement between two or more parties that is intended to be legally binding.
- The first requisite of any contract is an agreement (consisting of an offer and acceptance). At least two parties are required; one of them, the offeror, makes an offer which the other, the offeree, accepts.
- **Offer**

  An offer is an expression of willingness to contract made with the intention that it shall become binding on the offeror as soon as it is accepted by the offeree.

  A genuine offer is different from what is known as an "invitation to treat", ie where a party is merely inviting offers, which he is then free to accept or reject. The following are examples of invitations to treat:

- **Auctions**

  In an auction, the auctioneer's call for bids is an invitation to treat, a request for offers. The bids made by persons at the auction are offers, which the auctioneer can accept or reject as he chooses. Similarly, the bidder may retract his bid before it is accepted.

- **Display of Goods**

  The display of goods with a price ticket attached in a shop window or on a supermarket shelf is not an offer to sell but an invitation for customers to make an offer to buy.

- **Advertisements**

  Advertisements of goods for sale are normally interpreted as invitations to treat. However, advertisements may be construed as offers if they are unilateral, ie, open to all the world to accept (eg, offers for rewards).

- **Mere Statements of Price**

  A statement of the minimum price at which a party may be willing to sell will not amount to an offer.

- **Tenders**

  Where goods are advertised for sale by tender, the statement is not an offer, but an invitation to treat; that is, it is a request by the owner of the goods for offers to purchase them.

- **Acceptance**

  An acceptance is a final and unqualified acceptance of the terms of an offer. To make a binding contract the acceptance must exactly match the offer. The offeree must accept all the terms of the offer.

  However, in certain cases it is possible to have a binding contract without a matching offer and acceptance.

The following rules have been developed by the courts with regard to acceptance:

- **Counter Offers**

  If in his reply to an offer, the offeree introduces a new term or varies the terms of the offer, then that reply cannot amount to an acceptance. Instead, the reply is treated as a "counter offer", which the original offeror is free to accept or reject. A counter-offer also amounts to a rejection of the original offer which cannot then be subsequently accepted.

  A counter-offer should be distinguished from a mere request for information.

  If A makes an offer on his standard document and B accepts on on a document containing his conflicting standard terms, a contract will be made on B's terms if A acts upon B's communication, eg by delivering goods. This situation is known as the "battle of the forms".

- **Conditional Acceptance**

  If the offeree puts a condition in the acceptance, then it will not be binding.

- **Tenders**

  A tender is an offer, the acceptance of which leads to the formation of a contract. However, difficulties arise where tenders are invited for the periodical supply of goods:

  Where X advertises for offers to supply a specified quantity of goods, to be supplied during a specified time, and Y offers to supply, acceptance of Y's tender creates a contract, under which Y is bound to supply the goods and the buyer X is bound to accept them and pay for them.

  Where X advertises for offers to supply goods up to a stated maximum, during a certain period, the goods to be supplied as and when demanded, acceptance by X of a tender received from Y does not create a contract.

Instead, X's acceptance converts Y's tender into a standing offer to supply the goods up to the stated maximum at the stated price as and when requested to do so by X. The standing offer is accepted each time X places an order, so that there are a series of separate contracts for the supply of goods.

- **Communication of Acceptance**

  The general rule is that an acceptance must be communicated to the offeror. Until and unless the acceptance is so communicated, no contract comes into existence:

  The acceptance must be communicated by the offeree or someone authorised by the offeree. If someone accepts on behalf of the offeree, without authorisation, this will not be a valid acceptance:

  The offerer cannot impose a contract on the offeree against his wishes by deeming that his silence should amount to an acceptance:

  Where an instantaneous method of communication is used, eg telex, it will take effect when and where it is received.

- **Exceptions to the Communication Rule**

  In unilateral contracts the normal rule for communication of acceptance to the offeror does not apply. Carrying out the stipulated task is enough to constitute acceptance of the offer.

  The offeror may expressly or impliedly waive the need for communication of acceptance by the offeree, eg, where goods are dispatched in response to an offer to buy.

  The Postal Rule - Where acceptance by post has been requested or where it is an appropriate and reasonable means of communication between the parties, then acceptance is complete as soon as the letter of acceptance is posted, even if the letter is delayed, destroyed or lost in the post so that it never reaches the offeror.

The postal rule applies to communications of acceptance by cable, including telegram, but not to instantaneous modes such as telephone, telex and fax. The postal rule will not apply:

Where the letter of acceptance has not been properly posted, as in Re London and Northern Bank (1900), where the letter of acceptance was handed to a postman only authorised to deliver mail and not to collect it.

Where the letter is not properly addressed. There is no authority on this point.

. Where the express terms of the offer exclude the postal rule, ie if the offer specifies that the acceptance must reach the offeror. In Holwell Securities v Hughes (1974, below), the postal rule was held not to apply where the offer was to be accepted by "notice in writing". Actual communication was required.

It was said in Holwell Securities that the rule would not be applied where it would produce a "manifest inconvenience or absurdity".

- **Revocation of posted acceptance**

Can an offeree withdraw his acceptance, after it has been posted, by a later communication, which reaches the offeror before the acceptance? There is no clear authority in English law. The Scottish case of Dunmore v Alexander (1830) appears to permit such a revocation but it is an unclear decision. A strict application of the postal rule would not permit such withdrawal. This view is supported by decisions in: New Zealand in Wenkheim v Arndt (1873) and South Africa in A-Z Bazaars v Ministry of Agriculture (1974). However, such an approach is regarded as inflexible.

- **Method of Acceptance**

The offer may specify that acceptance must reach the offeror in which case actual communication will be required.

If a method is prescribed without it being made clear that no other method will suffice then it seems that an equally advantageous method would suffice.

- **Knowledge of the Offer**

  An offeree may perform the act that constitutes acceptance of an offer, with knowledge of that offer, but for a motive other than accepting the offer. The question that then arises is whether his act amounts to a valid acceptance. The position seems to be that:

  (a) An acceptance which is wholly motivated by factors other than the existence of the offer has no effect.

  R v Clarke (1927) 40 CLR 227

  (b) Where, however, the existence of the offer plays some part, however small, in inducing a person to do the required act, there is a valid acceptance of the offer.

  Recommended reading: Williams v Carwardine (1833) 5 Car & P 566.

  Cross-Offers

  A writes to B offering to sell certain property at a stated price. B writes to A offering to buy the same property at the same price. The letters cross in the post. Is there (a) an offer and acceptance, (b) a contract? This problem was discussed, obiter, by the Court in Tinn v Hoffman (1873) 29 LT 271. Five judges said that cross-offers do not make a binding contract. One judge said they do.

- **Termination of the Offer**

- **Acceptance**

  Once an offer has been accepted, a binding contract is made and the offer ends.

- **Rejection**

  If the offeree rejects the offer that is the end of it.

- **Revocation**

  The offer may be revoked by the offeror at any time until it is accepted. However, the revocation of the offer must be communicated to the offeree(s). Unless and until the revocation is so communicated, it is ineffective.

  The revocation need not be communicated by the offeror personally, it is sufficient if it is done through a reliable third party.

  Recommended reading: Dickinson v Dodds (1876) 2 ChD 463.

  Where an offer is made to the whole world, it appears that it may be revoked by taking reasonable steps.

  Recommended reading: Shuey v United States [1875] 92 US 73.

  Once the offeree has commenced performance of a unilateral offer, the offeror may not revoke the offer.

- **Counter Offer**

  See above for Hyde v Wrench (1840).

- **Lapse of Time**

  Where an offer is stated to be open for a specific length of time, then the offer automatically terminates when that time limit expires. Where there is no express time limit, an offer is normally open only for a reasonable time.

  Recommended reading: Ramsgate Victoria Hotel v Montefiore (1866) LR 1 Ex 109.

- **Failure of a Condition**

  An offer may be made subject to conditions. Such a condition may be stated expressly by the offeror or implied by the courts from the circumstances. If the condition is not satisfied the offer is not capable of being accepted.

- **Death**

The offeree cannot accept an offer after notice of the offeror's death. However, if the offeree does not know of the offeror's death, and there is no personal element involved, then he may accept the offer.

In short, there are five basic requirements that need to be satisfied in order to make a contract: ? An agreement between the parties (which is usually shown by the fact that one has made an offer and the other has accepted it).

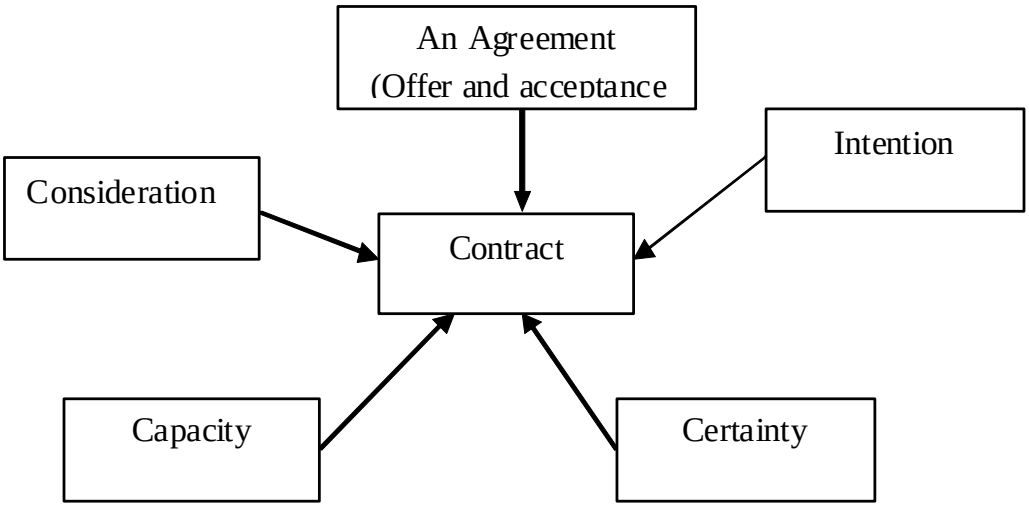
An intention to be legally bound by that agreement (often called intent to create legal relations).

Certainty as to the terms of the agreement

Capacity to contract.

Consideration provided by each of the parties - put simply, this means that there must be some kind of exchange between the parties. If I say I will give you my car, and you simply agree to have it, I have voluntarily made you a promise (often called a gratuitous promise), which you cannot enforce in law if I change my mind. If, however, I promise to hand over my car and you promise to pay me a sum of money in return, we have each provided consideration.

In addition, in some cases, the parties must comply with certain formalities. Remember that, with a few exceptions, it is not necessary for a contract to be in writing - a contract is an agreement, not a piece of paper. In this part of the book we will consider these different requirements for the creation of a contract.



- **Elements of Formation of Contract**

  Two main elements:

  1) Agreement

  a) Offer

  b) Acceptance

  2) Consideration

  Other elements:

  1) Intention to create legal relations

  2) Capacity

  3) Formalities

- **Agreement - Offer**

  Definition - Statement by one person to another person, evincing his/ her willingness to enter into contractual relations with that person on certain terms.

Distinguish offer from an "Invitation to Treat" - E.g. auctions, tenders - Test of intention: Did the party making the statement intend that an affirmative response would give rise to an agreement or simply result in further negotiation? If YES, then you have a legal offer. If NO, then there is no offer which may be accepted which subsequently gives rise to legal obligations. o

- **Scope**

  An single offer may be made to a distinct person or people, or the world at large (Carbolic Smoke Ball case). o

- **Central requirement** -

  The statement alleged to be an offer must indicate a willingness to be bound without further negotiations as to the terms of the proposed contract.

- **Termination** -

  Revocation; 2) Rejection; 3) Lapse of time; 4) Death of the offeree; and 5) Failure of condition precedent.

- **Agreement - Acceptance**

  Definition - Unequivocal statement (oral, written or by conduct) by the offeree agreeing to the offeror's offer.

  Requirements: 1) Must exactly correspond with the offer (otherwise will be deemed a counter-offer).

  Must be unequivocal (hence an offeree must have knowledge of an offer before accepting it).

  Must be communicated by the offeree to the offeror (onus of communication is on the offeree). An agreement is concluded upon the communication being received by the offeror.

Note that there are several exceptions to the requirement of communication which may apply. E.g. waiver by offeror.

- **Consideration**

  Definition under the "Bargain Theory of Consideration" (Adopted in Australia by Australian Woolen Mills case) - An act/forbearance of the one party on the promise thereof is the price for which the promise is bought.

- **Requirements**:

  Must be a connection between the consideration and the promise which it is said to support.

. Must move from the promisee, but not necessarily to the promisor (Coulls v Bagot's Executor and Trustee).

Must be sufficient but need not be adequate (Chappell & Co v Nestle & Co Ltd)- Illegal consideration is not sufficient, and excessively inadequate consideration may not be sufficient.

Past consideration is not good consideration (Lampleigh v Brathwait).

- **Exceptions to the requirement of consideration**:

  Promises under seal (deeds).

  Doctrine of Promissory estoppel - Where it would be inequitable for the promisor not to be held to the promise.

- **Rationale for the requirement of consideration?**: 1) Evidentiary and cautionary function - Corroborates the seriousness of intent to be bound.

  Maintains equity/fairness - Contracts ought to be of quid pro quo nature.

  Identifies the measure of relief in circumstances of breach.

  Distinguishes equitable remedies applicable in circumstances of contract and circumstances of gift - Different equitable remedies become available.

- **Intention to create legal relations**
- **Concept**-

  For a contract to exist the parties to an agreement must intend to create legal relations.

- **Role of consideration** -

  Consideration is often evidence of intention.

- **Presumptions of intent**

  Certain relationships between persons carry with them a rebuttable presumption. E.g. familial relationships are presumed not to give rise to an intention to create legal relations, while the opposite is true for commercial relations.

- **Capacity**

  Concept - For a contract to exist the parties must have contractual capacity. There are certain persons and classes of persons that lack the capacity to enter into a contract with the consequence (normally) that resulting contracts will not be enforceable against them.

- **Rationale** :

  Protection of persons who may be vulnerable to exploitation.

- **Classes of persons**:

  Mental disorder or intoxication - A contract is voidable at the option of a party who, as a result of mental disorder or intoxication, is unable to understand the nature of the contract being made (provided that the other party knew, or ought to have known, of that person's disability).

- **Bankrupts** -

  A bankrupt person may make a contract but unprofitable contracts made prior to bankruptcy may be disclaimed by the trustee.

- **The Crown** -

  At common law proceedings could not be taken against the Crown, but legislation has removed this immunity in most cases.

  Minors -

  Generally, both the common law and statute restrict the capacity of minors to enter into contracts.

- **Companies** -

  At common law, a company only has capacity to enter into contracts permitted by its constitution.

- **Formalities**

  Concept - As a general rule contracts do not need to comply with any sort of formalities. However, nowadays many categories of contract are governed by statute. o

- **Contracts for sale of land**

  Must be in writing, otherwise are unenforceable.

- **Effect of non-compliance**

  Renders a contract unenforceable.

- **Doctrine of part-performance**

  This doctrine provides that where the plaintiff has partly carried out the contract, relying on the defendant's promise, equity may enforce the contract despite non- compliance with formalities.

- **Rationale**

Formalities requirements are generally designed to prevent fraud, but strict adherence to such requirements might themselves facilitate fraud by enabling those who entered into such contracts to deny the existence of the contract or

otherwise seek to avoid their promised obligations by relying on non-compliance as a defence to a contractual claim.

2.6 SUMMARY

Business law refers to the laws which are applied to business entities such as partnerships and corporations. These are used as reference when putting up businesses whether big or small - from sole proprietorship to corporation. Business laws specify how different business can be set up, how taxes apply to them, registrations, documentations and requirements; define different terms pertaining to business, making by-laws, and articles of organization among many others. These also provide the authoritarian schemes on how commerce should be conducted. Every country has its own regulations, laws and regulatory bodies or agencies governing the manufacturing, sales, marketing and distribution of products within the country. Laws and regulations are intentionally made for human beings and other institutions as a guide to bring order and sanity into the society. Because of this, it is likely that their application will impact upon the plans of firms; their effects on a given firm are also inevitable. Indian Contract Act embodied the simple and elementary rules relating to Sale of goods and Partnership. The developments of modern business world found the provisions contained in the Indian Contract Act inadequate to deal with the new regulations or give effect to the new principles. Subsequently the provisions relating to the Sale of Goods and Partnership contained in the Indian Contract Act were repealed respectively in the year 1930 and 1932 and new enactments namely Sale of Goods and Movables Act 1930 and Indian Partnership act 1932 were re-enacted. The law relating to sale of goods is contained in the Sale of Goods Act, 1930, which came into force on 1st July, 1930. The Act contains sixty-six Sections and extends to the whole of India except the State of Jammu and Kashmir. A few minor amendments in the Act were made by Sale of Goods (Amendment) Act, 1963. A contract of sale of goods results, like any other contract, by an offer by one party and its acceptance by the other. Thus, it is a consensual transaction. The parties to the contract

enjoy unfettered discretion to agree to any terms they like relating to delivery and payment of price, etc. The Sale of Goods Act does not seek to fetter this discretion. It simply lays down certain positive rules of general application for those cases where the parties have failed to contemplate expressly for contingencies which may interrupt the smooth performance of a contract of sale, such as the destruction pf the things sold, before it is delivered or the insolvency of the buyer, etc. The Act leaves the parties free to modify the provisions of the law by express stipulations. Section 4 (1) of Sale of Goods Act defines a contract of sale of goods as a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. There must be two distinct parties to a contract of sale, viz., a buyer and a seller, as a person cannot buy his own goods.

6.7 KEY WORDS

The Law of Sale of goods, Contract of Sale, Business Law, Offer, Auction, Tender, Revocation of Postal acceptance.

6.8 GLOSSARY

- **The Law of Sale of goods**: The law relating to sale of goods is contained in the Sale of Goods Act, 1930, came into force on 1st July, 1930. The Act contains sixty-six Sections and extends to the whole of India except the State of Jammu and Kashmir. A few minor amendments in the Act were made by Sale of Goods (Amendment) Act, 1963.

- **Contract of Sale**: a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price.

- **Business laws**: refers to the laws which are applied to business entities such as partnerships and corporations. These are used as reference when putting up businesses whether big or small - from sole proprietorship to corporation. Business laws specify how different business can be set up, how taxes apply to them, registrations, documentations and requirements; define

different terms pertaining to business, making by-laws, and articles of organization among many others.

- **Indian Contract Act, 1872**: The Act was passed by British India and is based on the principles of English Common Law. It is applicable to all the states of India except the state of Jammu and Kashmir. It determines the circumstances in which promises made by the parties to a contract shall be legally binding on them. All of us enter into a number of contracts everyday knowingly or unknowingly. Each contract creates some rights and duties on the contracting parties. Hence this legislation, Indian Contract Act of 1872, being of skeletal nature, deals with the enforcement of these rights and duties on the parties in India.

6.9 SELF ASSESSMENT QUESTIONS

1. What is the meaning of business laws ?

Ans. _____

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2. Explain different types of business laws in India?

Ans. _____

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3. Discuss the concept of Indian Contract Act?

Ans. _____

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4. What is a contract of sale of goods? Discuss the essential characteristics of a contract of sale of goods.

Ans. _____

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5. Define the term 'sale' and 'agreement to sell' and distinguish between the two. Give examples.

Ans. _____

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6. What do you understand by performance of a contract? State who can demand performance and by whom contracts must be performed?

Ans. _____

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6.10 RECOMMENDED READING

- Harvey v Facey [1893] AC 552
- Brogden v Metropolitan Railway Co. (1877) App Cas 666
- Lord Denning in Gibson v Manchester City Council [1979] above
- Hyde v Wrench (1840) 3 Beav 334.
- Percy Trentham Ltd v Archital Luxfer Ltd [1993] 1 Lloyd's Rep 25.
- Stevenson v McLean (1880) 5 QBD 346.
- Bradbury v Morgan (1862) 1 H&C 249.
- Mercantile Law by Arun Kumar.
- Indian Taxation and Corporate Law
- Jump up^ Pandia - Principles of Mercantile Law, 8th edition, by Ramkrishna R.Vyas.
- MC Kuchhal and Vivek Kuchhal :Vikas publication
- Byrne v Van Tienhoven (1880) 5 CPD 344.
- Dickinson v Dodds (1876) 2 ChD 463.
- Shuey v United States [1875] 92 US 73
- Ramsgate Victoria Hotel v Montefiore (1866) LR 1 Ex 109.

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-III**
PAPER-IV **LESSON -11**

MEANING AND CHARACTERISTICS OF A COMPANY

STRUCTURES

11.1 INTRODUCTION TO THE COMPANIES ACT, 2013 (18 OF 2013)

The Companies Bill, 2011 which was passed by the Lok Sabha on 18th Dec. 2012 and by Rajya Sabha on 8th Aug., 2013 became an Act called as "The Companies Act, 2013". The Companies Act, 2013 received the assent of President of India on 29th Aug. 2013 and came into force with effect from 30th Aug.,2013.

- The Companies Act, 2013 consists of 470 sections spread over 29 Chapters and Schedules.
- The Companies Act, 2013 repeals the previous Companies Act, 1956.
- As many as 188 Sections of the Companies Act, 1956 have been dropped in the CompaniesAct,2013.

The main changes introduced by the Companies Act. 2013

1. The concept of One Person Company (OPC) has been introduced by this Act which means a private limited company having only one person as a member.
2. Many terms and expressions which are occasionally -used in the company were not defined in the preceding company law and this void is filled by the Companies Act, 2013 in which more than 30 new definitions are included under Section 2 of the Act.
3. One of the important features of this Act is that it prescribes a uniform financial year i.e. from 1st April to 31st March for all the companies subject to certain exceptions. This would facilitate financial accounting of companies to a great extent.
4. The private companies can now have maximum of 200 members as against the maximum 50 as provided in the Companies Act, 1956. This increase would provide greater scope for operation of private companies.
5. The requirement of 'object clause' of the Memorandum of Association into three distinct classes, i.e. the main, ancillary and other objects, have been scrapped in the new Companies Act of 2013 and now only the objects for which the company is incorporated are required to be mentioned in the Memorandum of Association(MOA).
6. Where money raised from public through prospectus has not been fully utilised for the purpose and object it was raised, the un-spent money cannot be utilised for any other object unless a special resolution for this

purpose has been passed and dissenting share-holders are provided an exit-opportunity.

7. The requirement of Statement in lieu of Prospectus by private companies has been done away with. The new Act of 201.3. requires a detailed prospectus to be issued and the Companies cannot vary the terms of contract or objects referred to in the prospectus without the approval of share-holders by special resolution in the general meeting of the company.

8. The preceding Companies Act, 1956 permitted only financial institutions, public sector banks and scheduled banks to issue shelf prospectus but the Act of 2013 empowers SEBI to prescribe class/classes of companies which can file Shelf Prospectus with the Registrar (ROC).

9. The Act of 2013 requires the Companies to file return of allotment for all kinds of securities besides the securities in the form of shares and a Company may issue Global Depository Receipt (GDR) by passing a special resolution in the general meeting subject to conditions as prescribed.

10. The provisions relating to buy back of shares by companies have been fairly liberalized and now consequent to the enforcement of the Companies Act, 2013, the companies can buy back their shares even if they have defaulted in repayment of deposits or interest payable thereon, redemption of debentures or payment of dividend to shareholders etc.

11. The Non-Banking Financial Companies ('NBFC's,) will now be governed by RBI rules in the matter of acceptance of deposits and not by the provisions of Companies Act, 2013.

12. The permissible limit of 18 months for holding Annual General Meeting (AGM) from the date of its incorporation has been curtailed to nine months. Therefore, now the company shall have to hold its annual general meeting within nine months from the closure of its first financial

year, and in other case, within the period of six months from the date of closing of the financial year (Section 96 (1) Provison).

13. A significant change in the maintenance and submission of accounts of the companies is switching over to electronic media. The 2013 Act specifically provides that the books of accounts may be kept in the electronic form. (Jnder the new scheme, the company is required to prepare and file financial statement which shall include its balance sheet, profit and loss account and cash flow statement in a consolidated form. These documents are not required to be filed separately as was necessary under Section 212 of the preceding Companies Act, 1956.

14. The National Advisory Committee on Accounts Standards (NACAS) set up under the Companies Act, 1956 has been renamed by the 2015 Act as the flational Financial Reporting Authority (JYFJ?A), the reason being that the NACAS was merely an advisory body under the 1956 Act which has now been converted into a quasi judicial authority having power to exercise disciplinary control over the Chartered Accountants or C.A. firms. The 2013 Act also requires the Central Government to provide by notification not only the mandatory accounts standards (as was the case under the 1956 Act) but also the mandatory auditing standards in consultation with the National Financial Reporting Authority (NFRA).

15. A new provision relating to Corporate Social Responsibility (CS]?) has been introduced under Section 135 of the Companies Act, 2103, which provides, that every company having a specified net worth or turnover or net profit during any financial year shall constitute the Corporate Social

Responsibility Committee of its hoard of Directors to formulate policies for the activities specified in Schedule VII of the Act for social and economic welfare of the people, parucularly, those who have remained deprived or neglected so far.

16. The new Act of 2013, vide its Section 149 makes it mandatory that the prescribed class or classes of companies shall have at/east one woman Director. It also provides that atleast one Director of the hoard must have stayed in India for not less than 182 days in the previous calendar year.

17. Another significant change in the company law as regards Directors relates to mandatory provision for every listed company to have at/east 1/Y of the total number of its Directors on its Board as independent Directors. The independent Director shall be a non-executive Director, not being a promoter or key managerial personnel.

18. The maximum number of Directors that a company may have is raised from 12 to 15 under the 2013 Act. Similarly, now a person can be come Director of maximum 20 companies instead of 15 as was provided under the Companies Act, 1956. Out of these 20 companies, he canliot be the Director of more than ten public companies at a time.

19. The Companies Act, 2013 makes it mandatory for a Director who raised from his post, to forward the copy of his resignation to the Registrar of Con7panies (ROC',) within thirty days of such resignation. There was no such provision in the earlier Act of 1956.

20. The Companies Act of 2013 requires a company to hold at/east four meetings in every year and the gap between' the two consecutive meetings should not exceed 120 days. It allows the Director(s) to participate in hoard's meeting through Video-conferencing or other audio-visual mode as may be prescribed. Thus, the requirement that a company should hold its meeting quarterly as existed in the preceding Companies Act, 1956, has been changed and modified for the convenience of the companies.

21. The new Companies Act, 2013, has raised the limit of political contribution by company from 5 per cent to 7.5 per cent of the average net profit of the company during the three immediately preceding financial years.

22. In the preceding Companies Act of 1956, in the context of loan under

Section 372-A of that Act, debentures were also included but now as provided under Section 186 of the 2013 Act, the term 'loan' shall not include debentures. That apart, a company can make investment through not more than two layers of investment companies as prescribed.

23. The new Act has done away with the requirement of Central Government's approval for:

(I) giving 'loan to Directors by companies; or

(ii) for entering into any related party transactions; or

(iii) for appointment of any Director or any other person to any office of profit in the company or its subsidiary. Such approval was mandatory under the earlier Companies Act, 1956.

24. The Schedule V of the 2013 Act lays down conditions required to be fulfilled for the appointment of Managing Director/whole time Director/ Manager and the provisions of the Act in this regard shall also apply to a private company. Where the company by its special resolution decides to appoint its managerial personnel on terms and conditions set out in the said Schedule V. then in that case the approval of the Central Government shall be necessary.

25. Section 447 of the 2013 Act provides a new provision defining 'fraud' in relation to affairs of a company or any body corporate. It also provides stringent punishment br this offence. There was no definition of fraud' in the Companies Act, 1956 nor was there any specific punishment for this offence under that Act.

26 The Act of 201 3 contains a new provision which provides that where investigation against any Director, key managerial personnel or an officer of the company for having committed a fraud in the form of any assets, cash or property or in any other manner in relation to the company is reported, the Central Government may file an application to the tribunal for appropriate orders of disagreement of such assets, property or cash

and the said managerial personnel may be held personally liable for the fraud without any limitation of liability. Such investigation shall not be stopped or stayed even if the share-holders of the company have approved the winding up of the company.

27. A new provision relating to contract by One Person Company (OPC) has been incorporated under Section 193 of 2013 Act, describing the manner in which certain transactions or contracts are to be entered between OFC and its sole member. The earlier 1956 Act had no provision regarding One person Company (OFC).

28. The Companies Act, 2013 makes the submission of Auditors certificate mandatorv before the Tribunal grants sanction for compromise or arrangement. This is with a view to ensuring that the compromise or arrangement by the company is in conformity with the accounting standards prescribed by the Central Government.

29 The company Law Board having abolished, any application against oppression or mismanagement in a company has to be filed before the flat/anal Company Law Tribunal (IYCLT). The Companies Act of 2013, provides for 'class action suit' for relief from oppression and mismanagement. A specified number of members or depositors of a company may file a 'class action suit' against oppression/mismanagement in the company. However, this provision is not applicable in case of banking companies. These was no analogous provision in the preceding Companies Act, 1956

30. A new provision introduced by the Companies Act, 201 3 provides for valuation of company's assets by qualified registered valuer. The appointment of valuers is to be made by the Audit Committee or in its absence, by the 3oard of Directors of tile Company. A valuer is appointed or valuation of any property, stocks, shares, debentures, securities or goodwill or any other assets of the company.

31. The new Act of 20 13 seeks to rationalize the revival and rehabilitation of sick companies by providing that a company, which tails to repay the debt of secured creditors representing 50 per cent or more of its debt amount may also apply to the tribunal for declaring the company as sick company.

32. A new provision regarding appointment of interim administrator by the Tribunal has been inserted as Section 256 of the Companies Act, 2013.

The Tribunal shall within seven days of the receipt of petition for revival or rehabilitation of a sick company, appoint an interim administrator to convene a meeting of creditors of the company to consider whether on the basis of the particulars and documents furnished with the petition made under Section 254, a case of revival or rehabilitation is sufficiently made out and the draft scheme filed by the company justifies appointment of an interim administrator to take over management of the affairs of the company.

33. The Companies Act, 1956 contains a provision relating to Nidhi Companies which defined 'NIDHI' as company which the Central Government may by notification in the Official Gazette declare to be a Nidhi without specifying specific activities of a Nidhi Company. This definition has been enlarged by Section 406 of the Companies Act, 2013 which specifies the activities of Nidhi as cultivating the habit of thift and savings amongst the members, receiving deposits from, and lending to, 11s members only, for their mutual benefits as per the rules prescribed by the Central Government in this behalf. The new Act does not require the Central Government to notify companies as Nidhi Companies.

34. Making a departure from the provisions relating to compounding of certain offences as provided under Section 621A of the Companies Act, 1956, the Companies Act of 2013 now provides that only offences punishable with fine are compoundable by aggrieved parties mutually

under Section 441 (of the 2013 Act) and offence which is punishable with fine or imprisonment or with both can be compounded with the permission of the Special Court.

35. A new provision in the form of Section 442 is inserted in the Act of 2013 for setting up mediation and conciliation panel of experts to mediate at the request of parties to the proceedings before the Central Government i.e. Tribunal or the Appellate Tribunal.

36. Frior to the enactment of the Companies Act, 2103, the cases of insider trading were dealt with under the SEI3I Act, 1992 as there was no provision in this regard in the Companies Act, 1956. However, with a view to prohibit insider trading of securities by Directors or key managerial personnel of companies, a new provision in the form of Section 195 has been inserted in the Companies Act, 2013 where in the expressions 'insider trading' and 'price-sensitive information' have also been well defined.

Thus, the section prohibits the Directors or key managerial personnel of the company from dealing in securities of the company or counselling procuring or communicating directly or indirectly about non public price sensitive information to any person

37. In the procedure set out for the voluntary winding of a company some new requirements have been prescribed under Section 310 of the Companies Act, 2013. Firstly, the Company Liquidator for a voluntarily winding up company shall be appointed from the panel prepared by the Central Government Secondly the Company Liquidator so appointed shall (throughout the term of his appointment) file a declaration in the prescribed form disclosing conflict of interest or lack of independence in respect of his appointment, if any, with the company or the creditors.

The provision of appointment of a Company Liquidator by nomination by the company or the creditors, as existed in the earlier Companies Act, 1956 has been done away with under the Companies Act of 2013.

38. As regards disclaimer of onerous property of a company which is being wound up, by the Company Liquidator, the powers and functions which were hitherto exercisable by the Court under the Companies Act, 1956 are now transferred to the Tribunal under Section 333 of the new Companies Act, 2013.

39. A new provision has been inserted as Section 221 of the Companies Act, 2013 which empowers the Tribunal to freeze the assets of a company when a reference regarding inquiry or investigation is made in connection with the affairs of a company by the Central Government. If the company ransferred, removes or disposes of funds, assets or properties in contravention of the freezing order of the Tribunal, the company and its officers in default shall be liable to stringent punishment as provided under Section 221 (2) of the Act 2013.

40. Consequent to new information technology an internet as a medium of commercial transactions, a new provision giving statutory recognition to filing of applications, documents, inspection, production and evidence of documents kept by Registrar as contained in Sections 398 and 399 of the Companies Act, 2013, has been inserted in Section 400 of the Act, This section accepts electronic form to be the exclusive, alternative or in addition to physical form, for the aforesaid purposes.

41. The Companies Act of 2013 provides a new provision regarding dormant company (Le. Section 455 of the Act). A company which is formed and registered under the Act for some future product or to hold as asset or intellectual property or has no significant accounting transaction, may apply to the Registrar (ROC) in the prescribed manner for obtaining a status of dormant company'. The Registrar shall maintain a register of Dormant companies.

42. Although the Companies Act, 1956 stands repealed by Section 465 of the Companies Act, 2103, but as provided in this section, the provisions of Part IX-A of the Companies Act, 1956 relating to Producer Companies

shall be applicable mutatis mutandis to a Producer Company in the manner as if the Companies Act, 1956 has not been repealed, until Special Act is enacted for the producer companies. Thus, the entire Companies Act, 1956 excepting its Part IXA (consisting of Sections 581-A to 581-ZT) has been repealed by the Act of 2013

11.2 OBJECTIVES

After going through this lesson, you should be able to:

- Understand the Companies Act ,2013
- Define a company
- Explain its important features.

11.3 MEANING OF COMPANY

The word 'company' has no strict or technical or legal meaning. A company in the normal sense means an association of persons united for a common object. Accordingly the term is used to represent associations formed to carry on some business for profit or to promote art, science, education or some charitable purpose. Such an association may or may not be incorporated according to the law of the land.

Section 2(20) of the Companies Act 2013 provides that company means a company incorporated under this Act or, under any previous company law."

According to Chief Justice Marshall of USA, "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 incidentalto its very existence".

Thus, a company is a voluntary association of persons formed for the purpose of doing business having a distinct name and limited liability .It is a

juristic person having a separate legal entity distinct from its members who constitute it, capable of rights and duties of its own and endowed with the potential of perpetual succession.

11.4 CHARACTERISTICS OF A COMPANY

The main characteristics of a company are :

1. Incorporated Association : An incorporated company or a 'corporation' is a single person distinct from the individuals constituting it, whereas an unincorporated company, such as a partnership, is a mere collection or aggregation of individuals. Therefore, unlike a partnership, a company is a corporate body and a legal person having status and personality distinct and separate from that of the members constituting it. Section 2(20) of the Companies Act 2013 provides that company means a company incorporated under this Act or, under any previous company law.Company is a voluntary association of persons formed for the purpose of doing business having a distinct name and limited liability It is a juristic person having a separate legal entity distinct from its members who constitute it, capable of rights and duties of its own and endowed with the potential of perpetual succession.

Lord Justice Lindley has given a comprehensive definition of a company.

According to him ,

"A company is an association of many persons

-who contribute money or money s worth a common stock and.

-employed for a common purpose.

-the common stock so contributed is denoted in money and is capital of the company.

-the persons who contribute it or to whom it belongs are members.

- the proportion of capital to which each member is entitled in his share.

- shares are always transferable although the right to transfer is often more or less restricted."

The Leading case on this point is **SalomanV.Saloman and Co Ltd(1897)**

Points decided are :

(1) Company is a legal entity separate and distinct from the individuals who compose it.

(2) The company is not in law the agent of the subscribers or trustee for them.

Facts of the case are : Saloman had a boot business. He sold the business to a company named Saloman & Company Ltd., which he formed. There were seven members-his wife, daughter and four sons who took one share each and Saloman himself who took. 20,000 shares £1 each. The purchase consideration was £ 39,000 and was discharged in the following manner.

- £9,000 paid in cash.
- Fully paid 20,000 shares of £1 each issued to Salomon.
- Secured debentures issued to Salomon £10,000.

Owing to strike in the boot trade the company was wound up. After payment of mortgage debt and interest thereon, there were only£ I ,055. While liabilities were £17,773-Secured debentures held by Salomon £10,000 and Unsecured Creditors £7,773.

According to Salomon, his debentures were secured and hence he must get the remaining amount of £ 1,055.

Liquidator contention was that Salomon should indemnify the company against whole of unsecured debt.

House of Lords unanimously held that Salomon is separate from Salomon & Co.Ltd.

Salomon, being secured creditor and hence got priority over unsecured creditors. Hence the secured debentures even though held by Salomon were to be paid in priority to unsecured creditors. The unsecured creditors got nothing.

Saloman's case established beyond doubt that in law a registered company is an entity distinct from its members, even if one person holds all the shares in the company. There is no difference in principle between a company consisting of only two shareholders and a company consisting of two hundred shareholders. In each case the company is a separate legal entity.

Example : Of the 3,000 shares in a company L held 2,999. He voted himself as the governing director and chief pilot at a salary. I was killed in an air crash while working for the company. His widow claimed compensation under Workmens Compensation Act. The Company opposed the claim stating that Lee was not a worker as the same person could not be Employer and Employee. Held: There was a valid contract of service between Lee and Company, and Lee was, therefore, a worker. Mrs. Lee's contention was upheld and hens compensation was payable. [Lee v. Lee's Farming Co., Ltd. (1960) 3. All E.R. 420 P.C.]

Implications of separate legal entity. From the above characteristic that a company is distinct from the members who constitute it, the following consequences arise;-

- That the member has no insurable interest in the property of the company.
- When the member dies, the company continues to exist. His share and iot the assets of the company vest in his personal representatives;
- The naionality of the company does not depend on the natonaliiy of the member;
- The company can sue and be sued in its own name.

3. Limited liability :"Limited Liability" means "you have to pay as much as you have agreed to pay."

"Unlimited Liability" means "you have to pay as much as you owe."

It is the liability of a member to a company, which is limited. The company's liability is always unlimited. A company itself is always fully liable to pay its debts so long as there are assets available to pay the debts. When a company goes into liquidation, the debts must be paid in a strict order to the extent of availability of assets.

- Limited liability of members is another most important characteristic of a company. It is the reason why a great many people invest their money in limited companies.
- The contribution of a member in winding up towards debts and liabilities and costs shall not exceed the amount unpaid on the shares.
- A Company is a separate person, having its own name, identity, common seal and capacity to se and be sued in its own name.
- A Company's liability may be limited by shares or guarantee or unlimited as per its MOA.
- ln some cases, however, the limited liability of members may be rendered unlimited.

From the above, It is clear that the liability of the Company is also its own and not that of its members.

4. Separate property : Another characteristic of the company is that it is capable of owning, enjoying and disposing of property in its own name. It is a consequence of the fact that the company is a legal person. The property of the company will not be considered as the joint property of the members constituting the company, although the capital and assets of the company are contributed by members. A member does not even have an insurable interest in the property of the company.

5. Perpetual succession : Unlike a natural person a company never dies. Under Section 9 of the Companies Act, 2013. It is an entity with a perpetual succession. This means that the company being an entity separate and distinct

from its shareholders, the life of a company is not measured by the life of any member; it is independent of the lives of its members. The death or insolvency of a member does not affect the corporate existence of the company. A company is an immortal person.. Members may come and members may go, but the company continues its operations unless it is wound up. A company is created by the process of law and can be put to an end only by the process of law. The existence of the company is not affected by the death of all the shareholders. Thus where all the members of a company were killed by a bomb, the company was deemed to survive. In such a case, the legal heirs of the deceased shareholders will become members.

6. Transferability of shares : Under Section 56 of the Companies Act, 2013. The shares of a company are freely transferable and can be sold or purchased in the share market. This is one of the reasons why people perfer to form companies than partnerships. A shareholder is therefore no permanently wedded to a company. The Companies Act recognises the right of transferability shares and provides that, the shares or other interest of any member shall be movable property transferable in the manner provided for in the articles of the company. However, any change in membership does not affect the working of the Company. Hence, members may come and go, but the Company goes on forever. In a Private Company, there are certain restrictions and not prohibition on transfer of Shares.

7. Common seal : As a company is an artificial person it cannot sign its name on a contract. So it functions with the help of a seal. Common seal is used as a substitute for its signature. Every company must have a seal with its name engraved on it. A rubber stamp does not serve the purpose. Anything done under an agreement between the company and the third party requires recognition of the company in the Form of an official seal unless exempted by the Act. A document not bearing the common seal of the company is not authentic and as such is not binding on the company.

W.e.f 29/5/15. The World "Common Seal" have been omitted from sec. 9. Therefore use of common seal is now optional and no more mandatory. If the company does not have a common seal, the authorization u/s 22(2) shall be made by 2 directors or by one director & CS where ever company has appointed a company secretary.

8. Capacity to sue and be sued : On incorporation a company acquires a separate and independent legal personality. As a legal person it can sue and be sued in its own name. A company may be sued for infringement of copyrights, negligence and contempt of court. A company may sue for an injury done to its business reputation by defamation.

ADVANTAGES OF INCORPORATION

In comparison to other business enterprices, an incorporated company enjoys l:he following benefits.

1. Artificial Legal Person : Unlike the partnership firm the company enjoy separate legal personality. The famous case of Salomon V. Salomon Co. Ltd. has proved the fact that even one man company is valid. So every associations on being incorporated, enjoys a distinct entity separate from members forming it.

2. Limited Liability : The Act limits the liability of member forming the company upto the face value of the shares or the guaranted amount as the case may be. This privilage is one of the principal advantage of doing business under a company form of organisation.

3. Prepetual Succession : On being incorporated, company enjoys a perpetual existence. The existence of company is in no way affected by the change in the constitution of company. Member may come, members may go, the company will continue for ever.

4. Transferability of Shares : As per the provisions shares are the movable property of the members & are transferrable as per the provisions of Articles of

the respective company. This distinct advantage available to the company, grants liquidity to the shares, as they can be sold or purchased in the open market.

5. Infinite Membership : A public company enjoys infinite membership over the other forms of organisation. There is no restriction as to the maximum number of members in a public company. Thus, any number of persons can contribute to the functioning of public company.

6. Permanency of capital & protection to creditors : Buy back of shares is a privilage allowed to the company which provide the company to purchase its own shares. This provision gives the permanency to the capital & also protects the creditors in the events of winding up.

7. Mobilsation of huge resources: Since any number of persons can contribute towards the capital of the company, huge resources can be mobilised in case the company starts an expansion & diversification activities.

8. Separate property : As established by the well known case of Macaura V. Northern Assurance Co. Ltd. that the company's property is different from the property of member. Thus member can neither use Company's property for its own personal purpose nor can claim any insurable interest in Company's property;

9. Ease in Control & Managememt : Since there in divorce between ownership and management in a company, the company is managed by in elected representatives called directors & moreover directors are highly professionalised and are capable to manage the company efficiently & effectively.

10. Capacity to Sue : As a juridic legal person Company can sue others in its name & the third party can also sue it. The managing directors & others directors are not liable to be sued for the dues against a company i.e. they are not personaly liable.

DISADVANTAGES OF INCORPORATION

1. Formalities & Expenses : Incorporation of the company is coupled with many complex formalities, requiring considerable time, efforts & money.

Even after the incorporation, many legal formalities are to be complied with by the company & there non compliance will attract penal consequences. Other forms of business organisations are comparatively free from such procedural formalities.

2. Corporate Disclosures: A company have to ensure maximum disclosure of information to the member of the company but the members have a limited accessability to the management & day to day working of the conern.

3. Divorce of control from ownership: Unlike the partnership firm, where partners have a direct control over its working, the members of the company do not have any effective control over its working. This is because of the fact that company is controlled by the elected representatives called directors.

4. Loss of privacy : Many corporate disclosures are required to be made, & many documents are required to be kept at Registrar's office, its office becomes a public office & the documents so kept are public documents. So any person can inspect any document by paying a prescribed fees. Now this facility is available on the internet.

5. Detailed winding up procedure: The winding up procedure mentioned in Companies Act is very expensive & time consuming as compared to other business enterprises.

6. Control by few : The Company is controlled by only few persons with business background which are having very less financial stake in the business but on the contrary control the huge corporate economic resources.

7. Greater Social responsiblity : A company is always called upon to show greater social responsibility, the company is required not to go, in any case, against public interest.

8. More tax burden in certain cases : The tax implications have a crucial impact in the decision as to the selection of form of business organsiation. Company is liable to tax at a flat rate as compared to the sole proprietors who

are taxed under slab system. Moreover different tax rates are applicable to different Companies like domestic Companies, foreign companies closely related companies etc.

9. Possibility of frauds : Since the company is controlled by few, there is a possibility that they will defraud the other parties, internal & external, related with the business. Manipulators so cleverly commit frauds, that it becomes difficult to fix the responsibilities.

A COMPANY IS NOT A CITIZEN

A company is a legal person (though artificial) in the eyes of law. It can hold property and can sue and be sued in its own name. But unlike a natural person it cannot acquire citizenship. There is no provision in the Companies Act or in constitution expressly conferring citizenship on a company. A-company does not enjoy the fundamental rights which are enjoyed by a citizen. This has been very well explained in State Trading Corporation of India Ltd. v. C. T. O. and others1 where Justice Hidayatullah observed :

The members who form the incorporated company do not pool their status or personality. If all of them are citizens of India, the company does not become a citizen of India anymore than, if all are married, the company would be a married person.The Supreme Court of India in another case held the same opinion that a company registered under the Companies Act is not a citizen entitled to the fundamental rights.

Moreover, the Citizenship Act, 1955, denies citizenship to associations or body of individuals as they are not persons for the purpose of this Act. It cannot exercise the right of franchise (because it is not a citizen).

Although a company cannot be citizen, yet it has a nationality, domicile and residence. The nationality of the company is decided by the place of its incorporation. A company incorporated in India will be an Indian company even though its members are foreigners. Similarly the domicile of the company is the place of its registration and will remain so throughout the company's existence.

A company can have only one nationality and one domicile but may have several residences at the same time. Its residence is primarily important for taxation purposes.

LIFTING THE CORPORATE VEIL

One of the fundamental principles of company law is that a company has personality that is distinct from that of its shareholders. Once a company is formed and registered under the Act, it is a separate legal entity distinct from its members. It can sue and be sued in its own name. This rule was laid down by the House of Lords in Salomon v. Salomon St Co, in 1897 in which it was held that even if one individual held almost ail the shares and debentures in a company, and if the remaining shares were held on trust for him, the company is not to be regarded as a mere shadow of that individual.

The principle of separate entity is regarded as a curtain, a veil, or shield between the company and its members, thus protecting the later from the liability of the former. The veil is impassable as an iron curtain. This theory of corporate entity is still the basic principle on which the whole law of corporations is based. A land lady's attempt to regain tenanted premises for self business could not succeed as the business was in the name of the company. The managing director cannot be compelled in his personal capacity to produce books of which he has custody in his official capacity. Similarly the largest shareholder has no insurable interest in the property of the company.

The concept of corporate entity was evolved to encourage and promote trade and commerce but not to commit illegalities or to defraud people. Circumstances may occur which compel the courts to identify a company with its members. When the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud or defend crime the law will not regard the company as a corporate entity and pays regard to the economic realities behind the legal facade. It has long been established that the Courts will not allow the

Salomon principle to be used as an engine of fraud, or to avoid pre existing legal obligations.

In reality the business of the artificial person is always carried on for the benefit of some individuals. Since an artificial person is not capable of doing anything illegal or fraudulent, the notion of corporate personality might have to be abandoned to identify the persons who are really guilty. This is known as 'lifting the corporate veil'.

The concept of lifting the corporate veil is a changing concept. It can be lifted for the benefit of the company too.'

The circumstances under which the courts may lift the corporate veil may be discussed under the following two heads :-

A. Under Judicial Interpretations	B. Under Statutory Provisions
1. Determination of Character.	1. number of members below statutory minimum.
2. Where company is a sham.	2. Failure to refund application money.
3. Prevention of fraud or improper conduct.	3. Company not mentioned on a bill of exchange.

11.5 SUMMARY

Company may be defined as group of persons associated together to achieve some common objective. A company formed and registered under the Companies Act has certain special features, which reveal the nature of a company. These characteristics are also called the advantages of a company because as compared with other business organizations, these are in fact, beneficial for a company.

11.6 GLOSSARY

1. **Company**: A company means a body of individuals associated together for a common objective, which may be business for profit or for some charitable purposes.

2. **Separate legal entity**: It implies that a company has an entity of its own recognised by law quite distinct from that of the natural persons forming it.

3. **Perpetual existence**: It means that the company has a continuous existence.

4. **Common seal**: It acts as the official signature of the company.

11.7 SELF ASSESSMENT QUESTIONS

1. Define 'Company'. What are its essential characteristics ?

2. 'A company is an artificial person , created by law with a perpetual succession and a common seal.' Explain this statement.

3. Give the merits and demerits of incorporation.

4. 'A Company is a legal person distinct from its members taken individually or collectively.' Discuss this statement.

11.8 LESSON END ACTIVITIES

1.Explain corporate veil in detail.

Ans. _____

_____

_____

_____

2. What is corporate veil? When can it be lifted?

Ans. _____

_____

_____

_____

3. "The fundamental attributes of corporate personality is that the corporation is a legal entity distinct from its members." Discuss fully.

Ans. _____

_____

_____

_____

11.9 SUGGESTED READINGS

1. N.D. Kapoor, Company Law, Sultan Chand & Sons, New Delhi.
2. S.C. Aggarwal, Company Law, Dhanpat Rai Publications, New Delhi.
3. S.K. Aggarwal, Business Law, Galgotia Publishing Company, New Delhi.
4. G.K. Varshney, Elements of Business Law, S Chand & Co., New Delhi.
5. K.C. Garg, Vijay Gupta and Joy Dhingra,Corporate Laws, Kalyani Publishers

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-III**

PAPER -IV **LESSON-12**

KINDS OF COMPANIES

STRUCTURES

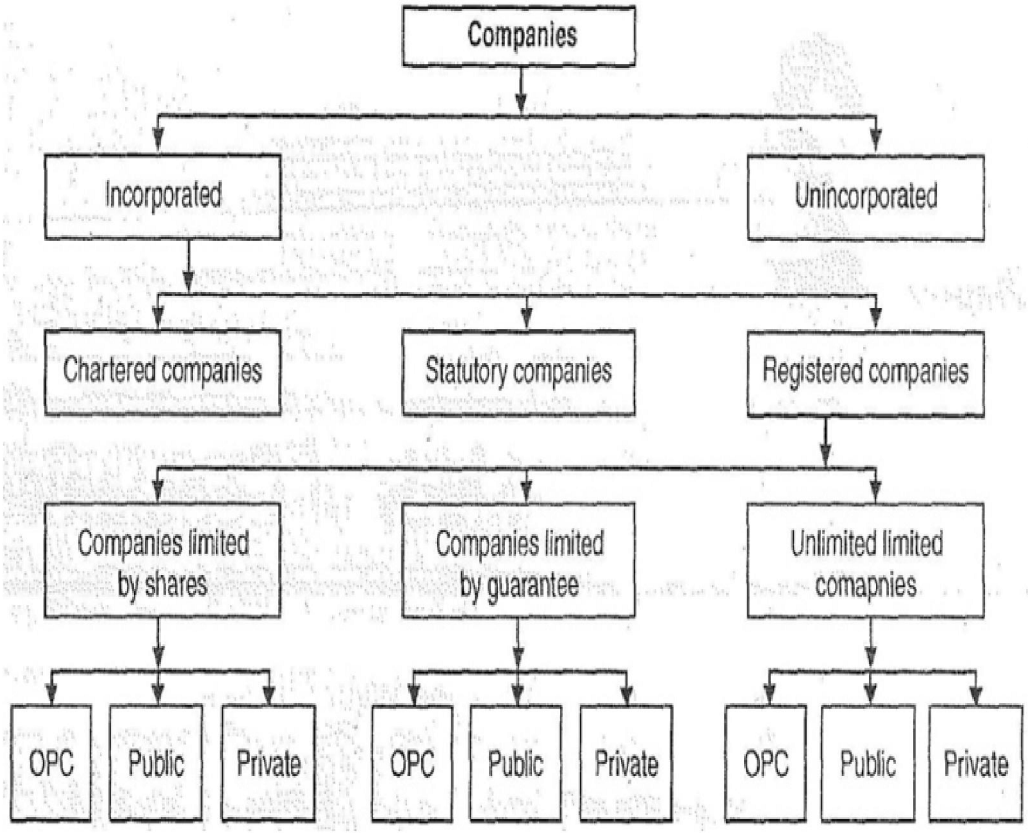
12.1 OBJECTIVES

After going through this lesson, you should be able to:

(a) Identify different types of companies

(b) Explain the basis on which companies are differentiated

12.2 KINDS OF COMPANIES



12.2 .1 CHARTERED COMPANIES

The 'Crown' in the exercise of the royal prerogative has power to create a corporation by the grant of a charter to persons assenting to be incorporated. Such companies or corporations are known as chartered companies. Examples of this type of companies are Bank of England (1694), East India Company (1600). The powers and the nature of business of a chartered company are defined by the charter which incorporates it. After the country attained independence, these types of companies do not exist in India. Moreover, the provisions of Companies Act, 2013 do not apply to such companies

12.2.2 STATUTORY COMPANIES

A company may be incorporated by means of a special Act of the Parliament or any State Legislature. Such companies are called statutory companies. Such companies are generally formed to carry out some special public undertaking, for example, railway, waterworks, gas, electric generation etc. Instances of statutory companies (which are also known as public corporations) in India are Reserve Dank of India, the Life Insurance Corporation of India, the Food Corporation of India, Unit Trust of India, State Trading Corporation etc.

Statutory companies are governed by the Acts creating them. They are not required to have any memorandum or articles of association. Changes in their structure are possible only by amendments in the Acts creating them. The annual report on the working of each statutory company is required to be placed on the table of the Parliament or the State Legislature as the case may be. A statutory company though owned by the government has a separate legal entity.

The provisions of the Companies Act, 2013, apply to the statutory companies except where the said provisions are inconsistent with the provisions of the Act creating them.

12.2.3. REGISTERED COMPANIES

Companies registered under the Companies Act, 2013, or the earlier Companies Acts are called registered companies. Such companies come into existence when they are registered under the Companies Act and a certificate of incorporation is granted to them by the Registrar.

A company registered under the Act may be

(a) a company limited by shares, or

(b) a company limited by guarantee, or

(c) an unlimited company.

(a) Companies limited by shares. (Sec. 2(22) of Companies Act, 2013).

In a company limited by shares the liability of the members is limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them. The liability can be enforced during the existence of the company as well as during the winding up. Where the shares are fully paid up, no further liability rests on them. The Companies limited by shares may be either 'private' or public companies.

For example, if a person holds 500 shares of the value of 10 and has paid ' 5 per share with the application and allotment of shares, his total liability will be 2,500 which can be called up at any time.

However, there is one exception to the above principle of limited liability. Where a company carries on business for more than six months with less than the statutory minimum (seven for public, and two for a private company), every member who knows of this fact will become liable to an unlimited extent for all debts contracted by the company in so carrying on business from the seventh month onwards. He will enjoy the limited liability privilege for the first six months only

(b) Companies limited by guarantee. (Sec. 2(2 1) of Companies Act, 2013)

It is a registered company public or private, in which the liability of members is limited to such amounts as they may respectively undertake in the memorandum to contribute to the assets of the company in the event of its being wound up. In the case of such companies as in the case of companies limited by shares the liability of its members is limited, to the amount of guarantee undertaken by them. The members are not required to contribute while the company is a going concern.

A company limited by guarantee may or may not have a share capital.

If it has a share capital the liability of the members is two fold :(1)liability to pay the share amount and (ii) the amount guaranteed .

A guarantee company without share capital does not obtain its initial and working funds from its members, but from some other source or sources e.g., grants, endowments, fees, subscriptions and the like. But a guarantee company having a share capital raises its initial capital from its members, while the normal working funds would be provided from other sources such as fees, charges, etc. The Companies limited by guarantee may also be either Private or Public Companies.

Every company limited by guarantee must have its memorandum and articles of association. The memorandum shall state that each member undertakes to contribute to the assets of the company in the event of its being wound up while he is a member or within one year after he ceases to be a member for payment of the debts and liabilities of the company such amount as may be required not exceeding a specified amount. In other words, the members give guarantee that when the company is to be wound up, they will contribute a certain fixed amount towards the assets of the company, if those assets are not sufficient to pay its debts.

(c) Unlimited companies. (Sec. 2(92) of Companies Act, 2013)

A company not having any limit on the liability of its members is termed as unlimited company. In such a company the liability of each member extends to the whole amount of the company's debts and liabilities, but he will be entitled to claim contribution from other members. The articles shall state the number of members with which the company is to be registered and if the company has a share capital, the amount of share capital with which the company is to be registered.

There are two varieties of each of these kinds of companies. A company may be either a public company or a private company.

PRIVATE AND PUBLIC COMPANIES

a) Private Company [Sec. 2(68)] : A private company is a very suitable form for carrying on the business of farmily and small concerns as the minimum number of members required is only two. [Sec. 2(68)] of the Companies Act,

2013 deals with the definition of a private company that provides that every private company should have a minimum paid-up capital of one lakh rupees.

Companies (Amendment) Act, 2015 has amended section 2(68) of the Companies Act, 2013. Now there is no requirement of minimum paid up capital for a private company. The definition o private company is quoted u/s 2(68) of the Companies Act, 2013. It means a company which has a minimum paid-up capital of one lakh rupees or such higher paid-up capital as may be prescribed, and by its articles :-

(i) restricts the right to transfer its shares

(ii) limits the numbers of its members to two hundred (excluding members who are or were in the employment of the company) ; (Maximum no. has been increased from 50 to 200 as per Companies Act, 20 13).

(iii) prohibits any invitation to the public to subscribe for any shares or debentures of the company; and

(iv) prohibits any invitation or acceptance of deposits from persons other than its members, directors or their relatives.

Stipulation of a minimum paid up equity capital of one lakh rupees does not apply to Section 8 companies which are associations not created for profit and do not distribute dividend.

b) **Public Company [Sec.2(71)]** : The definition of a public company has undergone a substantial change with the passing of the companies (Amendment) Act,2015. According to the Section 2(71) of the companies Act ,2013,A public company means a company which is not a private company has a minimum paid up capital ,as may be prescribed is a private company which is a subsidiary of a public company Thus, a public company is one that is not a private company.

As per companies (Amendment) Act 2015, there is no requirement of minimum paid up capital for a Public company (w.e.f.29/5/15)

c) Privileges of a private company :The following privileges and exemptions are available to a private company.

1. Number of members. A private company may consist of two members only against seven persons in the case of public company.

2. Prospectus. A private company may allot shares without issuing a prospectus or delivering to the Registrar a statement in lieu of prospectus.

3. Statutory meeting and statutory report. A private company is not required to hold a statutory meeting or file a statutory report with Registrar.

4. Number of directors u/s 149(a). A private company need not have more than two directors as against minimum three in the case of a public company.

5. Further issue of shares. The provisions of Section 62 as regards further issue of capital do not apply to a private company.

6. Allotment before minimum subscription. A private company can allot shares before the minimum subscription is subscribed or paid. The provisions of Section 39 as to the minimum subscription do not apply to private company.

7. Demand for poll. In the case of a private company, on any resolution, a poll may be demanded even by one member present in person or by proxy, if not more than seven such persons are personally present; if more than seven such persons are personally present, then by two such persons.

8. Rule regarding directors. The restrictions regarding appointment and re appointment of directors, and the provisions relating to retirement of directors by rotation do not apply to a private company.

   To increase the number of directors of a private company beyond the

maximum mentioned in the articles, the approval of the Central Government is not necessary.

Two or more directors of a private company can be appointed by single resolution.

The director of a private company is not required to file his consent to act as such with the Registrar .

9. Managerial remuneration: the rule of overall maximum 11% of net profit managerial remuneration does not apply to a private company.

10. A private company need not have an index of members.

11. Qualification of shares: Provision requiring the holding of share qualification by directors and fixing the time within which such qualification is to be acquired is not applicable to a private company.

12. Loans to directors. Prohibits loan to directors does not apply to private companies

13. Inter- corporate investments: the provisions of section regarding inter- corporate Investments donot apply to private company.

14. Paid-up capital. A private company can be registered with a paid-up capital of Rs one lakh while a public company is required to have a minimum on paid-up capital of Rs 5 lakhs. It is by virtue of these exemptions that a private company is described as an incorporated partnership, combining the advantages of both elements, the privacy of partnership and the permanence of the corporate constitution.

Distinction between a public company and a private company

Basis	Public company	Private company
Minimum number of members	The minimum number of members required to form a public company is seven	The minimum number of members required to form a private company is only two.
Maximum number of members	There is no limit to the maximum number of members.	A private company cannot have more than two hundred members excluding past and present employees
Restriction on Name	The name of the public company must end with the word 'limited'	But a private company must add the words 'Pvt. Ltd' at the end of its name
Invitation to public	4. A public company by issuing a prospectus may invite public to subscribe to its shares	A private company cannot extend such invitation to the public.
Transferability of Shares	5. There is no restriction on the transfer of shares in the case of a public company. Demat Shares are now freeely transperable.	A private company by its articles must restrict the right of members to transfer the shares.
Issue of Share Warrants	A public company can issue Share Warrants	Private Company can not issues Shares Warrants.
Further Issue of Capital	7. A public company proposing further issue of shares must offer them to the existing members.	A private company is free to allot new issue outsiders.
Number of Directors	A public company must have atleast three directors	A private company may have two directors
Statutory Meeting	A public company must hold a statutory meeting and file with the Registrar a Statutory Report.	A private company need not hold statutory meeting and hence no such obligations.
Quorum	. If the articles of a company do not otherwise provide the quorum is five members personally present in the case of a public company	The quorum in the case of private companies is two members personally present.
Restrictions on the Appointment	A director of a public company shall file with the Registrar	These restrictions do not apply to a private company

GOVERNMENT COMPANIES

Section 2(45) of the Companies Act defines a government company to mean any company in which not less than 51 % of the paid-up share capital is held by :

(a) the Central Government; or

(b) any State Government or Governments ; or

(c) partly by the Central Government and partly by one or more State

Governments, central government, or by any state government or governments, or partly by the central government and partly by one or more state governments. Shares held by municipal and other local authorities or public corporations are not to be taken into consideration. A subsidiary of a government company is also of a government company. Certain special provisions have been laid down in the Act regarding government companies. They are discussed below :

a) Appointment of auditor : The auditor of a government company shall be appointed or re-appointed by the Comptroller and Auditor-General of India. The Comptroller and Auditor- General of India will have the power to direct the manner in which the company's accounts shall be audited by the auditor.

b) Audit report : The auditor will submit a copy of the audit report to the Comptroller and Auditor General of India who may comment upon or supplement the audit report in such manner as he may think fit. Such comments or supplementary report shall be placed before the annual general meeting along with the audit report.

c) Annual reports : Where the central government is a member of the government .company. It shall cause an annual report on the working and affairs of the company to be prepared and laid before both houses of Parliament along with the audit report and the comments, if any, of the Comptroller and Auditor

General of India. The report shall be prepared within 3 months of the "annual general meeting. Where the state government, is also a member, the.report shall also be laid before the state legislature. But where the central government is not a member of the government company, the state government concerned shall cause the above documents prepared and laid before the state legislature. (Section 619-A).

d) Certain provisions of the Companies Act not to apply. The central government may by notification in the Official Gazette direct that any of the provisions of the Act (except the above-noted provisions), shall not apply to any government company or shall apply with such exceptions, modifications and adaptations as may be specified in the notification. In the absence of any such exemption the whole of the Act applies to government companies.

FOREIGN COMPANIES [SEC.2(42)]

It means a company incorporated outside India which has an established place of business in India .Accordingly a company which is incorporated outside India and employs agents in India but has no office or does not establish a place of business in India will not be a foreign company.

According to section 2(42) of Companies Act 2013, a foreign company is one incorporated outside India (a) which established a place of business within India after the commencement of this Act, or (b) which had a place of business within India before the commencement of this Act and continues to have the same at the commencement of this Act. The Companies (Amendment) Act, 1974, provides, that where not less than 50% of the share capital is held by Indian citizens and/or companies incorporated in India it shall have to comply with such of the provisions of the Act as may be prescribed as were a company incorporated in India.

The object of the above provision is to extend the regulatory provisions of the Act to those foreign companies which though incorporated outside India have raised a major portion of their capital from citizens of India or companies incorporated in India and carry on practically the entire business in India.

As already stated a foreign company must have a place of business in India. This, however, must be distinguished from a foreign controlled company. A company will be establishing a place of business in India if it has a specified or an identifiable place at which it carries on business such as an office, store house, godown etc. or some other premises with some visible sign or physical indication that company has a concrete connection with the particular premises, The word 'Establish' indicates more than occassional connection. Having a share transfer office or share registration office will constitute establishing a place of business. Even where representatives of a company incorporated outside the country frequently visited and stayed in a hotel for looking after purchases of machinery and other articles it was held that the company had a place in the hotel.

Whether a company is a foreign company or Indian company , will mainly depend on the incorporation of the company. Incorporation is the nationality of the company, and it may have nationality different from its shareholders. A company having all foreign shareholders may be incorporated in India and in that case the company will be an Indian company. Similary, a company may be incorporated in England having shareholders who are all Indian citizens and the company will be a foreign company.

ONE PERSON COMPANY

One person company is new concept in India under the Companies Act 2013 Section 2(62) of the Companies Act, 2013 defines that "One Person Company" means a company which has only one person as a member. One person company is required to identify in its name in bracket as One Person Company after its name .

Section 3(1)(c) of the Companies Act, 2013 provides that where the company to be formed is to be One Person Company that is to say, a private company, the company may be formed by one person subscribing his name to a memorandum and complying with the requirements of this Act in respect of registration .

One Person Company formed under section 3 may be either-

(a) a company limited by shares or

(b) a company limited by guarantee or

(c) an unlimited company

ILLEGAL ASSOCIATIONS

The aim of Companies Act is to prevent the mischief arising from large trading undertaking being carried on by large fluctuating and un-incorporated bodies making it difficult for persons dealing with them to know with whom they are contracting and so might be put to great difficulty and expense.The law has put a ceiling on the number of persons constituting an association or partnership. An unicorporated company, association or partnership consisting of large number of persons has been declared illegal.The law requires these associations to be compulsorily registered under the Companies Act, before they can function as legal associations.

Section 11 provides that no company, association or partnership consisting of more than 10 persons in case of banking business or more than 20 persons in the case of any other business which has for its objects the acquisition of gain can be legally formed unless it is registered under the Companies Act or is formed in pursuance of some other Indian law. If they are not so registered they would be considered as illegal associations.

Example : An unregistered association consisting of 115 members was formed at the instance of the government to help in the distribution of grams among people. It was established from evidence that elements of gain was present in this formation. It was held to be an illegal association under Section 11 (Babulal vs. Laxmi Bharat Trading Co. AIR 1966 Raj 14)

It may be noted that an illegal association under the section is not an assocation for illegal purpose. Section 11 only makes the association

illegal, that is the law does not recognise the right of more than 10 or 20, as the case may be, persons to carry on business as association. But that does not imply that the business of the association is unlawful. If the objects are lawful, just for want of registration it does not become an unlawful association. It is a lawful association but an illegal association and the consequences of section 11 would follow.In order to come within the operation of section 11 and following conditions are necessary :

1. There must be an association.
2. The association must be formed for the purpose of carrying on a business.
3. The business must have for its object the acquisition of gain.
4. The number of persons composing such association should exceed 10 in case of banking business and 20 in the case of any other business.
5. The association must not have been registered as a company under the Companies Act nor must it have been formed in pursurance of some other Indian law.

All the above conditions must be fulfilled before an unregistered association can be called an illegal association. An association once illegal retains its illegal character until registration or dissolution. Section 464 governs not only the first formation of the company, association or partnership but rules its continuance. The moment the number of members or persons in a partnership exceeds 10 or 20 as the case may be, it would become illegal for the members of the partnership to carry on business without registration.

Exceptions

(1) Associations with more than 20 persons as members and which carry on business but whose object is not the earning of profit are not compulsorily registrable. Associations like charitable, religious or scientific which are not formed for the purpose of acquisition of gain are excluded from the scope of section 11 of the Companies Act. Similarly the prohibition under section 11will not apply to an assocation of more than twenty persons like the Bombay Stock

Exchange which is not registered as it is not for the purpose of carrying on any business for acquisition of any gain for itself.

(ii) Section 11 does not also apply to a joint hindu family carrying on business, even though the number of members may be more than twenty. But if two or more joint families carry on business with more than 20 adult persons the association will be unlawful. In computing the number of persons of two or more joint hindu families, minor members of such families are excluded.

Example : XY and Z three joint hindu families, combined together for carrying on business for profit. X family consisted of a father and six major sons; Y family consisted of a father, 2 minor and seven major sons and Z family consisted of 4 minor and eight major sons. As the number of adult members that would be carrying on the business exceeds twenty, it would be regarded as an illegal association unless it is registered under the Companies Act, 1956.

Consequences of illegal association. The consequences of an illegal association are as follows :

1. Every member of such an association shall be personally liable for all liabilities incurred in such business and shall also be liable to a fine which may extend upto Rs 10,000. A suit will lie against each member of an illegal association but not against the association as such for enforcing all liabilities incurred in the business of such association.

2. An illegal association cannot sue to recover any debt or other property. But such an association may get itself registered and after becoming legal, may enforce its claims.

3. 3. Such an association cannot be dissolved under the Act either at the instance of a creditor, a member, or the association itself.

4. Its members have no remedy against each other for contribution in respect of partnership dealings and transactions.

ASSOCIATIONS NOT FOR PROFIT

Section 4 requires that the name of a public company must end with word 'limited' and in case of a private company with the words 'private limited'. Section 8, however , provides that the central Government may be licence direct that any association be registered as company with limited liability without using the words 'limited' or the words ' private limited.'

1. The Central Government shall grant a licence only if it is satisfied that-

(i) the association about to be formed as limited company aims at thepromotion of commerce, art, science, religion, charity or any other useful object, and

(ii) it intends to apply its profits, if any, in promoting its objects, and

(iii) it prohibits the payment of any dividend to its members.

On the above conditions being fulfilled such an association may be registered accordingly and on registration shall enjoy all the privileges and be subject to all the obligations of limited companies. Thus, an association registered under section 25 becomes a body corporate with perpetual succession.

It can adopt in lieu of company a more suitable name such as club, chamber, society, association. It can have a common seal, and it can sue and be sued in its own name. Its officers and members are free from personal liability.

The Central Government may grant the licence on such terms and conditions as it may think fit and the same shall be binding on the association. The Central Government may require such terms and conditions to be inserted in the memorandum or articles or both.

A company which has been granted licence under section 25 cannot alter the provisions of its memorandum with respect to its objects except with the previous approval of the Central Government signified in writing.

The licence can be revoked by the Central Government at any time after notice to the body of its intention to do so and after giving it an

opportunity of being heard against such revocation. On revocation of licence the Registrar shall enter the word 'Limited' or 'Private Limited' against its name in the register and ttie association shall thereupon cease to enjoy the exemptions.

PUBLIC FINANCIAL INSTITUTIONS

The Companies Act provides that each of the following institutions shall be deemed to be public financial institutions for the purpose of this Act, namely :

(i) the Industrial Credit and Investment Corporation of India Limited ;

(ii) the Industrial Development Bank of India ;

(iii) the Life Insurance Corporation of India ;

(iv) the Unit Trust of India.

(v) the Infrastructure Development Finance Company Limited,a company formed and registered under this Act.

The Central Government may be notification in the Official Gazette specify any other institution as it may think fit to be a public financial institution. But any such institution will not be so specified unless-

(i) it has been established or constituted by or under any Central Act; or institution is held or controlled by the Central Government. (ii) not less than 51 per cent of the paid up share capital of such institution is held or controlled by the Central Government.

In exercise of the powers conferred by section 4-A, the central government has notified the following institutions to be public financial institutions ; namely-

1. The Industrial Reconstruction Corporation of India Ltd.

2. The General insurance Corporation of India.

3. The National Insurance Company Ltd.
4. The New India Assurance Company Ltd.
5. The Oriental Fire and General Insurance Company Ltd.
6. The United Fire and General Insurance Company Ltd.
7. The Tourism Finance Corporation of India Ltd.
8. Risk Capital and Technology Finance Corporation Ltd.
9. Technology Development and Information Company of India Ltd.
10. Power Finance Corporation Limited.
11. National Housing Bank.
12. Small Industries Development Bank of India.
13. Rural Electrification Corporation Limited.
14. IFCI Ltd.

GROUP

It means a group of two or more individuals, associations, firms or bodies corporate or any combination thereof, which exercises or is in a position to exercise or has the object of exercising, control over any body corporate, firm or trust.

Where any question arises as to whether two or more individuals, associations, firms or bodies corporate or any combination thereof, constitute or fall within the definition of a group, the Company Law Board will decide after giving a reasonable opportunity of being heard.

Two important features of the definition of 'Group' may be noted, (i) A group may consist of not only natural persons like individuals and legal persons such as companies and other bodies corporate but it may also include unincorporated bodies such as associations and firms, (ii) It must exercise control

or be in a position to exercise control or must have for its object the exercise of control over any body corporate or firm or trust. The essential element in the definition is the exercising or being in a position to exercise control. In order to exercise control holding of shares is not always necessary..

OFFICER WHO IS IN DEFAULT

The Companies Amendment Act, 1988, has substituted section 5 of the Act. Prior to its amendment, under section 5 an officer who was knowingly guilty was an officer in default. The Amendment Act, 1988, has revised the definition of officer in default so that officers and directors who are incharge of management or who have been charged with the responsibility of complying with any provision of the Act are held responsible for any contravention of the Act.

The expression 'officer who is in default" means all the following officers of the company, namely-

(a) the managing director or managing directors ;

(b) the whole time director or whole time directors ;

(c) the manager ; .

(d) the secretary ;

(e) any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act;

(f) any person charged by the Board with the responsibility of complying with that provision, provided the person so charged has given his consent in this behalf to the Board ;

(g) where any company does not have any of the officers specified in clauses (a) to (c) any director or directors who may be specified by the Board in this behalf or where no director is so specified all the directors.

Provided that where the Board exercises any power under clause (f) or clause (g) it shall, within thirty days of exercise of such powers, file with the Registrar a return in the prescribed form.

It may be noted that this section would be applicable only to those provisions which provide for punishment of 'officer in defult' and it will not apply to provisions in which the said expression has not been used. In case of later mentioned provisions of the Act, means will continue to be a determining factor and the prosecution will have to prove that the offence was committed Knowingly or wilfully.

Default : Default has been explained as meaning "nothing more, nothing less that not doing what is reasonable under the circumstances or not doing anything which you ought to do, having regard to the relation which you occupy towards the other persons interested in the transaction. A wilful default has been defined thus "An act or omission to do an act is 'wilful' where the person who acts or omits to act knows what he is doing and intends to do what he is doing and in case of breach of duty it will be considered wilful even if it arises out of being recklessly careless, even though there may not be knowledge or intent .

12.3 SUMMARY

In this unit we have discussed the different kind of companies. The companies are broadly classified as incorporated and unincorporated companies.further they can be classified on the basis of incorporation, on the basis of liability, on the basis of nationality and on the basis of public interest.

12.4 GLOSSARY

a) *Incorporation*: It means when a company is formed into a legal corporation

b) *Shares*: A part of a portion of a large amount which is divided among a member of people.

c) *Capital*: Wealth owned by a person or organisation or invested ,lent or borrowed.

d) *Charter*: It means a written constitution or description of an organisation's functions.

12.5 SELF ASSESSMENT QUESTIONS

1. State in brief the various kinds of companies which can be registered under the Companies Act, 2013.

2. Define a private company and state the special privileges which it enjoys under the Companies Act, 2013.

3. 'Not only does the legislature recognise the private company, it is said to bestow its benediction upon it. Comment.

4. Explain why many of the provisions of the Companies Act, 2013, have been made inapplicable to private companies or have been made rigorous in their application to private companies.

5. What are the privileges and exemptions enjoyed by a private company when compared with a public company? Mention eight such items. Can a private company which is a subsidiary of a public company enjoy such privilages as are mentioned above?

12.6 LESSON END ACTIVITIES

1. Distinguish between a private and a public company.

Ans. _____

_____

_____

_____

2. What is the procedure for converting a private limited company into a public limited company?

Ans. _____

_____

_____

_____

3. Narrate the full procedure for conversion of a public company into a private company.

Ans. _____

_____

_____

_____

4. What is an illegal association? What are its effect?

Ans. _____

_____

_____

_____

5. What is a foreign company? How far is it governed by the companies Act 2013?

Ans. _____

_____

_____

_____

12.7 SUGGESTED READING

1. N.D. Kapoor, Company Law, Sultan Chand & Sons, New Delhi.
2. S.C. Aggarwal, Company Law, Dhanpat Rai Publications, New Delhi.
3. S.K. Aggarwal, Business Law, Galgotia Publishing Company, New Delhi.
4. G.K. Varshney, Elements of Business Law, S Chand & Co., New Delhi.
5. K.C. Garg ,Vijay Gupta and Joy Dhingra,Corporate Laws, Kalyani Publishers

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LEGAL ASPECTS OF BUSINESS

SEMESTER : IST **UNIT-III**
PAPER -IV **LESSON-13**

INCORPORATION OF A COMPANY

STRUCTURES

13.1 INTRODUCTION

A company, generally, comes into existence when a number of persons

come together with a view to forming an association to exploit the business opportunities by bringing together men, material, money and management.

13.2 OBJECTIVES

After going through this lesson, you should be able to:

* Define promoters
* Explain important steps in the formation of a company.
* Understand the Incorporation of a company

Formation of a company

In the case of formation of a private company, only the first two stages are involved as a private company can commence its business and exercise its borrowing powers immediately after securing the certificate of incorporation from registrar. Therefore,, a public company has to pass two more stages before it can commence business.

13.3 PROMOTION

Promotion of a company is the first important preliminary stage where in recessàry steps are taken for the registration of a company. Promotion is the process of organizing and planning the finances of a business enterprise under the corporate form. In other words promotion means the taking of such steps as would persuade a number of persons to come together for the achievement of a common objective through the company form of organisation. It is the discovery of business opportunities and subsequent organisation of funds, property and managerial ability into a business concern for the purpose of making profits thereform. The persons who undertake the task of promotion are called promotersJ

WHO IS A PROMOTER?

U/s 2(69) of the Companies Act 2013

Promoter means a person:

(a) Who has been named as such in a prospectus or is identified by the company in the annual return referred to in Section 92 ; or

(b) Who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

(c) In accordance with whose advice, directions or instructions the l3oard of Directors of the company is accustomed to act.

Provided that nothing in sub-section (c) shall apply to a person who is acting merely in a professional capacity. The promoter is a person who brings a company into existence. A company may have several promoters. A promoter may be an individual, a firm or body corporate One existing company may promote another new company. Everyone who is connected with the formation of a company may not be a promoter. A person who merely acts in a professional capacity on behalf of a promoter such as a solicitor, engineer, accountant or. a valuer is not a promoter in the eye of law.

FUNCTIONS OF A PROMOTER

A promoter takes all the necessary steps to create and mould a company and set it going. The promoters function till the board of directors of a company is legally constituted and starts governing the company.

Promoters perform the following functions:

1. Discovery of Idea. It promotion stage begins with the discovery of idea to set up a business. It can be an idea to set up a new business or an idea to expand the existing business. Promoter also analyses the amount of capital required and the degree of risk involved. .

2. Detailed Investigation. After analysing all the concepts related to the idea discovered, the promoter starts doing the detailed investigation regarding cost, profitability, production process, demand of the product etc. While doing the detailed investigation the promoter takes the help of the specialist or experts

such a chartered accountants, engineers etc. The reports of specialists help the promoter to take decision regarding the size of the business, location of the plant, amount of capital etc.

3. Assembling of Resources. In this stage a practical shape is given to the idea which is investigated and also verified by specialists. The promoter starts collecting all the resources necessary to form a company. Promoter makes contracts for purchase of material, land, machinery, recruitment of staff, etc.

4. Preparing Preliminary Documents. After assembling the physical, financial and human resources, the promoter prepares or gets prepared the necessary documents which are compulsory to be prepared for the formation of a company.

The important documents prepared by the promoter are:

(a) MemorandumofAssociation

(b) ArticlesofAssociation

(c) Prospectus.

5. Entering into Preliminary Contracts. The promoter signs a contract with different parties before the incorporation of the company. Generally company approves these contracts after incorporation but in case company does not approved these contracts, then promoter is personally liable for these contracts.

6. Naming a Company. The promoter has to select a name of the company. While selecting the name the promoter keeps in mind that the name should not be identical to the name of any of the company.

7. Appointment of Bankers; Brokers, Solicitors and Underwriters. The promoter appoints the brokers and underwriters to ensure the availability of capital by sale of company's securities, solicitors are appointed to deal with the legal matters of the company and the bankers are appointed to have smooth financial deaIings.

LEGAL POSITION OF A PROMOTER

As to the exact position of a promoter, the statutory provisions are silent. There is no doubt that the promoters occupy an important position and have wide powers relating to the formation of a company. It may, however, be noted that a promoter is not an agent because there is no trust in existence.

The correct way to describe his legal position is that from the moment he acts with the company in mind, he stands in a fiduciary position towards the company. Lord Cairns has correctly stated the position of a promoter in Erlanger v. New Sombrero Phosphate Co.

"The promoters of a company stand undoubtedly in a fiduciary position. They have in their hands the creation and moulding of the company. They have the power of defining how, and when, and in what shape and under what supervision, it shall come into existence and begin to act as a trading corporation."

The importance of the rule which creates a fiduciary relationship between the promoter and the company he brings into existence, can be seen when we consider its consequences which are as follows:

1. A promoter cannot make either directly or indirectly any profits at the expense of the company he promotes, without the knowledge and consent of the company and that if he does so, in disregard of this rule, the company can compel him to account for it. Any profit which the promoter makes after he has begun to promote the company and the benefits of any contracts into which he enters during that period belongs to the Company.

Where the promoter fails to make full disclosure of the profit that he is making, the company may sue him for damages for breach of his fiduciary duty and recover from him any secret profit made. In relation to disclosure it may be noted that half disclosure is worse than none.

Example: The old 'Olempia' Co. was in difficulties and the

debentures were worth very little. A syndicate consisting of X, Y and Z purchased a great number of debentures very cheaply. Then they purchased Olempia for 1,40,000 pounds and sold it to a new company which they promoted for 1,80,000 pounds. Consequently the debentures were paid in full out of 1,40,000 pounds and the syndicate made a profit of 20,000 pounds on debentures. X, Y and Z became directors of the new company. They disclosed their profit of 40,000 pounds but not their profit of 20,000 pounds. It was held that there was not sufficient disclosure and X, Y and Z must pay 20,000 pounds to the company [Gluckstein v Barnes (1900) A C 2401

2. A promoter is not allowed to derive a profit from the sale of his own property to the company unless all material facts are disclosed. If a promoter contracts to sell his own property to the company without making a full disclosure, the company may either repudiate the sale or affirm the contract and recover the profit made out of it by the promoter. Either way the dishonest promoter is deprived of his advantage.

The leading case on this point is

Erlanger V New Sombrero Phosphate Co. (1878)

Point decided is

Promoter, must make an honest disclosure to the company of all relevant facts which might affect the willingness of the company to purchase the property.

Facts of the case are

A syndicate of which E was the head purchased an island containing mines of phosphate for 55,000 pounds. E then formed a company to buy this island. A contract was made between X a nomine of the syndicate and the company for its purchase at 1,10, 000 pounds. The details of the sale were not disclosed to the shareholders or to an independent Board of directors. The company now sought to rescind the contract of sale. It was held that as there

had been no disclosure by the promoters of the profit they were making, the company was entitled to rescind the contract.

3. A promoter who wishes to sell his own property to the company must make a full disclosure of his interest in the transaction. The disclosure may be made (a) to an independent board of directors, or (b) in the articles or association of the company, or (c) in the prospectus, or (d) to the existng and intended shareholders directly.

4. The promoter shall not make an unfair or unreasonable use of his position. He must take care to avoid anything which has the appearance of undue influence or fraud.

RIGHTS OF PROMOTERS

The promoters being in a fiduciary relation with the company they form, have certain rights and liabilities the company. The rights of a promoter of the company are :-

1. Right to Receive Preliminary Expenses

The promoters are entitled to receive all the expenses incurred in setting up and registering the company from the Board of Directors. The articles may provide for payment of preliminary expenses to the promoters. The company may pa the expenses to the promoters even after its formation but such payments should not be ultra vires the articles of the company.

2. Right to Recover Proportionate Amount from the Co-promoters

The promoters are held jointly and severally liable for the secret profits made by them in formation of a company. Therefore, if the entire amount of secret profits is paid to the company by a single promoter, he is entitled to recover the proportionate amount from his co-promoters. Likewise, if the entire liability arising out of misstatement in the from his co-promoters. Likewise, if the entire liability arising out of mis-statement in the prospectus is borne by one of the promoters, he is entitled to recover proportionately from the co-promoters.

3. Right to Remuneration

A promoter having made proper disclosure, has a right to be paid remuneration for his efforts. The payment of remuneration to a promoter in consideration of his services may be in the form of fully or partly paid-up shares, debenture or commission or it can even be in the form of a lump sum-amount.

LIABILITY OF PROMOTERS

1. Pre-Incorporation Contracts : these Pre-incorporation contracts are entered into personally by the promoters. Promoters shall be liable jointly and severally and if only one promoter is sued he can claim contribution from others.

2. Liability to handover secret profits : A promoter can be compelled by the company to hand over any secret profit which he has made without full disclosures to

3. Mis statement in Prospectus

(a) Civil Liability

1. Under Section 35(1) : A promoter is liable for any untrue statement in the prospectus to a person who has subscribed for any shares or debentures on the faith of the prospectus. Such a person may sue the promoter for compensation for any loss or damage sustained by him.

2. Under Section 36 : lays down matters to be stated and reports to be set out in the prospectus. He may be held liable for fraudulently inducing persons to invest money on the basis of false or misleading statements made in the prospectus.

3. Criminal Liability under Section 34 : Besides civil liability, the promoters are criminally liable under Section 34 for the issue of prospectus containing untrue statements for imprisonment or fine or both.

4. Liability in Case of a Winding up of the Company.

(i) Liability in Case of a Public Examination: A promoter may be liable to public examination like any other director or officer of the company if the Tribunal so directs on a liquidator's report alleging fraud in the promotion or formation of the company.

(ii) Misapplication : A company may proceed against a. promoter for deceit or breach of duty, where the promoter has misapplied or retained any property of the company or is guilty of misfeasance or breach of trust in relation to the company.

REMUNERATION OF PROMOTERS

The nature of the promoter's work in the formation of a company calls for considerable skill for which he should be adequately remunerated. A promoter has no right against the company for his remuneration unless there is a contract to that effect. In the absence of such a contract, he cannot even recover from company payments he has made in connection with the formation of the company.

Example :A syndicate promoted a company and paid 416.25 pounds in respect of registration fees and stamp duty. The company shortly afterwards went into liquidation. It was held that syndicate could not, recover the payments it has made[Clinton's Claim(1908)]

Remuneration of Preliminary expensive. The articles generally give the directors power to pay the preliminary expenses out of the company's funds. Even in such a case it does not amount in law to a binding contract between the promoter and the company. However, the promoters are usually the directors, so that in practice the promoters will receive their remuneration.

13.4 INCORPORATION OF A COMPANY

A company comes into existence when a number of persons come together with a view to exploit some business opportunity. These persons are called promoters. Under Section 3, any seven or more persons (2 or more in the case of

a private company and 1 person in case of a one person company) may form an incorporated company for a lawful purpose by subscribing their names to the memorandum of association and complying with the other requirements in respect of registration. Such an incorporated company may be a company (a) limited by shares, (b) limited by guarantee, or (c) an unlimited company)

The purpose for which a company is going to be incorporated must be lawful) It means a purpose not forbidden by law or contrary to public policy. If one of the objects is unlawful the purpose is not lawful. Where the main object of a company is the conduct of a lottery, the mere fact that some of its objects were philanthropic will not save the company from being unlawful. The purpose would still be illegal even where the illegal business is merely annexed to the real 'one which is philanthropic. A certificate of incorporation is not conclusive as to the fact that the objects of the company are lawful.

The expression 'subscribing' their names to the memorandum of association means putting their signatures to the memorandum It means an agreement between the persons concerned to associate themselves into a body corporate.. A person becomes a subscriber by signing the memorandum.

The 'persons' who subscribe to the memorandum of association of the company should not be an infant, an undischarged bankrupt, a lunatic, an alien enemy and a person disqualified by law from entering into a contract. A partnership firm is not, but an incorporated company is a person under section 12 of the Act. A person whose signature appears in documents but not in the declaration in the memorandum as signatory to it is not a subscriber and even the certificate of incorporation will not cure this defect.

Steps before Proceeding with the procedure of filing documents:

1. DIN (Directors Identification Number) has to be obtained.
2. Digital Signatures of the Promoters.
3. Both DIN and Digital Signatures will be registered with the MCA

(Ministry of Corporate Affairs) Portal. After registration and verification of DIN and Digital Signatures of the Promoter who is to sign eform the following steps will be taken.

Availability of name. Section 4 of the Companies Act provides that a company cannot be registered by a name, which in the opinion of the Central Government, is undesirable. So, it is advisable that promoters find out the availability of the proposed name of the company from the Registrar of Companies. The promoters are required to select at least six alternative names in the order of preference for the proposed company and secure the name availability by making an application to the Registrar of Companies of the State in which they want to have the proposed company incorporated. The application is required to be made in the prescribed form (e-form INC-I) alongwith the prescribed fees and shall be with Digital Signatures of the promoter as per Companies (Registration Offices and Fees) Rules, 2014.

Applicant will get SRN (Service Request Number), which can be used to trace position about approval of name.

Availability of a name can be checked using the 'Check Company Name' service under 'Other Services' tab on homepage of MCA i.e. www.mca.gov.in. Once this is done, chances of rejection of proposed name will be reduced.

Six names are required to be suggested in order of preference, out of which, one may be approved, if none of the names suggested are acceptable, further names may be suggested.

If some key words or coined words are used, its significance should be stated. if proposed name is based on registered trade mark or application has been made for registration of trade mark, details should be furnished. Registrar of Companies is required to inform approval of name/rejection of proposed name within seven days.

Powers of approval of name have been given to Registrar of Companies. Once name is approved, it is kept reserved for 6 months. If application for

incorporation is not submitted within 6 months, the name can be allotted to other applicant.

The name should not be undersirable or be identical with or to nearly resemble the name of an existing Company.

Names prohibited under the Emblems and Names (prevention of improper use) Act, 1950, should not be used. In other words, a name which is undesirable in the opinion of Central Govt. should not be selected.

13.5 MINIMUM PAID UP CAPITAL

Minimum Paid-up Capital

It must be ensured that the minimum paid-up capital of the company is 5 lakh in case of public company and 1 lakh in case of private company.

Formalities to obtain Certificate of Incorporation

(a) Application Form. An application shall be filed with ROC in Form No. INC.2 (for one person company) and Form No. INC. 7 (other than one person company) [Under the Companies (Registration Offices & Fees) Rules, 2014 and Companies (Incorporation) Rules, 2014)]

Documents to be filed with the Registrar

After ascertaining the availability of name, the promoter should proceed to file with the Registrar of companies along with the fee and the required documents:

1) **Memorandum of Association** : The Memorandum of Association, is the charter of the company. This includes its objectives, its name, the address of its registered office, the capital which the company is authorised to raise, the nature of liability of members as well as the names, addresses and agreement of people who agree to form a company.

   For purpose of registration, the promoters have to file with the Registrar of Companies, a duly signed and properly stamped printed Memorandum ofAssociation.

2) **Articles of Association** : The other important document is the articles of association which contains the rules and regulations relating to the internal management of the company. However, it is not necessary for a public company limited by shares to file the articles of association. If such public company does not file Articles of Association, it is deemed to have adopted 'Table A' of schedule I of the Act.

3) **Vetting of Memorandum and Articles** : printing, stamping and signing of the same. Before proceeding with the printing of th memorandum and articles of association of a company it is usual for the promoters to approach the Registrar of companies concerned for vetting the draft memorandum and articles.

4) **Printing of Memorandum and Articles** : It is to be printed in accordance with the provisions.

5) **Stamping of Memorandum and Articles** : It is to be stamped in accordance with the stamp laws prevalent in the State where the registered office of the Company is to be situated.

6) **Signing of MOA & AOA** : To be signed by each subscriber (7 in the case of public Company or 2 in the case of private Company or 1 in case of OFC as the case may be or his duly appointed power of attorney indicating such capacity) and add his address, description and occupation, if any. In the case of limited company, an agent may sign a memorandum on behalf of the company, if he is authorised by power of attorney to do so.

   In case of Companies having share capital, each subscriber is to take up atleast one share and state clearly the number and nature of shares taken up. The above signatures are to be attested by Witness. The witness shall also sign and write in his own hand, his name, his father name, occupation and address.

7) **Dating of Memorandum and Articles** : The Memorandum and Articles are then dated, but the date must be a date of stamping or later than the

date of their stamping and not, in any event, a date prior to the date of their stamping.

8) Copy of proposed agreement : If a company purposes to enter into an agreement with any individual for appointment as a managing director, or a whole- time director or manager, a copy of such an agreement should also be filed with the Registrar of companies along with the other document.

9) Power of Attorney : With a view to fulfilling various formalities that are required for incorpoaration of a company, the promoters may execute a power of attorney in favour of one of them or an advocate or some other professional like the Chartered Accountant or a Company Secretary. The power of attorney to be given on a non judicial stamp paper of appropriate value with reference to the State in which the office of the ROC is situated or on a paper affixing non-judicial special adhesive stamps of same value.

10) Consent of the directors [Sec. 152(5)]: According to section 266, in the case of a public limited company having share capital, person cannot be appointed as a director by the Articles of Association unless, he has, before the registration of the articles, either himself or through his agent, signed aid filed, with the Registrar, his consent in writing to act as director. Consent of the directors is not required in case of private company.

11. Particulars of Directors along with DIN (Directors Identification Number) : Where a company by its articles of association appoint any person or persons as a directors, manager or secretary it may also file their particulars with the Registrar at the time of incorporation.

12. Filing of Agreemen : The agreement if any, which the company proposes to enter into with any individual for appointment as its

(a) managing director

(b) whole-time director

(c) manager.

Note : A public company or a subsidiary of a public company with paid-up capital of 5 crores or more is required to have a managing or whole-time director or manager.

13. Notice of Registered address must also be made Documents to be Filed :The following documents are to be filed to ROC to incorporate a company:

(a) Memorandum of Association duly stamped.

(b) Articles of Association, if any, duly stamped.

(c) If company proposes to appoint a person as Managing Director or Whole-time Director or Manager, a copy of agreement is to be enclosed.

(d) Statutory Declaration of Compliance.

(e) Power of attorney to correct Memorandum and Articles.

(f) If Articles of public company having share capital specify names of directors, their written consent as attachment.

(g) Original letter approving name of company.

(h) Notice of Registered Office.

(i) Proof of payment of filing fees.

Documents are to be filed with ROC (Registrar of Companies) of concerned State, along with filing fees. The documents are to be submitted electronically as scanned attachment to eform No, I. After submission, a SRN (Service Request Number) will be generated by system. The original Memorandum of Association and Articles of Association duly stamped signed should be submitted to ROC giving reference to SRN.

14. Statutory Declaration of Compliance : A declaration is to be filed in Form INC-8 with the Registrar of companies. This is known as 'Statutory Declaration of Compliance'. The promoters must file a statutory declaration stating that all requirements of the Companies Act and its rules relating to registration have been complied with.

This declaration may be signed by any of the following:

(a) an advocate of the Supreme Court or of a High Court, or

(b) an attorney or a pleader entitled to appear before High Court, or

(c) a secretary or a Chartered Accountant in whole-time practice in India and who has been engaged in the formation of the company, or

(d) by a person named in the articles as a director, manager or secretary of the company.

(e) Filing of documents for registration. It is pertinent to mention that the documents are tequired to be filed with the Registrar of companies of the state in which the company is proposed to be incorporated. On presentation of documents to the Registrar, the requisite fee is payable, which fee is not refundable even though the documents are rejected and registralion refused.

(f) If the Registrar is satisfied that all the requisite documents delivered to him are in order, he shall retain and register the memorandum and the articles, if any, provided he is satisfied on the following points.

(g) The name selected by the company is acceptable.

(h) The relevant provisions of the Act have been complied with.

(I) The objects of the company are lawful.

(j) The requisite number of persons required under the Act have subscribed and duly signed.

(k) The memorandum and the articles comply in all respects with the provisions of the Act.

(I) The statutory declaration has been properly made.

If the Registrar of Companies is satisfied that all the aforesaid requirements have been complied with, he will register the company and place its name on the register of companies. It is not competent for him to refuse registration on any extraneous considerations or for any reasons other than non.compliance. If there is any minor defect in any document, the Registrar may ask for its rectification. But if there is a material defect, he may refuse registration. It is clear that once the statutory requirements have been complied with, the Registrar has no option but to register it. On refusal to register on improper grounds, he may be compelled by a writ of mandamus.'

The Court or NCLT does not generally interfere with the decision of the Registrar unless such decision is based on wrong principles.

Certificate of Incorporation [Sec. 7(2)]

On registration, the Registrar will issue a certificate of incorporation in Form INC11 whereby he certifies that the company is incorporated and in the case of a limited company, that the company is limited. These days, Registrar of Companies issue a certificate of incorporation bearing a Corporate Identity Number (CIN) consisting of 21 digits.

From the date of incorporation mentioned in the certificate of incorporation, such of the subscribers to the memorandum and other persons, as may from time to time be members of the company, shall be a body corporate by the name contained in the memorandum. It becomes capable of exercising all the functions of an incorporated company having perpetual succession and a common seal. From the date of incorporation mentioned in the certificate, the company becomes a legal person separate from its shareholders.

The legal effect of incorporation is as under:

1. A company becomes a body corporate distinct from its members. .
2. A company has a perpetual succession and common seal.
3. A company can sue and be sued in its own name.
4. A company has a right to hold and alienate its own property. .
5. Company's debts and obligations are the liabilities of the company only and cannot be enforced against the individual shareholders.

When the memorandum is signed and registered, the subscribers are a body corporate capable immediately of exercising all the functions of an incorporated company. The company thus attains maturity at its birth. There is no period of minority, no interval of incapacity. A public company, however, cannot commence its business until the requirements have been complied with.

Conclusiveness of the Certificate of Incorporation

The certificate of incorporation is conclusive evidence that the requirements of the Act have been complied with and prevents the reopening of matters prior and incidental thereto, and it places the existence of the company as a legal person beyond doubt.

The certificate of incorporation shall be conclusive evidence that

(i) all the requirements of the Act have been complied with in respect of registration,

(ii) the company is duly registered, and

(iii) that the company came into existence on the date mentioned in the certificate.

However, where the object of a company is unlawful, it has been held that the certificate of registration is not conclusive for this purpose.

The validity of the certificate of incorporation cannot be disputed on any grounds whatsoever, It prevents the re-opening of the matters prior to the registration and essential to it. The reason underlying is that once a company is registered and has begun business and entered into contracts it would be disastrous if any person could allege that the company was not duly registered.

When the Registrar registers a company with the knowledge of defects in a document, no subsequent plea can be put up that the certificate is not a conclusive evidence.

The certificate would be conclusive that the company was duly registered even if the signatures to a memorandum were written by one person or were all forged. Similarly, if the signatories were all infants, the certificate would still be conclusive.

Certificate of incorporation does not mean all objects are legal

The certificate only proves conclusively that it has been properly incorporated. It does not prove that all the objects mentioned in it are legal or permissible. The certificate cannot validate illegal objects. A company cannot carry out an illegal object even if it is specified in the memorandum.

13.6 CAPITAL SUBSCRIPTION

When a company has been registered and has received certificate of incorporation it is ready for 'floatation', i.e., it can go ahead with raising capital necessary to commnence business and to carry on its operations satisfactory. It may be noted a private company is prohibited from inviting public to subscribe to its share capital. It has to raise the necessary capital from friends and relatives by private agreement.

The promoters of a public company may not invite the public for raising capital and may arrange privately as in the case of a private company. However, majority of the public companies raise their capital in the very first instance by

inviting public to subscribe to its share capital.

The Companies Act requires every public company to take either of the following two steps:

(i) Issue a Prospectus if public is to be invited to subscribe to its share capital, or

(ii) File A Statement in Lieu of prospectus' in case capital has been arranged privately.

13.7 COMMENCEMENT OF BUSINESS

NOTE. W.e.f. 29/5/15, as per the Companies (Amendment) Act, 2015, Section 11 regarding commencement of business has been completely abolished from the2013 Act.

Under the previous Act of 1956, a private company or ä company having no share capital can start business right from the date of its incorporation. Now the date of incorporation of a company shall not be the date of commencement of business. Both public & private company will have to obtain certificate of commencement of business.

U/s 11 of Companies Act, 2013, if the company has a share capital it shall not commence business until :-

(a) A declaration is filed by a director in the Form INC-2 1 along with the fee as per the Companies (Registration Offices and Fees) Rules, 2014 and the contents of the Form INC-21 shall be verified by a Company Sectary or Chartered Accountant or a Cost Accountant in Practice with the Registrar that:

(i) Every subscriber to the memorandum has paid the value of the shares agreed to be taken by him; and

(ii) The paid-up share capital of the company is not less than five lakh rupees in case of a public company arid not less than one lakh rupees

in case of a private company on the date of making of this declaration; and

(b) The company has filed with the Registrar a verification of its registered office as provided in sub-section (2) of section 12 and obtain a certificate from the Registrar of Companies for commencement of business.

A new company whether public or private will comply with the required formalities and obtain the commencement of business certificate from the Registrar as soon as possible after formation because, it cannot commence any business activities or exercise its borrowing powers without it.

On receipt of the declaration in the 'Form INC-21 and verification of the Registered Office in the form INC-22 the Registrar of Companies shall then issue the requisite certificate of commencement of business.

A certificate of commencement of business cannot be issued, if the company has not comp1ied with the provisions of section 11(1), [Malabar Iron & Steel Works Ltd. v Registrar of Companies (1963) 33 Comp Cas 813 (Ken)]

Certificate to commence business is conclusive evidence

The Registrar, on scrutiny of the declaration in e-Form INC-2 1, shall certify that the company is entitled to commence business and to exercise borrowing powers. The certificate shall be conclusive evidence that the company is entitled to commence its business. The Court will not take any evidence that there have been irregularities.

Procedure for obtaining certificate of commencement of business

In order to obtain certificate of commencement of business, by a company having share capital shall file the following documents with the Registrar of Companies according to section 11:-

(1) A declaration to be supported with the following documents attached

with the e-Form INC-2 1:-

(a) List of the members of the company with their shareholding;

(b) Confirmation for paid up share capital to the extent of Rs 5,O0,O0O in case of a public limited company and Rs 1,O0,O0O in case of a private limited and one person company and proof thereof, viz, copy of bank statement etc.;

(c) List of Managing Director, Directors, Manager, Secretary, CEO, CFO, Auditors and changes among them, if any since the data statement etc.;

(d) Consent of the Auditors;

(e) Copy of the agreements for appointment of Managing Director, Underwriters, contracts entered into by the promoters before incorporation of the company, etc. if any;

(f) Certified copy of the Memorandum and Articles of Association of the company;

(g) Details of the preliminary expenses already incurred and/or proposed to be incurred by the company;

(h) Power of attorney to obtain certificate for commencement of business from the Registrar of Companies;

(i) Certified copy of the resolution passed by the Board for approval of filling of declaration for obtaining certificate for commencement of business from the RoC.

(j) Copy of the NOC/Registration of the professional body/regulating authorities like RBI/SEBI/IRDA, etc.

Requirement to subscribe minimum capital

Before applying for obtaining a certificate for commencement of business by a company having share capital, it needs to file a declaration by a director in the Form INC-21 along with the fee as per the Companies (Registration Offices and Fees) Rules, 2014 with the Registrar confirming

that every subscriber to the memorandum has paid the value of the shares agreed to be taken by him and the paid-up share capital of the company is not less than five rupees in case of a public company and not less than one lakh rupees in case of a private company on the date of making of this declaration.

Filling of the notice for situation of the Registered Office with the RoC

A company shall, on and from the fifteenth day of its incorporation and at all times there after, have a registered office capable of receiving and acknowledging all communications and notices as may be addressed to it. Before applying for obtaining a certificate for commencement of business by a company the company needs to file with the Registrar a verification of its registered office in the Form INC22 as per section 12(2) of the Companies Act, 2013.

Penalty for default in obtaining certificate of commencement of business

If any default is made in complying with the requirements of section 11(1), the company shall be liable to a penalty which may extend to five thousand rupees and every officer who is in default shall be punishable with fine which may extend to one thousand rupees for every day during which the default continues.

13.8 SUMMARY

In this lesson we have discussed in detail the various stages through which a company is incorporated. A company , generally , come into existence when a number of persons come together with a view to forming an association to exploit the business opportunities by bringing together men, money, material and management. In the case of formation of a private company it commence its business after securing certificate of incorporation whereas a public company has to pass through two more stages before it is incorporated.

13.9 GLOSSARY

1. **Foreign Companies** : It means a company incorporated outside India which has an established place of business India.

2. **Contract** : It is a written or spoken agreement intended to be legally binding.

3. **Breach**: It is referred as an act of braking a rule or agreement

4. **Statutory Companies**: A company may be incorporated by means of special Act of the parliament or any state legislature.

13.10 SELF ASSESSMENT QUESTIONS

1. Name the documents which have to be filed with the Registrar at the time of incorporation of a public limited company.
2. What is meant by subscribing names to a memorandum of association?
3. What are qualification shares?
4. Who issues a certificate of incorporation?
5. When does a company legally come into existence?
6. Who is a promoter?
7. What is the position or status of a promoter?
8. What are pre-incorporation contracts?
9. Can a company ratify pre-incorporation contracts made for the benefit of the company?
10. When a public limited company can commence its business?
11. Discuss the different steps to be taken by the promoters from the formation of a company to the commencement of business.
12. Describe the procedure relating to the formation of companies under the Companies Act, 2013. Enumerate the various documents to be filed with the Registrar.

13.11 LESSON END ACTIVITIES

1. What is the effect of issuing a certificate of incorporation ? Can a court annul a certificate of incorporation which has been improperly issued?

Ans. _____

_____

_____

_____

2. A certificate of incorporation is conclusive evidence that all the requirements of the Companies Act have been complied with. Comment.

Ans. _____

_____

_____

_____

3. Who are the promoters? State the duties and liabilities of promoters.

Ans. _____

_____

_____

_____

4. A promoter is not a trustee or agent for the company but he stands in a

fiduciary position towards it. Discuss.

Ans. _____

_____

_____

_____

5. The services of a promoter are very pecul ar. Explain with reference to the activities of a promoter and discuss his legal relationship with the company he promotes.

Ans. _____

_____

_____

_____

13.12 SUGGESTED READING

1. N.D. Kapoor, Company Law, Sultan Chand & Sons, New Delhi.
2. S.C. Aggarwal, Company Law, Dhanpat Rai Publications, New Delhi.
3. S.K. Aggarwal, Business Law, Galgotia Publishing Company, New Delhi.
4. G.K. Varshney, Elements of Business Law, S Chand & Co., New Delhi.
5. K.C. Garg ,Vijay Gupta and Joy Dhingra,Corporate Laws, Kalyani Publishers

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-IV**

PAPER -IV **LESSON-14**

ARTICLES OF ASSOCIATION AND MEMORANDUM OF ASSOCIATION

STRUCTURE

14.1 OBJECTIVE

After reading this lesson, you should be able to

(a) Describe in detail the article of association and memorandum of association

(b) Explain the different clauses of memorandum of association and the alterations thereof.

(c) Discuss the contents of articles of association.

(d) highlight the importance of constructive notice of memorandum and articles of association

14.2 MEMORANDUM OF ASSOCIATION

Memorandum of Association is one of the documents which has to be filed with the Registrar of companies at the time of incorporation of a company. The memorandum of association of a company contains the fundamental conditions upon which alone the company has been incorporated.

Sec.2(56) of the companies Act, 2013	Memorandum means "Memorandum of Association of a Company as originally framed or altered from time to time in pursuance of any previous Companies Law or of this Act."
Cairns	Memorandum of Association of a Company is its charter and defines the limitations of the powers of a Company. (Ashbury Railway Carriage Co. vs. Riche)
Palmer	Memorandum of Association is a document of great importance in relation to the proposed Company. It contains the objects for which the Company is formed and identifies the possible scope of its operations beyond which its actions cannot go. It defines as well as confines the powers of the Company. If anything is done beyond these powers, that act will be ultra vires the Company and so void.
Bowen L.J.	Memorandum contains the fundamental conditions upon which alone the Company is allowed to be incorporated. Hence, MOA contains the objects for which the company is formed and there fore identifies the possible scope of its operations beyond which its actions cannot go. It

	defines as well as confines the powers of the company. If anything is done beyond these powers, that will be ultra vires the company and so void.

Importance

The memorandum of association is an extremely important document in relation to the affairs of the company. It is a document which sets out the constitution of the company and is really the foundation on which the structure of the company is based. It contains the fundamental conditions upon which alone the company is allowed to be incorporated. Its five clauses provide the basic features of the company's constitution. A company may pursue only such objects and exercise only such powers as are conferred expressly in the memorandum or by implication therefrom i.e., such powers as are incidental to the attainment of the objects. A company cannot depart from the provisions contained in its memorandum, however, great the necessity may be. If it does, it would be ultra vires the company and therefore wholly void. It defines its relation with the outside world and the scope of its activities.

After registration of the company, the memorandum becomes a public, document. While the memorandum must comply with the provisions of the Companies Act, all other documents of the company must comply with the memorandum.

Purpose of Memorandum

The memorandum of association is a public document available for inspection. It serves two purposes :

1. The intending shareholder who contemplates the investment of his capital shall know within what field it is to be put at risk. Thus he can find out from the memorandum the purpose for which his money is going to be used by the company and what risk he is taking in making the investment.

2. Anyone who deals with the company shall know without reasonable doubt whether the contractual- relation into which he contemplates entering with the

company is one relating to a matter within its corporate objects. Thus a supplier of goods or money will know whether the transaction he intends to make with the company is within the objects of the company and not Ultra vires its objects.

In short, the memorandum enables the shareholders, creditors and all those who deal with the company to know what its powers are and what the range of its activities is.

Printing and signing of Memorandum

U/S 3(1) of the companies Act,2013 :- At least seven persons in the case of a public company , at least two in the case of a private company and atleast one person in case of a one person company(OPC) must subscribe their name to the Memorandum.

Only a person capable to enter into a contract on his own can subscribe to the memorandum. Both artificial and natural persons can subscribe to the memorandum.

In the case of an illiterate subscriber to the memorandum, the thumb impression or mark duly attested by the person writing for him should be given.

The memorandum shall be printed. Computer printing is recognised for this purpose. It shall be divided into paragraphs numbered consecutively and shall be signed by each subscriber, with his address, description and occupation added, in the presence of at least one witness who will attest the same.

Form of memorandum (U/S 4 and 5).The memorandum of association of a company shall be in such one of the forms in Tables A, B, C, D and E in Schedule I of the companies Act,2013 as may be applicable in the case of the Company.

Table A is a form for memorandum of association of a company limited by shares.

Table B is a form for memorandum and article of association of a company limited by guarantee and not having a share capital.

Table C is a form for memorandum and articles of association of a company limited by guarantee and having a share capital.

Table D is a form for memorandum and articles of association of an unlimited company limited not having a share capital.

Table E is a form for memorandum and articles of association of an unlimited company and having share capital.

CONTENTS OF MEMORANDUM

According to Section 4 the memorandum of association of every company must contain the following clauses :

(a) Name Clause [Section 4(1) (a)].

The first clause of the memorandum requires a company to state its name. A company being a legal person, must have a name to establish its identity.The genera rule is that a company may be registered with any name it likes. But no company shall be registered by name which in the opinion of the Central Government is undesirable and in particular which is identical with or which too nearly resembles the name of an existing company .

A company which carries on or proposes to carry on business under a name calculated to deceive the public by confusion with the name of an existing concern commits the civil wrong of passing off and can be restrained by injunction from doing so.

Exampl : Plaintiff was carrying on business under the trade name of Buttercup Dairy Company. Another company was registered under the name of Buttercup Margarine Company Limited. It was held that the plaintiff was entitled to restrain the newly registered company from carrying on business on the ground that the public might reasonably think that the registered company was connected with his business. (Ewing v. Butter cut Margarine Company Ltd.(1917) 2 Ch. 1 (C.A.)l

According to Rule 8 of the Companies (Incorporation) Rules ,2014 a proposed name is considered to be undesirable if it is identical with or too nearly resembling with :

(1) Name of a company in existence; or

(2) A registered trade-mark or a trade mark which is subject of an application for registration, of any other person under the Trade Marks Act, 1999.

(3) The name shall also be considered undesirable if:

* It attracts the provision of Sec.3 of the Emblems and Names (Prevention and Improper use)Act,1950

* It includes any word or words which are offensive to any section of the people.

[Refer Rule 8 of Companies (Incorporation)Rules,2014 for detailed information on other reasons for an undesirable name]

Declaration by the Applicant

As per Companies (Incorporation) Rules, 2014, while applying for a name in the prescribed e-form-1 A, using Digital Signature Certificate (DSC), the applicant snail be required to furnish a declaration to the effect that:

(i) he has used the search facilities available on the portal of the Ministry of Corporate Affairs (MCA) i.e., www.mca.gov.in/ MCA2I for checking the resemblance of the proposed name(s) with the companies and Limited Liability Partnership (LLPs) already registered or the names already approved.

(ii) the proposed name(s) is/are not infringing the registered trademarks or a trademark which is subject of an application for registration, of any other person under the Trade Marks Act, 1999;

(iii) the proposed name(s) is/are not in violation of the provisions of Emblems and Names (Prevention of Improper Use) Act, 1950 as amended from time to time;

(iv) the proposed name is not offensive to any section of people, e.g., proposed name does not contain profanity or words or phrases that are generally considered a slur against an ethnic group, religion, gender or heredity;

(v) he has gone through all the prescribed guidelines, given in these Rules,understood the meaning thereof and the proposed name(s) is/are in conformity thereof;

(vi) he undertakes to be fully responsible for the consequences, in case the name is subsequently found to be in contravention of the prescribed guidelines.

As per **Companies (Incorporation) Rules 2014**, in determining whether a proposed name is identical with another, the following shall be disregarded.

(i) The words Private, Pvt., Pvt., (P), Limited, Ltd, Ltd., LLP, Limited Liability Partnership;

(ii) The words appearing at the end of the names-company, and company, co., co, corporation, corp, corpn, corp.;

(iii) The plural version of any of the words appearing in the name;

(iv) The type and case of letters, spacing between letters and punctuation marks;

(v) Joining words together or separating the words does not make a name distinguishable from a name that uses the similar, separated or joined words;

(vi) The use of a different tense or number of the same word does not distinguish one name from another;

(vii) Using different phonetic spellings or spelling variations does not distinguish one name from another.

For example, J.K. Industries limited is existing then J and K Industries or Jay Kay Industries or J n K Industries or J & K Industries will not be allowed. Similarly if a name contains numeric character like 5, resemblance shall be checked with 'Three' also;

(viii) Misspelled words, whether intentionally misspelled or not, do not conflict with the similar, properly spelled words;

(ix) The addition of an internet related designation, such as .COM, .NET, .EDU, .GOV, .ORG, .IN does not make a name distinguishable from another, even where (.) is written as 'dot';

(x) The addition of words like New, Modern, Nav, Snri, Sri, Shree, Sree, Om, Jai, Sai, The, etc. does not make a name distinguishable from an existing name such as New Bata Shoe Company, Nav Bharat Electronic etc. Similarly, if it is different from the name of the existing company only to the extent of adding the name of the place, the same shall not be allowed. For example, 'Unique Marbles Delhi Limited' cannot be allowed if 'Unique Marbles Limited' isalready existing;Such names may be allowed only if no objection from the existing company by way of Board resolution is produced/submitted;

(xi) Different combination of the same words does not make a name distinguishable from an existing name, e.g., if there is a company in existence by the name of "Builders and Contractors Limited", the name"Contractors and Builders Limited" should not be allowed;

(xii) If the proposed name is an exact Hindi translation of the name of an existing company in English especially an existing

company with a reputation, e.g., Hindustan Steel Industries Ltd. will not be allowed if there exists a company with name 'Hindustan Ispat Udyog Limited';

Required Authorised Capital in case of Certain Companies

With a view to maintain uniformity, the following guidelines may be followed in the use of keywords, as part of name, while making available the proposed names

SI. No	Key Words	Required authorized capital (in f)
1.	Corporation, corp, corpn, corp.	25 crore
2.	International, Globe, Global, World, Overseas, Universe, Universal, Continent, Continental, Inter Continental, Asiatic, Asia, Asian being the first word of the name	5 crore
3.	If any of the words at (2) above is used within the name (with or without brackets)	2 crore
4.	Hindustan, India, Indo, Indian, Bharat, Bharatvarsh, Bhartiya or any other country's name being first world of the name	2 crore
5.	If any of the words at (4) above is used, within the name (with or without brackets)	25 lakh
6.	If any of the words at (4) above is used within the name (with or without brackets)	25 lakh
7.	Industries/Udyog	5 crore
8.	Enterprises, Products, Business, Manufacturing, Venture.	50 lakh

Can Companies use the word State : If the proposed name includes the word "State", the same shall be allowed only in case the company is a Government company. Also, if the proposed name is containing only the name of continent, country, state, city such as Asia limited, Germany Limited, Haryana Limited, Mysore Limited, the same shall not be allowed;

Use of the word 'Limited' or 'Private Limited' : Every public company must write the word limited after its name and every private limited company must write the word 'private limited' after its name. The use of the word 'company' is however, not compulsory. Companies whose liabilities are not limited, are prohibited from using the word 'limited'.

If a limited company makes a contract without using the words 'limited', the effect may be most serious for the officers of the company because in that event the contract could be binding personally upon those who purported to act on behalf of the company.

When the word 'Limited' may be dropped: The word limited' may be dispensed with in the case of charitable companies. But companies formed to promote art, science, religion etc. which do not propose to pay dividend but intend to apply all its profits toward the working of the company, can be registered without the word 'limited' under licence granted by the Central Government.

Publication of name : Every company is required to publish its name outside its registered office, and outside every place where it carries on business, to have its name engraved on its seal and to have its name on all business letters, bill heads, notice and other official publications of the company.

If a company fails to paint or affix its name, the company and its officers who are in default shall be liable to a fine upon Rs 1000 for each day of default.

Seal. Every Company shall have its name engraved in legible characters on its Seal. Non-compliance will make the Company liable to a fine upto Rs 5,000.

(b) Registered Office Clause [Section 13(l)(b)].

This clause states the name of the State where the registered office of the company is to situate.

A company shall have its registered office. Such office must be in existence on and from the 15th day of its incorporation. Notice of situation of registered office and every change therein must be given the registrar within 15 .

Registered Office is really the permanent address of the company. It is residence of the company. It decides domicile of the company.

Address of registered office to fee specified in correspondence, bills etc.

Address of registered office must be specified in company's letter heads, bill books and in ail notices and official publications.Name board of company and address of registered office should be painted or affixed in a conspicuous position on the outside of every office or place in which business in carried out.

If default is made in complying with these requirements, the company and every other officer who is in default shall be punishable with fine which may extend to Rs 1000 for every day during which the default continues,but not exceeding Rs 1,00,000.

Importance of Registered Office

The registered office clause is important for following reasons.

1. It ascertains the domicile and nationality of a company.

2. The jurisdiction of a court is also determined with reference to the registered office of the company. It means, jurisdiction of High Court, Company Court, Registrar of Companies and Regional Director is decided on basis of registered office of the company.

3. It is the place where various registers relating to the company must be kept and to which all communications and notice must be sent.

4. Any document can be served on a company by sending it by post, under certificate of posting or by registered post or by hand delivery, at the registered office .

5. Case against company should normally be filed where registered office is situated, unless cause of action has arisen elsewhere.

6. Annual General Meetings of company must be held in city/ town in which registered office is situated.

7. As per Order 29, rule 2 of Code of Civil Procedure, summons on a company has to be served (a) On the Secretary or any director or other principal officer or (b) be leaving it or by sending it by post to its Registered Office.

8. Proxy for meetings have to be deposited at registered office of the company. As per section 169, requisition for calling of Extra Ordinary General Meeting (requisition meeting) shall be deposited at registered office. If members want to circulate a resolution u/s 188, its notice has to be served at Registered Office.

(c) Objects Clause (Section 4(1)(c)].

The third and important clause which defines the limits and extent of the activities of a company is its objects clause.

Section 4(1) (c) requires a company to divide its objects clause into two parts.

(i) Main Objects. This sub-clause has to state the main objects to be pursued by the company on its incorporation and objects incidental or ancillary to the attainment of the main objects.

(ii) Other Objects. This sub-clause shall state other objects which are not included in the above clause.

Further, in the case of a non-trading company, whose objects are not confined to one State, the objects clause must mention specifically the States to whose territories the objects extend.

Objects stated in the 'main objects' are to be pursued by the company immediately after incorporation or within a reasonable time thereafter. Where

the main objects of the company have failed to materialise, the Tribunal may order winding up under just and equitable ground.

Commencement of new business

No new business given in 'other objects' can, however, be commenced unless prior approval of shareholders with regard thereto is obtained by way of special resolution passed in general meeting .Where special resolution is not passed, the Central Government may, on an application made by the Board of directors, allow a company to commence business in the 'other objects', provided the votes cast in favour of the resolution exceed the votes cast against the resolution, if any .

The objects clause in the memorandum of a company is construed positively and negatively. Objects not mentioned in it are not the objects of the company, but this clause should not be construed too strictly and the company may not do anything which is fairly incidental to the main objects specified in it- Thus a company which has its main object the making of steel may want to run its own transport in order to supply its products to its purchasers. The transport aspect of the business would really be ancillary to the running of the business of making of the steel and ought to be implied so that it should not be necessary to provide for transport business in the memorandum.

Importance of the Objects clause : This clause is the most important clause in the memorandum of association of a company, because it not only shows the object or objects for which the company is formed but also determines the extent of the powers which the company can exercise in order to achieve the object or objects. It is essential that the public who purchase its shares should know clearly what are the objects for which they are paying and which they want to encourage. To give this information the statement of the objects should be clear. It must not be too vague and too general and too wide for in that case it will defeat its very purpose and object.

Lord Parkar in the case of Cotman v. Brougham has beautifully summed up importance of the objects clause.

"The truth is that the statement of the company's objects in its memorandum is intended to serve a double purpose. In the first place it gives protection to the subscribers who learn from it the purpose to which their money can be applied. In 'he second place it gives protection to persons who deal with the company and who can infer from it the extent of the company's powers. The narrower the objects expressed in the memorandum the less is the subscribers risk, but wider such objects the greater is the security of those who transact business with the company."

(d) Liability Clause [Section4(1)(d)]

This clause has to state the nature of liability that the members incur. In the case of a company limited by shares, the members are liable only to the amount unpaid on the shares taken by them. If his shares are fully paid up his liability is nil. Where a shareholder holding a Rs 10 share has paid Rs5 on it, he can be called upon to pay the balance of Rs5. In case he has paid the full value of Rs 10 he cannot be required to pay anything more even if the company owes huge debts to its creditors. In the case of a company limited by guarantee the members are liable to the amount undertaken to be contributed by them to the assets of the company in the event of its being wound up.

The liability clause is omitted from the memorandum of association of unlimited companies.

Any alteration in the memorandum compelling a member to take up more shares, or which increases his liability, would be null and void.

If a company carries on business for more than six months while the number of members is less than 7 in the case of a public company and' less than 2 in case of a private company, each member aware of this fact, is liable for all the debts contracted by the company after the period of six months has elapsed.

(e) Capital Clause [Section (4)(1)(e)] .The memorandum of a company limited by shares must state the authorised or nominal share capital, the different kinds of shares and the nominal value of each share. Provisions as to the nature

of these shares are more properly to be made in the articles.

The amount of the capital with with which company is to be registered is left to the discretion of those promoting it. It depends upon the needs of the company and the availability of finance. Moneys borrowed on debentures do not form part of the capital of a company.

Publication of authorized as well as subscribed and paid up capital

If a company publishes its authorized capital in any notice, advertisement or official publication or bill head or letter head, it shall also mention with equal prominence the amount subscribed and paid up. Otherwise, just looking at authorized capital, a person may be mislaid to believe that the company is big, though actually, it may be a small company.

(f) Association or Subscription Clause [Section 13(4)(c)}. This clause provides that those who have agreed to subscribe to the memorandum must signify their willingness to associate and form a company. The association clause generally runs in the following form, "We the several persons whose names and addresses are subscribed, are desirous of being formed into a company in pursuance of the memorandum of association and we respectively agree to take the number of sharesin the capital of the company set opposite our respective names."

The memorandum has to be signed by each subscriber in the presence of at least one witness who must attest the signatures. One witness to all the signatures is sufficient. But a subscriber cannot attest the signatures of another subscriber. Each subscriber must write opposite his name the number of shares he shall take. Mo subscriber to the memorandum shall take less than one share. This clause need not be numbered.

ALTERATION OF MEMORANDUM

The clauses in the memorandum as regards name, situation, objects, capital, liability of members and the undertaking of subscribers to take at least one share each are conditions. Since 'Memorandum of Association' is the constitution of the company, there are more restrictions on change of any of the

clause in the memorandum. Alteration of the memorandum only to the extent necessary for efficient and fair working of the company would be permitted.

The procedure for the alteration of the compulsory clauses or conditions of the memorandum is discussed below.

(a) Change of name [Sec 13(2)]

(1) By Special resolution : A company can change its name. For this purpose it must first pass a special resolution and then obtain approval of the Central Government in writing. However, no such approval is necessary for merely including or deleting the word 'Private' consequent on the conversion of the public company into private company and vice versa.

(2) By Ordinary resolution : If through inadvertence or otherwise a company is registered by a name, which in the opinion of the Central Government is indential with or too nearly resembles the name of an existing company, it can change its name by passing an ordinary resolution and with the previous approval of the Central Government signified in writing.

(3) Direction for changing name : The Central Government may also, within twelve months of registration, direct the company to change its name. Within three months of such directions the company must change its name by passing an ordinary resolution and with the previous approval of the Central Government. Default in complying with the direction is punishable with fine upto Rs 1000 for every day during which the default continues.

(4) Defaulting Companies Prohibited to Change the Name : Change of name shall not be allowed to a company which is defaulting in filing its due Annual Returns or Balance Sheets or which has defaulted in repayment of matured deposits and debentures and/or interest thereon.

(5) New Certificate of Incorporation : The Registrar shall enter the new name in the register in place of former name and shall issue a fresh certificate of incorporation. The change of name shall be complete and effective only on the issue of such a certificate. An application shall be filed in Form No.INC.24

along with the fee for change in the name of the company and a new certificate of Incorporation in Form No.INC.25 shall be issued to the company consequent upon change of name.

The Registrar shall also make the necessary alteration in the memorandum of association of the Company. (Section 23 (2))

Rights and obligations to remain unaffected. The rights and obligations of a company will not be affected on the change of its name (Section 23 (3)). Thus a company can continue legal proceedings which had been commenced by it in its former name. Similarly, the rights of the creditors will not be prejudiced by the change of name. But a company is not authorised to commence a legal proceeding in its former name at a time when it had acquired its new name.

Example : A company had changed its name from 'Malhati Tea Syndicate Ltd.' to 'Maihati Tea Industries Ltd.' Thereafter it filed a writ petition in its former name. The Court declared the petition to be incompetent. (Malhati Tea Syndicate Ltd. v. Revenue Officer AIR 1973 Cal. 781)

(b) Change of Registered Office

The change of registered office may involve any of the following :

(1) Change of registered office from one place to another place in the same city, town or village.

(2) Change of registered office from one town to another town in the same State.

(3) Change of registered office from one State to another State.

(i) Change within the City

If a company wants to change its registered office from one place to another within the same city, town or village, the board of directors will pass a resolution and the Registrar must be informed of the change in eForm 18 within 30 days.

(ii) Change within the State

Special Resolution under the jurisdiction of same ROC. Where the registered office is to be changed outside the local limits of any city, town or village in the same State, a special resolution to that effect must be passed. A notice of such change shall be given to the Registrar within 30 days of the change.

Confirmation by Regional Director in case of jurisdiction of different ROC within the same state. The confirmation by the Regional Director will be necessary for changing registered office of a company from one place to another if the change of registered office is from the jurisdiction of one Registrar of Companies to the jurisdiction of another Registrar of Companies within the state.

- For this purpose, the company shall make an application to the Regional Director in the prescribed form (Regional Director shall confirm within 4 weeks from the date of receipt of application) and the comfirmation shall be communicated within four weeks from the date of receipt of the application for such change.

- The company is required to file with the Registrar a certified copy of the confirmation by the Regional Director within 2 months from the date of confirmation, together with a printed copy of the memorandum as altered.

- The Registrar shall register the same and certify the registration under his . hand within 1 month from the date of filing of such document.

- The certificate shall be conclusive evidence that all the requirements with respect to alternation and confirmation have been complied with. Henceforth, the MOA as altered shall be the MOA of the Company*

- Compay shall give Notice of new location to ROC, in e-Form No. 18 within 30 days of change in Registered Office.

At present, this provision will have applicability only to companies situated in the States of Tamilnadu and Maharashtra which have more than one office of the Registrar of Companies.

These two changes in the registered office do not involve alteration of memorandum since in the memorandum of the company only the name of the State is mentioned.

(iii) Change of Registered Office from one State to another

Section 13 deals with the change of place of registered office from one State to another State. According to it, a company may alter the provisions of its memorandum so as to change the place of its registered office from one State to another for certain purposes referred to in Section 13of the Act. These purposes are discussed under the heading 'Change of objects clause'. In addition the following steps will be taken.

(a) Special resolution : For effecting this change a special resolution must be passed by the company and a copy thereof must be filed with the Registrar within 30 days. Special resolution must be passed in a duly convened meeting otherwise the Central Government cannot exercise jurisdiction.

(b) Confirmation by Central Government : The alteration of the provisions of memorandum relating to the change of the registered office from one state to another state shall take effect only when it is confirmed by the Central Government on petition. An application for approval of the central government shall be made inform No. INC.23 along with the prescribed fee u/s 13 of the companies to confirm the change in the registered office of a company from one State to another State has been transferred from Company Law Board to the Central Government.

Before confirming the resolution, the Central Government will give an opportunity to members, creditors and other persons such as State and the Registrar. The employees union of the company may also object. The Central Government before confirming or refusing to confirm the change will consider primarily the interest of the company and its shareholders and also whether the change is bonafide and not against the public interest. The Central Government may then issue the confirmation order on such terms and conditions

as it may think fit.

The shifting of the registered office is purely a domestic matter for the shareholders of the company. But some State governments in India have resisted the shifting of offices on the grounds of loss of revenue to the State or adverse effect on the general economy of the State. The State Government has no right to object on the ground of loss of possible future revenue, though it may do so as a creditor in respect of arrears of revenue due to it.

Example : A company desired to shift its registered office from the State of West Bengal to the State of Maharashtra. The petition was opposed by the State on the ground of loss of revenue. The Calcutta High Court allowed the petition and observed that "the question of loss of revenue to one state would have to be considered in the total conspectus of revenue for the Republic of India and no parochial consideration should be allowed to turn the scale in regard to change of registered office from one State to another within India." '(In re Machinnon Mackenzie and Co. (1967) 37 Com. cas. 516).

The company shall file with the Registrar in Form No.INC.28 a certified copy of the order of the Central Government confirming the alteration, within 30 days from the date of order together with a printed copy of the memorandum as altered and the Registrar shall register the same and certify the registration under his hand within one month from the date of filing of such documents .

The certificate shall be conclusive evidence that all the requirements of this Act with respect to the alteration and the confirmation there of have been complied with and henceforth the memorandum so altered shall be the memorandum of the company.

A certified copy of the order confirming the alteration shall be filed by the company with the Registrars of each of the States and the Registrar of each State shall registrar the same. The Registrar of the State from which such office is transferred shall send to the Registrar of the other State all documents relating to the company registered, recorded or filed in his office.

Change outside India. A Company cannot change its registered office from India to another country and the Central Government has no power to sanction such alteration of the memorandum.

(c) Change of the Object Clause : A company has no unlimited right to alter the objects clause of the memorandum, however, urgent or benefical such alteration may be. A company exists only for the purposes as are defined in the objects clause. The alteration of the objects clause is, therefore, subject to many restrictions and limitations which are intended to protect the interests of shareholders and creditors.

The power of alteration of objects clause is subject to two limits :

1. Substantive Limits 2. Procedural Limits.

1. Substantive Limits

A company may Change its registered office from one state to another or objects clause in so far as it is necessary for any of the following purposes

(a) To carry on its business more economically or more efficiently

There is very limited scope for alteration under this clause because.. The business of the company must remain substantially the same. In other words, this clause permits the alteration which will assist the company in the method of conducting its business and not alteration in the type of business which the company is conducting. The additions or alterations should be a step in aid to improve efficiency. When a company is not in fact carrying on any business, it cannot alter its objects under this clause.

(b) To attain its main purpose by new or improved means.

This clause is intended to enable companies to take advantage of new scientific discoveries. The company cannot alter its main objects, but can merely alter its ancillary powers or provide new powers to assist it in achieving its main objects.

This sub-clause uses the expression 'main purposes' and not

object. The word purpose is more restricted than object and consequently the alteration must be one to carry out the main purpose of the company rather than one of the objects of the company.

(c) To enlarge or change the local area of its operations

This clause permits alteration to enlarge or change the local area of operation but no alteration in the company's business is allowed.

(d) To carry on some business which under existing circumstances may be conveniently or advantageously combined with the business of the company.

This clause gives wide scope for carrying on any business which may conveniently or advantageously be combined with the existing business. Under this clause sweeping changes can be made in the memorandum of association. A company may start a new business which is wholly different from and bears no relation to the existing business of the company. All that is essential is that the new business should be capable of being conveniently and advantageously combined with the existing business. Thus a company which was formed for generating power was allowed to carry on cold storage and other allied business. But a company which carries on distillery business cannot alter its objects so as to include cinema business as it is not a business which can be said to be conveniently or advantageously carried on with the distillery business.

(e) To restrict or abandon any of the objects specified in the memorandum : A company may alter the memorandum to restrict or abandom any specified objects. It may occur due to the needs of time. But no such alteration will be deemed valid if it is done to give effect to a specified object on the winding up of a company.

(f) To sell or dispose of the whole or any part of the undertaking of the company : Alteration may be required when a company sells the whole or part of its undertaking. Under such circumstances policy changes

become inevitable.

(g) To amalgamate with any other company or body of persons : In case of amalgamation of a company with another company, a common plan is formulated. Change of memorandum is required to include or exclude the objects in accordance with the common plan.

The company can alter its objects clause only to the above extent and only for the above named purposes.

2. Procedural Limits

The following procedure must be followed for altering the objects clause.

a) Special resolution : Before the company can alter its objects clause, it shall pass a special resolution sanctioning the alteration. It may be noted that under section 13 ,the procedure to alter the objects clause has been simplified. Now the only requirement is to pass a special resolution to that effect and file it with the Registrar of Companies. The Confirmation of the Central Government is not at all required. However, the special resolution authorising the alteration of the objects clause should be for one of the purposes mentioned in section 13 as stated above. Any alteration in excess of the permitted range will amount to a violation of the Act..

Copy of the special resolution to be filed with the Registrar

The company shall file with the Registrar a special resolution passed by the company within one month from the date of such resolution together with a printed copy of the memorandum as altered and the Registrar shall register the same and certify the registration under his hand within one month from the date of filing of such documents.

The certificate shall be the conclusive evidence that all the requirements of the Act with respect to alteration and confirmation thereof have been complied with and henceforth as the memorandum so altered

is the memorandum of the company.

b) Consequence of non-filing : If the copy of the order is not registered within the prescribed period, the proceedings connected with the order will become void and inoperative. However, the Central Government may revive the order on an application made within one month of its lapse .It has been held that the application for revival of the order can be made even after the expiry of the period of three months i.e. after the order becomes void.

(d) Change of Liability Clause.

Limited Company	Unlimited Company	Club, or Association
-Ordinarily liability clause cannot be altered so as to make the liability of members unlimited.	-Section 32 permits an - unlimited company to register as a limited company.	Where as a result of alternation of Liability Clause of a Company which is a Club or any othersimilar Association
-Member's Consent may, be given either before or after the alternation.	On alteration, the Registrar shall close the former registration of the company and new registration shall take effect as if it were the first registration.	A member is required to pay recurring or periodical subscription or charges at a higher rate.
-Increase in liability may be by way of subscribing for more shares than the number held by him at the date on which the alteration is made or in any other manner.	The registration of an unlimited company as a limited company shall not, however, affect any debts, liabilities obligations or contracts incurred or entered into before the conversion.	-It shall be binding on him, even though he does not agree in writing to be bound by such alteration.

-Any alteration in the memorandum will be void if the effect of the alteration is the enhancement of the liability of members.		
-This provision, however, will not apply to a case where the mem-bers agree in writing to be bound by the alteration.		

A limited company if authorised by its articles by a special resolution may alter its memorandum to make the liability of its directors or manager unlimited. This rule applies to future appointees only. Such alteration will not affect the existing directors; and managers unless they have accorded their consent.

(e) Change of Capital Clause U/S 61(1)

SECTION 61 of the Companies Act, 2013 provides for alteration of Share Capital , whereas SECTION 62 provides for increase in share capital. A limited company, having a share capital may alter its capital clause subject to the provisions of its articles by a resolution in the general meeting. The confirmation of the Court is not required if alteration is made, for any of the following purposes :

1. To increase its share capital.
2. To consolidate and divide its capital into shares of larger amount.
3. To convert its fully paid shares into stock and reconvert the stock into fully paid up shares.
4. To sub-divide its shares into shares of smaller amount.
5. To cancel its shares.

A change in the description of shares from, say, Rs 100 to Rs 10 is no a change inthe fixed amount of the share and therefore, is not an alteration of a condition of the memorandum, so that no formalities are required by virtue of the Act.But in case of reduction of share capital, special resolution is necessary.

Filing with ROC [Sec. 64]

a) Where a Company has done any of the above alterations with regard to its! Share Capital, it shall within 30 days, give Notice to the ROC specifying the shares consolidated, divided, converted, sub-divided, redeemed or cancelled or the stock reconverted.

(b) Upon such Notice, the Registrar shall record the same and make any alterations that may be required in the Company's MOA and AOA.

(c) Default in giving Notice to Registrar shall render the Company and every Officer of the Company liable to fine upto Rs 500 per day of continuing default.

DOCTRINE OF ULTRA VIRES

The Companies Act requires that the memorandum of every company must state the object of the company. The objects clause must "delimit and identify the objects in such plain and unambiguous manner as that the reader can identify the field of industry within which corporate activities are to be confined." A company has power to carry out the objects set out in the memorandum and also everything which is reasonably necessary to enable it to carry out those objects. The objects clause requires that the company should devote itself only to the objects set out in the memorandum and to no others. The memorandum is thus the area beyond which a company cannot travel. Any activities not expressly or impliedly authorised by the memorandum are ultra vires the company.

'Ultra' means beyond, 'vires' means powers. An action outside the memorandum is ultra vires the company. An act is said to be ultra vires when it is performed which, though legal in itself, is not authorized by the objects clause

in the memorandum of association or the statute. Such an act is void and cannot be ratified even by unanimous resolution of all the shareholders.

Purpose. The doctrine serves two purposes :

1. It protects the shareholders. By it they are assured that their investment is not spent on activities which they did not have in mind when they invested in the company.

2. It safeguards the interests of the creditors as the property of the company cannot be diverted to unauthorised objects.

The purpose of the ultra vires rule is to ensure, 'that an investor in a gold mining company did not find himself holding .shares in fried fish shop and to give those who allowed credit to a limited company some assurance that its assets would not be dissipated in unauthorised enterprises

DRAFTING OF MEMORANDUM OF ASSOCIATION

The following steps are required for drafting a M.O.A of a company.

1. Contents of memorandum

Name

While drafting the M.O.A. the name should be written in full without any abbreviation including the words "LIMITED" or "PRIVATE LIMITED".

The name should be mentioned exactly as made available by the Registrar of Companies.

The word(s) "Limited" or "Private Limited", as the case may be, should be added as the last word(s) in the name. The Registrar of Companies should have permitted the name.

The Registrar may exempt the use of words "Limited" or "Private Limited" in the case of companies which have been granted licence under section 25 of the Act.

Place

While drafting the memorandum we should name the State in which the registered office is situated.

It is not required to mention the address or the place name of registered office. Even mention of such place name does not make it an unalterable condition.

Objects

The objects clause of a company formed after the commencement of the should specify the objects of the company under the following heads :

(a) Objects to pursued on incorporation; and

(b) Matters necessary for furtherance thereof.

The number of objects to be included in the Main Objects would depend upon the activities proposed to be carried on by the company.

In the case of non-trading companies, power to borrow should be specifically included. Such companies will have only those powers, which will enable them to carry out their objects.

The objects clause should state in the case of companies (other than Trading Corporations) where objects are not confined to one State, the States to whose territories the objects extend.

If the promoters so desire, other objects need not be mentioned. In such case under the heading Other Objects there should be written NIL

Limited liability

Where the liability of the members is limited, it should be so stated. The limited liability may be in respect of shares or guarantee.

Share Capital

The Memorandum shall state the amount of share capital with which the company is to be registered and the division thereof into shares of a fixed amount. It is not necessary to classify the shares into equity and/or preference.

Form of memorandum

The memorandum should be in one of the forms given in Tables A, B, C, D and E of Schedule I, as may be applicable, or in a form near thereto. Printing, etc.

The Memorandum should be printed and divided into paragraphs numbered consecutively.

Offset system is as good as normal printing, hence memorandum may be printed by offset method. Computer printing is also recognised for this purpose.

Xerox copies of the Memorandum and Articles of Association for the purposes of registration are not permissible.

Stamping

Stamp the Memorandum as per the Stamp Act provisions prevailing in the State

Subscribers to Memorandum

It may be noted that 7 persons are required for public companies and 2 for private companies and 1 person for One Person Company.

The liability of the subscriber is equal to the total amount due on the shares subscribed by him. It cannot be discharged by taking on transfer of shares from another.

The subscribers to the Memorandum should be the same as the promoters/directors stated in Form 1 A. Revise Form 1 A, in case there

is any change in the subscribers. To remove a subscriber, obtain a "No Objection Letter" from such subscriber. [Circular No, 27/1/89 CL-III, dated 17 February, 1989; Circular Ho. 1/90 (1/1/90 CL-V), dated 5 January, 1990]

Subscription of memorandum

The Memorandum as finally printed is thereafter signed by each, subscriber who shall add, in his own handwriting, his address, description and occupation, if any.

The subscriber shall also write opposite to his name the number of shares he takes.

The subscriber must take at least one share.

The signatures should be made in the presence of at least one witness who shall attest the signatures and shall likewise add his address, description and occupation, if any.

Then the memorandum should be dated.

A subscriber need not be beneficially interested. An agent may sign if he is authorised by a power of attorney to do so.

A guardian of a minor can sign in his capacity. Karta of a HUF may similarly sign.

In the case of an illiterate subscriber the thumb impression or mark should be duly attested. The person attesting the mark should state by way of an endorsement on the Memorandum and Articles that the contents have been read and explained to the subscriber.

In case of signature other than in English, there shall be attached an affidavit made by either the subscriber or the witness stating that the signature made is the usual signature of the subscriber.

In the case of Central and State Governments, subscription will be made in the name of the President or the Governor.

14.3 ARTICLES OF ASSOCIATION

Articles of Association is another important document which has to be filed with the Registrar at the time of the incorporation of the company. The articles of association sets out the regulations for the internal management of the company. According to section 2 (5) of the Companies Act, 2013 'articles' means the articles of association of a company as originally framed or as altered from time to time in pursuance of any previous companies law or of this Act. The articles of association contains the rules and regulations of a company framed for the purpose of management of its internal affairs. They define the powers of its officers. They also establish a contract between the company and members and the members interse. The articles are framed for carrying out the aims and objects of the memorandum of association.

The articles of association of a company are subordinate to and are controlled by the memorandum of association. The memorandum of association contains only the fundamental conditions upon which alone the company is allowed to be incorporated. The memorandum is as it were, the area beyond which company cannot go ; inside that area, the shareholders may make such regulations for their own government as they think fit.

Though the articles are subordinate to the memorandum, yet if there be any ambiguity in the memorandum, the articles may be used to explain it. Articles must not contain anything the effect of which is to alter a condition contained in the memorandum or which is contrary to its provisions. The articles should also not authorise the company to do anything which contravenes the provisions of the Companies Act. If they do, they would be ultra vires the Memorandum or the Act and will be null and void.

Compulsory to have articles : U/s 5(1) and 7(1) (a) of 2013 Act , it is compulsory for every company to have its own articles and file the same with

RoC for registration.

MODEL FORM OF ARTICLES

Schedule I to the Act gives various model forms of Memorandum of Association and Articles of Association for various types of companies. The schedule is divided into tables which serve as a model for various companies.

Companies which must have their own articles

The following companies shall have their own articles namely -

a) Public company limited by shares

b) private companies limited by shares

c) guarantee and unlimited companies.

Articles of a public company limited by shares:

Section 5(7) provides that a company may adopt all or any of the regulations contained in the model articles applicable to such company .

Therefore, a company may either:-

(1) Formulate and register Articles of its own within the provisions of the and the memorandum of association; or

(2) Adopt all or any of the regulations contained in the model articles(Table F);or

(3) Partially adopt Table F and also have its own articles

Regulations required in case of an unlimited company, a company limited by guarantee and a private company

Articles of a private company:-

A private limited company must have articles o f its own which must contain the restrictions as provided in section 2(68) of the companies Act, 2013.

Therefore, without following these restrictions in its articles it cannot have the status of a private company.

The company shall have a minimum paid uo capital of Rs 1,00,000 or such higher paid up capital as may be prescribed from time to time under the companies Act,2013.

It further-

(1) restrict the right to transfer its shares ;

(2) except in case of One Person Company, limits the number of its m e m bersto 200.

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member.

Following shall not be included in the number of members:

(a) Persons who are in the employment of the company; and

(b) Persons, who having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment closed

(3) prohibits any invitation to the public to subscribe for any securities of the company.

With these restrictions the private limited companies are having liberty to adopt to all or any of the regulations contained in Table 'F'

Articles of guarantee and unlimited companies

As per section 5(6) of the Act the articles of association of any company , not being a company limited by shares , shall be in such one of the forms in Tables G, H,I and J in schedule I as may be applicable , or in a Form as near thereto as circumstances admit.

The articles of the above types of companies , which do not have share capital, may follow the pattern as prescribed in the Act as under;-

Table 'G' : Articles of association of a company limited by guarantee and having a share capital.

Table 'H' : Articles of association of a company limited by guarantee and not having a share capital.

Table 'I' : Articles of association of an unlimited company and having a share capital.

Table 'J' : Articles of association of an unlimited company and not having a share capital.

Printing and signing of article [Section 7(1)(a)].

The articles must be printed and divided into paragraphs, numbered consecutively. The articles must be signed by each subscriber to the memorandum in the presence of at least one witness who will attest the signature and likewise add his address, description and occupation, if any. As in the case of memorandum no subscriber can attest the signature of another subscriber.

The Articles of Association printed on computer laser printers should be accepted by the Registrar for registration of a company provided they are neatly and legibly printed.

CONTENTS OF ARTICLES

The articles of a company may contain whatever rules the members decide should regulate the business of the company. The Act gives the members a free hand. Utmost care must be taken to prepare the articles of association of the proposed company. There are certain matters in respect of which powers can be exercised by the company only if its articles so provide and in the manner provided therein. At the same time, certain provisions of the Act are applicable to the company, notwithstanding anything to the contrary in the articles. Therefore,

the articles must contain provisions in respect of all matters which are required to be contained therein so as not to hamper the working of the company later. Everything stated in the articles is subject to the Companies Act. The articles cannot authorise anything expressly or impliedly forbidden by the Act. Any clause which is contrary to the provisions of the Act is simply inoperative and void. Section 439 of the Act confers the right on a shareholder to petition for winding up of a company in certain circumstances. This right cannot be taken away or limited by the articles.

Example : The articles provided that no winding up petition could be presented without the consent of two directors or unless a resolution to wind up was passed at a general meeting or the petitioner held one-fifth of the share capital rione of these conditions was fulfilled. Meld, the restrictions were invalid and the petition could be presented. (Re Peveril Gold Mines Ltd. (1898) 1. Ch. 122 C.A.).'

The articles usually contain rules regarding following matters :

I.Adoption of preliminary contracts. 2. number and value of shares.

3. Allotment of shares. 4. Calls on shares.

5. Lien on shares. 6. Transfer and transmission oshares.

7. Forfeiture of shares. 8. Alteration of capital.

9. Conversion of shares into stock. 10. Voting rights and proxies.

11. Meetings. 12. Directors, their appointment etc.

13. Borrowing powers. 14. Dividends and reserves.

15. Accounts and audit. 16. Winding up.

ALTERATION OF ARTICLES [SECTION-14]

A company has a statutory right to alter its articles of association. Any regulation or article purporting to deprive the company of this power would

be invalid. The company cannot contract itself out of its inherent statutory power to alter its articles and provide that any of its articles are to remain unaltered. Thus, a provision in the articles that no alteration of articles shall be made without the consent of X is contrary to the provisions of Companies Act and is therefore ineffective or void.A company can never replace its articles. It is only regulations contained therein which may be changed.

ALTERATION OF ARTICLES UNDER ORDER OF THE NATIONAL COMPANY LAW TRIBUNAL (SECTION 241-242)

The Tribunal may order a company to alter its articles with a view to resolving complaints against oppression and mismanagement in the company on an application made under Section 241 of the Act. The alterations made under an order of the Tribunal shall have the same effect as if they were made by the company in accordance with the Act . The company must file a certified copy of the order with the Registrar within 30 days of the issue of that order.

Procedure

Subject to the provisions of the Act and to the conditions contained in its memorandum, a company may by a special resolution alter or add to its articles. The company must file with the Registrar a copy of the special resolution within one month from the date of its passing. The altered articles will bind the members in the same way as did the original articles.

A Company can alter its articles of association at any time by passing a special resolution. The company can exercise its power of alteration subject to certain limitations.

LIMITATIONS ON POWER TO ALTER ARTICLES

1. Must not be against the provisions of Act : The alteration must not authorise anything expressly or impliedly forbidden by the Companies Act. Thus, the articles cannot authorise a company to pay dividends out of capital. Where a resolution was pased expelling a member and authorising the directors to

register the transfer of shares without an intstrument of transfer the resolution was held to be invalid as being against the provisions of the Act.

2. Must not be inconsistent to the Memorandum : The alteration must not extend or modify the memorandum. The memorandum of association is a superior document and the provisions of the articles cannot override it. What is prohibited by the memorandum cannot be authorised by altering the articles.

Example : A resolution passed at a general meeting of a company altered the articles by inserting the power to issue new shares with preferential dividend. The memorandum contained no such power. The alternation was held to be inoperative (liulton v. Scarborough Cliff Hotel Co. (1865) 62 EE 717.)

3. Must not sanction anything illegal : The alteration must not contain anything illegal. The company is the absolute master of its internal regulations and may alter those regulations provided such alteration is legal and is not prohibited by its memorandum. Such an alteration will be valid even if it alters the whole structure of the company.

4. Not be inconsistent with any alteration made by Tribunal (Sec. 404): Where an order u/s 397 or 398 makes any alteration in MOA or AOA of a Company, then Company shall not have power to make any alteration which is inconsistent with its orders except with approval of NCLT.

5. Approval of Central Government for conversion of public company : into private company. No alteration can be made in the articles which has the effect of converting the public company into private company unless such alteration has been approved by the Central Government.

Where an alteration has been approved by the Government, a printed copy of the articles as altered must be filed by the company with the Registrar within one month of the date or receipt or order of the approval.

6. No increase in the liability of members : No alteration may be made. in either the memorandum or the articles compelling a person who is a member at the date of the alteration to take or subscribe for more shares or increase his liability to the company unless he agrees in writing before or after the alteration is made.

7. Alteration by special resolution only : Alteration of articles will be made only by a special resolution as defined in the Act. Articles can never by altered by an ordinary resolution even if they provide for such a procedure. Even clerical errors in the articles should be set right by a special resolution.

8. Should not cause breach of contract : A company cannot by altering its articles escape liability for breach of a contract into which it has entered. It cannot plead its altered articles as a defence in an action for a breach of contract. The rights which have already accrued under the contract cannot be disturbed by the alteration.

Example : An agreement provided that so long as X company should hold 5,000 shares in the Y company, it should have the right of nominating two directors on the Board of the Y company, A provision to the same effect was contained in the articles of the Y company. X company had nominated two persons as directors whom the Y company refused to accept. An attempt was made to alter the articles but an injunction was granted to restrain it as it would constitute a deliberate breach of contract with an outsider. (British Murac Syndicate v. Alperton Rubber Co. Ltd. (1915) 2 Ch. 186).

9. Must be for the benefit of the company : The power to alter the articles must be exercised bonafide for the benefit of the company as a whole. If the alteration is bonafide for the benefit of the company as a whole, the interests of the minority may be sacrificed. Companies enjoy wide powers as regards alteration of articles. But this power must be exercised not only in the manner required by laws but also bonafide for the benefit of the company as a whole. An alteration will not be restrained merely because it inflicts hardships on some

members and not on others.

Example : The articles gave the company lien on all shares 'not fully paid' for calls due to the company. A was the only shareholder holding fully paid shares. He also owed money to the company for calls due on other shares. A died. The company altered its articles by deleting the words 'not fully paid up' and thus gave itself the power to exercise lien on all of A's shares. It was held that the alteration was good as it was done bonafide for the benefit of the company as a whole. (Allen v. Gold Reefs West Africa Ltd. (1900) 1. Ch. 657).

The expression for the benefit of the company as a whole' means for the benefit of the shareholders as a general body. Its effect should not be such as to discriminate between the majority shareholders and minority shareholders so as to give the former an advantage of which the latter are deprived.

10. Fraud on the minority : The alteration must not constitute a' fraud on the minority. The basic requirement is that the power of alteration must be exercised in good faith in the interests of the company.

In a case of Bwown vs. British Abrasive Wheel Co. (1919)101290 the majority which held 98% of shares passed a Special Resolution that upon request of holders of 9/1Oth of issued shares, a shareholder shall be bound to sell and transfer his share to the nominee of such holder at a fair value. Alternation was held to be invalid since it amounted to oppression of minority.

11. Retrospective alteration : Articles may be so altered as to have retrospective effect e.g. the insertion of a lien clause so as to give the company a lien on shares of members for debts incurred both before and after the insertion of the clause. But alterations should not be such as to throw an increased liability on members more than they contracted for when they became members.

But in case of pyara Lai Sharma Managing Director, J & K Industries

Ltd. (1989)3 Comp. L.J. (SL) 70, the Court held that the amended regulation in the articles of association cannot operate retrospectively, but only from the date of amendment.

12. Articles cannot be made unalterable: The alteration must not make the articles unlaterable as it is regarded bad in law.

13. An alteration of articles with permission of Central Goverment only under section 14 : An alternation of articles to effect a conversion of a public company into a private company cannot be made without the approval of the Central Government (Section 31).

14.4 MEMORANDUM AND ARTICLES DISTINGUISHED

Memorandum and articles arepublic documents. They are inter-linked and require to be registered for theformation of the company. Where there is any ambiguity or where the memorandum is silent on any point, the articles may serve to explain or supplement the memorandum. Beyond this the two documents have nothing in common and differ from one another in the following respects.

Particulars	Memorandum of Association	Articles of Association
Meaning	Memorandum of Association defines the relation of the company with the outside world	Articles of Association deals with the rights of the members of the company Inter se and also establishes the relationship of the company with the members.
Scope	Memorandum of Association is the charter of the company and defines the scope of its activities. management of the company	Articles of Association of the company is a document which regulates the internal These are the rules made by the company for carrying out the objects of the company as set out in the memorandum.
Contents"	Name Clause, Registered Offic Clause, Objects Clause, Liability Clause, Capital	Contains Regulations for Company management and those

	Clause and Association Clause.	that regulate relationship between members inter se.
Status	Memorandum is a supreme document of the company	Articles are subordinate to the memorandum.Theycannot alter or control the Memorandum of Association.
Alteration	Can be altered only under certain situations and in the manner provided. Approval of Central Government is required, besides approval of Shareholders in a General Meeting by way of Ordinary or Special Resolution.	Can be altered by the members by passing a Special Resolution only.
Ultra vires	A company cannot depart from the provisions contained in its Memorandum, and if it does, it would be *ultra vires the company*.	Anything done against the provisions of is *intra vires the Memorandum, Articles, but which can be ratified*.

14.5 CONSTRUCTIVE NOTICE OF MEMORANDUM AND ARTICLES OF ASSOCIATION

- The memorandum and articles of association of every company are required to be registered with the Registrar of Companies. The office of the Regislrar is a public office and consequently the memorandum and the articles on registration become public documents. They are open and accessible to all.

- These documents are open for public inspection on payment.

- Every one dealing with the company, whether a shareholder or an outsider is presumed to have read the two documents. He will be presumed to know the

- contents of these documents. This deemed knowledge of the two documents and their contents is known as the contructive notice of memorandum and articles.

- The parties dealing with the company must be taken not only to have

read these documents but also to have understood them according to their proper meaning.

- When a person deals with a company in a manner which is inconsistent with the provisions of the memorandum or articles, or enters into a transaction which is beyond the scope of the powers of the company, he must take the consequences in respect of such dealings.

DOCTRINE OF INDOOR MANAGEMENT

The doctrine of indoor management is an exception to the rule of constructive notice. A person dealing with a company is deemed to have knowledge of the memorandum and the articles of association of the company. So, if he enters into a transaction with the company which is ultra vires of the memorandum or articles, he cannot treat the transaction as binding on the company. On the other hand, if the transaction appears to be proper one, when compared with the memorandum and articles, it would be grossly unfair if the company could escape liability under it by showing that there was some irregularity in the conduct of the company's affairs leading upto the transaction, when the other party did not know of the irregularity and had no means of discovering it.

This rule has been described by Lord Hatherley as the 'Doctrine of Indoor management.' According to him, "Persons transacting business with the company are deemed to have notice of what they would have discovered by making a search at the office of the Registrar of Companies, and they would be stopped from asserting that they had not read the documents. But such persons are not deemed to have notice of, nor are they under a duty to inquire into the internal proceedings of a company. So an outsider is presumed to know the constitution of a company, but not what may or may not have taken place within the doors that are closed to him.

Thus, where as the doctrine of constructive notice protects the company against outsiders, the doctrine of indoor management seeks to protect outsiders

against the company.

The doctrine had its origin in the leading case of *Royal British Bank v.* Turquand **Royal British Bank V, Turquand (1856) 6E & B. 327].**

Point decided is

The outsiders dealings with the company are entitled to presume that as far as the internal managment of the company is concerned, every thing has been regularly done.

Facts of the case are

- The articles of a company stated that the directors could borrow money on behalf of the company, if they are so authorized by a resolution passed by the shareholders in general meeting.
- The directors borrowed money from Mr. T without obtaining any authorization from shareholders.
- They had lent the money to the company assuming that the shareholders had authorized the directors to borrow money as per the requirement of the articles.
- It was held that borrowing of money by the directors without any authorization from the shareholders amounted to a mere internal irregularity and further held that Mr. T could sue the company on the strength of the bond as he was entitled to assume that necessary resolution had been passed.

The lot of creditors of a company is not a particularly happy one; it would be unhappier still if the company could escape liability by denying the authority of the officials to act on its behalf.

The doctrine is quite useful in the sense that it covers acts done on behalf of a company by directors who have never been appointed or who have exercised authority without proper quorum, or who having power to allot shares only with the consent of general meeting allotted them without any such consent.

Example : The articles of a company provided that the directors could allot shares only to the existing members and could not without the consent of the company in general meeting allot them to outsiders. They allotted certain shares to P without the consent of the company in general meeting. It was held that the applicant was entitled to assume that the sanction of the company in general meeting must have been obtained. The allotment was held valid. (P. V. Damodara Reddi v. Indian national Agencies Ltd. AIR 1946 Mad. 35).

Exceptions

The doctrine is subject to the following exceptions :

1. Knowledge of irregularity. A person, who deals with company and who has knowledge of the irregularity in its internal management in connection with subject matter of his dealings, cannot claim the benefit of the rule in Turquand's case.

2. Negligence. A person cannot claim the benefit of the rule in Turquand's case circumstances under which he would have discovered the irregularity if he had made proper inquiries.

3. Forgery. The rule in Turquand's case will not apply where a document on which the person seeks to rely is a forgery. The rule cannot be invoked in favour of transactions involving forgery or otherwise void or illegal abinitio.

4. Acts outside the apparent authority. The rule in Turquand's case does not apply where a person acting on behalf of the company exceeds any actual or ostensible authority given to him. If the act of an officer of a company is one which would ordinarily be beyond the powers of such an officer, the plaintiff cannot claim the protection of the Turquand rule.

A company will be liable for fraudulent act of its officers acting under their ostensible authority on its behalf for their own benefit and not for the benefit of the company.

5. No Knowledge of the contents of articles. A person who has not actually read the memorandum and articles of a company and who was not at the time, he entered into the contract, aware of their contents, cannot seek to rely on statement contained therein.

He cannot claim that he should for his own benefit be treated as if he has read them by virtue of the doctrine of constructive notice. The rule of constructive notice operates against the person who fails to enquire but does not operate in hi| favour. In other words, it operates in favour of a company and not against it Act to Override Memorandum, Articles, etc. (Sec. 9) Section 9 provides that the provisions of the Companies Act will prevail in case there is a conflict between the Act and the company's memorandum, articles, resolutions or agreement. As for example, the quorum at a Board meeting, according to section 287 (2) of the Act, will be two directors, or one third of the total number of directors in office, whichever is higher. If the articles provide that the quorum will be minimum three, or one third, whichever is large, such provision will be ineffective.

Any provision contained in the memorandum, articles, agreement or resolution of the company is void to the extent to which it goes against the provisions of the Companies Act.

14.6 SUMMARY

Memorandum and Articles of association are the two important document which has to be filed with the registrar at the time of Incorporation of the company. Memorandum of association contains the fundamental conditions upon which alone the company has been incorporated. Hence, it contains the object for which the company is formed and Articles of association sets out the regulations for the internal management of the company. Therefore, this lesson enlighten us about the two vital documents which plays a significant part in the formation of a company.

14.7 GLOSSARY

1. Memorandum: A written message in business which has to be filed with the registrar of companies at the time of incorporation of a company.
2. Preliminary: it means happening before or preparing for a main action or event
3. Forfeit: It means a lose property or right as a punishment for a fault or mistake.
4. Debts: It is referred as a sum of money owned

14.8 SELF ASSESSMENT QUESTIONS

1. Mention the two purposes of a memorandum of association ?
2. List the various clauses of a memorandum of association.
3. How a company can change its name ?
4. Is it necessary for a company to have a registered office ?
5. 'The object clause is the most important clause in the memornadum of association of a company.' Why ?
6. Explain the doctrine of ultra vires.
7. Set out the steps to be followed by a company which desires to alter the objects clause of its memorandum of association.
8. What is the relation of memorandum of association with articles of association ?

14.9 LESSON END ACTIVITIES

1. Can a company ratify an act which is ultra vires the company ?What procedure is to be followed by a company when it wants to change its registered office from one town to another town in the same State ?

Ans. _____

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2. What is meant by 'articles of association' of a company.

Ans. _____

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3. Define articles of association and give the contents thereof. Is it necessary for every company to have articles of association of its own ?

Ans. _____

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4. Discuss how and to what extent articles of association of a company can be altered ?

Ans. _____

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5. Explain the doctrine of indoor management and state the exceptions, if ato the doctrine.

Ans. _____

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6. Explain the principle laid down in Royal British Bank v. Turquand. What are the exceptions to this princple ?

Ans. _____

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14 .10 SUGGESTED READINGS

1. N.D. Kapoor, Company Law, Sultan Chand & Sons, New Delhi.
2. S.C. Aggarwal, Company Law, Dhanpat Rai Publications, New Delhi.
3. S.K. Aggarwal, Business Law, Galgotia Publishing Company, New Delhi.
4. G.K. Varshney, Elements of Business Law, S Chand & Co., New Delhi.
5. K.C. Garg ,Vijay Gupta and Joy Dhingra,Corporate Laws, Kalyani Publishers.

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LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-III**
PAPER -IV **LESSON-15**

PROSPECTUS : ISSUE OF CAPITAL, SHARES AND SHARE CAPITAL; KINDS OF SHARES

STRUCTURES

15.1 INTRODUCTION

One great advantage of floating a company is the raising of capital required for business from the general public. This is done by issuing a document called 'prospectus'. In essence, prospectus sets out the prospects of the company and the purpose for which the capital is required. It intends to arouse the interest of the investors in the proposed company and induces them to invest in its shares or debentures. However, a private company is prohibited from inviting public to subscribe to its shares or debentures. It is only the participate in its investments.

Definition

Section 2(70) of the Act defines a prospectus as" any document described or issued as a prospectus and includes red herring prospectus referred to Sec.32 or shelf prospectus referred to in Sec.31or any notice, circular, advertisement or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of any shares in, or debentures of a body corporate."

U/S 31, Shelf prospectus means a prospectus in which the securities or class of securities are issued for subscription in one or more issues over a certain period without the issue of further prospectus.

U/S 32, Red Herring Prospectus means a prospectus which doesnot include complete particulars of the quantum or price of the securities included therein.

In other words, a prospectus means any invitation issued to the public

inviting it to deposit money with the company or to take shares or debentures of the company. Such invitation may be in the form of a document or a notice, circular, advertisement etc.

Any document to be called a prospectus must have the following ingredients :

(a) there must be an invitation offering to the public ;

(b) the invitation must be made by or on behalf of the company or in relation to an intended company;

(c) the invitation must be to subscribe or purchase;

(d) the invitation must relate to shares or debentures.

The first condition implies that an oral invitation shall not be regarded as a prospectus. Thus a TV or Radio advertisement, not being document does not become a prospectus. Thus, a prospectus must be in writing.

A prospectus is not an offer in itself but an invitation to make an offer, signifying thereby that on acceptance of such an invitation by any member of the public, no binding contract between him and the company comes into existence, it is rather a counter-offer by him to the company which, when accepted by it brings into existence a binding contract.

Any advertisement offering to the public shares or debentures of the company for sale is prospectus. An advertisement was Inserted in a newspaper stating, "Some shares are still available for sale according to the terms of the prospectus of the company which can be obtained on application." This was held to be a prospectus as it invited the public to purchase shares.

As aforesaid, a prospectus is usually a circular or newspaper advertisement published by the promoters after the formation of the company to induce the public to take or subscribe shares in the company. Subscription or

purchase means a subscription or purchase for cash. Accordingly a document which offers shares in exchange for shares is not a prospectus.

Meaning of issued : The rules as to prospectus are attracted only where a prospectus is 'issued'. Issued here means issued to the public. Whether the prospectus has been issued or not is a question of fact in each case and is not capable of exact meaning.

Example : Several copies of a document marked 'strictly private and confidential' and containing particulars of a proposed issue of shares, were sent accompanied by form of application by the managing director of the company to a co-director, but the document did not contain all the material facts required by the Act to be disclosed. It was also not advertised. The co-director sent a copy to a solicitor who, in turn, gave it to a client who passed it on to a relation. Thus, the document was passed on privately through a small circle of friends of the directors. It was held that this did not amount to an issue and accordingly, an action for compensation by the allottee (the relative of the client of the solicitor) for loss sustained by reasons of the omissions in the document, failed. (Nash v., Lynde 1929 AC 158).

Offer to the public : A document will be treated as a prospectus only when it invites offers from the public. Whether shares have been "offered to the public" or not is a matter of fact to be decided by considering the circumstances of a particular case.

The word 'public' is a general word : Mo particular numbers are prescribed. According to Section 42 of the Companies Act 2013, the term 'Public' includes any section of the public, whether selected as members or debenture holders of the company or as clients of the company issuing the prospectus.

It provides that any offer of shares or debentures to more than 50 persons shall be treated as public issue. The effect is that an issue will remain in the category of a 'domestic concern' only when the offer is

confined to less than fifty persons. An offer extending to fifty or more persons will tantamount to a public issue. (However, non-banking financial institutions or public financial institutions are excluded from the application of this proviso.)

Where the invitation or offer of shares made to a section of the public does not entitle other than those who received the invitation or offer it will not be an invitation to the public. Thus the offering of shares to the kith and kin of a director is not an invitation to the public to buy shares. The test is not who receives the circular but who can accept the offer put forward.

A private placement where the company's directors approach a few likely investors with request that they or other individuals whom they may introduce should subscribe for the company's securities is again not a prospectus. But a document addressed to the public even if it is in fact shown to one person only in the expectation that he will be willing to subscribe all the capital will be a prospectus and is deemed to be 'issued' when it is shown to that person.

Example : 3000 copies of a prospectus headed 'for private circulation only' were distributed to shareholders of gas companies. It was not publicly advertised. It was held that the prospectus was an offer of shares 'to thepublic', (Re South of England Natural Gas and petroleum Company Ltd. (1911) 1. Ch. 573).

A mere offer made to a person holding shares to purchase securities held by him is not a prospectus. But an offer by a company of rights shares to its shareholders with an option of renouncing them in favour of other persons is a prospectus.

When prospectus is not required to be issued(Sec.26)

The issue of a prospectus by a company is not necessary in the following cases.

(1) When an offer is made in connection with a bonafide invitation to a person to enter into an underwriting agreement with respect to shares

or debentures.

(2) When the shares or debentures are not offered to the public.

(3) Where the offer is made only to exiting members or debenture holders of the company with or without a right to renounce, e.g. when shares are placed privately to less than 50 persons.

(4) Where the shares or debentures offered are in all respects uniform with shares or debentures previously issued and dealt in or quoted on a recognised stock exchange.

(5) Where invitation to the public for subscription to the shares or debentures of a company is made in the form of newspaper advertisement.

(6) A private company is not required to issue prospectus.

Form of application to be accompanied by a Memorandum containing salient features of a prospectus

No one shall issue any form of application for shares in or debentures of a company unless the form is accompanied by a memorandum containing such salient features of a prospectus as may be prescribed. A copy of the prospectus would, however, be furnished by the company on demand made by a person before the closing of the subscription list.

It is now not necessary to furnish a copy of the prospectus along with every application form which the company may issue while inviting the public to purchase or subscribe for its shares or debentures. If each application form is to be accompanied by full prospectus, the cost of issue may become exorbitant, because of the expenditure involved in printing and posting the prospectus. In future, application form is to be accompanied only by a gist of material information. This is referred to as 'memorandum' containing salient features of a prospectus as may be prescribed. (Section 26).

15.2 OBJECTIVES

After going through this lesson, you should be able to:

- Recognize the meaning of prospectus
- Legal relation interms of prospectus
- Describe the issue of share capital
- Distiniguish between different kinds of shares
- Explain its important features.

15.3 LEGAL REQUIREMENTS IN RELATION TO A PROSPECTUS

(1) Dating of prospectus (Section 26)

A prospectus issued by a company must be dated. Section 26 further provides that the date on the prospectus shall, unless contrary is pvovide, be taken as the date of the publicaton of the prospectus. This ensures a prima facie evidence of the date of its publication. However, this evidence may be rebutted by a contrary evidence.

(2) Registration of prospectus [Section 27(7)]

(i) **Nature**: A prospectus must not be issued unless a copy thereof has been delivered to the Registrar for registration.

(ii) **Time Limit** : Registration must be made on or before the publication of the prospectus.

(iii) **Signatures** : The copy sent for registration must be signed by every person who is named in the prospectus as a director or a proposed director of the company or by his agent duly authorised in writing.

(iv) **Date of issue of prospectus** : The date of issue of prospectus is the date on which the prospectus first appears as a newspaper dvertisement.

(v) **Contents** : Prospectus should-

(a) State that a Copy thereof has been delivered to ROC for registration,

(b) Specify documents endorsed or attached to the copy so delivered, and

(c) Contain an endorsement that the consent of Experts has been obtained .

(vi) Enclosures

(a) Consent of the Expert to the Issue of Prospectus, where it contains a Report by an Expert,

(b) Copy of every material contract appointing or fixing remuneration of a MD or Manager.

(c) Copy of every other material contract. However, the following need not be enclose-Contract entered into in ordinary course of business, or-Contract entered into more than 2 years before the date of Prospectus.

(d) Written statement from Auditors relating to the adjustments to figures of abridged Financial Statements along with reasons therefor.

(e) Consent of every person named therein as Auditor, Legal Adviser, Attorney, Solicitor, Banker or Broker of the Company/Intended Company to act in that capacity.

(vii) **Registration :** The prospectus must be issued within ninety days of its registration. If it is issued say 91 days after, it shall be deemed to be a prospectus a copy of which has not been delivered for registration.

(viii) **Penalty for non-registration of prospectus** : If a prospectus is issued without a copy thereof being delivered to the Registrar for registration or without the required documents or consent attached thereto, the

company and every person knowingly party to the issue of the prospectus, shall be punishable with fine which may extend to Rs 50000 which may extend to rupees three lakhs.

(ix) **Opening of subscription list** : Where a prospectus has been issued, no allotment of any shares shall be made until-

(a) The beginning of the 5th day after prospectus is first issued ; or

(b) Such later time as may be specified in the prospectus ; or

(c) The beginning of the 5th day after public notice is give u/s 62. Such day is referred to as 'date of opening of subscription list'.

Disclosures to be made (Section 26)

Section 26 of the Companies Act requires every prospectus to disclose the matters specified in Schedule II of the Act. The Schedule is divided into three parts.

When Registrar can Refuse registration(Sec.26)

The Registrar can refuse to register a prospectus if:

(a) it is not dated;

(b) it does not comply with the requirements of as to the matters and reports to be set out in it;

(c) it contains statements or reports of experts engaged or interested in the formation or promotion or management of the company.

(d) it includes a statement purported to be made by an expert without a statement that he has given and has not withdrawn his consent to the manner of its inclusion in the prospectus ;

(e) it does not contain the consent in writing of directors and copy

of the documents has not been filed or does not comply with the provisions of with regard to the fact that a copy of it has been filed with the Registrar;

(f) it is not accompanied by the consent in writing of the auditor, legal adviser, solicitor, banker or broker of the company if named in the prospectus to act in that capacity.

15.4 CONTENTS OF PROSPECTUS

A prospectus is the most important document since the intending investors base their decisions on the facts and figures furnished in the prospectus. It is the window through which a prospective investor can look into the soundness of a company's venture. In order to protect the interests of the investing public against the frauds of the promoters, the Companies Act requires every company issuing a prospectus to observe a large number of regulations. Failure to observe them is made punishable with fine or imprisonment or both. Hence, utmost care should be taken in drafting a prospectus.

Section 26 Of Companies Act, 2013 Read With Rule-3 Of Companies (Prospectus And Allotment of Securities) Rule , 2014

Under Section 26 and Rule 3 , every prospectus shall be dated and signed and shall disclose the following matters:

(a) MATTERS IN PROSPECTUS

(1) Names and addresses of the registered office of the company, company secretary, chief financial officer, auditors, legal advisors, bankers , trusties, if any underwriters and such other persons as may be prescribed;

(2) Dates of the opening and closing of the issue, and declaration about the issue of allotment letters and refunds within the prescribed time;

(3) A statement by the Board of Directors about the separate bank

account where all monies received out of the issue are to be transferred and disclosure of details of all monies including utilized and unutilized monies out of the previous issue in the prescribed manner;

(4) Details about underwriting of the issue;

(5) Consent of the directors, auditors, bankers to the issue, expert's opinion, if any, and of such other persons as may be prescribed;

(6) The authority for the issue and the details of the resolution passed therefore;

(7) Procedure and time schedule for allotment and issue of securities;

(8) Capital structure of the company in the prescribed manner;

(9) Main objects of public offer, terms of the present issue and such other particulars as may be prescribed;

(10) Main objects and present business of the company and its location, schedule of implementation of the project;

(11) **Particulars relating to-**

(a) Management perception of risk factors specific to the project;

(b) Gestation period of the project;

(c) Extent of progress made in the project;

(d) Deadlines for completion of the project; and

(e) Any litigation or legal action pending or taken by a Government Department or a statutory body during the last five years immediately preceding the year

of the issue of prospectus against the promoter of the company;

(12) **Minimum subscription**, amount payable by way of premium, issue of shares otherwise than on cash;

(13) **Details of directors** including their appointments and remuneration and such particulars of the nature and extent of their interests in the company as may be prescribed; and

(14) **Disclosures** in such manner as may be prescribed about sources of promoter's contribution;

(B) REPORTS IN PROSPECTUS

The prospectus must set out the following reports for the purposes of the financial information, namely:

(i) Reports by the auditors of the company with respect to its profits and losses and assets and liabilities and such other matters as may be prescribed;

(ii) Reports relating to profit and losses for each of the five financial years immediately preceding the financial year of the issue of the prospectus including such reports of its subsidiaries and in such manner as may be prescribed;

(iii) Reports made by the auditors upon the profits and losses of the business of the company for each of the five financial years immediately preceding issue and assets and liabilitiesof its business on the last date to which the accounts of the business were made up, being a date not more than one hundred and eighty days be before the issue of prospectus.

(iv) Reports about the business or transaction to which the proceeds of the securities are to be applied directly or indirectly.

(C) DECLARATION

The prospectus shall make a declaration about the compliance of the provisions of this act and a statement to the effect that nothing in the prospectus in con contracts to the provisions of this act, the securities contracts (Regulation) Act,1956(42 of 1956) and the Securities and Exchange Board of India Act ,1992(15 of 1992) and the rules and regulations made thereunder.

15.5 SHELF PROSPECTUS (section 31)

- It has been observed that many public financial institutions have approached the capital market more than once in the course of one year period.
- The concept of 'Shelf Prospectus' enacted in the Companies Act has come as a great relief to such institutions.
- According to Section 31, 'shelf prospectus' means a prospectus issuedby any company prescribed by SEBI(Under Rule 10)
- For one or more issues of the securities or class of securities specified in that document.
- Shelf prospectus enables public financial institutions and banks to raise capital from the public more than once without issue of a fresh prospectus every time.
- The shelf prospectus will be valid for a period of one year from the date of first issue of securities.

15.6 BOOK-BUILDING AND RED-HERRING PROSPECTUS (Section 32)

- Section 32 provides that in order to explore the demand for securities and price at which securities may be offered to the public, a public company, before issuing prospectus, circulates information memorandum and red-herring prospectus to the public.
- 'Red-herring prospectus' means a prospectus which does not have complete particulars on the price of the securities offered and the quantum of securities offered. Instead, it contains either the floor price of the securities

offered through it or a price band along with the range within which the bids can move.

- The applicants bid for the shares quoting the price and the quantity that they would like to bid at.
- Only the retail investors have the option of bidding at 'cut-off.
- Information memorandum containing material information regarding the issuer company but without the price structure can be circulated to the public prior to the filing of prospectus.
- But the red-herring prospectus is to be filed with Registrar of companies by unlisted public company and with SEBI by listed company at least three days prior to the opening of the offer.

Any variation between the information memorandum and the red-herring prospectus shall be high lighted by the issuer company and individually intimated to the person invited to subscribe.

Not to encash advance subscription. Any advance subscription for securities (by way of cash or post dated cheques or stock invest), if already received by the issuing company, shall not be encashed until-

- Such variation is individually intimated to the proposed investors ; and
- The company has offered an opportunity to the proposed investors to withdraw their applications and cancel the subscription moneys paid.

Withdrawal of applications. A proposed investor may withdraw his application within 7 days of receipt of intimation given by the company.

Upon closing of the offer, a final prospectus stating the total capital raised, closing price of the security and any other details which were not complete in the red-herring prospectus shall be filed-in the case of a listed public company, with SEBI and the Registrar of Companies, and in any other case, with the Registrar of Companies alone. The object of this new provision is to enable the issuers to take the book-building route to determine the quantum of securities to be issued, as

also a realistic price. This could be beneficial to the issuer company.

15.7 DEEMED PROSPECTUS (Section 25) : A company may instead of offering its shares or debentures for sale to the public allot its shares or debentures to an intermediary called 'issuing house'. Thereafter the 'issuing house' offers them for sale to the public by advertisement or circular of its own. The document by which the offer is made to the public by the issuing house is deemed for all purposes to be a -prospectus' issued by the company. The main reason for using an offer for sale through issuing house is that the company saves underwriting expenses and in addition it obtains the expertise of the issuing house.

When applications are received by the issuing house, it renounces its interest in the shares or debentures to the extent of the number of shares or debentures allotted to the applicant. In this case the applicant becomes allottee of the company.

All enactments and rules of law as to the contents of the prospectus and to liability in respect of statements and omissions from the prospectus shall apply to such a document. The object of these provisions is to check the company from evading the provisions of the Act relating to the issue of a prospectus.

In the absence of evidence to the contrary an allotment or agreement to allot shares or debentures is deemed to have been made with a view to them being offered for sale to the public if:

(i) the offer for sale is made within six months after the allotment or agreement to allot; or

(ii) at the date when the offer for sale is made, company has not received from the issuing the whole of the consideration it is to receive for the shares or debentures. [Section 25(2)]

The offer for sale must contain :

(a) all matters required to be stated in prospectus ;

(b) the net amount of the consideration received or to be received

by the company in respect of the shares or debentures to which the offer relates; and

(c) the place and time at which the contract under which the said shares or debentures have been or are to be alloted, may be inspected .

The persons making the offer of sale to the public are to be deemed directors of the company for the purpose of registration of the prospectus .

The document containing the offer for sale must be signed on behalf of the company or firm by two directors of the company or by not less than one half of the partners in the firm, as the case may be .

Statement of experts

The expression 'expert' includes an engineer, a valuer, an accountant and any other person whose profession gives authority to a statement made by him. [Sec. 2(38)]

1. Expert to be unconnected with the formation or management of the company. The report of an expert cannot be included in a prospectus if he is in any way connected with the formation or promotion or management of the company. (Section 26).

2. Expert's written consent to the issue of the prospectus containing his statement. A prospectus including a statement purporting to be made by an expert shall not be issued, unless-

(a) he has given his written consent to the issue of the prospectus and has not withdrawn such consent before the delivery of the copy of the prospectus to the Registrar for registration; and

(b) a statement that he has given and has not withdrawn his consent as aforesaid appears in the prospectus.

It is a sound rule designed to protect intending investors by making the 'expert' a party to the issue of the prospectus and making him liable for untrue

statements.

Penalty for contravention .If any prospectus is issued in contravention of section 26, the company and every person who is knowingly a party to the issue thereof, shall be punishable with fine which may extend to fifty thousand rupees and can extend to Rs3 lakh.

15.8 SHARE CAPITAL

In order to finance its activities the company needs to have capital. The words 'capital' and 'share capital' are synonymous in the case of a company. Share capital means the capital raised by a company by the issue of shares.

Share capital can be raised either at the time of formation of the company for starting business operations or later on, for further expansion or diversification of the business. But once raised, share capital becomes a permanent liability of the company and, except in the case of redeemable preference shares, can be returned or repaid only at the time of winding up.

The memorandum of association of every limited company must state the amount of share capital with which the company is to be registered and the division thereof Into shares of a fixed amount. An unlimited company and a company limited by guarantee may not have a share capital.

The word 'capital' has several different meanings. It may mean the nominal, issued, paid-up or reserve share capital of the company.

1. **Nominal, Registered or Authorised Capital [Sec 2(28)]**: The nominal or authorised capital is the amount of share capital which a company is authorised to issue. The amount is set out in the memorandum in the case of companies limited by shares or companies limited by guarantee and having a share capital. This is the maximum amount which a company is authorised to raise by the issue of shares and upon which it pays stamp duty and registration fees. Nominal capital is divided into shares of a fixed amount. The amount of the company's nominal capital depends on itsbusiness requirements. Nominal capital can be

increased or reduced by following the prescribed procedure.The whole of the nominal capital may be issued and subscribed and sometimes paid up, or only a portion of its nominal capital may be applied for and allotted.

2. Issued Capital [Sec 2(50)] : It is that part of the nominal capital which is actually issued by the company for public subscription. A company is not obliged to issue all its nominal capital at once. It may have unallotted residue to be alloted in the near future as and when the company needs further capital. The difference between the nominal and the issued capital is known as the 'unissued capital'. The issued capital can never be more than the nominal capital. It can at the most be equal to the nominal capital; it can so happen when all the shares have been issued to the public.

3. Subscribed Capital [Sec 2(86)] : It is the total amount of the nominal value of shares which have been actually taken up, i.e., subscribed for by the public. It is that type of the nominal capital which has actually been taken up by shareholders who have agreed to give consideration in cash or kind for the shares issued to them. The subscribed capital is thus a reality. Where the shares issued for subscription are wholly subscribed for, issued capital would mean the same thing as 'subscribed capital'.

4. Called up. Capital : It is that amount of the nominal value of shares subscribed for, which the company has asked its shareholders to pay by means of calls or otherwise.

5. Paid-up Capital : The paid-up capital is that part of the issued capital which has been paid up by the shareholders. The money received on each share is result of calls is said to be paid-up and the total amount that has been paid upon the company's shares is the paid-up capital which can never exceed the issued capital.

6. Uncalled capital : This is the amount which remains uncalled on shares.The company may, at any time, call upon the shareholders to pay the uncalled capital in accordance with the provisions of the articles. When shares

are fully paid there is no uncalled capital.

7. Reserve Capital : A company may resolve by special resolution that part or the whole of the uncalled capital shall not be called upon except in the event of winding up. This amount is called 'the reserve capital' or 'the reserve liability.' The Companies Act deals with the question of reserve capital. Reserve capital cannot be turned into ordinary capital without leave of the court and it cannot be dealt with or charged by the directors. Thus, where a company issued debentures charging its undertaking including the uncalled capital, the charge will not be operative on the reserve capital. It can not also be cancelled by a reduction of capital. It is available only for the creditors on the winding up of the company and is thus a kind of guarantee for them.

Reserve capital should be distinguished from a reserve or Reserve fund'. The latter expressions are applied to undistributed profits. Such reserves can be spent, charged or divided among share-holders at the company's discretion.

Publication of capital

Any notice, advertisement, official publication, business letter, bill head or letter paper which mentions the authorised capital of the company must also mention in equal prominence the subscribed and paid-up capital of the company. On a default being made, the company and every officer of the company in default shall be punishable with fine which may extend to ten thousand rupees.

The provision is incorporated so that the company may not mislead the public by showing an impressive figure as authorised capital but having very little paid-up capital.

15.9 CLASSES OF CAPITAL

Section 43 of the Companies Act, 2013 prescribes that Share capital of a company can be of two types or classes namely, equity and preference:

(a) equity share capital

(b)preference share capital.

While a company may issue equity share capital with differential rights as to dividend, voting or otherwise, no preference capital with any such differential rights could be issued.

a) **Preference share capital** : It is the sum total of preference shares. These shares carry the following preferential rights over equilty shares.

(i) as regards dividends, to be paid a fixed amount or an amount calculated at a fixed rate ;

(ii) on winding up of the company, repayment of capital paidup.

b) **Equity share capital** : It means all share capital which is not preference share capital. It may be noted that while a company can have only equity share capital, but it cannot have only preference share capital. As per the definition of 'preference share capital' in Section 85, preference shareholders have certain preferential rights over the equity shareholders. Thus in the absence of equity share capital, there cannot be preference share capital.

15.10 ALTERATION OF CAPITAL

A company limited by shares may in general meeting, if so authorised by its articles, alter the conditions of its memorandum relating to share capital in order to :

(a) increase its share capital by issuing new shares ;

(b) consolidate and divide all or any of its share capital into shares of larger amount than its existing shares ;

(c) convert all or any of its fully paid-up shares into stock or reconvert that stock into fully paid-up shares of any denomination ;

(d) sub-divide its shares into shares of smaller amount than is fixed

by the memorandum, provided the paid-up amount will remain at the same proportion to the unpaid amount of the shares;

(e) cancel shares which have not been taken by any person and diminish the amount of its share capital.

Any of the above alterations of capital may be effected by an ordinary resolution by the shareholders in general meeting.

No sanction or confirmation of the National Company Law Tribunal is required for this alteration. Within 30 days of passing the resolution for alteration of share captiai, notice must be given to the Registrar who shall thereupon make necessary changes in the company's memorandum or articles or both. On failure to give notice to the Registrar, the company and every officer in default shall be liable to a fine which may extend up to five hundred for every day during which the default continues.

A notice to the Registrar shall also be given by a company when redeemable preference shares have been redeemed or where its share capital has been increased beyond the authorised capital. A company having no share capital shall inform by similar notice any increase in its membership

The power of alteration must be exercised bona fide in the interests of the company and not for benefitting any group.

15.11 REDUCTION OF CAPITAL

The share capital of a company is the only security on which the creditors rely. Any reduction of capital, therefore, reduces the fund out of which they are to be paid. Reduction of capital means reduction of issued, subscribed and paid up capital of a company. The capital of a company cannot be reduced unless all the formalities as laid down in the Companies Act are complied with.

A company may wish to reduce its capital for a number of reasons, namely-

1. The capital of the company may be more than enough for its needs, and so, it may return the surplus capital to the shareholders.

2. The paid-up capital of the company is sufficient and it may refrain from calling up the unpaid portion of share money.

3. Some of the capital may in fact have been lost or diminished

Reduction under item (1) or (2) above will reduce the funds available to the creditors. Reduction under item (3) affects the rights of different classes of shareholders as well as the interest of the members of the public who may be induced to take shares in the company.

Reduction of capital may be effected in several ways which may be classified under two heads.

1. Reduction without the consent of the Tribunal : There are a number of cases where a company may reduce its capital without the sanction of the Tribunal.

(a) Where redeemable preference shares are redeemed in accordance with the provisions of the companies act 2013.

(b) Where unissued shares are cancelled.

(c) Where any shares are forfeited for non-payment of calls.

(d) Where there is a surrender of shares or a gift is made to the company of its own shares.

(e) The company may purchase its own shares under the Companies Act.

(f) The Tribunal may, order the purchase of the shares or interest of any members of the company by the company.

In all these cases the procedure laid down under the Companies Act is not required to be followed.

2. Reduction with the consent of the Tribunal : gives a company limited by shares or a company limited by guarantee and having a share capital the power to reduce its share capital in any way. The Act has not prescribed the

manner in which the reduction is to be carried out, nor has it prohibited any method of effecting that object.

The reduction of capital can only be made-

(i) if authorised by its articles,

(ii) by passing a special resolution,

(iii) which is confirmed by the Tribunal.

The following three modes in particular, without in any way affecting the various other ways by which a company may reduce its share capital :-

(1) By extingushing or reducing the liability of members for unpaid capital,

(2) By writing off lost or unwanted capital. This is the most common method of reduction of capital.

(3) By paying off capital which is in excess of the needs of the company with or without reducing members' liability (i.e. by refunding a portion of the paid up capital).

Illustrations of the third mode of reduction of share capital are-

(1) Payment of dividend out of paid up share capital.

(2) Purchase by the company of its own shares.

Procedure for reducing share capital

The procedure for reducing the share capital of a company is as follows:

1. Special resolution. A company shall pass a special resolution for reduction of share capital.

Power to reduce share capital must be given in the articles, it is not sufficient if memorandum of the company confers such power to reduce. If the articles do not contain any provision for reduction of capital, the articles must first be altered so as to give the power and then the resolution for reducing the capital must be passed.

2. Application to the Tribunal. After having passed the special resolution for reducing the share capital, sanction of the national Company Law Tribunal shall be obtained by the company for an order confirming the reduction.

The object of requiring this sanction is three-fold: (1) To protect persons dealing with the company so that the funds available for satisfying their claim shall not be diminished except by ordinary business risks. (2) To ensure that the reduction is equitable as between the shareholders of the company.

3 To protect the interest of the public.

3. Substituted by the Companies Act 2013

Interests of the creditors : The primary duty of the Tribunal is to look after the interests of creditors. Creditors are entitled to object if the reduction of share capital involves (a) reduction of liability in respect of uncalled capital, (b) payment to any share holder of any paid-up capital and (c) in any other case if the court (now Tribunal) so directs.

However, it may be noted that only such creditors are entitled to object to whom the company owes a debt which would have been provable in the winding up of the company. The creditors have, however, no right to object to the proposed reduction of capital where no asset out of which their claims could be satisfied is being given up or returned to the shareholders.

The Tribunal shall settle a list of creditors who may object to such reduction. The Tribunal may publish notices fixing a day or days within which the creditors not entered on the list or to claim to be so entered or are to be excluded from the right of objecting to the reduction.

Under special circumstances, the Tribunal may sanction such reduction without settling the list of creditors or without securing the debt of any creditor.

Where the Tribunal is satisfied that the interests of the creditors have

been secured, it may confirm the reduction on such terms and conditions as it may think fit. The Tribunal may, at the time of confirmation, direct the company to add to its name the words 'and reduced' for a specified period and these words will be deemed to be part of the company's name for such specified time. The Tribunal may also make an order requiring the company to publish the reasons for such reduction for the information of the public.

The addition of the words 'and reduced' is required in order to give warning to the public of the financial position of the company.

The object is to give public notice that the company had once a larger capital and had reduced it.

Interests of the shareholders. The second duty of the Tribunal is to protect the interests of the shareholders. The proposed scheme of reduction must be reasonable and fair between all the classes of shareholders in the company.

If the scheme of reduction is unfair and would work injustice between the different classes of shareholders, it will not be sanctioned by the Tribunal. Thus, where under a scheme of reduction the whole burden of the loss was thrown upon the ordinary shareholders and as such was not fair between the ordinary shareholders and the preference shareholders, the Tribunal refused to sanction the scheme.

The question of reducing the capital is a domestic affair to be decided by the majority, but this power must be exercised in fair and equitable manner.

Example : A company reduced its capital by paying back the preference stock. The power to pay of the preferential stock was in the articles. Yet the reduction was opposed by some preference stock-holders on the ground that it deprived them of the advantage of their investment. It was held that the proposed reduction was not unfair because even without it the preference stock holders would not be entitled to anything more than the return of their paid-up capital. [Scottish Insurance Co. v. Wilson and Clyde Coal Co. (1949) AC 462).

3. Registration of the order of Tribunal with Registrar

The company shall deliver to the Registrar a certified copy of the Tribunal order and a minute approved by the Tribunal showing the following details for registration-

(a) the amount of the share capital ;

(b) the number of shares into which it is to be divided ;

(c) the amount of each share; and

(d) the amount, if any, at the date of registration deemed to be paid-up on each share.

The Registrar will, thereupon register the order and the minute. On such registration, the resolution for reducing the capital takes effect. Notice of the registration shall be published in such manner as may be directed by the Tribunal.The Registrar shall certify the registration of the order and the minute under his hand. Such certificate shall be conclusive evidence that all the requirements of the Act have been complied with.

The reduction takes effect as from the date of registration by the Registrar. The minute when registered is deemed to be substituted for the corresponding part of the memorandum of association and is deemed to be an alteration of the memorandum of association and such alteration shall be noted on every copy of the memorandum issued after the date of registration.

If any officer of the company knowingly conceals the name of any creditor entitled to object, or knowingly misrepresents the amount or nature of his claim or debt or is party to such concealment or misrepresentation, he will be liable to imprisonment upto one year or fine or both.

Liability of members on reduction : On reduction of capital, the members of a company whether present or past are not liable beyond a certain limit. The liability of the members is limited to the difference, if any, between the amount of the share as fixed by the minute and the amount paid up in respect of

the shares and the amount to which the shares are finally reduced as a result of reduction of capital i.e. the amount payable by any member is reduced to the difference between the amount paid up and the amount reduced. If the company is unable to pay the claim of any creditor entitled to object who was ignorant of the proceedings for reduction or of their nature and effect and who was not entered on the list of creditors then-

(a) every member of the company at the date of the registration of the order for reduction will be liable to contribute for the payment of the claim an amount not exceeding the amount, which he would have been liable to contribute if the company had commenced to be wound up on the day before that registration; and

(b) if the company is wound up, the Tribunal on the application of such creditor may settle a list of members so liable to contribute and enforce calls on them as if they were ordinary contributories in a winding up. (Section 104).

15.12 SHARES

Definition of share : A 'share' in a company denotes rights and obligations. It is the interest of a shareholder in a definite portion of the capital. It expresses a proprietory relationship between the company and the shareholder. A shareholder is the proportionate owner of the company but he does not own the company's assets which belong to the company as a separate legal entity. According to section 2(46) a share means, "A share in the share capital of a company and includes stock except where a distinction between stock and shares is expressed or implied." An exhaustive definition of share has been given by Farwel! J. in Borland's Trustee v. Steel Bros, in the following words :

"A share is the interest of a shareholder in the company, measured by a sum of money, for the purpose of liability in the first place, and of interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders inter se in accordance with the Companies Act."

The Supreme Court of India has approved the above definition of share

in the Commissioner of Income-tax v. Standard Vacuum OH Company wherein it has observed, "By a share in a company is meant not any sum of money but an interest measured by a sum of money and made up of diverse rights conferred on its holder by the articles of the company which constitute a contract between him and the company." Thus, a share (i) measures the right of a shareholder to receive a certain proportion of the profits of the company when it is a going concern and to contribute to assets of the company when it is being wound up; and (ii) forms the basis of the mutual covenants contained in the articles binding the shareholders inter se.

A share is a persona! estate capable of being transferred in the manner laid down in the articles of association. It is a movable property which can either be mortgaged or pledged. Share is included in the definition of 'goods' under the provisions of the Sale of Goods Act, 1930.

On the basis of above discussion, the nature of share can be summed up as under.

1. Share gives some rights and liabilities to the holder.

2. Shareholder is not a part owner of the company or property of the company.

3. The share is a movable property. The movable property of a person can be a 'chose in action' or chose in possession. Share is chose in action.

4. Share is 'goods'.

According to section 83, every share issued by a company must be numbered so that one share may be distinguished from another share. However this provision will not apply to the shares held with a depository. A certificate of shares issued by a company under its common seal specifies the shares held by any member.

15.13 STOCK AND SHARES

Stock is a different concept When shares are fully paid up, they may be

converted into stock. Stock is simply a set of shares put together in a bundle. Stock is expressed in terms of money and not as so many shares. It is the aggregate of fully paid shares legally consolidated. The aggregate can be split up into fractions of any amount without regard to the original nominal value of shares. The issue of partly-paid up stock is invalid.

A company limited by shares, may, if so authorised by its articles, convert all or some of the fully paid-up shares into stock or reconvert its stock into fully paid up shares of any denomination. A company cannot issue stock directly but can only convert fully paid-up shares into stock. The company shall give notice to the Registrar of such conversion within 30 days of its doing so. When shares are converted into stock, the register of members must show the amount of stock held by each member. Further, the annual return must state the amount of stock held by each member. Stock certificates, similar to share certificates, must be issued.

Stock is transferable like share. The Board may, however, fix the minimum amount of stock transferable. The holders of the stock have according to the amount of stock held by them the same rights, privileges and advantages as regards dividends, voting at the meetings of the company and other matters as if they held the shares from which the stock arose.

EFFECT OF CONVERSION OF SHARES INTO STOCK (SECTION 96).

Where a company having a share capital has converted any of its shares into stock, and given notice of the conversion to the Registrar, all the provisions of this Act which are applicable to shares only shall cease to apply as to so much of the share capital as is converted into stock.

Stock and shares distinguished. The main points of distinction between the two are as under.

1. A share is one of a number of individual units into which the capital of a company is divided. Stock is the capital in the form of a fund which may be divided into any desired amount. Thus, shares are in units, whereas

stock is in lump holding.

2. Shares may be partly or fully paid-up, but stock must be fully paid.

3. Shares can be issued directly but stock cannot be issued directly.

4. Share has a nominal value, whereas stock has none.

5. Shares must bear distinctive numbers, while stock is never numbered.

6. Shares are of equal denomination while stock may be split into unequal amounts.

7. Shares cannot be transferred in fractional amount; stock can be transferred in any fraction although the articles may provide the minimum fractional amount of stock which can be transferred.

As regards voting rights, the holders of the stock can vote in the same way as if the stock represented a defined number of shares of corresponding amount taken at nominal value.

15.14 KINDS OF SHARES

Section 86 has been substantially changed by the Companies (Amendment) Act, 2000. The share capital of a company will continue to be of two kinds, namely, equity and preference. But equity shares have been subdivided into two categories, namely, shares with equal rights and shares with differential rights.

a) **Equity shares** : All shares which are not preference shares are equity shares. Equity shareholders have the residual right of the company. They may get higher dividend than preference shareholders if the company is prosperous or get nothing if the business of the company flops. It is pertinent to note that the amended Section 86 of the Act empowers companies to issue equity shares without voting rights subject to the rules and terms and conditions that may be prescribed.

With respect to issue of shares with differential voting rights, the Department of Company Affairs has notified Companies (Issue of share capital

with differential voting rights) Rules, 2001.

These rules provide :

(i) Shares with differential voting rights, including non-voting shares, shall be allowed to the extent of 25 percent of the total issued share capital.

(ii) The Company must have distributable profits, as per section 205, in the three years preceding such issue.

(iii) Equity capital with regular voting rights will not be allowed to be converted into shares with differential voting rights and vice-versa.

(iv) Issue of such shares shall have to be approved by the shareholders through resolution in a general meeting. A listed company may obtain the shareholders approval through postal ballot.

(v) The notice of the general meeting must give the prescribed details by way of explanatory statement.

(vi) A company which has defaulted in filing annual returns during the precedi ng three years or has failed to repay its deposits or interest there on on duedate or redeem debentures on due date or pay dividend shall not be eligible to issue shares with differential rights.

(vii) A company should not have defaulted in addressing investors' grievances.

(viii) The issue of such shares should be permissible under the Articles of association of the company.

(ix) The company should not have been convicted of any offence under :

(a) Securities and Exchange Board of India Act, 1992 ;

(b) Securities Contracts (Regulation) Act; 1956 ; and

(c) Foreign Exchange Management Act, 1999.

(x) Members holding equity shares with differential rights shall be entitled to bonus and rights issue of the same class.

(b) **Preference shares :** Preference shares. A preference share must satisfy

the following two conditions:

(i) It shall carry a preferential right as to the payment of dividend at a fixed rate ; and

(ii) In the event of winding up, there must be a preferential right to the payment of the paid up capital.

These are two dominant characteristics of preference shares. A preference share may or may not carry such other rights as-

(a) a preferential right to any arrears of dividend ;

(b) a right to share in surplus profits by way of additional dividend :

(c) a right to be paid a fixed premium specified in the memorandum ; and

(d) a right to share in surplus assets in the event of a winding up, after all kinds of capital have been repaid.

Before there can be preference shares there must be at least two kinds of shares in which one class is given preferential treatment over the other. Where there is only one class of shares, there is no question of preferential treatment of one class of shareholders over another in the matter of dividends.

1) Kinds of preference shares : Following are the various kinds of preference shares :

1. Cumulative and non-cumulative preference shares : With regard to the payment of dividend, preference shares may be cumulative or non-cumulative. In the case of cumulative preference shares, if the profits of the company in any year are not sufficient to pay the fixed dividend on the preference shares, the deficiency must be made up out of the profits of subsequent years. The accumulated arrears of dividend must be paid before anything is paid out of the profits to the holders of any other class of shares. In the case of non-cumulative preference share, the dividend is only payable out of the net profits of each year. If there are no profits in any year, the arrears of dividend cannot be

claimed in the subsequent year. Preference shares are presumed to be cumulative unless expressly described as non-cumulative.

2. Participating and non-participating preference shares : Participating preference shares are those shares which are entitled, in addition to preference dividend at a fixed rate, to participate in the balance of profits with the equity shareholders after they get a fixed rate of dividend on their shares. The participating preference shares may also have the right to share in the surplus assets of the company on its winding up. Such a right must be expressly provided in the memorandum or the articles of association of the company.

Non-participating preference shares are entitled only to a fixed rate of dividend and do not share in the surplus profits. The preference shares are presumed to be non-participating unless expressly provided in the memorandum or the articles or the terms of issue.

3. Convertible and non-convertible preference shares : Convertible preference shares are those shares which can be converted into equity shares within a certain period. Those shares, which do not carry the right of conversion into equity shares, are called non-convertible preference shares.

4. Redeemable preference shares : According to section 80, a company limited by shares, if so authorised by its articles, may issue redeemable preference shares. Such shares may be redeemed either after a fixed period or earlier at the option of the company. In the case of irredeemable shares, the capital is to be returned on the winding up of the company.

The redeemable preference shares can be redeemed, only subject to the following conditions :

(i) Such shares must be fully paid.

(ii) Such shares shall be redeemed out of distributable profits or

out of the proceeds of a fresh issue made for the purposes of redemption.

(iii) Any premium to be paid on redemption of such shares must be paid out of profits or out of the securities* premium account.

(iv) Where shares are so redeemed out of profits, a sum equal to the nominal value of the shares redeemed must be transferred to the 'Capital Redemption Reserve Account'. This amount shall be treated as capital of thecompany and the provisions as regards reduction of capital shall apply.

No company limited by shares shall, after the commencement of the Companies (Amendment) Act, 1996, issue irredeemable preference shares or redeemable preference shares which are redeemable after 20 years of its issue. (Section 80(5A)).

Where a company fails to comply with these provisions, the company and every officer of the company who is in default shall be punishable with fine which may extend to ? 10,000.

Redemption of redeemable preference shares shall be notified to the Registrar within one month of redemption (Section 95). Where redeemable preference shares have been issued, the balance sheet must contain a statement specifying what part of the capital consists of such shares and the earliest date on which the company has power to redeem the shares. (Schedule VI).

Basis	Preference Shares	Equity Shares
Definition	Shares that carry a Preferential Right as to payment of - (a) Dividend and (b) Repayment of Capital.	Shares that are not Preference Shares are called Equity Shares.
Return	Preference shares are more like debentures than like equity shares. Preference shares are	The rate of dividend on equity shares depends upon the

	entitled to a fixed rate of dividend as debentures carry a fixed rate of interest.	amount of profits available.
Priority	Dividend on the preference shares is paid in priority to the equity shares.	The dividend on equity shares is paid only after the preference dividend has been paid.
Repayment of Capital	The preference shares must be fully repaid first.	The equity shares rank behind the preference shares for repayment of capital on winding up.
Arrears of	Dividend Generally accumulates unless specifically said to be non-cumulative.	No accumulation of Unpaid Dividend. No Profits means no Dividend payable to equity shareholders.
Voting Rights	The voting rights of preference shareholders are usually restricted.	An equity shareholder can vote on all matters affecting the company. However, Section 86 of the Companies Act as amended by the Companies
Preference Shares compared with Equity Shares		
		(Amendment) Act, 2000 empowers companies to issue equity shares without voting rights.

Bonus Shares or Right Shares	Bonus shares or Right shares are are usually not allowed to the preference shareholders.	A company may issue bonus or Right shares to the company's existing equity shareholders.
Redemption	Redeemable preference shares are redeemed by the company on the expiry of the stipulated period. .	But equity shares cannot be redeemed But now buy back is permitted u/s 77A.
Control and management	No right to take part in management Management	Equity Shareholders the real owners, hence have a right to control the of Company.

15.15 SUMMARY

In this lesson ,a detailed discussion has been done on prospectus and share capital of a company. One great advantage of a floating a company is the raising of capital required for business from the general public and this is done by issuing a document called prospectus. Along with prospectus an elaborative discussion has also been made on share capital , shares and different types of shares.

15.16 GLOSSARY

Shares: 'Share ' means a share in the share capital of a company and includes stock.Allotment money: the amount payable on allotment is called allotment money Capital reserve: it is reserved carried out of capital profitForfeiture of share: cancellation of share.

Par value: par value means the Nominal or Face value of a share

Amendment: A minor changes designed to improve.

15.17 SELF ASSESSMENT QUESTIONS

1. What is a share ? Discuss the various kinds of the share capital? How is the preference share capital distintinguished from equity share capital?

2. Explain different methods by which a company can alter its share capital.

3. How and under what circumstances can a company reduce its share capital? Discuss the relevant procedure for the reduction of share capital?

4. What is a prospectus? Is the issue of prospectus compulsory on the part of a company?

5. Explain the legal provisions relating to issue and registration of a prospectus.

6. Indicate in detail the steps a public company has to take for raising additional equity capital. Can new shares be offered by a company to outsiders without offering the same first to the existing shareholders ? If so, state the circumstances underwhich it can be done.

7. How and in what circumstances can a company reduce, increase and reorganise its share capital ?

8. Discuss the voting rights of the members in a public company limited by shares both with reference to equity and preference share capital.

9. Under what circumstances may the Central Govt, order conversion of debentures or loans into shares ? What remedy is available to a company if the terms and conditions of such conversion are not acceptable to it ?

10. Explain the procedure for increasing, re-organising and reducing the share capital of a company ?How and under what circumstances can a company reduce its share capital?

11. Discuss the relevant procedure for the reduction of share capital. 7. How can the share capital of the company be reduced ? What is the liability of the members in respect of reduced shares ?

15.18 LESSON END ACTIVITIES

1. What is a prospectus? who are liable for misstatement in a prospectus? Explain the civil and criminal liability for such mis- statements?

Ans. _____

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2. What do you mean by share capital of a company ?

Ans. _____

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3. What is the difference between issued and subscribed capital ?

Ans. _____

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4. What do you mean by reserve capital ?

Ans. _____

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5. Distinguish between capital reserve and reserve capital ?

Ans. _____

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6. Discuss the various kinds of the share capital. How is the preference

share capital distinguished from equity share capital ?

Ans. _____

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7. Explain fully the different methods by which a company can alter its share capital.

Ans. _____

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8. What are the different kinds of shares which a company can issue under the Companies Act, 2013 ? What are the provisions regarding further issue of share capital ?

Ans. _____

_____

_____

_____

15.19 SUGGESTED READINGS

1. Corporate laws by K.C..Garg. Vijay Gupta and Joy Dhingra
2. Company Law by K.C Garg,Vijay Gupta, Poonam Gupta and R.C Chawla
3. Company law by N.D Kapoor
4. Indian Company Law by Avtar Singh
5. Business law in India by Surajit Sen Gupta.

LEGAL ASPECTS OF BUSINESS

SEMESTER : I **UNIT-IV**

PAPER -IV **LESSON-16-20**

E-FILING, COMPANY LAW IN COMPUTERISED ENVIRONMENT, DIGITAL SIGNATURE CRRTIFICATE DIN, CIN , LIMITED LIABILITY PARTNERSHIP ACT, 2008

OBJECTIVES

- The lesson will help you to
- Understand the concept of E-filing
- Explain Company Law in a computerised environment
- Understand the concept of Director Identification Number
- Explain the concept of Corporate Identification Number
- Understand the concept and formation of Limited Partnership

STRUCTURE

4.1 INTRODUCTION

One of the major challenges facing consultants today is maintaing a level of knowledge of leading and emerging technologies, beyond the superficial or buzz word level. We need to develop a level of understanding that allows us to communicate effectively with both suppliers and customers . One would then be able to demonstrate his knowledge of the business issues being addressed; the application of technology to provide solution & the business benefits for the customer. Private companies and government agencies all around the world make huge investments for the automation of their process and in the management of the electronic documentation. The main requirement in the management of digital documentation its quivalence, from a legal perspective, to paper work, affixing a signature on a digital document is the fundamental principle on which are based the main processes of authorization and validation. Many benefits for the introduction of digital signing process are cost reduction &complete automation of documental work flow, including authorization and validation process. In scenario of e-filing, Director identification number will be a pre-reuisite for filing of certain company related documents. DIN is a unique identification number for an existing director or a person intending to become the director of a company. Corporate identity number (CIN) has been designed to

help easily companies belonging to a state ,industry ,ownership or age. It will be 21-digitnumber. More over,

Recently most entrepreneurs have started opting for limited liability partnership, considering it has most positive features of partnership and companies. It is hybrid from which incorporates benefits of both partnership and companies such as separate legal entity ,less cost of formation, limited liability of each partner etc.

4.2 CONCEPT AND MEANING OF E-FILING

The process of using a computer program to transmit information electronically to another party is called E-filing. This allows the user to complete and submit the information in a timely fashion. The electronic filing system prevents the user from making small mistakes by alerting them if something does not register correctly. A large majority of federal and state revenue departments offer citizens the ability to file yearly tax returns using an electronic filing system. The Internal Revenue Service provides this service free of charge for federal tax returns. E-filing is the electronic submission of information that is required by law. It is up to the regulating agency to decide the criteria for what types of information must be filed electronically and what types of information can be submitted in hard copy form. Since e-filed returns can be processed much faster than paper returns, the taxpayer can generally expect a faster tax refund, if applicable. The benefits of e-filing have made it increasingly popular in recent years. E-filing saves the tax agency time and money, because the tax data is transmitted directly into its computers, significantly reducing the possibility of keying and input errors.

One of the biggest advantages of e-filing is speed. Returns are processed in a staggeringly fast 24-28 hours if you're working digitally, while a mailed return has to plod along and sit on a few shelves. This means that a refund for an e-filed tax return is paid right quick; the IRS estimates nine out of 10 taxpayers see a refund in less than 21 days if e-filing [source: Greene-Lewis]. You are also assured your return is being processed if you're using e-file; use the mail and

you're crossing your fingers it got to the IRS, unless you're paying for a certified service. But not everyone agrees that e-filing is going to leave you less vulnerable to an audit. The IRS uses an algorithm to watch for red flags on returns; time doesn't allow for every handwritten form to go through it. Of course, it's pretty simple to run each and every digital return through the math. Some would even argue that the big speed advantage is working for the IRS and not the taxpayer: Although you get your refund sooner, don't forget that means that they're immediately scouring your finances. In a lot of ways, e-filing will save you time, but whether that saves money by avoiding an audit is still a bit of a mystery.

ADVANTAGES OF E-FILING

• There are also advantages to both Revenue and the customer in electronic filing. These include:

a) Improved customer service: Revenue can provide a more efficient, timely and cost effective service to our customers. Access to your own Revenue account from your own PC with 24 hour, 365 day access to ROS. Calculation facilities to assist customers with determining their exposure to tax. Built-in electronic acknowledgments and uniform communications with all customers.

b) Faster turnaround time: By eliminating mailing, handling, and keying in of returns, they are now processed more quickly and retrieved rapidly.

c) Improved accuracy and audit trails : By eliminating the manual keying in of tax data and by implementing a series of computer checks and validations, the system allows more accurate processing of tax data. Specific problem fields are more easily identified.

d) Reduced Processing Costs : There will be cost savings as a result of the reduction in duplicated manual processing, that substantially reduce compliance costs for the customer along with a better distribution of the workload for employees. Staff resources will be redeployed to other areas e.g. customer service.

e) Other Potential Savings : There will be a reduction in costs associated with procurement, printing, postage, storage, replacement, stocktaking and distributing printed forms.

Once you are familiar with the advantages of electronic filing, there is a good chance you will put down the pen forever. Here are some of the biggest advantages of electronic filing:

f) Tracking and organizing your records : When you file your taxes online, you are creating a permanent electronic record for use in the future. If a question comes up about your tax return, you will not have to dig through filing cabinets or giant stacks of paper. Instead, you can pull up your information on your computer and get to work right away.

g) Better returns : While you may have to pay a fee to file your taxes electronically, in the end you could very well make this money back (plus more). Most people find that filing their taxes online gives them the chance to take advantage of more tax credits and tax deductions. Many tax preparation programs will help you file your return and tell you about potential tax benefits. In turn, you may get a larger tax refund or end up owing less money.

h) More accuracy : It should go without saying, but you need to make sure that your tax return is 100% accurate. When you file online this is often much easier to do. Online filing takes much of the guesswork out of the tax return process ? many programs even do the calculations for you. You won't have to worry about which tax forms you need or what step to take next, because your tax software will show you the way. Believe it or not, some programs even have audit protection tools built into them. With this type of tool, mistakes are found before you submit your tax return electronically to the IRS. Not only does this mean a more accurate tax return; it translates into a lesser chance of being audited.

Faster to file. The last thing most people want to do is spend days and weeks sifting through papers to file their return. When you opt to file your taxes online, that will speed up the process, which will save you a lot of time and frustration.

When an individual is filing taxes online he must ensure that he will get his money as soon as possible. With an online tax filing program, using the "Direct

Deposit" option allows people to get refund in two weeks or less (in most cases). Your tax refund will be deposited in your bank account so you can use that money immediately. There are many advantages to filing taxes online. With all of these benefits in mind, it is hard to imagine that anybody would want to file using paper tax forms.

4.3 COMPANY LAW IN A COMPUTERIZED ENVIRONMENT

Section 398 of the Companies Act, 2013 empowers the central Government to make rules in regard to filing of various applications, documents, returns etc. services or delivery of documents, notice or communication etc., maintenance of various applications, documents and returns filed etc. in the electronic form. Ministry of Company Affairs (MCA), has initiated MCA 21 programme, for easy and secure access to MCA services in a manner that best suits the business and citizens.

The programme goals have been set as follows keeping in mind stakeholders' needs:

- Business shall be enabled to register a company and file statutory documents quickly and easily
- Public to get easy access to relevant records and effective grievances redressal
- Professionals to be able to offer efficient services to their client companies
- Financial institutions to easily find charges registration and verification
- Employees to ensure proactive and affective compliance of relevant laws and corporate governance

Procedure of electronic fillings: in order to carry out E-filling MCA21. Facility to download E-form and fill in an off line mode is available. Every form has a facility to pre-fill the data available in MCA21 system. Once the e-form is filled one needs to validate the e-form using pre-scrutiny button. One would

then have to affix the relevant digital signatures and save the form. One would need to be connected to the internet to carry out the pre-fill and pre-scrutiny functions. The step by step process is given below. Once the payment has been made the status of payment and filling status can be tracked on the MCA21 portal by using the 'Track Your Payment Status' and 'Track Your Transaction Status' link respectively.

Steps for the e-filling: Following are the steps given below to proceed to do e-filling:

1. Select a category to download an e-form from the MCA21 portal
2. At any time, can read the related instruction kit to familiarize with the procedures
3. Fill the downloaded e-form.
4. Attach the necessary documents as attachments
5. Use the pre-fill button in e-Form to populate the grayed out portion by connecting to the internet.
6. The application or a representative of the applicant needs to sign the document using a digital signature.
7. Need to click the check form button available in the e-form. System will check the mandatory fields, mandatory attachments and digital signatures.
8. Upload the e-form for prre-scrutiny. The pre-scrutiny service is available under the services tab or under the e forms tab by clicking the upload e-form button. The system will verify (pre-scrutinize) the documents. In case of any inadequacies the use will be asked to rectify the mistakes before getting the document ready for execution (signature).
9. The system will calculate the free, including late payment fees based on the due date of filing, if applicable.
10. Payments will have to be made through appropriate mechanisms-electronic (credit card, internet banking) or traditional means (at the bank

counter through challan).

11. The payment will be exclusively confirmed for all online (internet) payment transactions using payment gateways.

12. Acceptance or rejection of any transaction will be explicitly communicated to the applicant (including facility to print a receipt for successful transactions).

13. MCA21 will provide a unique transaction number, the Service Request Number (SRN) which can be used by the applicant for enquiring the status pertaining to that transaction.

14. Filing will be complete only when the necessary payment are made.

15. In case of a rejection, helpful remedial tips will be provided to the applicant.

16. The applicants will be provided an acknowledgement through e-mail or alternatively they can check the MCA portal.

MCA21 programme will provide for anytime anywhere electronic services with speed and certainly to all the stakeholders. It will include:

- Design and development of application system
- Setting up of IT infrastructure
- Setting up the digital signature and associated security requirements
- Setting up of physical front offices
- Setting up of temporary front offices for the peak periods to meet with the requirements and subsequent shut down of temporary front offices at the end of such peak periods
- Migrating legacy data and digitization of paper documents to

the new system

- Providing user training at all levels and all offices (Front and Back Offices)

4..4 DIGITAL SIGNATURE CERTIFICATE

One of the major challenges facing consultants today is maintaining a level of knowledge of leading and emerging technologies, beyond the superficial or buzzword level. We need to develop a level of understanding that allows us to communicate effectively with both suppliers and customers. We then can understand :

- Our knowledge of the business issues being addressed;
- The application of technology to providing solutions;
- The business benefits for the customer;
- The limitations that will remain and that will need to be mitigated in other ways.

Digital Signature and Verification Digital signature is a mechanism by which a message is authenticated i.e. proving that a message is effectively coming from a given sender, much like a signature on a paper document. For instance, suppose that Alice wants to digitally sign a message to Bob. To do so, she uses her private-key to encrypt the message; she then sends the message along with her public-key (typically, the public key is attached to the signed message). Since Alice's public-key is the only key that can decrypt that message, a successful decryption constitutes a Digital Signature Verification, meaning that there is no doubt that it is Alice's private key that encrypted the message.

A digital signature is a mathematical scheme for demonstrating the authenticity of a digital message or documents. A valid digital signature gives a recipient reason to believe that the message was created by a known sender,

that the sender cannot deny having sent the message (authentication and non-repudiation), and that the message was not altered in transit (integrity). Digital signatures are a standard element of most cryptographic protocol suites, and are commonly used for software distribution, financial transactions, contract management software, and in other cases where it is important to detect forgery or tampering. The digital equivalent of a handwritten signature or stamped seal, but offering far more inherent security, a digital signature is intended to solve the problem of tampering and impersonation in digital communications.

Digital signatures can provide the added assurances of evidence to origin, identity and status of an electronic document, transaction or message, as well as acknowledging informed consent by the signer. In many countries, including the United States, digital signatures have the same legal significance as the more traditional forms of signed documents. The United States Government Printing Office publishes electronic versions of the budget, public and private laws, and congressional bills with digital signatures.

To create RSA signature keys, generate a RSA key pair containing a modulus, N, that is the product of two large primes, along with integers, e and d, such that e d ? 1 (mod ?(N)), where ? is the Euler phi-function. The signer's public key consists of N and e, and the signer's secret key contains d.

To sign a message, m, the signer computes ? ? md (mod N). To verify, the receiver checks that ?e ? m (mod N). This basic scheme is not very secure. To prevent attacks, one can first apply a cryptographic hash function to the message, m, and then apply the RSA algorithm described above to the result. This approach is secure assuming the hash function is a random oracle. M o s t early signature schemes were of a similar type: they involve the use of a trapdoor permutation, such as the RSA function, or in the case of the Rabin signature scheme, computing square modulo composite. A trapdoor permutation family is a family of permutations, specified by a parameter, that is easy to compute in the forward direction, but is difficult to compute in the reverse direction without already knowing the private key ("trapdoor"). Trapdoor permutations can be used for digital signature schemes, where computing the reverse direction with

the secret key is required for signing, and computing the forward direction is used to verify signatures.

Used directly, this type of signature scheme is vulnerable to a key-only existential forgery attack. To create a forgery, the attacker picks a random signature ? and uses the verification procedure to determine the message, m, corresponding to that signature. In practice, however, this type of signature is not used directly, but rather, the message to be signed is first hashed to produce a short digest that is then signed. This forgery attack, then, only produces the hash function output that corresponds to ?, but not a message that leads to that value, which does not lead to an attack.

How digital signatures work

Digital signatures are based on public key cryptography, also known as asymmetric cryptography. Using a public key algorithm such as RSA, one can generate two keys that are mathematically linked: one private and one public. To create a digital signature, signing software (such as an email program) creates a one-way hash of the electronic data to be signed. The private key is then used to encrypt the hash. The encrypted hash -- along with other information, such as the hashing algorithm -- is the digital signature. The reason for encrypting the hash instead of the entire message or document is that a hash function can convert an arbitrary input into a fixed length value, which is usually much shorter. This saves time since hashing is much faster than signing.

The value of the hash is unique to the hashed data. Any change in the data, even changing or deleting a single character, results in a different value. This attribute enables others to validate the integrity of the data by using the signer's public key to decrypt the hash. If the decrypted hash matches a second computed hash of the same data, it proves that the data hasn't changed since it was signed. If the two hashes don't match, the data has either been tampered with in some way (integrity) or the signature was created with a private key that doesn't correspond to the public key presented by the signer (authentication).

A digital signature can be used with any kind of message -- whether it is

encrypted or not -- simply so the receiver can be sure of the sender's identity and that the message arrived intact. Digital signatures make it difficult for the signer to deny having signed something (non-repudiation) -- assuming their private key has not been compromised -- as the digital signature is unique to both the document and the signer, and it binds them together. A digital certificate, an electronic document that contains the digital signature of the certificate-issuing authority, binds together a public key with an identity and can be used to verify a public key belongs to a particular person or entity. If the two hash values match, the message has not been tampered with, and the receiver knows the message is from sender. Most modern email programs support the use of digital signatures and digital certificates, making it easy to sign any outgoing emails and validate digitally signed incoming messages. Digital signatures are also used extensively to provide proof of authenticity, data integrity and non-repudiation of communications and transactions conducted over the Internet.

Digital signatures are often used to implement electronic signatures, a broader term that refers to any electronic data that carries the intent of a signature, but not all electronic signatures use digital signatures. In some countries, including the United States, India, Brazil, Indonesia, Saudi Arabia, Switzerland and the countries of the European Union, electronic signatures have legal significance. Digital signatures employ asymmetric cryptography. In many instances they provide a layer of validation and security to messages sent through a non secure channel: Properly implemented, a digital signature gives the receiver reason to believe the message was sent by the claimed sender. Digital seals and signatures are equivalent to handwritten signatures and stamped seals. Digital signatures are equivalent to traditional handwritten signatures in many respects, but properly implemented digital signatures are more difficult to forge than the handwritten type. Digital signature schemes, in the sense used here, are cryptographically based, and must be implemented properly to be effective. Digital signatures can also provide non-repudiation, meaning that the signer cannot successfully claim they did not sign a message, while also claiming their private key remains secret; further, some non-repudiation schemes offer a time

stamp for the digital signature, so that even if the private key is exposed, the signature is valid.

Digitally signed messages may be anything representable as abitstring: examples include electronic mail, contracts, or a message sent via some other cryptographic protocol.

A digital signature scheme typically consists of three algorithms; A key generation algorithm that selects a private key uniformly at random from a set of possible private keys. The algorithm outputs the private key and a corresponding public key. A signing algorithm that, given a message and a private key, produces a signature. A signature verifying algorithm that, given the message, public key and signature, either accepts or rejects the message's claim to authenticity. Two main properties are required. First, the authenticity of a signature generated from a fixed message and fixed private key can be verified by using the corresponding public key. Secondly, it should be computationally infeasible to generate a valid signature for a party without knowing that party's private key.

A digital signature is an authentication mechanism that enables the creator of the message to attach a code that acts as a signature.

There are several reasons to sign such a hash (or message digest) instead of the whole document.

ADVANTAGES OF DIGITAL SIGNATURE CERTIFICATE

Digital being added to almost anything makes it a lot faster than the non-digital version of that thing. Similarly a digital signature can be used to send documents a lot faster, almost instantaneously, as the documents can now be sent via mail and do not need to be delivered in person or via courier. Also an added advantage would be the decreased cost of sending the documents as the digital signatures are comparatively a lot less expensive than any courier service charge for sending documents. Not only this, a document sent via courier or in person could be tampered with on the way but when sent using a digital signature it gets encrypted in such a way that any kind of tampering with the document is

not possible. Further, a document which is digitally signed can effortlessly tracked and located in few minutes. Nobody else can fake your digital signature or present an electronic file incorrectly claiming it was signed by you. The documents containing digital signatures are in no way different form documents containing a pen on paper signature as they would even stand in court when produced because a digital signature cannot be copied and also contains a date and time stamp. The digital signatures process is essential for the formal approval processes of every companies, a typical scenario require multiple authorization of multiple offices for each document.Thus digital signatures allow alternate approval processes, collaboration and delivery of paper (expensive and slow), with a digital system (faster, cheaper and more efficient).This results in a number of advantages: Improved operational efficiency, reduce cycle time and elimination of costs; Risk mitigation, compliance assurance, data quality and long-term storage of files;Increase the competitiveness and service levels. Resuming, digital signatures can reliably automate the signatures of authorization allowing the elimination of paper, reducing costs and improving the speed of production processes. By virtue of all these advantages, the digital signature can be particularly useful for: Government agencies in regulated sectors with workflows subject to formal approval; organizations must submit documents that need to be approved by various offices;representatives of organizations that use, or services that require commercial building and the provision of reports or contracts signed;Away from executives such as a signature is required to activate the processes;organizations which cooperate with external partners and require approval for workflows;Web portals with external modules that require compilation and signing.

Type of documents to which to apply the digital signature is particularly composite, and includes:

- sales proposals, contracts with customers.
- purchase orders, contracts / agreements with partners.
- contracts, agreements, acts of the board.

- leases, contracts, expense reports and reimbursement approvals.
- Human Resources: Documentation of employment of employees, presence control cards.
- Life Sciences: Questions and proposals, QC records, standard operating procedures (SOPs), policies, work instructions.
- Mechanical work: drawings, sketches, plans, instructions and relations of production health services: medical and patient consent forms, medical exams, prescriptions, laboratory reports.

GENERAL ADVANTAGES OF USING A DIGITAL SIGNATURE

a) Efficiency : The signature will be much shorter and thus save time since hashing is generally much faster than signing in practice.

b) Compatibility : Messages are typically bit strings, but some signature schemes operate on other domains (such as, in the case of RSA, numbers modulo a composite number N). A hash function can be used to convert an arbitrary input into the proper format.

c) Integrity : Without the hash function, the text "to be signed" may have to be split (separated) in blocks small enough for the signature scheme to act on them directly. However, the receiver of the signed blocks is not able to recognize if all the blocks are present and in the appropriate order.

d) Notions of security : In their foundational paper, Goldwasser, Micali, and Rivest lay out a hierarchy of attack models against digital signatures: In a key-only attack, the attacker is only given the public verification key. In a known message attack, the attacker is given valid signatures for a variety of messages known by the attacker but not chosen by the attacker. In an adaptive chosen message attack, the attacker first learns signatures on arbitrary messages of the attacker's choice. They also describe a hierarchy of attack results: A total break results in the recovery of the signing key. A universal forgery attack results in the ability to forge signatures for any message.

A selective forgery attack results in a signature on a message of the

adversary's choice.

An existential forgery merely results in some valid message/signature pair not already known to the adversary.

The strongest notion of security, therefore, is security against existential forgery under an adaptive chosen message attack.

Applications of digital signatures

As organizations move away from paper documents with ink signatures or authenticity stamps, digital signatures can provide added assurances of the evidence to provenance, identity, and status of an electronic document as well as acknowledging informed consent and approval by a signatory. The United States Government Printing Office (GPO) publishes electronic versions of the budget, public and private laws, and congressional bills with digital signatures. Universities including Penn State, University of Chicago, and Stanford are publishing electronic student transcripts with digital signatures.

ADVANTAGES OF DIGITAL SIGNATURE TO COMMUNICATIONS

a) Authentication : Although messages may often include information about the entity sending a message, that information may not be accurate. Digital signatures can be used to authenticate the source of messages. When ownership of a digital signature secret key is bound to a specific user, a valid signature shows that the message was sent by that user. The importance of high confidence in sender authenticity is especially obvious in a financial context. For example, suppose a bank's branch office sends instructions to the central office requesting a change in the balance of an account. If the central office is not convinced that such a message is truly sent from an authorized source, acting on such a request could be a grave mistake.

b) Integrity : In many scenarios, the sender and receiver of a message may have a need for confidence that the message has not been altered during transmission. Although encryption hides the contents of a message, it may be possible to change an encrypted message without understanding it. (Some

encryption algorithms, known as nonmalleable ones, prevent this, but others do not.) However, if a message is digitally signed, any change in the message after signature invalidates the signature. Furthermore, there is no efficient way to modify a message and its signature to produce a new message with a valid signature, because this is still considered to be computationally infeasible by most cryptographic hash functions (seecollision resistance).

c) Non-repudiation : Non-repudiation, or more specifically non-repudiation of origin, is an important aspect of digital signatures. By this property, an entity that has signed some information cannot at a later time deny having signed it. Similarly, access to the public key only does not enable a fraudulent party to fake a valid signature.

Authentication, non-repudiation etc. properties rely on the secret key not having been revoked prior to its usage. Public revocation of a key-pair is a required ability, else leaked secret keys would continue to implicate the claimed owner of the key-pair. Checking revocation status requires an "online" check; e.g., checking a "Certificate Revocation List" or via the "Online Certificate Status Protocol". Very roughly this is analogous to a vendor who receives credit-cards first checking online with the credit-card issuer to find if a given card has been reported lost or stolen. Of course, with stolen key pairs, the theft is often discovered only after the secret key's use, e.g., to sign a bogus certificate for espionage purpose.

d) Additional security precautions : Putting the private key on a smart card All public key / private key cryptosystems depend entirely on keeping the private key secret. A private key can be stored on a user's computer, and protected by a local password, but this has two

DISADVANTAGES

- The user can only sign documents on that particular computer
- The security of the private key depends entirely on the security of the computer

A more secure alternative is to store the private key on a smart card.

Many smart cards are designed to be tamper-resistant (although some designs have been broken, notably by Ross Anderson and his students). In a typical digital signature implementation, the hash calculated from the document is sent to the smart card, whose CPU signs the hash using the stored private key of the user, and then returns the signed hash. Typically, a user must activate his smart card by entering a personal identification number or PIN code (thus providing two-factor authentication). It can be arranged that the private key never leaves the smart card, although this is not always implemented. If the smart card is stolen, the thief will still need the PIN code to generate a digital signature. This reduces the security of the scheme to that of the PIN system, although it still requires an attacker to possess the card. A mitigating factor is that private keys, if generated and stored on smart cards, are usually regarded as difficult to copy, and are assumed to exist in exactly one copy. Thus, the loss of the smart card may be detected by the owner and the corresponding certificate can be immediately revoked. Private keys that are protected by software only may be easier to copy, and such compromises are far more difficult to detect.

The advantages greatly overshadow the disadvantages. Practically the only disadvantages of using digital signature are the weak laws regarding cyber security which might cause any unnecessary hassles in case of a court case and that both parties have to purchase the certificates for the digital signature in order to use it instead of the one party courier charge. Private companies and governments agencies all around the word make huge investments for the automation of their processes and in the management of the electronic documentation.

The main requirement in the management of digital documentation is its equivalence, from a legal perspective, to paperwork, affixing a signature on a digital document is the fundamental principle on which are based the main processes of authorization and validation, apart from the specific area of application. Main benefits for the introduction of digital signing processes are cost reduction and complete automation of documental workflow, including authorization and validation phases. In essence, digital signatures allow you to

replace the approval process on paper, slow and expensive, with a fully digital system, faster and cheaper. The digital signature is simply a procedure which guarantees the authenticity and integrity of messages and documents exchanged and stored with computer tools, just as in traditional handwritten signature for documents. Essentially The digital signature of an electronic document aims to fulfill the following requirements:

- that the recipient can verify the identity of the sender (authenticity); that the sender can not deny that he signed a document (non-repudiation);
- that the recipient is unable to invent or modify a document signed by someone else (integrity).

Using smart card readers with a separate keyboard

Entering a PIN code to activate the smart card commonly requires a numeric keypad. Some card readers have their own numeric keypad. This is safer than using a card reader integrated into a PC, and then entering the PIN using that computer's keyboard. Readers with a numeric keypad are meant to circumvent the eavesdropping threat where the computer might be running a keystroke logger, potentially compromising the PIN code. Specialized card readers are also less vulnerable to tampering with their software or hardware and are often EAL3 certified.

To protect against this scenario, an authentication system can be set up between the user's application (word processor, email client, etc.) and the signing application. The general idea is to provide some means for both the user application and signing application to verify each other's integrity. For example, the signing application may require all requests to come from digitally signed binaries.

A digital signature applies to a string of bits, whereas humans and applications "believe" that they sign the semantic interpretation of those bits. In order to be semantically interpreted, the bit string must be transformed into a form that is meaningful for humans and applications, and this is done through a combination of hardware and software based processes on a computer system.

The problem is that the semantic interpretation of bits can change as a function of the processes used to transform the bits into semantic content. It is relatively easy to change the interpretation of a digital document by implementing changes on the computer system where the document is being processed. From a semantic perspective this creates uncertainty about what exactly has been signed. WYSIWYS (What You See Is What You Sign) means that the semantic interpretation of a signed message cannot be changed. In particular this also means that a message cannot contain hidden information that the signer is unaware of, and that can be revealed after the signature has been applied. WYSIWYS is a necessary requirement for the validity of digital signatures, but this requirement is difficult to guarantee because of the increasing complexity of modern computer systems. The term WYSIWYS was coined by Peter Landrock and Torben Pedersen to describe some of the principles in delivering secure and legally binding digital signatures for Pan-European projects.

Digital signatures versus ink on paper signatures

An ink signature could be replicated from one document to another by copying the image manually or digitally, but to have credible signature copies that can resist some scrutiny is a significant manual or technical skill, and to produce ink signature copies that resist professional scrutiny is very difficult.

Digital signatures cryptographically bind an electronic identity to an electronic document and the digital signature cannot be copied to another document. Paper contracts sometimes have the ink signature block on the last page, and the previous pages may be replaced after a signature is applied. Digital signatures can be applied to an entire document, such that the digital signature on the last page will indicate tampering if any data on any of the pages have been altered, but this can also be achieved by signing with ink and numbering all pages of the contract. Aggregate signature - a signature scheme that supports aggregation: Given n signatures on n messages from n users, it is possible to aggregate all these signatures into a single signature whose size is constant in the number of users. This single signature will convince the verifier that the n

users did indeed sign the n original messages. Signatures with efficient protocols - are signature schemes that facilitate efficient cryptographic protocols such as zero-knowledge proofs or secure computation.

All digital signature schemes share the following basic prerequisites regardless of cryptographic theory or legal provision:

Quality algorithms

Some public-key algorithms are known to be insecure, as practical attacks against them having been discovered.

Quality implementations

An implementation of a good algorithm (or protocol) with mistake(s) will not work.

Users (and their software) must carry out the signature protocol properly.

The private key must remain private

If the private key becomes known to any other party, that party can produce perfect digital signatures of anything whatsoever.

The public key owner must be verifiable

A public key associated with Bob actually came from Bob. This is commonly done using a public key infrastructure (PKI) and the public key?user association is attested by the operator of the PKI (called acertificate authority). For 'open' PKIs in which anyone can request such an attestation (universally embodied in a cryptographically protected identity certificate), the possibility of mistaken attestation is non-trivial. Commercial PKI operators have suffered several publicly known problems. Such mistakes could lead to falsely signed, and thus wrongly attributed, documents. 'Closed' PKI systems are more expensive, but less easily subverted in this way.

Only if all of these conditions are met will a digital signature actually be any evidence of who sent the message, and therefore of their assent to its contents. Legal enactment cannot change this reality of the existing engineering

possibilities, though some such have not reflected this actuality.

Legislatures, being importuned by businesses expecting to profit from operating a PKI, or by the technological avant-garde advocating new solutions to old problems, have enacted statutes and/or regulations in many jurisdictions authorizing, endorsing, encouraging, or permitting digital signatures and providing for (or limiting) their legal effect. The first appears to have been in Utah in the United States, followed closely by the states Massachusetts and California. Other countries have also passed statutes or issued regulations in this area as well and the UN has had an active model law project for some time. These enactments (or proposed enactments) vary from place to place, have typically embodied expectations at variance (optimistically or pessimistically) with the state of the underlying cryptographic engineering, and have had the net effect of confusing potential users and specifiers, nearly all of whom are not cryptographically knowledgeable. Adoption of technical standards for digital signatures have lagged behind much of the legislation, delaying a more or less unified engineering position on interoperability, algorithm choice, key lengths, and so on what the engineering is attempting to provide.

In several countries, a digital signature has a status somewhat like that of a traditional pen and paper signature, like in the EU digital signature legislation. Generally, these provisions mean that anything digitally signed legally binds the signer of the document to the terms therein. For that reason, it is often thought best to use separate key pairs for encrypting and signing. Using the encryption key pair, a person can engage in an encrypted conversation (e.g., regarding a real estate transaction), but the encryption does not legally sign every message he sends. Only when both parties come to an agreement do they sign a contract with their signing keys, and only then are they legally bound by the terms of a specific document. After signing, the document can be sent over the encrypted link. If a signing key is lost or compromised, it can be revoked to mitigate any future transactions. If an encryption key is lost, a backup or key escrow should be utilized to continue viewing encrypted content. Signing keys should never be backed up or escrowed unless the backup destination is securely encrypted.

Most of the times the question of what a digital signature is, is asked by - not exactly smart but not even technically challenged people. So first of all let us understand what a digital signature is:-

For an easier understanding think of a digital signature as serving a purpose similar to that of an on paper signature. A signature is used to authenticate a person as it is very unlikely that anyone would be able to copy the signature of an individual. Similarly digital signature uses mathematical functions which give a unique signature to the sender at the same time encrypting the message if required to make sure that the message or the documents being sent via email or through any digital medium are sent by the person they are claimed to be sent by. And even these documents or messages are not tampered with or edited and reach in the same condition they are se

Digital Signature Process

A Digital signature is a one-way hash, of the original data, that has been encrypted with the signer's private key. A digital signature process is composed by the following steps:

The signer calculates the hash for the data he needs to sign. The message digest is a file size small (160-bit SHA-1 now deprecated, with 256-bit SHA-256) that contains some sort of control code that refers to the document. The hash function is produced minimizing the likelihood to get the same value of the digest from different texts and is also "one way" function: this means that from calculates hash it is impossible to get back the original text.

The signer, using his private key, encrypt the hash calculate.

- Signer sends the original data and the digital signature to the receiver. The pair (document and signature) is a signed document or a document to which was attached a signature. The document is in clear text but it has the signature of the sender and can be sent so that it can be read by anyone but not altered since the digital signature guarantees also integrity of the message.
- For the verification, The receiving software first uses the signer's public

key to decrypt the hash, then it uses the same hashing algorithm that generated the original hash to generate a new one-way hash of the same data. The receiving software compares the new hash against the original hash. If the two hashes match, the data has not changed since it was signed.

- The authenticity of a document can be verified by anyone decrypting the signature of the document with the sender's public key, obtaining the fingerprint of the document, then comparing it with that obtained by applying the hash function (which is known) to the document received which was attached the signature. If the two fingerprints are equal, the authenticity and integrity of the document are demonstrated.

- The signing and verification operations may be delegated to a schedule issued by the certification.

Thanks to the mechanism shown, the digital signature ensures non-repudiation: the signer of a document transmitted cannot deny having sent it and the receiver can deny to have received it. In other words means that the information cannot be ignored, as in the case of a conventional signature on a paper document in the presence of witnesses.

4.5 DIRECTOR IDENTIFICATION NUMBER

The concept of Director Identification Number (DIN) has been introduced under MCA21 e-Governance programme. A reference to DIN allotted to a Director is a mandatory field in e-filing in respect of certain filings.

A reference to DIN Allotted to a Director is a mandatory field in e-filing in respect of certain filings. The Companies (Amendment) Act, 2006 has inserted new sections 266 A to 266 G which contain certain provisions regarding the allotment of a unique Director Identification Number (DIN).

PROCEDURE OF OBTAINING DIN

As per the revised procedure for DIN Allotment, any person intending to apply for DIN shall have to make an application in e-Form DIR-3 and should

follow the following procedure:

1. e-Form DIR-3 has to follow the offline e-Filing process.

2. Attach the photograph and scanned copy of supporting documents i.e. proof of identity, and proof of residence as per the guidelines. Physical documents are not required to submit at DIN cell.

3. Along with the supporting documents, verification by the applicant for applying for allotment of Director Identification Number (DIN) shall also be attached. This shall contain the Name, Father's name, date of birth, present address and text of declaration and physical signature of the applicant.

4. The eForm shall have to be digitally signed and shall be uploaded on MCA21 portal.

5. Upon upload, Pay the fees for DIR-3 eForm. Only electronic payment of the fees shall be allowed (I.e. Netbanking / Credit Card). No challan payment will be accepted under revised procedure of DIN allotment. The user is required to get himself/ herself registered on the MCA21 Portal to obtain login id, which is necessary for payment of the fees. After obtaining the login?id, Login to the MCA21 portal and click on 'eForm upload' link available under the 'eForms' tab for uploading the eForm DIR-3. eForm DIN-3 will be processed only after the DIN application fee is paid.

6. Upon upload and successful payment, In case Form DIR-3 details have not been identified as potential duplicate, Approved DIN shall be generated and if the details have been identified as potential duplicate, Provisional DIN shall be generated.

7. Processing of e Form DIR-3 In case, DIR-3 is a potential duplicate, the MCA DIN cell will examine the e Form DIR-3 and same shall be disposed of within one or two days.

8. Post-approval changes in particulars of DIR-3 If there is any change in

the particulars submitted in form DIN?3, applicant can submit e?form DIN?6 online. For instance in the event of change of address of a director, he/ she is required to intimate this change by submitting eform DIN?6 along with the required attested documents. 2. What things should be taken care of while filling form DIR-3? Please note that Income Tax PAN is mandatory in case of Indian applicants so the applicant details (name, father's name, date of birth) should be as per the PAN details. The particulars filled in form DIN-3 should match with the details given in the supporting documents to be submitted along with DIN application. Any mis-match will lead to rejection of DIN application. Particulars filled in form DIR-3 should match with the details given in the supporting documents to be submitted along with DIN application.

Fill the given Particulars in e-form : Attach the photograph (JPEG).

- Attach scanned copy of supporting documents (Proof of Identity, Proof of Residence of Applicant and DIR-4): List Attached Below
- Physical documents are not required to submit at DIN cell.
- The e-Form shall have to be digitally signed and shall be uploaded on MCA21 portal.
- Form DIR-3 is mandatorily to be signed by an Applicant and a practicing professional or secretary (who is a member of ICSI) in whole time employment or the Director of the existing company.
- The applicant is required to get himself/herself registered on the MCA21 Portal to obtain login id, which is necessary for payment of the fees or the Professional is required to get himself/herself registered on the MCA21 Portal to obtain login id, which is necessary for payment of the fees

After obtaining the login-id, Login to the MCA21 portal and click on 'e-Form upload' link available under the 'e-Forms' tab for uploading the e-Form DIR-3. Upon upload, pay the fees for e-Form DIR-Only electronic payment of

the fees shall be allowed (I.e. Net banking / Credit Card). No challan payment will be accepted under revised procedure of DIN allotment. e-Form DIR-3 will be processed only after the DIN application fee is paid. Approved DIN shall be generated in case the form is being signed by a practicing professional and details have not been identified as potential duplicate. Provisional DIN shall be generated in case form is signed by secretary in whole time employment or Director of existing company and details have been found as potential duplicate. A suitable informational message and an email shall be provided to the user that the DIN shall be approved after due verification by the DIN cell.

Processing of e Form DIR-3.

In case, DIR-3 gets certified by the professional (i.e. CA (in whole time practice)/ CS (in whole time practice)/ CWA (in whole time practice)/, the DIN will be approved by the system immediately online (in case it is not potential duplicate). Post-approval changes in particulars of Form DIR-3. If there is any change in the particulars submitted in e-form DIR-3, applicant can submit e-form DIR-6 online. For instance in the event of change of address of a director, he/ she is required to intimate this change by submitting e-form DIR-6 along with the required attested documents.

Method to get e-form DIR-3 attested from Pofessionals

- If eForm is digitally signed by a Chartered Accountant (CA) or Cost Accountant (CWA) or Company Secretary (CS) (in whole time practice) then the supporting documents attached shall be self-attested by the applicant.

- If eForm is digitally signed by secretary (who is member of ICSI), in whole time employment or director of existing company then the supporting documents attached shall be either self-attested by the applicant or duly attested by either Public Notary or a Gazette Officer of a Government. {The attesting authority must indicate the following while attesting the documents:- (i) Signatures; (ii)Name in full in Capitals; (iii) Registration No.; and (iv) Seal/ Stamp.

- In case, the director/ designated partner is residing outside India, then the

attached supporting documents should be attested by the Consulate of the Indian Embassy, Foreign public notary. In case of director, supporting documents can also be attested by Company secretary in full time employment /CEO / Managing director of the Indian company in which he / she proposed to be a director.

List of Mandatory Attached Documents

The following are the mandatory attachments to be filed in all cases:

a) Proof of Identity of Applicant

In case of Indian nationals, Income-tax PAN is a mandatory requirement for proof of identity. In case of foreign nationals, passport is a mandatory requirement for proof of identity.

Proof of identify enclosed with e-Form DIR-3 should also contain the date of birth of the applicant and the same should match the date of birth filled in the application form. In case the proof of identify does not indicate the Date of Birth then additional proof of Date of Birth, duly certified/ attested, should be attached.

b) Proof of residence of applicant

- Address proofs like: Passport, Election (Voter Identity) Card, and Ration Card, Driving License, Electricity Bill, Telephone Bill or Aadhar shall be attached and should be in the name of applicant only.
- In case of Indian applicant, documents should not be older than 2 months from the date of filing of the e-Form.
- In case of foreign applicant, address proof should not be older than 1 year from the date of filing of the e-Form

c) Copy of verification by the applicant as per e-Form No. DIR-4- DIR-4 shall contain the Name, Father's name, date of birth and text of declaration and physical signature of the applicant)

In case of proofs which are in languages other than Hindi / English, the proofs should be translated in Hindi / English from professional translator carrying

his details (name, signature, address) and seal. In the case of foreign nationals, translation done by the notary of home country is also acceptable.

Ground of Rejections of e-form.

Rejection Code	Description
1	Proof of identity has not been attested by an authorized person.
2	Proof of residential address has not been attested by an authorized person.
3	The supporting document for identity proof is not valid as it has not been issued by any Government Authority
4	The enclosed evidence has handwritten entries.
5	Date of Birth is not matching with the date of birth mentioned in the proof attached.
6	Applicant's Name is not matching with the name mentioned in the proof attached.
7	Address is not matching with the address details mentioned in the proof attached
8	Applicant's Father's Name is not matching with the father's name mentioned in the proof attached.
9	The submitted application is duplicate DIN application i.e. an approved DIN already exists in this name.
10	Identification number entered in application does not match with the identity proof enclosed.
11	The gender is not entered correctly in DIN form. 12 ID proof not attached with the application
13	Address proof not attached with the application.

14	Non-submission of copy of passport (for foreign nationals)
15	Passport duly appostillised not enclosed (For foreign nationals)
16	Verification by applicant is not attached
17	Verification by applicant not in prescribed format
18	Verification by applicant is not signed
19	The prefixes/ suffixes like Mr. / Ms. / Kumari / Shri / Late or Ji etc. are used in your name or your father's name field in DIN form.
20	The supporting documents attached not valid or current or has expired.

4.6 CORPORATE IDENTITY NUMBER (CIN)

A new investor friendly Corporate Identity Number (CIN) is being introduced to uniquely identify every company registered with the Registrar of Companies. Currently, the present registration number assigned to a company does not reflect the activity or the State or ownership of the company.

The CIN assigned to a company indicates the following :

Listing Status

Economic Activity (Industry)

State

Year of Incorporation

Ownership

Sequential Number assigned by RoC's

The CIN is explained schematically below:-

- The first digit of the CIN represents the Listing Status of a company. If the company is unlisted the alphabet entered is 'U' and in case the company is

listed the alphabet entered is 'L'. In general, freshly incorporated companies are unlisted.

- The second five digits represent the economic activity of the company. The standard National Industrial Classification (NIC) 98, at the 5-digit level, would be used to assign activity/Industry code. The NIC '98 has been devised by Central Statistical Organisation (CSO), Ministry of Statistics and Program Implementation, Government of India. The document giving details on the codes can be procured from the CSO. Annexure-1 presents a sample classification for a few economic activities.

- The next two places represent the State in which the company's registered office is located. All States are represented by a two-alphabet code. The complete list of State code is presented in Annexure-II to this note.

- The next four places indicate the year in which the company was incorporated.

- Next, the ownership code is indicated through a three-alphabet code. The list of codes with their description is presented in Annexure-III to this note.

- The last six places in the CIN are the sequential number assigned to every company by the concerned ROC office of the State. There is no space, hyphen, oblique sign, etc. between the various code components

1. I am directed to say that it has been decided that all Registrar of Companies will allocate a Corporate Identity Number (CIN) to each company registered on or after 1st November, 2000.

2. The CIN has been designed to help easily identify companies belonging to a State, industry, ownership or age. It will be 21-digit number.

3. The first letter denotes the listed or unlisted company. The first five digits represent, the economic activity of the company, the second two places represent the State in which the company's registered office is located, the next four places indicate the year in which the company was incorporated, the next three places indicate ownership code and the last six places in the CIN are the unique number

assigned to every company in any particular economic activity, in a particular State, of a particular year of incorporation and of a particular ownership category

4. Training schedule for the officers and staff of Registrars of Companies in this regard is being chalked out by the NIC and will be sent to you shortly.

5. All Registrar of companies are directed to act accordingly. A copy of this circular is also available on web site http://www.nic.in/dca of the department and can be accessed in case of need.

STEPS FOR IMPLEMENTATION OF CIN

Step 1 : First place in CIN represents the Listing status of a company. The listing status code is represented by a alphabet. If Company is Listed then assign 'L' otherwise assign 'U' for unlisted company.

Step 2 : The next five places represent the economic activity of the company according to the standard National Industrial Classification (NIC) 98. Select the economic activity code of the company from NIC 98 manual and assign the code. In case if a company is operating in a diverse fields, then assign '00000' as a 'Diversified' company. The manual/document on NIC '98 can be obtained from CSO.Annexure-I presents a sample classification for a few economic activities.

Step 3 : The next two places represent the State in which the company's registered office is located. All States are represented by a two-alphabet code. The complete list of State code is presented in Annexure-II to this note. Assign the State code from the list given in Annexure-II.

Step 4 : The next four places represent the year of incorporation of the compny. Assign the year of incorporation of a company in 'YYYY' format. Example, if a company is incorporated on April 2, 1982. Then assign 1982 as year of incorporation.

Step 5 : The next three places represent the ownership of a company. Whether the company is Union Government Company or State Government Company, Private limited or Public limited company. Ownership code is

represented by three alphabet code. The list of codes with their description is presented in Annexure-III to this note. Assign the ownership code from the list presented in Annexure-III.

Step 6 : The last six places represents the unique sequential number assigned to every company by the concerned Registrar of Companies (RoCs) office of the State. This unique six digit sequential number is assigned by the respective RoCs.

Note that there is no space, hyphen, oblique sign, etc. between the various code components.

Consider an example of an existing company ABC India Ltd.

ABC India Ltd. - 1393 (Registration Number)

ABC India Ltd. - L60230AS1972PLC1393 (CIN)

The registration number does not give any information about the company where as the CIN provides information about the listing status, activity (Industry), ownership, registered office, and year of incorporation of the company.

Corporate Identity Number (CIN) :- Each Indian company (Listed or Unlisted) has a unique 21 Digit CIN (Corporate Identity Number). This is required to be quoted on all forms. Once this number is filled, company details are automatically filled in E-Forms issued by MCA by using pre-fill function. How CIN is structured Digit No. What it Shows? Remarks 1 st digit Listing status If Company is Listed it will start with 'L 'and if Company is not Listed it will start with 'U' Next 5 digit Industry code Next 2 digit State code i.e. MH for Maharashtra. Next 4 digit Year of incorporation I.e. for Company formed in Calendar Year 2011 the same will be 2011. Next 3 digit Ownership PLC for Public Limited Company PTC for Private Limited Company. Last 6 digit ROC reg. i.e. 090868 for ROC- Mumbai i.e. 090633 for ROC- KOLKATA. Tax Deduction and Collection Account Number(TAN) It is a 10 digit alpha numeric number required to be obtained by all persons who are responsible for deducting or collecting tax. Under Section 203A of the Income Tax Act, 1961, , it is

mandatory to quote Tax Deduction Account Number (TAN) allotted by the Income Tax Department (ITD) on all TDS returns.Since last few years ITD has revised the structure of TAN. It is a unique 10 digit alphanumeric code. Accordingly, they have issued TAN in this new format to all existing TAN holders. How TAN is structured B L R W 3 9 5 6 7 H RCC Code Bangalore First Alphabet of the Organisation Name Numeric (5 places) Alphabet TAN structure is as follows: AAAA99999A: First four characters are letters, next 5 numerals, last" character letter. The first three characters represent the city or state where the TAN was issued. In the below table

- First three letter in TAN 'BLR' signifies that city in which TAN issued is Bangalore. The fourth character of the TAN is the initial letter of the tax deductor. Which Means name of the
- Tax Deductor starts with this letter. Next five characters are system generated numeric Numbers
- Last character is Alphabetic Number which is also known as check digit which is also system generated. Each tax deduction is uniquely identified by his TAN
- If the TAN does not follow the above structure, then the TAN will be shown invalid.

4.7 LIMITED LIABILITYPARTNERSHIP ACT, 2008

MEANING OF LIMITED PARTNERSHIP ACT, 2008

Section 2:- DEFINITION

(1) In this Act, unless the context otherwise requires,-

(a) "address", in relation to a partner of a limited liability partnership, means-

(i) if an individual, his usual residential address; and

(ii) if a body corporate, the address of its registered office;

(b) "advocate" means an advocate as defined in clause (a) of sub-section (1) of section 2 of the Advocates Act, 1961 (25 of 1961);

(c) "Appellate Tribunal" means the National Company Law Appellate Tribunal constituted under sub-section (1) of section 10FR of the Companies Act, 1956 (1 of 1956);

(d) "body corporate" means a company as defined in section 3 of the Companies Act, 1956 (1 of 1956) and includes-

(i) a limited liability partnership registered under this Act;

(ii) a limited liability partnership incorporated outside India; and

(iii) a company incorporated outside India,

but does not include-

(i) a corporation sole;

(ii) a co-operative society registered under any law for the time being in force; and

(iii) any other body corporate (not being a company as defined in section 3 of the Companies Act, 1956 (1 of 1956) or a limited liability partnership as defined in this Act), which the Central Government may, by notification in the Official Gazette, specify in this behalf;

(e) "business" includes every trade, profession, service and occupation;

(f) "chartered accountant" means a chartered accountant as defined in clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 (38 of 1949) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;

(g) "company secretary" means a company secretary as defined in clause (c) of sub-section (1) of section 2 of the Company Secretaries Act,

1980 (56 of 1980) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;

(h) "cost accountant" means a cost accountant as defined in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act;

(i) "Court", with respect to any offence under this Act, means the Court having jurisdiction as per the provisions of section 77;

(j) "designated partner" means any partner designated as such pursuant to section 7;

(k) "entity" means any body corporate and includes, for the purposes of sections 18, 46, 47, 48, 49, 50, 52 and 53, a firm set-up under the Indian Partnership Act, 1932 (9 of 1932);

(l) "financial year", in relation to a limited liability partnerships, means the period from the 1st day of April of a year to the 31st day of March of the following year :

Provided that in the case of a limited liability partnership incorporated after the 30th day of September of a year, the financial year may end on the 31st day of March of the year next following that year;

(m) "foreign limited liability partnership" means a limited liability partnership formed, incorporated or registered outside India which establishes a place of business within India;

(n) "limited liability partnership" means a partnership formed and registered under this Act;

(o) "limited liability partnership agreement" means any written agreement between the partners of the limited liability partnership or between the limited liability partnership and its partners which determines the mutual

rights and duties of the partners and their rights and duties in relation to that limited liability partnership;

(p) "name", in relation to a partner of a limited liability partnership, means-

(i) if an individual, his forename, middle name and surname; and

(ii) if a body corporate, its registered name;

(q) "partner", in relation to a limited liability partnership, means any person who becomes a partner in the limited liability partnership in accordance with the limited liability partnership agreement;

(r) "prescribed" means prescribed by rules made under this Act;

(s) "Registrar" means a Registrar, or an Additional, a Joint, a Deputy or an Assistant Registrar, having the duty of registering companies under the Companies Act, 1956 (1 of 1956);

(t) "Schedule" means a Schedule to this Act;

(u) "Tribunal" means the National Company Law Tribunal constituted under sub-section (1) of section 10FB of the Companies Act, 1956 (1 of 1956).

(2) Words and expressions used and not defined in this Act but defined in the Companies Act, 1956 (1 of 1956) shall have the meanings respectively assigned to them in that Act.

4.7.1 THE LIMITED LIABILITY PARTNERSHIP ACT, 2008

An Act to make provisions for the formation and regulation of limited liability partnerships and for matters connected therewith or incidental thereto. BE it enacted by Parliament in the Fifty-ninth Year of the Republic of India as follows:-

Short title, extent and commencement.-

(1) This Act may be called the Limited Liability Partnership Act, 2008.

(2) It extends to the whole of India.

(3) It shall come into force on such date1 as the Central Government may, by notification in the Official Gazette, appoint: Provided that different dates may be appointed for different provisions of this Act and any reference in any such provision to the commencement of this Act shall be construed as a reference to the coming into force of that provision.

2. Definitions.-(1) In this Act, unless the context otherwise requires,- (a) "address", in relation to a partner of a limited liability partnership, means- (i) if an individual, his usual residential address; and (ii) if a body corporate, the address of its registered office; (b) "advocate" means an advocate as defined in clause (a) of sub-section (1) of section 2 of the Advocates Act, 1961 (25 of 1961); (c) "Appellate Tribunal" means the National Company Law Appellate Tribunal constituted under sub-section (1) of section 10FR of the Companies Act, 1956 (1 of 1956); (d) "body corporate" means a company as defined in section 3 of the Companies Act, 1956 (1 of 1956) and includes- (i) a limited liability partnership registered under this Act; (ii) a limited liability partnership incorporated outside India; and (iii) a company incorporated outside India, but does not include- (i) a corporation sole; (ii) a co-operative society registered under any law for the time being in force; and (iii) any other body corporate (not being a company as defined in section 3 of the Companies Act, 1956 (1 of 1956) or a limited liability partnership as defined in this Act), which the Central Government may, by notification in the Official Gazette, specify in this behalf; (e) "business" includes every trade, profession, service and occupation; (f) "chartered accountant" means a chartered accountant as defined in clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 (38 of 1949) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act; 1. 31st March, 2009, vide notification No. S.O. 891 (E), dated 31st March, 2009, see Gazette of India, Extraordinary, Part II, Sec. 3(ii). 6 (g) "company secretary" means a company secretary as defined in clause (c) of sub-section (1) of section 2 of the Company Secretaries

Act, 1980 (56 of 1980) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act; (h) "cost accountant" means a cost accountant as defined in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959) and who has obtained a certificate of practice under sub-section (1) of section 6 of that Act; (i) "Court", with respect to any offence under this Act, means the Court having jurisdiction as per the provisions of section 77; (j) "designated partner" means any partner designated as such pursuant to section 7; (k) "entity" means any body corporate and includes, for the purposes of sections 18, 46, 47, 48, 49, 50, 52 and 53, a firm setup under the Indian Partnership Act, 1932 (9 of 1932); (l) "financial year", in relation to a limited liability partnership, means the period from the 1st day of April of a year to the 31st day of March of the following year: Provided that in the case of a limited liability partnership incorporated after the 30th day of September of a year, the financial year may end on the 31st day of March of the year next following that year; (m)"foreign limited liability partnership" means a limited liability partnership formed, incorporated or registered outside India which establishes a place of business within India; (n) "limited liability partnership" means a partnership formed and registered under this Act; (o) "limited liability partnership agreement" means any written agreement between the partners of the limited liability partnership or between the limited liability partnership and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that limited liability partnership; (p) "name", in relation to a partner of a limited liability partnership, means- (i) if an individual, his forename, middle name and surname; and (ii) if a body corporate, its registered name; (q) "partner", in relation to a limited liability partnership, means any person who becomes a partner in the limited liability partnership in accordance with the limited liability partnership agreement; (r) "prescribed" means prescribed by rules made under this Act; (s) "Registrar" means a Registrar,

or an Additional, a Joint, a Deputy or an Assistant Registrar, having the duty of registering companies under the Companies Act, 1956 (1 of 1956); (t) "Schedule" means a Schedule to this Act; (u) "Tribunal" means the National Company Law Tribunal constituted under sub-section (1) of section 10FB of the Companies Act, 1956 (1 of 1956). (2) Words and expressions used and not defined in this Act but defined in the Companies Act, 1956 (1 of 1956) shall have the meanings respectively assigned to them in that Act.

NATURE OF LIMITED LIABILITY PARTNERSHIP

Limited Liability Partnership (LLP) has the following features:

Recently most entrepreneurs have started opting for Limited Liability Partnership, considering it has most positive features of Partnership and Companies. It is hybrid form which incorporates benefits of both partnership and companies. It has the following features:

- The liability of each partner is limited to the contribution mention in agreement.
- The cost of formation is limited.
- Less restriction and compliance.
- Separate Legal Entity
- A limited liability partnership is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners.
- A limited liability partnership shall have perpetual succession.
- Any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.
- Non-applicability of the Indian Partnership Act, 1932.-Save as otherwise provided, the provisions of the Indian Partnership Act, 1932 (9 of 1932) shall not apply to a limited liability partnership.

- Partners.-Any individual or body corporate may be a partner in a limited liability partnership: Provided that an individual shall not be capable of becoming a partner of a limited liability partnership, if- (a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force; (b) he is an undischarged insolvent; or (c) he has applied to be adjudicated as an insolvent and his application is pending.
- Minimum number of partners.-(1) Every limited liability partnership shall have at least two partners. (2) If at any time the number of partners of a limited liability partnership is reduced below two and the limited liability partnership carries on business for more than six months while the number is so reduced, the person, who is the only partner of the limited liability partnership during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the limited liability partnership incurred during that period.
- Designated partners.-(1) Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India: Provided that in case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners. Explanation.-For the purposes of this section, the term "resident in India" means a person who has stayed in India for a period of not less than one hundred and eighty-two days during the immediately preceding one year. (2) Subject to the provisions of sub-section (1),- (i) if the incorporation document- (a) specifies who are to be designated partners, such persons shall be designated partners on incorporation; or (b) states that each of the partners from time to time of limited liability partnership is to be designated partner, every such partner shall be a designated partner; (ii) any partner may become a designated partner by and in accordance

with the limited liability partnership agreement and a partner may cease to be a designated partner in accordance with limited liability partnership agreement.

- An individual shall not become a designated partner in any limited liability partnership unless he has given his prior consent to act as such to the limited liability partnership in such form and manner as may be prescribed.

- Every limited liability partnership shall file with the registrar the particulars of every individual who has given his consent to act as designated partner in such form and manner as may be prescribed within thirty days of his appointment.

- An individual eligible to be a designated partner shall satisfy such conditions and requirements as may be prescribed.

- Every designated partner of a limited liability partnership shall obtain a Designated Partner Identification Number (DPIN) from the Central Government and the provisions of sections 266A to 266G 8 (both inclusive) of the Companies Act, 1956 (1 of 1956) shall apply mutatis mutandis for the said purpose.

- Liabilities of designated partners.-Unless expressly provided otherwise in this Act, a designated partner shall be- (a) responsible for the doing of all acts, matters and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement and the like report pursuant to the provisions of this Act and as may be specified in the limited liability partnership agreement; and (b) liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

- Changes in designated partners.-A limited liability partnership may appoint a designated partner within thirty days of a vacancy arising for any reason and provisions of sub-section (4) and sub-section (5) of section 7 shall apply in respect of such new designated partner: Provided that if no designated partner is appointed, or if at any time there is only one designated partner, each partner shall be deemed to be a designated partner. 10. Punishment for contravention

of sections 7, 8 and 9.-(1) If the limited liability partnership contravenes the provisions of sub-section (1) of section 7, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees. (2) If the limited liability partnership contravenes the provisions of sub-section (4) and sub-section (5) of section 7, section 8 or section 9, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

INCORPORATION OF LIMITED LIABILITY PARTNERSHIP AND MATTERS INCIDENTAL THERETO

Incorporation document.-

(1) For a limited liability partnership to be incorporated,- (a) two or more persons associated for carrying on a lawful business with a view to profit shall subscribe their names to an incorporation document; (b) the incorporation document shall be filed in such manner and with such fees, as may be prescribed with the Registrar of the State in which the registered office of the limited liability partnership is to be situated; and (c) there shall be filed along with the incorporation document, a statement in the prescribed form, made by either an advocate, or a Company Secretary or a Chartered Accountant or a Cost Accountant, who is engaged in the formation of the limited liability partnership and by any one who subscribed his name to the incorporation document, that all the requirements of this Act and the rules made thereunder have been complied with, in respect of incorporation and matters precedent and incidental thereto.

(2) The incorporation document shall- (a) be in a form as may be prescribed; (b) state the name of the limited liability partnership; (c) state the proposed business of the limited liability partnership; (d) state the address of the registered office of the limited liability partnership; (e) state the name and address of each of the persons who are to be partners of the limited liability partnership on incorporation; 9 (f) state the name and address of the persons who are to be

designated partners of the limited liability partnership on incorporation; (g) contain such other information concerning the proposed limited liability partnership as may be prescribed.

(3) If a person makes a statement under clause (c) of sub-section (1) which he- (a) knows to be false; or (b) does not believe to be true, shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees. 12. Incorporation by registration.-(1) When the requirements imposed by clauses (b) and (c) of sub-section (1) of section 11 have been complied with, the Registrar shall retain the incorporation document and, unless the requirement imposed by clause (a) of that sub-section has not been complied with, he shall, within a period of fourteen days- (a) register the incorporation document; and (b) give a certificate that the limited liability partnership is incorporated by the name specified therein. (2) The Registrar may accept the statement delivered under clause (c) of sub-section (1) of section 11 as sufficient evidence that the requirement imposed by clause (a) of that sub-section has been complied with.

(3) The certificate issued under clause (b) of sub-section (1) shall be signed by the Registrar and authenticated by his official seal.

(4) The certificate shall be conclusive evidence that the limited liability partnership is incorporated by the name specified therein. 13. Registered office of limited liability partnership and change therein.-(1) Every limited liability partnership shall have a registered office to which all communications and notices may be addressed and where they shall be received. (2) A document may be served on a limited liability partnership or a partner or designated partner thereof by sending it by post under a certificate of posting or by registered post or by any other manner, as may be prescribed, at the registered office and any other address specifically declared by the limited liability partnership for the purpose in such form and manner as may be prescribed.

(5) A limited liability partnership may change the place of its registered office and file the notice of such change with the Registrar in such form and manner

and subject to such conditions as may be prescribed and any such change shall take effect only upon such filing.

(6) If the limited liability partnership contravenes any provisions of this section, the limited liability partnership and its every partner shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

(7) Effect of registration.-On registration, a limited liability partnership shall, by its name, be capable of- (a) suing and being sued; (b) acquiring, owning, holding and developing or disposing of property, whether movable or immovable, tangible or intangible; (c) having a common seal, if it decides to have one; and (d) doing and suffering such other acts and things as bodies corporate may lawfully do and suffer. Name.-(1) Every limited liability partnership shall have either the words "limited liability partnership" or the acronym "LLP" as the last words of its name. 10 (2) No limited liability partnership shall be registered by a name which, in the opinion of the Central Government is- (a) undesirable; or (b) identical or too nearly resembles to that of any other partnership firm or limited liability partnership or body corporate or a registered trade mark, or a trade mark which is the subject matter of an application for registration of any other person under the Trade Marks Act, 1999 (47 of 1999). 16. Reservation of name.-(1) A person may apply in such form and manner and accompanied by such fee as may be prescribed to the Registrar for the reservation of a name set out in the application as- (a) the name of a proposed limited liability partnership; or (b) the name to which a limited liability partnership proposes to change its name. (2) Upon receipt of an application under sub-section (1) and on payment of the prescribed fee, the Registrar may, if he is satisfied, subject to the rules prescribed by the Central Government in the matter, that the name to be reserved is not one which may be rejected on any ground referred to in sub-section (2) of section 15, reserve the name for a period of three months from the date of intimation by the Registrar.

(8) Change of name of limited liability partnership.-(1) Notwithstanding anything contained in sections 15 and 16, where the Central Government is

satisfied that a limited liability partnership has been registered (whether through inadvertence or otherwise and whether originally or by a change of name) under a name which- (a) is a name referred to in sub-section (2) of section 15; or (b) is identical with or too nearly resembles the name of any other limited liability partnership or body corporate or other name as to be likely to be mistaken for it, the Central Government may direct such limited liability partnership to change its name, and the limited liability partnership shall comply with the said direction within three months after the date of the direction or such longer period as the Central Government may allow.

(9) Any limited liability partnership which fails to comply with a direction given under sub-section (1) shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to five lakh rupees and the designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

(10) Application for direction to change name in certain circumstances (1) Any entity which already has a name similar to the name of a limited liability partnership which has been incorporated subsequently, may apply, in such manner as may be prescribed, to the Registrar to give a direction to any limited liability partnership, on a ground referred to in section 17 to change its name.

(11) The Registrar shall not consider any application under sub-section (1) to give a direction to a limited liability partnership on the ground referred to in clause (b) of sub-section (1) of section 17 unless the Registrar receives the application within twenty-four months from the date of registration of the limited liability partnership under that name.

(12). Change of registered name.-Any limited liability partnership may change its name registered with the Registrar by filing with him a notice of such change in such form and manner and on payment of such fees as may be prescribed. 20. Penalty for improper use of words "limited liability partnership" or "LLP".- If any person or persons carry on business under any name or title of which the

words "Limited Liability Partnership" or "LLP" or any contraction or imitation thereof is or are the last word or words, that person or each of those persons shall, unless duly incorporated as limited liability partnership, be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees. Publication of name and limited liability.-(1) Every limited liability partnership shall ensure that its invoices, official correspondence and publications bear the following, namely:- (a) the name, address of its registered office and registration number of the limited liability partnership; and (b) a statement that it is registered with limited liability. (2) Any limited liability partnership which contravenes the provisions of sub-section (1) shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

PARTNERS AND THEIR RELATIONS

Eligibility to be partners : On the incorporation of a limited liability partnership, the persons who subscribed their names to the incorporation document shall be its partners and any other person may become a partner of the limited liability partnership by and in accordance with the limited liability partnership agreement.

(1) Save as otherwise provided by this Act, the mutual rights and duties of the partners of a limited liability partnership, and the mutual rights and duties of a limited liability partnership and its partners, shall be governed by the limited liability partnership agreement between the partners, or between the limited liability partnership and its partners.

(2) The limited liability partnership agreement and any changes, if any, made therein shall be filed with the Registrar in such form, manner and accompanied by such fees as may be prescribed.

(3) An agreement in writing made before the incorporation of a limited liability partnership between the persons who subscribe their names to the incorporation document may impose obligations on the limited liability partnership, provided

such agreement is ratified by all the partners after the incorporation of the limited liability partnership.

(4) In the absence of agreement as to any matter, the mutual rights and duties of the partners and the mutual rights and duties of the limited liability partnership and the partners shall be determined by the provisions relating to that matter as are set-out in the First Schedule. 24. Cessation of partnership interest.-(1) A person may cease to be a partner of a limited liability partnership in accordance with an agreement with the other partners or, in the absence of agreement with the other partners as to cessation of being a partner, by giving a notice in writing of not less than thirty days to the other partners of his intention to resign as partner. (2) A person shall cease to be a partner of a limited liability partnership- (a) on his death or dissolution of the limited liability partnership; or (b) if he is declared to be of unsound mind by a competent court; or (c) if he has applied to be adjudged as an insolvent or declared as an insolvent. (3) Where a person has ceased to be a partner of a limited liability partnership (hereinafter referred to as "former partner"), the former partner is to be regarded (in relation to any person dealing with the limited liability partnership) as still being a partner of the limited liability partnership unless- (a) the person has notice that the former partner has ceased to be a partner of the limited liability partnership; or (b) notice that the former partner has ceased to be a partner of the limited liability partnership has been delivered to the Registrar. 12 (4) The cessation of a partner from the limited liability partnership does not by itself discharge the partner from any obligation to the limited liability partnership or to the other partners or to any other person which he incurred while being a partner.

(5) Where a partner of a limited liability partnership ceases to be a partner, unless otherwise provided in the limited liability partnership agreement, the former partner or a person entitled to his share in consequence of the death or insolvency of the former partner, shall be entitled to receive from the limited liability partnership- (a) an amount equal to the capital contribution of the former partner actually made to the limited liability partnership; and (b) his right to share in the accumulated profits of the limited liability partnership, after the deduction of

accumulated losses of the limited liability partnership, determined as at the date the former partner ceased to be a partner.

(6) A former partner or a person entitled to his share in consequence of the death or insolvency of the former partner shall not have any right to interfere in the management of the limited liability partnership. Registration of changes in partners.-(1) Every partner shall inform the limited liability partnership of any change in his name or address within a period of fifteen days of such change. (2) A limited liability partnership shall- (a) where a person becomes or ceases to be a partner, file a notice with the Registrar within thirty days from the date he becomes or ceases to be a partner; and (b) where there is any change in the name or address of a partner, file a notice with the Registrar within thirty days of such change.

(7) A notice filed with the Registrar under sub-section (2)- (a) shall be in such form and accompanied by such fees as may be prescribed; (b) shall be signed by the designated partner of the limited liability partnership and authenticated in a manner as may be prescribed; and (c) if it relates to an incoming partner, shall contain a statement by such partner that he consents to becoming a partner, signed by him and authenticated in the manner as may be prescribed.

(8) If the limited liability partnership contravenes the provisions of sub-section (2), the limited liability partnership and every designated partner of the limited liability partnership shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

(9) If any partner contravenes the provisions of sub-section (1), such partner shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees.

(10) Any person who ceases to be a partner of a limited liability partnership may himself file with the Registrar the notice referred to in sub-section (3) if he has reasonable cause to believe that the limited liability partnership may not file the notice with the Registrar and in case of any such notice filed by a partner, the Registrar shall obtain a confirmation to this effect from the limited liability

partnership unless the limited liability partnership has also filed such notice: Provided that where no confirmation is given by the limited liability partnership within fifteen days, the registrar shall register the notice made by a person ceasing to be a partner under this section.

EXTENT AND LIMITATION OF LIABILITY OF LIMITED LIABILITY PARTNERSHIP AND PARTNERS

Partner as agent : Every partner of a limited liability partnership is, for the purpose of the business of the limited liability partnership, the agent of the limited liability partnership, but not of other partners. Extent of liability of limited liability partnership.

(1) A limited liability partnership is not bound by anything done by a partner in dealing with a person if- (a) the partner in fact has no authority to act for the limited liability partnership in doing a particular act; and (b) the person knows that he has no authority or does not know or believe him to be a partner of the limited liability partnership.

(2) The limited liability partnership is liable if a partner of a limited liability partnership is liable to any person as a result of a wrongful act or omission on his part in the course of the business of the limited liability partnership or with its authority.

(3) An obligation of the limited liability partnership whether arising in contract or otherwise, shall be solely the obligation of the limited liability partnership.

(4) The liabilities of the limited liability partnership shall be met out of the property of the limited liability partnership. 28. Extent of liability of partner.-(1) A partner is not personally liable, directly or indirectly for an obligation referred to in sub-section (3) of section 27 solely by reason of being a partner of the limited liability partnership. (2) The provisions of sub-section (3) of section 27 and sub-section (1) of this section shall not affect the personal liability of a partner for his own wrongful act or omission, but a partner shall not be personally liable for the wrongful act or omission of any other partner of the limited liability

partnership. 29. Holding out.-(1) Any person, who by words spoken or written or by conduct, represents himself, or knowingly permits himself to be represented to be a partner in a limited liability partnership is liable to any person who has on the faith of any such representation given credit to the limited liability partnership, whether the person representing himself or represented to be a partner does or does not know that the representation has reached the person so giving credit: Provided that where any credit is received by the limited liability partnership as a result of such representation, the limited liability partnership shall, without prejudice to the liability of the person so representing himself or represented to be a partner, be liable to the extent of credit received by it or any financial benefit derived thereon.

(5) Where after a partner's death the business is continued in the same limited liability partnership name, the continued use of that name or of the deceased partner's name as a part thereof shall not of itself make his legal representative or his estate liable for any act of the limited liability partnership done after his death. 30. Unlimited liability in case of fraud.-(1) In the event of an act carried out by a limited liability partnership, or any of its partners, with intent to defraud creditors of the limited liability partnership or any other person, or for any fraudulent purpose, the liability of the limited liability partnership and partners who acted with intent to defraud creditors or for any fraudulent purpose shall be unlimited for all or any of the debts or other liabilities of the limited liability partnership: Provided that in case any such act is carried out by a partner, the limited liability partnership is liable to the same extent as the partner unless it is established by the limited liability partnership that such act was without the knowledge or the authority of the limited liability partnership.

(6) Where any business is carried on with such intent or for such purpose as mentioned in sub-section (1), every person who was knowingly a party to the carrying on of the business in the manner aforesaid shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees. (3) Where a limited liability partnership or any partner or designated

partner or employee of such limited liability partnership has conducted the affairs of the limited liability partnership in a fraudulent manner, then without prejudice to any criminal proceedings which may arise under any law for the time being in force, the limited liability partnership and any such partner or designated partner or employee 14 shall be liable to pay compensation to any person who has suffered any loss or damage by reason of such conduct: Provided that such limited liability partnership shall not be liable if any such partner or designated partner or employee has acted fraudulently without knowledge of the limited liability partnership. Whistle blowing.-(1) The Court or Tribunal may reduce or waive any penalty leviable against any partner or employee of a limited liability partnership, if it is satisfied that- (a) such partner or employee of a limited liability partnership has provided useful information during investigation of such limited liability partnership; or (b) when any information given by any partner or employee (whether or not during investigation) leads to limited liability partnership or any partner or employee of such limited liability partnership being convicted under this Act or any other Act. (2) No partner or employee of any limited liability partnership may be discharged, demoted, suspended, threatened, harassed or in any other manner discriminated against the terms and conditions of his limited liability partnership or employment merely because of his providing information or causing information to be provided pursuant to sub-section (1).

CONTRIBUTION

Form of contribution

(1) A contribution of a partner may consist of tangible, movable or immovable or intangible property or other benefit to the limited liability partnership, including money, promissory notes, other agreements to contribute cash or property, and contracts for services performed or to be performed.

(2) The monetary value of contribution of each partner shall be accounted for and disclosed in the accounts of the limited liability partnership in the manner as may be prescribed. 33. Obligation to contribute.-(1) The obligation of a partner to contribute money or other property or other benefit or to perform

services for a limited liability partnership shall be as per the limited liability partnership agreement. (2) A creditor of a limited liability partnership, which extends credit or otherwise acts in reliance on an obligation described in that agreement, without notice of any compromise between partners, may enforce the original obligation against such partner.

FINANCIAL DISCLOSURE

Maintenance of books of account, other records and audit, etc.

(1) The limited liability partnership shall maintain such proper books of account as may be prescribed relating to its affairs for each year of its existence on cash basis or accrual basis and according to double entry system of accounting and shall maintain the same at its registered office for such period as may be prescribed.

(2) Every limited liability partnership shall, within a period of six months from the end of each financial year, prepare a Statement of Account and Solvency for the said financial year as at the last day of the said financial year in such form as may be prescribed, and such statement shall be signed by the designated partners of the limited liability partnership.

(3) Every limited liability partnership shall file within the prescribed time, the Statement of Account and Solvency prepared pursuant to sub-section (2) with the Registrar every year in such form and manner and accompanied by such fees as may be prescribed.

(4) The accounts of limited liability partnerships shall be audited in accordance with such rules as may be prescribed: Provided that the Central Government may, by notification in the Official Gazette, exempt any class or classes of limited liability partnerships from the requirements of this sub-section.

(5) Any limited liability partnership which fails to comply with the provisions of this section shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every

designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

(6) Annual return.-(1) Every limited liability partnership shall file an annual return duly authenticated with the Registrar within sixty days of closure of its financial year in such form and manner and accompanied by such fee as may be prescribed.

(7) Any limited liability partnership which fails to comply with the provisions of this section shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.

(8) If the limited liability partnership contravenes the provisions of this section, the designated partner of such limited liability partnership shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees. 36. Inspection of documents kept by Registrar.-The incorporation document, names of partners and changes, if any, made therein, Statement of Account and Solvency and annual return filed by each limited liability partnership with the Registrar shall be available for inspection by any person in such manner and on payment of such fee as may be prescribed. 37. Penalty for false statement.-If in any return, statement or other document required by or for the purposes of any of the provisions of this Act, any person makes a statement- (a) which is false in any material particular, knowing it to be false; or (b) which omits any material fact knowing it to be material, he shall, save as otherwise expressly provided in this Act, be punishable with imprisonment for a term which may extend to two years, and shall also be liable to fine which may extend to five lakh rupees but which shall not be less than one lakh rupees. 38. Power of Registrar to obtain information.-(1) In order to obtain such information as the Registrar may consider necessary for the purposes of carrying out the provisions of this Act, the Registrar may require any person including any present or former partner or designated partner or employee of a limited liability partnership to

answer any question or make any declaration or supply any details or particulars in writing to him within a reasonable period. (2) In case any person referred to in sub-section (1) does not answer such question or make such declaration or supply such details or particulars asked for by the Registrar within a reasonable time or time given by the Registrar or when the Registrar is not satisfied with the reply or declaration or details or particulars provided by such person, the Registrar shall have power to summon that person to appear before him or an inspector or any other public officer whom the Registrar may designate, to answer any such question or make such declaration or supply such details, as the case may be.

(9) Any person who, without lawful excuse, fails to comply with any summons or requisition of the Registrar under this section shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees. 39. Compounding of offences.-The Central Government may compound any offence under this Act which is punishable with fine only, by collecting from a person reasonably suspected of having committed the offence, a sum which may extend to the amount of the maximum fine prescribed for the offence. 40. Destruction of old records.-The Registrar may destroy any document filed or registered with him in physical form or in electronic form in accordance with such rules as may be prescribed. 41. Enforcement of duty to make returns, etc.-(1) If any limited liability partnership is in default in complying with- (a) any provisions of this Act or of any other law which requires the filing in any manner with the Registrar of any return, account or other document or the giving of notice to him of any matter; or 16 (b) any request of the Registrar to amend or complete and resubmit any document or to submit a fresh document, and fails to make good the default within fourteen days after the service on the limited liability partnership of a notice requiring it to be done, the Tribunal may, on application by the Registrar, make an order directing that limited liability partnership or its designated partners or its partners to make good the default within such time as specified in the order. (2) Any such order may provide that all the costs of and incidental to the application shall be borne by that limited

liability partnership. (3) Nothing in this section shall limit the operation of any other provision of this Act or any other law imposing penalties in respect of any default referred to in this section on that limited liability partnership.

ASSIGNMENT AND TRANSFER OF PARTNERSHIP RIGHTS

Partner's transferable interest.-

(1) The rights of a partner to a share of the profits and losses of the limited liability partnership and to receive distributions in accordance with the limited liability partnership agreement are transferable either wholly or in part.

(2) The transfer of any right by any partner pursuant to sub-section (1) does not by itself cause the disassociation of the partner or a dissolution and winding up of the limited liability partnership.

(3) The transfer of right pursuant to this section does not, by itself, entitle the transferee or assignee to participate in the management or conduct of the activities of the limited liability partnership, or access information concerning the transactions of the limited liability partnership.

INVESTIGATION

Investigation of the affairs of limited liability partnership.-

(1) The Central Government shall appoint one or more competent persons as inspectors to investigate the affairs of a limited liability partnership and to report thereon in such manner as it may direct if- (a) the Tribunal, either suo motu, or on an application received from not less than one-fifth of the total number of partners of limited liability partnership, by order, declares that the affairs of the limited liability partnership ought to be investigated; or (b) any Court, by order, declares that the affairs of a limited liability partnership ought to be investigated.

(2) The Central Government may appoint one or more competent persons as inspectors to investigate the affairs of a limited liability partnership and to report on them in such manner as it may direct.

(3) The appointment of inspectors pursuant to sub-section (2) may be made,-

(a) if not less than one-fifth of the total number of partners of the limited liability partnership make an application along with supporting evidence and security amount as may be prescribed; or

(b) if the limited liability partnership makes an application that the affairs of the limited liability partnership ought to be investigated; or

(c) if, in the opinion of the Central Government, there are circumstances suggesting-

(i) that the business of the limited liability partnership is being or has been conducted with an intent to defraud its creditors, partners or any other person, or otherwise for a fraudulent or unlawful purpose, or in a manner oppressive or unfairly prejudicial to some or any of its partners, or that the limited liability partnership was formed for any fraudulent or unlawful purpose; or

(ii) that the affairs of the limited liability partnership are not being conducted in accordance with the provisions of this Act; or 17

(iii) that, on receipt of a report of the Registrar or any other investigating or regulatory agency, there are sufficient reasons that the affairs of the limited liability partnership ought to be investigated. 44. Application by partners for investigation.-An application by partners of the limited liability partnership under clause (a) of sub-section (1) of section 43 shall be supported by such evidence as the Tribunal may require for the purpose of showing that the applicants have good reason for requiring the investigation and the Central Government may, before appointing an inspector, require the applicants to give security, of such amount as may be prescribed, for payment of costs of the investigation. 45. Firm, body corporate or association not to be appointed as inspector.- No firm, body corporate or other association shall be appointed as an inspector. 46. Power of inspectors to carry out investigation into affairs

of related entities, etc.-(1) If an inspector appointed by the Central Government to investigate the affairs of a limited liability partnership thinks it necessary for the purposes of his investigation to investigate also the affairs of an entity which has been associated in the past or is presently associated with the limited liability partnership or any present or former partner or designated partner of the limited liability partnership, the inspector shall have the power to do so and shall report on the affairs of the other entity or partner or designated partner, so far as he thinks that the results of his investigation thereof are relevant to the investigation of the affairs of the limited liability partnership. (2) In the case of any entity or partner or designated partner referred to in sub-section (1), the inspector shall not exercise his power of investigating into, and reporting on, its or his affairs without obtaining the prior approval of the Central Government thereto: Provided that before according approval under this sub-section, the Central Government shall give the entity or partner or designated partner a reasonable opportunity to show cause why such approval should not be accorded. 47. Production of documents and evidence.-(1) It shall be the duty of the designated partner and partners of the limited liability partnership-

(a) to preserve and to produce before an inspector or any person authorised by him in this behalf with the previous approval of the Central Government, all books and papers of, or relating to, the limited liability partnership or, as the case may be, the other entity, which are in their custody or power; and

(b) otherwise to give to the inspector all assistance in connection with the investigation which they are reasonably able to give.

(4) The inspector may, with the previous approval of the Central Government, require any entity other than an entity referred to in sub-section (1) to furnish such information to, or produce such books and papers before him or any person authorised by him in this behalf, with the previous approval of that Government,

as he may consider necessary, if the furnishing of such information or the production of such books and papers is relevant or necessary for the purposes of his investigation.

(5) The inspector may keep in his custody any books and papers produced under sub-section (1) or sub-section (2) for thirty days and thereafter shall return the same to the limited liability partnership, other entity or individual by whom or on whose behalf the books and papers are produced: Provided that the inspector may call for the books and papers if they are needed again: Provided further that if certified copies of the books and papers produced under sub-section (2) are furnished to the inspector, he shall return those books and papers to the entity or person concerned.

(6) An inspector may examine on oath-

(a) any of the persons referred to in sub-section (1);

(b) with the previous approval of the Central Government, any other person in relation to the affairs of the limited liability partnership or any other entity, as the case may be; and 18 (c) may administer an oath accordingly and for that purpose may require any of those persons to appear before him personally.

(7) If any person fails without reasonable cause or refuses-

(a) to produce before an inspector or any person authorised by him in this behalf with the previous approval of the Central Government any book or paper which it is his duty under sub-section (1) or sub-section (2) to produce; or

(b) to furnish any information which is his duty under sub-section (2) to furnish; or

(c) to appear before the inspector personally when required to do so under sub-section (4) or to answer any question which is put to him by the inspector in pursuance of that sub-section; or

(d) to sign the notes of any examination, he shall be punishable with fine which shall not be less than two thousand rupees but which may extend to twenty-five thousand rupees and with a further fine which shall not be less than fifty rupees but which may extend to five hundred rupees for every day after the first day after which the default continues.

(8) The notes of any examination under sub-section (4) shall be taken down in writing and signed by the person whose examination was made on oath and a copy of such notes shall be given to the person so examined on oath and thereafter be used as an evidence by the inspector. 48. Seizure of documents by inspector.-(1) Where in the course of investigation, the inspector has reasonable ground to believe that the books and papers of, or relating to, the limited liability partnership or other entity or partner or designated partner of such limited liability partnership may be destroyed, mutilated, altered, falsified or secreted, the inspector may make an application to the Judicial Magistrate of the first class, or, as the case may be, the Metropolitan Magistrate, having jurisdiction, for an order for the seizure of such books and papers.

(9) After considering the application and hearing the inspector, if necessary, the Magistrate may, by order, authorise the inspector-

(a) to enter, with such assistance, as may be required, the place or places where such books and papers are kept;

(b) to search that place or those places in the manner specified in the order; and

(c) to seize books and papers which the inspector considers it necessary for the purposes of his investigation.

(10) The inspector shall keep in his custody the books and papers seized under this section for such period not later than the conclusion of the investigation as he considers necessary and thereafter shall return the same to the concerned entity or person from whose custody or power they were seized

and inform the Magistrate of such return: Provided that the books and papers shall not be kept seized for a continuous period of more than six months: Provided further that the inspector may, before returning such books and papers as aforesaid, place identification marks on them or any part thereof.

(11) Save as otherwise provided in this section, every search or seizure made under this section shall be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973 (2 of 1974) relating to searches or seizures made under that Code. 49. Inspector's report.-(1) The Inspector may, and if so directed by the Central Government, shall make interim reports to that Government, and on the conclusion of the investigation, shall make a final report to the Central Government and any such report shall be written or printed, as the Central Government may direct. 19 (2) The Central Government-

(a) shall forward a copy of any report (other than an interim report) made by the inspectors to the limited liability partnership at its registered office, and also to any other entity or person dealt with or related to the report; and

(b) may, if it thinks fit, furnish a copy thereof, on request and on payment of the prescribed fee, to any person or entity related to or affected by the report. 50. Prosecution.-If, from the report under section 49, it appears to the Central Government that any person in relation to the limited liability partnership or in relation to any other entity whose affairs have been investigated, has been guilty of any offence for which he is liable, the Central Government may prosecute such person for the offence; and it shall be the duty of all partners, designated partners and other employees and agents of the limited liability partnership or other entity, as the case may be, to give the Central Government all assistance in connection with the prosecution which they are reasonably able to give. 51. Application for winding up of limited liability partnership.-If any such limited liability partnership is liable to be wound up under this Act or any other law for the time being in force, and it appears to the

Central Government from any such report under section 49 that it is expedient to do so by reason of any such circumstances as are referred to in sub-clause (i) or sub-clause (ii) of clause (c) of sub-section (3) of section 43, the Central Government may, unless the limited liability partnership is already being wound up by the Tribunal, cause to be presented to the Tribunal by any person authorised by the Central Government in this behalf, a petition for the winding up of the limited liability partnership on the ground that it is just and equitable that it should be wound up. 52. Proceedings for recovery of damages or property.-If, from any report under section 49, it appears to the Central Government that proceedings ought, in the public interest, to be brought by the limited liability partnership or any entity whose affairs have been investigated,-

(a) for the recovery of damages in respect of any fraud, misfeasance or other misconduct in connection with the promotion or formation, or the management of the affairs, of such limited liability partnership or such other entity; or

(b) for the recovery of any property of such limited liability partnership or such other entity, which has been misapplied or wrongfully retained, the Central Government may itself bring proceedings for that purpose. 53. Expenses of investigation.-(1) The expenses of, and incidental to, an investigation by an inspector appointed by the Central Government under this Act shall be defrayed in the first instance by the Central Government; but the following persons shall, to the extent mentioned below, be liable to reimburse the Central Government in respect of such expenses, namely:-

(a) any person who is convicted on a prosecution, or who is ordered to pay damages or restore any property in proceedings brought by virtue of section 52, may, in the same proceedings, be ordered to pay the said expenses to such extent as may be specified by the court convicting such person, or ordering him to pay such damages or restore such property, as the case may be;

(b) any entity in whose name proceedings are brought as aforesaid shall be liable, to the extent of the amount or value of any sums or property recovered by it as a result of the proceedings; and

(c) unless, as a result of the investigation, a prosecution is instituted in pursuance of section 50,- (i) any entity, a partner or designated partner or any other person dealt with by the report of the inspector shall be liable to reimburse the Central Government in respect of the whole of the expenses, unless and except in so far as, the Central Government otherwise directs; and (ii) the applicants for the investigation, where the inspector was appointed in pursuance of the provisions of clause (a) of sub-section (1) of section 43, shall be liable to such extent, if any, as the Central Government may direct. 20 (2) Any amount for which a limited liability partnership or other entity is liable by virtue of clause (b) of sub-section (1) shall be a first charge on the sums or property mentioned in that clause. (3) The amount of expenses in respect of which any limited liability partnership, other entity, a partner or designated partner or any other person is liable under sub-clause (i) of clause (c) of sub-section (1) to reimburse the Central Government shall be recoverable as arrears of land revenue. (4) For the purposes of this section, any costs or expenses incurred by the Central Government or in connection with the proceedings brought by virtue of section 52 shall be treated as expenses of the investigation giving rise to the proceedings. 54. Inspector's report to be evidence. A copy of any report of any inspector or inspectors appointed under the provisions of this Act, authenticated in such manner, if any, as may be prescribed, shall be admissible in any legal proceeding as evidence in relation to any matter contained in the report.

CONVERSION INTO LIMITED LIABILITY PARTNERSHIP

Conversion from firm into limited liability partnership.-

A firm may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Second Schedule. 56. Conversion from

private company into limited liability partnership.-A private company may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Third Schedule. 57. Conversion from unlisted public company into limited liability partnership.-An unlisted public company may convert into a limited liability partnership in accordance with the provisions of this Chapter and the Fourth Schedule. 58. Registration and effect of conversion.-

(1) The Registrar, on satisfying that a firm, private company or an unlisted public company, as the case may be, has complied with the provisions of the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be, shall, subject to the provisions of this Act and the rules made thereunder, register the documents submitted under such Schedule and issue a certificate of registration in such form as the Registrar may determine stating that the limited liability partnership is, on and from the date specified in the certificate, registered under this Act: Provided that the limited liability partnership shall, within fifteen days of the date of registration, inform the concerned Registrar of Firms or Registrar of Companies, as the case may be, with which it was registered under the provisions of the Indian Partnership Act, 1932 (9 of 1932) or the Companies Act, 1956 (1 of 1956) as the case may be, about the conversion and of the particulars of the limited liability partnership in such form and manner as may be prescribed.

(2) Upon such conversion, the partners of the firm, the shareholders of private company or unlisted public company, as the case may be, the limited liability partnership to which such firm or such company has converted, and the partners of the limited liability partnership shall be bound by the provisions of the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be, applicable to them.

(3) Upon such conversion, on and from the date of certificate of registration, the effects of the conversion shall be such as specified in the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be.

(4) Notwithstanding anything contained in any other law for the time being

in force, on and from the date of registration specified in the certificate of registration issued under the Second Schedule, the Third Schedule or the Fourth Schedule, as the case may be,-

(a) there shall be a limited liability partnership by the name specified in the certificate of registration registered under this Act;

(b) all tangible (movable or immovable) and intangible property vested in the firm or the company, as the case may be, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, as the case may be, and the whole of the undertaking of the firm or the 21 company, as the case may be, shall be transferred to and shall vest in the limited liability partnership without further assurance, act or deed; and

(c) the firm or the company, as the case may be, shall be deemed to be dissolved and removed from the records of the Registrar of Firms or Registrar of Companies, as the case may be.

FOREIGN LIMITED LIABILITY PARTNERSHIPS

Foreign limited liability partnerships.-The Central Government may make rules for provisions in relation to establishment of place of business by foreign limited liability partnerships within India and carrying on their business therein by applying or incorporating, with such modifications, as appear appropriate, the provisions of the Companies Act, 1956 (1 of 1956) or such regulatory mechanism with such composition as may be prescribed.

COMPROMISE, ARRANGEMENT OR RECONSTRUCTION OF LIMITED LIABILITY PARTNERSHIPS

Compromise, or arrangement of limited liability partnerships.-

(1) Where a compromise or arrangement is proposed-

(a) between a limited liability partnership and its creditors; or

(b) between a limited liability partnership and its partners, the Tribunal may, on the application of the limited liability partnership or of any creditor or partner of the limited liability partnership, or, in the case of a limited liability partnership which is being wound up, of the liquidator, order a meeting of the creditors or of the partners, as the case may be, to be called, held and conducted in such manner as may be prescribed or as the Tribunal directs.

(2) If a majority representing three-fourths in value of the creditors, or partners, as the case may be, at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the Tribunal, by order be binding on all the creditors or all the partners, as the case may be, and also on the limited liability partnership, or in the case of a limited liability partnership which is being wound up, on the liquidator and contributories of the limited liability partnership: Provided that no order sanctioning any compromise or arrangement shall be made by the Tribunal unless the Tribunal is satisfied that the limited liability partnership or any other person by whom an application has been made under sub-section (1) has disclosed to the Tribunal, by affidavit or otherwise, all material facts relating to the limited liability partnership, including the latest financial position of the limited liability partnership and the pendency of any investigation proceedings in relation to the limited liability partnership.

(3) An order made by the Tribunal under sub-section (2) shall be filed by the limited liability partnership with the Registrar within thirty days after making such an order and shall have effect only after it is so filed.

(4) If default is made in complying with sub-section (3), the limited liability partnership, and every designated partner of the limited liability partnership shall be punishable with fine which may extend to one lakh rupees.

(5) The Tribunal may, at any time after an application has been made to it under this section, stay the commencement or continuation of any suit or proceeding against the limited liability partnership on such terms as the

Tribunal thinks fit, until the application is finally disposed of. 61. Power of Tribunal to enforce compromise or arrangement.-(1) Where the Tribunal makes an order under section 60 sanctioning a compromise or an arrangement in respect of a limited liability partnership, it-

(a) shall have power to supervise the carrying out of the compromise or an arrangement; and 22

(b) may, at the time of making such order or at any time thereafter, give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper working of the compromise or arrangement.

(2) If the Tribunal aforesaid is satisfied that a compromise or an arrangement sanctioned under section 60 cannot be worked satisfactorily with or without modifications, it may, either on its own motion or on the application of any person interested in the affairs of the limited liability partnership, make an order for winding up the limited liability partnership, and such an order shall be deemed to be an order made under section 64 of this Act. 62. Provisions for facilitating reconstruction or amalgamation of limited liability partnerships.-(1) Where an application is made to the Tribunal under section 60 for sanctioning of a compromise or arrangement proposed between a limited liability partnership and any such persons as are mentioned in that section, and it is shown to the Tribunal that-

(a) compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of any limited liability partnership or limited liability partnerships, or the amalgamation of any two or more limited liability partnerships; and

(b) under the scheme the whole or any part of the undertaking, property or liabilities of any limited liability partnership concerned in the scheme (in

this section referred to as a "transferor limited liability partnership") is to be transferred to another limited liability partnership (in this section referred to as the "transferee limited liability partnership"), the Tribunal may, either by the order sanctioning the compromise or arrangement or by a subsequent order, make provisions for all or any of the following matters, namely:- (i) the transfer to the transferee limited liability partnership of the whole or any part of the undertaking, property or liabilities of any transferor limited liability partnership; (ii) the continuation by or against the transferee limited liability partnership of any legal proceedings pending by or against any transferor limited liability partnership; (iii) the dissolution, without winding up, of any transferor limited liability partnership; (iv) the provision to be made for any person who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement; and (v) such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction or amalgamation shall be fully and effectively carried out: Provided that no compromise or arrangement proposed for the purposes of, or in connection with, a scheme for the amalgamation of a limited liability partnership, which is being wound up, with any other limited liability partnership or limited liability partnerships, shall be sanctioned by the Tribunal unless the Tribunal has received a report from the Registrar that the affairs of the limited liability partnership have not been conducted in a manner prejudicial to the interests of its partners or to public interest: Provided further that no order for the dissolution of any transferor limited liability partnership under clause (iii) shall be made by the Tribunal unless the Official Liquidator has, on scrutiny of the books and papers of the limited liability partnership, made a report to the Tribunal that the affairs of the limited liability partnership have not been conducted in a manner prejudicial to the interests of its partners or to public interest.

(6) Where an order under this section provides for the transfer of any property or liabilities, then, by virtue of the order, that property shall be

transferred to and vest in, and those liabilities shall be transferred to and become the liabilities of, the transferee limited liability partnership; and in the case of any property, if the order so directs, freed from any charge which is, by virtue of the compromise or arrangement, to cease to have effect.

(7) Within thirty days after the making of an order under this section, every limited liability partnership in relation to which the order is made shall cause a certified copy thereof to be filed with the Registrar for registration. 23 (4) If default is made in complying with the provisions of sub-section (3), the limited liability partnership, every designated partner of the limited liability partnership shall be punishable with fine which may extend to fifty thousand rupees. Explanation.-In this section "property" includes property, rights and powers of every description; and "liabilities" includes duties of every description.

WINDING UP AND DISSOLUTION

Winding up and dissolution.-The winding up of a limited liability partnership may be either voluntary or by the Tribunal and limited liability partnership, so wound up may be dissolved. 64. Circumstances in which limited liability partnership may be wound up by Tribunal.-A limited liability partnership may be wound up by the Tribunal,-

(a) if the limited liability partnership decides that limited liability partnership be wound up by the Tribunal;

(b) if, for a period of more than six months, the number of partners of the limited liability partnership is reduced below two;

(c) if the limited liability partnership is unable to pay its debts;

(d) if the limited liability partnership has acted against the interests of the sovereignty and integrity of India, the security of the State or public order;

(e) if the limited liability partnership has made a default in filing with the Registrar the Statement of Account and Solvency or annual return for any five consecutive financial years; or

(f) if the Tribunal is of the opinion that it is just and equitable that the limited liability partnership be wound up. 65. Rules for winding up and dissolution.-The Central Government may make rules for the provisions in relation to winding up and dissolution of limited liability partnerships.

MISCELLANEOUS

Business transactions of partner with limited liability partnership.-

A partner may lend money to and transact other business with the limited liability partnership and has the same rights and obligations with respect to the loan or other transactions as a person who is not a partner. 67. Application of the provisions of the Companies Act.-

(1) The Central Government may, by notification in the Official Gazette, direct that any of the provisions of the Companies Act, 1956 (1 of 1956) specified in the notification-

(a) shall apply to any limited liability partnership; or

(b) shall apply to any limited liability partnership with such exception, modification and adaptation, as may be specified, in the notification. (

2) A copy of every notification proposed to be issued under sub-section (1) shall be laid in draft before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in disapproving the issue of the notification or both Houses agree in making any modification in the notification, the notification shall not be issued or, as the case may be, shall be issued only in such modified form as may be agreed upon by both the Houses. 68. Electronic filing of documents.-(1) Any document required to be filed, recorded or registered under this Act may be filed, recorded or registered

in such manner and subject to such conditions as may be prescribed. 24 (2) A copy of or an extract from any document electronically filed with or submitted to the Registrar which is supplied or issued by the Registrar and certified through affixing digital signature as per the Information Technology Act, 2000 (21 of 2000) to be a true copy of or extract from such document shall, in any proceedings, be admissible in evidence as of equal validity with the original document.

(3) Any information supplied by the Registrar that is certified by the Registrar through affixing digital signature to be a true extract from any document filed with or submitted to the Registrar shall, in any proceedings, be admissible in evidence and be presumed, unless evidence to the contrary is adduced, to be a true extract from such document. 69. Payment of additional fee.-Any document or return required to be filed or registered under this Act with the Registrar, if, is not filed or registered in time provided therein, may be filed or registered after that time upto a period of three hundred days from the date within which it should have been filed, on payment of additional fee of one hundred rupees for every day of such delay in addition to any fee as is payable for filing of such document or return: Provided that such document or return may, without prejudice to any other action or liability under this Act, also be filed after such period of three hundred days on payment of fee and additional fee specified in this section. 70. Enhanced punishment.-In case a limited liability partnership or any partner or designated partner of such limited liability partnership commits any offence, the limited liability partnership or any partner or designated partner shall, for the second or subsequent offence, be punishable with imprisonment as provided, but in case of offences for which fine is prescribed either along with or exclusive of imprisonment, with fine which shall be twice the amount of fine for such offence. 71. Application of other laws not barred.-The provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force. 72. Jurisdiction of Tribunal and Appellate Tribunal.-

(4) The Tribunal shall exercise such powers and perform such functions as are, or may be, conferred on it by or under this Act or any other law for the time being in force.

(5) Any person aggrieved by an order or decision of Tribunal may prefer an appeal to the Appellate Tribunal and the provisions of sections 10FQ, 10FZA, 10G, 10GD, 10GE and 10GF of the Companies Act, 1956 (1 of 1956) shall be applicable in respect of such appeal. 73. Penalty on non-compliance of any order passed by Tribunal.-Whoever fails to comply with any order made by the Tribunal under any provision of this Act shall be punishable with imprisonment which may extend to six months and shall also be liable to a fine which shall not be less than fifty thousand rupees.

74. General penalties.-Any person guilty of an offence under this Act for which no punishment is expressly provided shall be liable to a fine which may extend to five lakh rupees but which shall not be less than five thousand rupees and with a further fine which may extend to fifty rupees for every day after the first day after which the default continues.

75. Power of Registrar to strike defunct limited liability partnership off register.-Where the Registrar has reasonable cause to believe that a limited liability partnership is not carrying on business or its operation, in accordance with the provisions of this Act, the name of limited liability partnership may be struck off the register of limited liability partnerships in such manner as may be prescribed: Provided that the Registrar shall, before striking off the name of any limited liability partnership under this section, give such limited liability partnership a reasonable opportunity of being heard.

76. Offences to limited liability partnerships.-Where an offence under this Act committed by a limited liability partnership is proved- (a) to have been committed with the consent or connivance of a partner or partners or designated partner or designated partners of the limited liability partnership; or 25 (b) to be attributable to any neglect on the part of the partner or partners

or designated partner or designated partners of that limited liability partnership, the partner or partners or designated partner or designated partners of the limited liability partnership, as the case may be, as well as that limited liability partnership shall be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

77.Jurisdiction of Court.-Not withstanding any provision to the contrary in any Act for the time being in force, the Judicial Magistrate of the first class or, as the case may be, the Metropolitan Magistrate shall have jurisdiction to try any offence under this Act and shall have power to impose punishment in respect of said offence.

(6). Power to alter Schedules.-(1) The Central Government may, by notification in the Official Gazette, alter any of the provisions contained in any of the Schedules to this Act. (2) Any alteration notified under sub-section (1) shall have effect as if enacted in the Act and shall come into force on the date of the notification, unless the notification otherwise directs. (3) Every alteration made by the Central Government under sub-section (1) shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the alteration, or both Houses agree that the alteration should not be made, the alteration shall, thereafter, have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done in pursuance of that alteration. 79. Power to make rules.-(1) The Central Government may, by notification in the Official Gazette, make rules for carrying out the provisions of this Act.

(7) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:- (a) form and manner of prior consent to be given by designated partner under

sub-section (3) of section 7; (b) the form and manner of particulars of every individual agreeing to act as designated partner of limited liability partnership under sub-section (4) of section 7; (c) the conditions and requirements relating to the eligibility of an individual to become a designated partner under sub-section (5) of section 7; (d) the manner of filing the incorporation document and payment of fees payable thereof under clause (b) of sub-section (1) of section 11; (e) the form of statement to be filed under clause (c) of sub-section (1) of section 11; (f) the form of incorporation document under clause (a) of sub-section (2) of section 11; (g) the information to be contained in the incorporation document concerning the proposed limited liability partnership under clause (g) of sub-section (2) of section 11; (h) the manner of serving the documents on a limited liability partnership or a partner or a designated partner and the form and manner in which any other address may be declared by the limited liability partnership under sub-section (2) of section 13; (i) the form and manner of notice to the Registrar and the conditions in respect of change of registered office under sub-section (3) of section 13; (j) the form and manner of application and amount of fee payable to the Registrar under sub-section (1) of section 16; (k) the manner in which names will be reserved by the Registrar under sub-section (2) of section 16; 26 (l) the manner in which an application may be made by an entity under sub-section (1) of section 18; (m) the form and manner of notice of change of name of limited liability partnership and the amount of fee payable under section 19; (n) the form and manner of the limited liability partnership agreement and the changes made therein and the amount of fee payable under sub-section (2) of section 23; (o) the form of notice, the amount of fee payable and the manner of authentication of the statement under clauses (a), (b) and (c) of sub-section (3) of section 25; (p) the manner of accounting and disclosure of monetary value of contribution of a partner under sub-section (2) of section 32; (q) the books of account and the period of their maintenance under sub-section (1) of section 34; (r) the form of Statement of Account and Solvency under sub-section (2) of section 34; (s) the form, manner, fee and time of filing of Statement of Account and Solvency under sub-section (3) of

section 34; (t) the audit of accounts of a limited liability partnership under sub-section (4) of section 34; (u) the form and manner of annual return and fee payable under sub-section (1) of section 35; (v) the manner and amount of fee payable for inspection of incorporation document, names of partners and changes made therein, Statement of Account and Solvency and annual return under section 36; (w) the destruction of documents by Registrar in any form under section 40; (x) the amount required as security under clause (a) of sub-section (3) of section 43; (y) the amount of security to be given under section 44; (z) the fee payable for furnishing a copy under clause (b) of sub-section (2) of section 49; (za) the manner of authentication of report of inspector under section 54; (zb) the form and manner of particulars about conversion under the proviso to sub-section (1) of section 58; (zc) in relation to establishment of place of business and carrying on business in India by foreign limited liability partnerships and regulatory mechanism and composition under section 59; (zd) the manner of calling, holding and conducting meeting under sub-section (1) of section 60; (ze) in relation to winding up and dissolution of limited liability partnerships under section 65; (zf) the manner and conditions for filing document electronically under sub-section (1) of section 68; (zg) the manner for striking off the names of limited liability partnerships from the register under section 75; (zh) the form and manner of statement containing particulars and amount of fee payable under sub-paragraph (a) of paragraph 4 of the Second Schedule; (zi) the form and manner of particulars about conversion under the proviso to paragraph 5 of the Second Schedule; (zj) the form and manner of the statement and the amount of fee payable under sub-paragraph (a) of paragraph 3 of the Third Schedule; (zk) the form and manner of particulars about conversion under the proviso to paragraph 4 of the Third Schedule; the form and manner of the statement and amount of fee payable under sub-paragraph (a) of paragraph 4 of the Fourth Schedule; and the form and manner of particulars about conversion under the proviso to paragraph 5 of the Fourth Schedule.

(8) Every rule made under this Act by the Central Government shall be laid, as soon as may be after it is made, before each House of Parliament, while it is

in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule, or both Houses agree that the rule should not be made, the rule shall, thereafter, have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule. 80. Power to remove difficulties.-(1) If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order published in the Official Gazette, make such provisions, not inconsistent with the provisions of this Act as may appear to it to be necessary for removing the difficulty: Provided that no such order shall be made under this section after the expiry of a period of two years from the commencement of this Act.

(9) Every order made under this section shall be laid, as soon as may be, after it is made, before each House of Parliament.

FORMATION OF LLP

Recently most entrepreneurs have started opting for Limited Liability Partnership, considering it has most positive features of Partnership and Companies. It is hybrid form which incorporates benefits of both partnership and companies. It has the following features:

- The liability of each partner is limited to the contribution mention in agreement.
- The cost of formation is limited.
- Less restriction and compliance.
- Separate Legal Entity

  Following is Step wise Registration process for incorporation of Limited Liability Partnership (LLP)

  Step 1) Obtain Designated Identification Number (DIN)

4.7.2 FORMATION OF REQUIREMENT FOR THE INFORMATION OF LLP

1. The minimum number of partners to incorporate a LLP is two, they may be individuals or body corporate who may be acting through their representatives
2. There is no upper limit on the maximum number of partners of LLP. Out of the partners two shall be designated partners one whom shall be resident in India.
3. All the designated partners shall obtain Designated Partner Identification Number (DPIN),DPIN is an eight digit numeric number allotted by the Central Government in order to identify a particular partner.
4. The application for allotment of DPIN shall be made online in (E-Form 7)
5. As all the documents in relation to LLP whether they may relate to incorporation, filing etc are filed online and are required to be digitally signed atleast one Designated Partner to obtain the digital signature certificates from government recognized DSA's
6. The name with which LLP is to be incorporated is to be decided.
7. The registrar will approve the name applied for provided the name is not either undesirable in the opinion of the Central Government or that is identical with or that which too nearly resembles to the name of any existing partnership firm or a LLP or a body corporate or a trade mark registered or pending registration under the Trade Marks Act, 1999.
8. Application shall be made in (E-Form 1) for the availability of the proposed name with the Registrar
9. Applicable fees has to be paid by of credit card.

10. The name approved shall be available for adoption for a period of 3 months.

11. Thereafter Limited Liability Partnership Agreement governing the mutual rights and duties among the partners and among the LLP and its partners is to be prepared which contains :

    Name of the LLP

    Name of Partners & Designated Partners

    Manner of contribution

    Profit/Loss Sharing ratio between partners

    Rights & Duties and obligations of Partners

    Proposed Business of LLP

    Rules for governing the conduct of operations of LLP

    In case no agreement is entered into, the rights & duties as prescribed under Schedule I to the LLP Act shall be applicable.

12. LLP agreement contains a subscription sheet which must be subscribed by the partners who shall sign the same along with their name. The subscription sheet must be witnessed by any chartered Accountant/Company Secretary/Advocate in practice.

13. Incorporation documents must be filed with the Registrar in (E-Form 2) with the following attachments.

    1. Copy of authorization where the partner is a limited liability partnership, or company, or a limited liability partnership incorporated outside India or a company incorporated outside India.

    2. Proof of address of registered office of limited liability partnership.

3. Details in respect of names of partners/witnesses and their signatures.

4. Attachments in respect of details of individuals/bodies corporate where the number exceeds five.

5. Optional attachments as may be required.

14. E-Forms contains details such as name of designated partners, SRN no. of E-Form 1, name of LLP, address of LLP, particulars of the state in which LLP is being incorporated.

15. After the Registrar is satisfied that all the formalities with respect to the incorporation has been complied , he will issue a Certificate of Incorporation as to formation of the LLP within maximum of 14 days from date of filing of documents . The Certificate of Incorporation issued shall be the conclusive evidence of formation of the LLP.

16 On incorporation Every LLP so registered shall be assigned a LLP identification number (LLPIN) in one consecutive series

17 LLP agreement must be filed in (E-Form 3) with the Registrar. This form must be filed within 30 days of incorporation.

18 The LLP Agreement must be stamped in accordance with the stamp Act applicable in the relevant state where LLP is being incorporated.

19 The consent of the partner to act as partner of LLP must be filed in (E-Form no. 4) along with the following attachments :

Address proof.

Identity proof. This form must be filed within 30 days of incorporation

20. All the E-Forms will be digitally signed by any Designated partner and shall be certified by an advocate/company secretary/chartered accountant/cost accountant in practice engaged in the formation of LLP.

NOTE

In the office of Registrar there shall be maintained a Register of LLPs in which the names of LLPs shall be entered in the order in which they are registered. In case of foreign nationals residing outside India in countries signatory to the Hague Apostile Convention, 1961 and seeking to register a LLP in India, their signatures and address on the incorporation documents and proof of identity, where required, shall be notarized before the notary of the country of their origin and be duly apostillised in accordance with the said Hague Convention.

4.8 SUMMARY

E-filing has many benefits over other methods of filing. The IRS doesn't have to re-enter your information into its system. So, e-filing results in fewer data-entry errors. One receives an acknowledgment that the IRS received your return. The IRS doesn't send an acknowledgment when it receives paper returns. One receives refund faster if he/she e-file return rather than mail it, if one owes the IRS, one can ask the IRS to electronically withdraw the money you owe directly from your bank account. One can decide when the IRS withdraws the money --up to the last minute on the filing deadline, even if one filed his/ her return earlier. The Ministry claims that with the introduction of the concept of DIN: Offences committed by the directors will be immediately detected as all the 20 offices of the Registrars of Companies (ROC) will be networked by April, 2006. It would also help in addressing the concerns of companies vanishing after raising funds from the public. Investors will also get the chance to take more informed decision by knowing the top management of the company. Every individual intending to be appointed as director of a company shall make an application for allotment of Director Identification Number to the Central Government in such form and manner and along with such fees as may be prescribed. Every individual, who is to be appointed as director of a company shall make an application electronically in Form No. DIR-3, to the Central Government

for the allotment of a Director Identification Number (DIN) along with such fees as provided in the Companies (Registration Offices and Fees) Rules, 2014. Any person intending to become the director in a company is required to make an application to MCA for allotment of a unique identification, namely, Director Identification Number (DIN) through this e-Form. Limited liability partnership to be body corporate.-(1) A limited liability partnership is a body corporate formed and incorporated under this Act and is a legal entity separate from that of its partners. (2) A limited liability partnership shall have perpetual succession. (3) Any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

The provisions of the Indian Partnership Act, 1932 (9 of 1932) shall not apply to a limited liability partnership. Partners.-Any individual or body corporate may be a partner in a limited liability partnership: Provided that an individual shall not be capable of becoming a partner of a limited liability partnership, if- (a) he has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force; (b) he is an un discharged insolvent; or (c) he has applied to be adjudicated as an insolvent and his application is pending. Minimum number of partners.-(1) Every limited liability partnership shall have at least two partners. (2) If at any time the number of partners of a limited liability partnership is reduced below two and the limited liability partnership carries on business for more than six months while the number is so reduced, the person, who is the only partner of the limited liability partnership during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone, shall be liable personally for the obligations of the limited liability partnership incurred during that period. Designated partners.-(1) Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

4.9 KEY CONCEPTS/TERMS

Digital Signature Certificate; Director Identification Number; E-filing; Corporate Identity Number (CIN).

4.10 GLOSSARY

- Digital Signature Certificate: is a big breakthrough in the field of technology and can be used, generously as its advantages greatly overshadow their disadvantages. A Digital signature is a one-way hash, of the original data, that has been encrypted with the signer's private key. The signer calculates the hash for the data he needs to sign. The message digest is a file size small (160-bit SHA-1 now deprecated, with 256-bit SHA-256) that contains some sort of control code that refers to the document.

- Director Identification Number: The Ministry of Company Affairs (MCA) has launched a major e-Governance initiative. It envisages e-filing of all documents related to company matters on the MCA portal. Director Identification Number (DIN) is a unique identification number for an existing director or a person intending to become the director of a company. In the scenario of e-filing, DIN will be a pre-requisite for filing of certain company related documents.

- E-filing: is the electronic submission of information that is required by law. It is up to the regulating agency to decide the criteria for what types of information must be filed electronically and what types of information can be submitted in hard copy form.

- Corporate Identity Number (CIN): Each Indian company (Listed or Unlisted) has a unique 21 Digit CIN (Corporate Identity Number). This is required to be quoted on all forms. Once this number is filled, company details are automatically filled in E-Forms issued by MCA by using pre-fill function.

4.11 SELF ASSESSMENT QUESTIONS

1. Explain how director identification certificate number can be obtained ?

Ans. _____

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2. Explain in brief the formation of LLP?

Ans. _____

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3. What is a digital signature? Explain fundamental principles guiding digital signatures?

Ans. _____

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4. Explain the concept of company law in a computerised environment?

Ans. _____

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5. Discuss the concept of Corporate Identity Number. Explain the steps required for obtaining Corporate Identity Number.

Ans. _____

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6. Explain the meaning and concept of Limited Liability Partnership Act, 2008.

Ans. _____

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4.12 RECOMMENDED READING

- Corporate Manslaughter and Corporate Homicide Act 2007
- David Kershaw, Company Law in Context (OUP, Oxford, 2009)
- RC Clark, Corporate Law (Aspen 1986)
- Reiner Kraakman, Henry Hansmann, Paul L. Davies, Klaus Hopt, Gerard Hertig, Hideki Kanda, The Anatomy of Corporate Law (OUP 2004)
- Paul L. Davies QC, Gower and Davies' Principle of Modern Company Law, 8th Edition, 2008.

- Black's Law Dictionary, 8th Edition, 2004.
- Ministry of Corporate Affairs-The Limited LiabilityPartnership Act, 2008.
- LLP Act, 2008
- Sanjiv Agarwal and Rohini Agarwal, 2009
- D.S.R. Krishnamurti, 2009

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