

Legal Aspect of Business

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Edited by:
Dr. Sukhpreet Kaur



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Legal Aspect of Business

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Unit 01: Indian Contract Act, 1872

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Summary

Keywords

Self-Assessment

Answers for Self Assessment

Review Questions

Further Reading

Objectives

After studying this unit, you will be able to:

- appraise the importance of the Indian Contract Act, 1872.
- illustrate the difference between agreement and contract.
- explain the essentials of a valid contract.
- categorize and illustrate the various types of contract.
- explain the meaning of free consent.
- illustrate the situations where consent of a party to a contract is not free.
- review the situations under which the consent of a party to a contract is not free and comment on its effect on the validity of the contract.
- explain the meaning of discharge of a contract.
- illustrate the various modes of discharge of a contract.
- explain the meaning of Breach of contract.
- review the remedies for the Breach of Contract.
- review the relevance of the Indian Contract Act, 1872 in protecting the interests of contractual parties.

Introduction

The law relating to contracts is contained in the Indian Contract Act, 1872. For business executives, contract law is tremendously significant because it underlies or is related to all major areas of law affecting business. It is the most important branch of business law. It is, however, of particular importance to people engaged in trade, commerce and industry as the bulk of their business transactions are based on contracts.

The law of contract is branch of law that determines the circumstances in which promises made by the parties to a contract shall be legally binding on them. Its rules define the remedies that are

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available in a court of law against a person who fails to perform his contract, and the conditions under which remedies are available.

The law relating to contracts is contained in the Indian Contract Act, 1872. The Act deals with:

- a) General principles of the law of contract (Secs. 1 to 75),
- b) Some special contracts (Secs. 124 to 238).

In the present unit, meaning and essentials of a valid contract, kinds of contract, concept of free consent, discharge of contract, and remedies for breach of contract are discussed.

1.1 The Indian Contract Act, 1872: Introduction

- It is applicable to all states of India.
- It does not affect any usage or custom of trade.
- It is the most important part of commercial law because every commercial transaction starts from an agreement between two or more persons.
- The main objective of law of contract is to bring definiteness in commercial and other transactions.
- This act came into force on September 1, 1872.
- The Act is not exhaustive: The act does not profess to be a complete and exhaustive code.
- It creates Jus in Personam NOT Jus in Rem



Did you know? **What is meant by Jus in Personam?**

- A Jus in Personam: It means a right against or in respect of a specific person. It is available only against particular persons.

What is meant by Jus in Rem?

- A jus in rem: means a right against or in respect of a thing. It is available against the world at large.



Examples:

- Mr. Amit owes an amount of 80,000 to Mr. Bhasin. Mr. Bhasin has the right to recover this amount from Mr. Amit only, not from anybody else. This right is known as Jus in Personam.
- Mr. Sahil owns 50 acres of land. In this case, Mr. Sahil has the full liberty to enjoy the land against every member of the public. This right is known as Jus in Rem.

1.2 Contract: Meaning and Definition

A contract is an agreement, enforceable by law, made between at least two parties to do a particular act or abstain from doing a particular act. When parties create a contract, they create legal rights and obligations between themselves. If the party, which had agreed to do something, fails to do that, then the other party has legal remedies.

“Contract is an agreement, enforceable by law”

- Sec.2(h)

“A contract is an agreement, creating and defining the obligation between Parties.”

- Salmond

“Every agreement and promise enforceable at law is a contract.”

- Sir Fredrick Pollock

Unit 01: Indian Contract Act, 1872

We can easily understand that a contract essentially has two following elements from the above definitions:

- An agreement, and
- Enforceable by Law or Legal obligation

Agreement + Enforceable by Law = Contract

Agreement

“Every promise and every set of promises forming the consideration for each other is an agreement”.

-Sec.2(e)

In this context, the word ‘promise’ is defined by Sec. 2(b) as follows:

“A proposal, when accepted becomes a promise”.

In a contract there are at least two parties. The person making the proposal is called ‘promisor’ and the person accepting the proposal is called the ‘promisee’ [Sec. 2(c)].

Thus, an agreement is an accepted proposal. Thus an agreement has two following elements:

- Offer
- Acceptance

Offer + Acceptance = Agreement



Example: Ritu offered to sell his car to Shruti for 2,00,000. Shruti accepted this offer. Now, this offer to sell and acceptance to purchase can be treated as an agreement.

Two Parties

There should be two parties for making a valid agreement viz. Offeror and Offeree. One of them makes a proposal (or an offer) to the other, to do something, with a view to obtaining the assent of that other to such act. The person who makes an offer is termed as Offeror and the person to whom the offer is made is termed as Offeree.

When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted.

Consensus ad idem (Similarity of Minds)

The second important aspect of a valid agreement is consensus ad idem that is the identity of minds. Difference in opinion of two parties involved in forming an agreement will render the agreement void.



Example: Varun owns two houses, One located in Delhi and the other in Chandigarh. He offers to sell his Chandigarh house to Karan. Karan accepts the offer under the impression that he is buying the Delhi house. Here, in the minds of Varun and Karan, there are two different houses. So, there is no agreement on the subject-matter of the intended contract. In this case, although an offer and acceptance involves two separate parties, this agreement is void because of absence of consensus ad idem that is similarity of minds.

Thus, it is clear that the identity of minds has to be essentially present to bring an enforceable agreement into existence.

Enforceable by Law, or Legal Obligation

The agreement must be such which is enforceable by law to become a contract. Thus, there are certain agreements which do not become contracts as this element of enforceability by law is absent.



Example: An agreement to go for a stroll together or a picnic does not become a contract, and therefore, neither rights nor obligations are created on the part of the parties to the agreement.



Caution:

- There is no intention to create legal obligation in moral, religious or social agreements.
- All business agreements are created with an intention to create legal obligations.



Example: Tom agrees to sell his car to Bruno for 50,000. The agreement gives rise to an obligation on the part of Tom to deliver the car to Bruno and on the part of Bruno to pay 50,000 to Tom.

Hence, it can be concluded from the above discuss that **all contracts are agreements but all agreements are not necessarily contracts.**

1.3 Essential Elements of a Valid Contract

"All agreements are contracts if they are made by free consent of the parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void."

-Sec. 10

- Offer and Acceptance
- Intention to Create Legal Relationship
- Lawful Consideration
- Capacity of Parties
- Free or Genuine Consent
- Lawful Object
- Agreement Not Expressly Declared Void
- Certainty of Meaning
- Possibility of Performance
- Legal Formalities

Offer and Acceptance

To create a valid contract, there must be two or more parties. One who makes the offer and the other who accepts the offer. One person cannot make an offer and accept it. There must be at least two persons namely offeror and offeree. Also the offer must be clear and properly communicated to the other party. Similarly acceptance must be communicated to the other party and the proper and unconditional acceptance must be communicated to the offeror. Proper offer and proper acceptance should be there to treat the agreement as a contract which is enforceable by law.

Intention to Create Legal Relationship

The parties entering into a contract must have an intention to create a legal relationship. If there is no intention to create a legal relationship that agreement cannot be treated as a valid contract.

In case of Domestic Agreements

Presumption: Generally, there is no intention to create a legal relationship in social and domestic agreements.



Case Study

A husband promised to pay his wife a household allowance of 5,000 every month. Later, the parties separated and husband failed to pay the amount. The wife sued for an allowance.

Point of Discussion

Will she succeed in the lawsuit?

[Hint: No, held these agreements are outside the realm of contract.]



Case Study

A resident of India invited her daughter who lived and worked in the US to move to India to study. They agreed that the mother would let the daughter stay in the house without any expectation of house rent from her daughter. A dispute arose and the mother took an action to evict the daughter from the house.

Point of Discussion

Will such an agreement bind the mother and daughter legally?

[Hint: No, the court decided the case in favor of the mother and stated that there was no legally binding agreement between the parties.]

Rebutting the presumption

The presumption can be easily debited in certain circumstances, for example if the parties who are in a familial relationship are contacting in a business context. Even, if the word used in the contract indicates a legal intention, that may otherwise have a Rises may be rebutted.



Example: If a husband and wife enter into an agreement in such circumstances in which they are no longer living in harmony.



Case

An elder brother, owner of considerable wealth, invited his sister and her husband, who gave up paid employment, to come to Australia to live with him and care for him until his death. In consideration of the services of his sister and brother-in-law, the brother promised to pay them an income for life and his property upon his death. Subsequently the brother changed his mind and breached the promise. A dispute arose and the couple sued for breach of contract.

Point of Discussion

Can couple win the case?

[Hint: Yes, the court held that in the given circumstances, the agreement was something more than a familial relationship because of the serious consequences of the arrangement for the plaintiffs namely the husband giving up his salaried position and pension and both of them moving permanently to Australia.]

In case of Commercial Agreements

Presumption: Where parties negotiate and agree in a business setting, it is assumed that they intend the agreement to have legal consequences.

Rebutting the presumption: The intention not to create legal relations may be evident in a number of different ways.



Example: The agreement may contain an express clause that no legal consequences flow from the document.

Lawful Consideration

An agreement must be supported by a consideration of something in return. That is, the agreement must be supported by some type of service or goods in return of money or goods. However, it is not necessary the price should be always in terms of money. It could be a service or another goods.



Example: Samiksha agreed to buy a Hindi Literature book from Yuvan for 500. Here, the consideration of Samiksha is book and the consideration of Yuvan is 500.

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Capacity of Parties

As per Sec. 11, every person is competent to contract who is of the age of majority according to law to which he is subject, and who is of sound mind and is not disqualified from contracting by any law to which he is subject.



Case Study

Trinum agreed to sell a government property to Bittu, Bittu agreed to buy that property.

Point of Discussion

Is this a valid agreement?

[Hint: No, as Trinum is not competent to sell the property which is owned by government.]

Free or Genuine Consent

The consent of the parties must be genuine and free consent. According to section 14, consent is said to be free when it is not caused by (i) coercion, (ii) undue influence, (iii) fraud, (iv) misrepresentation, or (v) mistake. If the contract made by any of the above reasons except for "mutual mistake", the could be treated as a voidable contract. It means the contract can be rescinded at the option of the aggrieved party. If the agreement induced by mutual mistake the agreement would stand void or canceled. An agreement can be treated as a valid contract when the consent of the parties are free and not under any undue influence, fear or pressure etc.

Lawful Object

The objective of the agreement must be lawful. Any act prohibited by law will not be valid and such agreements cannot be treated as a valid contract.



Case Study

Anand and Krish agree that Anand shall pay him 10,000 if Krish shall deliver Anand Opium afterwards.

Point of Discussion

Is it a valid Contract?

[Hint: No, due to illegal object.]

Agreement Not Expressly Declared Void

Sec.24-30 of the Act specify certain types of agreement that have been expressly declared void. Like: an agreement in restraint of legal proceedings, agreement in restraint of trade, agreement in restraint of marriage (Sec.26) and agreement by way of wager.



Case Study

Carew Co Ltd. V North Bengal

Two sugar manufacturers had entered into an agreement allocating zones to procure sugar for meeting the needs of their respective factories. It was agreed between the parties that none of them would draw any cane from the zones allotted to the factory of other party.

Point of Discussion

Is the agreement between the sugar manufacturers enforceable by law?

[Hint: No, as the agreement is in restraint of trade and hence void.]

Certainty of Meaning

The wording of the agreement must be clear and must not be uncertain or vague.



Example: Johny agrees to sell 500 tons of oil to Mathew. But, what kind of oil is not mentioned clearly. So on the ground of uncertainty, this agreement stands void.

Possibility of Performance

As per Sec. 56, if the act is impossible of performance, physically or legally, the agreement cannot be enforced by law. There must be possibility of performance of the agreement.



Example: Ananya agreed with Bhushan to put life into Bhushan's dead wife, the agreement is void as it is not possible to perform.

Legal Formalities

The contract act does not insist that the agreement must be in writing, it could be oral. But, in some cases, the laws strictly insist that the agreement must be in writing.



Example: An agreement to sell immovable property must be in writing and should be registered under the Transfer of Property Act, 1882.

1.4 Kinds of Contract

Contracts can be classified as follows:

On the basis of "Validity"	On the basis of "Formation"	On the basis of "Performance"
Valid	Express	Executed
Voidable	Implied	Executory
Void	Quasi	
Void Agreements	E-Commerce	
Unenforceable		
Illegal Contract		

On the basis of Validity

a) Valid contract

A contract that satisfies all the conditions prescribed by law is a valid contract, and hence enforceable by law.



Example: Suman offers to buy Devansh's Motor bike for 80,000. Devansh accepted her offer. This constitutes a valid contract between Suman and Devansh.

b) Voidable contract

"An agreement which is enforceable by law at the option of one or more of the parties thereon but not at the option of the other or others, is a voidable contract". - Sec. 2(i)



Case Study

Jamuna Das threatens to shoot Bittu Lal, if he does not sell his new Audi Car to Jamuna Das for 2,00,000, Bittu Lal agrees.

Point of Discussion

Is this a valid contract?

[Hint: No, the contract is voidable at the option of Bittu Lal as his consent is taken through coercion.]

c) Void contract

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A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable [Sec. 2(j)].

In other words, a void contract is a contract which is valid when entered into but which subsequently became void due to impossibility of performance, change of law or some other reason.



Example: Danny, a resident of America, entered into a contract to import certain toys from Chin Chen, a resident of China, for \$ 50,000. This is a valid contract.

However, subsequently, before the execution of the contract, a trade war was declared between America and China. And the American government banned the import of toys from China. Thus, after the declaration of such trade war. The contract turned into a Void contract due to the impossibility of performance.

d) Void Agreements

According to Section 2(g), an agreement not enforceable by law is said to be void.



Example: An agreement with a minor or a person of unsound mind is void-ab-initio because a minor or a person of unsound mind is incompetent to contract.

e) Unenforceable Contracts

It is a contract that is legally binding but cannot be enforced due to a technical flaw (such as not being in writing or not being properly stamped or some other reasons). Such contracts can be enforced if the technical defect involved is removed.

f) Illegal or unlawful Agreement

An illegal agreement is one the object of which is unlawful. Such an agreement cannot be enforced by law. Thus, illegal agreements are always void-ab-initio (i.e. void from the very beginning).



Examples:

- Tom promises to give Jerry five grams of cocaine if Jerry promises to drive Tom to Manhattan on Saturday.
- Tom promises to give Jerry \$5,000 if Jerry robs a bank on Saturday.



Caution:

All illegal agreements are void but all void agreements or contracts are not necessarily illegal.



Task: Karan agrees to pay Vishal 1 lakh, if Vishal kills Sameer. Vishal killed Sameer and claims 1 lakh. Karan denied paying 1 lakh to Vishal.

Point of Discussion

Can Vishal recover 1 lakh from Karan through a law suit? Justify.

On the basis of Formation

a) Express Contact

It is contract that is made in writing or by word of mouth.



Example:

- Apple calls Banana and offers to sell his car for \$80,000; Banana responds by informing Apple that he accepts the offer.
- Vivan writes a letter to Yuvraj, "I offer to sell my car for 1,00,000 to you". Yuvraj sends a letter to Vivan saying "I am ready to buy you a car for 100000".

b) Implied Contract

An implied contract is inferred from the conduct of a person or the circumstance of a particular case.

 <i>Example:</i>	• Ankush, a coolie in uniform, takes up the luggage of Bharat to be carried out of the railway station without being asked by Bharat, and Bharat allows him to do so. In this case there is an implied offer by the coolie (Ankush) and an implied acceptance by the passenger (Bharat). Now, there is an implied contract between Ankush and Bharat. Hence, Bharat is bound to pay for the services of the Ankush. • If Akash boards a bus to go to his destination and whether he takes a seat or not, the law will imply a contract from the very nature of the circumstances, and Akash will have to pay the fare.

c) Quasi Contract or Constructive Contract

A quasi contract is based on the principle that a person shall not be allowed to enrich himself at the expense of another. These contracts are strictly not contracts as there is no intention of parties to enter into a contract.

 <i>Example:</i>	• ABC Ltd., a TV co., wrongly delivered a new TV to Mrs. Zenith that she did not order. She kept the TV and did not attempt to return it. In this case, a Quasi-contract may be enforced on her to pay for the TV. • Where certain books are delivered to a wrong address, the person receiving the same is under an obligation to either pay for them or return them. If the person opts to retain the books, then quasi contract will be created between the book seller and the person retaining the books and he/she will be liable to pay the price of books to the book seller.

d) E-Commerce Contract

A contract modelled, specified, executed and deployed by a software system. It is very similar to traditional contracts.

Formation of E-Commerce contracts:

- **Click-Wrap:** In click-wrap contract, the party's affirmative acceptance is taken by means of checking on an 'I accept' tab with the scroll box that allows the accepting party to view the terms and conditions.
- **Browse-Wrap:** In case of browse-wrap agreement the mere use (or browse) of the website makes the terms binding on the contracting party.
- **Shrink-Wrap:** In case of shrink-wrap agreement the contracting party can read the terms and conditions only after opening the box within which the product (commonly a license) is packed. Such agreements are relevant in the context of e-commerce mostly because of the kind of goods associated with shrink-wrap agreements.

On the Basis of Performance

a) Executed Contract

It is a contract where both the parties to the contract have fulfilled their respective obligations under the contract.

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Example: Amita agrees to paint a picture of Seema for ₹ 1 Lakh. Amita paints the picture on set time and Seema pays ₹ 1 Lakh to Amita.

b) Executory Contract

It is a contract where both the parties to the contract have to perform their respective obligations.



Example: Ankur offers to sell his car to Nitin for ₹ 1 lakh. Nitin accepts the offer. If the car has not yet been delivered by Ankur and the price has not yet been paid by Nitin. It will be an executory contract as the performance from both parties is due.

Executory contracts can be further classified as Unilateral Contract and Bilateral Contract.

i) Unilateral Executory Contract

It is a contract in which only one party has to fulfill his/her obligation at the time of the formation of the contract. Such contracts are also known as contracts with executed consideration.



Example: Shilpa offers to sell her car to Rahul for ₹ 3 lakhs on a credit of 1 month. Rahul accepts the Shilpa offer. Shilpa sold the car to Rahul and delivered the same to him. It is an example of a unilateral executory contract.

Here the contract is executed as to Shilpa and Executory as to Rahul.

ii) Bilateral contract

It is a contract in which the obligations on the part of both parties to the contract are outstanding at the time of formation of the contract. These contracts are known as contracts with executory consideration.

1.5 Free Consent

According to Section 14, Consent is said to be free when it is not caused by:

- Coercion (Sec. 15)
- Undue Influence (Sec. 16)
- Fraud
- Misrepresentation
- Mistake (Sec. 18)



Did you know? **What is consent?**

As per Sec. 13, when two or more persons agree upon the same thing in the same sense, they are said to consent and have consensus ad idem.

In other words, consent is defined as an act of assenting to an offer.



Case Study

Bala Debi v. S. Majumdar, A.I.R (1956)

An illiterate woman executed a deed of gift in favour of her nephew to manage her lands. The evidence showed that the woman never intended to execute such a deed of gift, nor was the deed ever read or explained to her.

Point of Discussion

Is the deed operative in the eyes of law?

[Hint: It was held, the deed was void and inoperative due to absence of consent.]

Coercion: Sec. 15

Coercion is:

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1) the committing, or threatening to commit, any act forbidden by the Indian Penal Code, 1860.

**Case Study****Ranganayakamma v. Alwar Shetty (1889)**

A young girl of 13 years was forced to adapt a boy to her husband who had just died by the relatives of her husband who prevented the removal of his body for cremation until she consented.

Point of Discussion

Was the consent of young girl free?

[Hint: the consent was not free but was free but was induced by coercion.]

2) the unlawful detaining, or threatening to detain, any property.

**Case Study****Mutha v. Muthu Karuppa (1927)**

An agent refused to hand over books of accounts of a business to new agent unless principal released him from all liabilities, principal had to give release deed as demanded.

Point of Discussion

Was the release deed valid?

[Hint: It was held, the release deed was given under coercion and voidable at the option of the principal.]

Threat to Commit Suicide----Does it amount to Coercion?

A threat to commit suicide amounts to coercion.

**Case Study****ChikhamAmiraju v. Seshamma (1917)**

A person held out a threat of committing suicide to his wife and son if they did not execute a release in favour of his brother in respect of certain properties. The wife and son executed the release deed under the threat.

Point of Discussion

Discuss the validity of deed.

[Hint: It is held, the threat of suicide amounted to coercion with Sec. 15 and the release deed under the threat.]

Duress----Does it amount to Coercion?

Duress involves actual or threatened violence over the person or another (or his wife, parent, or child) with a view to obtain his consent to the agreement. If the threat is with regard to goods or property of the other party, it is not duress.

**Case Study**

Xavier forcibly kidnaps the son of David and asks him to execute a promissory note of rupees one lakh in his favour. Now, under threat, David signs a promissory note in favor of Xavier.

Point of Discussion

Is the promissory note enforceable?

[Hint: Such a promissory note cannot be enforced in the court of law as the consent was not free]

and was induced by coercion.

Effect of Coercion (Section 19)

- Agreement is voidable at the option of the aggrieved party.
- A person to whom money has been paid, or anything delivered under coercion must repay or return it.



Example: A railway company refuses to deliver certain goods to the consignee, except upon the payment of an illegal charge for carriage. The consignee pays the sum charged in order to obtain the goods.

- Coercion may be directed against anybody



Example: Amit threatens to kill Chirag (Ashok's son) if Ashok does not let out his house to Amit. Is this agreement caused by coercion?

Onus of Proof

It lies with the party who wants to relieve himself of the consequences of coercion.

Undue Influence: Sec. 16

(1) 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. - Sec. 16(1)

(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. - Sec. 16(2)



Examples: Lina, a woman enfeebled by disease and age, is induced by Sonu's influence over her as her medical attendant, to agree to pay Sonu an unreasonable amount for his professional services. In this example, Sonu employs undue influence.

Viren 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. Viren 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.



Case Study

Mannu Singh v. Umadat Pandey, 1890

A spiritual guru induced his devotee to gift him his entire property in return for a promise of salvation from the devotee.

Point of Discussion

Will the consent of devotee be treated as free? State reasons.

[Hint: The consent of the devotee was given under undue influence.]

(3) Burden of Proof: Sec. 16(3)

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 lie upon the person in a position to dominate the will of the other.



Caution: In an action to avoid a contract on the ground of undue influence, the plaintiff has to establish that---

- The other party was in a position to dominate his will.
- The other party actually used his influence to obtain the plaintiff's consent to the contract.
- The transaction is unreasonable.

Effect of Undue Influence:

Agreement is voidable at the option of the aggrieved party.

The Court may:

- Set aside the case, or
- Implement it in the modified form, or
- Ask the parties to contract to return the benefit if contract is set aside.



Case Study

RaneeAnnapurni v. Swaminatha (1910)

A poor Hindu widow who was in dire need of money was forced by a money lender to agree to pay a 100% rate of interest. She needed the money to establish her right to maintenance.

Point of Discussion

Is the contract valid?

[Hint: No, it was case of undue influence and the court reduced the interest to 24%.]

Difference between Coercion and Undue Influence

Basis	Coercion	Undue Influence
Definition	Committing, or threatening to commit, any act forbidden by the Indian Penal Code 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.	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.
Nature of force	It involves mostly use of physical or violent force.	Use of moral Force/Pressure to obtain consent.
Burden of Proof	Party whose consent was so caused by Coercion.	Party who was in a position to dominate the will of other party.
Effect	Rescission of contract- return any benefit received by aggrieved party.	Court discretion to direct aggrieved party to restore benefit whether in whole or part or set aside the contract with directions for refund of benefit.
Criminal Liability	Yes, under Indian Penal Code.	No criminal liability.
Directed against	Directed against a person or	Threat against person himself

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	his property.	and not against his property.
Existence of Relation	No relationship need to exist between parties.	Some sort of relationship between the parties to contract.

Fraud: Sec. 17

Fraud means and includes any of the following acts committed by a party to a contract with intent to deceive the other party thereto or to induce him to enter into a contract:

- The suggestion as a fact of that which is not true by one who does not believe it to be true;
- The active concealment of a fact by one having knowledge or belief of the fact;
- A promise made without any intention of performing it;
- Any other act fitted to deceive;
- Any such act or omission as the law specifically declares to be fraudulent.

Essential elements of Fraud

- The representation or assertion must be false.
- The representation or assertion must be of a fact.
- There must be an intention to deceive the other party.
- Fraudulent act must be committed with knowledge of its falsity.
- Fraudulent act must be done by a party to the contract or his authorized agent.
- Fraudulent act must have deceived the other party.



Example:

- Maggie, a seller of a horse, says that the horse is a “Beauty” and is worth 5 lakh. It is merely Maggie’s opinion. Thus, it will not act as a fraud. But if, in fact, Maggie paid only 2 lakh for it, then he has misstated a fact and will be considered as fraud on grounds of Representation or assertion must be a fact.
- Priya sells to Mohit locally manufactured goods as imported goods charging a higher price. This amounts to fraud.
- Zeenat, a seller, claimed that his projector is made in Japan, and sold it for 1,50,000. However, the fact is that the projector was made in China. This amounted to fraud.

Does mere silence amount to fraud? [Sec. 17]

No, mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud.

There are two statutory exceptions to the above rule:

- Where the circumstances of the case are such that, regard being had to them, it is the duty of the person to keep silence to speak.
- Where silence, is in itself, equivalent to speech.



Example: Lalit sells, by auction, to Bablu, a horse which Lalit knows to be unsound. Lalit says nothing to Bablu about the horse unsoundness. This is not fraud in Lalit.

Apple and Banana, being traders, enter upon a contract. Apple has private information of a change in prices which would affect Banana’s willingness to proceed with the contract. Apple is not bound to inform B. It is not a fraud.



Case Study

Unit 01: Indian Contract Act, 1872

Bheem says to Ajay , "If you do not deny it, I shall assume that the horse is sound." Ajay says nothing.

Point of Discussion

Is it a case of fraud?

[Hint: Yes, it is a case of fraud as silence is equivalent to speech.]

Effects of Fraud: Sec. 19

- Aggrieved party can avoid or rescind the contract.
- Aggrieved party may affirm the contract and insist that he shall put in same position in which he would have been if the representation made was true.
- Aggrieved party can claim for damages.

**Case Study**

A company issued a prospectus giving false information about the unbounded wealth of the company. A share broker who bought shares on the faith of that information wanted to avoid the contract.

Point of Discussion

Can a share broker avoid the contract?

[Hint: He could do so as the false representation in the prospectus amounted to fraud.]

Misrepresentation: Sec. 18-19

It is a false statement that the person making it honestly believes to be true or that he is unaware is false.

Sec. 18 defines that "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 to 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.



Example: Arun, by a misrepresentation, leads Bhushan erroneously to believe that 500 kilos of indigo are made annually at Arun's factory. Bhushan examines the account of the factory, which shows that only 400 kilos of indigo have been made. After this, Bhushan buys the factory. The contract is not voidable on account of Arun's misrepresentation.

Essentials of Misrepresentation

- There should be a representation or assertion – mere expression or opinion will not amount to misrepresentation.
- Such representation must relate to a matter of fact which has become untrue.
- It should be done prior to the finalization of transaction to induce other party to enter into the contract.
- The party should have actually acted upon it.
- It should have been done by the party or his authorized agent.
- It should be made not with the intention of deceiving.
- It need not to be made directly to other party.

Effect of Misrepresentation (Section 19)

Legal Aspects of Business

- The aggrieved party may avoid or rescind the contract.
- The aggrieved party may affirm the contract and insist upon the misrepresentation being made good.



Caution:

- If truth could have been discovered by means of diligence-then no remedy for misrepresentation.
- 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 [Sec. 19].
- A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practiced, or to whom such misrepresentation was made, does not render a contract voidable[Sec. 19].



Example:

- (a) Apple, intending to deceive Banana, falsely represents that five hundred maunds of indigo are made annually at Apple's factory, and thereby induces Banana to buy the factory. The contract is voidable at the option of Banana.
- (b) Apple, by a misrepresentation, leads Banana erroneously to believe that, five hundred maunds of indigo are made annually at Apple's factory. Banana examines the accounts of the factory, which show that only four hundred maunds of indigo have been made. After this Banana buys the factory. The contract is not voidable on account of Apple's misrepresentation.

Difference b/w Fraud and Misrepresentation

Basis	Fraud	Misrepresentation
Intention	There is an intention to deceive.	There is no an intention to deceive.
Belief	Person making representation himself/herself belief it as false or untrue.	Person making representation himself/herself belief it as true.
Rights	Aggrieved party can: • Rescind the contract. • Sue for damages	Aggrieved party can only rescind the contract.
Discovery of truth	The aggrieved party can rescind the contract even if he/she could have discovered the truth with ordinary diligence except for the cases where there is fraudulent silence.	If the aggrieved party might have discovered the truth with ordinary diligence, the contract cannot be avoided.

Mistake: Sec. 21

Mistake may be defined as an erroneous belief about something. It may be a mistake of fact or a mistake of law.

It is an erroneous belief on the part of the parties to the contract concerning something pertaining to the contract.



Example: Vicky agrees to buy from Shanky a certain house. It turns out that the house had been destroyed by fire before the time of the bargain, though neither party was aware of the fact. The agreement is void. Vicky cannot insist on possession of the house.

The agreement is void as there is a mistake on the part of both the parties about the existence of the subject-matter.

Kinds of Mistake**1. Mistake of fact**

(A) Bilateral mistake

i) Bilateral Mistake as to the subject-matter:

- a) Existence
- b) Identify
- c) Title
- d) Quantity
- e) Quality
- f) Price

ii) Bilateral Mistake as to the possibility of performing the contract

- a) Physical impossibility
- b) Legal impossibility

(B) Unilateral mistake

2. Mistake of law

(A) Mistake of law of country

(B) Mistake of law of a foreign country

1. Mistake of fact**A. Bilateral mistake**

When both parties to an agreement make a factual error that is critical to the agreement, the mistake is referred to as a bilateral mistake, and the agreement is null and void.

In case of Bilateral Mistake, the contract is void. The following two conditions should be fulfilled to hold a mistake as bilateral mistake:

1. Mistake should be mutual

Example: Arun agreed to purchase Bheem's motor cycle which was lying in Bheem's garage. Unknown to either party, the motor cycle and garage were completely destroyed by fire a day earlier. Thus, it is a void agreement.



Caution: An erroneous opinion about something is not a mistake.

2. Must be related to a factual matter that is essential to an agreement.



Example: A man and woman entered into an agreement of separation and under this agreement the man agreed to pay a weekly allowance, mistakenly believing that both were married. It was held that the agreement is void.

Bilateral mistake can further be classified as:

i) Bilateral Mistake as to the subject-matter

- a) Existence
- b) Identify
- c) Title
- d) Quantity
- e) Quality
- f) Price

a) Mistake as to the existence of subject-matter: Where the both parties to an agreement are working under a mistake relating to the subject-matter, the agreement is void.

Legal Aspects of Business



Example: Jatin agrees to buy a horse from Saurabh. It turns out that the horse was dead at the time of the bargain. Thus, the agreement is void due to bilateral mistake related to existence of the subject-matter.

b) Mistake as to the identity of the subject-matter: It usually arises where one party intends to deal in one thing and the other intends to deal in another.



Example: Whisky agreed to buy from Rum, a cargo of cotton “to arrive ex-peerless from Bombay”. There were two ships of that name sailing from Bombay, one is in October and one is in December. Whisky meant the former ship and Rum meant the latter. There was a mutual mistake related to the identity of the subject-matter, so there was no contract.

c) Mistake as to title of the subject-matter: If the seller is selling things which he is not entitled to sell and both parties are acting under a mistake then the agreement will be void.



Example: Gopi told his nephew that he was entitled to a textile mill, and the nephew entered into a contract with Gopi’s daughter to rent the textile mill. Unknown to both parties, the textile mill belongs to Nephew himself. Thus, the agreement was held to be void.

d) Mistake as to quantity of subject-matter: If both the parties are working under a mistake as to the quantity of the subject-matter, the agreement will be treated as void.



Example : Ritu enquired about the price of the latest version of a smart mobile from Suraj, suggesting that he may buy as many as 15 such mobiles. Suraj intimated the price by writing a letter. Ritu sent an SMS for the supply of the 5 mobiles but due to a mistake in writing SMS, Suraj dispatched 15 mobiles. There is no valid contract between the parties as there was a mistake as to the quantity of the subject-matter.

e) Mistake as to the quality of the subject-matter: If the subject-matter is something essentially different from what the parties thought it to be, the agreement is void.



Example: Stupid entered into a contract with Crazy to sell him top-class Dehradun basmati rice. Both of them believed that the rice was of top-class Dehradun quality. But rice turned out to be of the local variety.

The contract was held to be void as both parties were mistaken as to the quality of the subject-matter.

f) Mistake as to the price of the subject-matter: If there is a mutual mistake as to the price of the subject-matter, the agreement is void.

ii) Bilateral Mistake as to the possibility of performing the contract

Consent is nullified if both parties believe that an agreement is capable of being performed when in fact it is not the case. the agreement, in such a case, is void on the ground of impossibility.

a) Physical impossibility



Example: A contract for the hire of a room for witnessing the (procession of king) procession that has been cancelled, unknown to both of the parties.

b) Legal impossibility

A contract is void if it provides that something shall be done which cannot, as a matter of law, be done.

B) Unilateral mistake

As per Sec. 22, a contract is not voidable due to a unilateral mistake. When only one party is mistaken in regard to subject-matter or any term and condition or the legal effect of a contract, it will be termed as unilateral mistake.

A unilateral mistake is not allowed as a defense in avoiding a contract unless the mistake is brought about by the other party’s fraud or misrepresentation.



Example: Tom offers to sell his house for an intended sum of 44,000 but mistakenly in writing, he wrote 40,000. He cannot plead mistake as a defense.

Exceptions

A unilateral mistake is generally not allowed as a defence in avoiding a contract. but in certain cases, the consent is given by a party under an error or mistake which is so fundamental as it goes to the root of the agreement. In such cases, the agreement is void. Thus, in the following cases, even though there is a unilateral mistake, the agreement is void.

- Mistake as to the identity of the person contracted with.



Example: Ankle intends to contract with backbone but finds she has contracted with chin, there is no contract if the identity of backbone was a material element of the contract and Chin knows it.

- Mistake as to the nature of contract.



Example: Madan, an old man of poor sight, indorsed a bill of exchange thinking that it was a guarantee. It was held that there was no contract on the ground that the mind of the signer did not accompany the signature. [Foster v. Mackinnon, 1869]

Mistake of Law

Mistake of law may be a mistake of the law of the home country and a mistake of the law of foreign country.

- Mistake of law of the home country:** A party cannot be allowed to get any relief on the ground that it had done a particular act in ignorance of law. But if a person enters into a contract by making a mistake of law through the inducement of another, whether innocent or otherwise, the contract may be avoided.
- Mistake of law of the foreign country:** Such a mistake is treated as mistake of fact and the agreement in such a case is void.



Caution:

- The general rule as regards to mistake of home law is no excuse.
- However, Mistake of law of the foreign country is regarded as mistake of fact.

1.6 Discharge of Contract

A contract is discharged when rights and obligations created by it comes to an end, i.e., contracting parties no more have any responsibility or liability to each other. Discharge of contract is the termination of a contractual obligation on court orders (via an order of discharge) or mutual agreement (see Accord and Satisfaction), or caused by breach of contract, frustration of contract, performance of contract.

- It means “termination” of a contractual relationship between the parties.
- By discharge of contract, the rights and obligations of the parties come to an end.

Modes of Discharge of Contract

- Discharge by Performance
 - Actual
 - Attempted
- Discharge by Lapse of Time
- Discharge by Breach of Contract
 - Actual
 - Anticipatory

- d) Discharge by Agreement or Consent
 - i. Novation.
 - ii. Rescission
 - iii. Alteration
 - iv. Remission
 - v. Waiver
 - vi. Merger
- e) Discharge by Operation of Law
 - i. Death
 - ii. Merger
 - iii. Insolvency
 - iv. Unauthorized alteration
- f) Discharge by Impossibility of performance
 - i. Initial impossibility
 - ii. Subsequent impossibility

a) Discharge by performance

When a contract is duly performed by both the parties and nothing more remains to be done. The performance may be either Actual or Attempted performance (tender).



Case Study

Peter agrees to sell his cycle to John for an amount of 10,000 to be paid by John on the delivery of the cycle. As soon as it is delivered, John pays the promised amount.

Point of Discussion

Has the contract discharged?

[Hint: Yes, the contract is discharged through actual performance.]



Did you know? What is Tender?

The tender or attempted performance or offer of performance has the same effect as performance. If a promisor tenders performance of his promise but the other party refuses to accept, the promisor stands discharged of his obligations.

b) Discharge by lapse of time

Ordinarily, parties must perform their obligations at the stipulated time. But if the time is essence to the contract, then a failure to perform at time specified, renders the contract voidable at the option of opposite parties.



Case Study

Peter takes a loan from John and agrees to pay instalments every month for the next five years. However, he does not pay even a single instalment. John calls him a few times but then gets busy and takes no action. Three years later, John approaches the court to help him recover his money.

Point of Discussion

Can John win in lawsuit and be able to recover his amount?

[Hint: No, due to elapse of time]

c) Discharge by Breach of Contract

Unit 01: Indian Contract Act, 1872

When a party in a contract has refused to perform, or disabled himself from performing his promise in its entirety, the aggrieved party may put an end to the contract unless he has waived his right expressly or impliedly.

Breach of contract may either be:

- i. an actual breach or
- ii. an anticipatory breach

i) **Actual breach:** The actual breach can occur by (i) failure to perform as promised, (ii) making it impossible for the other party to perform. The failure to perform means that one party must not have performed a material part of the contract by a stated deadline. The actual breach by failure to perform may take place (a) at the time when performance is due, or (b) during the performance of the contract. Thus, if a person does not perform his part of the contract at the stipulated time, he will be liable for its breach.

ii) **Anticipatory breach:** The anticipatory breach of contract occurs when a party repudiates it before the time fixed for performance has arrived or when a party by his own act disables himself from performing the contract.

Where a party to a contract refuses to perform his part of the contract before the actual time arrives, the promise may either (i) rescind the contract and treat the contract as at an end, and at once sue for damages, or (ii) he may elect not to rescind but to treat the contract operative and wait for the time of performance and then hold the other party liable for the consequences of non-performance. In the latter case, the party who has repudiated may still perform if he can.



Caution: The anticipatory breach of contract does not by itself discharge the contract. The contract is discharged only when the aggrieved party accepts the repudiation of the contract, i.e., elects to rescind the contract.



Case Study

Sanaya, a dance artist entered into a contract with Mukesh to perform at his theatre every night during next month. Mukesh agreed to pay her 5,000 for each night. On 10th night, Sanaya willfully absented herself from the theatre.

Point of Discussion

Such absenteeism amounts to breach of contract?

[Hint: Yes, such absenteeism amounts to actual breach of contract.]

d) Discharge by Agreement or Consent

As we know that a contract is created by means of an agreement so it may also be discharged by another agreement between the same parties. Let's learn how parties get discharged through mutual agreement or consent.



Example: Priya and Bhanu entered into a contract, according to which Priya had to supply 1000 pairs of ready-made dresses to Bhanu on January 10, 2021. Where the date of formation of contract was January 1, 2021. On 2nd January, 2021, Priya told to Bhanu that the ordered dresses had been out of fashion and hence not possible to assemble 1000 pairs. Priya said that though Bhanu will be supplied with 1000 pairs by taking a lot of risk and efforts, Bhanu could not sell them due to their obsolescence. Bhanu decided to cancel the contract. Thus, by Mutual understanding, they have terminated their contract.

- i) **Novation:** It means substitution of a new contract for the original one. An older contract get discharged through new contract, when a
- new contract is formed with same parties
 - same contract is formed with different party/parties

Legal Aspects of Business



Example: Ritu owes 80,000 to Minakshi and Minakshi owes 80,000 to Neetu. By mutual agreement, Ritu's debt to Minakshi and Minakshi debt to Neetu are cancelled and Ritu accepts Neetu as her creditor for 80,000.

ii) Rescission

When a contract is discharged before the date of performance by agreement between the parties to the effect that it shall no longer bind them.



Case Study: Mina promised to deliver certain goods to Tina on a certain date. Before the date of performance Mina and Tina mutually agreed that the contract would not be performed.

Point of Discussion

Is the contract get discharged?

[Hint: Yes, through rescission.]

iii. Alteration

It means changes in the terms of contract. If the parties mutually are to change certain terms of the contract, it has the effect of terminating the original contract. There is, however, no change in the parties.



Case Study

Peter Contracted to deliver a rolling machine to Queen at 50,000 after six month. Because of the increase in price of the spare parts of the rolling machine, Peter was unable to deliver the machine at agreed price (50,000) and increased the price of rolling machine to 60,000.

Point of Discussion

Decide in this case the contract between Peter& Queen get discharged?

[Hint: yes, the old contract is discharged through alteration.]

iv) Waiver

It means relinquishment or abandonment of a right. Where a party waives his rights under the contract, the other party is released of his obligations. In other words, waiver is to give up the rights under the contract.

v) Remission

Where a party to contract agrees to:

- accept a lesser amount for full discharge of contract or
- extends the time of performance.



Example: Leena, the promisee agreed to accept 2,000 from Jacky in full settlement of a claim of 5,000, the promise is enforceable and the promisee cannot in future bring a suit for the recovery of 5,000.

vi) Merger

A contract is said to have been discharged by way of merger where an inferior right possessed by a person coincides with a superior right of the same person.



Example

Arun, who is holding a certain property under a lease, buys it. His rights as a lessee vanish; they are merged into the rights of ownership which he has now acquired. The rights associated with lease were inferior to the rights associated with the ownership.

e) Discharge by operation of law

Discharge by operation of law may take place in five ways:

i) Insolvency

The insolvency law provides for discharge of contracts under certain circumstances so where an order of discharge is passed by an insolvency court the insolvent stands discharged of all debts incurred previous to his adjudication.

ii) Death

Death of the promisor results in termination of the contract in cases involving personal skill or ability.

iii) Merger

When between the same parties, a new contract is entered into, and a security of a higher degree or a higher kind is taken, the previous contract merges in the higher security. Thus a right of action on an ordinary debt would be merged in the right of suing on a mortgage for the same debt.

iv) By right and liability going into the hands of the same party

Contract creates right to one party and liability to other when right and liability reach the same person, the result is discharge of contract.

v) Unauthorized material alteration

Where any of the parties alters any of the terms of the contract without seeking the consent of the other party to it, the contract terminates.

f) Discharge by impossibility of performance

A contract may be discharged because of impossibility of performance. There are two types of impossibility: (i) Initial Impossibility that may be inherent in the transaction (i.e., the contract), (ii) Subsequent Impossibility that may emerge later by the change of certain circumstances material to the contract.

i) Initial Impossibility (Pre-contractual)

It means impossibility at the time of formation of the contracts.

- either known to the parties (Void ab initio)
- or unknown to the parties (Void due to mutual mistake)



Caution: Where the promisor knows about the initial impossibility then he is liable to pay compensation to promise.



Examples

- Arun promises to pay Bittu 50,000 if Bittu rides on a horse to the moon. The contract is void ab initio.
- Arun agrees with Bittu to discover treasure by magic. The agreement is void ab initio, as there is an impossibility inherent therein.

ii) Subsequent or Supervening Impossibility (Post contractual)

Sometimes a contract is capable of being performed when it was formed, but some subsequent event renders the performance impossible. In such a case also the contracts become void.

1. Destruction of subject-matter

Where the subject matter of a contract is destroyed for no fault of the promisor, the contract becomes void by impossibility of performance.



Example: A music hall was let for a series of concerts on certain days. The hall was burnt down before the date of the first concert. The contract was held to be void.

2. Non-existence/non-occurrence of particular state of things

When certain things necessary for performance cease to exist, the contract becomes void.

Legal Aspects of Business



Example: Pihu and Biku contract to marry each other. Unfortunately, before the time fixed for marriage Pihu goes mad. The Contract becomes Void.

3. Death/ Incapacity for personal service

Where the performance of the contract must be executed personally by the promisor, his death or physical disability to perform shall render the contract void and thus exonerate him from the obligation.



Example: A boy was engaged for 5 years to perform as a drummer for all the seven nights in a week whenever the band had business. But on contract of illness, he was certified to be able to perform only 4 nights, the contract was held to have been frustrated because of personal incapacity to perform.

4. Change of law

If there is a subsequent change in law which may render the contract illegal, the contract is deemed discharged.



Example: There was a contract between Lila and Kittu to supply of oilseeds of a specific quality. But the Indian Govt. rendered the sale and purchase of oilseeds illegal. Both parties were discharged from performance of such contract.

5. Outbreak of war

If war is declared between two countries subsequent to the making of the contract, the parties would be exonerated from its performance.

- Contracts Entered into during war with an alien enemy are void initially.
- Even after the peace returns , they remain void and of no effect.

1.7 Breach of Contract

Breach of contract amounts to a broken promise to do or not to do an act in legal terms. It may be single, occurring at a single point of time or continuing breaches. A lawsuit for breach of contract is a civil action and the remedies awarded to the aggrieved party are designed to place him in the position that he would be in if not for the breach. Remedies for contractual breaches are not designed to punish the breaching party but aim at compensating the injured party for its loss due to the breach.

Breach of contract can be an Actual Breach or Anticipatory Breach.

Actual Breach

Actual breach occurs when one of the parties denies to perform its side of the bargain on the due date or performs incompletely. It is failure of one party to perform as promised, or making it impossible for the other party to perform.

- a) at the time when performance is due, or
- b) during the performance of the contract. Thus, if a person does not perform his part of the contract at the stipulated time, he will be liable for its breach.



Example: Eraser contracted with a Railway Company to supply a certain quantity of railway chairs at a certain price. The delivery was to be made in installments. After a few installments had been made, the Railway Company asked Eraser to deliver no more. Held, Eraser could sue for breach of contract.

Anticipatory Breach

The anticipatory breach of contract occurs when a party repudiates it before the time fixed for performance has arrived or when a party by his own act disables himself from performing the contract.



Example: Parker contracts to supply Marker with certain articles on 1st August. On 20th July, Parker informs Marker that he will not be able to supply the goods. Marker is entitled to sue Parker for breach of promise.

Consequences of Anticipatory Breach

- The aggrieved/injured party can rescind the contract and treat the contract as an end, and at once sue for damages, or
- The aggrieved/injured party may elect not to rescind but to treat the contract operative and wait for the time of performance and then hold the other party liable for the consequences of non-performance.

Remedies of Breach of Contract

In case of breach of contract, the injured party may go for the following remedies available under the Act:

- 1) Rescind the contract and refuse further performance of the contract.
- 2) Sue for damages
- 3) Sue for specific performance
- 4) Sue for an injunction to restrain the breach of a negative term
- 5) Sue for quantum meruit

1. Rescind the Contract and Refuses Further Performance of Contract

Under Sec. 65, when a party treats a contract as rescinded, it makes itself liable to restore any benefits it received under the contract to the party from whom such benefits were received.



Example: Dhruv promises Star to supply 10 bags of cement on a certain day. Star agrees to pay the price after the receipt of the goods. Dhruv does not supply the goods. Star is discharged from liability to pay the price.

The court may grant rescission –

- a) Where the contract is voidable by the plaintiff; or
- b) Where the contract is unlawful for causes not apparent on its face and the defendant is more to blame than the plaintiff.

The court may refuse to grant rescission –

- a) Where the plaintiff has expressly or implied ratified the contract; or
- b) Where owing to the change of circumstances, the parties cannot be restored to their original positions; or
- c) Where third parties, during the subsistence of contract, acquired rights in good faith and value; or
- d) Where only a part of the contract is sought to be rescinded and such part is not severable from the rest of the contract.



Case Study

Palak, a music teacher, enters into a contract with Rohit, a theatre manager, to provide music training to his singers at his theatre for two nights per week for the next two months, and Rohit agrees to pay her 5,000 for each night of training. Palak willfully absents herself from the theatre on the sixth night.

Point of Discussion

Can Rohit rescind the contract?

[Hint: Yes, Rohit is entitled to claim compensation for the damage which he has sustained]

through non-fulfilment of the contract.]

2. Sue for damages: Sec. 73

The party injured by the breach of contract can claim damages. Damage is the monetary compensation allowed by the court to the injured party for the loss or injury suffered by him as a result of breach by the other party.



Case Study

Mika, a buyer, agreed to purchase a TV for 50,000, but Jassi, the seller, failed to deliver it on the specified date. In such a case, normally, the buyer will be forced to go and buy a TV elsewhere.

However, if, in the meantime, the price of a TV has gone up by 10,000.

Point of Discussion

What remedy does Mika have against Jassi?

[Hint: Mika can claim 10000 from Jassi as damages.]

Types of damages

Unliquidated damages

a) General or ordinary damages

These damages are those which naturally arise in the usual course of things from such breach.



Case Study

Pencil agreed to sell to Sharpener 100 quintals of Kalyan wheat at 335 per quintal and the price was to be paid at the time of delivery. The price of wheat rose to 350 per quintal and Pencil refused to sell the wheat.

Point of Discussion

Can Sharpener claim any damages from Pencil?

[Hint: Yes, Sharpener can claim ordinary damages worth 1500.]

b) Special damages

Damages occur under some special or peculiar circumstances. The communication of the special circumstances is a prerequisite to the claim for special damages.



Case Study

Ritik delivered goods to the railway admin. to be carried to a place where an exhibition was being held and told the clerk that if the goods did not reach the destination on the stipulated date, he would suffer a special loss. The goods arrived late.

Point of Discussion

Can Ritik claim any damages from Railways?

[Hint: Yes, Ritik can claim special damages as he pre-informed the railways about the special loss that he could have incurred in case railways would fail to perform its contractual obligation.]

c) Exemplary, or punitive, vindictive damages

- These damages are awarded to punish the defendant and are not granted for breach of contract.

Legal Aspects of Business

- These damages are awarded in case of breach of marriage promise and wrongful dishonour of cheque by the bank.



Caution: In the case of breach of marriage, the amount of vindictive damages will depend upon the extent of injury to the party's feelings.

In the case of wrongful dishonour of cheque by the bank, the smaller the amount of the cheque dishonoured, the larger will be the damages as the credit of the customer would be injured in a far greater measure, if a cheque for a small amount is wrongfully dishonoured.

d) Nominal damages

Where there has been an infringement of contractual rights, but no actual loss has been suffered, then nominal damages are awarded.



Case Study

Preety agreed to supply sleepers to the railway administration. According to one of the terms of the contract, Preety was required to pay damages to railways on her failure to supply whether the railways suffered loss or not. Preety failed to supply the sleepers and railways did not suffer any loss. A case was filed by the Railways administration against Preety to claim the damages.

Point of Discussion

Could Railways administration be able to claim damages from Preety?

[Hint: The court disallowed the suit and held that railways could claim only nominal damages from Preety.]

e) Damages for loss of reputation

- These damages are not recoverable.
- An exception is banker who wrongfully dishonours the customer's cheque.
- In this case, the smaller the amount of cheque is dishonoured, the larger the amount of damages are awarded to a business man
- Nominal damages can be recovered by non-business man

f) Damages for inconvenience and discomfort

These damages can be recovered for physical inconvenience and discomfort. The general rule is that the measure of these damages is not affected by the motive and the manner of breach of contract.



Case Study

Table, a surveyor told Chair, a client that the house which Chair is buying is in good condition, but, in fact, substantial work needed to be carried on it. This put considerable strain on Chair's marriage as he has to live under those appalling conditions with his wife. Chair sued Table and claimed damages.

Point of Discussion

Could Chair win in the law suit?

[Hint: Yes, Chair was entitled to receive an award for his physical discomfort and hardship.]

Some other following damages can also get claimed in case of breach of contract:

- Difficulty of assessment
- Mitigation of damages
- Cost of a decree

Liquidated damages

Unit 01: Indian Contract Act, 1872

Where the contracting parties agree in advance the amount payable in the event of breach, the monetary compensation payable is called liquidated damages. The essence of liquidated damages is a genuine covenanted pre-estimate of the damages.

If a contract includes a provision that, on a breach of contract, damages of a certain amount or calculable at a certain rate will be payable to the aggrieved party, the court will normally accept the relevant figure as a measure of damages. In case, the court finds the stipulated damages as unreasonable, then court may decide the reasonable damages itself to be paid as penalty for breach of contract.



Case Study

Promod gave Suresh a bond for the repayment of 1,000 with interest at 12%, at the end of 6 months, with a stipulation that in case of default, the interest would be payable at 75%, from the date of default.

Point of Discussion

Is such a rate of interest valid?

[Hint: This is a stipulation by way of penalty, and Suresh is only entitled to recover from Promod such compensation as the court considers reasonable.]

3. Sue for specific performance

Where damages are not an adequate remedy, the court may direct the party in breach to carry out his promise according to the terms of the contract. This is called specific performance of the contract.



Example: Zeenat, a party to a contract, paid for the delivery of goods, but Hema, the other party, did not ship them properly. A specific performance decree might require the goods to be properly delivered.

Cases where specific performance is not granted:

- Where monetary compensation is an adequate relief.
- Where the court cannot supervise the execution of the contract.
- Where a contract is for personal service.
- Where one party is minor.

Cases where specific performance is granted:

- Where actual damage cannot be determined.
- If monetary compensation will not be adequate.
- Where the act to be done is in the performance of trust.
- Where, in general, it would be just and equitable to do.

4. Sue for an injunction to restrain the breach of a negative term

- The power to grant an injunction is discretionary.
- It may be granted temporarily or for an indefinite period.
- It may be prohibitory or mandatory.



Case Study

Lumley v. Wagner (1852)

Wagner agreed to sing at Lumley's theatre, and during a certain period to sing nowhere else. Afterwards, Wagner made a contract with Z to sing at their theatre and refused to perform the contract with Lumley.

Point of Discussion

Legal Aspects of Business

Which remedy can Lumley use against Wagner in court?

[Hint: Held, Wagner could be restrained by Injunction from singing for Z.]

5. Sue for quantum meruit

It means “as much as earned or deserved” or “as much as is merited”.



Example: A contractor was contracted to work at a school. The contractor did some work but messed up part of the work (breach of contract). The school suspended the construction work because of the problem. On the basis of quantum meruit, the contractor was entitled to be paid for the services he had already performed for the school.

Summary

- A contract is an agreement, enforceable by law, made between at least two parties to do a particular act or abstain from doing a particular act.
- A contract essentially has two elements: Agreement and Enforceability.
- All agreements are contracts if they are made by free consent of the parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void.
- Contracts can be classified on the basis of validity, formation and performance.
- When two or more persons agree upon the same thing in the same sense, they are said to consent and have consensus ad idem.
- The consent is said to be free when it is not caused by Coercion, Undue Influence, Fraud, Misrepresentation, and Mistake.
- Coercion is (i) the committing or threatening to commit any act forbidden by the Indian Penal Code or (ii) 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.
- When consent to an agreement is caused by coercion the agreement is voidable at the option of the party whose consent was so obtained. Thus, the aggrieved party can have the contract set aside if he so desires otherwise the contract is a valid one.
- 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. The burden of proving that the contract is not induced by undue influence lies on the party who is in a position to dominate the will of the other.
- 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.
- Misrepresentation is a false statement that the person making it honestly believes to be true or that he is unaware is false.
- A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practiced, or to whom such misrepresentation was made, does not render a contract voidable.
- Mistake is defined as an erroneous belief about something. It may be a mistake of fact or a mistake of law.
- A contract is discharged when rights and obligations created by it comes to an end.

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- A contract may be discharged by (i) performance; (ii) tender; (iii) mutual consent; (iv) subsequent impossibility; (v) operation of law; (vi) breach.
- If the parties to a contract agree to substitute a new contract for it, or to rescind it or alter it, the original contract is discharged. A contract may terminate by mutual consent in any of the six ways viz. novation, rescission, alteration and remission, waiver and merger.
- Breach of contract amounts to a broken promise to do or not to do an act in legal terms. It may be single, occurring at a single point of time or continuing breaches.
- Breach of contract can be an Actual Breach or Anticipatory Breach.
- Actual breach occurs when one of the parties denies to perform its side of the bargain on the due date or performs incompletely.
- The anticipatory breach of contract occurs when a party repudiates it before the time fixed for performance has arrived or when a party by his own act disables himself from performing the contract.
- In case of breach of contract, the injured party may go for the following remedies available under the Act:
 - 1) Rescind the contract and refuse further performance of the contract.
 - 2) Sue for damages
 - 3) Sue for specific performance
 - 4) Sue for an injunction to restrain the breach of a negative term
 - 5) Sue for quantum meruit

Keywords

- **Alteration:** If the parties mutually are to change certain terms of the contract, it has the effect of terminating the original contract. There is, however, no change in the parties.
- **Contract:** It is an agreement, enforceable by law, made between at least two parties by which rights are acquired by one and obligations are created on the part of another.
- **Executed contract:** A contract which is wholly performed by both parties.
- **Executory contract:** A contract at which performance of both parties have yet to be performed.
- **Express contract:** The terms of a contract may be stated in words (written or spoken).
- **Illegal agreement:** It is one that the courts will not enforce because the purpose is to achieve an illegal end.
- **Implied contract:** May be implied in fact or implied in law. Contracts implied in fact and contracts implied in law are not really contracts at all.
- **Misrepresentation:** It is also known as simple misrepresentation whereas fraud is known as fraudulent misrepresentation.
- **Mistake of foreign law:** The above maxim – “ignorance of law is no excuse” is in-applicable to foreign law. The mistake of foreign law is to be treated as a mistake of fact.
- **Mistake:** May be defined as an erroneous belief on the part of the parties to the contract concerning something pertaining to the contract.
- **Nominal damages:** These are awarded in cases of breach of contract where there is only technical violation of the legal right but no substantial loss is caused thereby.
- **Ordinary damages:** Cannot be claimed for any remote or indirect loss or damages by reason of the breach.
- **Remission:** It is the acceptance of a lesser sum than what was contracted for or a lesser fulfillment of the promise made.

Legal Aspects of Business

- **Special damages:** These damages are claimed in case of loss of profit.
- **Waiver:** It means relinquishment or abandonment of a right.
- **Undue influence:** Consists in the improper exercise of power over the mind of one of the contracting parties by the other.
- **Vindictive or punitive damages:** These damages are awarded with a view to punish the defendant and not solely with the idea of awarding compensation to the plaintiff.
- **Void agreement:** An agreement not enforceable by law.
- **Void contract:** A contract which ceases to be enforceable by law.
- **Voidable contract:** A contract which is enforceable by law at the option of one party thereto, but not at the option of other.

Self-Assessment

1. Mr. Akhilesh owes an amount of 76,000 to Mr. Keshav. Mr. Keshav has the right to recover this amount from Mr. Akhilesh only, not from anybody else. This right is known as:

A. Jus in Personam
B. Jus in Rem
2. An agreement between Neha and Arun to go for a picnic does not become a contract as:

A. there is no valid offer involved
B. there are not two competent parties involved
C. it is not a valid agreement
D. it is not enforceable at law as there is no intention of both parties to create legal obligations and rights for each other
3. Pretty agreed to sell a government property to Mandeep for 1.12 crores, Mandeep agreed to buy that property. Is this a valid agreement?

A. Yes, as there is a lawful offer and acceptance
B. Yes, as it is enforceable at law
C. No, as Pretty is incompetent to enter such a contract
D. No, as the consideration is unlawful
4. If an agreement is induced by unilateral mistake, it will be:

A. valid
B. void
C. voidable at the option of either party to the contract
D. voidable at the option of an aggrieved party
5. Mridul, a trader of oils, deals in 10 types of different oil, enters into a contract with Sanchit to sell him 560 tons of oil. But, what kind of oil is not mentioned clearly. Such contract will be:

A. Valid, as all essentials of a valid contract are fulfilled
B. Invalid, on the ground of uncertainty of terms of the contract
C. Invalid, based on agreement Not Expressly Declared Void
D. Invalid, based on the impossibility to perform

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6. Madhur Das threatens to shoot Pappu Lal if he does not sell his new BMW Car to Madhur Das for 6,15,000; Pappu Lal had to agree to such offer, hence entered into a contract with Madhur Das for such sale of the car. Such contract between Madhur Das and Pappu Lal is _____ in the eyes of the law.
- A. valid
 - B. void
 - C. void ab initio
 - D. voidable
7. It is a legally binding contract but cannot be enforced due to a technical flaw such as not being properly stamped.
- A. valid
 - B. unenforceable
 - C. void ab initio
 - D. voidable
8. Cherry calls Strawberry and offers to sell her car for \$ 45,000; Strawberry responds by informing Cherry that she accepts the offer. Such contract between Cherry and Strawberry is termed as:
- A. Express contract
 - B. Implied contract
 - C. Quasi-contract
 - D. E-Commerce contract
9. Megha offers to sell her car to Ajay for 6 lakhs on a credit of 2 months. Ajay accepts the Megha offer. Megha sold the car to Ajay and delivered the same to him. It is an example of a/an:
- A. Executed contract
 - B. Unilateral Executory contract
 - C. Bilateral Executory contract
 - D. Quasi-contract
10. Julie asked a railway coolie to carry her luggage and place it in a carriage for 500 as charges. Coolie accepted her offer and picked the luggage, and started carrying the same to the destination place. In such a scenario, the contract among them would be termed as:
- A. Executed contract
 - B. Unilateral Executory contract
 - C. Bilateral Executory contract
 - D. Implied contract
11. An agent refused to hand over books of accounts of a business to a new agent unless the principal released him from all liabilities; the principal had to give release deed as demanded. Comment on the consent of the principal to provide a release deed in such a scenario.
- A. Consent of principal is free
 - B. Consent of principal is not free due to coercion
 - C. Consent of principal is not free due to undue influence

D. Consent of principal is not free due to misrepresentation

12. Amitabh threatens to kill Chetan (Kelash's son) if Kelash does not sell his house to Amitabh. Kelash agreed to sell his house to Amitabh on Amitabh terms. Does coercion cause this agreement?

A. No, as Kelash agreed to Amitabh terms

B. No, as Amitabh has not exercised coercion against Kelash

C. Yes, as coercion may be directed against anybody

D. Yes, as the unlawful detaining, or threatening to detain, any property also amounts to coercion

13. A contract is said to be induced by _____, where the relation subsisting between the parties is 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.

A. Coercion

B. Undue Influence

C. Fraud

D. Misrepresentation

14. Pihu sells to Rohit locally manufactured goods as imported goods charging a higher price. This amounts to:

A. Coercion

B. Undue Influence

C. Fraud

D. Misrepresentation

15. If truth could have been discovered through diligence, then no remedy is available for misrepresentation.

A. True

B. False

16. Mukesh takes a loan from Amitabh and agrees to pay instalments every month for the next five years. However, he does not pay even a single instalment. Amitabh calls him a few times but then gets busy and takes no action. Three years later, Amitabh approaches the court to help him recover his money. Can Amitabh win in the lawsuit and be able to recover his amount?

A. Yes, as Amitabh has all rights to recover his money

B. No, as the contract is discharged by lapse of time

C. No, as the contract is discharged by performance

D. No, as the contract is discharged by mutual consent

17. When an older contract get discharged through a new contract with the same parties, it is termed as:

A. Novation

B. Rescission

C. Alteration

D. Merger

18. When a contract is discharged before the date of performance by agreement between the parties to the effect that it shall no longer bind them, it is termed as:
- A. Novation
 - B. Rescission
 - C. Alteration
 - D. Merger
19. Lekha, the lender agreed to accept 5,000 from Shakuntla in full settlement of a claim of 7,500. Such a case is an example of:
- A. Discharge of contract by Novation
 - B. Discharge of contract by Alteration
 - C. Discharge of contract by Remission
 - D. Discharge of contract by Rescission
20. A music hall was taken on lease for a series of concerts on certain days. The hall was burnt down before the date of the first concert. Such contract will be held:
- A. Valid and hence enforceable at law
 - B. Void due to initial impossibility
 - C. Void due to destruction of subject-matter
 - D. Void due to destruction incapacity of personal service
21. Pinchu contracts to supply Shabnam with certain articles on 1st August. On 15th July, Pinchu informs Shabnam that he will not be able to supply the goods on the specified date. It is an example of:
- A. Actual breach of contract by Pinchu
 - B. Actual breach of contract by Shabnam
 - C. Anticipatory breach of contract by Pinchu
 - D. Anticipatory breach of contract by Shabnam
22. Emson contracted with a School to supply a certain quantity of Student chairs at a certain price. The delivery was to be made in installments. After a few installments had been made, the School asked Emson to deliver no more. In such a case,
- A. Emson could sue the School for actual breach of contract at the time when performance is due.
 - B. Emson could sue the School for actual breach of contract during the performance of the contract.
 - C. Emson could sue the School for anticipatory breach of contract.
 - D. School could sue Emson for anticipatory breach of contract.
23. Damages that naturally arise in the usual course of events from the breach of contract are termed as:
- A. Ordinary damages
 - B. Nominal damages
 - C. Natural damages
 - D. Special damages

Legal Aspects of Business

24. The damages that may be awarded to punish the defendant in case of breach of marriage promise are called:

- A. Ordinary damages
- B. Nominal damages
- C. Exemplary damages
- D. Special damages

25. Himesh agreed to sing at Mukesh's theatre, and during a certain period to sing nowhere else. Afterwards, Himesh made a contract with Karan to sing at his theatre and refused to perform the contract with Mukesh. Which remedy can Mukesh use against Himesh in court?

- A. Sue for an injunction
- B. Sue for quantum meruit
- C. Sue for punitive damages
- D. Sue for nominal damages

Answers for Self Assessment

1.	A	2.	D	3.	C	4.	D	5.	B
6.	D	7.	B	8.	A	9.	B	10.	C
11.	B	12.	C	13.	B	14.	C	15.	A
16.	B	17.	A	18.	B	19.	C	20.	C
21.	C	22.	B	23.	A	24.	C	25.	A

Review Questions

1. "All agreements are not contracts but all contracts are agreements." Discuss the statement explaining the essentials of a valid contract.
2. "In commercial and business agreements, the presumption is that the parties intended to create legal relation," Discuss.
3. Illustrate the difference between void, voidable and illegal agreements. Discuss the validity of agreements collateral to such agreements.
4. Distinguish between the following classes of contracts:
 - a) Express and implied contracts
 - b) Executed and executory contracts
 - c) Valid, void and voidable contracts
 - d) Void agreement and void contracts
5. Explain different types of contracts on various parameters of classification of contracts.
6. Write short notes on the following:
 - a) Illegal contract
 - b) Unenforceable contract
 - c) Quasi contract
 - d) E-Commerce contract
 - e) Unilateral executed contract
7. "All illegal agreements are void but all void agreements are not illegal." Comment on the statement and support your answer with suitable examples.

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8. Tom offered to sell his car to Jerry for 50000 and daddy orally agreed for purchasing the car. Can such agreement be enforced by the parties?

[Hint: as an oral contract is fully enforceable in the court of law.]

9. Doraemon agreed to pay 1000 to Shin Chen and in consideration Shin Chen agreed to write 1000 pages in 10 minutes. Is it a valid contract?

[Hint: No, it is a void contract as an agreement to do an impossible act renders the contract void.]

10. Lalita invites Sharmila for dinner at her house on a Sunday. Sharmila hires a taxi and reaches Lalita's house at the appointed time, but Lalita fails to fulfill her promise. Can Sharmila recover any damages from Lalita?

[Hint: No, as there is no intention to create legal obligations in social agreements.]

11. "Two or more persons are said to consent when they agree upon the same thing in the same sense". Explain this statement and give illustrations.

12. Discuss the law relating to the effect of mistake on contracts.

13. What is misrepresentation? Distinguish it from fraud.

14. What remedies are available to a person induced to enter into a contract by misrepresentation which is not fraud and fraud?

15. What is coercion? Distinguish it from undue influence.

16. When consent is not said to be free? What is the effect of such consent on the validity of a contract?

17. Explain the mistake of fact and law and Illustrate the effect of the same on an agreement.

18. When is consent said to be given under coercion? What is its effect on the contract? Also discuss the position of the parties to a contract entered into under coercion.

19. Cat orally offered to pay Ant, an auto mechanic, 500 for testing a used car which Cat was about to purchase from Dog. Ant agreed and tested the car. Cat paid Ant 500 in cash for his services. Is the agreement between Cat and Ant (a) express or implied, (b) executed or executory, (c) valid, void, voidable or unenforceable?

20. Anil promised to pay 5,00,000 to Rita, if she did not marry throughout her life. Rita promised not to marry at all. Can this agreement be treated as a valid contract?

[Hint: No, the agreement is in restraint of marriage. Hence, it is void.]

21. My grandmother invited my brother to come and stay with her for a week. My brother accepts the invitation but when he reaches at grandmother's house, she could not accommodate him because of no room availability. Can my brother claim compensation from her? Give reasons.

[Hint: No, as it is social agreement.]

22. Shridhar calls and offers to sell his Diamond Bracelet to Gaurav for 9 lakhs, which Gaurav accepts. Shridhar delivers the bracelet to Gaurav and Gaurav pays 9 lakhs to Shridhar. Identify the type of contract exists between Shridhar and Gaurav on the basis of performance and formation.

23. Tittu agrees to coach Ritu, a medical student, from the first day of the coming month and Ritu agrees to pay a consideration of 3000 p.m. at the end of each month of coaching. Identify the type of contract exists between Tittu and Ritu on the basis of performance and validity.

24. Tina permits a railway coolie to carry her luggage and place it in a carriage. Coolie duly placed her luggage in the carriage. Is this a unilateral executory, bilateral executory or executed contract? State reasons.

25. Arpit, being in debt to Bhanu, the money-lender of his village, contracts a fresh loan on terms which appear to be unconscionable. Can it be said that Arpit gave free consent to terms of fresh loan? If Not, who should prove that the consent was free? Justify.

[Hint: No, Arpit consent is influenced by undue influence. It lies on Bhanu to prove that the contract was not induced by undue influence.]

Legal Aspects of Business

26. Hitesh sold to Lalit certain pigs. The pigs were suffering from a fever and Hitesh knew it. The pigs were sold "with all faults." Hitesh did not disclose the fever to Lalit. Has Hitesh frauded with Lalit? State reasons.

27. Pihu bought a cannon from Akshay. Akshay knew the cannon had a defect, which rendered it worthless, and so he put a metal plug to conceal the defect. Pihu accepted the cannon without examining it. The cannon burst when used. Pihu filed a law suit against Akshay on ground of being frauded and claimed damages. Will Pihu succeed in the law suit?

[Hint: No, it was held there was no fraud because Pihu would have bought it even if no deceptive plug had been put. Pihu was not in fact deceived by it.]

28. Avinash, intending to deceive Bikku, falsely represents that nine hundred maunds of indigo are made annually at Avinash's factory, and thereby induces Bikku to buy the factory. Discuss the validity of contract.

[Hint: The contract is voidable at the option of Bikku due to fraud.]

29. Bat, having discovered a vein of ore on the estate of Arrow, adopts means to conceal, and does conceal, the existence of the ore from Arrow. Through Arrow's ignorance Bat is enabled to buy the estate at an under-value. Discuss the validity of the contract.

[Hint: The contract is voidable at the option of Arrow due to fraud.]

30. Peter rents John's apartment for two years. One year into the contract, he offers to buy the property from John, who agrees. The enter a sale contract and Peter becomes the owner of the apartment. Here Peter has two rights; one accorded by the lease agreement making him the renter and second by the sale agreement making him the owner. Is the contract of lease discharged?

31. C offers to sell to D a painting which C knows is a good copy of a well-known masterpiece. D thinking that painting is an original one and that C must be unaware of this, immediately accepts D's offer. Does this result in a contract?

[Hint: Yes. The doctrine of Caveat Emptor (Get the buyer beware) will apply.]

32. Explain the various ways in which a contract may be discharged.

33. Discuss the effects of supervening impossibility on the performance of a contract.

34. Write short notes on the following:

- a) Discharge of contract by alteration
- b) Discharge of contract by merger
- c) Discharge of contract by initial impossibility
- d) Discharge of contract by performance
- e) Discharge of contract by novation
- f) Discharge of contract by remission
- g) Discharge of contract by operation of law
- h) Discharge of contract by attempted performance

34. Explain the different ways in which a breach of contract may arise.

35. S agreed to act as sales manager for Company X for a period of three years at monthly salary of 1000. S worked for six months and then left and joined another company at a higher salary. What are the rights of Company X?

[Hint: Company X may not only treat the contract as rescinded but also bring suit against S to recover any monetary loss suffered by it as a result of the breach].

36. M, a retailer of milk, supplied C with milk which was consumed by C and his family. The milk contained typhoid germs and C's daughter was infected thereby and died. Discuss the legal position of the parties.

[Hint: C can recover damages from M (Frost v. Aylesbury Dairy Co. Ltd., (1925) 1 K.G. 608.)]

37. Explain 'breach of contract' as a mode of discharge of contract.

38. Illustrate the circumstances under which a party is entitled for specific performance of a contract.

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39. Krrish, a ship owner, agreed to carry a cargo of sugar belonging to Suraj from Mumbai to Kolkata. He knew that there was a sugar market in Kolkata and that Krrish was a sugar merchant, but did not know that he intended to sell the cargo immediately on its arrival. Owing to Shipment's default, the voyage was delayed and sugar fetched a lower price than it would have done had it arrived on time. Krrish claimed compensation for the full loss suffered by him because of the delay. Could Krrish get demanded compensation? Give and justify your decision.

[Hint: Krrish can claim only ordinary damages. He could have claimed special damages only if the other party was made known of the possibility of such special loss in advance.]

40. Deepak contracts to sell and deliver to Rohit, on the 1st of January, certain cloth from which Rohit intends to manufacture caps of a particular kind, for which there is no demand except during that season. The cloth is not delivered till after the appointed time and too late to be used that year in making caps. How will the compensation table to Rohit by Deepak, be calculated?

[Hint: Rohit is entitled to receive from Deepak, by way of compensation, the difference between the contract price of the cloth and its market price at the time of delivery, but not the profits which we expected to obtain by making caps, 9 the expenses which we have been put to in making preparation for the manufacture.]

**Further Reading**

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**Web Links**

- <https://www.indiacode.nic.in/handle/123456789/2187?locale=en>
- <https://legislative.gov.in/sites/default/files/A1872-09.pdf>

Unit 02: The Sale of Goods Act, 1930

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Objectives

After studying this unit, you will be able to:

- explain the meaning and essentials of a valid contract of sale.
- illustrate the difference between contract of sale and agreement to sell.
- illustrate the meaning and types of conditions in a contract of sale.
- explain the consequences of breaching the various implied conditions by parties of contract of sale.
- illustrate the meaning and types of various warranties in a contract of sale.
- explain the consequences of breaching the warranties by parties of contract of sale.
- compare the conditions and warranties.
- explain the doctrine of caveat emptor with its exceptions.
- illustrate the concept of an unpaid seller.
- explain the rights available to an unpaid seller.
- review the importance of the Sale of Goods Act, 1930 in promoting the contracts of sale and protecting the interests of buyer and seller.

Introduction

A sale is a type of contract in which the seller transfers the ownership of goods to the buyer for a money consideration. 'Goods' means every kind of movable property, other than actionable claims and money; and includes stocks 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.

Legal Aspects of Business

Sale of goods is the most prevalent of all commercial contracts. Awareness of its key principles is inevitable to all those involved in any business function. The law relating to sale of goods or movable property in India is codified in the Sale of Goods Act, 1930.

The Act covers topics such as the concept of sale of goods, conditions and warranties arising out of sale, delivery of goods and passing of property, rights of an unpaid seller and other rights and obligations of the buyer and the seller. The Act came into force on 1st July, 1930. It extends to the whole of India.

It is well known fact that before a contract of sale is entered into, a seller frequently makes representations or statements with reference to the goods which influence the buyer to clinch the bargain. Such representations or statements differ in character and importance. Whether any statement or representation made by the seller with reference to the goods is a stipulation forming part of the contract or is a mere representation (such as expression of an opinion) forming no part of the contract, depends on the construction of the contract. If there are no such representations, the ordinary rule of law - caveat emptor', i.e., "let the buyer beware" --applies. This means the buyer gets the goods as they come, and it is no part of the seller's duty to point out the defects in the goods to the buyer.

In this unit, concept, and essentials of a valid contract of sale of goods, meaning and types of conditions, meaning and types of warranties, and rights of unpaid seller are discussed.

2.1 Contact of Sale of Goods: Concept and Definition (Sec. 4)

"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. There may be a contract of sale between one part-owner and another" [Sec. 4(1)].

A contract of sale is a legal term which includes both sale and an agreement to sell. There are always two parties viz. a buyer and a seller in a sale. Sale means the transfer of goods from a seller to the buyer for a price. A contract of sale may be absolute or conditional [Sec. 4(2)].

There can be two types of contracts related to Sales:

- Actual or Absolute Sale
- Conditional Sale or Agreement to sell

Actual or Absolute Sale

Under actual or absolute sale, property in the form of goods is immediately transferred from sellers to buyers. In other words, 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)].



Example: Miss. Rina enters into contract of sale of horse to Mr. Guru against 30,000. Mr. Guru pays 30,000 to Miss. Rina and she delivers her horse to Mr. Guru. Hence, It is an actual sale.

Agreement to Sell or Conditional Sale

Where the transfer of property, in the goods is to take place at a future date or subject to some condition to be fulfilled, the contract is called an agreement to sell [Sec. 4(3)].



Example: Miss. Poonam agrees with Mr. Mirza to sell him her house against 30 lakh after the construction next year. Hence, it is an agreement to sell.



Case Study

Mohit is entering into one contract to sell 100 bales of cotton to Ramesh at 1,000 per bale. Mohit put a term to deliver the bales only when Ramesh will pay him 50% of contract amount in advance.

Point of Discussion

Is this a contract of Sale?

{Hint: No, as it is a conditional sale, where the transfer of property in the goods will take place post payment of 50% of contractual amount by Ramesh.}

2.2 Goods: Meaning and Classification

Goods: Meaning

'Goods' means every kind of movable property other than actionable claims and money 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)



Examples

- Good-will
- Trademarks
- Copyrights
- Patents
- Water
- Gas
- Electricity
- Shares and Stock
- Growing crops
- Vehicles

What is not treated as goods ?

- immovable property
- money (current money not old rare coins)
- actionable claims (loan/debt)



Task

Associated hotels of India Vs Excise and Taxation officer

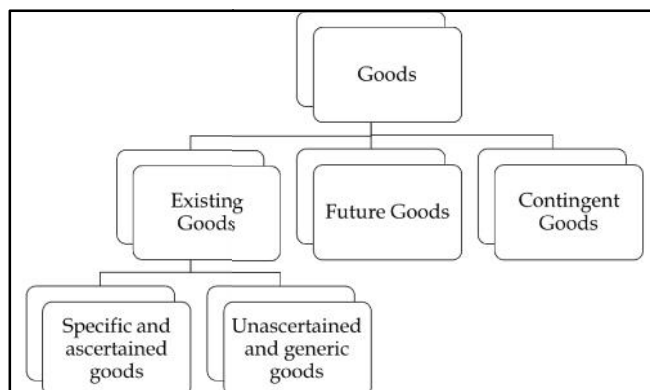
A hotel company provided residence and food making a consolidated charge for both the services. No rebate was allowed if food was not taken by the customer.

Point of Discussion

Does supply of food considered as good?

Classification of Goods

Goods are categorized into the following three kinds, namely, existing goods, future goods and contingent goods.



Source: Gupta, P. *Legal aspects of Business: Concept and Applications*. Vikas Publishing House Pvt. Ltd

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1. Existing Goods

The goods owned and possessed by the seller at the time of entering in the contract of sale are called existing goods. Existing goods are of two types:

- Specific Goods and ascertained Goods
- Unascertained and generic Goods

a) Specific and ascertained goods

“**Specific goods** means goods which are clearly identified and agreed upon at the time, the contract of sale is made”.



Example: Ashwani, a mobile dealer enters into a contract to sell an Apple Black colored iPhone 13 to Khushi for 60,000. In this example, as the subject matter (good) is clearly identified and agreed upon at the time of entering contract, thus “Apple Black colored iPhone 13” is a specific good.

“**Ascertained goods** are the goods separated from the bulk or stock to perform the contract of the buyer”.



Example: Sheela owns 20 i20 Asta Cars of white color. Uma enters into a contract with Sheela to buy one car out of those 20 cars. After the contract, one car is given to Uma. The car that is delivered to Uma is an ascertained good.

b) Unascertained and generic goods

These are the goods that cannot be identified or are not specifically agreed upon, but can only be indicated by description at the time of contract of sale. The goods may be existing in large quantity from which only a part thereof is to be sold. The part to be sold cannot be ascertained unless it is separated from the bulk.

- In a contract of sale for 10 black leather jackets of XL size, the wholesaler may deliver any 10 black leather jackets out of 100 black leather jackets of XL size, the wholesaler is in possession of. He may not deliver to buyer any specific black leather jacket.
- Arun who wants to buy a television set goes to a showroom where four sets of Janta Model of Oscar television are displayed. He sees the performance of a particular set, which he agrees to buy. The set so agreed to buy is specific set. If after having bought one set he marks a particular set, the set so marked becomes ascertained. Till this is done, all sets are unascertained.

2. Future Goods

Future goods means the goods not existing at the time of entering in contract of sale but subsequently to be manufactured or produced or acquired by the seller after making the contract of sale.

- Sec. 2(6)



Example: Rama agrees to sell to Urmilla, the entire crop of sugarcane to be grown at her farm in Uttar Pradesh for an amount of 2,00,000.

3. Contingent Goods

Contingent goods are the goods the acquisition of which by the seller depends upon a contingency which may or may not happen [Sec. 6(2)].



Example: Ravi agreed to sell 100 cotton shirts he was importing from China provided his ship arrived safely in time.

2.3 Essential elements of a Valid Contract of Sale of Goods

The definition of contract of sale of goods reveals the following essential elements of a contract of sale of goods:

- 1) Two parties
- 2) Transfer of property (ownership) in the goods
- 3) Subject matter of the contract of sale must necessarily be goods
- 4) Price to be consideration of contract of sale
- 5) Includes both a 'Sale' or 'an Agreement to sell'
- 6) No formalities to be observed
- 7) All essentials of a valid contract

1) Two parties

A sale has to be bilateral because the property in goods has to pass from one person to another i.e. Seller to buyer. However, an owner of a one part can sell his share to the owner of other part. Similarly a partner may buy the goods from the firm in which he is partner and vice-versa.



Case Study

State of Gujrat Vs Raman Lal & Co (1965)

A partnership firm was dissolved and the surplus asset including the stock in trade was divided among the partners.

Point of Discussion

Is it contract of Sale?

[Hint: No, as the partners themselves were joint owner of goods.

Explanation: As per Sec 2(1), Buyer means who buys and agrees to buy goods, Sec 2(13) Seller means who sells and agrees to sell goods. They could not be both buyer and seller.]

2) Transfer of property (ownership) in the goods

In a contract of sale, it is the ownership that is transferred (in the case of sale), or agreed to be transferred (in the case of agreement to sell), as against transfer of mere possession or limited interest (as in the case of bailment or pledge).



Example: Karan sells his car to Varun for 8,00,000. The ownership and possession of the car will be transfer from Karan to Varun as per contract terms.

3) Subject matter of the contract of sale must necessarily be goods

The sale of immovable property is not covered under Sale of Goods Act. The expression 'goods' is defined in Sec.2(7).

4) Price to be consideration of contract of sale

The consideration in a contract of sale has necessarily to be 'money', (i.e., the legal tender money). If for instance, goods are offered as the consideration for goods, it will not amount to sale. It will be called 'barter'.



Caution: If goods are sold partly for goods and partly for money, the contract is one of sale.



Case Study

Karan sells his car to Varun for 8,00,000 in consideration of a diamond necklace worth 6,00,000 and cash worth 2,00,000.

Point of Discussion

Is it a valid contract of sale?

[Hint: No, as it is barter, governed by the Transfer of Property Act.

Ascertainment of price –

1. The price in a contract of sale may be fixed by the contract or may be left to be fixed in manner thereby agreed or may be determined by the course of dealing between the parties.
2. Where the price is not determined in accordance with the foregoing provisions, the buyer shall pay the seller a reasonable price. What is a reasonable price is a question of fact dependent on the circumstances of each particular case.

5) Includes both a 'Sale' or 'an Agreement to sell'

A contract of sale may be absolute or conditional. 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, but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell.

An agreement to, sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

*Examples*

- Ankita buys a book from Sunit and pays the entire price on a counter and received the goods. It is an actual sale between Ankita and Sunit.
- Ankita agree to buy Bruno's car for 2 lakhs, but delivery will be taken placed after a month. It is an example of agreement to sell.

6) No formalities to be observed

- The act does not provide any specific form to constitute a valid contract of a sale.
- It can be made orally, or in writing, or partly orally and partly in writing.
- It can be made by mere offer and acceptance.

7) All essentials of a valid contract

As contract of sale is itself a contract between seller and buyer so all essentials of a valid contract such as free consent, lawful object, lawful consideration, capacity of parties, etc. should be present in a contract of sale.

2.4 Sale & Agreement to sell

- When under a contract of sale, the property in the goods is transferred from the seller to the buyer, the contract is called a 'sale',
- But where the transfer of the property in the goods is to take place at a future time or subject to some conditions thereafter to be fulfilled, the contract is called an 'agreement to sell' [Sec. 4(3)].
- An agreement to, sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred[Sec. 4(4)].

Sale vs. Agreement to Sell

Basis	Sale	Agreement to Sell
Type of Contract	The contract is complete.	The contract is to be completed.
Transfer of Rights	The Buyer becomes the owner. (Jus in ram)	The buyer gets a 'jus in personam' i.e. (a right of buyer/seller against default).

Unit 02: The Sale of Goods Act, 1930

Transfer of Property	In case of Sale, the property is transferred immediately.	In case of Agreement to sell, the property is to be transferred in the future.
Transfer of Risk	The risk of danger or loss passes with property to the buyer.	Risk of loss or damage has to be borne by the seller.
Rights of seller if there is breach of contract by buyer	The Seller can sue the buyer for price even if goods are in possession of the seller.	Seller can sue the buyer for damages of breach of contract and not for recovery of goods.
Rights of buyer if there is breach of contract by seller	The Buyer can sue the seller for damages and sue the third party.	The Buyer can sue the seller for damages only.
Right of Resale	The Seller cannot resell the goods even if he has their possession.	The Seller can sell to another buyer, but the first buyer can sue the seller for damages.
Insolvency of Seller and its effects	The Buyer recover his goods from official receiver.	The Buyer can claim only a proportional amount, depending on the payment that he has made for the purchase of the goods.
Insolvency of buyer and its effects	He can get the delivery of the goods through his legal representative.	The Seller can refuse to sell the goods until the entire price has been paid, by the buyer.

2.5 Condition and its types**What is Condition?**

A condition is a stipulation(Prerequisite) essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated.

- Sec. 12(2)

In addition the aggrieved party may claim for damages for loss suffered.



Task

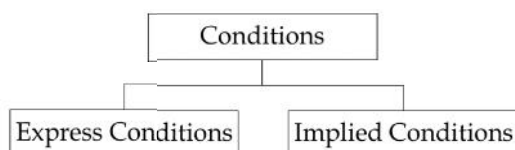
Parrot goes to the horse dealer and says "I want a horse which can run at a speed of 30 km/hr". The dealer points out a horse and says "It will suit you". After the sale, Parrot finds that the horse can run only at speed of 20 km/hr.

Point of Discussion

Will it be treated Condition?

Types of Conditions

Conditions are categorized as Express conditions and Implied conditions.

**Express Conditions**

Express conditions are the ones which are expressly mentioned in the contract. They are generally denoted by language such as 'if', 'on condition that', 'provided that', 'subject to', and 'In the event

Legal Aspects of Business

of'. In case of any dispute between the seller and the buyer, the court generally decide whether an agreement makes an event as a condition by the process of interpretation.

Implied Conditions

If an agreement does not make an event as a condition, then the court may supply a term that does so. Such conditions are referred to as 'implied' conditions. Implied conditions are those which are implied by law or custom. These shall prevail in a contract of sale unless the parties agree to the contrary.

The following are the implied conditions:

1. Condition as to title [Sec. 14(a)]
2. Condition as to description (Sec. 15)
3. Sale by sample (Sec. 17)
4. Sale by description as well as sample (Sec. 15)
5. Condition as to quality and fitness [Sec. 16(1)]
6. Condition as to merchantability [Sec. 16(2)]
7. Condition as to wholesomeness
8. Conditions implied by trade custom/usage

1. Condition as to title [Sec. 14(a)]

In a 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, in the case of a sale, he has a right to sell the goods and that, in the case of an agreement to sell, he will have a right to sell the goods at the time when the property is to pass.



CaseStudy

Rowland v/s Divall (1923)

Rowland bought a car from Divall and used it for four months. Divall had no title to the car. Consequently, Rowland had to hand it over to true owner. Rowland sued Divall and asked for repudiation of contract.

Point of Discussion

Could Rowland rescind the contract and get any amount from Divall?

[Hint: yes, Rowland could cancel the contract and recover the price from Divall on grounds of breach of condition as to title.]

2. Condition as to description (Sec. 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.

"Sale of Description" may include the following:

- Where the buyer has not seen the goods and relies on their description given by the seller.
- Where the buyer has seen the goods but he relies not on he has seen but what was stated to him. And deviation from the description is not apparent.
- Packing of goods may sometimes be part of the description



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.

3. Sale by sample (Sec. 17)

(1) 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.

(2) In the case of a contract for sale by sample there is an implied condition –

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- (a) that the bulk shall correspond with the sample in quality;
- (b) that the buyer shall have a reasonable opportunity of comparing the bulk with the sample;
- (c) that the goods shall be free from any defect, rendering them unmerchantable, which would not be apparent on reasonable examination of the sample.

*Case Study*

In a contract for sale of brandy by sample, brandy colored with a dye was supplied.

Point of Discussion

Is buyer bound by contract of sale?

[Hint: No, the buyer was not bound to the contract even though the goods supplied were equal to sample, as the defects were not apparent on reasonable examination of sample.]

4. Sale by description as well as sample (Sec. 15)

Sec. 15 further provides that if the sale is by sample as well as by description, it is not sufficient that the bulk of the goods corresponds with the sample, if the goods do not also correspond with the description.

This implied condition signifies:

- The goods must correspond with sample in quality.
- The buyer shall have a reasonable opportunity of comparing the bulk with the sample.
- The goods shall be free from any hidden defect (latent defect).

*Case Study***Wallis v. Pratt, (1911)**

In a contract for the sale of a quantity of seed described as “Common English Sainfoin”, the seed supplied was of a different kind, though the difference was not discoverable except by sowing. The defect also existed in the sample.

Point of Discussion

Can buyer claim any damages from seller?

[Hint: Yes, the buyer was entitled to recover damages for the breach of condition.]

5. Condition as to quality and fitness [Sec. 16(1)]

Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the 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, there is an implied condition that the goods shall be reasonably fit for such purpose.

But, an implied condition is deemed to exist on the part of the seller that the goods supplied shall be reasonably fit for the purpose for which buyer wants them, if the following conditions are satisfied:

- Where goods are ordered for specific purpose and the same is made known to seller.
- Where buyer buys under a trade name, nothing is implied unless told to seller.



Task: Bittu went to Sattu, a chemist and demanded a hot water bottle from him, Sattu gave a bottle to him telling that it was meant for hot water, but not boiling water. After few days while using the bottle, Bittu'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. Bittu filed a case against Sattu for breach of condition as to quality and fitness. Will Sattu succeed?

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Caution: Seller is not responsible if:

- If goods have number of purposes, the buyer must tell the purpose for which he requires the good otherwise seller is not responsible
- Where the buyer has an abnormality (unknown to the seller)



Example: An order was placed for some lorries to be used “for heavy traffic in a hilly area”. The Lorries supplied were unfit and breakdown. This is a breach of condition as to fitness.

**Case Study****Baldry v. Marshall (1925)**

Baldry told to Marshall, a motor car dealer, that he wanted a comfortable car suitable for touring purposes. Marshall recommended a “Bugatti car” and Baldry thereupon bought one. The car was uncomfortable and unsuitable for touring purposes. Baldry filed a case and asked for repudiation of contract (return the car)?

Point of Discussion

Could Baldry win the case?

[Hint: Yes, Baldry could reject the car and recover the price, and the mere fact that Baldry bought the car under its trade name did not necessarily exclude the condition of fitness.]

**Case****Griffiths v. Peter Company Ltd. (1939)**

Griffiths purchased a coat which caused her inflammation of the skin due to her unusually sensitive skin.

Point of Discussion

Is seller liable?

[Hint: No, the seller was not liable, the cloth being fit for any one with a normal skin.]

6. Condition as to merchantability [Sec. 16(2)]

- Merchantable means that the goods must be fit for the ordinary purpose for which such goods are used.
- Merchantable quality means goods must be in saleable condition.
- Where goods are bought by description from a seller who deals in goods of that description, there is implied condition that the goods must be of merchantable quality.

The condition of merchantability is applicable when,

- The goods are sold by description
- The seller deals with such goods

**Example**

Mohan a blacksmith sells to Das his old car, no implied condition as to merchantability applies.

**Case Study****R.S. Thakur Vs H.G.E.Corp, A.I.R. (1971)**

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A radio set was sold to a layman. The set was defective. It did not work in spite of repairs.

Point of Discussion

Can the buyer claim the refund?

[Hint: Yes, the buyer could return the set and claim refund on account of breach of condition as to merchantability.]

*Case Study***Morelli V. Fitch & Gibbons**

Morelli asked for a bottle of stone's ginger wine at Fitch & Gibbons's shop, which was licensed for the sale of wines. While Morelli was using it, the bottle broke at the neck & injured his hand.

Point of Discussion

Can Morelli file a case against Fitch & Gibbons and claim damages?

[Hint: Yes, the sale was by description and Morelli was entitled to recover the damages as the bottle was not of merchantable quality.]

7. Condition as to wholesomeness

- It applies to contract of sale of eatables & provision (necessities).
- Goods shall be wholesome. It means the goods should be in a condition to consume.



Example: Carol bought bun containing stone, which broke Carol's teeth. So she can repudiate the contract and claim damages.

*Case Study***Frost v. Aylesbury Dairy Co Ltd. (1905)**

F bought milk from A. The milk contained germs of typhoid fever. F's wife took the milk and got infection as a result of which she died. F filed case against A and asked for damages.

Point of Discussion

Can F win the law suit and claim damages from A?

[Hint: Yes, F could recover damages as there was breach of condition as to wholesomeness by A.]

8. Conditions implied by trade custom/usage

There is an implied condition as to the quality or fitness for the particular purpose may be annexed by the usage of trade/custom.

*Case Study***Priest V. Last (1903)**

Priest asked for a hot water bottle of Last, a retail chemist. He was supplied one which burst after a few days use and injured Priest's wife. Priest filed a case against Last for selling him such product.

Point of Discussion

Will Priest succeed?

[Hint: Yes, Last was liable for breach of implied condition because Priest had sufficiently made known the use for which he required the bottle.]

2.6 Warranty and its types

What is Warranty?

A warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated.

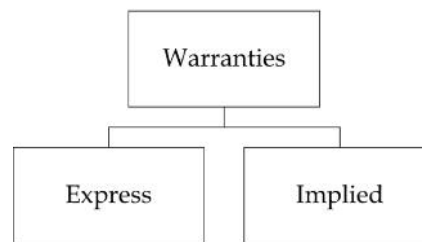
- Sec. 12(3)



Caution: Whether a stipulation in a contract of sale is a condition or a warranty depends in each case on the construction of the contract. A stipulation may be a condition, though called a warranty in the contract [Sec. 12(4)].

Types of Warranties

Warranties are categorized as express and implied warranties.



Express Warranties

Express warranties are those warranties which are expressly provided in the contract.

Implied Warranties

Implied warranties (contained in Secs. 14 to 17) are those which the law implies into the contract unless the parties stipulate to the contrary. Sec. 16(4) further provides that an express warranty or condition does not negative a warranty or condition implied by this Act unless inconsistent therewith. The following are the implied warranties.

1. Warranty of Quiet Possession [Sec. 14 (b)]
2. Warranty of freedom from encumbrances [Sec. 14 (c)]
3. Warranty as to quality or fitness by usage of trade [Sec. 16 (4)]
4. Warranty to disclose dangerous nature of goods

1. Warranty of Quiet Possession [Sec. 14 (b)]

In a contract of sale, unless the circumstances of the contract are such as to show a different intention, there is an implied warranty that the buyer shall have and enjoy quiet possession of the goods.

2. Warranty of freedom from encumbrances [Sec. 14 (c)]

In a contract of sale, unless the circumstances of the contract are such as to show a different intention, there is an implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.



Case Study

Arun, the owner of the watch, pledges it with Bharat. After a week, Arun obtains possession of the watch from Bharat for some implied purpose and sells it to Parul. Bharat approaches to Parul and tell him about the pledge. Parul has to make payment of pledge amount to Bharat.

Point of Discussion

Is Parul entitled to claim compensation from Arun??

[Hint: Yes, as there is breach of warranty of freedom from encumbrances.]

3. Warranty as to quality or fitness by usage of trade [Sec. 16 (4)]

An implied warranty as to quality or fitness for a particular purpose may be annexed by the usage of trade.

4. Warranty to disclose dangerous nature of goods

When a person sells goods, knowing that the goods are inherently dangerous or they are likely to be dangerous to the buyer and that the buyer is ignorant of the danger, he must warn the buyer of the probable danger, otherwise he will be liable for damages.

*Case Study***Clarke v. Army & Navy Co-operative Society Ltd. (1963)**

A sold a 'tin of disinfectant powder to C. He knew that it was likely to be dangerous to C if it was opened without special care being taken. C opened the tin where upon the disinfectant powder flew into her eyes, causing injury.

Point of Discussion

Could C get any claim from A?

[Hint: Yes, A was liable to pay damages to C as he failed to warn C of the probable danger of the goods sold by him.]

When Condition to be Treated as Warranty (Sec. 13)**(1) Voluntary Waiver of Condition**

Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty and not as a ground for treating the contract as repudiated.

(2) Acceptance of Goods by Buyer

Where a contract of sale is not severable and the buyer has accepted the goods or part thereof, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of the contract, express or implied, to that effect.

(3) Nothing in this section shall affect the case of any condition or warranty fulfilment of which is excused by law by reason of impossibility or otherwise.

2.7 Distinction between condition and Warranty

Basis	Condition	Warranty
Difference as to value	Essential to the main purpose of the contract	Collateral to the main purpose of the contract
Difference as to breach	Aggrieved party can repudiate the contract	Can claim damages only
Difference as to treatment	Breach of condition may be treated as a breach of warranty	Breach of warranty cannot be treated as a breach of condition

2.8 Doctrine of Caveat Emptor

This means 'let the buyer beware', i.e., in a contract of sale of goods the seller is under no duty to reveal unflattering truths about the goods sold. Therefore, when a person buys some goods, he must examine them thoroughly. If the goods turn out to be defective or do not suit his purpose or if he depends upon his own skill or judgment and makes a bad selection, he cannot blame anybody excepting himself.

**Case Study**

There was a sale by sample by a woolen manufacturer of cloth to merchant, who was also a tailor. The cloth was required for making liveries. But the fact was not made known to the seller. On account of the latent defect in the cloth, liveries could not be made out of it. But there was nothing to show that it was unfit for other purposes.

Point of Discussion

Could buyer cancel the contract or claim any damages from seller?

[Hint: No, It was held that the buyer was without any remedy due to non-communication of the purpose for which the cloth was required]

Exceptions to the Doctrine of Caveat Emptor**Fitness for Buyer's Purpose**

Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the 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 he is the manufacturer or producer or not), there is an implied condition that the goods shall be reasonably fit for such purpose. If the goods are not fit for the communicated purpose, the seller will be liable.

Merchantable Quality

Where goods are bought by description from a seller who deals in goods of that description (whether he is the manufacturer or producer or not), there is an implied condition that the goods shall be of merchantable quality. However, if the buyer has examined the goods, there shall be no implied condition as regards defects which such examination ought to have revealed. In such a situation, the doctrine will apply and protect the interest of the seller.

Usage of Trade

In the case of a contract for the sale of a specified article where the trade usage attaches an implied condition or warranty as to quality or fitness and the seller deviates from that.

Consent by fraud

Where the seller makes a false statement intentionally to the buyer amounting to fraud and the buyer relies on the statement or where the seller knowingly conceals the defect in the goods.

Misrepresentation by seller

In a case where the seller makes a misrepresentation and the buyer relies on it, the rule of Caveat emptor will not be applicable. Such a contract is voidable at the option of the buyer and he has a right to rescind the contract.

Purchase by sample and description

Where goods are bought by sample as well as by description and the bulk of goods do not correspond with the sample or with the description. In such a situation the buyer is entitled to reject the goods.

Purchase by description

Where goods are bought by description from a seller there is an implied condition that the goods shall correspond with the description; the breach of this condition entitles the buyer to reject the goods.

Sale by sample

If the bulk does not correspond with the sample, or if the buyer is not given an opportunity to compare bulk with the sample and goods have some latent or hidden defects then the rule of Caveat emptor is not applicable.

2.9 Unpaid Seller and his rights

A contract is comprised of reciprocal promises. In a contract of sale, if seller is under an obligation to deliver goods, buyer has to pay for it. In case buyer fails or refuses to pay, the seller, as unpaid seller, shall have certain rights.

Who is an unpaid seller?

According to sec. 45 of sale of goods act, a seller is unpaid when:

- Whole of the price has not been tendered or paid, or
- A Bill of exchange or negotiable instrument has been received as a conditional payment and the condition on which it was received has not been fulfilled by reason of the dishonor of the instrument or otherwise.

Rights of an unpaid seller

An unpaid seller can exercise his rights against the:

- Goods
- Buyer

An unpaid seller can exercise the following rights against the goods:

- Where the property in the goods has passed [Sec.46(1)]
 - ✓ Lien (Secs. 47 to 49)
 - ✓ Stoppage in transit (Sec.50 to 52)
 - ✓ Resale (Sec.54)
- Where the property in the goods has not passed {Sec.46(2)}
 - ✓ Withholding delivery
 - ✓ Stoppage in transit

An unpaid seller can exercise the following rights against the buyers:

- Suit for price (Sec. 55)
- Suit for damages (Sec.56)
- Repudiation of Contract(Sec.60)
- Suit for Interest (Sec.61)

Rights Against the Goods

1. Right of Lien [Sec 46(1), 47 to 49]

Right to retain possession of the goods and refuse to deliver them to the buyer until the price due in respect of them is paid or tendered.

It is available to the unpaid seller who is in possession of them where:

- The goods have been sold without any stipulation to credit.
- The goods have been sold on credit, but the term of the credit has expired.
- The buyer becomes insolvent, even though the period of credit has not yet expired.

Rules Regarding Lien

- It can be exercised only when the property in goods has been transferred to the buyer.
- When the seller has not lost with the possession.
- It is always possessory in nature. It depends on actual possession not title.
- It must not expressly waived off by seller expressively in the agreement.
- It can be used only for recovering price NOT for any other charges.

Legal Aspects of Business

- It is an indivisible right means When unpaid seller has made part delivery of goods, he may exercise right of lien on the remainder.
- It is personal right by nature. It can be exercised by seller only.
- The unpaid seller cannot exercise the right of lien even if he is in possession of goods as bailee or agent.
- The credit period suspends right of lien not destroys it.

Termination of Lien

- When the buyer lawfully obtains the possession of the goods.
- When seller expressly or impliedly waives his right of lien.
- When he delivers the goods to a carrier for the purpose of transmission to the buyer.



Case Study

A seller wants to recover dock dues from the buyer. Thus he wants to exercise right of lien against the goods, the property of whose the seller has transferred to buyer for such recovery.

Point of Discussion

Can seller exercise right of lien for recovering such charges?

[Hint: No, as the right of lien can be exercised for recovering only price.

Defeat of Right of lien

The right of lien is not affected by any sale or pledge by the buyer.

This right is defeated, if the buyer has transferred the document of title of goods to the third person and the third person took it in good faith. -Sec. 53

2. Right of stoppage in Transit (Sec. 50-52)

When the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit, and may retain them until payment or tender of the price (Sec. 50).

Available when:

- The seller should be an unpaid seller as defined in section 45.
- The buyer should be insolvent.
- The goods should be in transit.
- The buyer must not have acquired the possession.
- The seller must have lost the possession.
- The property in goods must have transferred to buyer.

Duration of Transit

Carrier may hold goods -

- As seller's Agent (Seller has lien on goods)
- As Buyer's Agent (Goods are in buyers possession)
- In his own name. It means that the carrier has the possession of the goods in his independent capacity as carrier.

Termination of Stoppage in transit

- When the buyer/agent takes delivery [Sec. 51(1)],
- When the carrier or the other bailee acknowledges to the buyer that he holds the goods on his behalf [Sec. 51(3)],

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- When the carrier wrongfully refuses to deliver the goods to the buyer [Sec. 51(6)],
- When part delivery of goods made to the buyer/agent [Sec. 51(7)].

Did you know? **Difference between Lien Vs. Stoppage in Transit**

- Activation of Right
- Possession of goods
- End/start to right
- Purpose of right



Case Study

Rita agrees to sell 100 pieces of computers with Mohit. Mohit promises to pay the price when Rita will dispatch the goods. Rita made a contract with Nagina transporters to deliver the goods and dispatch the goods. Afterwards, when goods were in transit, Mohit became insolvent.

Point of Discussion

What are the remedies available to Rita under the sale of goods act?

[Hint: Stoppage in transit is available.]

3. Right of Re-sale [Sec 54(2)]

The unpaid seller may re-sell them under any of the following circumstances:

- Where goods are of perishable nature;
- Where the seller gives notice to the buyer of his intention to resell and the buyer does not pay within a reasonable time after notice;
- Where the seller has expressly reserved his right of re-sale in case the buyer should make default.

Where the Property in goods has not passed

Where the property in goods has not passed to the buyer, the unpaid seller has, in addition to his other remedies, a right of withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer [Sec. 46(2)].

- **Right of Withholding Delivery [Sec. 46(2)]**

When property in goods has not passed to the buyer, unpaid seller has a right of withholding delivery with the right of lien and stoppage in transit.

Rights Against the Buyer Personally

1. Suit for price
2. Suit for damages for non-acceptance
3. Repudiation of contract before due date of delivery by buyer
4. Suit for special damages and interest

1. Suit for price(Sec. 55)

Where the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay the price, the seller can sue the buyer for the price of the goods.

Where the property in goods has not passed to the buyer, as a rule, the seller cannot file a suit for the price; his only remedy is to claim damages.



Example: Apple sold certain goods to Banana for 5,000 and the price was agreed to be paid before the expiry of ten days of the contract. Banana fails to pay the price within the stipulated time. Apple can file a suit for price against Banana even though the goods have not been delivered or the property in goods has not been passed to Banana.

Legal Aspects of Business**2. Suit for damages for non-acceptance (Sec. 56)**

Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance.

3. Repudiation of contract before due date of delivery by buyer (Sec. 60)

Where the buyer repudiates the contract before the date of delivery, the seller may either –

- a) treat the contract as subsisting and wait till the date of delivery, or
- b) seller may treat the contract as rescinded and sue for damages for the breach.

4. Suit for special damages and interest (Sec. 61)

- In case of specific agreement -- the seller may recover interest from the buyer.
- In absence of specific agreement – the seller may charge interest on the price when it becomes due from such day as he may notify to buyer.

Summary

- A contract of sale is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. Sale is to be distinguished from an agreement to sell.
- Where under a contract of sale, the property in goods is transferred from the seller to the buyer, it is called a sale.
- An agreement to sell means a contract of sale under which the transfer of property in goods is to take place at a future date or subject to conditions thereafter to be fulfilled.
- Goods may be classified as existing, future and contingent. In contract of sale, parties make certain stipulations.
- All stipulations are not treated on the same footing. These stipulations are technically known as conditions and warranties.
- These conditions and warranties may be express or implied. Thus, sale takes place when there is a transfer of ownership in goods from the seller to the buyer.
- A sale is an executed contract.
- The term seller includes any person who is in the position of a seller, e.g., an agent of the seller, to whom a bill of lading has been endorsed, or a consignee or agent who has paid for the goods or is responsible for the price (s.45).
- The word lien means to retain possession of.
- No gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment.
- Unpaid seller" defined as:
 - (1) The seller of goods is deemed to be an "unpaid seller" within the meaning of this Act –
 - (a) when the whole of the price has not been paid or tendered.
 - (b) when a bill of exchange or other negotiable instrument has been received as conditional payment, and the condition on which it was received has not been fulfilled by reason of the dishonour of the instrument or otherwise.
- Subject to the provisions of this Act and of any law for the time being in force, notwithstanding that the property in the goods may have passed to the buyer, the unpaid seller of goods, as such, has by implication of law –
 - (a) a lien on the goods for the price while he is in possession of them.

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(b) in case of the insolvency of the buyer a right of stopping the goods in transit after he has parted with the possession of them.

(c) a right of re-sale as limited by this Act.

- Where the property in goods has not passed to the buyer, the unpaid seller has, in addition to his other remedies, a right of withholding delivery like and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer.

Keywords

Buyer: "Buyer" means a person who buys or agrees to buy goods.

Condition: A condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated.

Contract of sale: 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.

Delivery: It is defined as a voluntary transfer of possession from one person to another.

Future goods: "Future goods" means goods to be manufactured or produced or acquired by the seller after the making of the contract of sale.

Goods: Goods mean every kind of movable property other than actionable claims and money.

Implied conditions and warranties: These are deemed to be incorporated by law in every contract of sale of goods unless the terms of the contract show a contrary intention.

Lien: It means to retain possession.

Seller: "Seller" means a person who sells or agrees to sell goods. Seller includes any person who is in the position of a seller, as, for instance, an agent of the seller to whom the bill of lading has been endorsed, or a consignor or agent who has himself paid, or is directly responsible for, the price.

Specific goods: "Specific goods" means goods identified and agreed upon at the time a contract of sale is made.

Unpaid seller: A person who is in possession of goods is entitled to retain them in his possession until payment.

Warranty: A warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated.

Self-Assessment

1. Mannu is entering into one contract to sell 500 bales of cotton to Rohit at 500 per bale. Mannu put a term to deliver the bales only when Rohit will pay him 60% of contract amount in advance. What is the nature of contract of between Mannu and Rohit?

- Contract
- Contract of Sale
- Contract of an agreement to sell
- Actual Sale

2. Price of Sale of Goods should be

- Fixed by the contract itself
- Agreed to be fixed in a manner provided by contract
- Determined by the course of dealing between parties
- Any of above

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3. Surinder owns 40 i20 Asta Cars of white color. Kush enters into a contract with Surinder to buy one car out of those 40 cars. After the contract one car is given to Kush. This is a case of selling of which of the following goods?
 - A. Specific Goods
 - B. Ascertained Goods
 - C. Unascertained Goods
 - D. Future Goods

4. Ritik agrees to sell to Karina, the entire crop of potatoes to be grown at his farm in Uttar Pradesh for an amount of 5,00,000. Identify the types of goods involved in the contract between Ritik and Karina.
 - A. Specific Goods
 - B. Ascertained Goods
 - C. Unascertained Goods
 - D. Future Goods

5. Keshav sells his car to Vivek for 7,00,000 in consideration of a gold necklace worth 4,00,000 and cash worth 3,00,000. Is it a valid contract of sale?
 - A. No, as the whole consideration in contract is not in money
 - B. Yes, as the consideration is partly for goods and partly for money
 - C. No, as the consideration is partly for goods and partly for money
 - D. None of above

6. Pear goes to the horse dealer and says "I want a horse which can run at a speed of 50 km/hr". The dealer points out a horse and says "It will suit your purpose". After the sale, Pear finds that the horse can run only at speed of 20 km/hr. Which of the following remedies the pear has against seller in such case and why?
 - A. Pear can repudiate the contract due to breach of condition
 - B. Pear can only claim damages due to breach of condition
 - C. Pear can repudiate the contract and claim damages (if any) due to breach of condition
 - D. Pear can neither repudiate the contract nor claim damages

7. Ritu bought a car from Divya and used it for six months. Divya had sold the theft car to Ritu. Consequently, Ritu had to hand it over to true owner. In such a case, Ritu can legally ask for repudiation of contract and recover her price back from Divya on account of breach of:
 - A. An implied condition as to title
 - B. An implied condition as to sale by description
 - C. An implied condition as to sale by sample
 - D. An implied condition as to wholesomeness

8. Mohit sold to Luv 300 tins of Australian Orange by describing that they will be packed in containers containing 30 tins each. Mohit delivered a substantial portion in containers containing 24 tins in each. In such a case, Luv can reject the goods on account of breach of which of the following implied condition?
 - A. An implied condition as to title
 - B. An implied condition as to sale by description
 - C. An implied condition as to sale by sample

- D. An implied condition as to wholesomeness
9. Nitin agreed to sell to Ginni 5 tins of oil described as "refined olive oil, warranted only equal to sample". The goods delivered were equal to sample, but contained an admixture of palm oil. Can Ginni reject the goods and why?
- A. No, Ginni cannot reject the goods
 - B. Yes, Ginni can reject the goods due to breach of an implied condition as to sale by description
 - C. Yes, Ginni can reject the goods due to breach of an implied condition as to sale by sample
 - D. Yes, Ginni can reject the goods due to breach of an implied condition as to sale by description as well as sample
10. Vishal bought Pizza, Pizza has one stone in itself, which broke Vishal's teeth. Can Vishal repudiate the contract and claim damages from the seller of Pizza?
- A. Yes, on account of breach of an implied condition as to sale by description
 - B. Yes, on account of breach of an implied condition as to sale by sale
 - C. Yes, on account of breach of an implied condition as to wholesomeness
 - D. Yes, on account of breach of an implied condition as to title
11. In case of breach of warranty by the seller, the buyer can:
- A. Claim for damages
 - B. Repudiate the contract
 - C. Return goods
 - D. Refuse to pay the price
12. In the Contract of Sale, the following warranty/warranties are impliedly applicable:
- A. Seller has a right to sell the goods
 - B. The buyer does not have any right to enjoy the quiet possession of goods
 - C. The goods shall be unfree from any charge or encumbrance
 - D. The buyer has the right to have and enjoy the quiet possession of goods and that the goods shall be free from any charge or encumbrance
13. Krishna contracts to sell Bheem a piece of silk. Bheem thinks that it is a piece of Indian silk. Krishna knows that Bheem thinks so and further knows that it is not Indian silk. Krishna does not correct Bheem's impression. Bheem afterward discovers that it is not an Indian silk. Which of the following, Bheem can do in such situation and reason of the same?
- A. Bheem can rescind the contract due to breach of implied condition by seller
 - B. Bheem can rescind the contract due to breach of implied warranty by seller
 - C. Bheem cannot rescind the contract due to doctrine of caveat emptor
 - D. Bheem can claim damages due to breach of implied warranty by seller
14. Amit, the owner of the bike, pledges it with Bhushan. After a week, Amit obtains possession of the bike from Bhushan on account some emergency and sells it to Piyush. Bhushan approaches to Piyush and tell him about the pledge. Piyush has to make payment of pledge amount to Bhushan. Which of the following remedy, the Piyush has against Amit and why?
- A. Piyush can repudiate the contract due to breach of implied condition as to title
 - B. Piyush can repudiate the contract due to breach of implied warranty against encumbrances
 - C. Piyush can claim damages due to breach of implied condition as to title
 - D. Piyush can claim damages due to breach of implied warranty against encumbrances

15. Doctrine of Caveat Emptor applies when:

- A. Buyer discloses the purpose of his purchase to seller
- B. Buyer relies on his judgement
- C. Buyer does not disclose the purpose of purchase to seller and relies on his judgement
- D. Buyer discloses the purpose of purchase to seller and relies on seller's judgement

16. "The lien of an unpaid seller" depends upon?

- A. Possession
- B. Title
- C. Ownership
- D. Whether the buyer has paid the price or not

17. Which of the following is true about Right of stoppage in transit?

- A. The seller should be an unpaid seller as defined in section 45.
- B. The buyer should be insolvent.
- C. The goods should be in transit.
- D. All of the above

18. An unpaid seller can exercise Right of lien for recovering the price of goods only NOT other charges.

- A. True
- B. False

19. Apple sells 100 bales of Jute to Blueberry and sends 50 bales by motor and 50 bales by railway. Blueberry receives delivery of the bales sent by motor, but before Blueberry receives the delivery of the bales sent by railway, he becomes insolvent. Which of the following right Apple, the unpaid seller can exercise in such situations?

- A. Right of Lien
- B. Right of Stoppage in Transit
- C. Right to Re-sale
- D. All of above

20. What is the Right of lien by the unpaid seller as per sale of goods act?

- A. Retain possession
- B. Regain possession
- C. Recover price and damages
- D. Recover damages

Answers for Self Assessment

1. C	2. D	3. B	4. D	5. B
6. C	7. A	8. B	9. D	10. C

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11. A	12. D	13. C	14. D	15. C
16. A	17. D	18. A	19. B	20. A

Review Questions

1. Define contract of sales of goods. State the essentials of a contract of sale under the Sale of Goods Act, 1930.
2. What is meant by goods? Illustrate the types of goods.
3. Define an unpaid seller. Explain the different rights of an unpaid seller against the goods?
4. Illustrate the different rights of an unpaid seller against the buyer.
5. When can a seller resell the goods?
6. Distinguish between the right of lien and stoppage in transit.
7. State the circumstances when the right of stoppage in transit ends.
8. Distinguish between condition and warranty.
9. What do you understand by express conditions and implied conditions? Discuss in detail with suitable examples.
10. What do you understand by express warranty and implied warranty? Discuss in detail with suitable examples.
11. When a breach of condition is treated as breach of warranty?
12. Parrot changes with Sparrow 100 rupee note with coins for hundred rupees. Is this transaction a sale?
13. Piyush changes 32 Bullocks for the entire crop of wheat harvested from Simran's land. Does the transaction amount to sale?
14. Rama bought a refrigerator from ABC enterprise for a sum of rupees 12000. The refrigerator was defective right from the beginning and it did not work in spite of repair by expert mechanics. Rama wants to return the refrigerator to ABC Enterprises and claim a refund. Will Rama succeed? Explain.
15. Manu purchases some chocolates from a shop. One of the chocolates contains a poisonous matter and as a result Manu's wife who has eaten it falls seriously ill. What remedy is available to Manu against the shopkeeper? [Hint: The chocolates are not of merchantable quality and hence A can repudiate the contract and recover damages.]
16. A piece of cotton cloth with some manufacturing faults equal to sample was sold to a tailor who could not stitch it into coats owing to some defect in its texture. The tailor had examined the cloth before effecting the purchase. Is the tailor entitled to damages? [Hint: Yes, due to latent defect.]
17. Moore sold to Landauver 300 tins of Australian Apple by describing that they will be packed in containers containing 30 tins each. Moore delivered a substantial portion in containers containing 24 tins in each. Is it a Breach of condition? State reasons.
18. In an auction sale of a set of napkins and table cloths, these were described as dating from the seventh century. The buyer bought the set after seeing it. Subsequently he found the set to be an eighteenth century set. Could he reject the set? State reasons.
19. Nichol agreed to sell to Godts some oil described as "foreign refined rape oil, warranted only equal to sample". The goods tendered were equal to sample, but contained an admixture of hemp oil. Could Godts reject the goods? State reasons.
20. The buyer ordered for the best quality of 'toor dal'. The dal was loaded in rain and by the time it reached the destination, it became damaged by moisture. The buyer filed a case against seller and ask for repudiation of contract and recover his funds. Will buyer succeed? State reasons.
21. If Pearl says to Rahul that I want a good horse. Rahul shows him a horse and says, " This is a good horse and it can run at a speed of 30 kilometers per hour" and Pearl buys the horse and finds later on that it can run at a speed of 20 kilometers per hour only. Is it the case of breach of condition and warranty? State reasons

Legal Aspects of Business

22. Ashwani (Buyer) of Delhi order Bahubali (Seller) of Mumbai to deliver certain goods to him at Delhi. Bahubali supplies the goods, but Ashwani delays to take the delivery. The station master at Delhi informs Ashwani that the goods are lying at the station at Ashwani's risk. Before taking the delivery, Ashwani becomes insolvent. Can Bahubali recover the goods by stopping them in transit? Explain.

23. What do you understand by unpaid seller's "Right of Lien"? When an unpaid seller's lien is lost?

24. How can an unpaid seller exercise his right for stopping the goods in transit? Discuss in detail.

25. Akash of Delhi orders Binny of Chennai, to deliver certain goods to him at Delhi. While the goods are lying at Delhi Railway Station, the station master informs Akash that the goods are held at the station at Akash's risk. But Akash has become insolvent. Has Binny any right over the goods as an unpaid seller? Justify.

26. Explain the Doctrine of Caveat Emptor. Discuss the exceptions of Doctrine of Caveat Emptor in detail.

**Further Reading**

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**Web Links**

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Unit 03: The Consumer Protection Act, 2019

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Objectives

After studying this unit, you will be able to:

- explain the features and objectives of the Consumer Protection Act, 2019.
- illustrate the meaning and use of various terminologies used in the Consumer Protection Act, 2019.
- explain the various consumers rights provided under the Consumer Protection Act, 2019.
- illustrate the procedure to get redressal from various Consumer Disputes Redressal Commissions and Councils.
- appraise the importance of forming Central Consumer Protection Authority (CCPA).
- review the role of the Consumer Protection Act, 2019 in protecting the consumers in current digital world.

Introduction

The origin of the principle "Consumer is King" lies in the fact that in today's mass production and digital economy where there is little direct or face to face contact between the producer and consumer, often sellers make exaggerated claims and advertisements, which they do not intend to fulfill. This leaves the consumer in a difficult position with very few avenues for redressal.

The onset on intense competition also made producers aware of the benefits of customer satisfaction and hence by and large, the principle of "Consumers are the kings and hence they always need to be served the best." is now accepted.

The need to recognize and enforce the rights of consumers is being well understood and several laws have been made for this purpose. In India, we have the Indian Contract Act, the Sale of Goods Act, the Dangerous Drugs Act, the Agricultural Produce (Grading and Marketing) Act, the Indian Standards Institution (Certification Marks) Act, the Prevention of Food Adulteration Act, the Standards of Weights and Measures Act, the Trade and Merchandise Marks Act, etc. which to some extent protect consumer interests.

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However, these laws required the consumer to initiate action by way of a civil suit, which involved lengthy legal process proving, to be too expensive and time consuming for lay consumers.

Therefore, the need for a simpler and quicker access to redressal to consumer grievances was felt and accordingly, it led to the legislation of the Consumer Protection Act, 1986. The main objective of this Act is to provide better protection to the consumers. The Act intends to provide simple, speedy and inexpensive redressal to the consumers' grievances.

The Parliament of India has repealed the three-decade old Consumer Protection Act, 1986, and replaced it with the new Consumer Protection Act, 2019, w.e.f 20.07.2020. The Government has broadened the horizon of the Act and has given holistic and all-encompassing definitions of consumer, consumer rights (which also include right to consumer awareness), e-commerce, endorsement, product liability, unfair contract, misleading advertisement, inserted 'telecom' in the definition of "service", provided for establishment of Central Consumer Protection Authority with the power of search & seizure and issue directions and penalties against false or misleading advertisements. The new law provides for stringent provisions including rigorous punishment & penalties in tune with the current digital world.

3.1 Consumer Protection Act, 2019: Introduction, Objects and Features

Consumer Protection Act, 2019: Introduction

- This Act may be called the Consumer Protection Act, 2019.
- The Act applies to all goods and services.
- The 2019 Act has been enacted for the purpose of providing timely and effective administration and settlement of consumer disputes and related matters.

Consumer Protection Act, 2019: Objects

- To provide enhanced protection to the consumers taking into consideration the booming e-commerce industry, and
- The modern methods of providing goods and services such as online sales, teleshopping, direct selling and multi-level marketing in addition to the traditional methods.
- To make significant changes and provide greater consumer protection in comparison to the previous 1986 Act.

Consumer Protection Act, 2019: Salient features

1. The 2019 Act expands the scope of the definition of Consumer.
2. The 2019 Act has also widened the definition of Unfair Trade Practices as compared to the 1986 Act which now includes within its ambit:
 - a) online misleading advertisements;
 - b) the practice of not issuing a bill/memo for the goods and services;
 - c) failing to take back defective goods or deactivate defective services and refund the amount within the stipulated time mentioned in the bill or memo or within 30 days in the absence of such stipulation; and
 - d) disclosing personal information of a consumer unless such disclosure is in accordance with law.
3. The 2019 Act has also introduced the concept of 'unfair contract' ---
 - a) such as contracts requiring manifestly excessive security deposits to be given by a consumer for the performance of contractual obligations;
 - b) imposing any penalty on the consumer for a breach of the contract, which is wholly disproportionate to the loss that occurred due to such breach to the other party to the contract;
 - c) refusing to accept early repayment of debts on payment of applicable penalty;

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- d) entitlement of a party to the contract to terminate such contract unilaterally without reasonable cause;
- e) permitting or has the effect of permitting one party to assign the contract to the detriment of the other party who is a consumer, without his consent; and
- f) imposing on the consumer any unreasonable charge, obligation or condition which puts such a consumer to any disadvantage.
- It would help to keep a check on businesses, including banks and e-commerce sites.
 - The proposal to establish a Central Consumer Protection Authority ("CCPA").

3.2 Consumer Protection Act, 2019: Definitions

1. Advertisement	13. Goods
2. Appropriate Laboratory	14. Harm
3. Complainant	15. Injury
4. Complaint	16. Manufacturer
5. Consumer	17. Misleading advertisement
6. Consumer dispute	18. Person
7. Defect	19. Product
8. Deficiency	20. Restrictive trade practice
9. Direct selling	21. Service
10. E-commerce	22. Unfair trade practice
11. Electronic service provider	23. Product Liability
12. Express Warranty	

1. Advertisement: Sec. 2(1)

Any audio or visual publicity, representation, endorsement or pronouncement made by means of light, sound, smoke, gas, print, electronic media, internet or website and includes any notice, circular, label, wrapper, invoice or such other documents.

2. Appropriate Laboratory: Sec. 2(2)

"appropriate laboratory" means a laboratory or an organization--

- (i) recognized by the Central Government; or
- (ii) recognized by a State Government, subject to such guidelines as may be issued by the Central Government in this behalf; or
- (iii) established by or under any law for the time being in force, which is maintained, financed or aided by the Central Government or a State Government for carrying out analysis or test of any goods with a view to determining whether such goods suffer from any defect.

3. Complainant: Sec. 2(5)

"Complainant" means--

- (i) a consumer; or
- (ii) any voluntary consumer association registered under any law for the time being in force; or
- (iii) the Central Government or any State Government; or
- (iv) the Central Authority; or
- (v) one or more consumers, where there are numerous consumers having the same interest; or
- (vi) in case of death of a consumer, his legal heir or legal representative; or
- (vii) in case of a consumer being a minor, his parent or legal guardian.



Did you know? **Who cannot be complainant?**

A person who obtains;

- goods free of charge
- who avails services free of charge
- who obtains goods for resale or for any commercial purposes
- who avails services for any commercial purposes
- who avails services under contract of service

4. Complaint: Sec. 2(6)

"Complaint" means any allegation in writing, made by a complainant for obtaining any relief provided by or under this Act, that--

- (i) an unfair contract or unfair trade practice or a restrictive trade practice has been adopted by any trader or service provider;
- (ii) the goods bought by him or agreed to be bought by him suffer from one or more defects;
- (iii) the services hired or availed of or agreed to be hired or availed of by him suffer from any deficiency;
- (iv) a trader or a service provider, as the case may be, has charged for the goods or for the services mentioned in the complaint, a price in excess of the price--
 - (a) fixed by or under any law for the time being in force; or
 - (b) displayed on the goods or any package containing such goods; or
 - (c) displayed on the price list exhibited by him by or under any law for the time being in force; or
 - (d) agreed between the parties;
- (v) the goods, which are hazardous to life and safety when used, are being offered for sale to the public--
 - (a) in contravention of standards relating to safety of such goods as required to be complied with, by or under any law for the time being in force;
 - (b) where the trader knows that the goods so offered are unsafe to the public;
- (vi) the services which are hazardous or likely to be hazardous to life and safety of the public when used, are being offered by a person who provides any service and who knows it to be injurious to life and safety;
- (vii) a claim for product liability action lies against the product manufacturer, product seller or product service provider, as the case may be.

5. Consumer: Sec. 2(7)

Consumer is a person who:

(In context to goods)

- buys any goods for consideration and;
- includes any user of such goods and;
- does not include a person who obtains such goods for resale or for any commercial purpose.

(In context to services)

- hires or avails of any service for a consideration, and
- includes any beneficiary of such service,
- does not include a person who avails of such service for any commercial purpose.

6. Consumer dispute: Sec. 2(8)

"Consumer dispute " means a dispute where the person against whom a complaint has been made, denies or disputes the allegations contained in the complaint.

**Task**

Sant Ram admitted his only infant son in a private nursing home. As a result of strong dose of medicine administered by the nursing attendant, the child became mentally retarded. Sant Ram wants to make a complaint to the district forum seeking relief by way of compensation on the ground that there was deficiency in service by the nursing home. Does his complaint give rise to a consumer dispute? Who is the consumer in the instant case?

[Hint: Yes, this complaint gives rise to a consumer dispute. Sant Ram is a consumer who hires the services of the nursing home. Also the infant is a beneficiary and therefore he is also a consumer.]

7. Defect: Sec. 2(10)

It means any fault, imperfection or shortcoming in the quality, quantity, potency, purity or standard which is required to be maintained.

8. Deficiency: Sec. 2(11)

Deficiency means any fault, imperfection, shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service and includes--

- (i) any act of negligence or omission or commission by such person which causes loss or injury to the consumer; and
- (ii) deliberate withholding of relevant information by such person to the consumer.

9. Direct selling: Sec. 2(13)

It means marketing, distribution and sale of goods or provision of services through a network of sellers, other than through a permanent retail location.

10. E-commerce: Sec. 2(16)

It means buying or selling of goods or services including digital products over digital or electronic network.

11. Electronic service provider: Sec. 2(17)

It means a person who provides technologies or processes to enable a product seller to engage in advertising or selling goods or services to a consumer and includes any online market place or online auction sites.

12. Express warranty: Sec. 2(20)

It means any material statement, affirmation of fact, promise or description relating to a product or service warranting that it conforms to such material statement, affirmation, promise or description and includes any sample or model of a product warranting that the whole of such product conforms to such sample or model.

13. Goods: Sec. 2(21)

It means every kind of movable property and includes "food" as defined in clause (j) of sub-section (1) of section 3 of the Food Safety and Standards Act, 2006 (34 of 2006).

14. Harm: Sec. 2(22)

"harm", in relation to a product liability, includes--

- (i) damage to any property, other than the product itself;
- (ii) personal injury, illness or death;
- (iii) mental agony or emotional distress attendant to personal injury or illness or damage to property; or

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(iv) any loss of consortium or services or other loss resulting from a harm referred to in subclause (i) or sub-clause (ii) or sub-clause (iii), but shall not include any harm caused to a product itself or any damage to the property on account of breach of warranty conditions or any commercial or economic loss, including any direct, incidental or consequential loss relating thereto.

15. Injury: Sec. 2(23)

It means any harm whatever illegally caused to any person, in body, mind or property.

16. Manufacturer: Sec. 2(24)

"Manufacturer" means a person who--

- (i) makes any goods or parts thereof; or
- (ii) assembles any goods or parts thereof made by others; or
- (iii) puts or causes to be put his own mark on any goods made by any other person

17. Misleading advertisement: Sec. 2(28)

"Misleading advertisement" in relation to any product or service, means an advertisement, which--

- (i) falsely describes such product or service; or
- (ii) gives a false guarantee to, or is likely to mislead the consumers as to the nature, substance, quantity or quality of such product or service; or
- (iii) conveys an express or implied representation which, if made by the manufacturer or seller or service provider thereof, would constitute an unfair trade practice; or
- (iv) deliberately conceals important information.

18. Person: Sec. 2(31)

"Person" includes--

- (i) an individual;
- (ii) a firm whether registered or not;
- (iii) a Hindu undivided family;
- (iv) a co-operative society;
- (v) an association of persons whether registered under the Societies Registration Act, 1860 (21 of 1860) or not;
- (vi) any corporation, company or a body of individuals whether incorporated or not;
- (vii) any artificial juridical person, not falling within any of the preceding sub-clauses

19. Product: Sec. 2(33)

It means any article or goods or substance or raw material or any extended cycle of such product, which may be in gaseous, liquid, or solid state possessing intrinsic value which is capable of delivery either as wholly assembled or as a component part and is produced for introduction to trade or commerce, but does not include human tissues, blood, blood products and organs.

20. Restrictive trade practice: Sec. 2(41)

It means a trade practice which tends to bring about manipulation of price or its conditions of delivery or to affect flow of supplies in the market relating to goods or services in such a manner as to impose on the consumers unjustified costs or restrictions and shall include--

- (i) delay beyond the period agreed to by a trader in supply of such goods or in providing the services which has led or is likely to lead to rise in the price;
- (ii) any trade practice which requires a consumer to buy, hire or avail of any goods or, as the case may be, services as condition precedent for buying, hiring or availing of other goods or services.

21. Service: Sec. 2(42)

It means service of any description which is made available to potential users and includes, but not limited to, the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, telecom, boarding or lodging or both, housing

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construction, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service.

22. Unfair trade practice: Sec. 2(47)

"Unfair trade practice" means a trade practice which, for the purpose of promoting the sale, use or supply of any goods or for the provision of any service, adopts any unfair method or unfair or deceptive practice including any of the following practices, namely:--

(i) making any statement, whether orally or in writing or by visible representation including by means of electronic record, which--

(a) falsely represents that the goods are of a particular standard, quality, quantity, grade, composition, style or model;

(b) falsely represents that the services are of a particular standard, quality or grade;

(c) falsely represents any re-built, second-hand, renovated, reconditioned or old goods as new goods;

(d) represents that the goods or services have sponsorship, approval, performance, characteristics, accessories, uses or benefits which such goods or services do not have;

(e) represents that the seller or the supplier has a sponsorship or approval or affiliation which such seller or supplier does not have;

(f) makes a false or misleading representation concerning the need for, or the usefulness of, any goods or services;

(g) gives to the public any warranty or guarantee of the performance, efficacy or length of life of a product or of any goods that is not based on an adequate or proper test thereof:

Provided that where a defence is raised to the effect that such warranty or guarantee is based on adequate or proper test, the burden of proof of such defence shall lie on the person raising such defence;

(h) makes to the public a representation in a form that purports to be--

(A) a warranty or guarantee of a product or of any goods or services; or

(B) a promise to replace, maintain or repair an article or any part thereof or to repeat or continue a service until it has achieved a specified result, if such purported warranty or guarantee or promise is materially misleading or if there is no reasonable prospect that such warranty, guarantee or promise will be carried out;

(i) materially misleads the public concerning the price at which a product or like products or goods or services, have been or are, ordinarily sold or provided, and, for this purpose, a representation as to price shall be deemed to refer to the price at which the product or goods or services has or have been sold by sellers or provided by suppliers generally in the relevant market unless it is clearly specified to be the price at which the product has been sold or services have been provided by the person by whom or on whose behalf the representation is made;

(j) gives false or misleading facts disparaging the goods, services or trade of another person.

23. Product Liability: Sec. 2(34)

It means the responsibility of a product manufacturer or product seller, of any product or service, to compensate for any harm caused to a consumer by such defective product manufactured or sold or by deficiency in services relating thereto.

3.3 Rights of Consumer

The Consumer Protection Act, 2019 recognizes the following six rights of consumers under Sec. 2(9):

- 1) Right to safety
- 2) Right to information
- 3) Right to choose
- 4) Right to be heard
- 5) Right to seek redressal
- 6) Right to consumer education/ awareness

1. Right to Safety

The right to be protected against the marketing of goods, products or services which are hazardous to life and property. Appropriate Government bodies do ban products to be sold in Indian Market which are found hazardous in nature from time to time as to protect Indian consumers due to their right of being saved from such unhealthy and hazardous goods and services.



Example: **Maggi Ban in India (2015)**

The Delhi government on June 3, 2015 banned Swiss foods major Nestle Maggi noodles from its stores after it found lead and monosodium glutamate in the eatable beyond the permissible limit. The government announced a "15-day ban" on sale of Maggi noodles and has asked Nestle to recall current stocks from the market in that time and make new stock available, which will be allowed on shelves only after proper checks.

FSSAI found stapled tea bags hazardous, sought ban (2019)

The Food Safety and Standards Authority of India (FSSAI) issued a notification to the food business operators (FBOs) seeking a ban on the use of pins in tea bags which are been sold in wide range. A senior official said they have asked all the FBOs to use staple-less tea bags and discard all the staple pins tea bags by June 30.

2. Right to information

The right to be informed about the quality, quantity, potency, purity, standard, and price of goods, products, or services, as applicable, in order to protect the consumer from unfair trade practices, misleading advertising, and so on.



Examples: The companies are required to provide following information to the consumers of their products due to right of information:

- Nutrition Facts
- Date of Manufacturing and Expiry;
- Ingredients;
- Details about the manufacturing company an marketing company of the product;
- Clear demarcation about the use of non-vegetarian ingredient through red colored circle logo; and
- Date of import etc.

You can find all above and alike information on the packaging of eatable and drinkable products.

3. Right to choose

The right to be assured, wherever possible, access to a variety of goods, products or services at competitive prices.



Example: Whenever you visit any consumer retail supermarkets and convenience stores such as Easyday, DMart, Shoppers Stop, you must observe that you are offered each or most product category/categories from different brands. For instance, you will find chocolates, detergents, and drinks etc. of different companies and you are provided with an opportunity to choose as per your requirement from the given offerings.

It is the right to choose only that demands from the seller to provide options to the consumers where the consumers can make choices as per their discretion while taking purchasing decisions.

4. Right to be heard

The right to be heard and to be assured that consumer's interests will receive due consideration at appropriate fora (forums).

Under this act, various forums, commissions, councils and authorities have been established district wise, state wise and on national fronts for the consumers where they are provided with the opportunities of being heard.



Example:

- Central Protection Council
- State Consumer Protection Council
- District Consumer Protection Council

5. Right to seek redressal

The right to seek redress for unfair trade practices, restrictive trade practices, or unscrupulous consumer exploitation. The consumers are given rights to seek redressal in way of Repair, Replace and Refund. Other remedies are also available for consumers if the defects in the products are proved.

Under this act, various redressal forums have been established district wise, state wise and on central level for the consumers where they are provided with the opportunities of being redressed.



Example:

- National Consumer Disputes Redressal Commission
- State Consumer Disputes Redressal Commission
- District Consumer Disputes Redressal Commission

6. Right to consumer education/awareness

According to this right, it is the right of the consumer to acquire knowledge and skills. It is easier for literate consumers to know their rights and take actions, but this right assures that illiterate consumers can seek information about the existing acts and agencies are set up for their protection. The various government authorities, consumer forums, NGOs do come up with different campaigns to educate the consumers about their rights from time to time.



Example

JagoGrahakJago: The campaign, 'JagoGrahakJago' means 'wake up consumer, be aware'. It is a consumer awareness programme that was started by the Department of Consumer Affairs, to create consumer awareness through adverts, audio-visual campaigns and consumer education in 2005.



Case Study

Sehgal School of Competition v. Dalbir Singh (2005)

Facts of the case

A student was asked to deposit lump sum fees of 18,734 as fees for coaching for medical entrance examinations for the next two years. This was deposited by the student in two complete instalments within the first six months of classes. However, the student realized later that the quality of the coaching institute was substandard, and therefore sought a refund for the remaining period, which was refused by the coaching institute.

The respondent coaching centre argued before the commission that the student had withdrawn voluntarily and, therefore, there exists no deficiency of service. They submitted records that showed good results of the institute and alleged that it was wrong to observe that their coaching was not up to the mark. To justify taking the entire fees of two years lump sum, it was stated that the conditions imposed by the coaching required non-transferability of the seat, and therefore no refund of the fee was possible under any circumstance.

Points of Discussion

1. Can a student seek a refund of fees paid to a coaching class for the remaining period of classes that are yet to be held?
2. In case of a refusal to refund fee, can a claim for mental agony for pressing legal charges to be sought?

Judgement

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The State Tribunal following the view of the apex court and the National Commission, held that no educational institution shall collect lump sum fee for the duration of the entire course and if one does, such extra fee should be returned in case the student drops out due to deficiency.

The reasoning of the Commission – Upholding (supported) student's right to be refunded for remaining classes are on the following basis:

- **Clauses prohibiting refund of fees are unfair:** Any clause saying that fees once paid shall not be refunded is unconscionable and unfair and therefore not enforceable. This view was maintained by District and State Forums as well as in appeal by the National Commission.
- **Quashing respondent's argument on the reservation of seat:** The court dismissed this argument and further quoted UGC guidelines that mention that even if a student has not attended even a single class, an amount of 1000 may be deducted and proportionate charges for hostel fees, etc, and the balance amount has to be refunded in its entirety. On blocking of the seat, the Commission advised that a reserve list of candidates may be maintained, and waitlisted candidates may be given the opportunity to apply for the seat.
- **Additional compensation:** In the order by State Consumer Forum, it was mentioned that not just the balance amount of fee, but also a higher compensation for legal costs as well as the pain that the student had to undertake, could be availed in such cases.

Source: <https://vakilsearch.com/advice/the-top-ten-consumer-court-cases-and-trials-in-india/>

3.4 Consumer Disputes Redressal Commission

- 1) District Consumer Disputes Redressal Commission
- 2) State Consumer Disputes Redressal Commission
- 3) National Consumer Disputes Redressal Commission

1. District Consumer Disputes Redressal Commission

Establishment of District Consumer Disputes Redressal Commission (Sec. 28)

(1) The State Government shall, by notification, establish a District Consumer Disputes Redressal Commission, to be known as the District Commission, in each district of the State:

Provided that the State Government may, if it deems fit, establish more than one District Commission in a district.

(2) Each District Commission shall consist of--

- (a) a President; and
- (b) not less than two and not more than such number of members as may be prescribed, in consultation with the Central Government.

Qualifications, etc., of president and members of the District Commission (Sec. 29)

The Central Government may, by notification, make rules to provide for the qualifications, method of recruitment, procedure for appointment, term of office, resignation and removal of the President and members of the District Commission.

Salaries, allowances and other terms and conditions of service of President and members of District Commission (Sec. 30)

The State Government may, by notification, make rules to provide for salaries and allowances and other terms and conditions of service of the President, and members of the District Commission.

Officers and other employees of the District Commission (Sec. 33)

(1) The State Government shall provide the District Commission with such officers and other employees as may be required to assist the District Commission in the discharge of its functions.

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(2) The officers and other employees of the District Commission shall discharge their functions under the general superintendence of the President of the District Commission.

(3) The salaries and allowances payable to, and the other terms and conditions of service of, the officers and other employees of the District Commission shall be such as may be prescribed.

Jurisdiction of District Commission (Sec. 34)

(1) Subject to the other provisions of this Act, the District Commission shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration does not exceed one crore rupees:

Provided that where the Central Government deems it necessary so to do, it may prescribe such other value, as it deems fit.

(2) A complaint shall be instituted in a District Commission within the local limits of whose jurisdiction,--

(a) the opposite party or each of the opposite parties, where there are more than one, at the time of the institution of the complaint, ordinarily resides or carries on business or has a branch office or personally works for gain; or

(b) any of the opposite parties, where there are more than one, at the time of the institution of the complaint, actually and voluntarily resides, or carries on business or has a branch office, or personally works for gain, provided that in such case the permission of the District Commission is given; or

(c) the cause of action, wholly or in part, arises; or

(d) the complainant resides or personally works for gain.

(3) The District Commission shall ordinarily function in the district headquarters and may perform its functions at such other place in the district, as the State Government may, in consultation with the State Commission, notify in the Official Gazette from time to time.

Manner in which complaint shall be made (Sec. 35)

(1) A complaint, in relation to any goods sold or delivered or agreed to be sold or delivered or any service provided or agreed to be provided, may be filed with a District Commission by--

(a) the consumer,--

(i) to whom such goods are sold or delivered or agreed to be sold or delivered or such service is provided or agreed to be provided; or

(ii) who alleges unfair trade practice in respect of such goods or service;

(b) any recognized consumer association, whether the consumer to whom such goods are sold or delivered or agreed to be sold or delivered or such service is provided or agreed to be provided, or who alleges unfair trade practice in respect of such goods or service, is a member of such association or not;

(c) one or more consumers, where there are numerous consumers having the same interest, with the permission of the District Commission, on behalf of, or for the benefit of, all consumers so interested; or

(d) the Central Government, the Central Authority or the State Government, as the case may be:

Provided that the complaint under this sub-section may be filed electronically in such manner as may be prescribed.

Explanation.--For the purposes of this sub-section, "recognized consumer association" means any voluntary consumer association registered under any law for the time being in force.

(2) Every complaint filed under sub-section (1) shall be accompanied with such fee and payable in such manner, including electronic form, as may be prescribed.

Proceedings before the District Commission (Sec. 36)

(1) Every proceeding before the District Commission shall be conducted by the President of that Commission and at least one member thereof, sitting together:

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Provided that where a member, for any reason, is unable to conduct a proceeding till it is completed, the President and the other member shall continue the proceeding from the stage at which it was last heard by the previous member.

(2) On receipt of a complaint made under section 35, the District Commission may, by order, admit the complaint for being proceeded with or reject the same:

Provided that a complaint shall not be rejected under this section unless an opportunity of being heard has been given to the complainant:

Provided further that the admissibility of the complaint shall ordinarily be decided within twenty-one days from the date on which the complaint was filed.

(3) Where the District Commission does not decide the issue of admissibility of the complaint within the period so specified, it shall be deemed to have been admitted.

Findings of District Commissioner Reliefs provided by District Commission (Sec. 39)

(1) Where the District Commission is satisfied that the goods complained against suffer from any of the defects specified in the complaint or that any of the allegations contained in the complaint about the services or any unfair trade practices, or claims for compensation under product liability are proved, it shall issue an order to the opposite party directing him to do one or more of the following, namely:--

- (a) to remove the defect pointed out by the appropriate laboratory from the goods in question;
- (b) to replace the goods with new goods of similar description which shall be free from any defect;
- (c) to return to the complainant the price, or, as the case may be, the charges paid by the complainant along with such interest on such price or charges as may be decided;
- (d) to pay such amount as may be awarded by it as compensation to the consumer for any loss or injury suffered by the consumer due to the negligence of the opposite party:

Provided that the District Commission shall have the power to grant punitive damages in such circumstances as it deems fit;

(e) to pay such amount as may be awarded by it as compensation in a product liability action under Chapter VI;

- (f) to remove the defects in goods or deficiencies in the services in question;
- (g) to discontinue the unfair trade practice or restrictive trade practice and not to repeat them;
- (h) not to offer the hazardous or unsafe goods for sale;
- (i) to withdraw the hazardous goods from being offered for sale;
- (j) to cease manufacture of hazardous goods and to desist from offering services which are hazardous in nature;
- (k) to pay such sum as may be determined by it, if it is of the opinion that loss or injury has been suffered by a large number of consumers who are not identifiable conveniently:

Provided that the minimum amount of sum so payable shall not be less than twenty-five percent of the value of such defective goods sold or service provided, as the case may be, to such consumers;

- (l) to issue corrective advertisement to neutralize the effect of misleading advertisement at the cost of the opposite party responsible for issuing such misleading advertisement;
- (m) to provide for adequate costs to parties; and
- (n) to cease and desist from issuing any misleading advertisement.

(2) Any amount obtained under sub-section (1) shall be credited to such fund and utilized in such manner as may be prescribed.

(3) In any proceeding conducted by the President and a member and if they differ on any point or points, they shall state the point or points on which they differ and refer the same to another member for hearing on such point or points and the opinion of the majority shall be the order of the District Commission:

Provided that the other member shall give his opinion on such point or points referred to him within a period of one month from the date of such reference.

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(4) Every order made by the District Commission under sub-section (1) shall be signed by the President and the member who conducted the proceeding:

Provided that where the order is made as per majority opinion under sub-section (3), such order shall also be signed by the other member.

Review by the District Commission in certain cases (Sec. 40)

The District Commission shall have the power to review any of the order passed by it if there is an error apparent on the face of the record, either of its own motion or on an application made by any of the parties within thirty days of such order.

Appeal against the order of the District Commission. (Sec. 41)

Any person aggrieved by an order made by the District Commission may prefer an appeal against such order to the State Commission on the grounds of facts or law within a period of forty-five days from the date of the order, in such form and manner, as may be prescribed:

The State Commission may entertain an appeal after the expiry of the said period of forty-five days, if it is satisfied that there was sufficient cause for not filing it within that period:

No appeal by a person, who is required to pay any amount in terms of an order of the District Commission, shall be entertained by the State Commission unless the appellant has deposited fifty percent of that amount in the manner as may be prescribed:

No appeal shall lie from any order passed under sub-section (1) of section 81 by the District Commission pursuant to a settlement by mediation under section 80.

2) State Consumer Disputes Redressal Commission**Establishment of State Consumer Disputes Redressal Commission (Sec. 42)**

(1) The State Government shall, by notification, establish a State Consumer Disputes Redressal Commission, to be known as the State Commission, in the State.

(2) The State Commission shall ordinarily function at the State capital and perform its functions at such other places as the State Government may in consultation with the State Commission notify in the Official Gazette:

Provided that the State Government may, by notification, establish regional benches of the State Commission, at such places, as it deems fit.

(3) Each State Commission shall consist of--

(a) a President; and

(b) not less than four or not more than such number of members as may be prescribed in consultation with the Central Government.

Qualifications, etc., of President and members of State Commission: Sec. 43

The Central Government may, by notification, make rules to provide for the qualification for appointment, method of recruitment, procedure of appointment, term of office, resignation and removal of the President and members of the State Commission.

Salaries, allowances and other terms and conditions of service of President and members of State Commission: Sec. 44

The State Government may, by notification, make rules to provide for salaries and allowances and other terms and conditions of service of the President and members of the State Commission.

Jurisdiction of State Commission: Sec. 47

(1) Subject to the other provisions of this Act, the State Commission shall have jurisdiction--

(a) to entertain--

(i) complaints where the value of the goods or services paid as consideration, exceeds rupees one crore, but does not exceed rupees ten crore:

Provided that where the Central Government deems it necessary so to do, it may prescribe such other value, as it deems fit.

(ii) complaints against unfair contracts, where the value of goods or services paid as consideration does not exceed ten crore rupees.

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(iii) appeals against the orders of any District Commission within the State; and

(b) to call for the records and pass appropriate orders in any consumer dispute which is pending before or has been decided by any District Commission within the State, where it appears to the State Commission that such District Commission has exercised a jurisdiction not vested in it by law, or has failed to exercise a jurisdiction so vested or has acted in exercise of its jurisdiction illegally or with material irregularity.

(2) The jurisdiction, powers and authority of the State Commission may be exercised by Benches thereof, and a Bench may be constituted by the President with one or more members as the President may deem fit. The senior-most member shall preside over the Bench.

(3) Where the members of a Bench differ in opinion on any point, the points shall be decided according to the opinion of the majority, if there is a majority, but if the members are equally divided, they shall state the point or points on which they differ, and make a reference to the President who shall either hear the point or points himself or refer the case for hearing on such point or points by one or more of the other members and such point or points shall be decided according to the opinion of the majority of the members who have heard the case, including those who first heard it:

The President or the other members, as the case may be, shall give opinion on the point or points so referred within a period of one month from the date of such reference.

(4) A complaint shall be instituted in a State Commission within the limits of whose jurisdiction, --

(a) the opposite party or each of the opposite parties, where there are more than one, at the time of the institution of the complaint, ordinarily resides or carries on business or has a branch office or personally works for gain; or

(b) any of the opposite parties, where there are more than one, at the time of the institution of the complaint, actually and voluntarily resides, or carries on business or has a branch office or personally works for gain, provided in such case, the permission of the State Commission is given; or

(c) the cause of action, wholly or in part, arises; or

(d) the complainant resides or personally works for gain.

Review by the State Commission in certain cases (Sec. 50)

The State Commission shall have the power to review any of the order passed by it if there is an error apparent on the face of the record, either of its own motion or on an application made by any of the parties within thirty days of such order.

Appeal to the National Commission (Sec. 51)

(1) Any person aggrieved by an order made by the State Commission in exercise of its powers conferred by sub-clause (i) or (ii) of clause (a) of sub-section (1) of section 47 may prefer an appeal against such order to the National Commission within a period of thirty days from the date of the order in such form and manner as may be prescribed.

The National Commission shall not entertain the appeal after the expiry of the said period of thirty days unless it is satisfied that there was sufficient cause for not filing it within that period:

No appeal by a person, who is required to pay any amount in terms of an order of the State Commission, shall be entertained by the National Commission unless the appellant has deposited fifty percent of that amount in the manner as may be prescribed.

(2) Save as otherwise expressly provided under this Act or by any other law for the time being in force, an appeal shall lie to the National Commission from any order passed in appeal by any State Commission, if the National Commission is satisfied that the case involves a substantial question of law.

(3) In an appeal involving a question of law, the memorandum of appeal shall precisely state the substantial question of law involved in the appeal.

(4) Where the National Commission is satisfied that a substantial question of law is involved in any case, it shall formulate that question and hear the appeal on that question:

Provided that nothing in this sub-section shall be deemed to take away or abridge the power of the National Commission to hear, for reasons to be recorded in writing, the appeal on any other substantial question of law, if it is satisfied that the case involves such question of law.

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(5) An appeal may lie to the National Commission under this section from an order passed ex parte by the State Commission.

3) National Consumer Disputes Redressal Commission**Establishment of National Consumer Disputes Redressal Commission (Sec. 53)**

(1) The Central Government shall, by notification, establish a National Consumer Disputes Redressal Commission, to be known as the National Commission.

(2) The National Commission shall ordinarily function at the National Capital Region and perform its functions at such other places as the Central Government may in consultation with the National Commission notify in the Official Gazette:

The Central Government may, by notification, establish regional Benches of the National Commission, at such places, as it deems fit.

Composition of National Commission (Sec. 54)

The National Commission shall consist of--

(a) a President; and

(b) not less than four and not more than such number of members as may be prescribed.

Qualifications, etc., of President and members of National Commission (Sec. 55)

(1) The Central Government may, by notification, make rules to provide for qualifications, appointment, term of office, salaries and allowances, resignation, removal and other terms and conditions of service of the President and members of the National Commission:

Provided that the President and members of the National Commission shall hold office for such term as specified in the rules made by the Central Government but not exceeding five years from the date on which he enters upon his office and shall be eligible for re-appointment:

No President or members shall hold office as such after he has attained such age as specified in the rules made by the Central Government which shall not exceed,--

(a) in the case of the President, the age of seventy years;

(b) in the case of any other member, the age of sixty-seven years.

(2) Neither the salary and allowances nor the other terms and conditions of service of President and members of the National Commission shall be varied to his disadvantage after his appointment.

Jurisdiction of National Commission (Sec. 58)

(1) Subject to the other provisions of this Act, the National Commission shall have jurisdiction--

(a) to entertain--

(i) complaints where the value of the goods or services paid as consideration exceeds rupees ten crore:

Provided that where the Central Government deems it necessary so to do, it may prescribe such other value, as it deems fit;

(ii) complaints against unfair contracts, where the value of goods or services paid as consideration exceeds ten crore rupees;

(iii) appeals against the orders of any State Commission;

(iv) appeals against the orders of the Central Authority; and

(b) to call for the records and pass appropriate orders in any consumer dispute which is pending before or has been decided by any State Commission where it appears to the National Commission that such State Commission has exercised a jurisdiction not vested in it by law, or has failed to exercise a jurisdiction so vested, or has acted in the exercise of its jurisdiction illegally or with material irregularity.

(2) The jurisdiction, powers and authority of the National Commission may be exercised by Benches thereof and a Bench may be constituted by the President with one or more members as he may deem fit. The senior-most member of the Bench shall preside over the Bench.

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(3) Where the members of a Bench differ in opinion on any point, the points shall be decided according to the opinion of the majority, if there is a majority, but if the members are equally divided, they shall state the point or points on which they differ, and make a reference to the President who shall either hear the point or points himself or refer the case for hearing on such point or points by one or more of the other members and such point or points shall be decided according to the opinion of the majority of the members who have heard the case, including those who first heard it:

Provided that the President or the other member, as the case may be, shall give opinion on the point or points so referred within a period of two months from the date of such reference.

Review by the National Commission in certain cases. (Sec. 60)

The National Commission shall have the power to review any of the order passed by it if there is an error apparent on the face of the record, either of its own motion or on an application made by any of the parties within thirty days of such order.

Appeal against order of the National Commission. (Sec. 67)

Any person, aggrieved by an order made by the National Commission in exercise of its powers conferred by sub-clause (i) or (ii) of clause (a) of sub-section (1) of section 58, may prefer an appeal against such order to the Supreme Court within a period of thirty days from the date of the order:

The Supreme Court may entertain an appeal after the expiry of the said period of thirty days if it is satisfied that there was sufficient cause for not filing it within that period:

No appeal by a person who is required to pay any amount in terms of an order of the National Commission shall be entertained by the Supreme Court unless that person has deposited fifty percent of that amount in the manner as may be prescribed.

3.5 Consumer Protection Councils

The following consumer protection councils are established at District, State and Central level under this act:

1. Central Consumer Protection Council
2. State Consumer Protection Councils
3. District Consumer Protection Council

1. Central Consumer Protection Council

Establishment of Central Consumer Protection Council (Sec. 3)

(1) The Central Government shall, by notification, establish with effect from such date as it may specify in that notification, the Central Consumer Protection Council to be known as the Central Council.

(2) The Central Council shall be an advisory council and consist of the following members, namely:-

-

(a) the Minister-in-charge of the Department of Consumer Affairs in the Central Government, who shall be the Chairperson; and

(b) such number of other official or non-official members representing such interests as may be prescribed.

Objects of Central Council (Sec. 5)

The objects of the Central Council shall be to render advice on promotion and protection of the consumers' rights under this Act.

2. State Consumer Protection Councils

Establishment of State Consumer Protection Councils (Sec. 6)

(1) Every State Government shall, by notification, establish with effect from such date as it may specify in such notification, a State Consumer Protection Council for such State to be known as the State Council.

(2) The State Council shall be an advisory council and consist of the following members, namely:--

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- (a) the Minister-in-charge of Consumer Affairs in the State Government who shall be the Chairperson;
- (b) such number of other official or non-official members representing such interests as may be prescribed;
- (c) such number of other official or non-official members, not exceeding ten, as may be nominated by the Central Government.
- (3) The State Council shall meet as and when necessary but not less than two meetings shall be held every year.
- (4) The State Council shall meet at such time and place as the Chairperson may think fit and shall observe such procedure in regard to the transaction of its business, as may be prescribed.

Objects of State Council. (Sec. 7)

To render advice on promotion and protection of consumer rights under this Act within the State.

3. District Consumer Protection Council**Establishment of District Consumer Protection Council (Sec. 8)**

- (1) The State Government shall, by notification, establish for every District with effect from such date as it may specify in such notification, a District Consumer Protection Council to be known as the District Council.
- (2) The District Council shall be an advisory council and consist of the following members, namely:-
-
- (a) the Collector of the district (by whatever name called), who shall be the Chairperson; and
- (b) such number of other official and non-official members representing such interests as may be prescribed.
- (3) The District Council shall meet as and when necessary but not less than two meetings shall be held every year.
- (4) The District Council shall meet at such time and place within the district as the Chairperson may think fit and shall observe such procedure in regard to the transaction of its business as may be prescribed.

Objects of District Council (Sec. 9)

The objects of every District Council shall be to render advice on promotion and protection of consumer rights under this Act within the district.

3.6 Central Consumer Protection Authority (CCPA)**Establishment of Central Consumer Protection Authority. (Sec. 10)**

- (1) The Central Government shall, by notification, establish with effect from such date as it may specify in that notification, a Central Consumer Protection Authority to be known as the Central Authority to regulate matters relating to violation of rights of consumers, unfair trade practices and false or misleading advertisements which are prejudicial to the interests of public and consumers and to promote, protect and enforce the rights of consumers as a class.
- (2) The Central Authority shall consist of a Chief Commissioner and such number of other Commissioners as may be prescribed, to be appointed by the Central Government to exercise the powers and discharge the functions under this Act.
- (3) The headquarters of the Central Authority shall be at such place in the National Capital Region of Delhi, and it shall have regional and other offices in any other place in India as the Central Government may decide.

Powers of CCPA

CCPA is empowered to--

- Conduct investigations into violations of consumer rights and institute complaints/prosecution.
- Order recall of unsafe goods and services.

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- Order discontinued of unfair trade practices and misleading advertisements.
- Impose penalties on manufacturers /endorsers/ publishers of misleading advertisements.

3.7 The Consumer Protection Act, (1986 V. 2019)

The key differences between the Consumer Protection Act, 1986 and 2019 are discussed below:

Consumer Protection Act, 1986	Provisions	Consumer Protection Act, 2019
No separate regulator	Regulator	Central Consumer Protection Authority (CCPA) to be formed
Complaints can be filed in consumer courts where the seller (defendant) office is located	Consumer Court	Complaints can be filed in consumer courts where the complainant resides or works
No provision: Consumer can approach a civil court but not to consumer court	Product Liability	Consumer can seek compensation for harm caused by a product or service
District Commission : up to 20 lakhs State Commission: 20 lakhs to 1 Crore National Commission: above 1 crore	Pecuniary Jurisdiction	District Commission: up to 1 Crore State Commission: 1 Crore to 10 Crore National Commission: above 10 Crore
No legal provision	E-commerce	All rules of direct selling extended to e-commerce
No legal provision	Mediation cells	Court can refer settlement through mediation

Summary

- The Parliament of India repealed the three-decade old Consumer Protection Act, 1986, and replaced it with the new Consumer Protection Act, 2019, w.e.f 20.07.2020.
- While retaining certain old provisions, the New Act has certain new provisions that tightens the existing rules to further safeguard consumer rights and create exhaustive consumer protection law.
- The key new provisions under Consumer Protection Act 2019 are:
 - ✓ Inclusion of E- commerce, Direct selling
 - ✓ Establishment of Central Consumer Protection Authority (CCPA)
 - ✓ Strict Norms for Misleading Advertisement
 - ✓ Strict Norms for product liability
 - ✓ Changes in the Pecuniary Jurisdiction
 - ✓ Greater ease to dispute resolution
 - ✓ Addition in the clause of “Unfair Trade Practice”
 - ✓ Unfair Contract
 - ✓ Alternate Dispute Resolution through mediation

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- The new Act proposes the establishment of the Central Consumer Protection Authority (CCPA) to promote, protect and enforce the rights of consumers.
- It seeks to be more holistic with stricter rules, including jail term for unfair trade practices like adulteration and misleading ads by firms.
- The CCPA is also determined to initiate class action, including enforcing recall, refund and return of products.
- The consumers can now file complaints at any district or state Consumer Commission closest to them instead of travelling to the location where the service were sold.
- Thus, the new act provides for stringent provisions including rigorous punishment & penalties in tune with the current digital world and social norms.
- Consumer is a person who buys any goods or services for a consideration, which has been paid or promised or partly paid and partly promised, or under any system of deferred payment also includes the user with approval of such goods or beneficiary of services.
- As per Consumer Protection Act 2019, the expression “buys any goods” and ‘hires or avails any services” includes offline or online transactions through electronic means or by teleshopping or direct selling or multi-level marketing.
- A complaint:
 - ✓ Should be in writing
 - ✓ Can be filed in a regular way (offline)
 - ✓ Can be filed online – <http://edaakhil.nic.in/>
- A complaint can be presented by the complainant in person or by his agent. It can even be sent by registered post along with the court fee.

Keywords

Complaint: Complaint many allegation in writing by a complainant with a view to obtaining any relief under the Act.

Consumer: Any person who buys any goods for consideration which has been paid or promised or partly paid and partly promised.

Consumer Dispute: Dispute where the person against whom a complaint has been made, denies or disputes the allegation contained in the complaint.

Defect: It is defined to mean any fault, imperfection or shortcoming in the quality, quantity, potency, purity or standard which is required to be maintained.

Goods: 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.

Injury: It means any harm whatever illegally caused to any person, in body, mind or property.

Product: It means any article or goods or substance or raw material or any extended cycle of such product, which may be in gaseous, liquid, or solid state possessing intrinsic value which is capable of delivery either as wholly assembled or as a component part and is produced for introduction to trade or commerce, but does not include human tissues, blood, blood products and organ.

Product seller: Product seller in relation to a product, means a person who, in the course of business, imports, sells, distributes, leases, installs, prepares, packages, labels, markets, repairs, maintains, or otherwise is involved in placing such product for commercial purpose.

Service: Service means service of any description which is available to potential users and includes, but not limited.

Spurious goods: Spurious goods mean such goods which are falsely claimed to be genuine.

Trader: A trader in relation to any goods, means a person who sells or distributes any goods for sale and includes the manufacturer thereof, and where such goods are sold or distributed in package form, includes the packer thereof.

Self Assessment

1. As per Consumer Protection Act, 2019, Who can be a Complainant?
 - A. A consumer
 - B. Any voluntary consumer association registered under any law for the time being in force
 - C. The Central Government or any State Government
 - D. All of above

2. As per Consumer Protection Act, 2019, Who can be a Consumer?
 - A. Who buys any goods without consideration
 - B. Who buys any goods for a consideration
 - C. Who buys any goods for a commercial purpose
 - D. Who buys any goods for a resale purpose

3. As per Consumer Protection Act, 2019, A Manufacturer is a person who?
 - A. makes any goods or parts thereof
 - B. assembles any goods or parts thereof made by others
 - C. puts or causes to be put his own mark on any goods made by any other person
 - D. all of above

4. Misleading advertisement in relation to any product or service, means an advertisement, which:
 - A. truly describes such product or service
 - B. gives a true guarantee to, or is likely to mislead the consumers as to the nature, substance, quantity or quality of such product or service
 - C. conveys an express or implied representation which, if made by the manufacturer or seller or service provider thereof, would constitute an unfair trade practice
 - D. conveys all important information

5. Prakhar purchased an ISI mark electric iron from Bharat Electricals. While using, he found that it was not working properly. He approached the seller and complained for the same. The seller satisfies Prakhar by saying that he will ask the manufacturer to replace this iron. The manufacturer refused to replace and Bharat Electricals decided to file a complaint in the consumer court. Is Bharat Electricals entitled to do so and why?
 - A. Yes, Bharat Electricals is a consumer as per Consumer Protection Act, 2019.
 - B. No, Bharat Electricals is not a consumer as per Consumer Protection Act, 2019.
 - C. Yes, Bharat Electricals is a manufacturer as per Consumer Protection Act, 2019.
 - D. Yes, Bharat Electricals is a complainant as per Consumer Protection Act, 2019.

6. Making any statement, whether orally or in writing or by visible representation including by means of electronic record, which falsely represents that the goods are of a particular standard, quality, quantity, grade, composition, style or model is an example of:
 - A. Restrictive trade practice
 - B. Unfair trade practice
 - C. Deficiency
 - D. Product liability

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7. "A" or "Group of" consumers can demand any company to recall the current stock of a product from the market through appropriate consumer redressal mechanism if that product is proved to cause harm to the consumers' health post consumption because of:
- A. Right to safety
 - B. Right to education
 - C. Right to be heard
 - D. Right to be informed
8. The consumers should get knowledge about the quality, quantity, potency, purity, standard and price of goods, products or services, as the case may be due to which of the following consumer right?
- A. Right to safety
 - B. Right to education
 - C. Right to be heard
 - D. Right to information
9. The consumers should have access to a variety of goods, products or services at competitive prices wherever possible due to:
- A. Right to safety
 - B. Right to education
 - C. Right to choose
 - D. Right to information
10. A consumer has the right to represent him or advocate his interest at appropriate forums as per the following right:
- A. Right to be heard
 - B. Right to education
 - C. Right to choose
 - D. Right to information
11. "JagoGrahakJago" campaign is one the implications of which of the following rights of a consumer?
- A. Right to be heard
 - B. Right to education
 - C. Right to choose
 - D. Right to information
12. Any person aggrieved by an order made by the District Commission may prefer an appeal against such order to the State Commission within a period of ----- days from the date of the order.
- A. 30
 - B. 25
 - C. 45
 - D. 60

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13. Subject to the other provisions of this Act, the State Commission shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration, exceeds rupees -----, but does not exceed rupees -----.
- A. 25 Lakhs, 1 Crore
 B. 1 Crore, 10 Crore
 C. 10 Crore, 25 Crore
 D. 1 Core, 5 Crore
14. The age of president of National Commission shall not exceed??
- A. Seventy years
 B. Sixty-five years
 C. Sixty-seven years
 D. Sixty years
15. Subject to the other provisions of this Act, the State Commission shall have jurisdiction to entertain complaints where the value of the goods or services paid as consideration, exceeds rupees -----.
- A. 25 Lakhs
 B. 1 Crore
 C. 10 Crore
 D. 25 Crore

Answers for Self Assessment

1. D	2. B	3. D	4. C	5. B
6. B	7. A	8. D	9. C	10. A
11. B	12. C	13. B	14. A	15. C

Review Questions

- Write the objectives and features of the Consumer Protection Act, 2019.
- Define the following terms:
 - Consumer
 - Direct selling
 - E-commerce
 - Electronic service provider
 - Goods
 - Product Liability
 - Express Warranty
- Differentiate between defect and deficiency.
- Who can and cannot be complainant as per the Consumer Protection Act, 2019.
- Define "Complaint".
- What is a misleading advertisement? Who all can be made liable for a misleading advertisement?
- What is meant by 'Harm'?
- State the establishment and jurisdiction of National Consumer Disputes Redressal Commission.

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9. Write about the Qualifications, etc., of President and members of Consumer Disputes Redressal Commissions at District, State and Central level.
10. Discuss the establishment and jurisdiction of State Consumer Disputes Redressal Commission.
11. Write about the establishment and jurisdiction of District Consumer Disputes Redressal Commission.
12. State the manner in which complaint shall be made to District Consumer Disputes Redressal Commission.
13. Differentiate between the jurisdiction of District, State and National commissions.
14. Explain the reliefs provided by District Commissions to the complainant?
15. Discuss the establishment and objectives of various consumer protection councils.
16. Discuss the mechanism available for the aggrieved consumer under the Consumer Protection Act, 2019 if the he/she is not satisfied with the order of the various consumer commissions.
17. What is CCPA? Discuss the powers of CCPA.
18. State the provisions of reviewing the orders by various consumer commissions.
19. Illustrate the consumer rights guaranteed under the Consumer Protection Act, 2019.
20. Suraj booked a motor vehicle through one of the dealers. He was informed subsequently that the procedure for purchasing the motor vehicle had changed and was called upon to make further payment to continue the booking before delivery. On being aggrieved, Suraj filed a complaint with the State Commission. Would he succeed?

[Hint: Suraj would not succeed, as he is not a consumer. The sale transaction has not taken place so far. Therefore there is no question of any defect in the goods. In case it is alleged that the dealer is indulging in any unfair trade practice and that Suraj has suffered some loss or damage as a result thereof, then Suraj has to prove all these before his petition can be entertained.]

**Further Reading**

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- Kapoor, N. (2020). *Elements of Mercantile Law* (38 ed.). Sultan Chand & Sons.

**Web Links**

<https://www.indiacode.nic.in/handle/123456789/15256?locale=en>

<https://consumeraffairs.nic.in/sites/default/files/file-uploads/latestnews/FAQ.pdf>

Unit 04: Intellectual Property Rights

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Objectives

After studying this unit, you will be able to:

- explain the meaning and importance of Intellectual Property Rights (IPRs).
- categorize the IPRs.
- illustrate the meaning of Patents, Copyrights and Trademarks.
- review the registration procedure of Patents, Copyrights and Trademarks in India.
- comment on repercussions of infringement of Patents, Copyrights and Trademarks in India.
- illustrate the meaning of Geographical Indication and Trade Secret.
- review the registration procedure of Geographical Indication and Trade Secret in India.
- comment on repercussions of infringement of Geographical Indication and Trade Secret in India.
- appraise the purpose and scope of the Traditional Knowledge Digital Library.
- comment on the importance of IPRs in the Business world.

Introduction

Intellectual property rights (IPRs) are the rights given to persons over the creations of their minds. They usually give the creator an exclusive right over the use of his/her creation for a certain period of time.

In the modern era, Intellectual property rights plays an important role on trade of every nation. In this globalized and digitized world, there stands a higher risk of creative ideas getting copied or stolen without the permission of the author. The need for strong IP laws gives an overall contribution in the economy of the respective state. IPR is one of the security mean for intangible properties which are still open to the public and which can be quickly replicated by anyone. IP crimes have become the part and parcel of the digitized era leading to failure of business.

Numerous companies rely on adequate protection of their IPRs viz. patents, trademarks, and copyrights, while customers make use of IPRs to ensure that they purchase secure, assured goods. An IPR asset seeks to offer the same security protection as any other physical property, leading to its potential to offer the same comparative benefits to businesses. In a web-based world, it has now become much more relevant as it is comparatively simpler than ever to reproduce any specific template, logo, or functionality.

Thus, it has become indispensable for each nation to establish proficient laws for protection of various IPRs to strengthen its business environment.

In the present unit, the meaning, importance and types of IPRs, the infringement of various IPRs, and remedies available in case of infringement of various IPRs under their respective acts have been discussed.

4.1 Intellectual Property Rights (IPRs)

Intellectual property (IP) refers to the intangible assets (creations of the mind: inventions, literary and artistic works, and symbols, names, images, and designs used in commerce) created by the human mind.

In other words, Intellectual Property is a generic term that defines intangible assets that are owned by individual person or company contributing to the national as well the state economies.

4.2 IPR: Types

IPR: Types as per TRIPS

1. Copyright and Related Rights

- a) Rights of artists, painters, musicians, sculptors, photographers;
- b) Rights of computer programmes;
- c) Rights of phonogram performers and producers, as well as broadcasting.

2. Right of traders to use their trade marks.

3. Right of manufacturers & producers on geographical indication in relation to such products and produce.

4. Right of designers for their distinctive design striking to the eye.

5. Patents:

- a) Right of the inventor for patent is his invention.
- b) Rights of plant breeders and farmers.
- c) Rights of biological diversity.

6. Right of computer technologist for their layout design of integrated circuits.

7. Right of businessmen for protection of their undisclosed information on technology and management.

IPR: Types

- Copyrights
- Patents
- Trademarks
- Designs

- Geographical Indications
- Trade Secrets
- Plant Varieties
- Superconductor Chips and Integrated Circuits
- Traditional Knowledge
- Biological Diversity

4.3 Indian Statute for IPRs

- The Patents Act, 1970;
- The Trade Marks Act, 1999;
- The Copyright Act, 1957;
- The Designs Act, 2000;
- The Geographical Indications of Goods (Registration & Protection) Act, 1999;
- The Semiconductor Integrated Circuits Layout Design Act, 2000;
- The Biological Diversity Act, 2002;
- The Protection of Plant Varieties and Farmers' Rights Act, 2001.

4.4 Patent: The Patents Act, 1970

Patent: Meaning

In India, the law relating to patents is contained in the Patents Act, 1970. This Act has been amended in the year 1995, 1999, 2002, 2005, 2017 and 2019 to meet India's obligations under the agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS) forming part of the Agreement establishing the World Trade Organization (WTO). Now Indian Patents Act is fully compliant with India's obligations under the TRIPS Agreement of the WTO.

A patent is an exclusive statutory right granted to the inventor for his invention, which is either a product or a process that provides, in general, a new way of doing something, or offers a new technical solution to a problem.

Patent : Definition

As per Sec. 2(m) of the Patent act, 1970, "patent means a patent for any invention granted under this Act".

Patent: Key Features

- It is granted for both product and process.
- It is granted for limited period i.e. 20 years from the date of filing (Sec. 53).
- Patent rights are territorial rights (Sec. 48).
- It gives monopolistic rights to its owner.
- A patent shall be granted for one invention only provided that it shall not be competent for any person in a suit or other proceeding to take any objection to a patent on the ground that it has been granted for more than one invention (Sec. 46).
- Every patent shall be in the prescribed form and shall have effect throughout India (Sec. 46).

Patent: Importance

- It protects intellectual property for 20 years.
- ✓ No one else can manufacture, use, offer for sale, sell, import, distribute or license the product.
- ✓ Patentees can earn royalties for using your patent post their consent.

- ✓ Patentees can block competitors.

Patentability Criteria

- Patentable Subject Matter
- Industrial Applicability
- Novelty
- Incentive Step
- Specification
- Should not attract the provisions of section 3 and 4 of the Patents Act 1970.

Patentable Subject Matter: It can be a product or process.

Industrial Applicability: Industrial applicability requirement checks if an invention is capable of being made or used in an industry. If a product can be manufactured repeatedly and has at least one use in an industry, it will be considered as industrially applicable.

Novelty: This means that your invention must not have been made public – not even by yourself – before the date of the application.

Incentive Step or Non-obvious: It means a feature of an invention that involves technical advance as compared to the existing knowledge or having economic significance or both and that makes the invention not obvious to a person skilled in the art [Sec. 2(ja)].

It means a feature of an invention that involves technical advance as compared to the existing knowledge or having economic significance or both.

Specification: The specification has to enable the invention, which means it must fully and particularly describe the invention and its operation or use and the method by which it is to be performed.

Patentable Subject Matter

An invention relating either to a product or process that is new, involving inventive step and capable of industrial application can be patented. However, it must not fall into the categories of inventions that are non-patentable under sections 3 and 4 of the Act. Thus, the following are patentable subject matters:

- Any article, apparatus or machinery or its components.
- Any living or nonliving substance, product, or pharmaceutical product.
- Any composition of matter in pharmaceutical products.
- Any process, manner or art of manufacturing other than the essential biological process.

Non Patentable Inventions: Sec. 3

Sec. 3(a): Frivolous inventions.

Sec. 3(b): Inventions which are contrary to Law or Morality or injurious to public health.

Sec. 3(c): Mere discovery of a scientific principle or formulation of an abstract theory.

Sec. 3(d): The mere discovery of a new form of a known substance which does not result in the enhancement of the known efficacy of that substance or the mere discovery of any new property.

Sec. 3(e): A substance obtained by a mere admixture resulting only in the aggregation of the properties of the components thereof or a process for producing such substance is not an invention.

Sec. 3(f): Mere arrangement or re-arrangement of known devices.

Sec. 3(h): Method of agriculture or horticulture.

Sec. 3(i): Any process for the medicinal, surgical, curative, prophylactic diagnostic therapeutic or other treatment of human being or any process for a similar treatment of animals to render them free of disease or to increase their economic value or that of their products is not patentable.

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Sec. 3(j): Plants and animals in whole or any part thereof other than micro-organisms but including seeds, varieties and species and essentially biological processes for production or propagation of plants and animals are not inventions.

Sec. 3(k): A mathematical or business method or a computer programme per se or algorithms are not inventions and hence not patentable.

Sec. 3(l): A literary, dramatic, musical or artistic work or any other aesthetic creation whatsoever including cinematographic works and television productions is not patentable.

Sec. 3(m): A mere scheme or rule or method of performing mental act or method of playing game is not patentable.

Sec. 3(n): A presentation of information is not patentable.

Sec. 3(o): Topography of integrated circuits is not patentable.

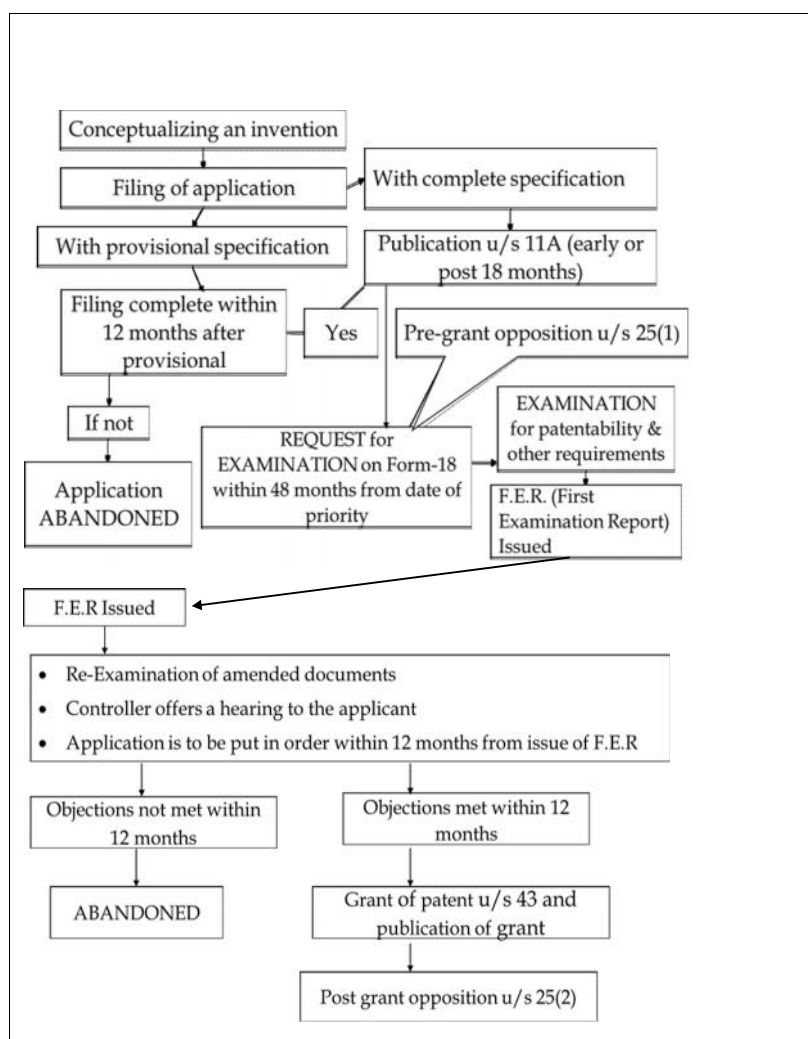
Sec. 3(p) An invention which in effect, is traditional knowledge or which is an aggregation or duplication of known properties of traditionally known component or components is not patentable.

Filing of Application for Patent

- Physical filing at patent office
- Electronic filing (July 20, 2007)

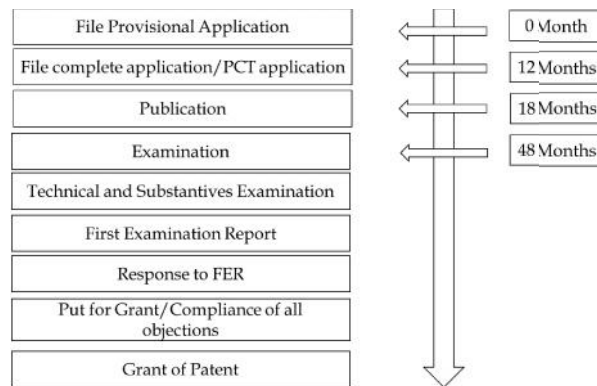
Patent Grant in India

The procedure for patent grant in India is discussed through the following flow chart:



Source: https://ipindia.gov.in/writereaddata/Portal/Images/pdf/Final_FREQUENTLY_ASKED_QUESTIONS_-PATENT.pdf

Patent Grant in India: Nutshell



Renewal of Patent

- It has to be renewed every year by paying the renewal fee.
- A patent in India can be renewed for a maximum period of 20 years from the patent filing date.

Infringement of a Patent

As per the provisions mentioned in the Indian Patents Act, 1970; following amount as an act of Patent Infringement:

- ✓ The colorable imitation of the invention
- ✓ Mechanical Equivalents
- ✓ Carrying essential features of the invention
- ✓ Immaterial variation in the invention
- The limitation period for instituting a suit for patent infringement is 3 years from the date of infringement and the jurisdiction is the geographic area where the infringement has taken place.
- The burden of proof to establish that an infringement has occurred lies on the patentee (Patent holder).

Infringement of a Patent: Remedies

Under the (Indian) Patents Act, 1970, the following remedies are provided:

- Administrative remedy: The patent owner can reach the collector of customs and prohibit the entry of these goods into Indian market. The patent owner must provide the name of the exporter, consignee, port of entry, name of the ship etc. details.
- Civil Remedies
 - ✓ Injunctions: When there is a prima facie case and/or balance of convenience is in the favor of the plaintiff; Interim injunction is granted. Whereas after the complete trial permanent injunctions are granted.
 - ✓ Damages: Damages or accounts of profits is granted if it is established that on the date of the infringement; the defendant was aware about the prior existence of the patent.

The court may also order delivery up of the infringing goods. This is mentioned in order XXXIX rule 7 of the Civil Procedure Code.

Groundless Threats for Infringement Proceedings: Remedies (Sec. 106)

(1) Where any person (whether entitled to or interested in a patent or an application for a patent or not) threatens any other person by circulars or advertisements or by communications, oral or in writing addressed to that or any other person, with proceedings for infringement of a patent, any person aggrieved thereby may bring a suit against him praying for the following reliefs, that is to say--

- (a) a declaration to the effect that the threats are unjustifiable;
- (b) an injunction against the continuance of the threats; and
- (c) such damages, if any, as he has sustained thereby.

(2) Unless in such suit the defendant proves that the acts in respect of which the proceedings were threatened constitute or, if done, would constitute, an infringement of a patent or of rights arising from the publication of a complete specification in respect of a claim of the specification not shown by the plaintiff to be invalid, the court may grant to the plaintiff all or any of the reliefs prayed for.



Case Study

Indoco Remedies Ltd v. Bristol Myers Squibb Holdings

Facts

Bristol Myers Squibb (Bristol) was the patent holder and producer of a drug called "Apixaban". Bristol approached Delhi HC in 2019, seeking an ad-interim injunction against Indoco Remedies (Indoco) for infringing their patent and producing a generic form of the drug called "APIXABID".

In 2020, Indoco approached the court seeking permission to sell the already manufactured (58,000) strips of the drug on grounds of 'public interest', especially during the COVID 19 pandemic.

Indoco submitted that the drug was important for treating COVID 19 and was much cheaper than Bristol Myers' drug.

Bristol Myers argued that Indoco had only manufactured these strips in anticipation of the injunction and the sale cannot be allowed due to clear infringement. They further contended that in light of 'public interest' the appropriate remedy would be a compulsory license.

Court Decision

Indoco's request to sell the drug was denied by the court, citing that there was no evidence for the shortage of the Bristol Myers drug to allow the sale of the generic drug and also it did not prove any overwhelming public interest reason.

Source: <https://www.casemine.com/judgement/in/56b48d73607dba348fff3029>

4.5 TradeMark(The Trade Marks Act, 1999)

Trade Mark: Definition

As per the definition provided under Section 2 (zb) of the TM Act, "trade mark" means a mark capable of being represented graphically and which is capable of distinguishing the goods or services of one person from those of others and may include shape of goods, their packaging and combination of colors.

Trade Mark: Importance

It helps consumers identify and purchase a product or service because its nature and quality, indicated by its unique trade mark, meets their needs.

Registration of Trade Mark

- The registration procedure in India is based on the 'first to file' system. It is therefore important that the rights holder applies for the registration of its mark as soon as possible.

- The registration of a trade mark confers on the registered proprietor of the trade mark the exclusive right to use the trade mark in relation to the goods or services in respect of which the trade mark is registered.
- While registration of a trade mark is not compulsory, it offers better legal protection for an action for Infringement the renewable . It is pertinent to note that the letter "R" in a circle i.e. ® with a trademark, can only be used after the registration of the trademark under the TM Act.

Trade Mark: Forms

- Word
- Device/Picture
- Label
- Name
- Signature
- Logo
- Letter
- Numerals
- Shape of Goods
- Combination of colors

Groundsfor Accepting a Trade Mark For Registration

- It should be unique and distinctive.
- It should not indicate kind, quality, quantity, intended purpose, values of the product.



Case Study

ELGI Ultra Industries Limited v The Assistant Registrar of Trade Marks, 2008

The Intellectual Property Appellate Board [IPAB], held that “the words “ultra” and “perfect” are highly descriptive and laudatory. They cannot be seen as trademarks.”

- It should not be customary in the current language.



Example

Otis’s trademark “Escalator” for moving staircases became a generic word and therefore, the Trademark Office concluded that Otis cannot use its trademark since the mark has become customary in respect of moving stairs.

- It should not deceive or cause confusion to the public.



Example

If a company starts to make biscuits by the name of Parle-J, it would be an infringement of the right of Parle-G, since it is highly deceptive.

- It should not hurt the religious susceptibilities of any class or section of the citizens of India.



Case Study

Lal Babu Priyadarshi v. Amrit Pal Singh (Civil Appeal No. 2138 of 2006, Supreme Court)

The appellant had applied for registration of the mark “Ramayan” with the device of a crown in

relation to incense sticks and perfumeries. The court observed that “no person can claim the name of a holy text as a trademark.”

- It should not be scandalous or obscene.
- It should not be prohibited under the Emblem and names (Prevention of Improper use Act, 1950)
- It should not consists exclusively of-
 - a) the shape of goods which results from the nature of the goods themselves; or
 - b) the shape of goods which is necessary to obtain a technical result; or
 - c) the shape which gives substantial value to the goods.

Symbols of a Trade Mark

- TM for pending/applied marks
- R for registered marks
- SM for service marks

Duration of a Trade Mark

- A Trade Mark/Service Mark is valid for a period of 10 years.
- Trade Mark can be renewed every 10 years. Renewal application can be filed 6 months prior to the due date of the next renewal date.
- Non-user of a registered trademark for a continuous period of 5 years is a ground for cancellation of registration of such trademark at the behest of any aggrieved party.
- A service mark is not separately defined under the 1999 Act but is included in the definition of a trademark.
- Using this symbol TM with your trademark simply implies that you claim to be the proprietor of the trademark. There is no prohibition on the use of the symbol TM in India.
- Only the proprietor of a trademark whose trademark has been registered in India can use the symbol ® in India. Using the symbol ® unless your mark has been registered in India is unlawful.

Remedies for Infringement

Civil remedies

- Injunction or authoritative direction by the court of law
- Damages can be claimed by the aggrieved party on grounds that his exclusive right of using the trademark has been ceased and this subsequently has led to him or his enterprise suffering losses.
- A civil remedy that is often claimed is handling of the profit accounts along with a command for delivery or removal of the products that have been infringed.

Criminal remedies

- Six months of imprisonment, which can be extended to a time frame of three years, for infringing trademark rights.
- Fine of fifty thousand rupees which can be increased to an extent of two lakhs in case someone is found to transgress the trademark rights.



Case Study

The Coca Cola Company v. Bisleri International Pvt. Ltd.

The defendant, Bisleri by a master agreement, had sold and assigned the trademark MAAZA

including formulation rights, know-how, intellectual property rights and goodwill for India with respect to a mango fruit drink known as MAAZA to Coca Cola.

In 2008, the defendant company filed for registration of the mark MAAZA in Turkey and started exporting fruit drink under the name MAAZA. The plaintiff, Coca Cola claimed permanent injunction and damages for infringement of trademark and passing off.

The court granted an interim injunction against the defendant (Bisleri) from using the trademark MAAZA in India as well as for export, which was infringement of trademark.

Source: <https://www.hg.org/legal-articles/top-5-interesting-trademark-cases-in-india-51057>

4.6 Copyrights: The (Indian) Copyright Act, 1957

The (Indian) Copyright Act, 1957, pursuant to the amendments in the year 1999, fully reflects the Berne Convention for Protection of Literary and Artistic Works, 1886 and the Universal Copyrights Convention, to which India is a party.

Copyrights: Meaning

- The term original in the copyright law means that the work originated with the author.
- There is no requirement for novelty or uniqueness as there is in patent law.
- Copyright law protects the expression of an idea. Not the idea itself.

Copyrightable Matter

- Literary work including software – Books, Essay, Compilations, computer programs.
- Artistic work – Drawing, painting, logo, map, chart, plan, photographs, work of architecture.
- Dramatic work – Screenplay, drama.
- Musical work – musical notations.
- Sound Recording – Compact Disc.
- Cinematograph Films – Visual Recording which includes sound recording.

Registration of Copyright

The registration of copyright is not compulsory but advisable.

Enforcement of Copyright in India

- Civil remedies in the form of permanent injunction, damages or accounts of profits, delivery of the infringing material for destruction and cost of the legal proceedings. etc.
- A cognizable offence punishable for a term which shall not be less than six months but which may extend to three years with a fine which shall not be less than 50,000 but may extend to 2,00,000.

Duration/Term of Copyright

a) Lifetime of the author plus sixty years from the beginning of the calendar year next following the year in which the author dies in case of the following copyrights:

- Literary works
- Dramatic works
- Musical works
- Artistic works

b) Until sixty years from the beginning of the calendar years next following the year in which the works is first publish in case of the following copyrights:

- Anonymous and pseudonymous works
- Posthumous works
- Cinematograph films

- Sound records
- Government work
- Public undertakings
- International agencies
- Photographs

Process to Obtain Copyright

The person applying for copyright has to follow the following steps:

1. The person has to file the application along with the fee either in the form of DD/ IPO
2. Then the diary number will be issued.
3. The person has to compulsorily wait for 30 days for objections.
4. If no objection is filled, then the examiner goes ahead to review and scrutinize the application to find any discrepancy.
5. If in case objection is filed:
 - The letter will be sent to both parties, i.e., party filing the objections and the party against whom the objection is filed.
 - Reply will be awaited from both the parties.
 - Reply by both the parties will be heard by the registrars.
 - If in case objections are rejected the application will be accepted and if objection will be accepted, then the application will be rejected.
 - This procedure applies in the case of both published and unpublished work.

When is a Copyright Infringed?

Copyright in a work shall be deemed to be infringed –

- a) when any person, without a license granted by the owner of the copyright or the Registrar of Copyrights under this Act or in contravention of the conditions of a license so granted or of any condition imposed by a competent authority under this Act –
 - (i) does anything, the exclusive right to do which is by this Act conferred upon the owner of the copyright, or
 - (ii) permits for profit any place to be used for the communication of the work to the public where such communication constitutes an infringement of the copyright of the work, unless he was not aware and had no reasonable ground for believing that such communication to the public would be an infringement of his copyright.
- (b) when any person –
 - i. makes for sale or hire, or sells or lets for hire, or by way of trade displays or offers for sale or hire, or
 - ii. distributes either for the purpose of trade or to such an extent as to affect prejudicially the owner of the copyright, or
 - iii. by way of trade exhibits in public, or
 - iv. imports into India

(Any infringing copies of the work)

Infringement of Copyrights: Remedies

Civil remedies

Injunction, damages, accounts and otherwise as are or may be conferred by law for the infringement of a right.

4.7 Geographical Indication (GI): The Geographical Indications of Goods (Registration & Protection) Act, 1999

The Geographical Indications of Goods (Registration and Protection) Act, 1999 (GI Act), in Section 2(e), defines the term “geographical indication” as –

“An indication which identifies such goods as agricultural goods, natural goods or manufactured goods as originating, or manufactured in the territory of a country, or a region or locality in that territory, where a given quality, reputation or other characteristic of such goods is essentially attributable to its geographical origin and in case where such goods are manufactured goods one of the activities of either the production or of processing or preparation of the goods concerned takes place in such territory, region or locality, as the case may be.”



Notes

In simpler terms, GI is a status accorded to a good which is unique to a particular region or area and are originated from there.

These goods have a reputation for their quality. They are associated with a sense of legitimacy and trust simply because they have the tag of belonging to that region.



Examples

Basmati rice is known for its unique aroma and long grains. It is unique to the Indo-Gangetic plains.

"Champagne", "Bordeaux" and "Chianti", the first two being regions in France and the third, a region in Italy, all are famous for their wines.

Why GI?

- They identify goods as originating in a particular territory or a region or locality in that territory;
- They suggest to consumers that the goods come from an area where a given quality, reputation or other characteristics of the goods is essentially attributable to their geographic origin; and
- They promote the goods of producers of a particular area.



Did you know? **Difference between Trademark and GI?**

A trademark can be associated with objects, companies etc., while a GI can only be associated with a particular geographical location.

Duration of Protection

A Geographical Indication is registered for a period of 10 years and the registration may be renewed from time to time for a period of 10 years at a time.

GI: Scope

- Agricultural (example, Basmati rice)
- Natural (example, Makrana marble)
- Handicraft or of any industry (example, Kashmiri pashmina)
- Food stuff (example, Dharwad pedha)

Why to register a GI?

Prevent unauthorized use of the registered geographical indication by others by initiating infringement action by way of a civil suit or criminal complaint.

Is Registration of GI compulsory?

The registration of GI is not compulsory but advisable in India.

Registration Procedure of GI

- The application must be filed to the office of the GI registry, which is in Chennai.
- The application must contain all the relevant details like –The details of the “principal place of business”, Historical evidence to back the claims, a detailed description of the good and its usage, the method of production.
- The application will be subjected to scrutiny by the Registry and a panel of experts, which will be designated by them.
- The applicant will have one month to correct any mistakes.
- The Registrar is further vested with the power to rescind the application if the errors are not dealt with.
- Upon the acceptance of the application, the Registry will publish the same within three months of its acceptance.
- Any person can file an opposition to the publication of the GI application within three months (extension can be provided for another month).



Examples of State wise GIs

- Phulkari (Handicraft) --- Punjab, Haryana, Rajasthan
- Basmati (Agricultural) --- Punjab, Haryana, Himachal Pradesh, Delhi, Uttarakhand, Uttar Pradesh, J&K
- Kangra Tea (Agricultural) --- Himachal Pradesh
- Mysore Sandalwood Oil (Manufactured) --- Karnataka
- ChambaRumal (Handicraft) --- Himachal Pradesh
- Nirmal Furniture (Handicraft) --- Telangana
- Kashmir Pashmina (Handicraft) --- J & K
- Baluchari Saree (Handicraft) --- West Bengal
- BanglarRasogolla (Food Stuff) --- West Bengal
- Kutch Embroidery (Handicraft) --- Gujarat
- Odisha Rasagola (Food Stuff) --- Odisha
- Feni (Manufactured) --- Goa
- Makrana Marble (Natural Goods) --- Rajasthan

GI Infringement: Remedies (Sec. 67)

Action for infringement of a Geographical Indication may be instituted at a District Court or High Court having jurisdiction. Available relief's include: -

- Injunction: The order of injunction under sub-section (1) may include an ex parte injunction or any interlocutory order for any of the following matters, namely:--
 - (a) for discovery of documents;
 - (b) preserving of infringing goods, documents or other evidence which are related to the subject-matter of the suit;
 - (c) restraining the defendant from disposing of or dealing with his assets in a manner which may adversely affect plaintiffs ability to recover damages, costs or other pecuniary remedies which may be finally awarded to the plaintiff.
- Both civil and criminal remedies are available.
- Criminal action lies in the case of falsification and false application of Geographical Indications.

- Civil action lies in the case of infringement of a registered Geographical Indication.
- Imprisonment for a term which may not be less than six months but may extend to three years and with
- A fine which may not be less than 50,000 (approx. US\$ 800) but may extend to 2,00,000 (approx. US\$ 3,000).

*Notes*

- The relief which a court may grant in any suit for infringement or for passing off referred to in section 66 includes injunction (subject to such terms, if any, as the court thinks fit) and at the option of the plaintiff, either damages or account of profits, together with or without any order for the delivery-up of the infringing labels and indications for destruction or erasure.
- Notwithstanding anything contained in sub-section (1), the court shall not grant relief by way of damages (other than nominal damages) on account of profits in any case--
 - (a) where in a suit for infringement the defendant satisfies the court--
 - (i) that at the time he commenced to use the geographical indication complained of in the suit he was unaware and had no reasonable ground for believing that the geographical indication of the plaintiff was on the register; and
 - (ii) that when he became aware of the existence and nature of the plaintiff's right in the geographical indication, he forthwith ceased to use the geographical indication in relation to good in respect of which it was registered; or
 - (b) where in a suit for passing off, the defendant satisfies the court--
 - (i) that at the time he commenced to use the geographical indication complained of in the suit he was unaware and had no reasonable ground for believing that the geographical indication relating to the plaintiff was in use; and
 - (ii) that when he became aware of the existence and nature of the geographical indication relating to the plaintiff he forthwith ceased to use the geographical indication complained of.

How to protect GI?

- So-called sui generis systems (i.e. special regimes of protection);
- Using collective or certification marks; and
- Methods focusing on business practices, including administrative product approval schemes.

*Case Study***Tea Board, India v ITC Limited****Plaintiff: Tea Board****Defendant: ITC Ltd.**

The Tea Board of India filed a suit against ITC Ltd. for using the name "Darjeeling" at one of its refreshment lounges at its Hotel, Calcutta which leads to infringement of the plaintiff's geographical indication mark, and certification mark. The plaintiff is the registered owner of trademark "Darjeeling." The marks are independently registered under the Geographical Indication of Goods (Registration & protection Act) 1999 and the Trade Marks Act, 1999. ITC introduced the term 'Darjeeling Lounge' in January 2003. Later in April 2005, the Tea Board became aware about the ITC's trademark application for 'Darjeeling lounge.' After exchange of certain notices, the plaintiff filed a suit in 2010 before the Court requesting temporary injunction against the alleged defendant.

Points of Discussion

1. Whether the plaintiff has acquired any right to use the logo or name "Darjeeling" other than the authority to certify the tea that originates from Darjeeling?
2. Whether the defendant used the name Darjeeling Lounge with Malafide intention to make believe its customers that they owe their origin to Darjeeling?
3. Whether the plaintiff can protect logo "Darjeeling" under Copyright Act?

Arguments by Plaintiff

According to the plaintiff, defendant has infringed the registered geographical indication rights by naming one of its business premises as 'DARJEELING LOUNGE.' The defendant has a malice intention used the word Darjeeling for the sale of products, misleads its customers made them trust that the goods are originated from the specific area of source. The cause of publicity and promoting of products has created an unfair competition within the market. The defendant with the aid of using the impugned name 'DARJEELING' has threaten the business exercises of the people groups who are absolutely occupied with the Darjeeling Tea.

To prevent the Defendant from violating the above rights in reference with the Trademark Act and Geographical Indications, the plaintiff had moved an interlocutory application for temporary injunction to restrain the defendant from infringing the rights in any viable manner.

Arguments by defendant

According to Defendant, there is no reason for filing the suit as it was barred by limitation. Since the plaintiff had only certification trademark, no right or cause of action could arise for the plaintiff under such certification trademark against the defendant using the 'DARJEELING LOUNGE' in view with the Trademark Act. The suit is also not maintainable under the section 26 of the Geographical Indications Act.

The rights of plaintiff is limited only to certify tea that originates from registered tea garden in Darjeeling. This has no reference with regard to the geographical origin of the place of Darjeeling. Infringement of certification trade mark is confined only to Section 75 and that too, such infringement is confined to the goods, and services for which the certification trade mark is registered and it cannot be extended to any other goods and services.

Judgement

The court observed that, there has been no infringement under the Geographical Indications of Goods Act because the defendant's 'Lounge' is not relating to goods. It has been used for their hotel services therefore it could not be constituted as infringement of the Geographical Infringement. Plaintiff's rights conferred by the registration of the word 'Darjeeling' is only in relation to tea. 'Darjeeling' is not a trade mark. It is only used to indicate geographical indication of a place of origin of tea originating from Darjeeling.

The Court additionally brought up that the parties were engaged in different industries, and there was no competition between the two. Unfair Competition which means any act of competition contrary to honest practice in commercial area. Hence, the court ruled out the possibility of any unfair competition on the part of the defendant. It also emphasized the defendant's case that the lounge is generally accessed by educated and knowledgeable guests and thus, they were not likely to be confused or mislead by the use of it. Therefore, it was adjudged by the Court there was no fraudulent act committed on the part of the defendant.

Regarding the issue of copyright infringement asserted by the plaintiff, the Court brought up there is no similarity between the certification trademark logo and the logo of the defendant. Thus, the court held this issue to be immaterial.

The court concluded by saying that the suit was frivolous and dismissed it with an expense of Rs. One Lakh.

Source: <https://iprlawindia.org/caselaw/tea-board-india-vs-itc-limited/>

4.8 Trade Secret

A "trade secret" is any valuable information that is not publicly known and for which the owner has taken "reasonable" steps to maintain secrecy. These include information such as business plans, customer lists, confidential business information ideas related to your research and development cycle, etc.

- It relates to business information not known or disclosed to the public.
- It provides competitive advantage to the business.
- It may be any information such as a formula pattern, compilation of any data or information, program, device, method, technique, or process which has economic value and is required to maintain secrecy.
- Such information should have certain attributes in order to qualify as a trade secret. These are:
 - ✓ It has Independent economic value
 - ✓ It is not generally known
 - ✓ It is not readily ascertainable
 - ✓ The owner is making reasonable efforts to maintain secrecy

Examples

1. Coca Cola Formula
2. Secret Spice -Mix
3. McDonald's Big Mac sauce
4. Google search algorithm
5. New York Times bestseller list
6. Listerine
7. WD-40
8. Krispy Kreme Doughnut Recipe

How are Trade Secrets Protected?

- There is no statute or legislation that governs the protection of trade secrets in India. However, rights in respect of trade secrets are enforced through the Contract Law (Indian Contract Act, 1872) principles of Equity or by way of common law for breach of confidence.
- Thus, contrary to other IPRs, trade secrets are protected without registration, that is, trade secrets are protected without any procedural formalities.
- Consequently, a trade secret can be protected for an unlimited period of time.
- Trade secrets are not registered with a governmental body.
- All you need to do to establish your information as such is to treat it as a trade secret.
- The subject matter of trade secrets is usually defined in broad terms and includes sales methods, distribution methods, consumer profiles, advertising strategies, lists of suppliers and clients, and manufacturing processes.
- The final determination of what information constitutes a trade secret will depend on the circumstances of each individual case.

Trade Secrets: Requisites

- It must be documented.
- It must have limited access.
- It must be protected using administrative, legal and technical means.
- It must have an appropriate legal framework in place if shared with another entity.
- It must not be in the public domain.
- It must be of commercial value to the organization now or in the future.
- It must be kept secret.

Trade Secret Infringement: Remedies

In India only civil or equitable remedies are available for a breach of confidence cause of action. The following remedies are available in case of trade secret infringement.

- The award of an injunction “preventing a third party from disclosing the trade secrets,” the return of all “confidential and proprietary information,” and
- The award of compensation or damages “for any losses suffered due to disclosure of trade secrets.”
- The court may also order the party at fault to “deliver-up” such materials.

4.9 Traditional Knowledge Digital Library (TKDL)

The Traditional Knowledge Digital Library (TKDL) project, initiated in India in 2001, is a collaboration between the Council of Scientific and Industrial Research (CSIR), Ministry of Science and Technology, and the Department of Ayurveda, Yoga and Naturopathy, Unani, Siddha and Homeopathy (AYUSH), Ministry of Health and Family Welfare, of India.

It is being implemented at the CSIR (Council of Scientific and Industrial Research). The interdisciplinary team involved in the creation of the TKDL for Indian Systems of Medicine included traditional medicine experts (Ayurveda, Unani, Siddha and Yoga), patent examiners, IT experts, scientists and technical officers.

Traditional Knowledge (TK) is a valuable yet vulnerable asset to indigenous and local communities who depend on TK for their livelihood. The healthcare needs of more than 70% of the population and the livelihood of millions of people in India is dependent on traditional medicine.

The next challenge is to use India’s strength in traditional knowledge for its effective promotion, development and utilization.

TKDL: Key Facts

The TKDL contains documentation of publicly available traditional knowledge (TK) that:

- relates to Ayurveda, Unani, Siddha and Yoga.
- is in digitized format.
- is available in five languages: English, German, French, Japanese and Spanish.

TKDL: Key Features

- It provides information on TK existing in India, in languages and a format understandable by patent examiners at international patent offices.
- It contains information for patent examiners on prior art that would otherwise be available only in Sanskrit and other local languages in Indian libraries.
- It lists the precise time, place and medium of publication for prior art searches by patent examiners.
- It aims to prevent the granting of erroneous patents.

TKDL: Purpose

- It protects traditional knowledge, which will safeguard the misappropriation of traditional knowledge as well as promote further research and development of products and services based on traditional knowledge.
- It seeks to prevent patents from being granted for products developed with TK that have little, if any, inventive steps.
- It intends to act as a bridge between information recorded in ancient Sanskrit and patent examiners (with its database containing information in a language and format understandable to patent examiners).

- It facilitates access to information not easily available to patent examiners, thereby minimizing the possibility that patents could be granted for “inventions” involving only minor or insignificant modifications.

TKDL: Latest Facts

- CSIR recently celebrated 20 years of India’s Traditional Knowledge Digital Library, the first of its kind globally.
- TKDL database contains more than 3.9 lakh formulations/ practices from the Indian systems of medicine (Ayurveda, Siddha, Unani and Sowa Rigpa) and Yoga.
- The database is available to only patent examiners through the TKDL Access (Non-disclosure) Agreement.
- So far, Access Agreements have been signed with 13 international patent offices, including India.
- Significantly, 239 patent applications have either been set aside/ withdrawn/ amended, based on the prior art evidence present in the TKDL database.

Summary

- Intellectual property rights (IPRs) are the rights given to persons over the creations of their minds. They usually give the creator an exclusive right over the use of his/her creation for a certain period of time.
- In India, the law relating to patents is contained in the Patents Act, 1970. Patent is granted for both product and process for limited period i.e. 20 years from the date of filing.
- Patent gives monopolistic rights to its owner. It has to be renewed every year by paying the renewal fee.
- A trade mark helps consumers identify and purchase a product or service because its nature and quality, indicated by its unique trade mark, meets their needs.
- The registration procedure in India is based on the ‘first to file’ system. It is therefore important that the rights holder applies for the registration of its mark as soon as possible. A Trade Mark/Service Mark is valid for a period of 10 years.
- Copyright law protects the expression of an idea. Not the idea itself. The registration of copyright is not compulsory but advisable.
- Geographical Indication (GI) suggests to consumers that the goods come from an area where a given quality, reputation or other characteristics of the goods is essentially attributable to their geographic origin.
- A Geographical Indication is registered for a period of 10 years and the registration may be renewed from time to time for a period of 10 years at a time. The registration of GI is not compulsory but advisable in India.
- Trade Secret relates to business information not known or disclosed to the public.
- There is no statute or legislation that governs the protection of trade secrets in India. However, rights in respect of trade secrets are enforced through the Contract Law (Indian Contract Act, 1872) principles of Equity or by way of common law for breach of confidence.
- The Traditional Knowledge Digital Library (TKDL) protects traditional knowledge, which will safeguard the misappropriation of traditional knowledge as well as promote further research and development of products and services based on traditional knowledge.

Unit 04: Intellectual Property Rights

- The Traditional Knowledge Digital Library (TKDL) provides information on TK existing in India, in languages and a format understandable by patent examiners at international patent offices.
- CSIR recently celebrated 20 years of India's Traditional Knowledge Digital Library, the first of its kind globally.

Keywords

Copyright: It signifies the work originated with the author.

Geographical Indication: It is a status accorded to a good which is unique to a particular region or area, and are originated from there.

Intellectual Property (IP): It refers to the intangible assets (creations of the mind: inventions, literary and artistic works, and symbols, names, images, and designs used in commerce) created by the human mind.

Patent: It is an exclusive statutory right granted to the inventor for his invention, which is either a product or a process that provides, in general, a new way of doing something, or offers a new technical solution to a problem.

Trademark: It means a mark capable of being represented graphically and which is capable of distinguishing the goods or services of one person from those of others and may include shape of goods, their packaging and combination of colors.

Trade Secret: It is any valuable information that is not publicly known and for which the owner has taken "reasonable" steps to maintain secrecy.

Traditional Knowledge: It is a valuable yet vulnerable asset to indigenous and local communities who depend on TK for their livelihood.

Traditional Knowledge Digital Library (TKDL): The TKDL contains documentation of publicly available traditional knowledge (TK) that:

- relates to Ayurveda, Unani, Siddha and Yoga.
- is in digitized format.
- is available in five languages: English, German, French, Japanese and Spanish.

Self Assessment

1. ----- are considered as territorial rights.
 - A. Copyrights
 - B. Patents rights
 - C. Trade marks rights
 - D. Intellectual property rights
2. Patent gives ----- to its owner to exclude others from making, using, selling, offering for sale or importing the product or the process for producing the product without his/her/its consent.
 - A. monopolistic rights
 - B. territorial rights
 - C. personal rights
 - D. positive rights
3. The mere discovery of a new form of a known substance which does not result in the enhancement of the known efficacy of that substance:
 - A. Is patentable invention
 - B. Is non-patentable invention

4. The limitation period for instituting suit for the patent infringement is ----- from the date of infringement.
- A. 3 years
 - B. 3 months
 - C. 1.5 years
 - D. 6 months
5. A ----- is a sign capable of distinguishing the goods or services of one enterprise from those of other enterprises.
- A. Trademark
 - B. Patent
 - C. Copyright
 - D. All of above
6. The registration of a trade mark is compulsory as per the Trade Marks Act, 1999.
- A. True
 - B. False
7. A company can get its trademark registered in any of the following form.
- A. Numerals
 - B. Sound
 - C. Book
 - D. Poem
8. If a company starts to make biscuits by the name of Parle-J, it would be an infringement of which of the following right of Parle-G?
- A. Copyright
 - B. Trademark
 - C. Patent
 - D. Trade Secret
9. Lifetime of the author plus sixty years from the beginning of the calendar year next following the year in which the author dies is the term of copyright of the following work:
- A. Cinematograph films
 - B. Sound records
 - C. Musical works
 - D. Government work
10. Until sixty years from the beginning of the calendar years next following the year in which the works is first publish is the term of copyright of the following work:
- A. Literary works
 - B. Dramatic works
 - C. Musical works
 - D. Posthumous works

11. A Geographical Indication is registered for a period of -----.
- A. 10 years
 - B. 20 years
 - C. 60 years
 - D. 30 years
12. The GI of “Feni” is provided to which of the following states/union territory of India?
- A. Goa
 - B. Odisha
 - C. Assam
 - D. West Bengal
13. “Makrana marble” is registered as GI by Rajasthan. It is covered under which of the following type of goods within the ambit of the Geographical Indications of Goods (Registration and Protection) Act, 1999 (GI Act)?
- A. Agricultural goods
 - B. Natural goods
 - C. Handicrafts
 - D. Food stuff
14. Coca Cola Formula to make Coca Cola drink is an example:
- A. Geographical Indication
 - B. Trade Secret
 - C. Traditional knowledge
 - D. Patent
15. The TKDL contains documentation of publicly available traditional knowledge (TK) that relates to:
- A. Ayurveda
 - B. Unani
 - C. Siddha
 - D. All of above

Answers for Self Assessment

1. B	2. A	3. B	4. A	5. A
6. B	7. A	8. B	9. C	10. D
11. A	12. A	13. B	14. B	15. D

Review Questions

1. What are Intellectual Property Rights (IPRs)? State the types of IPRs as per TRIPS.
2. What do you mean by Patent? Discuss its features and importance.

3. Discuss the criteria based on which patent is granted under the Patents Act, 1970.
4. State the non-patentable inventions as per the Patents Act, 1970.
5. What is meant by Infringement of a Patent? Write the remedies available in case of Infringement of a Patent.
6. Define a trade mark. Discuss the procedure for registration of a trade mark.
7. Illustrate the grounds for accepting a trade mark for registration.
8. What are Copyrights? Explain the registration procedure of copyrights in India along with the duration of various registered copyrights.
9. When a copyright is infringed? Discuss.
10. Illustrate the meaning and importance of Geographical Indications. Explain the registration Procedure of a Geographical Indication.
11. Explain the remedies available in case of infringement of a GI as per Sec. 67 of the Geographical Indications of Goods (Registration and Protection) Act, 1999 (GI Act).
12. What do you mean by Trade Secret? Discuss its key features and requisites.
13. How are Trade Secrets Protected?
14. Discuss about the Traditional Knowledge Digital Library (TKDL) in detail.



Further Reading

<https://www.icsi.edu/media/webmodules/publications/9.4%20Intellectual%20Property%20Rights.pdf>

https://www.indiacode.nic.in/handle/123456789/1981?view_type=browse&sam_handle=123456789/1362

<https://ipindia.gov.in/the-registration-process-gi.htm>

https://ipindia.gov.in/writereaddata/Portal/Images/pdf/GI_Application_Register_10-09-2019.pdf

https://ipindia.gov.in/writereaddata/Portal/Images/pdf/Final_FREQUENTLY_ASKED_QUESTIONS_-PATENT.pdf

<https://www.mondaq.com/india/trademark/1020686/significance-of-intellectual-property-rights-in-current-era>

<https://legislative.gov.in/sites/default/files/A1999-48.pdf>

<http://www.tkdl.res.in/tkdl/langdefault/common/Home.asp?GL=Eng>

https://www.indiacode.nic.in/handle/123456789/1981?view_type=browse&sam_handle=123456789/1362

<https://www.indiacode.nic.in/handle/123456789/1367?locale=en>

<https://www.indiacode.nic.in/handle/123456789/1993?locale=en>

Unit 05: The Negotiable Instruments Act, 1881

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Objectives

After studying this unit, you will be able to:

- explain the meaning and characteristics of negotiable instruments.
- review the classification of negotiable instruments.
- illustrate the various negotiable instruments as per its classification.
- explain the meaning and essentials of promissory note, bill of exchange and cheque.
- discuss the concept of crossing of cheques.
- review the differences between the promissory note, bill of exchange and cheque.
- review the importance of promissory note, bill of exchange and cheque in the Business world.

Introduction

Negotiable instruments are commercial documents that are used as means of payment of goods and services. They are the documents of certain type used in the commercial transactions and monetary dealings and are significant part of the modern business world. The need to pay for goods and services in physical cash is obviated by using negotiable instruments.

The law dealing with negotiable instruments in India is known as the Negotiable Instruments Act, 1881. The Negotiable Instruments Act, 1881, defines and amends the law relating to Promissory Notes, Bills of Exchange and Cheques. The main objective of the Act is to legalize the system by which instruments contemplated by it could pass from hand to hand by negotiation like any other goods. The Act applies to the whole of India. The provisions of this Act are also applicable to Hundis, unless there is a local usage to the contrary.

In this unit, meaning and essentials of negotiable instruments, parties involved in negotiable instruments, types of negotiable instruments along with their meaning and essentials, crossing of cheques, and difference between promissory note, bill of exchange, and cheque are discussed.

5.1 Negotiable Instruments: Meaning and Definition

Negotiable Instrument: Meaning

Negotiable instrument is an instrument which is freely transferable (by customs of trade) from one person to another by mere delivery or by indorsement and delivery. The property in such instrument passes to bonafide transferee for value.



Examples

Bill of Exchange, Promissory Note; and Cheque

Negotiable Instruments: Important terms

It is extremely important to understand the following terms to have clear insights about meaning of a negotiable instrument.

Negotiable

It means 'transferable by delivery'.

Instrument

It means a written document which creates right in favour of some person.

Negotiable Instrument

It means 'a written document which creates a right in favour of somebody and is freely transferable by delivery or by indorsement and delivery.'

Negotiable Instruments: Definition

"A negotiable instrument" means a promissory note, bill of exchange or cheque payable either to order or to bearer.

- Sec. 13

"It is written instrument that is signed by the maker or drawer, includes an unconditional promise or order to pay a specific sum of money, it is payable on demand or at a definite time, and is payable to order or to bearer."

- Black's Law Dictionary

Negotiable Instruments: Conditions of Negotiability

- Instrument should be freely transferable.
- The person who takes it for value and in good faith is not affected by the defect in the title of the transferor.
- Such a person can sue upon the instrument in his own name.

Negotiable Instruments: Parties (Sec. 7)

"Drawer" and Drawee"

The maker of a bill of exchange or cheque is called the "drawer"; the person thereby directed to pay is called the "drawee".

"Drawee in case of need"

When in the bill or in any indorsement thereon the name of any person is given in addition to the drawee to be resorted to in case of need, such person is called a "drawee in case of need".

"Acceptor"

After the drawee of a bill has signed his assent upon the bill, or, if there are more parts thereof than one, upon one of such parts, and delivered the same, or given notice of such signing to the holder or to some person on his behalf, he is called the "acceptor".

"Acceptor for honour"

Unit 05: The Negotiable Instruments Act, 1881

When a bill of exchange has been noted or protested for non-acceptance or for better security, and any person accepts it supra protest for honour of the drawer or of any one of the indorsers, such person is called an "acceptor for honour".

"Payee"

The person named in the instrument, to whom or to whose order the money is by the instrument directed to be paid, is called the "payee".

5.2 Negotiable Instruments: Characteristics

1. Freely transferable
2. Transfer of absolute and good title
3. Written Instrument
4. Unconditional order or promise
5. Only for money
6. Time of payment
7. Involve certain payee
8. Signature
9. Delivery of Instrument
10. Stamping
11. Transferee can sue in his own name without giving notice to the debtor

1. Freely transferable

- Negotiable instrument is freely transferable from one person to another without any formality.
- The property (right of ownership) in these instruments passes by either indorsement and delivery (in case it is payable to order) or by delivery merely (in case it is payable to bearer) and no further evidence of transfer is needed. Thus, True owner could transfer the property (Right of ownership) by mere delivery (Bearer instrument) or indorsement & delivery (Order instrument) without formalities.
- The holder in due course is not affected by defective title of the transferor or of any other party.
- No notice is required to give to previous holder.

Negotiation by delivery (Sec. 47) (in case of Bearer instruments)

Subject to the provisions of section 58, a promissory note, bill of exchange or cheque payable to bearer is negotiable by delivery thereof.

Exception.-- A promissory note, bill of exchange or cheque delivered on condition that it is not to take effect except in a certain event is not negotiable (except in the hands of a holder for value without notice of the condition) unless such event happens.

(a) Apple, the holder of a negotiable instrument payable to bearer, delivers it to Banana's agent to keep for Banana. The instrument has been negotiated.

(b) Apple, the holder of a negotiable instrument payable to bearer, which is in the hands of Apple's banker, who is at the time the banker of Banana, directs the banker to transfer the instrument to Banana's credit in the banker's account with Banana. The banker does so, and accordingly now possesses the instrument as Banana's agent. The instrument has been negotiated, and Banana has become the holder of it.



Did you know? What is meant by "Delivery" under the Negotiable Instruments Act, 1881?

Legal Aspects of Business

As per Sec. 46, the making, acceptance or indorsement of a promissory note, bill of exchange or cheque is completed by delivery, actual or constructive.

As between parties standing in immediate relation, delivery to be effectual must be made by the party making, accepting or indorsing the instrument, or by a person authorized by him in that behalf.

As between such parties and any holder of the instrument other than a holder in due course, it may be shown that the instrument was delivered conditionally or for a special purpose only, and not for the purpose of transferring absolutely the property therein.



Caution

- A promissory note, bill of exchange or cheque payable to bearer is negotiable by the delivery thereof.
- A promissory note, bill of exchange or cheque payable to order is negotiable by the holder by indorsement and delivery thereof.

Negotiation by indorsement (Sec. 48) (in case of order instruments)

Subject to the provisions of section 58, a promissory note, bill of exchange or cheque payable to order, is negotiable by the holder by endorsement and delivery thereof.



Did you know?

What is indorsement?

It means and involves the writing of something on the back of an instrument for the purpose of transferring the right, title and interest therein to some other person.

The person in whose favour the instrument is indorsed is called in "indorsee".



Example:

Peter held a cheque payable to order. Peter signed on the back of the cheque and wrote "pay Shyam" thereafter, Peter delivered the cheque to Shyam. It is negotiation by indorsement and delivery.



Did you know? Is there any possibility for conversion of indorsement in blank into indorsement in full?

The holder of a negotiable instrument indorsed in blank may, without signing his own name, by writing above the indorser's signature a direction to pay to any other person as indorsee, convert the indorsement in blank into an indorsement in full; and the holder does not thereby incur the responsibility of an indorser [Sec. 49].

Indorsement "in blank" and "in full": Sec. 16

(1) If the indorser signs his name only, the indorsement is said to be "in blank," and if he adds a direction to pay the amount mentioned in the instrument to, or to the order of, a specified person, the indorsement is said to be "in full", and the person so specified

"Indorsee".-is called the "indorsee" of the instrument.

(2) The provisions of this Act relating to a payee shall apply with the necessary modifications to an indorsee.

2. Transfer of absolute and good title

- Negotiability awards absolute and good title on transferee.
- Bona-fide holder also known as holder in due course gets a good and undisputable title to the instrument.
- However, the holder in due course should have no knowledge of the defects in title of previous holder.



Example:

Sumit issued a bearer cheque payable to Prince. It was stolen from Prince place by Amit, who passed it on to Raghu. If Raghu received it in good faith and for value and without knowledge of cheque having been stolen, he would be entitled to receive the amount of the cheque. Here, Raghu is the regarded as “Holder in Due Course”.

3. Written Instrument

A negotiable instrument is always in writing. This includes handwriting, typing, engraving, computer printout, etc.

4. Unconditional order or promise

In every negotiable instrument, there must be an unconditional order or promise for payment.

5. Only for money

The instrument must involves payment of a specified sum of money only and nothing else. Thus, one cannot make a negotiable instrument on assets, goods, securities, or any other thing except for money.

6. Time of payment:

The time of payment should be certain and therefore, the instrument should be payable at a time that is certain to arrive. If time of payment is mentioned as “when convenient” on the negotiable instrument, then the negotiable instrument will be considered as invalid instrument.



Task: When time of payment is linked to the death of person, will it be a negotiable instrument?

(Hint: Yes, as death is certain, though the time thereof is not)

7. Payee a certain person

- Payee means in whose favour the instrument is made.
- Payee can be individual, corporate, trade union, secretary, chairman etc.
- Payee can be more than 1 person.

8. Signature

A negotiable instrument must bear the signature of its maker or drawer.

9. Delivery of Instrument

Delivery of the instrument is essential. Thus, any negotiable instrument like a cheque or a promissory note is not complete till it is delivered to its payee.

10. Stamping

Stamping of bill of exchange and promissory note is mandatory requirement. This is required as per Indian Stamp Act, 1899. The value of stamp depends on the value of the bill of exchange or promissory note and the time of its payment.

11. Transferee can sue in his own name without giving notice to the debtor

In case of transfer his right: The transferee of a negotiable instrument is entitled to sue on the instrument in his own name in case of dishonour, without giving notice to the debtor of the fact that he has become holder.

In case of transfer or assignment of an ordinary “actionable claim” (i.e., a book debt evidenced by an entry by the creditor in his account book, under the transfer of property act:

Notice to the debtor is necessary in order to make the transferee entitled to sue in his own name.

5.3 Classification of Negotiable Instruments

1. Bearer Instruments

A bearer instrument means payable to any person whosoever bears it. A promissory note, bill of exchange or cheque is payable to the bearer when:

- It is expressed to be so payable or,
- The only or last indorsement is blank.

Provisions of RBI with regard to Bearer Instruments:

- No person other than RBI, Central Govt. can issue a promissory note payable to the bearer.
- A bill of exchange cannot be made payable to bearer on demand though it can be made payable to the bearer after a certain time.
- But a cheque (though bill of exchange) payable to the bearer on demand can be drawn on a person's account with a banker.

2. Order Instruments

A promissory note, bill of exchange or cheque is payable to order if:

- It is expressed to be so payable or
- It is expressed to be payable to a particular person and does not contain any words prohibiting transfer.

3. Inland Instruments (Sec. 11)

A promissory note, bill of exchange or cheque shall be deemed to be an inland instrument if it is drawn or made in India and made payable in, or drawn upon any person resident in India.

4. Foreign Instruments (Sec. 12)

An instrument which is not an inland instrument is deemed to be a foreign instrument. Following are the essentials of a foreign instrument:

- Must be drawn outside India and made payable outside or inside India or
- Must be drawn in India and made payable outside India and drawn on a person resident outside India.

5. Demand Instrument: (Sec 19)

Section 19 of the act provides that a promissory note or a bill of exchange in which no time for payment is specified is an instrument payable on demand.

Specimen of Demand Bill of Exchange

₹ 20,000/-	Mr. Surinder (Drawer) 381-L, Model Town, Jalandhar Punjab, India 28.9.2020
On demand pay to Mr. Deepak or order a sum of ₹ Twenty thousand only, value received.	
To Mr. Subash (Drawee) 46, Ranjit Avenue, Amritsar Punjab, India	Stamp Sd/- Mr. Surinder

6. Time Instruments

A note or a bill payable after a fixed period or after sight or on a specified day or on the happening of an event which is certain to happen is known as time instrument.

Specimen of Time Bill of Exchange

Stamp ₹ 20,000/-	Mr. Surinder (Drawer) 381-L, Model Town, Jalandhar Punjab, India 28.9.2020
Three months after date pay Mr. Deepak or order a sum of ₹ Twenty thousand only, for the value received.	
To Mr. Subash (Drawee) 46, Ranjit Avenue, Amritsar Punjab, India	Sd/- Mr. Surinder

7. Ambiguous Instruments (Sec. 17)

Where an instrument may be construed either as a promissory note or bill of exchange, the holder may at his election treat it as either, and the instrument shall be thenceforward treated accordingly.



Example

A promissory note addressed to a third person may be treated as a bill by such person by accepting it, while a bill not addressed to anyone may be treated as note.

8. Inchoate Stamped or Incomplete Instruments (Sec. 20)

When one person signs and delivers to another person a paper stamped in accordance with the law relating to the Negotiable Instruments, and either wholly blank or having something written thereon is an incomplete negotiable instrument.

He thereby gives prima facie authority to the holder thereof to make or complete, as the case may be, upon it a negotiable instrument, for any amount specified therein and not exceeding the amount covered by the stamp. The person so signing shall be liable upon such instrument, in the capacity in which he signed the same, to any holder in due course for such amount: provided that no person other than a holder in due course shall recover from the person delivering the instrument anything in excess of the amount intended by him to be paid thereunder.

9. Accommodation Bills (Sec. 43)

A negotiable instrument made, drawn, accepted, indorsed or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction. But if any such party has transferred the instrument with or without indorsement to a holder for consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor for consideration or any prior party thereto.

- A bill which is drawn, accepted or indorsed without consideration.
- Accommodating or accommodation party and Accommodated party.
- Nothing is on the face of accommodation bill to distinguish it from ordinary trade bill.
- Accommodation party is not liable on the instrument to the accommodated party.
- The accommodation party is liable to holder for value, though such holder is not a holder in due course.



Example:

Parrot was in need of money for 3 months. He induced his friend Quail to accept a bill of exchange drawn on him for 10,000 for 3 months. The bill was drawn and accepted by Quail.

Exception I.-- No party for whose accommodation a negotiable instrument has been made, drawn, accepted or indorsed can, if he have paid the amount thereof, recover thereon such amount from any person who became a party to such instrument for his accommodation.

Exception II.-- No party to the instrument who has induced any other party to make, draw, accept, indorse or transfer the same to him for a consideration which he has failed to pay or perform in full shall recover thereon an amount exceeding the value of

the consideration (if any) which he has actually paid or performed.

10. Bills in sets

Foreign bills are usually drawn in sets to avoid the danger of loss. Bill of exchange drawn in part are known as bills in sets. Each part is numbered and it contains a provision that it shall continue to be payable only as long as the others remain unpaid.

11. Fictitious Bill (Sec. 42)

When the name of drawer or payee or both are fictitious. The fictitious means:

- A non-existing person
- A pretended person i.e. a person other than the actual person intended by the parties.

12. The Documentary Bill and Clean Bill

A bill which has documents attached is called documentary bill. Thus, the documentary bills are accompanied by documents that confirm that a trade has taken place between the buyer and the seller of goods. Such documents include the invoices and other documents of title such as railway receipts, bill of lading, and lorry receipts issued by custom officials.

Documentary bills can be further classified as:

- a) Documents against acceptance (D/A) bills.
- b) Documents against payment (DIP bills).

Clean Bill

Clean bills are not accompanied by any documents that show that a trade has been taken place between buyer and seller.

13. Escrow

When a bill is indorsed or delivered to a person subject to the understanding that it will be paid only if certain conditions are fulfilled, such a bill is called an "escrow".

14. Undated bills and Note

If an instrument is expressed to be payable at a fixed period after the date is issued undated, or where the acceptance of an instrument payable at a fixed period after sight is undated, any holder may insert therein the true date of issue or acceptance and the instrument is payable accordingly.

5.4 Kinds of Negotiable Instruments

The following negotiable instruments are recognized by status i.e., by Sec. 13 of the Negotiable instruments Act, 1881:

- Promissory note
- Bill of Exchange
- Cheque

However, some negotiable instruments are recognized by usage or customs of trade:

 <i>Examples:</i>	Hundis, Bank notes, exchequer bills, share warrants, bearer debentures, dividend warrants, circular notes, and share certificates.

Promissory Note

A promissory note is an instrument in writing (not being a bank-note or a currency-note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument."

- Sec. 4

Unit 05: The Negotiable Instruments Act, 1881

Following will be taken as promissory notes because there is an express promise to pay. If Suresh writes:

"I promise to pay Rakesh or order 15,000"

"I acknowledge myself to be indebted to Rakesh for 25,000 to be paid on demand, for the value received."

But, the following are NOT promissory notes:

(i) "Mr B, I.O.U. (I owe you) 1000."

(ii) "I am liable to pay you 500".

(iii) "I promise to pay B 500 and all other sums which shall be due to him."

(iv) "I promise to pay B 500, first deducting thereout any money which he may owe me."

(v) "I promise to pay B 1500 on D's death, provided he leaves me enough to pay that sum."

(vi) "I promise to pay B 500 seven days after my marriage with C."

(vii) "I promise to pay B 500 and to deliver to him my white Maruti Car 1 January next."

Specimen of Promissory Note

Mr. Dinesh Kumar	Jalandhar, Punjab
55,000/-	28.5.2021
Four months after date, I promise to pay Mr. Ashok Chauhan or order a sum of Fifty five thousand only, for value received.	
To	
Mr. Ashok Chauhan	Mr. Dinesh Kumar
89, Ranjit Avenue, Amritsar	444, Model Town, Jalandhar
Punjab, India	Punjab, India
Sd/- Mr. Dinesh	

Promissory Note: Parties

(i) The maker: the person who makes the note promising to pay the amount stated therein.

(ii) The payee: the person to whom the amount of the note is payable.

(a) The indorser: the person who indorses the note in favour of another person.



If Ramesh (a payee on a note) indorses it in favour of Ranjan and Ranjan also indorses it in favour of Puneet, then Ramesh and Ranjan both are indorsers.

Example:

(b) The indorsee: the person in whose favour the note is negotiated by indorsement.

Promissory Note: Essentials

1. It must be in writing

- A promissory note has to be in writing.
- An oral promise to pay does not become a promissory note.
- The writing may be on any paper or book or 'bahi'.

2. It must contain a promise or undertaking to pay

- There must be a promise or an undertaking to pay.
- The undertaking to pay may be gathered either from express words or by necessary implication.
- A mere acknowledgement of indebtedness is not a promissory note, although it is valid as an agreement and may be sued upon as such.

*Example*

- “Mr. Bharat I.O.U 8,000. There is no promise to pay and the instrument is not a promissory note.

*Task:*

Arpit signs the instruments in the following terms:

- a) “Mr. Bhanu I owe you 8,000”.
- b) “I am liable to pay to B 1,500”.

Are the above both valid Promissory notes?

3. The promise to pay must be definite and unconditional.

The promise to pay must not depend upon the occurrence of some uncertain event, i.e., a contingency or the fulfillment of a condition.

*Task:*

- I promise to pay B 5,700 seven days after my marriage with Carol.
- I promise to pay B 5,500 on Dhruv's death.

Are above both valid promissory notes?

4. It must be signed by the maker

The promissory note should be duly authenticated by the 'signature' of the maker.

5. The maker must be a certain person

Alternative promisors are not permitted in law because of the general rule that “where liability lies no ambiguity must lie.”

6. The payee must be certain

- A note in favour of fictitious person is illegal and void.
- A note made payable to the maker himself is a nullity.

7. The sum payable must be certain

The amount payable must not be capable of contingent additions or subtractions.

*Case*

“I promise to pay Lavish 8,000 and all other sums which shall be due to him”.

Is it a valid promissory note?

8. The amount payable must be in the money (Indian currency)

A document containing a promise to pay to deliver a certain quantity of goods is not a valid note.

*Task*

I promise to pay Vivek 8,000 and to deliver to him my black horse on 1st January 2020.

Is it a valid promissory note?

9. Bank note or currency note is not a promissory note

Unit 05: The Negotiable Instruments Act, 1881

The Act states that a bank note or currency note is not a promissory note within the meaning of Sec. 4 of the Act.

10. Payable on demand or after a definite period of time

A promissory note should only be payable on demand or at fixed or determinable future time.

11. Not payable to bearer on demand

A promissory note cannot be made payable to a bearer, no matter whether it is payable on demand or after a certain time.

12. Other formalities

- Date
- Consideration
- Place
- Stamped

Bill of Exchange

"A bill of exchange is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument." - Sec. 5



Example:

- Mr. Sumit purchases goods from Mr. Amit for 1000/-
- Mr. Amit buys goods from Mr. Prince for 1000/-
- Then Mr. Amit may order Mr. Sumit to pay 1000/- to Mr. Prince, which will be nothing but a bill of exchange.

Specimen of Bill of Exchange

₹ 20,000/-	Mr. Surinder (Drawer) 381-L, Model Town, Jalandhar Punjab, India 28.9.2020
On demand pay to Mr. Deepak or order a sum of ₹ Twenty thousand only, for value received.	
To Mr. Subash (Drawee) 46, Ranjit Avenue, Amritsar Punjab, India	Stamp Sd/- Mr. Surinder

Accepted
Sd/- Subash
4.10.2020

Bill of Exchange: Parties

There are three parties involved in a bill of exchange

- Drawer: The person to whom the amount of the bill is payable.
- Drawee: The person on whom the bill is drawn. Thus, drawee is the person responsible for acceptance and payment of the bill.
- Payee: The person to whom amount of the bill is payable. It may be the drawer himself or any other person.
- Indorser: It is the person who endorses a bill.
- Indorsee: It is the person to whom the bill is negotiated by endorsement.



Caution:

- The drawer can also draw a bill in his own name.
- A bill can be time bill or demand bill.

Legal Aspects of Business

Bill of Exchange: Essentials

1. Writing: It must be in writing.
2. Order to pay: It must contain an order to pay.



Example:

"Mr. Akash, Please let the bearer have 7,000 and oblige." signed by Mr. Ravi.

3. Unconditional: The order to pay must be unconditional.
4. Signed: It must be signed by the drawer.
5. Parties should be certain: The drawer, drawee and payee must be certain.
6. Certain sum: The sum payable must be certain.
7. Money: The bill must contain an order to pay money only.
8. Acceptance: The bill must be accepted by the drawee.
9. Other formalities: It must comply with the formalities as regards to date, consideration, stamps, etc.

Cheque

"A cheque is a bill of exchange drawn on a specified banker, and not expressed to be payable otherwise than on demand". - Sec. 5

A cheque is a kind of bill of exchange but it has additional qualification namely-

- 1- It is always drawn on a specified banker and
- 2- It is always payable on demand without any days of grace.

Cheque: Specimen



Did you know? IFSC V. MICR

IFSC Indian Financial System Code	MICR Magnetic Ink Character Recognition
It is used to facilitate electronic money transfer between banks in India	MICR code is initiated to make check process in simple and faster
IFSC code is a 11-digit alphanumeric code	MICR code is a 9-digit numeric code
The first four alphabets represent the name of a bank and fifth is always zero(0) and the last six digits represent the bank branch	The first three digits represents the city, middle 3 digits represent the bank, and the last 3 digits represent the branch

Cheque: Parties

Unit 05: The Negotiable Instruments Act, 1881

- **Drawer:** Drawer is the party who draws the cheque upon a specified banker. He is the maker of the cheque and the person who is directing the bank to pay a certain sum of money to a certain person or to the bearer.
- **Drawee:** Drawee is the party upon whom the cheque is drawn. It is always a bank in case of a cheque.
- **Payee:** Payee is the party who presents the cheque for payment. He/She is the person who receives money from the bank.

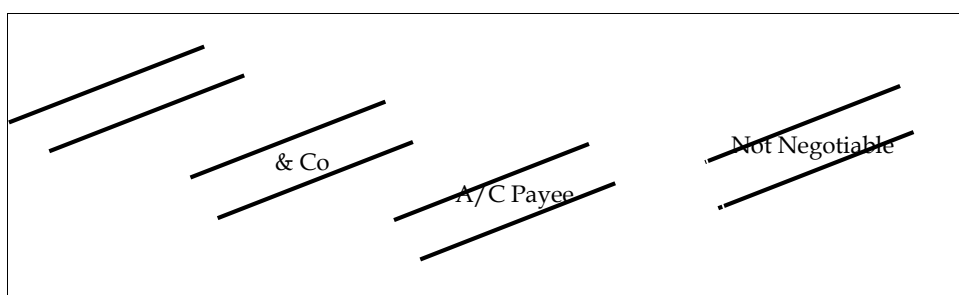
Essential Elements of Cheque

- **Writing:** A cheque must be in writing.
- **Unconditional order:** It should contain an unconditional order. Generally, the order to bank is expressed by the word "pay". If the word "please" precedes "pay" the document will not be regarded as invalid merely on this account.
- **Drawn on a specified banker only:** It is always drawn by a customer on his or her specified bank.
- **Signed:** It must be signed by the customer.
- **Payable on demand:** It is always payable on demand.
- **Certain amount:** It should contain an exact amount to be paid.
- **Certain payee:** The payee must be certain person whom the payment of cheque is to be made.
- **Duly dated:** A cheque should be duly dated.

Cheque: Crossing [Sec. 123-126]

Crossing is a unique feature associated with a cheque affecting to a certain extent the obligation of the paying banker and also its negotiable character. It is a peculiar method of modifying the instrument to the banker for payment of the cheque. Crossing on cheque is a direction to the paying banker by the drawer that payment should not be made across the counter.

- **General crossing:** Where a cheque bears across its face an addition of the words "and company" or any abbreviation thereof, between two parallel transverse lines, or of two parallel transverse lines simply, either with or without the words "not negotiable", that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed generally Sec. 123.



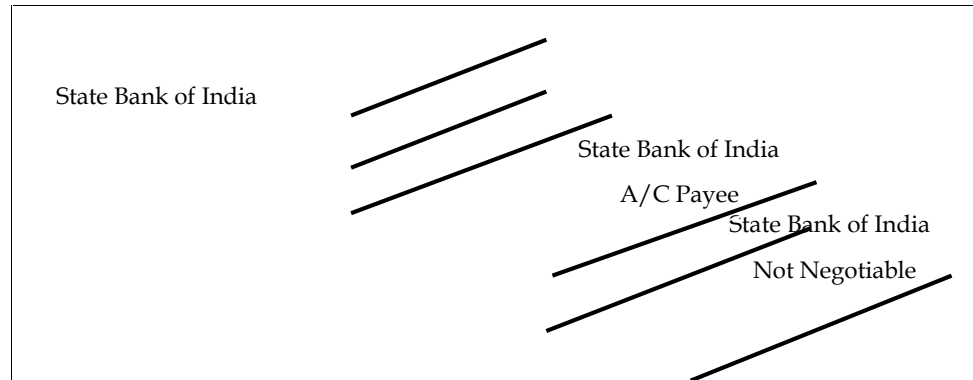
Specimen of General Crossing

Essentials For General crossing:

- ✓ Two transverse parallel lines
- ✓ Lines should be drawn on the top left corner of the cheque
- **Special crossing:** Where a cheque bears across its face an addition of the name of a banker, either with or without the words "not negotiable", that addition shall be deemed a

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crossing, and the cheque shall be deemed to be crossed specially, and to be crossed to that banker Sec. 124.



Specimen of Special Crossing

Essentials of Special Crossing:

- ✓ Two transverse lines are not necessary for a special crossing
- ✓ The name of the banker must be necessarily specified across the face of the cheque
- ✓ It must appear on the left hand side of the cheque
- Crossing after issue: Sec. 125
- ✓ Where a cheque is uncrossed, the holder may cross it generally or specially.
- ✓ Where a cheque is crossed generally, the holder may cross it specially.
- ✓ Where a cheque is crossed generally or specially, the holder may add the words "not negotiable".
- ✓ Where a cheque is crossed specially, the banker to whom it is crossed may again cross it specially to another banker, his agent, for collection.

5.5 Promissory Note v/s Bill of Exchange v/s Cheque

Basis	Promissory Note	Bill of Exchange	Cheque
Parties	2 Parties: Maker and Payee.	3 Parties: Drawer, Drawee and Payee.	3 Parties: Drawer, Banker and Payee.
Nature	Contains an unconditional promise by maker to pay a certain payee.	Contains an unconditional order by Drawer to Drawee to make payment to certain payee.	Drawn on a specified banker to pay on demand.
Acceptance	Not necessary.	Necessary, if the bill is payable after sight.	Not necessary.
Liability	Liability of the maker is primary and absolute.	Liability of Drawer is conditional and secondary. It will arise upon non-payment by Drawee.	Liability of Drawer is conditional and secondary. It will arise upon non-payment by Banker.
Notice of Dishonor	Not necessary.	Necessary.	Not necessary.
Payable	On demand or after a specified time. Cannot be	On demand or after a specified time. Cannot be	On demand, even to bearer, if so made.

Unit 05: The Negotiable Instruments Act, 1881

	made payable to bearer on demand or even after certain period.	made payable to bearer on demand.	
Crossing	Not possible.	Not possible.	Possible
Noting and protesting in case of dishonor.	Not required.	Required to establish the fact of dishonor.	Not required.
Grace Period	(3 days Grace period) Available, if payable after specified time.	(3 days Grace period) Available, if payable after specified time.	Not available.
Other features	Number, Date, Place are not essential. Must be stamped.	Number, Date, Place are not essential. Must be stamped.	Number, Date, Place are essential. Need not to be stamped.

Summary

- The Negotiable Instruments Act, 1881 deals with the laws relating to bills of exchange, promissory notes and cheques.
- “Negotiable” means ‘transferable by delivery’ and “Instrument” means a written document which creates right in favour of some person.
- Negotiable Instrument means a written document which creates a right in favour of somebody and is freely transferable by delivery or by indorsement and delivery.
- A bearer instrument means payable to any person whosoever bears it.
- An order instrument means a promissory note, bill of exchange or cheque is payable to order if it is expressed to be payable to a particular person.
- A promissory note or a bill of exchange in which no time for payment is specified is an instrument payable on demand.
- A note or a bill payable after a fixed period or after sight or on a specified day or on the happening of an event which is certain to happen is known as time instrument.
- Where an instrument may be construed either as a promissory note or bill of exchange, the holder may at his election treat it as either, and the instrument shall be thenceforward treated accordingly.
- A promissory note is an instrument in writing containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument.
- A bill of exchange is defined as “an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument”.
- A cheque is a bill of exchange drawn on a specified banker, and not expressed to be payable otherwise than on demand”.
- Crossing is a unique feature associated with a cheque affecting to a certain extent the obligation of the paying banker and also its negotiable character.

Keywords

- **Accommodation Bill:** It is a negotiable instrument made, drawn, accepted, indorsed or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction.
- **Bill in sets:** Bill of exchange drawn in part are known as bills in sets. It is generally used in International trade.
- **Bill of Exchange:** A bill of exchange is an instrument in writing containing an unconditional to the order of a certain person or to the bearer of the instrument.
- **Cheque:** A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable.
- **Holder:** It is either the original payee or any other person in whose favour the note has been endorsed.
- **Escrow:** When a bill is indorsed or delivered to a person subject to the understanding that it will be paid only if certain conditions are fulfilled, such a bill is called an “escrow”.
- **Indorser:** The person who endorses the note in favour of another person.
- **Indorsee:** The person in whose favour the note is negotiated by endorsement.
- **Negotiable Instrument:** Means a promissory note, bill of exchange or cheque payable either to order or to bearer.
- **Payee:** The person to whom the amount of the note is payable.
- **Promissory Note:** A promissory note is an instrument in writing containing an unconditional undertaking signed by the maker to pay a certain sum of money only to or to the order of a certain person or to the bearer of the instrument.

Self-Assessment

1. Cherry, the holder of a negotiable instrument payable to bearer, delivers it to Lichee's agent to keep for Lichee. The instrument has been _____ in such case.
A. Negotiated by mere delivery
B. Negotiated by indorsement and delivery
C. Negotiated by indorsement
D. None of above
2. _____ involves the writing of something on the back of an instrument for the purpose of transferring the right, title and interest therein to some other person.
A. Delivery
B. Negotiation
C. Indorsement
D. Negotiable Instrument
3. Pinky held a cheque payable to order. Pinky signed on the back of the cheque and wrote “pay Shanky” thereafter, Pinky delivered the cheque to Shanky. It is negotiation by _____.
A. Delivery
B. Indorsement
C. Indorsement and delivery
D. All of above

4. An Order instrument can be negotiated by:
- A. Mere delivery
 - B. Indorsement
 - C. Indorsement and delivery
 - D. All of above
5. Sahil issued a bearer cheque payable to Harmeet. It was stolen from Harmeet place by Ankush, who passed it on Rajeev. In such a case, Rajeev will be termed as holder in due course only if:
- A. he has received the instrument in good faith
 - B. he has received the instrument for value
 - C. he did not have knowledge of the defects in title of Ankush
 - D. All of above
6. Any individual or body corporate can issue a promissory note payable to the bearer.
- A. True
 - B. False
7. A promissory note or a bill payable on the happening of an event which is certain to happen is known as_____.
- A. Order Instrument
 - B. Time Instrument
 - C. Bearer Instrument
 - D. Demand Instrument
8. A promissory note addressed to a third person may be treated as a bill by such person by accepting is an example of:
- A. Ambiguous Instrument
 - B. Inchoate Instrument
 - C. Accommodation Instrument
 - D. Fictitious Instrument
9. A bill which is drawn, accepted or indorsed without consideration with a motive to financially assist a known person for certain period is known as:
- A. Ambiguous Bill
 - B. Inchoate Bill
 - C. Accommodation Bill
 - D. Fictitious Bill
10. When a bill is indorsed or delivered to a person subject to the understanding that it will be paid only if certain conditions are fulfilled, such a bill is called an _____.
- A. Escrow
 - B. Allonge
 - C. Clean Bill

D. Documentary Bill

11. If Kabir (a payee on a note) indorses it in favour of Pritam and Pritam further indorses it in favour of Puneet, then Puneet will be -----.

- A. Indorser
- B. Indorser and payee
- C. Indorsee and payee
- D. Maker

12. Jasdeep signs one promissory note thereby writing as "Mr. Sanjay, I owe you 44,000". Discuss the validity of such promissory note.

- A. It is a valid note as there is an acknowledgement of debt.
- B. It is an invalid note as there is no promise to pay.
- C. It is a valid note as it is fulfilling the essentials of a valid promissory note.
- D. It is an invalid note as there is no order to make payment.

13. Mahesh signs a promissory note thereby writing as "I promise to pay Lakhan 75,000 on Meera's death, provided Meera leaves me enough to pay that sum. Is it a valid promissory note?

- A. Yes, it is valid promissory note as promise to pay is definite.
- B. Yes, it is valid promissory note as promise to pay is unconditional.
- C. No, it is invalid promissory note as promise to pay depends on a contingency.
- D. No, it is invalid promissory note as there is no definite promise to pay.

14. Salman draws a bill on Sharukh thereby ordering him to pay Tiger Shroff 80,000 and to deliver to him his black horse on 1st January 2022. The bill was prepared on a stamped paper and accepted by Sharukh. Is it a valid Bill?

- A. Yes, it is a valid bill as drawer, drawee and payee are certain.
- B. Yes, it is a valid bill as it is containing a clear and unconditional order to pay.
- C. Yes, it is a valid bill as it is stamped and accepted by drawee.
- D. No, it is an invalid bill as the bill must contain an order to pay money only.

15. A Cross cheque is:

- A. Which can be encashed at counter
- B. Which can be encashed only by bearer
- C. Which can be encashed only by RBI
- D. Which can be encashed only through a bank

Answers for Self Assessment

1. A	2. C	3. C	4. C	5. D
6. B	7. B	8. A	9. C	10. A
11. C	12. B	13. C	14. D	15. D

Review Questions

1. What do you mean by negotiable instruments? Explain the essential elements of a valid negotiable instrument.
2. Discuss the instruments which are recognized as negotiable instruments by the Negotiable Instruments Act, 1881 in detail.
3. What is a bill of exchange? Describe its characteristics. How does a promissory note differ from a bill of exchange?
4. "A cheque is a bill of exchange drawn on a banker". Comment.
5. Describe briefly the concept of 'general' and 'special' crossing and "crossing after the issue of a cheque".
6. Define a promissory note. What are the parties of a promissory note. Also, discuss the essential elements of a promissory note.
7. Akshay signs the instruments in the following terms:
 - a) "I promise to pay Twinkle or order 500".
 - b) "I acknowledge myself to be indebted to Shilpa for 1,000 to be paid on demand, for value received".
 - c) "I promise to pay B 55,000 on Dhruv's death, provided Dhruv leaves me enough to pay that sum".
 - d) "I promise to pay Vita 5,800, first deducting any money which he may owe me"
 Are the above promissory notes valid? State reasons.
8. Write short notes on the followings:
 - a) Bills in sets
 - b) Accommodation bill
 - c) Escrow
 - d) Documentary Bill
 - e) Clean Bill
9. Piyush writes "I promise to pay "Brahmin" a sum of 2,000, seven days after my marriage with Cherry. Is this a promissory note?
10. Billu draws for his own accommodation a bill for 1,000 on Chikku, and after acceptance by Chikku indorses it to Lucky as security for 500. Chikku is adjusted insolvent. Discuss the rights of Lucky.

[Hint: Where there is partial absence or failure of money consideration for which a person signed a negotiable instrument, the same rules as apply to total absence or failure of consideration will apply. Thus, the parties standing in immediate relation to each other cannot recover more than actual consideration, but this rule does not apply to a holder in due course. So, Lucky can recover 500 from Billu.
11. Explain the essential elements of a valid bill of exchange.
12. What is a cheque? Explain the essential elements of a valid cheque.



Further Reading

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Web Links

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<https://www.incometaxindia.gov.in/pages/acts/negotiable-instruments-act.aspx>

Unit 06: The FEMA Act, 1999

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Objectives

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6.1 FEMA: Preliminaries

6.2 FEMA: Definitions

6.3 FEMA: Major Provisions

6.4 Limits on possession and retention of foreign currency or foreign coins, under Foreign Exchange Management (Possession & Retention of Foreign Currency) Regulations, 2015.

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6.7 Appointment of Adjudicating Authority: Sec. 16

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Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Reading

Objectives

After studying this unit, you will be able to:

- review the objects, scope and importance of FEMA, 1999.
- illustrate the meaning of various prominent terms of FEMA, 1999.
- explain the major provisions and regulations of FEMA, 1999.
- review the importance of FEMA, 1999 in promoting external trade and development of foreign exchange market in India.

Introduction

The Foreign Exchange Management Act (FEMA), 1999 has abrogated the Foreign Exchange Regulation Act (FERA), 1973. The FEMA amends and unifies the law relating to foreign exchange with the objective-

1. to ease external trade and payments, and
2. to facilitate and promote the orderly development and maintenance of foreign exchange market in India.

The FEMA was passed by Lok Sabha on December 2, 1999. It came into force: 1st of June 2000. It has total Sections: 49 (Divided into 7 Chapters). It extends to the whole of India [Sec. 1(2)]. It also applies to:

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- 1) All branches, offices and agencies outside India owned or controlled by a person resident in India (PRI), and,
- 2) Any contravention committed outside India, by any person to whom this Act applies. [Sec. 1(3)].

It shall come into force on such date 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.

6.1 FEMA: Preliminaries**FERA V. FEMA**

- In FEMA, only the specified acts related to foreign exchange are regulated. While in FERA anything and everything that has to do with foreign exchange was controlled.
- The objective of FEMA is to facilitate trade, while that of FERA is to prevent its misuse.
- FEMA is a much smaller enactment only 49 sections against 81 sections of FERA.

FEMA: Objectives

- To facilitate/promote external trade and payments.
- To promote the orderly development and maintenance of foreign exchange market in India.

FEMA: Structure

- Foreign exchange management Act 1999 provide only basic legal framework.
- Section 46: Empowers central government to make rules.
- Section 47: Empowers RBI to make regulations.

FEMA: Central Legislation

It deals with:

- inbound investments into India,
- outbound investments from India, and
- trade and business between India and the other countries.

FEMA: Provisions

Foreign Exchange Management Act, 1999 makes provisions for dealings in foreign exchange through Current Account Transactions and Capital Account Transactions.

FEMA: RBI's Role

- Foreign Exchange Management Act, 1999 envisages that RBI shall have a controlling role in management of foreign exchange.
- Since RBI cannot directly handle foreign exchange transactions, it authorizes "Authorized Persons" to deal in foreign exchange.

6.2 FEMA: Definitions

1. Authorized person
2. Foreign exchange
3. Foreign security
4. Person
5. Person resident in India
6. Person resident outside India
7. Non-resident Indian
8. Repatriate to India
9. Person of Indian Origin

10. Capital Account Transaction
11. Current Account Transaction



1. Authorized Person [u/s 2(c)]

It means an/a-

1. Authorized dealer,
2. Money changer,
3. Offshore banking unit or
4. Any other person for the time being authorized by RBI to deal in -
 - foreign exchange or,
 - foreign security



Who is an Authorized dealer?

An Authorized Dealer (AD) is any person specifically authorized by the Reserve Bank under Section 10(1) of FEMA, 1999, to deal in foreign exchange or foreign securities (the list of ADs is available on www.rbi.org.in) and normally includes banks.

Who is a Money changer?

Authorized Money Changers/ AMCs are entities who are authorized by the Reserve Bank of India as per Section 10 of the Foreign Exchange Management Act of 1999. Accordingly, an AMC may either be a Restricted Money Changer (RMC) or a Full Fledged Money Changer (FFMC). A license is required by FFMCs to purchase foreign exchange from residents and non-residents visiting India and to sell foreign exchange for specifically approved purposes.



- Aarohi Forex Pvt. Ltd
- Ambika Forex Pvt. Ltd

What is Offshore Banking Unit?

'Offshore Banking Unit' means a branch of a bank in India located in the Special Economic Zone and holds an authorization issued under clause (a) of sub-section (1) of section 23 of the Banking Regulation Act, 1949 (10 of 1949);

An offshore banking unit (OBU) is a bank shell branch, located in another international financial center. For instance, a London-based bank with a branch located in Delhi. Offshore banking units make loans in the Eurocurrency market when they accept deposits from foreign banks and other OBUs. Eurocurrency simply refers to money held in banks located outside of the country which issues the currency.

Authorized person: Sec. 10

Granting of authorization on application

The Reserve Bank may, on an application made to it in this behalf, authorize any person to be known as authorized person to deal in foreign exchange or in foreign securities, as an authorized dealer, money changer or offshore banking unit or in any other manner as it deems fit [Sec. 10(1)].

An authorization under this section shall be in writing and shall be subject to the conditions laid down therein [Sec. 10(2)].

Revocation of authorization

An authorization granted under sub-section (1) may be revoked by the Reserve Bank at any time if the Reserve Bank is satisfied that--

- (a) it is in public interest so to do; or
- (b) the authorized person has failed to comply with the condition subject to which the authorization was granted or has contravened any of the provisions of the Act or any rule, regulation, notification, direction or order made thereunder:

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Provided that no such authorization shall be revoked on any ground referred to in clause (b) unless the authorized person has been given a reasonable opportunity of making a representation in the matter [Sec. 10(3)].

Compliance with Conditions

An authorized person shall, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time, think fit to give, and, except with the previous permission of the Reserve Bank, an authorized person shall not engage in any transaction involving any foreign exchange or foreign security which is not in conformity with the terms of his authorization under this section Sec. 10(4)].

Declaration

An authorized person shall, before undertaking any transaction in foreign exchange on behalf of any person, require that person to make such declaration and to give such information as will reasonably satisfy him that the transaction will not involve, and is not designed for the purpose of any contravention or evasion of the provisions of this Act or of any rule, regulation, notification, direction or order made thereunder, and where the said person refuses to comply with any such requirement or make only unsatisfactory compliance therewith, the authorized person shall refuse in writing to undertake the transaction and shall, if he has reason to believe that any such contravention or evasion as aforesaid is contemplated by the person, report the matter to the Reserve Bank [Sec. 10(5)].

Contravention

Any person, other than an authorized person, who has acquired or purchased foreign exchange for any purpose mentioned in the declaration made by him to authorized person under sub-section (5) does not use it for such purpose or does not surrender it to authorized person within the specified period or uses the foreign exchange so acquired or purchased for any other purpose for which purchase or acquisition or foreign exchange is not permissible under the provisions of the Act or the rules or regulations or direction or order made thereunder shall be deemed to have committed contravention of the provisions of the Act for the purpose of this section [Sec. 10(6)].

Obligation of Authorized Person

- General and Special Directions.
- Obtaining Declaration and information & refusal to deal.
- Doubtful transaction should be refused.
- Contemplated Transaction.

Effect of misuse

1. Does not use foreign exchange for purpose for which it was acquired or
2. Does not surrender it to authorized person within the specified period or
3. Uses the foreign exchange for any other purpose other than for which it was acquired.

RBI's powers to issue directions to authorized person: Sec. 11**Issue Direction**

The Reserve Bank may, for the purpose of securing compliance with the provisions of this Act and of any rules, regulations, notifications, or directions made thereunder, give to the authorized persons any direction in regard to making of payment or the doing or desist from doing any act relating to foreign exchange or foreign security.

Furnish Information

The Reserve Bank may, for the purpose of ensuring the compliance with the provisions of this Act or of any rule, regulation, notification, direction, or order made thereunder, direct any authorized person to furnish such information, in such manner, as it deems fit.

Penalty

The Reserve Bank may, for the purpose of ensuring the compliance with the provisions of this Act or of any rule, regulation, notification, direction, or order made thereunder, direct any authorized person to furnish such information, in such manner, as it deems fit.

Power of Reserve Bank to inspect authorized person: Sec. 12

(1) The Reserve Bank may, at any time, cause an inspection to be made, by any officer of the Reserve Bank specially authorized in writing by the Reserve Bank in this behalf, of the business of any authorized person as may appear to it to be necessary or expedient for the purpose of--

- (a) verifying the correctness of any statement, information or particulars furnished to the Reserve Bank;
- (b) obtaining any information or particulars which such authorized person has failed to furnish on being called upon to do so;
- (c) securing compliance with the provisions of this Act or of any rules, regulations, directions, or orders made thereunder.

(2) It shall be the duty of every authorized person, and where such person is a company or a firm, every director, partner or other officer of such company or firm, as the case may be, to produce to any officer making an inspection under sub-section (1), such books, accounts and other documents in his custody or power and to furnish any statement or information relating to the affairs of such person, company or firm as the said officer may require within such time and in such manner as the said officer may direct.

2. Foreign Exchange [u/s 2(n)]

It means foreign currency and includes the following:

- Deposits, credits and balance payable in foreign currency;
- Drafts, travelers' cheques, letters of credit or bill of exchanges-
 - ✓ drawn in Indian currency but payable in foreign currency and
 - ✓ drawn outside India but payable in Indian currency

3. Foreign security [u/s 2(o)]

It means any security in the form of -

- Shares, Stocks
- Bonds
- Debentures or any other instrument denominated or expressed in foreign currency and
- includes security expressed in foreign currency but where redemption or return is payable in Indian currency

4. Person [u/s 2(u)]

It includes-

- An individual
- Hindu undivided family
- Company
- Firm
- An Association of Persons (AOPs) or Body of Individuals (BOI) (whether incorporated or not)
- Further it includes any artificial person
- Any agency office or branch owned or controlled by such persons

5. Person resident in India [u/s 2(v)]

Residing in India for > 182 days during the course of preceding Financial Year but doesn't include:

a) Person who has gone out of India or stays outside India:

- for taking up employment
- for carrying business or vocation
- for any other purpose in such circumstances as would indicate his intention to stay outside India for uncertain period

Legal Aspects of Business

b) Also, person who has come to India or stays in India for any purpose but other than for:

- for taking up employment
- for carrying business or vocation
- for any other purpose in such circumstances as would indicate his intention to stay in India for uncertain period

Further resident in India includes-

- Any person or body corporate registered or incorporated in India
- an office branch or agency established
- In India (but owned or controlled by a person resident outside India)
- Outside India (but owned or controlled by a person resident in India)

6. Person resident outside India [u/s 2(w)]

- A person who is not resident in India.

7. Non-Resident Indian

It means a person resident outside India who is-

- A citizen of India
- A person of Indian origin



Kamlesh was working as a crew member on an Indian ship plying in foreign waters. During the year ended 31.03.2018, the ship did not touch the Indian coast, except for 180 days.

State the residential status for the assessment year 2018-19 and the taxability of his salary. State the reasons also.



- X got employment in Singapore during the previous year, 2017-18.
- He left for Singapore on August 9, 2017. He is an Indian citizen.

Determine the residential status and state the reasons for the Assessment Year 2018-19.

8. Person of Indian Origin (POI)

It means -

an individual not being a citizen of

- Pakistan or;
- Bangladesh

A) who at any time held an Indian passport or

B) who or either of his parents or grandparents were the citizen of India or;

C) who is a spouse of an Indian citizen or above-mentioned person

9. Repatriate to India [u/s 2(y)]

It means bringing into India the realized foreign exchange and :-

- The selling of foreign exchange to an authorized person in India in exchange for rupees, or
- The holding of realized amount in an account with an authorized person to the extent notified by the RBI, and
- Use of the realized amount for discharge of a debt or liability denominated in foreign exchange.
-

Realization and repatriation of foreign exchange: Sec. 8

Where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within specified period and in specified manner by the RBI.

Exemption from realization and repatriation in certain cases: Sec. 9

The provisions of sections 4 and 8 shall not apply to the following, namely:--

- (a) possession of foreign currency or foreign coins by any person up to such limit as the Reserve Bank may specify;
- (b) foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify;
- (c) foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is held outside India by any person in pursuance of a general or special permission granted by the Reserve Bank;
- (d) foreign exchange held by a person resident in India up to such limit as the Reserve Bank may specify, if such foreign exchange was acquired by way of gift or inheritance from a person referred to in clause (c), including any income arising therefrom;
- (e) foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank may specify; and
- (f) such other receipts in foreign exchange as the Reserve Bank may specify.

Period for surrender of realized foreign exchange

- (1) Foreign exchange due or accrued as remuneration for services rendered, whether in or outside India, or in settlement of any lawful obligation, or income on assets held outside India, or as inheritance, settlement, or gift, within seven days from the date of its receipt.
- (2) in all other cases, within a period of ninety days from the date of its receipt.

10. Capital Account Transaction [u/s 2(e)]

Capital Account transaction means a transaction which alters assets or liabilities including contingent liabilities outside India of person resident in India and vice-versa.

Capital account transactions: Sec. 6**Foreign Exchange Transaction through authorized person**

Any person may sell or draw foreign exchange to or from an authorized person for a capital account transaction subject to the provisions of sub-section (2) [Sec. 6(1)]

Specification of capital account transactions and limit

- The Reserve Bank may, in consultation with the Central Government, specify--
 - (a) any class or classes of capital account transactions, involving debt instruments, which are permissible;
 - (b) the limit up to which foreign exchange shall be admissible for such transactions;
 - (c) any conditions which may be placed on such transactions [Sec. 6(2)].

The Reserve Bank or the Central Government shall not impose any restrictions on the drawal of foreign exchange for payment due on account of amortization of loans or for depreciation of direct investments in the ordinary course of business.

- The Central Government may, in consultation with the Reserve Bank, prescribe--
 - (a) any class or classes of capital account transactions, not involving debt instruments, which are permissible;
 - (b) the limit up to which foreign exchange shall be admissible for such transactions; and
 - (c) any conditions which may be placed on such transactions.

Holding by a person resident in India

A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India [Sec. 6(4)].

Holding by a person resident outside India

A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India. [Sec. 6(5)].

Prohibition of establishment

- Without prejudice to the provisions of this section, the Reserve Bank may, by regulation, prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business [Sec. 6(6)].

For the purposes of this section, the term “debt instruments” shall mean, such instruments as may be determined by the Central Government in consultation with the Reserve Bank [Sec. 6(7)].

Section 6(3) of FEMA specifies the class of capital account transactions which are regulated by RBI.

Capital account transactions of a person may be classified under the following heads, namely-

A) Transaction, specified in Schedule-I, of a person resident in India

B) Transactions, specified in Schedule II, of a person resident outside India

Schedule I: Classes of capital account transactions of persons resident in India

- Investment in foreign securities
- Foreign currency loans raised in India and abroad
- Transfer of immovable property outside India
- Guarantees issued by a person resident in India in favor of a person resident outside India
- Export, import and holding of currency/currency notes
- Loans and overdrafts (borrowings) from a person resident outside India
- Maintenance of foreign currency accounts in India and outside India
- Taking out of insurance policy from an insurance company outside India
- Loans and overdrafts to a person resident outside India
- Remittance outside India of capital assets of a person resident in India
- Sale and purchase of foreign exchange derivatives in India and abroad and commodity derivatives abroad by a person resident in India

Schedule II: Classes of capital account transactions of persons resident outside India.

- Investment in India by a person resident outside India:
 - Issue of security by a body corporate or an entity in India and investment therein by a person resident outside India; &
 - Investment by way of contribution by a person resident outside India to the capital of a firm or a proprietorship concern or an association of persons in India.
- Acquisition and transfer of immovable property in India by a person resident outside India.
- Guarantee by a person resident outside India in favor of, or on behalf of, a person resident in India.

- d) Import and export of currency/currency notes into/from India by a person resident outside India. Deposits between a person resident in India and a person resident outside India.
- e) Foreign currency accounts in India of a person resident outside India.
- f) Remittance outside India of capital assets in India of a person resident outside India.

Capital Account Transactions – Prohibited

- a. no person shall undertake or sell or draw foreign exchange to or from an authorized person for any capital account transaction,
- b. no person resident outside India shall make investment in India, in any form, in any company or partnership firm or proprietary concern or any entity, whether incorporated or not, which is engaged or proposes to engage -
 - I. In the business of chit fund, or
 - II. As Nidhi Company, or
 - III. In agricultural or plantation activities, or
 - IV. In real estate business, or construction of farmhouses, or
 - V. In trading in Transferable Development Rights (TDRs)



For the purpose of this regulation, 'real estate business' shall not include development of townships, construction of residential/commercial premises, roads or bridges.



What are Nidhi Companies?

Nidhi Company is a type of Non-Banking Financial Company (NBFC). It is formed to borrow and lend money to its members. It inculcates the habit of saving among its members and works on the principle of mutual benefit. These companies typically operate in the southern part of the country. Nidhi Company isn't required to receive the license from Reserve Bank of India (RBI), hence it is easy to form. It is registered as a public company and should have "Nidhi Limited" as the last words of its name.

What are TDRs?

'Transferable Development Rights' (TDRs) means certificates issued in respect of category of land acquired for public purpose either by Central or State Government in consideration of surrender of land by the owner without monetary compensation, which are transferable in part or whole.



Sec. 6(3) is just for your reference. However, The Proviso i.e., Sec. 6(3) substituted by section 139, with effect from 15-10-2019).

11.Current Account Transactions: Sec. 5

Any person may sell or draw foreign exchange to or from an authorized person if such sale or drawal is a current account transaction. However, the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed.

Current account transactions are divided into 3 schedules in Current Account Transactions Rules:-

Schedule I – Prohibited Transactions.

Schedule II – Transactions requiring prior approval of Government of India.

Schedule III – Transactions requiring prior approval of RBI.

Schedule I: Prohibited Transactions.

- Remittance out of lottery winnings.
- Remittance of income from racing/riding etc., or any other hobby.

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- Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes etc.

Schedule II: Transactions requiring prior approval of Government of India.

- Cultural tours.
- Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping.

Schedule III: Transactions requiring prior approval of RBI.

- Gift remittance exceeding US\$ 5,000 per remitter/donor per annum.
- Donation exceeding US\$ 10,000 per remitter/ donor per annum.
- Release of exchange for meeting expenses for medical treatment abroad exceeding the estimate from the doctor in India or hospital or hospital/doctor abroad.

Remittances exceeding five percent of the investment brought into India or US\$ 1,00,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses.

Regulatory bodies

- Current Account transactions are freely permitted unless prohibited - Central Government.
- Capital Account transactions are prohibited unless generally permitted - RBI.

6.3 FEMA: Major Provisions

- Provision of Free transactions on current accounts subject to reasonable restrictions that may be imposed.
- RBI controls capital account transactions.
- Ensures Control over the realization of export proceeds.
- Dealing in foreign exchange through authorized persons like an authorized dealer or money changer etc.
- Provision of appeal provision including Special Director (Appeals).
- Establishment of Directorate of enforcement.
- Any person can sell or withdraw foreign exchange, without any prior permission from RBI and then can inform RBI later.
- Enforcement Directorate will be more investigative in nature.
- FEMA recognized the possibility of Capital Account convertibility.
- The violation of FEMA is a civil offence.
- FEMA is more concerned with the management rather than regulations or control.
- FEMA is a regulatory mechanism that enables RBI and the Central Government to pass regulations and rules relating to foreign exchange in tune with the foreign trade policy of India.

6.4 Limits on possession and retention of foreign currency or foreign coins, under Foreign Exchange Management (Possession & Retention of Foreign Currency) Regulations, 2015.**(Possession & Retention of Foreign Currency) Regulations, 2015****a. Meaning of possession and retention**

It means to possess or to retain in physical form and the words 'possession' or 'retention' shall be construed accordingly.

b. Provision in the Act: Section 4 of Foreign Exchange Management Act, 1999

-Person resident in India can acquire, hold, own, possess or transfer any foreign exchange only after compliance with the provisions of the Act, Rules and Regulations.

c. Regulation framed

-RBI has framed FEM (Possession & Retention of Foreign Currency) Regulations, 2015.

d. Limits for possession and retention of foreign currency or foreign coins [Regulation 3]:

- i. An authorized person acting within the scope of his authority may possess foreign currency and coins without any limit.
- ii. Any person may possess foreign coins without any limit.
- iii. A person resident in India may possess foreign currency notes, bank notes and foreign currency travelers' cheque not exceeding US\$ 2,000 provided that such foreign exchange –
 1. was acquired by him while on a visit to any place outside India by way of payment for services not arising from any business in or anything done in India,
 2. was acquired by him, from any person not resident in India and who is on a visit to India as honorarium or gift or for services rendered or in settlement of any lawful obligation,
 3. was acquired by him by way of honorarium or gift while on a visit to any place outside India,
 4. represents unspent amount of foreign exchange acquired by him from an authorized person for travel abroad.

6.5 Contravention & Penalties under the Foreign Exchange Management Act, 1999: Sec. 13

a. Contravention: [Sec. 13(1)]

Contravention is a breach of:

- the provisions of the Foreign Exchange Management Act (FEMA), 1999 and
- the rules/regulations/notifications/orders/directions/circulars issued in exercise of the powers under the Act, or
- any condition subject to which an authorization is issued by the Reserve Bank

b. Penalties [Sec.13(1)]:

- If amount is quantifiable: Penalty up to thrice the sum involved in such contravention.
- If amount is not quantifiable: Penalty up to 2 lakhs.
- Continuing Contravention: - In case of continuing contravention additional penalty up to 5,000 per day can be imposed.

1A) If any person is found to have acquired any foreign exchange, foreign security or immovable property, situated outside India, of the aggregate value exceeding the threshold prescribed under the proviso to sub-section (1) of section 37A, he shall be liable to a penalty up to three times the sum involved in such contravention and confiscation of the value equivalent, situated in India, the foreign exchange, foreign security or immovable property.

(1B) If the Adjudicating Authority, in a proceeding under sub-section (1A) deems fits, he may, after recording the reasons in writing, recommend for the initiation of prosecution and if the Director of Enforcement is satisfied, he may, after recording the reasons in writing, may direct prosecution by filing a Criminal Complaint against the guilty person by an officer not below the rank of Assistant Director.

(1C) If any person is found to have acquired any foreign exchange, foreign security, or immovable property, situated outside India, of the aggregate value exceeding the threshold prescribed under the proviso to sub-section (1) of section 37A, he shall be, in addition to the penalty imposed under sub-section (1A), punishable with imprisonment for a term which may extend to five years and with fine.

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(1D) No court shall take cognizance of an offence under sub-section (1C) of section 13 except as on complaint in writing by an officer not below the rank of Assistant Director referred to in sub-section (1B).

(2) Confiscation – Further penalty

Any Adjudicating Authority adjudging any contravention under sub-section (1), may, if he thinks fit in addition to any penalty which he may impose for such contravention direct that any currency, security or any other money or property in respect of which the contravention has taken place shall be confiscated to the Central Government. He may further direct that the foreign exchange holdings, if any, of the persons committing the contraventions or any part thereof, shall be brought back into India or shall be retained outside India in accordance with the directions made in this behalf. [Sec. 13(2)]

Explanation. --For the purposes of this sub-section, “property” in respect of which contravention has taken place, shall include--

- (a) deposits in a bank, where the said property is converted into such deposits.
- (b) Indian currency, where the said property is converted into that currency; and
- (c) any other property which has resulted out of the conversion of that property.

6.6 Compounding of Offences under Foreign Exchange (Compounding Proceedings) Rules, 2000.

a. Compounding Meaning

- Compounding refers to the process of voluntarily admitting the contravention, pleading guilty and seeking redressal.
- The RBI is empowered to compound contraventions of the provisions of the FEMA.
- It is a voluntary process in which an individual or a corporate seeks the compounding of an admitted contravention.
- It provides comfort to any person who contravenes any provisions of FEMA, 1999 by minimizing transaction costs. Willful, mala fide and fraudulent transactions are, however, viewed seriously, which will not be compounded by the RBI.

b. Power to compound contravention: Sec. 15(1)

Any contravention under section 13 may, on an application made by the person committing such contravention, be compounded within one hundred and eighty days from the date of receipt of application by the Director of Enforcement or such other officers of the Directorate of Enforcement and officers of the Reserve Bank as may be authorized in this behalf by the Central Government in such manner as may be prescribed.

c. No further proceedings after compounding: Sec. 15(2)

Where a contravention has been compounded under sub-section (1), no proceeding or further proceeding, as the case may be, shall be initiated or continued, as the case may be, against the committing such contravention under that section, in respect of the contravention so compounded.

d. Power of Reserve Bank to compound contravention

1.[Rule 4(1)]

Sum involved in contravention is	Officer of RBI that can compound the offence
10 lakh or below	Assistant General Manager
More than 10 lakh but less than 40 lakh	Deputy General Manager

More than 40 lakh but less than 100 lakh	General Manager
More than 100 lakh	Chief General Manager

2. No compounding if similar offence is committed within a period of 3 years [Rule 4(2)].
3. Once an offence is compounded, similar offence committed within period of 3 years cannot be compounded. Thus, similar offence can be compounded only once in 3 years.
4. Every officer shall exercise the powers to compound any contravention subject to the direction, control and supervision of the Governor of the RBI. [Rule 4(3)]
5. Fee for compounding [Rule 4(4)]: Every application for compounding any contravention shall be made in prescribed Form to the Reserve Bank of India, Exchange Control Department, Central Office, Mumbai along with a fee of 5,000 by way of DD in favour of compounding authority.

e. The Power of Enforcement Directorate to compound contraventions [Rule 5(1)]:

1. Applications seeking compounding of contraventions u/s 3(a) shall be submitted to Enforcement Directorate as specified below:

Sum involved in contravention is	Directorate that can compound the offence
5 lakh or below	Deputy Director of the Directorate of Enforcement.
More than 5 lakh but less than 10 lakh	Additional Director of the Directorate of Enforcement.
More than 10 lakh but less than 50 lakh	Special Director of the Directorate of Enforcement.
More than 50 lakh but less than 100 lakh	Special Director with Legal Advisor of the Directorate of Enforcement.
More than 100 lakh	Director of Enforcement with Special Director of the Directorate of Enforcement.

6.7 Appointment of Adjudicating Authority: Sec. 16

(1) Appointment: Sec. 16(1)

For the purpose of adjudication under section 13, the Central Government may, by an order published in the Official Gazette, appoint as many officers of the Central Government as it may think fit, as the Adjudicating Authorities for holding an inquiry in the manner prescribed after giving the person alleged to have committed contravention under section 13, against whom a complaint has been made under sub-section (3) (hereinafter in this section referred to as the said person) a reasonable opportunity of being heard for the purpose of imposing any penalty:

Provided that where the Adjudicating Authority is of opinion that the said person is likely to abscond or is likely to evade in any manner, the payment of penalty, if levied, it may direct the said person to furnish a bond or guarantee for such amount and subject to such conditions as it may deem fit.

(2) Jurisdiction: Sec. 16(2)

The Central Government shall, while appointing the Adjudicating Authorities under sub-section (1), also specify in the order published in the Official Gazette, their respective jurisdictions.

(3) Procedure of enquiry

No Adjudicating Authority shall hold an enquiry under sub-section (1) except upon a complaint in writing made by any officer authorized by a general or special order by the Central Government [Sec. 16(3)]

The said person may appear either in person or take the assistance of a legal practitioner or a chartered accountant of his choice for presenting his case before the Adjudicating Authority [Sec. 16(4)].

(5) Powers of Adjudicating Authority: Sec. 16(5)

Every Adjudicating Authority shall have the same powers of a civil court which are conferred on the Appellate Tribunal under sub-section (2) of section 28 and--

(a) all proceedings before it shall be deemed to be judicial proceedings within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860);

(b) shall be deemed to be a civil court for the purposes of sections 345 and 346 of the Code of Criminal Procedure, 1973 (2 of 1974).

(6) Every Adjudicating Authority shall deal with the complaint under sub-section (2) as expeditiously as possible and endeavour shall be made to dispose of the complaint finally within one year from the date of receipt of the complaint:

Provided that where the complaint cannot be disposed of within the said period, the Adjudicating Authority shall record periodically the reasons in writing for not disposing of the complaint within the said period [Sec. 16(6)]

6.8 Appellate Tribunal: Sec. 18

The Appellate Tribunal constituted under sub-section (1) of section 12 of the Smugglers and Foreign Exchange Manipulators (Forfeiture of Property) Act, 1976 (13 of 1976), shall, on and from the commencement of Part XIV of Chapter VI of the Finance Act, 2017 (7 of 2017), be the Appellate Tribunal for the purposes of this Act and the said Appellate Tribunal shall exercise the jurisdiction, powers and authority conferred on it by or under this Act.

6.9 Directorate of Enforcement: Sec. 36

(1) The Central Government shall establish a Directorate of Enforcement with a Director and such other officers or class of officers as it thinks fit, who shall be called officers of Enforcement, for the purposes of this Act.

(2) Without prejudice to the provisions of sub-section (1), the Central Government may authorize the Director of Enforcement or an Additional Director of Enforcement or a Special Director of Enforcement or a Deputy Director of Enforcement to appoint officers of Enforcement below the rank of an Assistant Director of Enforcement.

(3) Subject to such conditions and limitations as the Central Government may impose, an officer of Enforcement may exercise the powers and discharge the duties conferred or imposed on him under this Act.

Summary

- The FEMA, 1999 was passed by Lok Sabha on December 2, 1999. It came into force: 1st of June 2000. It extends to the whole of India.
- The FEMA, 1999 is established with the objectives to facilitate external trade and payments, and to promote the orderly development and maintenance of foreign exchange market in India.
- The FEMA, 1999 envisages that RBI shall have a controlling role in management of foreign exchange.
- An authorized person shall, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time.

- The Reserve Bank may, at any time, may direct to inspect the business of any authorized person as may appear to it to be necessary or expedient.
- Where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within specified period and in specified manner by the RBI.
- Compounding refers to the process of voluntarily admitting the contravention, pleading guilty and seeking redressal.
- The RBI is empowered to compound contraventions of the provisions of the FEMA.
- The Central Government shall establish a Directorate of Enforcement with a Director and such other officers or class of officers as it thinks fit, who shall be called officers of Enforcement, for the purposes of this Act.

Keywords

Authorized Dealer: An Authorized Dealer (AD) is any person specifically authorized by the Reserve Bank to deal in foreign exchange or foreign securities and normally includes banks.

Authorized Person: Any person authorized by the Reserve Bank of India to deal in foreign exchange or in foreign securities, as an authorized dealer, money changer or off-shore banking unit or in any other manner as it deems fit.

Capital Account Transaction: Capital Account transaction means a transaction which alters assets or liabilities including contingent liabilities outside India of person resident in India and vice-versa.

Current Account Transactions: Current Account Transaction is a transaction other than a capital account transaction and includes:

- Payment due in connection with foreign trade, other current business, services and short term banking and credit facilities in the ordinary course of business
- Payments due as interest on loans and as net income from investments
- Remittances for living expenses of parents, spouse and children residing abroad
- Expenses in connection with foreign travel, education and medical care of parents, spouse and children.

Nidhi Companies: Nidhi Company is a type of Non-Banking Financial Company (NBFC). It is formed to borrow and lend money to its members. It inculcates the habit of saving among its members and works on the principle of mutual benefit.

Offshore Banking Unit: An offshore banking unit (OBU) is a bank shell branch, located in another international financial center.

Repatriate to India: It means bringing into India the realized foreign exchange and selling of foreign exchange to an authorized person in India in exchange for rupees.

Transferable Development Rights: It means certificates issued in respect of category of land acquired for public purpose either by Central or State Government in consideration of surrender of land by the owner without monetary compensation, which are transferable in part or whole.

Self Assessment

1. The objective/s of FEMA is /are:

- A. To facilitate and promote external trade and payments.
- B. To promote the orderly development of foreign exchange market in India.
- C. To promote the maintenance of foreign exchange market in India.
- D. All of above

2. FEMA deals with:

- A. Only inbound investments into India
- B. Only outbound investments from India

- C. trade and business within India
 - D. Both inbound and outbound investments into and from India
3. Foreign Exchange Management Act, 1999 makes provisions for dealings in foreign exchange through:
- A. Current Account Transactions
 - B. Capital Account Transactions
 - C. Both Current and Capital Account Transactions
 - D. None of above
4. _____ means a branch of a bank in India located in the Special Economic Zone and makes loans in the Eurocurrency market when they accept deposits from foreign banks and other OBUs.
- A. Offshore Banking Unit
 - B. Authorized dealer
 - C. Money Changer
 - D. Authorized person
5. _____ acts as a bank's guarantee that a buyer's payment to a seller will be received on time and for the correct amount in foreign trade.
- A. Credit letter
 - B. Traveler's cheque
 - C. Bill of exchange
 - D. Foreign Deposits
6. Debentures or any other instrument denominated or expressed in foreign currency is termed as:
- A. Foreign Exchange
 - B. Foreign Security
 - C. Foreign Deposit
 - D. Foreign Credits
7. As per section 2(v) of FEMA 1999, a person resident in India refers to a person who:
- A. has been residing in India for more than 182 days during the course of preceding Financial Year.
 - B. has gone out of India for taking employment.
 - C. stays outside India for carrying business.
 - D. has gone out of India for vocation.
8. _____ means bringing into India the realized foreign exchange and selling of same to an authorized person in India in exchange for rupees.
- A. Foreign trade
 - B. Repatriate to India
 - C. Money changing
 - D. Offshore banking
9. _____ is formed to borrow and lend money to its members and are prohibited for capital account transactions.

- A. Business of chit fund
 - B. Nidhi Company
 - C. Agricultural or plantation activities
 - D. Real estate business, or construction of farmhouses
10. Current account transactions in India are regulated by:
- A. Central Government
 - B. Reserve Bank of India
 - C. Either Central Government or Reserve Bank of India
 - D. Both Central Government and Reserve Bank of India
11. FEMA is more concerned with the management rather than regulations or control.
- A. True
 - B. False
12. An authorized person acting within the scope of his authority may possess foreign currency and coins:
- A. without any limit
 - B. not exceeding US\$ 2,000
 - C. not exceeding US\$ 3,000
 - D. not exceeding US\$ 2,50
13. In case of contravention of the provisions of the Foreign Exchange Management Act (FEMA), 1999 and amount involved in such contravention is quantifiable, then the responsible party may get:
- A. Penalty up to thrice the sum involved in such contravention
 - B. Penalty up to 2 lakhs
 - C. Penalty up to 5,000 per day
 - D. All of above
14. ----- refers to the process of voluntarily admitting the contravention, pleading guilty and seeking redressal.
- A. Contravention
 - B. Compounding
 - C. Repatriation
 - D. Realization
15. Any contravention u/s 13 may, on an application made by the person committing such contravention, be compounded within _____ from the date of receipt of application.
- A. 60 days
 - B. 90 days
 - C. 180 days
 - D. 182 days

Answers for Self Assessment

1. D	2. D	3. C	4. A	5. A
6. B	7. A	8. B	9. B	10. A
11. A	12. A	13. A	14. B	15. C

Review Questions

1. Discuss the objectives of passing the Foreign Exchange Management Act, 1999?
2. Who is an authorized person? What are his functions?
3. Write short notes on:
 - a) Authorized person
 - b) Foreign exchange
 - c) Foreign security
 - d) Person resident in India
 - e) Person resident outside India
 - f) Person of Indian Origin
 - g) Directorate of Enforcement
 - h) Appellate Tribunal
4. Discuss the RBI's powers to issue directions to authorized person and inspect the authorized person.
5. Define Repatriate to India. Discuss the realization and repatriation of foreign exchange and with its exemptions.
6. What are capital account transactions. Discuss the FEMA, 1999 provisions related to capital account transactions.
7. Write major provisions of FEMA, 1999.
8. Explain the contravention & penalties under the Foreign Exchange Management Act, 1999 as per Sec. 13.
9. Explain the compounding of Offences under Foreign Exchange (Compounding Proceedings) Rules, 2000.
10. Xero Limited is an Indian company. However, it carries on business in the USA. All the shareholders are residents of the USA. The Board Meetings and Annual General Meetings are held outside India. What is the residential status of Xero Limited? State reasons.
11. Discuss the appointment, jurisdictions and powers of Adjudicating Authority.
12. Write the possession & retention of Foreign Currency Regulations, 2015.

**Further Reading**

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Unit 07: The Competition Act, 2002

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Objectives

After studying this unit, you will be able to:

- explain the objectives of the Competition Act, 2002.
- explain the important definitions of the Competition Act, 2002.
- illustrate the meaning of Anti-competitive Agreements, Abuse of Dominant Position, and Combinations.
- review the major regulations of the Competition Act, 2002 related to Anti-competitive Agreements, Abuse of Dominant Position, and Combinations.
- comment on the importance and role of Competition Commission of India (CCI) to promote and sustain competition in India.
- review the need of the Competition Act, 2002 to eliminate practices having adverse effect on competition in India.

Introduction

India opened its economy by removing or reducing controls as a move towards liberalization. The direct implication of this move is that the Indian market should be ready to face the competition from within and outside the country.

The Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act) had become obsolete and was strangling the economy. Thus, India came up with the Competition Act, 2002, which has replaced the MRTP Act, 1969 to achieve the following objectives:

- a) to prevent practices having adverse effect on competition.
- b) to promote and sustain competition in market.
- c) to protect the interest of consumers, and

- d) to ensure freedom of trade carried on by other participants in markets in India.

The Competition Act, 2002 was passed by the Parliament in the year 2002, to which the President accorded assent in January 2003. It was subsequently amended by the Competition (Amendment) Act, 2007.

In accordance with the provisions of the Amendment Act, the Competition Commission of India and the Competition Appellate Tribunal have been established. The Competition Commission of India is now fully functional with a chairperson and six members. The provisions of the Competition Act relating to anti-competitive agreements and abuse of dominant position were notified on May 20, 2009.

With the advent of the Competition Act, 2002, all the cases relating to Monopolistic Trade Practices (MTP) and Restricted Trade Practices (RTP), and Unfair Trade Practices (UTP) were transferred to the Competition Appellate Tribunal with immediate effect.

In this unit, few key definitions of the Competition Act, 2002, provisions related to Anti-competitive Agreements, Abuse of Dominant Position, and Combinations are discussed.

7.1 The Competition Act, 2002: Introduction

- The Competition Act, 2002 was enacted by the Parliament of India and governs Indian competition law.
- It replaced the Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act).
- Under this legislation, the Competition Commission of India (CCI) was established to prevent the activities that have an adverse effect on competition in India.
- The Competition Act, 2002 contains various provisions for regulation of fair competition in the market and for cutting monopolies and dominant position or any act to eliminate any enterprise by other in the market.
- It applies to all enterprises whether they belong to private sector or government.
- The act applies to all goods and services including goods imported into India.
- However, any act of government relating to sovereign functions including the activities carried on by departments of the Central Government dealing with Security, Atomic Energy, Currency, Defence and Space are outside the scope of the act.
- Any dispute relating to consumers, which has not affected on the Competition will not be considered under provisions of this act.
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7.2 The Competition Act, 2002: Objectives

- To establish a commission, protect the interest of the consumers and ensure freedom of trade in Indian markets.
- To prohibit the agreement or practices that restrict free trading and also the competition between two business entities.
- To ban the abusive situation of the market monopoly.
- To provide the opportunity to the entrepreneur for the competition in the market.
- To have the international support and enforcement network across the world, and
- To prevent from anti competition practices and to promote a fair and healthy competition in the market.

7.3 The Competition Act, 2002: Definitions

- 1) Acquisition -Sec. 2(a)
- 2) Agreement – Sec. 2(b)

- 3) Cartel – Sec 2(c)
- 4) Consumer – Sec 2(f)
- 5) Enterprise – Sec. 2(h)
- 6) Goods – Sec 2(i)
- 7) Predatory Price



1. Acquisition -Sec. 2(a)

It means, directly or indirectly, acquiring or agreeing to acquire--

- (i) shares, voting rights or assets of any enterprise; or
- (ii) control over management or control over assets of any enterprise.

2. Agreement – Sec. 2(b)

"Agreement" includes any arrangement or understanding or action in concert -

- (i) whether or not, such arrangement, understanding or action is formal or in writing; or
- (ii) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings.

3. Cartel – Sec 2(c)

It includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control the production, distribution, sale or price of, or trade in goods or provision of services.

4. Consumer – Sec 2(f)

"Consumer" means any person who--

- (i) buys any goods for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and includes any user of such goods other than the person who buys such goods for consideration paid or promised or partly paid or partly promised, or under any system of deferred payment when such use is made with the approval of such person, whether such purchase of goods is for resale or for any commercial purpose or for personal use;
- (ii) hires or avails of any services for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and includes any beneficiary of such services other than the person who hires or avails of the services for consideration paid or promised, or partly paid and partly promised, or under any system of deferred payment, when such services are availed of with the approval of the first-mentioned person whether such hiring or availing of services is for any commercial purpose or for personal use.

5. Enterprise – Sec. 2(h)

"enterprise" means a person or a department of the Government, who or which is, or has been, engaged in any activity, relating to the production, storage, supply, distribution, acquisition or control of articles or goods, or the provision of services, of any kind, or in investment, or in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate, either directly or through one or more of its units or divisions or subsidiaries, whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or at different places, but does not include any activity of the Government relatable to the sovereign functions of the Government including all activities carried on by the departments of the Central Government dealing with atomic energy, currency, defence and space.

For the purposes of this clause,--

- (a) "activity" includes profession or occupation;
- (b) "article" includes a new article and service includes a new service;
- (c) unit" or "division", in relation to an enterprise, includes--
- (i) a plant or factory established for the production, storage, supply, distribution,

acquisition or control of any article or goods;

(ii) any branch or office established for the provision of any service.

6. Goods – Sec 2(i)

"Goods" means goods as defined in the Sale of Goods Act, 1930 (8 of 1930) and includes--

(A) products manufactured, processed or mined;

(B) debentures, stocks and shares after allotment;

(C) in relation to goods supplied, distributed or controlled in India, goods imported into India.

7. Predatory Price

It means the sale of goods or provision of services, at a price which is below the cost, as may be determined by regulations, of production of the goods or provision of services, with a view to reduce competition or eliminate the competitors.

7.4 Anti – Competitive Agreements – Sec. 3

No enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition within India.

- Sec. 3(1)

Agreement Void: Sec. 3(2)

Any agreement entered in contravention of the provisions contained in sub-section (1) shall be void.

Adverse effect on competition: Sec. 3(3)

Any agreement entered between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on, or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of services, which--

(a) directly or indirectly determines purchase or sale prices;

(b) limits or controls production, supply, markets, technical development, investment or provision of services;

(c) shares the market or source of production or provision of services by way of allocation of geographical area of market, or type of goods or services, or number of customers in the market or any other similar way;

(d) directly or indirectly results in bid rigging or collusive bidding,

shall be presumed to have an appreciable adverse effect on competition.



It means, these all above agreement shall be presumed to have an appreciable adverse effect on competition

Provided that nothing contained in this sub-section shall apply to any agreement entered into by way of joint ventures if such agreement increases efficiency in production, supply, distribution, storage, acquisition or control of goods or provision of services.



"Bid rigging" means any agreement, between enterprises or persons referred to in sub-section (3) engaged in identical or similar production or trading of goods or provision of services, which has the effect of eliminating or reducing competition for bids or adversely affecting or manipulating the process for bidding.

Bid rigging takes place when bidders collude and keep the bid amount at a pre-determined level. Such pre-determination is by way of intentional manipulation by the members of the

bidding group. Bidders could be actual or potential ones, but they collude and act in concert.

Any agreement amongst enterprises or persons at different stages or levels of the production chain in different markets, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services, including – (Vertical Agreements) - Sec. 4(4)

- (a) tie-in arrangement;
- (b) exclusive supply agreement;
- (c) exclusive distribution agreement;
- (d) refusal to deal;
- (e) resale price maintenance,

shall be an agreement in contravention of sub-section (1) if such agreement causes or is likely to cause an appreciable adverse effect on competition in India.



For the purposes of this sub-section,--

- (a) "tie-in arrangement" includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods;
- (b) "exclusive supply agreement" includes any agreement restricting in any manner the purchaser in the course of his trade from acquiring or otherwise dealing in any goods other than those of the seller or any other person;
- (c) "exclusive distribution agreement" includes any agreement to limit, restrict or withhold the output or supply of any goods or allocate any area or market for the disposal or sale of the goods;
- (d) "refusal to deal" includes any agreement which restricts, or is likely to restrict, by any method the persons or classes of persons to whom goods are sold or from whom goods are bought;
- (e) "resale price maintenance" includes any agreement to sell goods on condition that the prices to be charged on the resale by the purchaser shall be the prices stipulated by the seller unless it is clearly stated that prices lower than those prices may be charged.

Anti – Competitive Agreements – Sec. 3(5): Exceptions

Nothing contained in this section shall restrict--

- (i) the right of any person to restrain any infringement of, or to impose reasonable conditions, as may be necessary for protecting any of his rights which have been or may be conferred upon him under--
 - (a) the Copyright Act, 1957 (14 of 1957);
 - (b) the Patents Act, 1970 (39 of 1970);
 - (c) the Trade and Merchandise Marks Act, 1958 (43 of 1958) or the Trademarks Act, 1999 (47 of 1999);
 - (d) the Geographical Indications of Goods (Registration and Protection) Act, 1999 (48 of 1999);
 - (e) the Designs Act, 2000 (16 of 2000);
 - (f) the Semi-conductor Integrated Circuits Layout-Design Act, 2000 (37 of 2000);
- (ii) the right of any person to export goods from India to the extent to which the agreement relates exclusively to the production, supply, distribution or control of goods or provision of services for such export.

Anti – Competitive Agreements – Sec. 3: Types

- Horizontal Agreement: Example Cartel
- Vertical Agreement

**Horizontal Agreements**

Horizontal agreements are arrangements between enterprises at the same stage of the production chain and that is generally between two rivals for either fixing prices or for limiting production or for sharing markets. Basically, Horizontal agreements are agreements among competitors engaged in the same activity.



The agreements between producers or between wholesalers or between retailers, dealing in similar kind of products.

In all such agreements, there is a presumption in the Act that such agreements cause AAEC. Cartel is also a horizontal agreement. This is generally between producers of goods or providers of services for price-fixing or sharing of market and is generally regarded as the most pernicious form of anti-competitive agreement.

Vertical Agreements

Vertical agreements are between enterprises at different stages of the production chain, like an arrangement between the manufacturer and a distributor. Basically, vertical agreements are agreements between non-competing undertaking.



The agreements between manufacturers of components, manufacturer of products, between producers and wholesalers or between producers, wholesalers and retailers.

The presumptive rule does not apply to vertical agreements. The question whether the vertical agreement is causing AAEC is determined by rule of reason. When rule of reason is employed, both positive as well as negative impact of competition is analyzed. In order to determine whether any agreement is in contravention of section 3(4) read with section 3(1) of the Act, the following five essential ingredients of section 3(4) have to be satisfied:

1. There must be an agreement amongst enterprises or persons;
2. The parties to such agreement must be at different stages or levels of production chain, in respect of production, supply, distribution, storage, sale or price of, or trade in goods or provision of services;
3. The agreeing parties must be in different markets;
4. The agreement should cause or should be likely to cause AAEC;
5. The agreement should be of one of the following nature as illustrated in section 3(4) of the Act i.e.
 - (a) tie-in arrangement;
 - (b) exclusive supply agreement;
 - (c) exclusive distribution agreement;
 - (d) refusal to deal;
 - (e) resale price maintenance

7.5 Dominant Position: Meaning and Abuse (Sec. 4)**What is Dominant Position?**

It means a position of strength, enjoyed by an enterprise in the relevant market in India, which enables to-

- a. operate independently of competitive forces prevailing in the relevant market, or
- b. affects its competitors or consumers or the relevant market in its favor.

Abuse of Dominant Position – Sec. 4

If an enterprise-

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A	Directly or indirectly impose unfair or discriminatory	1. Condition in purchase or sale of goods or service; or 2. Price in purchase or sale of goods or service, or
B	Limit or restricts-	1. Production of goods or provision of service or market thereof; or 2. Technical or scientific development relating to goods or services to the prejudice of consumers; or
C	Denial of Market access	Indulges in practice or practices resulting in denial of market access; or
D	Cancellation of Contracts	Makes conclusions of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage have no connection with the subject of such contracts; or
E	Dominant position in one relevant market	Uses its dominant position in one relevant market to enter or protect other relevant market.

7.6 Combination- Sec. 5 and 6

Broadly combination under the act implies for acquisition of control, shares, voting rights or assets, acquisition of control by a person over an enterprise where such person has direct or indirect control over another Enterprise engaged in competing businesses, and Mergers and amalgamations between or amongst Enterprises then the combining parties exceed the thresholds set in the Act. The thresholds are mentioned in the Act in terms of assets or turnover in India and outside India.

As per section 5 of the act a combination comprises any of the following:

- any acquisition of control or share or voting rights or asset of an enterprise;
- acquiring of control by person over an enterprise, where such person already has direct or indirect control over another enterprise engaged in similar or competitive business;
- any merger or amalgamation between enterprises if it exceeds the monetary threshold of assets or turnover as given ahead:

	Applicable To	Assets		Turnover	
In India	Individual	> 1,000 cr		3,000 cr	
	Group	> 4,000 cr		> 12,000 cr	
In India or Outside India		Assets		Turnover	
		Total (in aggregate)	Minimum India Component	Total	Minimum India Component
	Individual	> \$ 500 million	500 crores	> \$ 1,500 million	1,500 cr
	Group	> \$ 2 billion	500 crores	> \$ 6 billion	1,500 cr



Source: https://www.indiacode.nic.in/handle/123456789/2010?view_type=browse&sample=123456789/1362

Combination: Type

- Horizontal Combinations
- Vertical Combinations

1. Horizontal Combination

Horizontal combination refers to the combination of the firms producing the same or similar type of products, engaged in the same or similar process of production. Combination of two or more jute mills, textile mills, and factories is examples for this type of combination. It is also known as parallel combination.

2. Vertical Combination

Vertical or sequence combination unites organizations which are in different places and which represent the successive stages or trade within an industry. The organizations combines are not competing side by side, but stand end to end, the one receiving the products of the other as its own material. In short, vertical combination is the linking up of all the stages of production right from the raw material to the finished product.

Regulation of Combinations – Sec. 6

(1) No person or enterprise shall enter into a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination shall be void.

(2) Subject to the provisions contained in sub-section (1), any person or enterprise, who or which proposes to enter into a combination, may, at his or its option, give notice to the Commission, in the form as may be specified, and the fee which may be determined, by regulations, disclosing the details of the proposed combination, within seven days of--

(a) approval of the proposal relating to merger or amalgamation, referred to in clause (c) of section 5, by the board of directors of the enterprises concerned with such merger or amalgamation, as the case may be;

(b) execution of any agreement or other document for acquisition referred to in clause (a) of section 5 or acquiring of control referred to in clause (b) of that section.

(2A) No combination shall come into effect until two hundred and ten days have passed from the day on which the notice has been given to the Commission under sub-section (2) or the Commission has passed orders under section 31, whichever is earlier.

(3) The Commission shall, after receipt of notice under sub-section (2), deal with such notice in accordance with the provisions contained in sections 29, 30 and 31.

(4) The provisions of this section shall not apply to share subscription or financing facility or any acquisition, by a public financial institution, foreign institutional investor, bank or venture capital fund, pursuant to any covenant of a loan agreement or investment agreement.

(5) The public financial institution, foreign institutional investor, bank or venture capital fund, referred to in sub-section (4), shall, within seven days from the date of the acquisition, file, in the form as may be specified by regulations, with the Commission the details of the acquisition including the details of control, the circumstances for exercise of such control and the consequences of default arising out of such loan agreement or investment agreement, as the case may be.

Explanation.--For the purposes of this section, the expression--

(a) "foreign institutional investor" has the same meaning as assigned to it in clause (a) of the Explanation to section 115AD of the Income-tax Act, 1961(43 of 1961);

(b) "venture capital fund" has the same meaning as assigned to it in clause (b) of the Explanation to clause (23 FB) of section 10 of the Income-tax Act, 1961(43 of 1961).

Orders of Commission on Certain Combinations: Sec. 31

1. Approve that combination.
2. Disapprove the combination.
3. Propose appropriate modification to the combination.
4. The parties, who accept the modifications proposed shall carry out such modifications within the period specified by the commission.
5. If the parties fail to carry out the modifications within the period specified, such combination shall be deemed to have an appreciable adverse effect on competition, and the commission shall deal with such combination in accordance with the provisions of this Act.
6. Submission of amendment to the modification proposed by the commission under that sub-section by the parties to the combination.
7. If the commission agrees with the amendment submitted by the party under sub-section (6), it shall, by order, approve the combination.
8. If the commission does not accept the amendment), then the parties shall be allowed for the period of 30 working days.
9. If the parties fail to accept modification proposed by the commission within 30 working days referred to in sub-section (6), or within a further period of 30 working days referred to in sub-section (8), the combination shall be deemed to have an appreciable adverse effect on competition and be dealt with in accordance with the provision of this Act.
10. The commission may order in case of disapprove the combination that:
 - a) the acquisition referred to in clause (a) of Section 5; or
 - b) the acquiring of control referred to in clause (B) of Section 5; or
 - c) the merger or amalgamation referred to in clause (C) of Section 5, shall not be given effect to:

Provided that the Commission may, if it considers appropriate, frame a scheme to implement its order under this sub-section.

11. The combination shall be deemed to have been approved by the commission.

7.7 Competition Commission of India (CCI): Sec. 7 to 10**Establishment of Competition Commission of India (CCI): Sec. 7**

(1) With effect from such date as the Central Government may, by notification, appoint, there shall be established, for the purposes of this Act, a Commission to be called the "Competition Commission of India".

(2) The Commission shall be a body corporate by the name aforesaid having perpetual succession and a common seal with power, subject to the provisions of this Act, to acquire, hold and dispose of property, both movable and immovable, and to contract and shall, by the said name, sue or be sued.

(3) The head office of the Commission shall be at such place* as the Central Government may decide from time to time.

(4) The Commission may establish offices at other places in India.

Composition of CCI: Sec. 8

(1) The Commission shall consist of a Chairperson and not less than two and not more than six other Members to be appointed by the Central Government.

(2) The Chairperson and every other Member shall be a person of ability, integrity and standing and who has special knowledge of, and such professional experience of not less than fifteen years in, international trade, economics, business, commerce, law, finance, accountancy, management,

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industry, public affairs or competition matters, including competition law and policy, which in the opinion of the Central Government, may be useful to the Commission.

(3) The Chairperson and other Members shall be whole-time Members

Selection Committee for Chairperson and Members of Commission: Sec. 9

(1) The Chairperson and other Members of the Commission shall be appointed by the Central Government from a panel of names recommended by a Selection Committee consisting of--

(a) the Chief Justice of India or his nominee....Chairperson;

(b) the Secretary in the Ministry of Corporate Affairs....Member;

(c) the Secretary in the Ministry of Law and Justice....Member;

(d) two experts of repute who have special knowledge of, and professional experience in international trade, economics, business, commerce, law, finance, accountancy, management, industry, public affairs or competition matters including competition law and policy....Members.

(2) The term of the Selection Committee and the manner of selection of panel of names shall be such as may be prescribed.

Term of office of Chairperson and other Members: Sec. 10

(1) The Chairperson and every other Member shall hold office as such for a term of five years from the date on which he enters upon his office and shall be eligible for re-appointment:

Provided that the Chairperson or other Members shall not hold office as such after he has attained the age of sixty-five years.

(2) A vacancy caused by the resignation or removal of the Chairperson or any other Member under section 11 or by death or otherwise shall be filled by fresh appointment in accordance with the provisions of sections 8 and 9.

(3) The Chairperson and every other Member shall, before entering upon his office, make and subscribe to an oath of office and of secrecy in such form, manner and before such authority, as may be prescribed.

(4) In the event of the occurrence of a vacancy in the office of the Chairperson by reason of his death, resignation or otherwise, the senior-most Member shall act as the Chairperson, until the date on which a new Chairperson, appointed in accordance with the provisions of this Act to fill such vacancy, enters upon his office.

(5) When the Chairperson is unable to discharge his functions owing to absence, illness or any other cause, the senior-most Member shall discharge the functions of the Chairperson until the date on which the Chairperson resumes the charge of his functions.

Duties of Commission: Sec. 18

Subject to the provisions of this Act, it shall be the duty of the Commission:

- to eliminate practices having adverse effect on competition,
- to promote and sustain competition,
- to protect the interests of consumers and
- to ensure freedom of trade carried on by other participants, in markets in India.

Provided that the Commission may, for the purpose of discharging its duties or performing its functions under this Act, enter into any memorandum or arrangement with the prior approval of the Central Government, with any agency of any foreign country.

**Builders Association of India V Cement Manufacturers' Association**

Builders Association of India, the informant, a society registered under the Societies Registration Act, 1860 was an association of Builders and other entities involved in the business of construction. The respondent was an association of the cement manufacturers of India (CMA) In which both public and private sector cement units were members. Respondent Association (CMA) included cement manufacturers, namely, Associated Cement Company Limited, Gujarat Ambuja Cement Limited, Grasim Cement, UltraTech Cement Limited, Jaypee Cement, India Cements Limited, JK Cements of group, Century Cement, Madras Cement Limited and Lafarge India Limited Hoover the leading

manufacturers, distributors and sellers of cement in India.

Builders Association of India, the informant alleged that the major 11 cement manufacturers all over India, under the aegis of CMA Indulge in the following activities:

1. In spite of the fact that the cement manufacturing units were graphically dispersed throughout the country, having different costs of production and transportation. the alleged cement manufacturing companies, simultaneously increased their prices at the same time in all the five zones, i.e., North, East, West, South and Central. Thus, the respondents Cement manufacturers had allocated the markets into 5 zones so as to enable them to control the supply and determine or fix exorbitantly high prices of cement by forming catches in contravention of section 3 of the act.
2. The respondents collectively reduced their capacity utilization from 88% in March 2009 to 82.46% in March 2010, in spite of an increase in their installed capacities from 219 million tons to 246 million tons during the same period. That is how they artificially increased the demand, which showed limiting and controlling the supplies in the market.
3. The government announced various concessions and stimulus packages in 2008 but the respondent collectively increased the unit sales price of the cement from 2008 to 2010, which showed collectively determining sale price.
4. The real estate sector recorded a slowdown in the growth during 2007-08 and 2009-10, however the operating profit margin (OPM) of the cement manufacturers increased during the same period. Similarly, the OPM within the cement industry of the six dominant players was 27.33 percent as against that of 17.68 percent of the industry as a whole.
5. The cement industry did not pass on the price benefit enjoyed in the form of “fly ash”, (which constituted 15 to 20% of the raw material to produce cement and was provided free to the cement industry by the thermal power plants, on mostly by government or semi government undertakings) to its customers and consumers.

Thus, the informant, alleged that the respondent cement manufacturers under the umbrella of CMA indulged directly and indirectly into Monopolistic and restrictive trade practices, in an effort to control the price of cement by limiting and restricting the production and supply of cement as against the available capacity of production and “collusive price fixing”. Effectively, the case was made out under section 3 and 4 of the acts.

The informant argued that search cartel formation had an adverse impact on the construction and real estate sector. Pursuant to the persistent complaints by the builders and the preponderance/ suspected cartel led to appointment of a standing committee by the Ministry of Commerce to investigate the action of the alleged cartel members. The commission after forming an opinion that a prima facie case exists in the matter and framed some issues against the respondents, under section 3 and 4 of the acts.

The respondents cement manufacturers rejected all the allegations and contended that there was no written agreement or direct evidence from which the existence of the cartel could be inferred.

Points of Discussion

1. Whether the respondent cement manufacturers violated the provisions of Section 4 of the Competition Act, 2002 as has been alleged?
2. Whether the acts and conduct of the respondents were subject matter of examination under section 3 of the act?
3. Was there an agreement or arrangement between the cement company under

which they have the details of price, production and capacity among others using the platform of CMA?

4. Whether they have indulged in directly or indirectly determining the prices of Cement?

Judgement and Explanation

The CCI found the respondent cement manufacturers in contravention of Section 3(3)(a) and 3(3)(b) read with Section 3(1) of the Act and Imposed a penalty of 0.5 times of net profit for 2009-10 and 2010-11 in case of each respondent cement manufacturer in this case. CCI also imposed a penalty of ₹ 73 lakh on the CMA @10% of its average turnover for the last three preceding years. The total penalty amount works out to ₹ 6,306.59 crore.



Source: Gupta, P. *Legal aspects of Business: Concept and Applications*. Vikas Publishing House Pvt. Ltd.

Summary

- The Competition Act, 2002 was enacted by the Parliament of India and governs Indian competition law. It replaced the Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act).
- The Competition Act, 2002 was enforced to prohibit the agreement or practices that restrict free trading and also the competition between two business entities, protect the interest of the consumers and ensure freedom of trade in Indian markets.
- Under this legislation, the Competition Commission of India (CCI) was established to prevent the activities that have an adverse effect on competition in India.
- No enterprise or association of enterprises or person or association of persons shall enter into any agreement in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition (AAEC) within India. Such agreements will be void.
- Dominant position has been appropriately defined in the competition act in terms of the position of strength, enjoyed by an enterprise or firm, in the relevant market, in India.
- The competition act also regulates operation and activities of combinations, a term, which contemplates acquisitions, mergers, and amalgamations.
- Entering a combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India is prohibited and such combination shall be void.
- The Competition Commission of India is a body corporate by its name having perpetual succession and common seal with power, subject to the provisions of this act, to acquire, hold and dispose of property, movable and immovable and to contract,

Keywords

Activity: It includes profession or occupation.

Agreement: It includes any arrangement or understanding or action in concert whether or not, such arrangement, understanding or action is formal or in writing; or whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings.

Anti-Competitive Agreements: Firms sometimes enter into agreements, which may have the potential of respecting competition, such agreements are treated as anti-competitive agreements.

Bid rigging: Bid rigging takes place when bidders collude and keep the bid amount at a pre-determined level.

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Cartel: It includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control the production, distribution, sale or price of, or trade in goods or provision of services.

Horizontal agreements: Horizontal agreements are agreements among competitors engaged in the same activity.

Predatory Price: It means the sale of goods or provision of services, at a price which is below the cost, as may be determined by regulations, of production of the goods or provision of services, with a view to reduce competition or eliminate the competitors.

Tie-in arrangement: It includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods.

Vertical agreements: Vertical agreements are agreements between non-competing undertaking.

Self Assessment

1. The objective/s of the Competition Act, 2002 is/are to:
 - A. establish a commission
 - B. protect the interest of the consumers
 - C. ensure freedom of trade in Indian markets
 - D. all of above
2. _____ means, directly or indirectly, acquiring or agreeing to acquire shares, voting rights or assets of any enterprise.
 - A. Acquisition
 - B. Agreement
 - C. Cartel
 - D. Purchase
3. _____ includes an association of producers who, by agreement amongst themselves, limit the production of goods.
 - A. Acquisition
 - B. Agreement
 - C. Cartel
 - D. Purchase
4. _____ means the sale of goods at a price which is below the cost, as may be determined by regulations, of production of the goods, with a view to eliminate the competitors.
 - A. Cartel
 - B. Acquisition
 - C. Predatory Price
 - D. Competitive agreement
5. Any agreement including cartels, engaged in identical or similar trade of goods or provision of services, which directly or indirectly determines purchase or sale prices is an example of:
 - A. a valid agreement
 - B. a competitive agreement
 - C. an anti-competitive agreement
 - D. none of above
6. _____ is an illegal practice in which competing parties collude to determine the winner of a bidding process.

- A. Auction
 - B. Bidding
 - C. Bid Rigging
 - D. Tie-in arrangement
7. _____ are arrangements between enterprises at the same stage of the production chain and that is generally between two rivals for either fixing prices or for limiting production or for sharing markets.
- A. Horizontal agreements
 - B. Vertical agreements
 - C. Horizontal collaborations
 - D. Vertical collaborations
8. _____ includes any agreement requiring a purchaser of goods, as a condition of such purchase, to purchase some other goods.
- A. tie-in arrangement
 - B. exclusive supply agreement
 - C. exclusive distribution agreement
 - D. refusal to deal
9. _____ includes any agreement restricting in any matter the purchaser in the course of his trade from acquiring any goods other than those of the seller or any other person.
- A. tie-in arrangement
 - B. exclusive supply agreement
 - C. exclusive distribution agreement
 - D. refusal to deal
10. Any agreement to allocate any area or market for the disposal or sale of the goods is termed as:
- A. tie-in arrangement
 - B. exclusive supply agreement
 - C. exclusive distribution agreement
 - D. refusal to deal
11. Any agreement which restricts by any method the persons to whom goods are sold or from whom goods are bought is termed as:
- A. tie-in arrangement
 - B. exclusive supply agreement
 - C. exclusive distribution agreement
 - D. refusal to deal
12. Section 4(2) of the Competition Act, 2002 provides that there shall be an abuse of a dominant position if an enterprise or a group:
- A. restricts or limits production of goods or services in the market
 - B. directly or indirectly imposes fair conditions in the purchase or sale of goods or services
 - C. indulges in a practice resulting in approval of market access in any manner

D. all of above

13. Export goods from India to the extent to which the agreement relates exclusively to the production, supply, distribution or control of goods or provision of services for such export is:

- A. an exception of Anti-competitive agreement
- B. an anti-competitive agreement
- C. an act of abuse of dominant position
- D. an example of collaboration

14. Any merger between enterprises if it exceeds the following monetary threshold of assets value will be termed as combination in India.

- A. 1,000 crores
- B. 1,500 crores
- C. 3,000 crores
- D. 12,000 crores

15. Any combination which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India shall be _____.

- A. Valid
- B. Void
- C. Voidable
- D. Unenforceable

Answers for Self Assessment

1. D	2. A	3. C	4. C	5. C
6. C	7. A	8. A	9. B	10. C
11. D	12. A	13. A	14. A	15. B

Review Questions

1. Discuss the objectives of the Competition Act, 2002. Also give major reasons for passing the Act.
2. Write a short note on the following terms as defined under the Competition Act:
 - a) Agreement
 - b) Predatory Pricing
 - c) Bid Rigging
 - d) Cartel
 - e) Consumer
 - f) Goods
3. What do you understand by Anti-Competitive Agreements? Explain the provisions given under section 3 of the Competition Act, 2002 related to Anti-Competitive Agreements.
4. Illustrate the types of Anti-Competitive Agreements.
5. Define Dominant position as per the Competition Act, 2002. Also discuss about abuse of dominance under the Competition Act, 2002.

Legal Aspects of Business

6. Discuss in detail about combinations in the light of the Competition Act, 2002.
7. Write the regulations of combinations under the Competition Act, 2002.
8. What are the major orders that Competition Commission of India (CCI) may give on certain combinations?
9. Discuss about the establishment, composition and duties of Competition Commission of India.



Further Reading

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Unit 08: The Companies Act, 2013 (Preliminary)

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Summary

Keywords

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Objectives

After studying this unit, you will be able to:

- explain the meaning of a company.
- illustrate the characteristics of a company.
- appraise the concept of lifting the corporate veil.
- review the grounds of lifting the corporate veil.
- illustrate the different kinds of companies based on various classification grounds such as incorporation, liability, number of members, control, ownership, etc.
- illustrate the concept of Limited Liability Partnership (LLP).
- review the salient features of LLP.
- review the steps of registering a firm as LLP.
- comment on the use of LLP by individuals to explore the business world opportunities by seeking limited liability.
- explain the procedure of incorporating a company in India.
- review the features of SPICe+ form.
- review the provisions related to incorporation of company contained in Sec. 7.

- comment on the legalities of forming and incorporating a company in India.

Introduction

A company, in its ordinary, non-technical sense, means a body of individuals associated for a common objective, which may be to carry on business for gain or to engage in some human activity for the benefit of the society. Accordingly, the word 'company' is employed to represent associations formed to carry on some business for profit or to promote art, science, education or to fulfill some charitable purpose.

The Companies Act, 2013 recognizes different types of companies that can be promoted and registered under the Act. There are various basis for classification of companies such as incorporation; number of members; control, ownership; liability and so on. Limited Liability Partnerships (LLPs), producer companies, and dormant companies are also recognized and registered under the Companies Act, 2013.

Being an incorporated entity, a number of steps are required to be followed to bring a company into existence. These steps demand a variety of documents and information to be furnished to different authorities.

In January 2020, the Ministry of Corporate Affairs (MCA), notified to issue new form SPICe+ as a part of India's Ease of Doing Business initiatives. The new form which is named Spice Plus or Spice+ shall be a replacement of the old system of spice 32 form.

SPICe+ has two parts viz.: Part A -for Name reservation for new companies and Part B offering a bouquet of services. Users may either choose to submit Part-A for reserving a name first and thereafter submit Part B for incorporation & other services or file Part A and B together at one go for incorporating a new company and availing the bouquet of services as above.

Incorporation applications (Part B) after name reservation (In Part A) can be submitted as a seamless process in continuation of Part A of SPICe+. Stakeholders are not required to even enter the SRN (Service Request Number) of the approved name as the approved Name is prominently displayed on the Dashboard and a click on the same will take the user for continuation of the application through a hyperlink that is available on the SRN/application number in the new dashboard.

In the present unit, meaning and characteristics of company; kinds of companies, concept, features, registration process of Limited Liability Partnership (LLP); and Incorporation procedure of a company under the Companies Act 2013 and the Companies Incorporation (Amendment) Rules, 2020 are discussed.

8.1 The Companies Act, 2013: Introduction

- The Indian Companies Act, 2013 replaced the Indian Companies Act, 1956.
- It provides comprehensive provisions to govern all listed and unlisted companies in that country.

8.2 The Companies (Amendment) Act, 2020

- It was passed by the Lok Sabha on 19th September 2020 and by the Rajya Sabha on 22nd September 2020.
- It got the assent of Hon'ble President as on 28th September 2020 and is thus operative since that date.
- There are amendments in 61 sections in the Act and 4 sections have been newly inserted which includes the provisions for Producer Companies.

8.3 Company: Meaning and Definition

A company is a voluntary association of persons formed for the purpose of doing business having a distinct name and limited liability.

Unit 08: The Companies Act, 2013 (Preliminary)

A company is nothing but a group of persons who have come together or who have contributed money for some common purpose and who have incorporated themselves into a distinct legal entity in the form of a company for that purpose.

Thus, a company has two following basic features:

- A voluntary association of persons, and
- An artificial person created by law.

Company: Definition

"Company" means a company incorporated under this Act (Companies Act, 2013) or under any previous company law. - Sec. 2(20)

The above definition does not reveal the distinctive characteristics of a company. A more comprehensive and clear definition was suggested by Lord Justice Lindley.

"An association of many persons who contribute money or money's worth to a common stock, and employ it in some common trade or business, and who share the profit or loss arising there from."

- Lord Lindley

8.4 Company: Essential Characteristics

1. Incorporated association
2. Artificial legal person
3. Separate legal entity
4. Perpetual existence
5. Common seal
6. Limited liability
7. Transferable shares
8. Separate property
9. Delegated Management

1. Incorporated association: It is created when it is registered under the Companies Act. It comes into being on the date mentioned in the certificate of incorporation.

2. Artificial legal person: It is an artificial person and not a natural person. It exists in the eyes of law but cannot act on its own. It has the right to acquire and dispose of property, to enter into contract with third parties in its own name, and can sue and be sued in its own name.

3. Separate legal entity: A company is an entity separate from its members. It is an independent corporate existence. Its members cannot be held liable for the acts of the company. The company's money and property belong to it and not to the shareholders.



Salomon v. Salomon & Co. Ltd. (1897)

Aron Salomon had for many years carried on a prosperous business as a leather merchant. In 1892, he decided to convert it into a limited company and for that purpose Salomon & Co. Ltd. was formed with Salomon, his wife, his daughter and his four sons as members, and Salomon as Managing Director.

The company purchased the business of Salomon for £ 39,000. The price was satisfied by £ 10,000 in debentures, conferring a charge over all the company's assets, £ 20,000 in fully paid up £ 1 shares, and the balance in cash. Seven shares were subscribed in cash by the members and the result was that Salomon held 20,001 shares out of 20,007 shares issued, and each of the remaining six shares was held by a member of his family. The company almost immediately ran into difficulties and only a year later, the holder of debentures (Salomon had transferred his shares to another person) appointed a receiver and the company went into liquidation. On liquidation the state of affairs of the company was broadly like this:

Realizable value of Assets: £ 6,000; Liabilities: Debentures-£ 10,000; Unsecured Debts- £

7,000.

Thus, after paying off the debenture holders nothing would be left for the unsecured creditors. An action was brought by the liquidator against Salomon holding him liable to indemnify the company against the company's trading debts.

Argument

The Liquidator and creditors contended that though Salomon & Co. Ltd. was incorporated under the Act, the company never had an independent existence. It was only a one man show since all the shares except six were held by Salomon himself. The vast preponderance of shares made Salomon absolute master. The business was solely conducted for and by him and the company was mere sham and fraud.

Points of Discussion

1. Whether the Salomon & Co. Ltd. was a company at all?
2. Whether in truth the separate legal entity, the company, had been validly created in this case?
3. Whether Salomon was liable for the debts of the company?
4. Whether the argument of unsecured creditors was valid?

Judgement

Rejecting the contention of the Liquidator and unsecured creditors that all the shares were bought by Salomon and his family members and that the company was nothing but one man show, House of Lords held that the provisions of the Act did not require that the persons subscribing shall not be related to each other or that holding of a single share shall not afford a sufficient qualification for membership. Whether the capital of the company is owned by seven persons in equal share, with the right to equal share in profits, or whether it is almost owned by one person who takes practically the whole profits, it does not concern a creditor of the company. The company does not lose its identity if the bulk of its capital is held by one person. The company at law is altogether different person from its subscribers. The House of Lords further stated that the Act said nothing about the subscribers being independent or that they should take a substantial interest in the undertaking, or that they should have a mind and will of their own. Thus, the Salomon & Co. Ltd. was a legal company that had separate legal identity in eyes of law.



Source: <https://lawlex.org/lex-bulletin/case-summary-salomon-v-salomon-co-ltd/23368>

4. Perpetual existence or succession: Being an artificial person a company never dies, nor does its life depend on the life of its members. A company is an artificial person created by law, thus it can be dissolved through the process of law. Its life does not depend on the death, insolvency or retirement of any or all shareholders or directors.



10 persons incorporated a limited liability company by the name "Trends Footwear limited company" for carrying on a business of trade in Men footwears. All of them subscribed to the shares of the company on an equal basis. One day, they planned to go for River Rafting and while doing the sport, they all together got dead in the deep water of the river.

Point of Discussion

Will the company dissolve with the death of all its members?

Judgement (Hint)

No, due to perpetual succession.

5. Common seal

- The common seal acts as the official signature of the company.
- In Companies Act, 2013, a common seal was required for a Company to provide various authorizations and attestations on behalf of the Company.
- The requirement for common seal has now been made optional.



Companies (Amendment Act, 2015) provided that in case a company does not have a common seal, the authorization shall be made by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary.

6. Limited liability

A company may be:

- a company limited by shares or
- a company limited by guarantee

In a company limited by shares, the liability of members is limited to the unpaid value of shares.

In a company limited by guarantee, the liability of members is limited to such amount as the member may undertake to contribute to the assets of the company in the event of being wound up.



If the face value of a share is 10 and a member has already paid 8 per share, he can be called upon to pay not more than 2 per share during the lifetime of a company or at the time of its winding up.

7. Transferable shares

- In case of a public company, the share are freely transferable.
- The articles of a company must prescribe the manner in which such transfer of shares will be made.

8. Separate property

- Being as separate legal entity, a company is capable of owning, enjoying and disposing of property in its own name.
- Company's property can be controlled, managed and disposed of by the company only.



Macaura V Northern Assurance Co Ltd (1925)

Mr. Macaura owned the Killymoon estate in County Tyrone, Northern Ireland. He sold all of his estate timber to a company by the name "Irish Canadian Sawmills Ltd" for 42,000 fully paid up £1 shares, making him the whole owner (with nominees). Mr. Macaura was also an unsecured creditor for £19,000. 'Macaura' held all except one share of a timber company.

He insured the company's timber in his personal name with Northern Assurance cover for fire. Two weeks later, the timber got destroyed by a fire. However, Northern Assurance refused to pay up because the timber was owned by the company, and that because the company was a separate legal entity, it did not need to pay Mr. Macaura any money.

On the other hand, Mr. Macaura contended that he was the major shareholder and creditor of the company. Thus, being the owner of the company, the company's loss is his own loss. Therefore, under the insurance contract, Northern Assurance Co Ltd should compensate the loss of Mr. Macaura.

Point of Discussion

Was the Northern Assurance Co Ltd liable for the contract?

Judgement

It was held that Northern Assurance Co Ltd, the insurers were not liable on the contract, since the timber that perished in the fire did not belong to Mr. Macaura, who held the insurance policy.



Source: Gupta, P. *Legal aspects of Business: Concept and Applications*.
Vikas Publishing House Pvt. Ltd.

9. Delegated Management

A company is an autonomous, self-governing and self-controlling organization. Since, it has a large number of members, all of them cannot take part in the management of the affairs of company. Actual control and management therefore, delegated by the shareholders to their elected representatives, known as directors. They look after the day to day working of the company.

8.5 Lifting the Corporate Veil

Lifting the corporate veil means disregarding the corporate personality and looking behind the real person who controls the company's affairs. In simple words, if someone makes a fraudulent and dishonest use of the legal entity, he will not be allowed to take shelter behind the corporate personality. In this regard, the court will break through the corporate shell and apply the principle of what is known as lifting or piercing through the corporate veil.

Judicial Provisions or Grounds for Lifting the Veil

1. Fraud or improper conduct
 2. Protection of revenue
 3. Enemy character
 4. Where the company is a sham
 5. Company avoiding legal obligations
 6. Single economic entity
 7. Company acting as agency or trust
 8. Avoidance of welfare legislation
 9. Public interest
-
1. **Fraud or improper conduct:** The court may pierce the corporate veil when it feels that fraud is or could be perpetrated behind the veil.
 2. **Protection of revenue:** The court can disregard the separate existence of the company where the sole purpose for which it appears to have been formed is tax evasion.
 3. **Enemy character:** A company may assume an enemy character when person in de facto control of its affairs, reside in an enemy country.
 4. **Where the company is a sham:** When a company is used to shield the wrongful acts of its directors and shareholders, the corporate veil will be pierced.
 5. **Company avoiding legal obligations:** If an incorporated company is used to avoid legal obligations, the court may disregard the legal personality of the company.
 6. **Single economic entity:** In the case of group of enterprises, the corporate legal entity may be set aside in order to examine the economic realities of the group itself.
 7. **Company acting as agency or trust:** Where the company is acting as an agent for its shareholders, the shareholders cannot hide themselves behind corporate veil. Thus, they will be liable for the acts of the company.
 8. **Avoidance of welfare legislation:** In every case, where ingenuity is expended to avoid welfare legislation, the court gets behind the scenes to discover the true state of affairs.
 9. **Public interest:** It is the duty of the court to lift the veil to protect public policy and prevent transactions contrary to public policy.

Statutory Provisions or Grounds for Lifting the Veil

1. Reduction in the number of members
2. Fraudulent trading
3. Misdescription of the company
4. Premature trading

5. Failure to refund application money
 6. Holding and subsidiary companies
1. **Reduction in the number of members:** If a company carries on business for more than six months after the number of its members has been reduced to seven in the case of a public company and two in case of a private company, every person who knows this fact will be jointly and severally liable for the payment of debts contracted after six months.
 2. **Fraudulent trading:** If any business of a company is carried on with the intent to defraud creditors or any other person or for any fraudulent purpose, then every person who was knowingly a party to the carrying on of the business in that manner is liable to imprisonment or fine or both.
 3. **Misdescription of the company:** When any officer of the company or any other person acting on behalf of company signs or authorizes to be signed on behalf of the company any negotiable instrument in which name is not mentioned in legible letters, then such person is personally liable to the holder of the instrument unless the company has already paid the amount. Such person may also be liable to pay fine.
 4. **Premature trading:** A public limited company newly incorporated as such must not "do business or exercise any borrowing power" until it has obtained from the registrar of companies a certificate that has complied with the provisions of the act relating to the raising of the prescribed share capital or until it has re-registered as a private company. If it enters into any transaction contrary to this provision not only are the company and its officers in default, liable to pay fines but if the company fails to comply with its obligations in that connection within 21 days of being called upon to do so, the directors of the company are jointly and severally liable to indemnify the other party in respect of any loss or damage suffered by reason of the company's failure.
 5. **Failure to refund application money:** Where the company fails to refund the money of the applicants within 130 days of the date of issue of prospectus. Then, the directors of the company are jointly and severally liable to repay the application money with interest.
 6. **Holding and subsidiary companies:** Subsidiary company may lose its separate entity in the following two circumstances:
 - a) Where at the end of its financial year, the company has subsidiaries, it must lay before its members in general meeting not only its own accounts, but also attach therewith annual accounts of each of its subsidiaries along with copies of the boards and auditors' reports; and
 - b) A statement of the holding company's interest in the subsidiary.

The court may, on the facts of a case, treat a subsidiary as merely a branch or department of one large undertaking owned by the holding company.

8.6 Kinds of Companies

On the basis of Incorporation

- o Chartered company
- o Statutory company
- o Registered company

On the basis of Liability

- o Companies with limited liability
- o Unlimited companies

Legal Aspects of Business

On the basis of number of members or size

- o Public company
- o Private company

On the control

- o Holding company
- o Subsidiary company
- o Associate company

On the basis of Ownership

- o Government companies
- o Foreign companies
- o Indian companies

Other companies

- o Investment companies
- o Producer companies
- o Dormant companies

On the basis of Incorporation

1. Chartered Companies:

Charters are legal documents that legally set up corporate companies. Only national and regional governments are authorized to issue charters. These companies are incorporated under special charter issued by the head of state. As these companies are incorporated under special charter, thus the power and nature of business of a chartered company are defined by the charter which incorporates it.



Chartered companies do not exist in India.



Examples

- The East India Company
- The Bank of England

2. Statutory Companies

A company which is created by a special Act of Parliament or State Legislature is called a Statutory Company and is governed by the provisions of that Act. These companies are formed mainly with an intention to provide the public services or to meet social needs and not for the purpose of earning profits. These companies are not required to have any Memorandum or Articles of Association.



Examples

- Reserve Bank of India, State Bank of India
- Life Insurance Corporation, Unit Trust of India
- State Trading Corporation



Though primarily they are governed under that Special Act, still the CA, 2013 will be applicable to them except where the said provisions are inconsistent with the provisions of the Act creating them (as Special Act prevails over General Act). Such companies derive their powers from the Act constituting them and enjoy certain powers under the Companies Act.

Principal Characteristics of a Statutory Company

- Owned by state
- Governance by special act
- Immunity from parliamentary scrutiny
- A body corporate
- Distinct relation with the government
- Independent finances
- Commercial audit
- Operation on business principles

3. Registered companies

Companies registered under the CA, 2013 or under any previous Company Law 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 it by the Registrar.

*Examples*

- Hindustan Unilever Ltd.
- Google India Pvt. Ltd.
- Procter and Gamble India Ltd.

On the basis of Liability**1. Companies with Limited Liability**

- **Companies limited by shares:** A company limited by shares is a registered company having the liability of its members limited by its memorandum of association to the amount, if any, unpaid on the shares respectively held by them. The amount remaining unpaid on the shares can be called up at any time – during the lifetime of the company or at the time of winding up. However, a shareholder cannot be called upon to pay more than the amount remaining unpaid on his shares.

His personal assets cannot be called upon for the payment of the liabilities of the company, if nothing remains to be paid on the shares purchased by him.

Basically, a shareholder is liable only up to the amount of face value of shares subscribed by him.

- **Companies limited by guarantee:** A company limited by guarantee is one having the liability of its members limited by the memorandum to such amount as the members may respectively undertake by the memorandum to contribute to the assets of the company in the event of its being wound up. The liability of the members of a guarantee company is limited by a stipulated sum mentioned in the memorandum. The guaranteed amount can be called up by the company from the members only at the time of winding up if the liabilities of the company exceed its assets.

2. Unlimited Companies

An unlimited company is a company not having any limit on the liability of its members. The members of such a company are liable, in the event of its being wound up, to the full extent of their fortunes to meet the obligations of the company. Even their private properties can be attached or called upon to meet the claim of the company's creditors.

Such companies may or may not have share capital. They may be either a public company or a private company.

The articles of the company shall state the number of members with which the company is to be registered.

On the basis of Number of Members

1. Public Companies

2. Private companies

- One person company
- Small company

1. Public Company - Sec. 2(71)

"Public company" means a company which--

- is not a private company;
- has a minimum paid-up share capital as may be prescribed:

Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.

- The words of five lakh rupees or such higher paid-up capital, omitted by Act 21 of 2015, s. 2 (w.e.f. 29-5-2015).
- Section 3(1) of the CA, 2013– Public company may be formed for any lawful purpose by 7 or more persons.
- Section 4(1)(a) of the CA, 2013 – A public company is required to add the words “Limited” at the end of its name.
- Section 149(1) of the CA, 2013 – Every public company shall have minimum 3 director in its Board.
- It is the essence of a public company that its shares and debentures can be transferable freely to the public unlike private company. Only the shares of a public company are capable of being dealt in on a stock exchange.
- A private company that is a subsidiary of a public company, will be considered a public company.

2. Private Company – Sec. 2(68)

A private company means a company which by its articles –

- a. Restricts the right to transfer its shares;
- b. Limits the number of its members to 200 hundred (except in case of OPC)

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:

The words of one lakh rupees or such higher paid-up share capital omitted by Act 21 of 2015, s. 2 (w.e.f. 29-5-2015).

Provided further that--

(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 ceased,

shall not be included in the number of members; and

(C) prohibits any invitation to the public to subscribe for any securities of the company;

- Section 3(1) of the CA, 2013 – Private Company may be formed for any lawful purpose by 2 or more persons.
- Section 149(1) of the CA, 2013 – Every Private company shall have minimum 2 director in its Board.

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- Section 4(1)(a) of the CA, 2013 – A private company is required to add the words “Private Ltd” at the end of its name.
- Special privileges – Private Companies enjoys several privileges and exemptions under the Companies Act.

Public Company V. Private Company

Private Limited Company	Public Limited Company
Minimum Capital- NIL Right to transfer the shares: Restricted	Minimum Capital- NIL Right to transfer of shares are allowed
Minimum members 2 (Two), Maximum members 200 (Two Hundred)	Minimum members 7 (Seven), Maximum members No Limits
Public offer is not applicable and no requirement of dematerialization of securities	In case of public offer of securities, the securities have to be in Dematerialized Form
Listing of securities on Stock exchange Not Applicable	Securities offered in Public Offer, to be listed in Recognized Stock Exchanges
Quorum of Meetings Two members personally present	Quorum of Meetings Five in case of Members up to 1000; Fifteen in case of Members more than 1000 up to 5000; Thirty in case of Members exceed 5000.
No restriction on amount of managerial remuneration	Managerial Remuneration is restricted to 11% of Net profit (subject to conditions); OR at least 30 lakh p.a. depending upon paid up capital
Retire by rotation is Not Applicable	At least two-third of total number of directors be liable to retire by rotation and eligible of being re-appointed in AGM
A private company may commence its business immediately after obtaining certificate of incorporation.	A public company cannot commence its business unless it is granted a certificate of commencement of business.
Not required to issue prospectus	Required to issue a prospectus or file a statement in lieu of prospectus with the registrar of companies before allotting shares.

One Person Company (OPC)

- One Person Company means a company which has only one person as a member. - Sec. 2(62)
- OPC (as private company) may be formed for any lawful purpose by 1 person. –Sec. 3(1)
- OPC shall have minimum 1 director in its Board, its sole member can also be director of such OPC. - Sec. 149 (1)

Features

Single-member: OPCs can have only 1 member or shareholder, unlike other private companies.

Nominee: A unique feature of OPCs that separates it from other kinds of companies is that the sole member of the company has to mention a nominee while registering the company. Since there is

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only one member in an OPC, his death will result in the nominee choosing or rejecting to become its sole member. This does not happen in other companies as they follow the concept of perpetual succession.

Special privileges: OPCs enjoys several privileges and exemptions under the Companies Act.

Small Company- Sec. 2(85)

“small company” means a company, other than a public company, –

1. paid-up share capital of which does not exceed 50 lakh rupees, or such higher amount as may be prescribed which shall not be more than 10 crore rupees; and
2. turnover of which as per profit and loss account for the immediately preceding financial year does not exceed 2 crore rupees or such higher amount as may be prescribed which shall not be more than 100 crore rupees.

Provided that nothing in this clause shall apply to –

- a holding company or a subsidiary company;
- a company registered under section 8; or
- a company or body corporate governed by any special Act;

Special privileges: Small Company enjoys several privileges and exemptions under the Companies Act.

On the basis of Control

1. Holding Company
2. Subsidiary company
3. Associate Company

1. Holding Company – Sec. 2(46)

“A holding company, in relation to one or more other companies, means a company of which such companies are subsidiary companies”.

2. Subsidiary Company – Sec. 2(87)

Subsidiary company or subsidiary, in relation to any other company (that is to say the holding company), means a company in which the holding company:

- a) Controls the composition of the Board of Directors; or
- b) exercises or controls more than one-half of the total voting power/ of the total share capital either at its own or together with one or more of its subsidiary companies.

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

For the purposes of this clause-

1. a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;
2. the composition of a company’s Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;
3. the expression “company” includes anybody corporate;
4. “layer” in relation to a holding company means its subsidiary or subsidiaries.

3. Associate Company – Sec. 2(6)

“Associate company”, in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.

For the purpose of this clause:

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1. the expression "significant influence" means control of at least 20% of total voting power, or control of or participation in business decisions under an agreement;
2. the expression "joint venture" means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement;

On the basis of Ownership

1. Government Company
2. Foreign company
3. Indian company

1. Government Company – Sec. 2(45)

"Government company" means any company in which not less than 51 % of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments and includes a company which is a subsidiary company of such a government company.



Explanation – "paid-up share capital" shall be construed as "total voting power", where shares with differential voting rights have been issued.

Special privileges: Government Company enjoys several privileges and exemptions under the Companies Act.

2. Foreign Company – 2(42)

foreign company" means any company or body corporate incorporated outside India which, –

- a) has a place of business in India whether by itself or through an agent, physically or through electronic mode; and
- b) conducts any business activity in India in any other manner.

Section 379 to Section 393 of the CA, 2013 prescribes the provisions which are applicable on such companies for registering in India.

3. Indian Company

A company formed and registered in India is known as an Indian Company.

Other Companies

1. Investment Company
2. Producer Company
3. Dormant Company

1. Investment Company

"Investment company" means a company whose principal business is the acquisition of shares, debentures or other securities.

2. Producer Company

Producer Company" means a body corporate having objects or activities specified in section 581B and registered as Producer Company under the Companies Act, 1956.

In other words, A producer company can be defined as a legally recognized body of farmers/ agriculturists with the aim to improve the standard of their living, and ensure a good status of their available support, incomes and profitability.



Recently the Companies (Amendment) Bill, 2020 was introduced in Lok Sabha i.e., on March 17, 2020. Thus, with this bill aims to remove these provisions and adds a new chapter in the Act with similar provisions on producer companies.

Some Conditions for Producer Company

- Only persons engaged in an activity connected with, or related to, primary produce can participate in the ownership.
- The members have necessarily to be primary producers.
- Name of the company shall end with the words "Producer Company Limited".

On registration, the Producer Company shall become as if it is a private limited company for the purpose of application of law and administration of the company, However it shall comply with the specific provisions of part IXA until a special Act is enacted for Producer Companies.

To incorporate Producer Company any of the following combination of producers is required:

- 10 or more producers (individuals); or
- 2 or more producer institutions; or
- Combination of the above 2.

Every Producer Company shall have at least 5 directors but not more than 15. Provided that in the case of an inter-State co-operative society incorporated as a Producer Company, such Company may have more than 15 directors for a period of one year from the date of its incorporation as a Producer Company.

PART IXA of Companies Act 1956 comprises of XII Chapters which prescribes different provisions to be complied by Producer Company.

3. Dormant Company – Sec. 455

(1) Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.



For the purposes of this section

- (i) "inactive company" means a company which has not been carrying on any business or operation, or has not made any significant accounting transaction during the last two financial years or has not filed financial statements and annual returns during the last two financial years;
- (ii) "significant accounting transaction" means any transaction other than –
 - (a) payment of fees by a company to the Registrar;
 - (b) payments made by it to fulfil the requirements of this Act or any other law;
 - (c) allotment of shares to fulfil the requirements of this Act; and
 - (d) payments for maintenance of its office and records.

(2) The Registrar on consideration of the application shall allow the status of a dormant company to the applicant and issue a certificate in such form as may be prescribed to that effect.

(3) The Registrar shall maintain a register of dormant companies in such form as may be prescribed.

(4) In case of a company which has not filed financial statements or annual returns for two financial years consecutively, the Registrar shall issue a notice to that company and enter the name of such company in the register maintained for dormant companies.

(5) A dormant company shall have such minimum number of directors, file such documents and pay such annual fee as may be prescribed to the Registrar to retain its dormant status in the register and may become an active company on an application made in this behalf accompanied by such documents and fee as may be prescribed.

(6) The Registrar shall strike off the name of a dormant company from the register of dormant companies, which has failed to comply with the requirements of this section.

Procedural Formalities to get the status of a Dormant Company

- File form MSC-1 + Fees _ Consent of 3/4th of the shareholders (in value) either by special resolution in the meeting or issuing notice to the shareholders.
- Registrar to issue certificate in Form MSC-2.
- The registrar shall maintain the registrar of dormant companies. The same is maintained on www.mca.gov.in or any other specified website.

8.7 Limited Liability Partnership (LLP)

Limited Liability Partnerships (LLPs) are commercial vehicles which combine the features of partnership and company form of business. The concept of Limited Liability Partnership (LLP) has been introduced in India by way of Limited Liability Partnership Act, 2008 (notified on 31st March 2008). LLP is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership. The LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name.

- The LLP is a separate legal entity, is liable to the full extent of its assets but liability of the partners is limited to their agreed contribution in the LLP.
- In an LLP one partner is not responsible or liable for another partner's misconduct or negligence.
- Further, no partner is liable on account of the independent or un-authorized actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct.
- In an LLP, all partners have limited liability for everyone's protection within the partnership, similar to that of the shareholders of a limited company.
- However, unlike the company shareholders, the partners have the right to manage the business directly. An LLP also limits the personal liability of a partner for the errors, omissions, incompetence, or negligence of the LLP's employees or other agents.
- Mutual rights and duties of the partners within a LLP are governed by an agreement between the partners or between the partners and the LLP as the case may be. The LLP, however, is not relieved of the liability for its other obligations as a separate entity.
- Since LLP contains elements of both 'a corporate structure' as well as 'a partnership firm structure' LLP is called a hybrid between a company and a partnership.

Limited Liability Partnership (LLP): Need

The Limited Liability Partnership (LLP) is viewed as an alternative corporate business vehicle that provides the benefits of limited liability but allows its members the flexibility of organizing their internal structure as a partnership based on a mutually arrived agreement.

The LLP form would enable entrepreneurs, professionals and enterprises providing services of any kind or engaged in scientific and technical disciplines, to form commercially efficient vehicles suited to their requirements.

Owing to flexibility in its structure and operation, the LLP would also be a suitable vehicle for small enterprises and for investment by venture capital.

Keeping in mind the need of the day, the Parliament enacted the Limited Liability Partnership Act, 2008 which received the assent of the President on 7th January, 2009.

Limited Liability Partnerships (LLPs): Structure

LLP shall be a body corporate, and a legal entity separate from its partners. It will have perpetual succession.

Limited Liability Partnerships (LLPs): Requirements**Partner:**

- A minimum of two partners will be required for formation of an LLP. There will not be any limit to the maximum number of partners.
- A body corporate can also be Partner of LLP.

Designated Partner:

- Every LLP shall be required to have at least TWO DESIGNATED PARTNERS.
- Designated Partners shall be Individuals.
- At least one of the Designated Partner shall be a resident of India.
- 4. In case of a LLP 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 LLP or nominees of such bodies corporate shall act as designated partners.

Registered Office:

Every LLP shall have a registered office to which all Communications and Notices may be addressed and where they shall be received. (Section- 13).

LLP Act, 2008: Salient Features

(i) The LLP shall be a body corporate and a legal entity separate from its partners. Any two or more persons, associated for carrying on a lawful business with a view to profit, may by subscribing their names to an incorporation document and filing the same with the Registrar, form a Limited Liability Partnership. The LLP will have perpetual succession;

(ii) The mutual rights and duties of partners of an LLP inter se and those of the LLP and its partners shall be governed by an agreement between partners or between the LLP and the partners subject to the provisions of the LLP Act 2008. The act provides flexibility to devise the agreement as per their choice. In the absence of any such agreement, the mutual rights and duties shall be governed by the provisions of proposed the LLP Act;

(iii) The LLP will be a separate legal entity, liable to the full extent of its assets, with the liability of the partners being limited to their agreed contribution in the LLP which may be of tangible or intangible nature or both tangible and intangible in nature.

No partner would be liable on account of the independent or un-authorized actions of other partners or their misconduct. The liabilities of the LLP and partners who are found to have 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 LLP;

(iv) Every LLP shall have at least two partners and shall also have at least two individuals as Designated Partners, of whom at least one shall be resident in India. The duties and obligations of Designated Partners shall be as provided in the law;

(v) The LLP shall be under an obligation to maintain annual accounts reflecting true and fair view of its state of affairs. A statement of accounts and solvency shall be filed by every LLP with the Registrar every year.

The accounts of LLPs shall also be audited, subject to any class of LLPs being exempted from this requirement by the Central Government;

(vi) The Central Government have powers to investigate the affairs of an LLP, if required, by appointment of competent Inspector for the purpose;

(vii) The compromise or arrangement including merger and amalgamation of LLPs shall be in accordance with the provisions of the LLP Act 2008;

(viii) A firm, private company or an unlisted public company is allowed to be converted into LLP in accordance with the provisions of the Act. Upon such conversion, on and from the date of certificate of registration issued by the Registrar in this regard, the effects of the conversion shall be such as are specified in the LLP Act.

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On and from the date of registration specified in the certificate of registration, all tangible (moveable or immovable) and intangible property vested in the firm or the company, all assets, interests, rights, privileges, liabilities, obligations relating to the firm or the company, and the whole of the undertaking of the firm or the company shall be transferred to and shall vest in the LLP without further assurance, act or deed and the firm or the company, 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;

(ix) The winding up of the LLP may be either voluntary or by the Tribunal to be established under the Companies Act, 1956. Till the Tribunal is established, the power in this regard has been given to the High Court;

(x) The LLP Act 2008 confers powers on the Central Government to apply provisions of the Companies Act, 1956 as appropriate, by notification with such changes or modifications as deemed necessary.

However, such notifications shall be laid in draft before each House of Parliament for a total period of 30 days and shall be subject to any modification as may be approved by both Houses;

(xi) The Indian Partnership Act, 1932 shall not be applicable to LLPs.

Limited Liability Partnerships (LLPs): Advantages

LLP form is a form of business model which:

- is organized and operates on the basis of an agreement.
- provides flexibility without imposing detailed legal and procedural requirements.
- (iii) enables professional/technical expertise and initiative to combine with financial risk-taking capacity in an innovative and efficient manner.

LLP V. Traditional Partnership firm

- Under “traditional partnership firm”, every partner is liable, jointly with all the other partners and also severally for all acts of the firm done while he is a partner.
- Under LLP structure, liability of the partner is limited to his agreed contribution. Further, no partner is liable on account of the independent or un-authorized acts of other partners, thus allowing individual partners to be shielded from joint liability created by another partner’s wrongful acts or misconduct.

LLP V. Company

- A basic difference between an LLP and a joint stock company lies in that the internal governance structure of a company is regulated by statute (i.e., Companies Act, 1956) whereas for an LLP it would be by a contractual agreement between partners.
- The management-ownership divide inherent in a company is not there in a limited liability partnership.
- LLP will have more flexibility as compared to a company.
- LLP will have lesser compliance requirements as compared to a company.

Steps to Register LLP

1. Do you want to start an Indian LLP?
2. Do you want to convert existing partnership firm into LLP?
3. Do you want to convert an existing private company/ unlisted public company into LLP?
4. Do you want to start a Foreign Limited Liability Partnership (FLLP)?

Steps to Register LLP (Start an Indian LLP)

To register a Indian LLP, you need to first apply for a Designated Partner Identification Number (DPIN), which can be done by filing eForm for acquiring the DIN or DPIN. You would then need to acquire your Digital Signature Certificate and register the same on the portal.

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Thereafter, you need to get the LLP name approved by the Ministry. Once the LLP name is approved, you can register the LLP by filing the incorporation form.

Steps for registration are as follows:

- Application for DIN or DPIN
- Acquire/ Register DSC
- New User Registration
- Incorporate a LLP
- File LLP Agreement



Step 1: Application for DIN or DPIN

All designated partners of the proposed LLP shall obtain “Designated Partner Identification Number (DPIN)”. You need to file eForm DIR-3 in order to obtain DIN or DPIN. In case you already have a DIN (Director Identification Number), the same can be used as a DPIN.

Step 2: Acquire/ Register DSC

Designated partner of LLP/proposed LLP, whose signatures are to be affixed on the e-forms has to obtain class Digital Signature Certificate (DSC) from any authorized certifying agency. Register Digital Signature of Designated Partner on the website of Ministry of Corporate Affairs.

Fill in the registration form. Fields marked * in the form are to be mandatorily filled. Upload digital signature certificate. On successful registration, system will give a message that you have been registered successfully.

Step 3: New User Registration

To file an eForm or to avail any paid service on LLP portal; you are first required to register yourself as a user in the relevant user category, such as registered and business user.

Search for name availability

Selection of business name is crucial for the image of your venture. You select a name which reflects the business you plan. Ensure selected name satisfy LLP Name Guidelines of Ministry of Corporate Affairs.

Free name search facility (of existing companies / LLPs) is available on MCA portal. The system will provide the list of similar/closely resembling names of existing companies/LLPs based on the search criteria filled up.

Step 4: Incorporate a LLP

Apply for the name of the LLP to be registered by filing Form 1 (Application for reservation or change of name) for the same. After that depending upon the proposed LLP, file required incorporation Form 2 (Incorporation document and Subscriber’s statement)

Once the form has been approved by the concerned official of the Ministry, you will receive an email regarding the same and the status of the form will get changed to Approved. To know more about e-Filing process click "All About e-Filing"

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Following Information are required to be filed in form LLP-1

- DIN of Designated Partner.
- Email Id
- Occupation
- State of Register office of Company
- Objects of LLP
- Partners Contribution into LLP
- Name of LLP
- Significant of Name
- If Proposed Name is Based on Trademark (NOC from the Owner of TM)
- DSC of Designated Partner

Step 5: File LLP Agreement

After incorporation of LLP, an initial LLP agreement is to be filed within 30 days of incorporation of LLP. The user has to file the information in Form 3 (Information with regard to Limited Liability Partnership Agreement and changes, if any, made therein).

How to convert an existing partnership firm into LLP

Any existing partnership firm that is willing to get converted into LLP will need to apply through Form 17 (Application and statement for the conversion of a firm into LLP. Form 17 needs to be filed along with Form 2 (Incorporation document and Subscriber's statement).

How convert an existing private company/ unlisted public company into LLP?

Any private company/ unlisted public company that is willing to get converted into LLP need to apply through Form 18 (Application and Statement for conversion of a private company/ unlisted public company into limited liability partnership (LLP). Form 18 needs to be filed along with Form 2 (Incorporation document and Subscriber's statement).

How to a Foreign Limited Liability Partnership (FLLP)?

Any Foreign LLP can establish its place of business in India by filling Form 27 (Registration of particulars by Foreign Limited Liability Partnership (FLLP)). The eForm has to be digitally signed by authorized representative of the FLLP.

There is no mandatory requirement to apply and obtain DPIN or DIN for Designated Partners of FLLP but the DSC of the authorized representative is mandatory.

8.8 Formation of Company: Stages

When we talk about forming a company, then there are 2 stages that we have to go through. These are:

- Promotion Stage
- Incorporation Stage

Promotion Stage:

The term 'promotion' refers to the sum total of activities by which a business enterprise is brought into existence. At the promotion stage of a company, the promoters conceive the idea of promoting a company and the type of activities that it intends to undertake.

Who promotes a Company?

It is the promoter or promoters who promote/s a company. 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 of the Board of Directors of the company is accustomed act.

In other words, A promoter is a person who does the necessary preliminary work incidental to the formation of a company. It is a compendious term used for a person who undertakes, does and goes through all the necessary and incidental preliminaries, keeping in view the object, to bring into existence an incorporated company.

A promoter may be an individual (like Jamsetji N. Tata, G.D. Birla, Dhirubhai H. Ambani, etc., the great promoters), a group of individuals or one or more companies (promoting a company by another company or group of companies is becoming very popular). Subsequently, activities related to promoting the company are undertaken.

Functions of Promoter

- Deciding the name of company and ascertains that it will be accepted by the Registrar of companies.
- Settles the details of the company's MOA and AOA, the nomination directors, solicitors, bankers, auditors and secretary and the registered office of the company.
- Arranging for printing of MOA.
- Follow the procedure to incorporate the company.
- Make arrangement to prepare a prospectus and issue of the same in case the company will go for public issue to finance itself.

Incorporation Stage

Formation of Company: Sec. 3

(1) A company may be formed for any lawful purpose by--

- (a) seven or more persons, where the company to be formed is to be a public company;
- (b) two or more persons, where the company to be formed is to be a private company; or
- (c) one person, where the company to be formed is to be One Person Company that is to say, a private company,

(2) A company formed under sub-section (1) may be either--

- (a) a company limited by shares; or

- (b) a company limited by guarantee; or
(c) an unlimited company.

- Members severally liable in certain cases (Sec. 3A)

If at any time the number of members of a company is reduced, in the case of a public company, below seven, in the case of a private company, below two, and the company carries on business for more than six months while the number of members is so reduced, every person who is a member of the company during the time it so carries on business after those six months and is cognizant of the fact that it is carrying on business with less than seven members or two members as the case may be, shall be severally liable for the payment of the whole debts of the company contracted during that time, and may be severally sued therefore.

8.9 Procedure for Incorporating Company

1. Name reservation for new companies

- Name will be reserved by using Part A of SPICe+ (Simplified Proforma for Incorporating Company Electronically Plus: INC-32),
- From 23rd February 2020 onwards, RUN service would be applicable only for 'change of name' of an existing company.
- Select, in order of preference, at least one suitable name up to a maximum of six names, indicative of the main objects of the company.
- Ensure that the name does not resemble the name of any other already registered company and also does not violate the provisions of emblems and names (Prevention of Improper Use Act, 1950) by availing the services of checking name availability on the portal.
- Apply to the concerned RoC to ascertain the availability of name in eForm 1 A by logging in to the portal. A fee of ₹ 500/- has to be paid alongside and the digital signature of the applicant proposing the company has to be attached in the form. If proposed name is not available, the user has applied for a fresh name on the same application.
- After the name approval the applicant can apply for registration of the new company by filing the required forms (that is Form 1, 18 and 32) within 60 days of name approval.



- Form-1 - Declaration of compliance.
- Form-18 - Notice of situation of registered office of the company -
- Form-32 - Particulars of the Director's, Manager or Secretary.

2. Obtain DIN and DSC

- Obtain Director Identification Number (DIN) for proposed Directors of the new company.
- Obtain Digital Signature Certificate (DSC) for proposed Directors of the Company.

Fee for Registration

For One Person and Small Companies

Nominal Share Capital	Registration Fees
Limited to 10,00,000	2,000

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10,00,000 to 50,00,000	2000. 200 will be added for every 10,000 or part thereof of nominal share capital.
50,00,000 to 1 crore	1,56,000. 100 will be added for every 10,000 or part thereof of nominal share capital.
More than 1 crore	2,06,000. 75 will be added for every 10,000 or part thereof of nominal share capital subject to a maximum of 250 crore.

For Companies without a Share Capital

Number of Members	Registration Fees
Limited to 20	2,000
Exceeds 20, but is limited to 200	5,000
Exceeds 200, on the condition that the number of members stated in the AOA isn't "unlimited"	5,000. 10 will be added for every member after counting the first 200, subject to a maximum of 10,000.

For Companies with Share Capital Other Than One Person and Small Companies

Nominal Share Capital	Registration Fees
Limited to 1,00,000	5,000
1,00,000 to 5,00,000	5,000. 400 will be added for every 10,000 or part thereof of nominal share capital.
5,00,000 to 50,00,000	21,000. 300 will be added for every 10,000 or part thereof of nominal share capital.
50,00,000 to 1 crore	2,06,000. 100 will be added for every 10,000 or part thereof of nominal share capital.
More than 1 crore	2,06,000. 75 will be added for every 10,000 or part thereof of nominal share capital subject to a maximum of 2.50 crores.

3. Application of Incorporation (Filing Form SPICe+)

- Incorporation applications (Part B) after name reservation (In Part A) will be submitted as a seamless process in continuation of Part A of SPICe+
- The new web form facilitates On-screen filing and real time data validation for seamless incorporation of companies.
- The approved name and related incorporation details as submitted in Part A, would be automatically Pre-filled in all linked forms also viz., eMoA, eAoA, etc. (other forms as applicable)

4. eMOA

- This is the first time ever that MCA is allowing to prepare Memorandum of Association through an electronic medium.

- Now in E-form INC-33, which governs the e-filing of MOA, we just have to enter the objects of the company.
- In this e form subscribers DSC are affixed instead of physical signature.
- There is no need of signature of witness because in this scheme affix the DSC of witness.
- In case of incorporation of a company falling under section 8 of the Act, FORM No. INC-13 (Memorandum of Association) (spice plus)

5. eAOA

- AOA's have been filled electronically under the Simplified Proforma for Incorporating Companies Electronically.
- Now with the introduction of E-Form INC-34 (spice plus) which provides pre-drafted clauses of Articles of Association, we just have to select the clauses to be mentioned in the Articles and see if any clause is not applicable or need to be altered and then select it.
- With SPICe or with electronic filing of AOA, the process of filing these documents has become easy manifolds.
- In case of incorporation of a company falling under section 8 of the Act, FORM No. INC-31 (Articles of Association) (spice plus)

6. Other Attachment of E form:

- Declaration by the first director(s) and subscriber(s) (Affidavit not required)
- Proof of office address
- Copy of utility bills
- Copy of certificate of incorporation of foreign body corporate (if any)
- A resolution passed by promoter company
- The interest of first director(s) in other entities
- Consent of Nominee (INC-3)
- Proof of identity as well as the residential address of subscribers
- Proof of identity and address of Applicant I, II, III
- Optional attachments (if any)
- Attachments – Part A

7. Declaration by a Professional

The DSC of a professional (Company Secretary, Chartered Accountant, advocate, Cost Accountant) along with the professional's membership and certificate number is required to file SPICe + Form (a declaration that all information provided is accurate and true).

8. Submission of form

- Part B of SPICe+ and linked forms can then be uploaded on the MCA portal.
- A Service Request Number is generated for making a payment towards company incorporation.
- Once the payment is made successfully, the forms would be processed.
- In a case where the forms need resubmission for any errors being flagged upon processing, the SPICe+ form has to be resubmitted in the same manner.

9. Issue of certificate of Incorporation

The Certificate of Incorporation of company shall be issued by the Registrar in Form No. INC-11 after process of registration is completed.

Conclusiveness of Certificate of Incorporation on following points:

- That requirement of the Act in respect of registration of matters precedent and incidental thereto have been complied with.
- That the association is a company to be registered under the act and has been duly registered.
- That the date borne by the certificate of incorporation is the date of birth of the company, i.e., the date on which the company comes into existence.
- Even though the certificate of incorporation is conclusive for the purpose of incorporation, it does not make an illegal object a legal one.
- But the position is firmly established that if a company is born, the only method to put an end to it is by winding it up.

Certificate of Commencement of Business

Sec. 11 of the Companies Act, 2013 was omitted by the Companies (Amendment) Act 2015, thereby permitting all companies, whether private or public, to commence business immediately after obtaining certificate of incorporation.

However, Section 10 A inserted by Amendment Act, 2019 reinstated the requirement of filing a declaration to be made by the director of a company with 180 days of its incorporation to the effect that:

- a) Every subscriber to the memorandum has paid the value of the shares agreed to be taken by him on the date of making of such declaration; and
- b) The registered office of the company so incorporated has been verified by filing requisite returns.

As per the Companies (Amendment) Ordinance 2018, there is a requirement for all the companies registered on or after 2 November 2018 to file a declaration in form 20A within 180 days of the date of incorporation of the company for issuance of certificate of commencement

The following companies are not required to file form 20A:

Companies incorporated before 2 November 2018 (i.e., before the commencement of the Companies (Amendment) Ordinance, 2018).

Companies incorporated after 2nd November 2018 without share capital.

Penalties for Default

- **Penalty to be levied on the company:** A penalty of 50,000 will be levied on the company if it fails to comply with the mentioned requirement.
- **Penalty to be levied on the officers:** Every such officer in default shall be liable to a penalty of 1,000 per day for each day during which the default continues subject to a maximum of 1,00,000.
- **Company strike-off:** If the Registrar has reasonable grounds to believe that the company is not carrying on any business or operations even after 180 days of incorporation, the registrar may remove the name of the company from the Register of companies.

8.10 Companies (Incorporation) Amendment Rules, 2020

(1) These rules may be called the Companies (Incorporation) Amendment Rules, 2020.

(2) They have come into force with effect from the 23rd of February 2020.

In January 2020, the Ministry of Corporate Affairs (MCA), notified to issue new form SPICe + as a part of India's Ease of Doing Business initiatives.

The new form which is named Spice Plus or Spice+ shall be a replacement of the old system of spice 32 form.

It means spice 32, shall be discontinued the launch of the new web-based SPICe plus Form.

8.11 SPICe+ Form: Features

1. While SPICe is an eform, SPICe+ is an integrated Web form.

SPICe+ offers 11 services by 3 Central Govt Ministries & Departments (Ministry of Corporate Affairs, Ministry of Labour & Department of Revenue in the Ministry of Finance) and 3 State Governments (Maharashtra, Karnataka, West Bengal) and NCT - Delhi, thereby saving as many procedures as possible, time and cost for Starting a Business in India and is applicable for all new company incorporations w.e.f 7th June 2021.

SPICe+ is part of various initiatives and commitment of Government of India towards Ease of Doing Business (EODB).

2. SPICe+ has two parts viz.: Part A -for Name reservation for new companies and Part B offering a bouquet of services viz.

(i) Incorporation

(ii) DIN allotment (Director Identification Number)

(iii) Mandatory issue of PAN

(iv) Mandatory issue of TAN (Tax deduction and collection account number)

(v) Mandatory issue of EPFO (Employee's Provident Fund Organization) registration

(vi) Mandatory issue of ESIC (Employee State Insurance Corporation) registration

(vii) Mandatory issue of Profession Tax registration (Maharashtra, Karnataka and West Bengal)

(viii) Mandatory Opening of Bank Account for the Company

(ix) Allotment of GSTIN (if so, applied for) and

(x) First time registration of shops and establishment for all new companies getting incorporated in Delhi.

3. Users may either choose to submit Part-A for reserving a name first and thereafter submit Part B for incorporation & other services or file Part A and B together at one go for incorporating a new company and availing the bouquet of services as above.

4. A new and user-friendly Dashboard on the Front Office has been created for company incorporation application (SPICe+ and linked forms as applicable).

5. Incorporation applications (Part B) after name reservation (In Part A) can be submitted as a seamless process in continuation of Part A of SPICe+. Stakeholders are not required to even enter the SRN (Service Request Number) of the approved name as the approved Name is prominently displayed on the Dashboard and a click on the same will take the user for continuation of the application through a hyperlink that is available on the SRN/application number in the new dashboard.

6. Resubmission of applications for company name reservation and/or incorporation shall also be handled through the application number/Name applied for link on the new dashboard.

A hyperlink is available for the SRN/application number, so as to enable easy resubmission, wherever required.

7. From 23rd February 2020 onwards, RUN service would be applicable only for 'change of name' of an existing company.

8. The new web form Facilitates On-screen filing and real time data validation for seamless incorporation of companies.

9. The approved name and related incorporation details as submitted in Part A, would be automatically pre-filled in all linked forms also viz., AGILE-PRO-S, eMoA, eAoA, URC1, INC-9 (as applicable).

10. For ensuring ease while filing, SPICe+ is structured into various sections.

11. Information once entered can be saved and modified.

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12. All Check form and Pre-scrutiny validations (except DSC validation) happens on webform itself.
13. Once the SPICe+ is filled completely with all relevant details, the same would then have to be converted into pdf format, with just a click of the mouse button, for affixing DSCs.
14. All digitally signed applications can then be uploaded along with the linked forms as per the existing process.
15. Changes/modifications to SPICe+ (even after generating pdf and affixing DSCs), can also be done by editing the same web form application which has been saved, generating the updated pdf affixing DSCs and uploading the same.
16. DSC validation and other validations will happen at Upload Level.
17. Registration for EPFO and ESIC shall be mandatory for all new companies incorporated w.e.f 23 February 2020 and no EPFO & ESIC registration nos. shall be separately issued by the respective agencies.
18. Registration for Profession Tax shall also be mandatory for all new companies incorporated in the State of
 - Maharashtra w.e.f 23rd February 2020
 - Karnataka w.e.f 8th October 2020
 - West Bengal w.e.f 12th March 2020
19. All new companies incorporated through SPICe+ (w.e.f 23rd February 2020) are also mandatorily required to apply for opening the company's Bank account through the AGILE-PRO-S linked web form.
20. First time Registration Number for Shops and Establishment, Delhi shall be provided for all new companies getting incorporated in Delhi w.e.f 07 June 2021.
21. Declaration by all Subscribers and first Directors in INC-9 shall be auto-generated in pdf format and would have to be submitted only in electronic form in all cases, except where: (i) Total number of subscribers and/or directors is greater than 20 and/or (ii) Any such subscribers and/or directors has neither DIN nor PAN.

Major Changes

- From 23rd February 2020 onwards, RUN service would be applicable only for 'change of name' of an existing company.
- Registration for EPFO and ESIC shall be mandatory for all new companies incorporated w.e.f 15 February 2020 and no EPFO & ESIC registration nos. shall be separately issued by the respective agencies, but application is same i.e spice plus.
- Registration for Profession Tax shall also be mandatory for all new companies incorporated in the State of Maharashtra w.e.f 15th February 2020.
- All new companies incorporated through SPICe+ (w.e.f 15th February 2020) would also be mandatorily required to apply for opening the company's Bank account.

8.12 Incorporation of Company: Sec. 7

- (1) There shall be filed with the Registrar within whose jurisdiction the registered office of a company is proposed to be situated, the following documents and information for registration, namely: --
 - (a) the memorandum and articles of the company duly signed by all the subscribers to the memorandum in such manner as may be prescribed.
 - (b) a declaration in the prescribed form by an advocate, a chartered accountant, cost accountant or company secretary in practice, who is engaged in the formation of the company, and by a person named in the articles as a director, manager or secretary of the company, that all the requirements of this Act and the rules made thereunder in respect of registration and matters precedent or incidental thereto have been complied with.
 - (c) a declaration from each of the subscribers to the memorandum and from persons named as the first directors, if any, in the articles that he is not convicted of any offence in connection with the

Unit 08: The Companies Act, 2013 (Preliminary)

promotion, formation or management of any company, or that he has not been found guilty of any fraud or misfeasance or of any breach of duty to any company under this Act or any previous company law during the preceding five years and that all the documents filed with the Registrar for registration of the company contain information that is correct and complete and true to the best of his knowledge and belief;

(d) the address for correspondence till its registered office is established;

(e) the particulars of name, including surname or family name, residential address, nationality and such other particulars of every subscriber to the memorandum along with proof of identity, as may be prescribed, and in the case of a subscriber being a body corporate, such particulars as may be prescribed.

(f) the particulars of the persons mentioned in the articles as the first directors of the company, their names, including surnames or family names, the Director Identification Number, residential address, nationality and such other particulars including proof of identity as may be prescribed; and

(g) the particulars of the interests of the persons mentioned in the articles as the first directors of the company in other firms or bodies corporate along with their consent to act as directors of the company in such form and manner as may be prescribed.

(2) The Registrar on the basis of documents and information filed under sub-section (1) shall register all the documents and information referred to in that subsection in the register and issue a certificate of incorporation in the prescribed form to the effect that the proposed company is incorporated under this Act.

(3) On and from the date mentioned in the certificate of incorporation issued under sub-section (2), the Registrar shall allot to the company a corporate identity number, which shall be a distinct identity for the company, and which shall also be included in the certificate.

(4) The company shall maintain and preserve at its registered office copies of all documents and information as originally filed under sub-section (1) till its dissolution under this Act.

(5) If any person furnishes any false or incorrect particulars of any information or suppresses any material information, of which he is aware in any of the documents filed with the Registrar in relation to the registration of a company, he shall be liable for action under section 447.

(6) Without prejudice to the provisions of sub-section (5) where, at any time after the incorporation of a company, it is proved that the company has been got incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company, or by any fraudulent action, the promoters, the persons named as the first directors of the company and the persons making declaration under clause (b) of subsection (1) shall each be liable for action under section 447.

(7) Without prejudice to the provisions of sub-section (6), where a company has been got incorporated by furnishing any false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants:

(a) pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or

(b) direct that liability of the members shall be unlimited; or

(c) direct removal of the name of the company from the register of companies; or

(d) pass an order for the winding up of the company; or

(e) pass such other orders as it may deem fit:

Provided that before making any order under this sub-section,-

(i) the company shall be given a reasonable opportunity of being heard in the matter; and

(ii) the Tribunal shall take into consideration the transactions entered into by the company, including the obligations, if any, contracted or payment of any liability.

8.13 Some important contracts

- Preliminary Contracts or Pre-Incorporation Contracts
- Provisional Contracts

Preliminary contacts

Preliminary contracts are those contracts made before the formation of the company. As per the provisions of the act, neither the company can sue nor can it be sued to enforce the preliminary contracts.

Provisional Contracts

Whereas the contract entered by a company after incorporation but before it is entitled to commence business is termed as provisional contracts. whereas the provisional contracts can be enforced only on receiving a certificate of Commencement of Business.

Summary

- A company is a voluntary association of persons formed for the purpose of doing business having a distinct name and limited liability.
- A company is an artificial person created by law; thus it can be dissolved through the process of law.
- In a company limited by shares, the liability of members is limited to the unpaid value of shares.
- In a company limited by guarantee, the liability of members is limited to such amount as the member may undertake to contribute to the assets of the company in the event of being wound up.
- In case of a public company, the shares are freely transferable.
- Lifting the corporate veil means disregarding the corporate personality and looking behind the real person who controls the company's affairs.
- Companies which are incorporated under special charter or proclamation issued by the head of state, are known as chartered companies.
- An unlimited company is a company not having any limit on the liability of its members. The members of such a company are liable, in the event of its being wound up, to the full extent of their fortunes to meet the obligations of the company.
- A holding company, in relation to one or more other companies, means a company of which such companies are subsidiary companies.
- Associate company means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.
- Government company means any company in which not less than 51% of the paid-up share capital is held by the Central Government, or by any State Government or jointly by both Central and State Government.
- A company formed and registered in India is known as an Indian Company.
- A producer company can be defined as a legally recognized body of farmers/agriculturists with the aim to improve the standard of their living, and ensure a good status of their available support, incomes, and profitability.
- Limited Liability Partnerships (LLPs) are commercial vehicles which combine the features of partnership and company form of business.

- In an LLP, all partners have limited liability for each individual's protection within the partnership, similar to that of the shareholders of a limited company.
- The term 'promotion' refers to the sum total of activities by which a business enterprise is brought into existence. At the promotion stage of a company, the promoters conceive the idea of promoting a company and the type of activities that it intends to undertake.
- Name of company can be reserved by using Part A of SPICe+ (Simplified Proforma for Incorporating Company Electronically Plus: INC-32)
- In E-form INC-33, which governs the e-filing of MOA, we just have to enter the objects of the company.
- E-Form INC-34 (spice plus) which provides pre-drafted clauses of Articles of Association, we just have to select the clauses to be mentioned in the Articles and see if any clause is not applicable or need to be altered and then select it.
- The Certificate of Incorporation of company shall be issued by the Registrar in Form No. INC-11 after process of registration is completed.
- Sec. 11 of the Companies Act, 2013 was omitted by the Companies (Amendment) Act 2015, thereby permitting all companies, whether private or public, to commence business immediately after obtaining certificate of incorporation.
- SPICe+ is part of various initiatives and commitment of Government of India towards Ease of Doing Business (EODB).

Keywords

Company: The Companies Act, 1956 defines the word 'company' as a company formed and registered under the Act or an existing company formed and registered under any of the previous company laws.

Company Limited by Shares: A company limited by shares is a registered company having the liability of its members limited by its memorandum of association to the amount, if any, unpaid on the shares respectively held by them.

Government Company: Section 617 defines a Government Company as any company in which not less than 51% of the paid-up share capital is held by the Central Government, or by any State Government.

One Man Company: A member may hold virtually the entire share capital of a company. Such a company is known as a 'one-man company'.

Pre-incorporation contract: A pre-incorporation contract never binds a company since a person cannot contract before his (or its) existence and a company before incorporation has no legal existence.

Promoters: Promoters have been described to be in fiduciary relationship (relationship of trust and confidence) with the company.

Promotion: 'Promotion' is a term of wide import denoting the preliminary steps taken for the purpose of registration and floatation of the company.

Private Company: A private company can be formed by merely two persons by subscribing their names to the Memorandum of Association.

Subsidiary Company: A company over which control is exercised by that other company is called the Subsidiary Company.

Self Assessment

1. A Company has the right to acquire and dispose of property, to enter into a contract with third parties in its name, and can sue and be sued in its name. Which of its following characteristics?

- A. Limited liability
 - B. Artificial legal person
 - C. Common Seal
 - D. Perpetual existence
2. "Company's money and property belong to itself and not to its shareholders". It is an implication of which of its following characteristics?
- A. Incorporated association
 - B. Artificial legal person
 - C. Separate legal entity
 - D. Perpetual existence
3. A company continues to operate despite all of its members get died together due to:
- A. Incorporated association
 - B. Artificial legal person
 - C. Separate legal entity
 - D. Perpetual succession
4. A listed company's shares are free traded among traders, brokers and investors due to:
- A. Common seal
 - B. Limited liability
 - C. Transferable shares
 - D. Separate property
5. Identify the judicial provision for lifting the corporate veil from the following:
- A. Reduction in the number of members
 - B. Fraudulent trading
 - C. Misdescription of the company
 - D. Protection of revenue
6. The following type of companies does not exist in India.
- A. Chartered Companies
 - B. Statutory Companies
 - C. Registered Companies
 - D. Nidhi Companies
7. A shareholder is liable only up to the amount of face value of shares subscribed by him in case of:
- A. Company limited by shares
 - B. Company limited by guarantee
 - C. Unlimited companies
 - D. Small Companies

8. Which of the following companies are prohibited from sending any invitation to the public to subscribe to any company's securities?
- A. Private companies
 - B. Public companies
 - C. Government companies
 - D. Registered companies
9. "Government company" means any company in which not less than _____ of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments.
- A. 20%
 - B. 21%
 - C. 50%
 - D. 51%
10. Only persons engaged in an activity connected with, or related to, primary produce can participate in the ownership of:
- A. Small companies
 - B. One Person companies
 - C. Producer companies
 - D. Dormant companies
11. The LLP can continue its existence irrespective of changes in partners.
- A. True
 - B. False
12. The liability of the partners in case of LLP is:
- A. limited to their agreed contribution in the LLP
 - B. unlimited
 - C. limited to unpaid value of shares
 - D. limited as per their guarantee
13. LLP contains elements of:
- A. 'a corporate structure'
 - B. 'a partnership firm structure'
 - C. both 'a corporate structure' as well as 'a partnership firm structure'
 - D. neither 'a corporate structure' nor 'a partnership firm structure'
14. Every LLP shall be required to have at least:
- A. 1 Designated partner
 - B. 2 Designated partners
 - C. 3 Designated partners
 - D. 4 Designated partners

Legal Aspects of Business

15. There is no mandatory requirement to apply and obtain DPIN or DIN for Designated Partners of FLLP.
- A. True
 - B. False
16. While applying for a name reservation for a new company, the following point/s should be ensured:
- A. The name does not resemble the name of any other already registered company
 - B. The name does not violate the provisions of emblems and names
 - C. Neither the name should resemble the name of any other already registered company, nor should it violate the provisions of emblems and names
 - D. Any of above
17. The registration fee for Companies without a Share Capital having members up to 200 but exceeding 20 will be:
- A. 2,000
 - B. 3,000
 - C. 5,000
 - D. 5,000. 10 will be added for every member after counting the first 50
18. E-form INC-33 governs the e-filing of:
- A. MOA
 - B. AOA
 - C. DSC
 - D. DIN
19. The Certificate of Incorporation of the company shall be issued by the Registrar in Form No.:
- A. INC-11
 - B. INC-30
 - C. INC-31
 - D. INC-33
20. Suppose the Registrar has reasonable grounds to believe that the company is not carrying on any business or operations even ----- of incorporation. In that case, the Registrar may remove the name of the company from the Register of companies.
- A. after 90 days
 - B. after 180 days
 - C. after 270 years
 - D. after one year

Answers for Self Assessment

1. B	2. C	3. D	4. C	5. D
6. A	7. A	8. A	9. D	10. C
11. A	12. A	13. C	14. B	15. A
16. C	17. C	18. A	19. A	20. B

Review Questions

1. "The legal personality of a company is distinct from its members individually and collectively". Comment and point out the circumstances when the separate entity of a company is disregarded by the courts.
2. What are the statutory exceptions to the decision in Salomon's case?
3. Clearly explain the meaning of 'lifting of the corporate veil' of a company. Under what circumstances may the court lift the veil of a company?
4. Discuss in detail the features of a company in India.
5. Which are the judicial grounds to lift the corporate veil? Discuss in detail.
6. State the different kinds of companies recognized by the Companies Act, 2013 on the basis of incorporation.
7. Discuss about the dormant companies in detail.
8. Illustrate the various kinds of companies on the basis of control, number of members, liability and ownership.
9. Differentiate a public company from a private company.
10. Write short notes on the following:
 - a) Statutory companies
 - b) Small companies
 - c) One Person companies
 - d) Producer companies
11. Explain the concept of Limited Liability Partnership (LLP). Discuss the salient features of LLPs.
12. Discuss the requirements to start a Limited Liability Partnership. Explain the advantages of a Limited Liability Partnership.
13. Write the short notes on the following:
 - a) Limited Liability Partnership V. Traditional Partnership firm
 - b) Limited Liability Partnership V. Company
14. Illustrate the steps to register a Limited Liability Partnership in India.
15. Who is a promoter? Discuss in detail, the functions of a promoter.
16. What steps are required to be taken for the formation of a public limited company?
17. What does "conclusive evidence" mean in relation to the certificate of incorporation?
18. Explain the salient features of SPICe+ form.
19. Write the short notes on the following:
 - a) Certificate of Commencement of Business
 - b) Preliminary contracts

c) Provisional contracts



Further Reading

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Web Links

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https://www.mca.gov.in/Ministry/pdf/ThirdAmdtRules_24122020.pdf

<https://mca.gov.in/MinistryV2/reforms.html>

<https://www.indiafilings.com/learn/companies-incorporation-third-amendment-rules-2020/>

Unit 09: Company Documents

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Summary

Keywords

Self Assessment

Answers for Self Assessment

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Further Reading

Objectives

After studying this unit, you will be able to:

- appraise the importance of Memorandum of association for incorporation of company.
- review the various clauses of Memorandum of association of company.
- illustrate the doctrine of ultra vires along with its effects.
- explain the meaning and importance of Articles of Association.
- review the contents of Articles of Association.
- review the provisions of company's act, 2013 related to Articles of Association.
- review the provisions relating to alteration of articles.

- assess the relation and difference between Articles of Association and Memorandum of Association.
- comment on the importance of Articles of Association for incorporation of a company and its internal management.
- review the Doctrine of Constructive Notice and its legal implications.
- review the Doctrine of Indoor Management and its legal implications along with its exceptions.
- comment on importance of Doctrine of Constructive notice for a company in fighting lawsuits.
- comment on importance of Doctrine of Indoor management for a company and outsiders in fighting lawsuits.

Introduction

Memorandum is one of the most essential pre-requisites for incorporating any form of company under the Companies Act, 2013 as preparing a document called Memorandum of Association (MOA, Memorandum) is the primary step in the formation of a company. The Articles of Association (AOA) or just Articles are the rules, regulations and bye-laws for the internal management of the affairs of a company. They are framed with the object of carrying out the aims and objects as set out in the Memorandum of Association. The Articles are next in importance to the MOA which contains the fundamental conditions upon which alone a company is allowed to be incorporated. They are as such subordinate to, controlled by, the Memorandum.

In framing the Articles of a company care must be taken to see that regulations framed do not go beyond the powers of the company itself as contemplated by the MOA. It is mandatory for every kind of company to register its articles of association. In this unit, meaning, need, importance, and contents of these two primary company documents viz. Memorandum of Association and Articles of Association are discussed. Three important doctrines related to these two company documents viz. doctrine of ultra vires, constructive notice, and indoor management are also discussed in this unit.

9.1 Memorandum of association (MOA): Meaning and Definition

Memorandum of association (MOA): Meaning

- It acts as the charter of a company.
- It is a legal document prepared during the formation and registration process of a company to define the scope of company's activities and its relationship with the outside world.
- It contains the fundamental conditions upon which the company can be incorporated.
- It specifies the objectives for which the company has been formed.
- The company has to act within objects specified in the MOA. It means the company can undertake only those activities that are mentioned in the Memorandum of Association.



As such, the MOA lays down the boundary beyond which the actions of the company cannot go.

Memorandum of association (MOA): Definition

"Memorandum" means the memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this Act.

- Sec 2(56)

9.2 Memorandum of Association: Need and Importance

- It defines the scope of the company's activities and its relationship with outside world.
- It defines as well as confines the powers of the company. Anything done beyond the objects specified in the MOA will be ultra vires.
- It provides the foundation on which the structure of the company is built.
- Anything done beyond the objects specified in the MOA will be ultra vires. Their transactions will be null and void.
- MOA helps the shareholders, creditors and any other person dealing with the company to know the basic rights and powers of the company.
- Also, the contents of the MOA help the prospective shareholders in taking the right decision while thinking of investing in the company.
- MOA must be signed by at least 2 subscribers in case of a private limited company, and 7 members in case of a public limited company.

Apart from other information, the memorandum of association of a company contains the objects to be pursued by the company and it also determines the scope of its operation beyond which company cannot act. Let us discuss a case to understand the importance of memorandum for the proposed company.



Ashbury Railway Carriage & Iron Co Ltd V. Riche

Facts of the case

Ashbury Railway Carriage and Iron Co. Ltd., in the object clause of its MOA had stated that the object of the incorporation of the company was 'to make or sell, or lend, or hire, railway carriages and wagons, and all kinds of railway plants, fittings, machinery and rolling stock; to carry on the business of the mechanical engineers and the general contractors; to purchase and sell, as merchants, timber, coal, metals, or other materials; and to buy and sell any such materials on commission, or as agents.'

The directors of the company entered into a contract with Mr. Riche, for financing a construction of a railway line in Belgium.

The Clause 4 of the object clause specifically mentioned that beyond the scope of the above-mentioned clause, there was a need of a special resolution to indulge in any activity which was beyond the scope of this clause of the object clause in the MOA. However, the company superseded this requirement and agreed to give Mr. Riche the loan and financing they needed to build the railway line. The contract which was thus entered into by the company was ratified by all the members of the company. But later on, the contract was repudiated by the company. Mr. Riche sued the company for the breach of contract.

Arguments from Company

The company denied the existence and formation of any valid contract between the company and Mr. Riche. The contract was challenged on the ground that the company was not allowed by its memorandum to undertake any construction activity as the object clause of the memorandum of the company did not include the construction activity.

Arguments from Mr. Riche

He argued that company's memorandum allowed the rolling stock and thus the contract of construction of railway was very much in the permitted scope of company's activities. Therefore, the contract between him and the company was valid and enforceable.

Point of Discussion

Was there any valid contract between Company and Mr. Riche?

Judgment (Hint)

The judgment in this case, laid down the foundation of the rule of 'ultra vires', which

meant that the company was only allowed to do what it had been enabled to do in the object clause of the MOA.

The contract was beyond the objects as defined in the objects clause of memorandum and therefore it was void, and

The company had no capacity to ratify ultra vires contract even all the shareholders gave approval for the same.

Therefore, Riche's action for breach of the alleged contract failed as it was void.



<https://www.lawteacher.net/cases/ashbury-railway-carrage-and-iron-co-v-riche.php>



Gupta, P. *Legal aspects of Business: Concept and Applications*. Vikas Publishing House Pvt. Ltd.

9.3 Memorandum of Association: Contents

1. Name Clause
2. Situation Clause
3. Objects Clause
4. Liability Clause
5. Capital Clause
6. Succession Clause for One-Person Company
7. Association Clause

1. Name Clause

- The memorandum of a company shall state-
the name of the company with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company. - Sec. 4(1)(a)
- The name stated in the memorandum shall not--
(a) be identical with or resemble too nearly to the name of an existing company registered under this Act or any previous company law; or
(b) be such that its use by the company--
(i) will constitute an offence under any law for the time being in force; or
(ii) is undesirable in the opinion of the Central Government. - Sec. 4(2)
- Without prejudice to the provisions of sub-section (2), a company shall not be registered with a name which contains – - Sec. 4(3)
(a) any word or expression which is likely to give the impression that the company is in any way connected with, or having the patronage of, the Central Government, any State Government, or any local authority, corporation or body constituted by the Central Government or any State Government under any law for the time being in force; or
(b) such word or expression, as may be prescribed, unless the previous approval of the Central Government has been obtained for the use of any such word or expression.
- A person may make an application, 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-- - Sec. 4(4)
(a) the name of the proposed company; or
(b) the name to which the company proposes to change its name.

- Upon receipt of an application under sub-section (4), the Registrar may, on the basis of information and documents furnished along with the application, reserve the name for a period of twenty days from the date of approval or such other period as may be prescribed:

Provided that in case of an application for reservation of name or for change of its name by an existing company, the Registrar may reserve the name for a period of sixty days from the date of approval. - Sec.

4(5)(i)

- As per Sec. 4(5)(ii), Where after reservation of name under clause (i), it is found that name was applied by furnishing wrong or incorrect information, then

(a) if the company has not been incorporated, the reserved name shall be cancelled and the person making application under sub-section (4) shall be liable to a penalty which may extend to one lakh rupees;

(b) if the company has been incorporated, the Registrar may, after giving the company an opportunity of being heard--

(i) either direct the company to change its name within a period of three months, after passing an ordinary resolution;

(ii) take action for striking off the name of the company from the register of companies; or

(iii) make a petition for winding up of the company.



A.B. Limited was registered with the Registrar of Companies, Calcutta on 15 January 2005.

The Registrar of Companies, Bombay also registered on 15th May 1995 a company with the same name.

On coming to know of this, the first registered company wants to prevent the company subsequently from continuing with the same name.

Point of Discussion

Can the first company advise or compel to second company for changing its name?

Judgement (Hint)

Yes, Explanation: The second registered company is advised to change its name.

In case it does not do so, the first registered company may approach Central Government and the Central Government may direct it to change its name.

2: Situation Clause: Sec. 12

Memorandum of Association must state the name of the State in:

- which the registered office of the company is to be situated.
- It will fix up the domicile of the company.

(1) A company shall, within thirty days of its incorporation and at all times, thereafter, have a registered office capable of receiving and acknowledging all communications and notices as may be addressed to it.

(2) The company shall furnish to the Registrar verification of its registered office within a period of thirty days of its incorporation in such manner as may be prescribed.

(3) Every company shall--

(a) paint or affix its name, and the address of its registered office, and keep the same painted or affixed, on the outside of every office or place in which its business is carried on, in a conspicuous position, in legible letters, and if the characters employed therefor are not those of the language or of one of the languages in general use in that locality, also in the characters of that language or of one of those languages;

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(b) have its name engraved in legible characters on its seal, if any;

(c) get its name, address of its registered office and the Corporate Identity Number along with telephone number, fax number, if any, e-mail and website addresses, if any, printed in all its business letters, billheads, letter papers and in all its notices and other official publications; and

(d) have its name printed on hundies, promissory notes, bills of exchange and such other documents as may be prescribed:

Provided that where a company has changed its name or names during the last two years, it shall paint or affix or print, as the case may be, along with its name, the former name or names so changed during the last two years as required under clauses (a) and (c):

Provided further that the words "One Person Company" shall be mentioned in brackets below the name of such company, wherever its name is printed, affixed or engraved.

(4) Notice of every change of the situation of the registered office, verified in the manner prescribed, after the date of incorporation of the company, shall be given to the Registrar within thirty days of the change, who shall record the same.

(5) Except on the authority of a special resolution passed by a company, the registered office of the company shall not be changed,c--

(a) in the case of an existing company, outside the local limits of any city, town or village where such office is situated at the commencement of this Act or where it may be situated later by virtue of a special resolution passed by the company; and

(b) in the case of any other company, outside the local limits of any city, town or village where such office is first situated or where it may be situated later by virtue of a special resolution passed by the company:

Provided that no company shall change the place of its registered office from the jurisdiction of one Registrar to the jurisdiction of another Registrar within the same State unless such change is confirmed by the Regional Director on an application made in this behalf by the company in the prescribed manner.

(6) The confirmation referred to in sub-section (5) shall be communicated within a period of thirty days from the date of receipt of application by the Regional Director to the company and the company shall file the confirmation with the Registrar within a period of sixty days of the date of confirmation who shall register the same and certify the registration within a period of thirty days from the date of filing of such confirmation.

(7) The certificate referred to in sub-section (6) shall be conclusive evidence that all the requirements of this Act with respect to change of registered office in pursuance of sub-section (5) have been complied with and the change shall take effect from the date of the certificate.

(8) If any default is made in complying with the requirements of this section, the company and every officer who is in default shall be liable to a penalty of one thousand rupees for every day during which the default continues but not exceeding one lakh rupees.

(9) If the Registrar has reasonable cause to believe that the company is not carrying on any business or operations, he may cause a physical verification of the registered officer of the company in such manner as may be prescribed and if any default is found to be made in complying with the requirements of sub-section (1), he may without prejudice to the provisions of sub-section (8), initiate action for the removal of the name of the company from the register of companies under Chapter XVIII.



The old name of this clause is Registered Office clause



The Board of directors of X Ltd. decides to change the place of its registered office from the state of Maharashtra to the State of Karnataka.

The State of Maharashtra, however, opposes the above petition for change, inter alia, on the grounds that:

(i) It would affect adversely the general economy of the State; and

(ii) there are arrears of sales tax dues of over 5 lakhs from the company.

Point of Discussion

Discuss the validity of these grounds referring to case law.

3.Objects Clause – Sec. 4(1)(c)

- The memorandum of a company shall state-
 - ✓ the objects for which the company is proposed to be incorporated and
 - ✓ any matter considered necessary in furtherance thereof
- Points to be kept in mind while drafting Object Clause are---
 - ✓ It should not be ILLEGAL
 - ✓ Must not be against the provisions of Companies Act
 - ✓ Must not be against PUBLIC POLICY
 - ✓ Must not be against the general law of land
 - ✓ Must be CLEAR AND DEFINITE



Now only main object clause is required in MOA and there is no provision of other objects as in Companies act 1956

The requirement of including a generic objects clause / no objects clause has been not been included in the Companies Amendment Act 2017.

Need of Object Clause

To protect the interest of:

- Shareholders or Members
- Creditors
- Public (Those who are dealing with company so as to know the permitted range of company)

As we know the Memorandum of the company is its charter defining the objects of its existence and operations and therefore the concerned ROC relies on the objects clause to enquire about the objects intended to be pursued by the company either immediately or within a reasonable time after its incorporation. Thus, the objects clause should be construed as to confer on the company all powers reasonably required to the attainment of the objects.



A company is authorized by the objects clause in its memorandum to run hotels only. Without any amendment of the objects clause, the directors want to buy some buses and a cinema theatre for the facility and entertainment of the occupants of the hotel. Some shareholders vehemently object to the company going into other business.

Point of Discussion

What can be done in such a case?

(Hint): This business will be considered ultra vires and thus all related contracts will be void. The company can alter its objects clause as per provisions of Company's Act for the time being in force in this regard. And, the dissenting shareholders will have to be given the option to exit as per the Regulations Specified by SEBI.

4.Liability Clause- Sec. 4(1)(d)

The memorandum should state the liability of members of the company, whether limited or unlimited, and also state,--

(i) in the case of a company limited by shares, that liability of its members is limited to the amount unpaid, if any, on the shares held by them; and

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(ii) in the case of a company limited by guarantee, the amount up to which each member undertakes to contribute –

(A) 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 or of such debts and liabilities as may have been contracted before he ceases to be a member, as the case may be; and

(B) to the costs, charges and expenses of winding-up and for adjustment of the rights of the contributories among themselves.

5. Capital Clause- Sec 4 (1)(e)

The memorandum should state –

In the case of a company having a share capital,--

(i) the amount of share capital with which the company is to be registered and the division thereof into shares of a fixed amount and the number of shares which the subscribers to the memorandum agree to subscribe which shall not be less than one share; and

(ii) the number of shares each subscriber to the memorandum intends to take, indicated opposite his name;

Usually, to state the capital in the memorandum, it is written in following manner:

"The capital of the company is 10,00,000 divided into 1,00,000 equity shares of 10 each."

- A company is not authorized to issue capital beyond its authorized/nominal/registered capital. Upon receiving the applications for shares beyond the shares covered by the authorized capital, the excess amount received has to be returned by the company.
- And the dissenting shareholders will have to be given the option to exit as per the Regulations Specified by SEBI

6. Succession Clause/Nominee of OPC- Sec. 4(1)(f)

In the case of One Person Company, the name of the person who, in the event of death of the subscriber, shall become the member of the company must be stated in the Memorandum.

7. Association Clause (Declaration for Subscription)

This clause states that the persons subscribing their signatures at the end of the Memorandum are desirous of forming themselves into an association in pursuance of the Memorandum.

There may be one witness for all signatures but one subscriber cannot be a witness to the signatures of another. Full description, address, occupation, etc. of the subscribers and witnesses must be written.



W.E.F from 1 Jan 2017 we can use INC 33 for filling eMOA. In that case, we require to affix DSC of subscribers as well as of witness to the e-MOA.

9.4 Doctrine of Ultra Vires

The object clause of the Memorandum of the company contains list of the object for which the company formed. Company must not act beyond the object clause of memorandum of association. If company acts beyond the object clause, then its ultra vires.

This doctrine got its roots firm in 1875 in case of Ashbury Railway Carriage and Iron company Ltd. v. Riche.

If the contract entered into is an ultra vires contract, then it becomes void and cannot ratified by majority or all shareholders also. This known as Doctrine of Ultra Vires.

Even if special resolution passed by shareholder with majority of votes, then also its ratification cannot happen. Where a company exceeds its power as conferred by objects clause, it is not bound by it because it lacks legal capacity to incur responsibility for the action.

Effects of Ultra Vires Act

- Void ab initio: In the eyes of law, the ultra vires contracts are null and void ab initio. The company cannot sue or be sued upon for such acts.
- No ratification possible: Ultra vires contracts cannot turn as intra vires through ratification.
- Injunction: The shareholders can get an injunction to restrain a company wherein ultra vires act has been done or is about to be undertaken.
- Personal liability of directors: It is one of the duties of the directors to ensure that the corporate capital is used only for the legitimate business/objects of the company and hence they will be personally liable to replace the misused capital.
- Right of the company on acquired property by ultra vires acts

If a company's money is used ultra vires to acquire some property, then the company has right to secure and protect the party.

- No legal relationship by ultra vires borrowing

Ultra vires borrowings cannot create the relationship of creditor and debtor between the company the one who gave money to the company.

9.5 Articles of Association

There are some Regulations & Rules in all companies managing the internal affairs of company and for managing the relation between members and company. These regulations and rules shall be in recorded written format; this written document is called Articles of Association (AOA). The Articles of Association can be seen as a rule book within a company.

An Article of Association (AOA) lays down the rules and regulations for the internal management of the company. It specifies the duties, rights, powers and authority of the shareholder, directors and management of the company.

A Memorandum of Association specifies the objectives of the company whereas, an Article of Association lays down the internal guidelines to be followed while achieving these objectives of the company.

Article of Association: Definition

As per 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 or applied in pursuance of any previous company law or of this Act.



An Article of Association brings clarity in the relationship between the shareholders and the company and among the shareholders themselves.

It contains the rules regarding the share capital, transfer of shares, voting rights of the shareholders, the appointment of directors, accounts, an audit of the company etc.

The articles of association set out how the company is run, governed, and owned. The articles can put restrictions on the company's powers which may be useful if shareholders want comfort that the directors will not pursue certain courses of action, at least without shareholder approval.

Articles of Association: Features

1. It is a part of the constitution of an organization.

This is in a document form and is a part of the company's constitution alongside the memorandum.

2. It lays down rules of internal management of a company.

This document contains internal detailed governing aspects of the company's organization.

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3. It lays down the detailed rules which govern the conduct of directors, the rights of the shareholders and the relationship between the two.
4. Few statutory clauses should be included in the article of associations. Other clauses can be chosen to make the bye-laws of the organization.
5. Article of Association can be inspected by anyone as they are a public document.
6. AOA defines the rights, duties, powers of the management of a company as between themselves and the company at large.
7. They also prescribe the mode and form in which changes in the internal regulation of a company may be made from time to time.
8. An Article of Association is subsidiary to the Memorandum of Association (MoA).

The articles of association of a company must always be in consonance with the memorandum of that company and being subordinate to the memorandum; they cannot extend the objects of a company as specified in the memorandum of the company.

9. Articles of association of a company also establish a contract between the company and its members as well as between the members. (Supreme court provided in the case of Naresh Chandra Sanyal v. Calcutta Stock Exchange Association Ltd). This contract governs the ordinary rights and obligations incidental to the membership in the company.

10. Articles of association are like the partnership deed in a partnership. They particularly provide for matters such as the making of calls, forfeiture of shares, directors qualifications, the procedure for transfer and transmission of shares and debentures, powers, duties and appointment of auditors.

Effect of Memorandum and Articles: Sec. 10 of Company Act, 2013

- (1) Subject to the provisions of this Act, the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been signed by the company and by each member, and contained covenants on its and his part to observe all the provisions of the memorandum and of the articles.
- (2) All money payable by any member to the company under the memorandum or articles shall be a debt due from him to the company.

Articles of Association: Importance

With respect to Sec. 10, the importance of articles as well as memorandum of association can be summed up as follows:

- 1) Binding on members in their relation to the company- The memorandum and articles constitute a contract binding the company's members. Thus, the members are bound to the company by the provisions of the memorandum and articles just as much as if they had all put their seals to them.
- 2) Binding on company in relation to its members- just as members are bound to the company, the company is bound to the individual members to observe and follow the articles. Eg. Right to receive share certificate in respect of shares allotted to them, or to receive notice of general meeting, etc.
- 3) Neither company, nor members bound to outsiders-

The outsider here means a person who is not a member of the company even he is director of or solicitor to the company. Articles bind the members to the company and company to the members but neither of them is bound to an outsider to give effect to the articles. So far as the relationship between outsiders and the company is concerned, neither the memorandum nor the articles would give the contractual rights to outsiders against the company or its members even though the names of the outsiders are mentioned in those documents in connection with the arrangements that the company might have contemplated for carrying on its business.

- 4) Binding between members inter se-

The articles define rights and liabilities of the members. As between members inter se the articles constitute a contract between them and are also binding on each member as against the other or others. Such contract can be enforced only through the medium of the company. It must be noticed that the memorandum and articles do not create an express contract among the members of the company.

Therefore, a member has no right to bring a suit to enforce the articles in his own name against any other member or members. It is the company only which can take the action against the offender so as to protect an aggrieved member.

9.6 AOA: Applicable Table

Prior to preparing SPICe AOA. Based on the type of company to be incorporated, the appropriate Table as per Schedule I of the Companies Act, 2013 must be selected. The following is the Table as per Schedule I and the relevant Company:

TABLE – F: Articles of Association of a Company Limited by Shares

TABLE – G: Articles of Association of a Company Limited by Guarantee and having Share Capital

TABLE – H: Articles of Association of a Company Limited by Guarantee and not having Share Capital

TABLE – I: Articles of Association of an Unlimited Company and having Share Capital

TABLE – J: Articles of Association of an Unlimited Company and not having Share Capital

9.7 Articles of Association: INC-34

Form INC-34 or SPICe AOA is an eAOA or electronic Articles of Association that is newly introduced by the MCA to simplify company registration in India.

SPICe AOA can be prepared in both Hindi and English. Care must be taken while preparing SPICe AOA to ensure its as per the Companies Act, 2013.

- Name of the Company
- Editing SPICe AOA
- Subscriber Sheet
- Witness Signature

Name of the Company

The name of the company must be entered into the place provided. If the name of the company has already been approved, then the SRN number for name approval can be entered to complete the relevant details. (Know about the Company Naming Guidelines)

Editing SPICe AOA

Based on the table that is selected by the applicant, the Articles of Association as per the relevant table would be displayed in the section under the Company's name.



To hide any article, click on 1st check box 'Not applicable' against the respective article. To entrench the article, click on 2nd check box 'Altered' against the respective article. Director name(s) should be entered mandatorily under "Board of directors".

Mention different appointments as a sub-article E.g. (a) – Managing Director, (b) – Director Names etc. Articles in addition to the standard table shall be mentioned in last blank box 'Others'

Subscriber Sheet

In the Subscriber area, the details of subscribers must be mentioned. Details of the subscribers should match with SPICe or Form INC-32. Hence, it's important to enter same DIN or PAN or Passport number as mentioned in the INC-32 for individual subscriber and/or authorized representative of body corporate subscriber.

Maximum details of shareholders allowed through form SPICe is seven. In case of more shareholders are required, then the normal incorporation process must be followed.

Witness Signature

SPICe AOA can be witnessed by anyone using a Class 2 digital signature. There is no requirement for the witness to be a Professional (although recommended). Witness must have a valid PAN or DIN or Passport number.

9.8 Articles of Association: Instruction Kit for eFormSPICe AOA (INC-34)

The Instruction Kit has been prepared to help you file eForms with ease. This document provides references to law(s) governing the eForms, instructions to fill the eForm at field level and common instructions to fill all eForms. The document also includes important points to be noted for successful submission. This document is divided into following sections:

Part I – Laws Governing the eForm

Part II – Instructions to fill the eForm

Part III – Important Points for Successful Submission

9.9 Articles of Association: Registration Fee

- Registration fee for Articles of Association (AOA) (in case of company having share capital)

Nominal Share Capital (₹)	Fee applicable (₹)
Less than ₹ 1,00,000	200
₹ 1,00,000 to ₹ 4,99,999	300
₹ 5,00,000 to ₹ 24,99,999	400
₹ 25,00,000 to ₹ 99,99,999	500
₹ 1,00,00,000 or more	600

- Registration fee for Articles of Association (AOA) (in case of company not having share capital): Fee applicable is 200 per document

9.10 Articles of Association: Contents of INC 34

Table F: Articles of Association of a Company Act, 2013 is applicable to the company.

- Share capital and variation of rights
- Lien
- Calls on shares
- Transfer of shares
- Transmission of shares
- Forfeiture of shares
- Alteration of capital
- Capitalizations of profits
- Buy-back of shares
- General meetings
- Proceedings at general meetings
- Adjournment of meeting
- Voting rights
- Proxy
- Board of Directors
- Proceedings of the Board
- Chief Executive Officer, Manager, Company Secretary or Chief Financial Officer
- The Seal

- Dividends and Reserve
- Accounts
- Winding up
- Indemnity
- Subscriber Details
- ✓ Name, Address, Description and Occupation
- ✓ DIN/PAN/Passport Number
- ✓ Place
- ✓ DSC
- ✓ Dated

9.11 Provision for entrenchment in case of Articles of Association

The word “entrench” means to establish an attitude, habit, or belief so firmly that change is very difficult or unlikely.

An entrenchment clause is the one which makes certain amendments either impossible or difficult. The articles may contain provisions for entrenchment to the effect that specified provisions of the articles and may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.

The provisions for entrenchment shall only be made by:

1. Private Company

New Company: During formation of a company

Existing Company: By an amendment in the Articles agreed to by all the members of the company and by passing a Board resolution

2. Public Company

New Company: During formation of a company

Existing Company: By passing a special resolution

Article of Association: Provisions (Sec. 5)

- The articles may contain provisions for entrenchment to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.
- The provisions for entrenchment referred to in sub-section (3) shall only be made either on formation of a company, or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by a special resolution in the case of a public company.
- Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in such form and manner as may be prescribed.
- The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company.
- A company may adopt all or any of the regulations contained in the model articles applicable to such company.
- In case of any company, which is registered after the commencement of this Act, in so far as the registered articles of such company do not exclude or modify the regulations contained in the model articles applicable to such company those regulations shall, so far as applicable, be the regulations of that company in the same manner and to the extent as if they were contained in the duly registered articles of the company.

- Nothing in this section shall apply to the articles of a company registered under any previous company law unless amended under this Act.

Statutory right of Alteration

- Sec 14 of the act gives a clear and statutory power to the company to alter AOA.
- This power cannot be taken away from company.
- Any clause in articles of association providing that company cannot alter its article, is invalid.

9.12 Alteration of Articles – Sec. 14

(1) Subject to the provisions of this Act and the conditions contained in its memorandum, if any, a company may, by a special resolution, alter its articles including alterations having the effect of conversion of

(a) a private company into a public company; (Alteration of Articles) or

(b) a public company into a private company: (Central Government approval)

Provided that where a company being a private company alters its articles in such a manner that they no longer include the restrictions and limitations which are required to be included in the articles of a private company under this Act, the company shall, as from the date of such alteration, cease to be a private company.

Provided further that any alteration having the effect of conversion of a public company into a private company shall not valid unless it is approved by an order of the Central Government on an application made in such form and manner as may be prescribed.

Disposal of such applications by Tribunal

Provided also that any application pending before the Tribunal, as on the date of commencement of the Companies (amendment) Act, 2019, shall be disposed of by the Tribunal in accordance with the provisions applicable to it before such commencement.

(2) Every alteration of the articles under this section and a copy of the order of the Central Government approving the alteration as per sub-section (1) shall be filed with the Registrar together with a printed copy of the altered articles, within a period of fifteen days in such manner as may be prescribed, who shall register the same.

(3) Any alteration of the articles registered under sub-section (2) shall, subject to the provisions of this Act, be valid as if it were originally in the articles.

9.13 Alteration of memorandum or articles to be noted in every copy – Sec. 15

(1) Every alteration made in the memorandum or articles of a company shall be noted in every copy of the memorandum or articles, as the case may be.

(2) If a company makes any default in complying with the provisions of sub-section (1), the company and every officer who is in default shall be liable to a penalty of one thousand rupees for every copy of the memorandum or articles issued without such alteration.

Limitations of Alteration

- Must not be inconsistent with the Act: (e.g., The articles cannot be altered so as to give power to a company to purchase its own shares)
- Must not conflict with the Memorandum: The alteration of articles must not exceed the power given by the memorandum, or conflict with the provisions of the memorandum. If it does, it will be ultra vires and wholly void and inoperative
- Must not sanction anything illegal: The alteration must not purport to sanction anything which is illegal.
- Must be for the benefit of the company: The alteration must be bonafide for the benefit of the company as a whole.

- Must not increase liability of members: The alteration must not in any way increase the liability of the existing members to contribute to the share capital of, or otherwise pay money to, the company unless they agree in writing before or after the alteration is made.
- Alteration by special resolution only: Even clerical errors in the Articles should be set right by a special resolution.
- Approval of the Tribunal when a public company is converted into a private company.
- Breach of contract: A company is not prevented from altering its articles even if such alteration would result in breach of some contract. The affected party may file a suit for damages for such breach.
- Must not result in expulsion of a member: An assumption by the BOD of a company of any power to expel a member by amending the articles is illegal and void.
- No power of the Tribunal to amend articles (the tribunal has no power to amend or rectify the articles even where there is a mistake or drafting error which the tribunal would rectify in any other case)
- Alteration may be with retrospective effect.

9.14 Copies of memorandum, articles, etc., to be given to members – Section 17

(1) A company shall, on being so requested by a member, send to him within seven days of the request and subject to the payment of such fees as may be prescribed, a copy of each of the following documents, namely:--

(a) the memorandum;

(b) the articles; and

(c) every agreement and every resolution referred to in sub-section (1) of section 117, if and in so far as they have not been embodied in the memorandum or articles.

(2) If a company makes any default in complying with the provisions of this section, the company and every officer of the company who is in default shall be liable for each default, to a penalty of one thousand rupees for each day during which such default continues or one lakh rupees, whichever is less.

9.15 Articles and Memorandum: Their Relation

- The articles are subordinate to Memorandum
- The memorandum must be read in conjunction with Articles
- The terms of the Memorandum cannot be modified or controlled by the Articles
- The articles are subordinate to Memorandum

The articles cannot give powers to a company which are not conferred by the memorandum, nor can they purport to create rights which are inconsistent with the memorandum.

- The memorandum must be read in conjunction with Articles

This is in case when it is necessary-

- ✓ To explain any ambiguity in the terms of the Memorandum, or
- ✓ To supplement the Memorandum upon any matter about which it is silent except as regards matters which must by Statute be provided by the Memorandum.
- ✓ The terms of the Memorandum cannot be modified or controlled by the Articles
- ✓ If, however, there is any ambiguity in the Memorandum, the Articles may be referred to for clarification. But so far as the fundamental conditions in Memorandum are concerned, they cannot be explained with the aid of the Articles.

9.16 Articles and Memorandum – Distinction

Memorandum of Association	Articles of Association
1. Memorandum of association is the charter of the company and defines the scope of its activities, nature of its business, its nationality and its capital. 2. It defines the company's relation with outside world. 3. Memorandum of association cannot be altered except in the manner and to the extent provided by the act. 4. Memorandum is a supreme document of the company. 5. Every company must have its own memorandum. 6. A company cannot depart from the provisions contained in its memorandum, and if it does, it would be ultra-virus the company.	1. Articles of association of the company are a document which regulates the internal management of the company and are subsidiary to the Memorandum. 2. It defines the rights, duties, powers of the management of a company as between themselves and the company at large. 3. The articles being only the bylaws of the company can be altered by a special resolution. 4. Articles are subordinate to the memorandum. 5. But a company limited by shares need not register its articles. 6. Anything did against the provisions of articles, but which is intra-virus the memorandum, can be ratified.

9.17 Doctrine of Constructive Notice of Memorandum and Articles

A company is public body and the documents such as Memorandum of Association and the Article of Association of the company are open to public for inspection.

Therefore, it is assumed that the outsider person, who is involving with the company for business, has gone through these documents. It is a duty of outsider person, to be aware of the rules and regulations of the company because they are available in public record in terms of documents naming memorandum and articles of association. This assumption is called the Doctrine of Constructive Notice.

Doctrine of Constructive Notice: Importance

- It reduces the complicity in the rules and regulations of the business.
- This Doctrine functions as a safety to the company while dealing with the outsider party.

Doctrine of Constructive Notice: Implication

This doctrine puts the obligation on the outsider person to inspect and well verse with these two documents. In the event of a dispute, the outsider person cannot take the defense that he doesn't have the knowledge of the rules given in the MOA or AOA.

Thus, where a person enters into a contract which is beyond the powers of the company, as defined in the memorandum, or outside the limits set on the authority of directors, he cannot, as a general rule, acquire any rights under the contract against the company.



In the ABC company, the articles required that all documents must be signed by the Managing Director, secretary, and the working director on behalf of the company. However, A deed of mortgage was executed by the secretary and the working directory only.

Point of Discussion

Is the mortgage deed valid?

Judgement (Hint): The mortgage was nevertheless invalid.

Doctrine of Constructive Notice: Implication: Legal foundation as per Sec. 399

Section 399 of the Companies Act, 2013 gives the legal foundation for this doctrine. As per this section,

The Companies Act allows the outsider person to inspect and go through the records of the Company which are available with registrar of the Company.

This section also provides the right of inspection of the documents of the company.

The MOA and AOA of the company are the public document and are duly filed with registrar as per the provisions of the Company Act, 2013 and Company (Incorporation) third Amendment rule (2020) and the outsider person shall get into the contract only after the inspection of these documents.

By this provision, the doctrine of constructive notice is established by which the person is presumed to have the knowledge of the information in the documents available publicly.

Thus, before getting into the contract with any company, the outsider person must have knowledge of the company and he shall ensure that his purpose shall be fulfilled. Making available the documents of the public is the assumed and implied notice to the outsider person.



This doctrine is applicable to the documents which are available in the public record at the Registrar of Company.

In the case of Oakbank Oil Co. vs. Crum it was held that, anyone who is involving in the contract with the company shall be assumed to have the knowledge and the understanding of the company's MOA and AOA. Therefore, the person is presumed to have the notice of it. This principle is called doctrine of the constructive notice.

9.18 Doctrine of Indoor Management

Doctrine of Indoor Management is also known as Turquand rule. Turquand rule is a 150-year-old concept, which protects the outsiders against the actions done by the company. The Limitation of the Doctrine of Constructive Notice is 'Doctrine of Indoor Management'.

Any person who enters into a contract with the company shall ensure that the transaction is authorized by the articles and memorandum of the company.

Assumption:

- The outsiders assume that internal proceedings of the company are regularly done with.

Constructive doctrine protects the company from outsiders and Doctrine of Indoor protects the outsiders from the company.

As per the Doctrine of Indoor Management, there is no requirement to look into the internal irregularities, and even if there are any irregularities, the company shall be held liable since the person has acted on the grounds of good faith.

The doctrine originated from the landmark case Royal British Bank V Turquand (1856)

**Royal British Bank V Turquand (1856)**

The Directors of the Company were authorized by the articles to borrow on bonds, if authorized by a special resolution passed at a general meeting. A bond under the seal of the company, signed by two directors and the secretary was given by the Directors to Turquand. And in this manner, the directors did acquire the loan but failed to pass the resolution.

The repayment on loan defaulted, and the company was held liable. The shareholders refused to accept the claim in the absence of the resolution.

Point of Discussion:

Whether the company was liable on that bond and owe bond amount to Turquand?

Judgement

It was held that the bond was binding on the company as Turquand was entitled to assume

that the resolution of the Company in general meeting had been passed. The person dealing with the company is entitled to assume that there has been necessary compliance with regards to the internal management.



<https://indianlawportal.co.in/royal-british-bank-v-turquand/>



Mahony V East Holyford Mining Co. [1875]

In this case, the Articles of the company provided that the cheque shall be signed by two directors and countersigned by the secretary. It later came to light that neither the directors nor the secretary who signed the cheque was appointed properly. After the payment was made against the cheques, the company sued the bank for the amount paid against the cheques.

Company's Arguments

The company argued that the cheques were not signed by the authorized persons, and it was the duty of the bank to enquire further before making a payment for the cheques. The company referred to the principle of constructive notice of memorandum and articles of the company and believed that the bank would have gone through the provisions mentioned in articles for signing the cheques.

Banks' Arguments

The bank contended that since it received a formal copy of the resolution passed in this regard, there was no further requirement of the enquiry.

Point of Discussion

Was the bank responsible for wrong payment as it did not conduct a further enquiry?

Judgement

It was held, the person receiving such cheque shall be entitled to the amount since the appointment of directors is a part of the internal management of the company and a person dealing with the company is not required to enquire about it. The above view held by House of Lords in case of Mahony V East Holyford Mining Co. is supported by Section 176 of the Companies Act, 2013, which states that the defects in the appointment of the director shall not invalidate the acts done.



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Doctrine of Indoor Management: Implications

The doctrine provides the third parties who enter into a contract with the company is protected against any irregularities in the internal procedure of the company. The third parties cannot find out internal irregularities that take place in a company, hence the company will be liable for any loss suffered by them due to these irregularities.

The doctrine of constructive notice protects the company against the claim of third parties while the doctrine of indoor management protects the third parties against the company procedures.

Doctrine of Indoor Management: Exceptions

- Where the outsider had knowledge of irregularity
- No knowledge of memorandum and articles
- Forgery
- Negligence
- Doubt about the existence of an agency
- Requirement of fulfilling a precondition



- **Where the outsider had knowledge of irregularity**

This rule does not apply to circumstances where the person affected has actual or constructive notice of the irregularity. It means this doctrine does not protect any person who has actual or even an implied notice of the lack of authority of the person acting on

behalf of company. Thus, a person knowing the fact that directors do not have the authority to make the transaction but still enters into it, cannot seek protection under the rule of indoor management.



Howard V. Patent Ivory Manufacturing Company (1888)

The Articles of the company empowered the directors to borrow up to 1,000 pounds. The limit could be raised provided consent was given in the General Meeting. Without the resolution being passed, the directors took 3,500 pounds from one of the directors (Mr. Howard) who took debentures. Subsequently, the company refused to pay the amount and argued that the act of exceeding the borrowing powers of the directors without passing a resolution in general meeting was not binding on the company.

The company further argued that Mr. Howard was expected to have notice of memorandum and articles of the company.

Mr. Howard claimed that the company was bound by the acts of director.

Point of Discussion

Were the debentures of Mr. Howard good and valid?

Judgement

No, it was Held, the company was liable only to the extent of 1,000 pounds. Since the directors even Mr. Howard being one of the directors knew the resolution was not passed, they could not claim protection under the Turquand's rule.



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- **No knowledge of memorandum and articles**

The doctrine of indoor management does not come to protect a person who never consulted the memorandum and articles and thus did not rely on them.

Thus, a person, who never tried to know the authority of directors by referring to the articles and memorandum of the company, cannot invoke the rule of doctoring of indoor management.



Rama Corporation V. Proved Tin & General Investment Co

Mr. X who was the director in the Proved Tin & General Investment company entered into a contract with Rama Corporation while purporting to act on behalf of the company and he also took a cheque from later.

The articles of the company did provide that the director may delegate their power to one of them. But Rama Corporation did not have knowledge of this as they did not read the articles and memorandum of the company (Proved Tin & General Investment Co). Now, later on, it was found that the company had never delegated its power to Mr. X.

Subsequently, the company (Proved Tin & General Investment Co) refused to perform the contract entered by Mr. X on behalf on company with the Rama Corporation. Later on , the Rama Corporation sued the Proved Tin & General Investment Co and referred to the articles where the directors could delegate their power to any one of them.

Point of Discussion

Could the rule of indoor management be applied in the circumstances mentioned above?

Judgement

It was held that the plaintiff could not take the remedy of the indoor management as they even did not know that power could be delegated. Hence, the benefit of doctrine of indoor management could not be extended to Rama corporation.



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- **Forgery**

The rule of indoor management cannot be invoked for the transactions involving forgery or to transactions which are otherwise void ab initio or illegal. Forgery, in the case of company can take different forms, including forgery of the signatures of the authorized officials, execution of a document towards the discharge of a personal liability instead of the liability of the company.



Kreditbank Cassel V. Schenkers Ltd

A bill of exchange signed by the branch manager of a Schenkers Ltd with his own signature under the words stating that he signed on behalf of the company in favor of his payee. He had no authority from the company to do so. The bill was held to be forgery when the bill was drawn in favor of a payee to whom the manager was personally indebted.

Point of Discussion

Could the rule of indoor management be avoided on the grounds of forgery?

Judgement

The bill, in this case, was held to be forged because it purported to be a different document from what it was in fact; it purported to be issued on behalf of the company in payment of its debt when in fact it was issued in payment of the manager's own debt



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- **Negligence**

The doctrine of indoor management, in no way, rewards those who behave negligently. Thus, where an officer of a company does something which shall not ordinarily be within his authority, the person dealing with him must make proper enquiries and satisfy him as to the officer's authority. If he fails to make an enquiry, he is estopped from relying on the rule.



B. Anand Behari Lal v. Dinshaw & Co. (Bankers) Ltd

An accountant of Dinshaw & Co (Bankers) Ltd (the company) transferred some property of the company in favor of Mr Anand Behari. Discovering this deal, the company deemed to perform the contract and stated that it never authorized its accountant to transfer any of its immovable property to anyone.

On the other hand, Mr. Anand Behari argued that the company was bound by the contract as he acted on the presumption that the accountant had the apparent authority to enter into the contract on behalf of the company. And thus the rule of indoor management was applicable there. Mr. Behari sued the company for the breach of contract.

Judgement

It was held that the transfer of immovable property was void as the power of transferring immovable property of the company could not be considered within the apparent authority of an accountant.



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- **Doubt about the existence of an agency**

The doctrine will not apply where the question is in regard to the very existence of an agency.

Varkey Souriar v. Leraleeya Banking Co. Ltd

The Kerala High Court held that the doctrine of Indoor management cannot apply where the question is not one as to the scope of the power exercised by an apparent agent of a company but is in regard to the very existence of the agency.

- **Requirement of fulfilling a precondition**

This doctrine is also not applicable where a pre-condition is required to be fulfilled before the company itself can exercise a particular power. In other words, the act done is not merely ultra vires the directors/officers but ultra vires the company itself.

Summary

- Memorandum of Association acts as the charter of a company. It is a legal document prepared during the formation and registration process of a company to define the scope of company's activities and its relationship with the outside world.
- MOA sets out the constitution of a company and thus it provides the foundation on which the structure of the company is built.
- The name clause of the MOA must state the name of the company with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company.
- The situation clause of the MOA must mention the name of the State in which the registered office of the company is to be situated. It should fix up the domicile of the company.
- The purpose of objects clause is to enable the shareholders, creditors and those dealing with the company to know the permitted range of the enterprise.
- MOA should state the liability of members of the company, whether limited or unlimited.
- MOA should state the amount of share capital with which the company is to be registered and the division thereof into shares of a fixed amount and the number of shares which the subscribers to the memorandum agree to subscribe which shall not be less than one share in the case of a company having a share capital.
- In the case of One Person Company, the name of the person who, in the event of death of the subscriber, shall become the member of the company must be stated in the Memorandum.
- Ultra vires means an act or transaction of a contract, which though may not be illegal, is beyond the company's powers by reason of not being within the objects of the MOA of the company.
- If the contract entered into is a ultra vires contract i.e. beyond the objects clause of MOA, then it becomes void and cannot be ratified by majority or all shareholders also.
- An Article of Association (AOA) lays down the rules and regulations for the internal management of the company. It specifies the duties, rights, powers and authority of the shareholder, directors and management of the company. The articles of a company are subordinate to and subject to the memorandum of association. Therefore, any clause in the articles going beyond the memorandum will be ultra vires.
- It is mandatory for every type of company to register its articles of association.
- Article of Association can be inspected by anyone as they are a public document.
- Articles of association of a company also establish a contract between the company and its members as well as between the members.
- Form INC-34 or SPICe AOA is an eAOA or electronic Articles of Association that is newly introduced by the MCA to simplify company registration in India.
- SPICe AOA can be prepared in both Hindi and English.
- The articles may contain provisions for entrenchment to the effect that specified provisions of the articles and may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with.
- Every alteration made in the memorandum or articles of a company shall be noted in every copy of the memorandum or articles, as the case may be.
- In case, there is any ambiguity in the Memorandum, the Articles may be referred to for clarification. But so far as the fundamental conditions in Memorandum are concerned, they cannot be explained with the aid of the Articles.
- The doctrine of constructive notice provides protection to the company against the outsiders. However, the doctrine of indoor management protects the outsiders against the company.

Keywords

Alteration of Articles: Section 31 provides that subject to the provisions of the Act and to the conditions contained in its memorandum, a company may, by special resolution alter or add to its articles.

Article of Association: The articles of association of a company and its bye laws are regulations which govern the management of its internal affairs and the conduct of its business.

Capital Clause: Capital clause states the amount of share capital with which the company is registered and the mode of its division into shares of fixed value, i.e., the number of shares into which the capital is divided and the amount of each share.

Doctrine of constructive notice: the doctrine of constructive notice is established by which the person is presumed to have the knowledge of the information in the documents available publicly such as Memorandum of association and Articles of association.

Doctrine of Indoor Management: Doctrine of indoor management allows all those who deal with the company to assume that the provisions of the articles have been observed by the officers of the company.

Liability Clause: Liability clause states the nature of liability of the members.

Memorandum of Association: The Memorandum of Association of a company is its charter which contains the fundamental conditions upon which alone the company can be incorporated.

Object Clause: The objects clause defines the objects of the company and indicates the sphere of its activities.

Self Assessment

1. A company can undertake only those activities that are:
 - A. mentioned in the Memorandum of Association
 - B. beyond the objects clause of Memorandum of Association
 - C. decided by the shareholders as per their discretion
 - D. chosen by the board of directors
2. Memorandum of Association is a document that:
 - A. defines the scope of the company
 - B. limits the power of the company
 - C. defines the relation of the company with the outside world
 - D. All of above
3. Memorandum of Association must mention the _____ in which the registered office of the company is to be situated.
 - A. Name of the State
 - B. Name of the City
 - C. Detailed address of the place
 - D. Pin code of the place
4. A company should consider the following point/s while drafting its Object Clause:
 - A. Objects should be illegal
 - B. Objects should be against the provisions of the companies act
 - C. Objects should be in favor of the public policy

- D. Objects should not be clear
5. The acts that are beyond the object clause of memorandum of association are:
- A. Void ab initio
 - B. Ratifiable
 - C. Valid and Ratifiable
 - D. Void ab initio and not ratifiable
6. _____ lays down the internal guidelines to be followed while achieving these objectives of the company.
- A. Memorandum of Association
 - B. Articles of Association
 - C. Objects clause of MOA
 - D. Both Memorandum of Association and Articles of Association
7. Articles of Association is assessable to:
- A. the Board of Directors only
 - B. some specific employees of the company
 - C. key managerial personnel of the company
 - D. any person irrespective of being internal or external to the company
8. Articles of Association is:
- A. A superior document to the memorandum of association
 - B. A subordinate document to the memorandum of association
 - C. Equivalent to the memorandum of association
 - D. A document that establishes a contract between the company and outsiders
9. INC-34 or SPICe AOA can be prepared in:
- A. Hindi only
 - B. English only
 - C. Both Hindi and English
 - D. Any language
10. Articles of Association can be altered in a way that:
- A. Alterations may get inconsistent with the act
 - B. Alterations may conflict with the memorandum of association
 - C. Alterations may sanction anything illegal
 - D. Alterations must be bonafide for the benefit of the company as a whole
11. It is presumed that the person dealing with the company has not only read MOA and AOA but also has understood them according to their proper meaning as per:
- A. The doctrine of constructive notice
 - B. The doctrine of indoor management
 - C. Neither doctrine of constructive notice nor doctrine of indoor management
 - D. Both doctrine of constructive notice and doctrine of indoor management
12. The doctrine of constructive notice applies to the documents which are available in the:

- A. company and are assessable only to key managerial personnel
 - B. company and are assessable to its employees
 - C. public record at the Registrar of Company
 - D. all of above
13. Any person who enters into a contract with the company shall ensure that the company's articles and memorandum authorize the transaction. There is no requirement to look into the internal irregularities of the company as per:
- A. The doctrine of constructive notice
 - B. The doctrine of indoor management
 - C. Neither doctrine of constructive notice nor doctrine of indoor management
 - D. Both doctrine of constructive notice and doctrine of indoor management
14. -----protects the company against the claim of third parties while ----- protects the third parties against the company procedures.
- A. The doctrine of constructive notice; the doctrine of indoor management
 - B. The doctrine of indoor management; the doctrine of constructive notice
 - C. MOA; AOA
 - D. AOA; MOA
15. A person who never tried to know the authority of directors by referring to the company's articles and memorandum can invoke the rule of doctoring of indoor management.
- A. True
 - B. False

Answers for Self Assessment

1. A	2. D	3. A	4. C	5. D
6. B	7. D	8. B	9. C	10. D
11. A	12. C	13. B	14. A	15. B

Review Questions

1. Explain memorandum of association and state its contents.
2. State the rule laid down in 'Ashbury Railway Carriage Co. vs. Riche's case.
3. Discuss the legal significance of the different clauses in the memorandum of association.
4. Write explanatory notes on "Doctrine of ultra vires and its implications".
5. Explain the nature and importance of memorandum of association of a company.
6. "Any clause" in the articles going beyond the memorandum will be ultra vires". Explain.
7. Discuss the contents of the articles of association in brief.
8. Differentiate between memorandum of association and articles of association with suitable examples.
9. "The power of altering the articles is wide, yet it is subject to a large number of limitations". Explain.

10. "Every person dealing with the company is deemed to have a constructive notice of the contents of its memorandum and articles". Do you agree with the statement? Justify.
11. What is the meaning and implications of the doctrine of indoor management? Discuss the situations where this doctrine will not be applicable with suitable cases.
12. Explain the rule laid down in the Royal British Bank vs. Turquand and state the exceptions to the rule.
13. State the inter-relationship of Doctrine of Indoor Management with the Doctrine of Constructive Notice.



Further Reading

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Web Links

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Unit 10: Prospectus

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Summary

Keywords

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Objectives

After studying this unit, you will be able to:

- explain the meaning of prospectus.
- review the matters to be stated in prospectus.
- review the provisions related to variations in terms of contract or objects in prospectus.
- explain the various types of prospectus to be used in specific situations.
- explain the criminal and civil liabilities for presenting mis-statement or omitting of material matter in the prospectus by a public company or its key personnel.
- comment on importance of prospectus in case of issue of shares or debentures to general public by any public company.
- write the consequences for presenting mis-statement or omitting of material matter in the prospectus by a public company or its key personnel.

Introduction

The prospectus contains information about the company, its management team, recent financial performance, and other related information that investors would like to know.

Investors use this legal document to determine the growth and profitability prospects of the selling company to decide whether they will take part in the offering or not.

Legal Aspects of Business

Prospectus is the window through which an investor can look into the soundness of the company's venture. The investor must, therefore, be given a complete picture company's intended activities and its position. This is done through prospectus which must secure the fullest disclosure of all material and essential particulars and lay the same in full view of all intending purchasers of shares.

In order to finance its activities, a company needs capital which is raised by public company by the issue of a prospectus inviting offers for shares and debentures from the public. A private company is prohibited from making any invitation to the public to subscribe for any shares or debentures of the company. Hence, it need not issue a prospectus.

Prospectus is a legal document and carry tremendous importance in eyes of laws. A public company which is approaching public for raising capital through issue of shares or borrowing funds through issue of debentures, it requires to strictly adhere the provisions related to prospectus as given under the Companies Act, 2013. Any mis-statement or omission related to material information that can influence the decisions of investors can bring civil and criminal liabilities to the company and any responsible person for such mis-statement and omission. In the present unit, the meaning and types of prospectus, other significant provisions related to prospectus, civil and criminal liabilities for mis-statement in prospectus are discussed.

10.1 Prospectus: Meaning and Definition

A prospectus is a legal disclosure document that provides information about an investment offering to the public, and that is required to be filed with the SEBI, stock exchanges and ROC.

Prospectus: Definitions 2(70)

"Prospectus" means any document described or issued as a prospectus and includes a red herring prospectus referred to in section 32 or shelf prospectus referred to in section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate.



It is clear from the definition that the word "prospectus" means a document which invites offers from the public to buy shares or debentures of the company. By virtue of the Amendment Act of 1974, an document inviting deposits from the public also falls within the definition of prospectus.

10.2 Components of a Prospectus

- Overview and history of the company
- Services/products offered by the company
- Management profile
- Desired deal structure
- Use of proceeds
- Security offering details
- Financial information
- Risks involved

10.3 Document containing offer of securities for sale to be deemed prospectus- Sec. 25

(1) Where a company allots or agrees to allot any securities of the company with a view to all or any of those securities being offered for sale to the public, any document by which the offer for sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the company; and all enactments and rules of law as to the contents of prospectus and as to liability in respect of mis-statements and omissions from, prospectus, or otherwise relating to prospectus, shall apply with the modifications specified in subsections (3) and (4) and shall have effect accordingly as if the securities had been offered to the public for subscription and as if persons accepting the offer in respect of any securities were subscribers for those securities but without prejudice to the liability, if

any, of the persons by whom the offer is made in respect of mis-statements contained in the document or otherwise in respect thereof.

(2) For the purposes of this Act, it shall, unless the contrary is proved, be evidence that an allotment of, or an agreement to allot, securities was made with a view to the securities being offered for sale to the public if it is shown:

(a) that an offer of the securities or of any of them for sale to the public was made within six months after the allotment or agreement to allot; or

(b) that at the date when the offer was made, the whole consideration to be received by the company in respect of the securities had not been received by it.

(3) Section 26 as applied by this section shall have effect as if--

(i) it required a prospectus to state in addition to the matters required by that section to be stated in a prospectus

(a) the net amount of the consideration received or to be received by the company in respect of the securities to which the offer relates; and

(b) the time and place at which the contract where under the said securities have been or are to be allotted may be inspected;

(ii) the persons making the offer were persons named in a prospectus as directors of a company.

(4) Where a person making an offer to which this section relates is a company or a firm, it shall be sufficient if the document referred to in sub-section (1) is 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.

10.4 Matters to be stated in Prospectus- Sec. 26

(1) Every prospectus issued by or on behalf of a public company either with reference to its formation or subsequently, or by or on behalf of any person who is or has been engaged or interested in the formation of a public company, shall be dated and signed and shall state such information and set out such reports on financial information as may be specified by the Securities and Exchange Board in consultation with the Central Government:

Provided that until the Securities and Exchange Board specifies the information and reports on financial information under this sub-section, the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992 (15 of 1992), in respect of such financial information or reports on financial information shall apply.

(c) make a declaration about the compliance of the provisions of this Act and a statement to the effect that nothing in the prospectus is contrary 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; and



Clause a, b and d have been omitted of Sec 26(1)

(2) Nothing in sub-section (1) shall apply--

(a) to the issue to existing members or debenture-holders of a company, of a prospectus or form of application relating to shares in or debentures of the company whether an applicant has a right to renounce the shares or not under sub-clause (ii) of clause (a) of sub-section (1) of section 62 in favour of any other person; or

(b) to the issue of a prospectus or form of application relating to shares or debentures which are, or are to be, in all respects uniform with shares or debentures previously issued and for the time being dealt in or quoted on a recognized stock exchange.

(3) Subject to sub-section (2), the provisions of sub-section (1) shall apply to a prospectus or a form of application, whether issued on or with reference to the formation of a company or subsequently.



The date indicated in the prospectus shall be deemed to be the date of its publication.

Legal Aspects of Business

(4) No prospectus shall be issued by or on behalf of a company or in relation to an intended company unless on or before the date of its publication, there has been delivered to the Registrar for filing, a copy thereof signed by every person who is named there in as a director or proposed director of the company or by his duly authorized attorney.

(5) A prospectus issued under sub-section (1) shall not include a statement purporting to be made by an expert unless the expert is a person who is not, and has not been, engaged or interested in the formation or promotion or management of the company and has given his written consent to the issue of the prospectus and has not withdrawn such consent before the delivery of a copy of the prospectus to the Registrar for 2 [filing] and a statement to that effect shall be included in the prospectus.

(6) Every prospectus issued under sub-section (1) shall, on the face of it,--

(a) state that a copy has been delivered for 2 [filing] to the Registrar as required under sub-section (4); and

(b) specify any documents required by this section to be attached to the copy so delivered or refer to statements included in the prospectus which specify these documents.

(8) No prospectus shall be valid if it is issued more than ninety days after the date on which a copy thereof is delivered to the Registrar under sub-section (4).

(9) If a prospectus is issued in contravention of the provisions of this section, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and every person who is knowingly a party to the issue of such prospectus shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees.



Subsection 7 is omitted.

10.5 Variation in terms of contract or objects in prospectus – Sec 27

(1) A company shall not, at any time, vary the terms of a contract referred to in the prospectus or objects for which the prospectus was issued, except subject to the approval of, or except subject to an authority given by the company in general meeting by way of special resolution:

Provided that the details, as may be prescribed, of the notice in respect of such resolution to shareholders, shall also be published in the newspapers (one in English and one in vernacular language) in the city where the registered office of the company is situated indicating clearly the justification for such variation.

Provided further that such company shall not use any amount raised by it through prospectus for buying, trading or otherwise dealing in equity shares of any other listed company.

(2) The dissenting shareholders being those shareholders who have not agreed to the proposal to vary the terms of contracts or objects referred to in the prospectus shall be given an exit offer by promoters or controlling shareholders at such exit price, and in such manner and conditions as may be specified by the Securities and Exchange Board by making regulations in this behalf.

10.6 Offer of sale of shares by certain members of company – Sec. 28

(1) Where certain members of a company propose, in consultation with the Board of Directors to offer, in accordance with the provisions of any law for the time being in force, whole or part of their holding of shares to the public, they may do so in accordance with such procedure as may be prescribed.

(2) Any document by which the offer of sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the company and all laws and rules made thereunder as to the contents of the prospectus and as to liability in respect of mis-statements in and omission from prospectus or otherwise relating to prospectus shall apply as if this is a prospectus issued by the company.

(3) The members, whether individuals or bodies corporate or both, whose shares are proposed to be offered to the public, shall collectively authorize the company, whose shares are offered for sale to

the public, to take all actions in respect of offer of sale for and on their behalf and they shall reimburse the company all expenses incurred by it on this matter.

10.7 When the prospectus is not required to be issued

1. If the shares and debentures are decided to be allotted to existing holders of shares and debentures.
2. If the shares and debentures to be allotted are similar to the current (already issued) shares and debentures that are being traded in a recognized stock exchange.
3. In case of a private company, it is not permitted by law to invite general public to subscribe shares and debentures.
4. If the invitation is made to some such person who has a contract for underwriting the shares and debentures of the company.

10.8 Advertisement of prospectus. Sec. 30

Where an advertisement of any prospectus of a company is published in any manner, it shall be necessary to specify therein the contents of its memorandum as regards the objects, the liability of members and the amount of share capital of the company, and the names of the signatories to the memorandum and the number of shares subscribed for by them, and its capital structure.

10.9 Types of Prospectus

- Shelf Prospectus
- Red Herring Prospectus
- Abridged Prospectus
- Deemed Prospectus

Shelf Prospectus- Sec. 31

"Shelf prospectus" means a prospectus in respect of which the securities or class of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.

(1) Any class or classes of companies, as the Securities and Exchange Board may provide by regulations in this behalf, may file a shelf prospectus with the Registrar at the stage of the first offer of securities included therein which shall indicate a period not exceeding one year as the period of validity of such prospectus which shall commence from the date of opening of the first offer of securities under that prospectus, and in respect of a second or subsequent offer of such securities issued during the period of validity of that prospectus, no further prospectus is required.

(2) A company filing a shelf prospectus shall be required to file an information memorandum containing all material facts relating to new charges created, changes in the financial position of the company as have occurred between the first offer of securities or the previous offer of securities and the succeeding offer of securities and such other changes as may be prescribed with the Registrar within the prescribed time, prior to the issue of a second or subsequent offer of securities under the shelf prospectus:

Provided that where a company or any other person has received applications for the allotment of securities along with advance payments of subscription before the making of any such change, the company or other person shall intimate the changes to such applicants and if they express a desire to withdraw their application, the company or other person shall refund all the monies received as subscription within fifteen days thereof.

(3) Where an information memorandum is filed, every time an offer of securities is made under subsection (2), such memorandum together with the shelf prospectus shall be deemed to be a prospectus.

Red Herring Prospectus- Sec. 32

"Red herring prospectus" means a prospectus which does not include complete particulars of the quantum or price of the securities included therein.

Red herring prospectus is the prospectus which lacks the complete particulars about the quantum of the price of the securities. A company may issue a red herring prospectus prior to the issue of prospectus when it is proposing to make an offer of securities.

(1) A company proposing to make an offer of securities may issue a red herring prospectus prior to the issue of a prospectus.

(2) A company proposing to issue a red herring prospectus under sub-section (1) shall file it with the Registrar at least three days prior to the opening of the subscription list and the offer.

(3) A red herring prospectus shall carry the same obligations as are applicable to a prospectus and any variation between the red herring prospectus and a prospectus shall be highlighted as variations in the prospectus.

(4) Upon the closing of the offer of securities under this section, the prospectus stating therein the total capital raised, whether by way of debt or share capital, and the closing price of the securities and any other details as are not included in the red herring prospectus shall be filed with the Registrar and the Securities and Exchange Board.



X and Co., Ltd., intended to buy a rubber estate in Peru. Its prospectus contained extracts from an expert's report giving the number of rubber trees in the estate. The report was inaccurate. Will any shareholder buying the shares of the company on the basis of the above representation have any remedy against the company? Can the person authorizing the issue of the prospectus escape from the liability?

Abridged Prospectus

The abridged prospectus is a summary of a prospectus filed before the registrar. It contains all the features of a prospectus. An abridged prospectus contains all the information of the prospectus in brief so that it should be convenient and quick for an investor to know all the useful information in short.

Sec 33(1) of the Companies Act, 2013 also states that when any form for the purchase of securities of a company is issued, it must be accompanied by an abridged prospectus.

Provided that nothing in this sub-section shall apply if it is shown that the form of application was issued--

(a) in connection with a bona fide invitation to a person to enter into an underwriting agreement with respect to such securities; or

(b) in relation to securities which were not offered to the public.

(2) A copy of the prospectus shall, on a request being made by any person before the closing of the subscription list and the offer, be furnished to him.

(3) If a company makes any default in complying with the provisions of this section, it shall be liable to a penalty of fifty thousand rupees for each default.

Deemed Prospectus

When any company to offer securities for sale to the public, allots or agrees to allot securities, the document will be considered as a deemed prospectus through which the offer is made to the public for sale. The document is deemed to be a prospectus of a company for all purposes and all the provision of content and liabilities of a prospectus will be applied upon it.

10.10 Liabilities for Mis-Statement in Prospectus

- Criminal Liabilities (Sec. 34)
- Civil Liabilities (Sec. 35)

Criminal Liabilities (Sec. 34)

Where a prospectus, issued, circulated or distributed, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any

matter is likely to mislead, then every person who authorizes the issue of such prospectus shall be liable under section 447:

Punishment for fraud (Sec. 447)

Sec. 447 states that Without prejudice to any liability including repayment of any debt under this Act or any other law for the time being in force, any person who is found to be guilty of fraud involving an amount of at least ten lakh rupees or one per cent of the turnover of the company, whichever is lower shall be punishable with:

- imprisonment for a term which shall not be less than six months but which may extend to ten years and
- shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud:

Where frauds involving Public Interest

Provided that where the fraud in question involves public interest, the term of imprisonment shall not be less than three years.

Where frauds do not involve Public interest

Provided further that where the fraud involves an amount less than ten lakh rupees or one per cent of the turnover of the company, whichever is lower, and does not involve public interest, any person guilty of such fraud shall be punishable:

- with imprisonment for a term which may extend to five years or
- with fine which may extend to fifty lakh rupees or
- with both.

Three important terms that are used in the Sec. 447:

- I. "fraud"
- II. "wrongful gain"
- III. "wrongful loss"

(i) "fraud", in relation to affairs of a company or anybody corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss;

(ii) "wrongful gain" means the gain by unlawful means of property to which the person gaining is not legally entitled;

(iii) "wrongful loss" means the loss by unlawful means of property to which the person losing is legally entitled.

Exemption from Penalties

Provided that nothing in this section (i.e Discussed Penalties of Sec. 447) shall apply to a person if he proves that:

- such statement or omission was immaterial or
- he had reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was necessary.

Civil Liabilities (Sec 35)

(1) Where a person has subscribed for securities of a company acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the company and every person who:

(a) is a director of the company at the time of the issue of the prospectus;

(b) has authorized himself to be named and is named in the prospectus as a director of the company, or has agreed to become such director, either immediately or after an interval of time

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- (c) is a promoter of the company;
- (d) has authorized the issue of the prospectus; and
- (e) is an expert referred to in sub-section (5) of section 26

shall, without prejudice to any punishment to which any person may be liable under section 36, be liable to pay compensation to every person who has sustained such loss or damage.

(2) No person shall be liable under sub-section (1) of Section 35, if he proves --

(a) that having consented to become a director of the company, he withdrew his consent before the issue of the prospectus, and that it was issued without his authority or consent; or

(b) that the prospectus was issued without his knowledge or consent, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent.

(c) that, as regards every misleading statement purported to be made by an expert or contained in what purports to be a copy of or an extract from a report or valuation of an expert, it was a correct and fair representation of the statement, or a correct copy of, or a correct and fair extract from, the report or valuation; and he had reasonable ground to believe and did up to the time of the issue of the prospectus believe, that the person making the statement was competent to make it and that the said person had given the consent required by sub-section (5) of section 26 to the issue of the prospectus and had not withdrawn that consent before filing of a copy of the prospectus with the Registrar or, to the defendant's knowledge, before allotment thereunder.

(3) Notwithstanding anything contained in this section, where it is proved that a prospectus has been issued with intent

- to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose,
- every person referred to in sub-section (1) shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.



A company issued a prospectus advertising that the company has a great Potential with “turnover of a million bags of cement in a year”. It is discovered later that while the company has the installed capacity of one million bags, it had never produced more than 6 lac bags of cement in a year. A buyer of shares seeks remedy against the misleading statement. Would he succeed? [Hint: Yes, he would succeed.]

10.11 Punishment for fraudulently inducing persons to invest money (Sec. 36)

This section provides that any person shall be liable for action under section 447 (as discussed before) who, either knowingly or recklessly makes any statement, promise or forecast which is false, deceptive or misleading, or deliberately conceals any material facts, to induce another person to enter into, or to offer to enter into,

- (a) any agreement for, or with a view to, acquiring, disposing of, subscribing for, or underwriting securities; or
- (b) any agreement, the purpose or the pretended purpose of which is to secure a profit to any of the parties from the yield of securities or by reference to fluctuations in the value of securities; or
- (c) any agreement for, or with a view to obtaining credit facilities from any bank or financial institution.



T.G. Venkatesh vs Registrar of Companies on 5 June, 2006

Background of the company, M/s. Richimen Silks Limited

M/s. Richimen Silks Limited was incorporated as private limited on 16-10-1984 with the

main objects of manufacturing of various types of silk fabrics.

The Company was converted into a public limited company and a fresh certification of Incorporation was issued on 19-9-1985.

Facts of the case

Then the Company issued a prospectus to the public, inviting subscriptions to its shares after obtaining necessary permission from the Controller of Capital Issues, Government of India, New Delhi. The prospectus was issued on 23-8-1986, inviting subscriptions from the public for its share capital and accordingly, received the public subscriptions.

In the present case, T.G. Venkatesh, the petitioner along with other Directors was signatory to the prospectus, issued by M/s. Richimen Silks Limited, stating that the trial production will be commenced in the first week of January, 1987 and the commercial production will be commenced in the second week of January, 1987 and dividends would be declared in the first year of operation, i.e., for the year ending 31-12-1987, which were not complied with.

But, however the Company failed to adhere to the schedules as issued, which was given under the heading of Project implementation Schedule and profitability and Dividend.

This fact of non-compliance of the projections and the declaration of dividend has come to light during the inspection conducted by the Inspector of the Company's Department, therefore, show cause notice was issued to all the Directors, including the petitioner, who was shown as Director and the Chairman of the Company in the prospectus.

Arguments of Petitioner

It is stated by the petitioner that while conducting investigation under Section 237 of the Act, the Inspecting Officer has noticed the failure of the Company to comply with the schedule fixed in the prospectus issued, as there was delay of 11 months for going to the trial production and one year and three months for going to the commercial production.

The petitioner stated that the said Company was promoted by Mr. G. Vittal, who persuaded the petitioner to give his consent to become one of the Directors of the company and the petitioner was appointed as a Non-Executive Independent Director, which the petitioner had relinquished on 26-4-1988.

It is stated that the petitioner is no way connected as to the day-to-day running of the said Company, as he was not in charge of or in control of the affairs of the Company.

The petitioner admitted the fact of the schedule specified in the prospectus issued on behalf of the Company, but, however, stated that due to unforeseen circumstances, inevitable delay was caused in project implementation over which the petitioner as a Non-Executive Independent director had no control whatsoever.

It is further stated that the Directors had expressed the intention to declare dividends based on the good market prospects in the prospectus. It is stated that the petitioner had resigned as a Non-Executive Independent Director of the said Company on 26-4-1988, by which time, the Company has achieved commercial production.

Thereafter the petitioner was given to understand that the said Company was not able to declare dividends due to unforeseen slump in the business of the said Company's products. Further, since the petitioner is no longer a Non-Executive Independent Director of the said Company had no connections whatsoever. Therefore, the petitioner cannot be made liable for such non-declaration of the dividend by the said Company.

In the absence of any profits, the Company could not have declared any dividend under the provisions of the Act. The statements made with good intentions could not be treated as a fraudulent or mischievous statements, therefore, sought for appropriate relief from being prosecuted under the above referred provisions.

Arguments of ROC

A counter is filed on behalf of the Central Government by the Registrar of the Companies, disputing and denying the allegations made by the petitioner.

It is stated that the petitioner along with other Directors are signatories to the prospectus where they have declared specific dates as to the trial production, commercial production as well as for the declaration of dividend, which the company failed to comply with.

It is stated that even though, G. Vittal was the promoter of the company and the Managing

Director, since the petitioner joined as one of the Director and was designated as chairman, has got equal responsibility and obligation to comply with the terms of the prospectus issued to which he is one of the signatories.

It is stated that the petitioner having subscribed his signature for issuance of the prospectus, the resignation on subsequent date would not relieve him of his obligation. In the counter, it is stated that the petitioner has failed to substantiate the reasons with adequate proof of non-commissioning of the project with the stipulated period, as stated in the prospectus, equally with reference to the commercial production and declaration of dividend.

ROC stated the promises made in the prospectus which are binding on the petitioner along with other directors both jointly and severally, petitioner was failed to comply with the said promises and also failed to explain with any detailed reasons, therefore, the petitioner is not entitled to any relief.

Point of Discussion

Is T.G. Venkatesh not liable for mis-statement in the prospectus?

Judgement:

The Company Petitions are, accordingly, dismissed. However, it is open to the petitioner to adduce necessary evidence before the Court, where prosecutions if launched against the petitioner, to prove his innocence.

Court Contentions for above decision

If the facts of the present case are examined in the light of the decisions and the facts of related cases, it is clear that the Registrar of Companies proposed to initiate proceedings for the alleged violations of Sections 63, 68 and 628 of the Act treating the disclosures in the prospectus, issued on behalf of the Company, are false and incorrect. Though the petitioner is seeking relief under Section 633 of the Act, but the explanation that was brought on record is so vague.

According to the petitioner, the petitioner admitted that the trial production as well as commercial production did not commence as declared in the prospectus, similarly even the dividend also was not declared not only for the first year ending 31-12-1987 but till 7-6-2004, when the Inspector of the Department had inspected the records of the Company. Therefore, it is clear that the schedules were not adhered as was declared in the prospectus, to which the petitioner is one of the signatories.

The explanation that is put forward by the petitioner is due to unforeseen circumstances inevitable delays were caused in project implementation over which the petitioner had no control. The petitioner did not elaborate what are the said inevitable circumstances under which the Company could not adhere to the schedules. The other explanation for non-declaration of dividend is also equally so vague and is not substantiated by any facts and figures.

Though the petitioner claimed that he had resigned from the Directorship on 26-4-1988, immediately after the commencement of the trial and commercial production, but still, being a signatory to the prospectus he cannot be relieved of his obligation as even by the date of his resignation, the provisions of the Act are already being contravened, therefore, the resignation from the Directorship itself would not absolve the petitioner of his obligations and liabilities.

Under the above circumstances, the petitioner is not entitled for the relief as sought for under Section 633 of the Act, in view of the fact that no material is placed, explaining the circumstances for non-compliance of the terms declared in the prospectus to prove that the statements made in the prospectus are not false, deceptive or misleading.



<https://indiankanoon.org/doc/1746257/>



Kuldeep Kumar Kohli & Ors. vs The Registrar of Companies (19 January, 2012)

Petitioner: Kuldeep Kumar Kohli & Ors

Respondent: ROC**Petition:**

The present petition is preferred by the petitioner under section 482 of the Code of Criminal procedure 1973, for quashing of the complaint lodged by the respondents against the petitioner under section 63 and 628 of the Companies Act, 1956 pending in the Court of Metropolitan Magistrate, Delhi and for quashing of the summoning order dated 13.11.2002.

The petitioners were directors of a finance, leasing and investment company named Pariksha Fin-invest-lease Pvt. Ltd having its registered office at B-18, Swami Dayanand Colony, Sarai Rohilla, Delhi-110007 since 27.8.1995.

The object of the company was investments, financing, leasing, consultancy services etc. mentioned in the articles and memorandum of association. The said company became a public company and made a public issue of its equity shares in September 1996.

In the prospectus issued for the said capital issue, the proposed deployment of the funds was given as leasing, finance and investments etc. The total issue size was Rs. 235 lakhs and the promoters' own contribution was Rs. 90 lakhs. The company shifted its registered office to another leased premises at 71/77, Prem Nagar, Janakpuri, Delhi on 22.06.1998.

The Delhi Stock Exchange corresponded with the petitioners' company at the old address between August 1998 to March 1999. Due to the letters being returned undelivered, the DSE sent a letter to the residential address of the petitioners on 23.3.1999 warning them of their company being treated as vanishing company.

The petitioners received a show cause notice under section 62,63 read with section 68 and section 628 of the Companies Act from the office of the Registrar of Companies. Then Deputy Registrar Mr. J.K. Jolly was appointed to inquire into the affairs of the company. On the above said premises, two complaints (no. 1332/2002 and 1333/2002) were lodged by Registrar of Companies in the court of MM against the petitioners on 13.11.2002.

In one complaint case, (1332/2002), it has been alleged that the directors of the company did not utilize the funds from the public issue for the purpose mentioned in the prospectus and in fact the funds were allocated and invested in purposes which were not mentioned in the prospectus, therefore, the company and its directors have made false statements in the prospectus by not disclosing the true purpose of the prospectus.

ROC stated that the funds for leased assets and the purchase of office space have not been used but have been diverted to investments for their own purposes. Therefore, the directors are liable to be prosecuted u/s 63 and 628 of the companies Act, 1956.

Section 63 and section 628 of the companies Act, 1956 are reproduced as under:

Sec. 63. Criminal liability for misstatements in prospectus.

(1) Where a prospectus issued after the commencement of this Act includes any untrue statement, every person who authorized the issue of the prospectus shall be punishable with imprisonment for a term which may extend to two years, or with both, unless he proves either that the statement was immaterial or that he had reasonable ground to believe, and did up to the time of the issue of the prospectus believe, that the statement was true.

(2) A person shall not be deemed for the purposes of this section to have authorized the issue of a prospectus by reason only of his having given:

(a) the consent required by section 58 to the inclusion therein of a statement purporting to be made by him as an expert, or

(b) the consent required by sub-section (3) of section 60.

Sec. 628.: PENALTY FOR FALSE STATEMENTS.

If in any return, report, certificate, balance sheet, prospectus, 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.

Arguments of Petitioner

The funds of the company which were generated through public issue were deployed in the objects of the company and the office could not be purchased because the deal failed due to volatility in the property market.

It is submitted that the Registrar of Companies did not take into account the report of the Deputy Registrar who had exonerated the petitioners from any criminal liability in his report. It is urged that the petitioners gave the notice of change in address to all the authorities like RBI, DSE and Income Tax Office by filling form 18.

Another contention of the petitioners is that they have resigned from the directorship of the company before the filing of the complaint and hence no liability can be fastened on them.

Amongst these grounds, the main ground taken up by the petitioners for quashing of the summoning order is that the complaint lodged by the Registrar of Companies is barred by time and is filed after the expiry of the limitation period.

It is contended that the prospectus was issued by the company on 10.09.1996 and the impugned complaint no. 1332/2002 was filed on 13.11.2002 which is beyond the limitation period of three years

At the outset, it must be mentioned that the petition having been filed after 8 years of passing of the summoning order, is highly belated and the petition finds no mention of any explanation of such a long delay. On this ground alone, it was liable to be dismissed.

Court's Contention on Limitation period

As far as limitation aspect is concerned, limitation of offences under Sections 63 and 628 of the Companies Act, 1956 starts from the date of knowledge of making a false statement. The Registrar of Companies learnt about making of false statement after filing of balance sheet in the year 1999-2000, and the complaint was filed in the year 2002 which is well within the prescribed limitation period of three years.

Therefore, limitation would start only after the date of filing of balance sheet and not from the date of issuing prospectus and this plea, therefore, is not tenable.

Thus, there is no ground for quashing of the summoning order on this ground.

The contention of the petitioners that they have resigned from the directorship of the company and hence cannot be made liable, does not find any favour as the question that whether they had resigned or not is a question of fact which cannot be gone into by this court and only the trial court, during trial can decide this issue. The argument of the petitioners that the fact of change of address was duly notified to all the agencies including RBI, DSE and Income Tax Office, does not have any merit because after the perusal of the record it can be seen that only correspondence made in this regard was to the Registrar of Companies and no other authority.

The petitioners cannot shift their liability arising out of their own inaction by stating that there was lack of communication between the various Authorities. The onus of notifying the various agencies about the change of address lied only and only on the petitioners which they have not been able to discharge.

Judgement

The petition was hereby dismissed. The Kuldeep Kumar Kohli & Ors. were held liable under Section 63 and section 628 of the companies Act, 1956. They were subjected to Criminal liability for misstatements in prospectus under Sec. 63 and penalties for false statements under Sec. 628.



<https://indiankanoon.org/doc/187283756/>

Summary

- A prospectus is a legal disclosure document that provides information about an investment offering to the public, and that is required to be filed with the SEBI, stock exchanges and ROC.
- Investors use the prospectus to determine the growth and profitability prospects of the selling company to decide whether they will take part in the offering or not.
- Where a company allots or agrees to allot any securities of the company with a view to all or any of those securities being offered for sale to the public, any document by which the offer for sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the company.
- Every prospectus issued by or on behalf of a public company either with reference to its formation or subsequently, or by or on behalf of any person who is or has been engaged or interested in the formation of a public company, shall be dated and signed and shall state such information and set out such reports on financial information as may be specified by the Securities and Exchange Board in consultation with the Central Government.
- No prospectus shall be issued by or on behalf of a company or in relation to an intended company unless on or before the date of its publication, there has been delivered to the Registrar for filing, a copy thereof signed by every person who is named there in as a director or proposed director of the company or by his duly authorized attorney.
- In certain cases, a company is not required to issue prospectus such as:
 1. If the shares and debentures are decided to be allotted to existing holders of shares and debentures.
 2. If the shares and debentures to be allotted are similar to the current (already issued) shares and debentures that are being traded in a recognized stock exchange.
 3. In case of a private company, it is not permitted by law to invite general public to subscribe shares and debentures.
 4. If the invitation is made to some such person who has a contract for underwriting the shares and debentures of the company.
- A company can prepare and issue different types of prospectus depending upon its need like Shelf prospectus, Red Herring prospectus, Abridged prospectus; and Deemed prospectus.
- In case a company or its directors, promoters or any of the key personnel present mis-statement in the prospectus or omit to present material information in the prospectus knowingly then the liable persons will be subjected to criminal and civil liabilities.

Keywords

- **Abridged Prospectus:** An 'abridged prospectus' need only be appended to the application form.
- **Deemed Prospectus:** When any company to offer securities for sale to the public, allots or agrees to allot securities, the document will be considered as a deemed prospectus through which the offer is made to the public for sale.
- **Prospectus:** A prospectus, as per s.2 (36), means any document described or issued as prospectus and includes any notice, circular, advertisement.
- **Red Herring Prospectus:** The 'red-herring' prospectus means, a prospectus which does not have the complete particulars on the price of the securities offered and the quantum of securities offered.

- **Shelf Prospectus:** A 'shelf-prospectus' means, a prospectus issued by any financial institution or bank, for one or more issues of the securities or class of securities specified in that prospectus.

Self Assessment

1. If the shares are decided to be allotted to existing shareholders, then the company is:
 - A. required to issue a statement in lieu of prospectus
 - B. required to issue new prospectus
 - C. required to red herring prospectus
 - D. not required to issue prospectus
2. A private company is required to issue a prospectus as per provisions of the companies act, 2013.
 - A. True
 - B. False
3. Suppose Tata chemicals Ltd. has plans to come up with three issues of its equity securities in the same financial year, i.e., 2022-23 in different months. In such a case, which of the following prospectus Tata Chemicals Ltd. Should issue to reduce its overall cost of securities issue?
 - A. Shelf Prospectus
 - B. Red Herring Prospectus
 - C. Abridged prospectus
 - D. Deemed Prospectus
4. A company filing a shelf prospectus shall be required to file a/an _____ with the registrar within the prescribed time, before the issue of a second or subsequent offer of securities under the shelf prospectus.
 - A. information memorandum
 - B. memorandum
 - C. articles
 - D. detailed prospectus
5. A prospectus that does not include complete particulars of the quantum or price of the securities included therein is termed as:
 - A. Shelf Prospectus
 - B. Red Herring Prospectus
 - C. Abridged prospectus
 - D. Deemed Prospectus
6. A company proposing to issue a red herring prospectus shall file it with the ----- to the opening of the subscription list and the offer.
 - A. registrar at least three days' prior
 - B. SEBI at least three days' prior
 - C. registrar at least three days' after

- D. SEBI at least three days' after
7. _____ contains all the information of the prospectus in brief so that it should be convenient for an investor to know all the valuable information in short.
- A. Shelf Prospectus
 - B. Red Herring Prospectus
 - C. Abridged prospectus
 - D. Deemed Prospectus
8. When any form for the purchase of securities of a company is issued, it must be accompanied by _____.
- A. Shelf Prospectus
 - B. Red Herring Prospectus
 - C. Abridged prospectus
 - D. Deemed Prospectus
9. A company shall not vary the terms of a contract mentioned in the prospectus or objects for which the prospectus was issued, except:
- A. subject to an authority given by the company in general meeting by way of special resolution
 - B. subject to an authority given by the company in general meeting by way of ordinary resolution
 - C. subject to publication of such resolution in English newspaper only
 - D. subject to publication of such resolution in vernacular language newspaper only
10. A prospectus is required to be filed with the:
- A. SEBI
 - B. Stock exchanges
 - C. ROC
 - D. All of above
11. Any person who is found to be guilty of fraud committed through misstatement in prospectus involving an amount of at least ten lakh rupees shall be punishable with:
- A. imprisonment for a term of six months
 - B. fine of the amount involved in the fraud
 - C. both imprisonment for six months and a fine of the amount involved in the fraud
 - D. either imprisonment for six months or a fine of the amount involved in the fraud
12. Where the fraud committed through misstatement in prospectus involves an amount less than ten lakh rupees or one percent of the turnover of the company, whichever is lower and does not involve public interest, any person guilty of such fraud shall be punishable with:
- A. with imprisonment for a term which may extend to five years
 - B. with fine which may extend to fifty lakh rupees
 - C. with both imprisonment and fine
 - D. either imprisonment or fine or both imprisonment and fine

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13. A person can get escaped from the penalties of Sec. 447 (Criminal liabilities for misstatements in the prospectus) if he proves that:
 - A. such statement or omission in the prospectus was immaterial
 - B. he had no reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was unnecessary
 - C. such statement or omission in the prospectus was material
 - D. all of above

14. Where a person has subscribed for securities of a company acting on any statement included in the prospectus which is misleading and has sustained any loss as a consequence thereof, the following person/s may be liable under section 36, be liable to pay compensation to such person who has sustained such loss or damage.
 - A. the promoter of the company;
 - B. a person who has authorized the issue of the prospectus; and
 - C. an expert referred to in sub-section (5) of section 26
 - D. all of above

15. No person shall be liable under sub-section (1) of Section 35 related to civil liabilities due to misstatement in the prospectus if he proves:
 - A. that having consented to become a director of the company, he withdrew his consent before the issue of the prospectus
 - B. that the prospectus was issued without his authority or consent
 - C. that having consented to become a director of the company, he withdrew his consent before the issue of the prospectus and that it was issued without his authority or consent
 - D. that the prospectus was issued with his authority or consent

Answers for Self Assessment

1. D	2. B	3. A	4. A	5. B
6. A	7. C	8. C	9.. A	10. D
11. C	12. D	13. A	14. D	15. C

Review Questions

1. Define a prospectus. Detail out its contents.
2. Explain the remedies available to an allottee who has subscribed for the shares on the faith of a false and misleading prospectus.
3. Describe the defences available to a director in case of a suit against him for misstatements made in the prospectus.
4. Enumerate cases in which a prospectus is not required to be issued by a public company.
5. State the matters to be stated in a prospectus.
6. Explain the various types of prospectus.



Further Reading

- Bhandari, C. C. (2021). *A Handbook on Corporate and Other Laws* (25 ed.). Bestword' Publications Pvt. Ltd.
- Gogna, P. P. S. *A Textbook of Company Law*. S. Chand Publishing.
- Gupta, P. *Legal aspects of Business: Concept and Applications*. Vikas Publishing House Pvt. Ltd.
- Kapoor, N. (2020). *Elements of Mercantile Law* (38 ed.). Sultan Chand & Sons



Web Links

<http://ebook.mca.gov.in/default.aspx>

https://www.indiacode.nic.in/handle/123456789/2114?view_type=browse&sam_handle=123456789/1362

Unit 11: Raising of Capital

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Summary

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Objectives

After studying this unit, you will be able to:

- explain the meaning and types of shares.
- illustrate the meaning and types of share capital.
- review the provisions related to alteration and reduction of share capital.
- illustrate the meaning and use of sweat equity shares.
- explain the bonus shares and their related provisions.
- review the provisions related to borrowing powers of the company.
- explain the provisions related to charges.
- review the importance of raising capital and exercising borrowing powers for a company to run its operations and need to follow the regulatory provisions related to same.

Introduction

Every company needs funds to run its business. A company can meet its financial needs by exercising its borrowing powers and raising funds through issuing capital. A public company if authorized by its articles can raise funds or capital by issuing equity shares or preference shares to general public. When the company issues its shares for the first time to general public, it is termed as company has come up with IPO i.e. Initial Public Offer. During its lifetime, a public company can further raise funds from the general public by coming up with FPO i.e. Follow up public offer. However, it must be noted that in no case, a company can raise capital above the authorized capital as fixed in its Memorandum of Association. However, a company can alter its capital by following provisions meant for the same under the Companies Act, 2013.

Raising funds through issuing shares involves huge cost, thus a company may hesitate to issue shares again and again if it requires funds for any reason such as expansion, starting new projects, replacing old technology with new one, etc. In such a case, a company can still arrange funds by exercising its borrowing powers. A company can raise loans from financial institutions through creating charge against its assets. A public company can even borrow funds from the general public through issue of Debentures. While raising capital or borrowing funds, the company has to comply with concerned provisions of the Companies Act, 2013. In this unit, significant provisions related to raising capital, borrowing powers and creating charge has been discussed.

11.1 Share: Definition and Nature**Share: Definition: Sec. 2(84)**

"share" means a share in the share capital of a company and includes stock.

Share: Nature

A share determines the rights to a specified amount of the share capital of a company. It carries with it certain rights and liabilities during the lifetime of the company and also when it is being wound up.

A share is shareholder's interest in the company measured by a sum of money, for the purposes of liability in the first place, and of interest in the second.

A share extends to the shareholders a right to participate in the profits made by a company, during the lifetime of the company when it declares the dividend and in the assets of the company when it is wound up.

A share is a bundle of rights and liabilities where these rights and liabilities are regulated by the articles of a company.

11.2 Share: Types

- Equity Shares.
- Preference Shares.
 - ✓ Cumulative and non-cumulative preference shares.
 - ✓ Convertible and non-convertible preference shares.
 - ✓ Redeemable and irredeemable preference shares.
 - ✓ Participating and non-participating preference shares.

11.3 Kinds of Capital: Sec. 43

The share capital of a company limited by shares shall be of two kinds, namely: --

(a) equity share capital--

(i) with voting rights; or

(ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed; and

(b) preference share capital.

Provided that nothing contained in this Act shall affect the rights of the preference shareholders who are entitled to participate in the proceeds of winding up before the commencement of this Act.

For the purposes of this section

(i) equity share capital, with reference to any company limited by shares, means all share capital which is not preference share capital;

(ii) preference share capital, with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to:

(a) payment of dividend, either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax; and

(b) repayment, in the case of a winding up or repayment of capital, of the amount of the share capital paid-up or deemed to have been paid-up, whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company;

(iii) capital shall be deemed to be preference capital, notwithstanding that it is entitled to either or both of the following rights, namely: -

(a) that in respect of dividends, in addition to the preferential rights to the amounts specified in sub-clause (a) of clause (ii), it has a right to participate, whether fully or to a limited extent, with capital not entitled to the preferential right aforesaid;

(b) that in respect of capital, in addition to the preferential right to the repayment, on a winding up, of the amounts specified in sub-clause (b) of clause (ii), it has a right to participate, whether fully or to a limited extent, with capital not entitled to that preferential right in any surplus which may remain after the entire capital has been repaid.

Nature of Share or Debentures: Sec. 44

The shares or debentures or other interest of any member in a company shall be movable property transferable in the manner provided by the articles of the company.

11.4 Numbering of Shares: Sec. 45

Every share in a company having a share capital shall be distinguished by its distinctive number:

Provided that nothing in this section shall apply to a share held by a person whose name is entered as holder of beneficial interest in such share in the records of a depository.

11.5 Certificates of Shares: Sec. 46

(1) A certificate, issued under the common seal, if any, of the company or signed by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary, specifying the shares held by any person, shall be prima facie evidence of the title of the person to such shares.

(2) A duplicate certificate of shares may be issued, if such certificate--

(a) is proved to have been lost or destroyed; or

(b) has been defaced, mutilated, or torn and is surrendered to the company.

(3) Notwithstanding anything contained in the articles of a company, the manner of issue of a certificate of shares or the duplicate thereof, the form of such certificate, the particulars to be entered in the register of members and other matters shall be such as may be prescribed.

(4) Where a share is held in depository form, the record of the depository is the prima facie evidence of the interest of the beneficial owner.

(5) In case of issue of duplicate shares to defraud:

-If a company with intent to defraud issues a duplicate certificate of shares, the company shall be punishable with fine which shall not be less than five times the face value of the shares involved in the issue of the duplicate certificate, but which may extend to ten times the face value of such shares or rupees ten crores whichever is higher and

-every officer of the company who is in default shall be liable for action under section 447.

11.6 Voting Rights: Sec. 47

(1) Subject to the provisions of section 43, sub-section (2) of section 50 and sub-section (1) of section 188, --

(a) every member of a company limited by shares and holding equity share capital therein, shall have a right to vote on every resolution placed before the company; and

(b) his voting right on a poll shall be in proportion to his share in the paid-up equity share capital of the company.

(2) Every member of a company limited by shares and holding any preference share capital therein shall, in respect of such capital, have:

- ✓ a right to vote only on resolutions placed before the company which directly affect the rights attached to his preference shares and, any resolution for the winding up of the company or for the repayment or reduction of its equity or preference share capital and
- ✓ his voting right on a poll shall be in proportion to his share in the paid-up preference share capital of the company.

Provided that the proportion of the voting rights of equity shareholders to the voting rights of the preference shareholders shall be in the same proportion as the paid-up capital in respect of the equity shares bears to the paid-up capital in respect of the preference shares.

Provided further that where the dividend in respect of a class of preference shares has not been paid for a period of two years or more, such class of preference shareholders shall have a right to vote on all the resolutions placed before the company.

11.7 Variation of shareholders' rights: Sec. 48

(1) Where a share capital of the company is divided into different classes of shares, the rights attached to the shares of any class may be varied with the consent in writing of the holders of not less than three-fourths of the issued shares of that class or by means of a special resolution passed at a separate meeting of the holders of the issued shares of that class, --

(a) if provision with respect to such variation is contained in the memorandum or articles of the company; or

(b) in the absence of any such provision in the memorandum or articles, if such variation is not prohibited by the terms of issue of the shares of that class:

Provided that if variation by one class of shareholders affects the rights of any other class of shareholders, the consent of three-fourths of such other class of shareholders shall also be obtained and the provisions of this section shall apply to such variation.

(2) Where the holders of not less than ten percent of the issued shares of a class did not consent to such variation or vote in favor of the special resolution for the variation, they may apply to the Tribunal to have the variation cancelled, and where any such application is made, the variation shall not have effect unless and until it is confirmed by the Tribunal:

Provided that an application under this section shall be made within twenty-one days after the date on which the consent was given or the resolution was passed, as the case may be, and may be made on behalf of the shareholders entitled to make the application by such one or more of their number as they may appoint in writing for the purpose.

(3) The decision of the Tribunal on any application under sub-section (2) shall be binding on the shareholders.

(4) The company shall, within thirty days of the date of the order of the Tribunal, file a copy thereof with the Registrar.

11.8 Calls on shares of same class to be made on uniform basis: Sec. 49

Where any calls for further share capital are made on the shares of a class, such calls shall be made on a uniform basis on all shares falling under that class.

For the purposes of this section, shares of the same nominal value on which different amounts have been paid-up shall not be deemed to fall under the same class.

11.9 Company to accept unpaid share capital, although not called up: Sec. 50

(1) A company may, if so, authorized by its articles, accept from any member, the whole or a part of the amount remaining unpaid on any shares held by him, even if no part of that amount has been called up.

(2) A member of the company limited by shares shall not be entitled to any voting rights in respect of the amount paid by him under sub-section (1) until that amount has been called up.

11.10 Payment of dividend in proportion to amount paid-up: Sec. 51

A company may, if so, authorized by its articles, pay dividends in proportion to the amount paid-up on each share.

11.11 Application of premiums received on issue of shares: Sec. 52

(1) Where a company issue shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the premium received on those shares shall be transferred to a securities premium account and the provisions of this Act relating to reduction of share capital of a company shall, except as provided in this section, apply as if the securities premium account were the paid-up share capital of the company.

(2) Notwithstanding anything contained in sub-section (1), the securities premium account may be applied by the company--

(a) towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares;

(b) in writing off the preliminary expenses of the company;

(c) in writing off the expenses of, or the commission paid, or discount allowed on, any issue of shares or debentures of the company;

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(d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company; or

(e) for the purchase of its own shares or other securities under section 68.

(3) The securities premium account may, notwithstanding anything contained in sub-sections (1) and (2), be applied by such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under section 133,

(a) in paying up unissued equity shares of the company to be issued to members of the company as fully paid bonus shares; or

(b) in writing off the expenses of or the commission paid, or discount allowed on any issue of equity shares of the company; or

(c) for the purchase of its own shares or other securities under section 68.

11.12 Prohibition on issue of shares at discount: Sec. 53

(1) Except as provided in section 54, a company shall not issue shares at a discount.

(2) Any share issued by a company at a discount shall be void.

2(2A) Notwithstanding anything contained in sub-sections (1) and (2), a company may issue shares at a discount to its creditors when its debt is converted into shares in pursuance of any statutory resolution plan or debt restructuring scheme in accordance with any guidelines or directions or regulations specified by the Reserve Bank of India under the Reserve Bank of India Act, 1934 (2 of 1934) or the Banking (Regulation) Act, 1949 (10 of 1949).

3(3) Where any company fails to comply with the provisions of this section, such company and every officer who is in default shall be liable to a penalty which may extend to an amount equal to the amount raised through the issue of shares at a discount of five lakh rupees, whichever is less, and the company shall also be liable to refund all monies received with interest at the rate of twelve per cent. per annum from the date of issue of such shares to the persons to whom such shares have been issued.

11.13 Issues of sweat equity shares: Sec. 54

(1) Notwithstanding anything contained in section 53, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled, namely: --

(a) the issue is authorized by a special resolution passed by the company;

(b) the resolution specifies the number of shares, the current market price, consideration, if any, and the class or classes of directors or employees to whom such equity shares are to be issued.

(c) C clause is omitted.

(d) where the equity shares of the company are listed on a recognized stock exchange, the sweat equity shares are issued in accordance with the regulations made by the Securities and Exchange Board in this behalf and if they are not so listed, the sweat equity shares are issued in accordance with such rules as may be prescribed.

(2) The rights, limitations, restrictions and provisions as are for the time being applicable to equity shares shall be applicable to the sweat equity shares issued under this section and the holders of such shares shall rank paripassu with other equity shareholders.

11.14 Issue and redemption of preference shares: Sec. 55

(1) No company limited by shares shall, after the commencement of this Act, issue any preference shares which are irredeemable.

(2) A company limited by shares may, if so, authorized by its articles, issue preference shares which are liable to be redeemed within a period not exceeding twenty years from the date of their issue subject to such conditions as may be prescribed:

Provided that a company may issue preference shares for a period exceeding twenty years for infrastructure projects, subject to the redemption of such percentage of shares as may be prescribed on an annual basis at the option of such preferential shareholders:

Provided further that—

(a) no such shares shall be redeemed except out of the profits of the company which would otherwise be available for dividend or out of the proceeds of a fresh issue of shares made for the purposes of such redemption;

(b) no such shares shall be redeemed unless they are fully paid;

(c) where such shares are proposed to be redeemed out of the profits of the company, there shall, out of such profits, be transferred, a sum equal to the nominal amount of the shares to be redeemed, to a reserve, to be called the Capital Redemption Reserve Account, and the provisions of this Act relating to reduction of share capital of a company shall, except as provided in this section, apply as if the Capital Redemption Reserve Account were paid-up share capital of the company; and

(d) (i) in case of such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under section 133, the premium, if any, payable on redemption shall be provided for out of the profits of the company, before the shares are redeemed:

Provided also that premium, if any, payable on redemption of any preference shares issued on or before the commencement of this Act by any such company shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

(ii) in a case not falling under sub-clause (i) above, the premium, if any, payable on redemption shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

(3) Where a company is not in a position to redeem any preference shares or to pay dividend, if any, on such shares in accordance with the terms of issue (such shares hereinafter referred to as unredeemed preference shares), it may, with the consent of the holders of three-fourths in value of such preference shares and with the approval of the Tribunal on a petition made by it in this behalf, issue further redeemable preference shares equal to the amount due including the dividend thereon, in respect of the unredeemed preference shares, and on the issue of such further redeemable preference shares, the unredeemed preference shares shall be deemed to have been redeemed:

Provided that the Tribunal shall, while giving approval under this sub-section, order the redemption forthwith of preference shares held by such persons who have not consented to the issue of further redeemable preference shares.



For the removal of doubts, it is hereby declared that the issue of further redeemable preference shares or the redemption of preference shares under this section shall not be deemed to be an increase or, as the case may be, a reduction, in the share capital of the company.

(4) The capital redemption reserve account may, notwithstanding anything in this section, be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.



For the purposes of sub-section (2), the term infrastructure projects mean the infrastructure projects specified in Schedule VI.

11.15 Publication of authorized, subscribed and paid-up: Sec. 60

(1) Where any notice, advertisement or other official publication, or any business letter, billhead or letter paper of a company contains a statement of the amount of the authorized capital of the company,

Such Communication modes in terms of notice, advertisement or other official publication, or such letter, billhead or letter paper shall also contain a statement, in an equally prominent position and in equally conspicuous characters, of the amount of the capital which has been subscribed and the amount paid-up.

(2) If any default is made in complying with the requirements of sub-section (1),

-the company shall be liable to pay a penalty of ten thousand rupees and

-every officer of the company who is in default shall be liable to pay a penalty of five thousand rupees, for each default.

11.16 Power of limited company to alter its share capital: Sec. 61

(1) A limited company having a share capital may, if so, authorized by its articles, alter its memorandum in its general meeting to--

(a) increase its authorized share capital by such amount as it thinks expedient;

(b) consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares:

Provided that no consolidation and division which results in changes in the voting percentage of shareholders shall take effect unless it is approved by the Tribunal on an application made in the prescribed manner;

(c) convert all or any of its fully paid-up shares into stock, and reconvert that stock into fully paid-up shares of any denomination;

(d) sub-divide its shares, or any of them, into shares of smaller amount than is fixed by the memorandum, so, however, that in the sub-division the proportion between the amount paid and the amount, if any, unpaid on each reduced share shall be the same as it was in the case of the share from which the reduced share is derived;

(e) cancel shares which, at the date of the passing of the resolution in that behalf, have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the shares so cancelled.

(2) The cancellation of shares under sub-section (1) shall not be deemed to be a reduction of share capital.

11.17 Further issue of share capital: Sec. 62

(1) Where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered-

(a) to persons who, at the date of the offer, are holders of equity shares of the company in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares by sending a letter of offer subject to the following conditions, namely: --

(i) the offer shall be made by notice specifying the number of shares offered and limiting a time not being less than fifteen days or such lesser number of days as may be prescribed and not exceeding thirty days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined;

(ii) unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favor of any other person; and the notice referred to in clause (i) shall contain a statement of this right;

(iii) after the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, the Board of Directors may dispose of them in such manner which is not disadvantageous to the shareholders and the company;

(b) to employees under a scheme of employees' stock option, subject to special resolution passed by company and subject to such conditions as may be prescribed; or

(c) to any persons, if it is authorized by a special resolution, whether or not those persons include the persons referred to in clause (a) or clause (b), either for cash or for a consideration other than cash, if the price of such shares is determined by the valuation report of a registered valuer, subject to the compliance with the applicable provisions of Chapter III and any other conditions as may be prescribed.

(2) The notice referred to in sub-clause (i) of clause (a) of sub-section (1) shall be dispatched through registered post or speed post or through electronic mode or courier or any other mode having proof of delivery to all the existing shareholders at least three days before the opening of the issue.

(3) Nothing in this section shall apply to the increase of the subscribed capital of a company caused by the exercise of an option as a term attached to the debentures issued or loan raised by the company to convert such debentures or loans into shares in the company:

Provided that the terms of issue of such debentures or loan containing such an option have been approved before the issue of such debentures or the raising of loan by a special resolution passed by the company in general meeting.

(4) Notwithstanding anything contained in sub-section (3), where any debentures have been issued, or loan has been obtained from any Government by a company, and if that Government considers it necessary in the public interest so to do, it may, by order, direct that such debentures or loans or any part thereof shall be converted into shares in the company on such terms and conditions as appear to the Government to be reasonable in the circumstances of the case even if terms of the issue of such debentures or the raising of such loans do not include a term for providing for an option for such conversion:

Provided that where the terms and conditions of such conversion are not acceptable to the company, it may, within sixty days from the date of communication of such order, appeal to the Tribunal which shall after hearing the company and the Government pass such order as it deems fit.

(5) In determining the terms and conditions of conversion under sub-section (4), the Government shall have due regard to the financial position of the company, the terms of issue of debentures or loans, as the case may be, the rate of interest payable on such debentures or loans and such other matters as it may consider necessary.

(6) Where the Government has, by an order made under sub-section (4), directed that any debenture or loan or any part thereof shall be converted into shares in a company and where no appeal has been preferred to the Tribunal under sub-section (4) or where such appeal has been dismissed, the memorandum of such company shall, where such order has the effect of increasing the authorized share capital of the company, stand altered and the authorized share capital of such company shall stand increased by an amount equal to the amount of the value of shares which such debentures or loans or part thereof has been converted into.

11.18 Issue of bonus shares: Sec. 63

(1) A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of--

- (i) its free reserves;
- (ii) the securities premium account; or
- (iii) the capital redemption reserve account:

Provided that no issue of bonus shares shall be made by capitalizing reserves created by the revaluation of assets.

(2) No company shall capitalize its profits or reserves for the purpose of issuing fully paid-up bonus shares under sub-section (1), unless –

- (a) it is authorized by its articles;
- (b) it has, on the recommendation of the Board, been authorized in the general meeting of the company;
- (c) it has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;
- (d) it has not defaulted in respect of the payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;
- (e) the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up;
- (f) it complies with such conditions as may be prescribed.

(3) The bonus shares shall not be issued in lieu of dividend.

11.19 Notice to be given to Registrar for alteration of share: Sec. 64

(1) Where--

(a) a company alters its share capital in any manner specified in sub-section (1) of section 61;

(b) an order made by the Government under sub-section (4) read with sub-section (6) of section 62 has the effect of increasing authorized capital of a company; or

(c) a company redeems any redeemable preference shares,

the company shall file a notice in the prescribed form with the Registrar within a period of thirty days of such alteration or increase or redemption, as the case may be, along with an altered memorandum.

(2) where any company fails to comply with the provisions of sub-section (1), such company rupees and every officer who is in default shall be liable to a penalty of five hundred rupees for each day during which such default continues, subject to a maximum of five lakh rupees in case of a company and one lakh rupees in case of an officer who is in default.

11.20 Borrowing Power: Introduction

The power to borrow monies is an inherent power with corporate entities for the purposes of company. This power is to be exercised in terms of provisions of Companies Act, 1956/2013 and Memorandum and Articles of Association of the company.

However, in case of companies registered under section 25 of the Companies Act, 1956 or section 8 of the Companies Act, 2013, (these sections are related to formation of companies with Charitable objects) there is a doubt whether such companies can borrow from the Bank under the provision of the Companies Act.

Powers of Board: Sec. 179

(1) The Board of Directors of a company shall be entitled to exercise all such powers, and to do all such acts and things, as the company is authorized to exercise and do:

Provided that in exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made thereunder, including regulations made by the company in general meeting;

Provided further that the Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting.

(2) No regulation made by the company in general meeting shall invalidate any prior act of the Board which would have been valid if that regulation had not been made.

(3) The Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board, namely: --

(a) to make calls on shareholders in respect of money unpaid on their shares;

(b) to authorize buy-back of securities under section 68;

(c) to issue securities, including debentures, whether in or outside India;

(d) to borrow monies;

(e) to invest the funds of the company;

(f) to grant loans or give guarantee or provide security in respect of loans;

(g) to approve financial statement and the Boards report;

(h) to diversify the business of the company;

(i) to approve amalgamation, merger or reconstruction;

(j) to take over a company or acquire a controlling or substantial stake in another company;

(k) any other matter which may be prescribed

The power to 'borrow monies' is specific power given to the board under clause (d) above.

It is further provided that power to borrow money can be delegated. The board may, by a resolution passed at a meeting, delegate to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the power specified in clauses (d) to (f) on such conditions as it may specify.

Provided further that the acceptance by a banking company in the ordinary course of its business of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise, or the placing of monies on deposit by a banking company with another banking company on such conditions as the Board may prescribe, shall not be deemed to be a borrowing of monies or, as the case may be, a making of loans by a banking company within the meaning of this section.

The borrower company which may be a private limited company or public limited company registered under the Companies Act, 1956 is eligible to borrow monies through its board subject to provisions in Articles of Association of the Company.

11.21 Restrictions on powers of Board: Sec. 180

(1) The Board of Directors of a company shall exercise the following powers only with the consent of the company by a special resolution, namely: --

(a) to sell, lease or otherwise dispose of the whole or substantially the whole of the undertaking of the company or where the company owns more than one undertaking, of the whole or substantially the whole of any of such undertakings.

(b) to invest otherwise in trust securities the amount of compensation received by it as a result of any merger or amalgamation;

(c) to borrow money, where the money to be borrowed, together with the money already borrowed by the company will exceed aggregate of its paid-up share capital, free reserves and securities premium, apart from temporary loans obtained from the company's bankers in the ordinary course of business;

(d) to remit, or give time for the repayment of, any debt due from a director.

(2) Every special resolution passed by the company in general meeting in relation to the exercise of the powers referred to in clause (c) of sub-section (1) shall specify the total amount up to which monies may be borrowed by the Board of Directors.

(3) Nothing contained in clause (a) of sub-section (1) shall affect--

(a) the title of a buyer or other person who buys or takes on lease any property, investment or undertaking as is referred to in that clause, in good faith; or

(b) the sale or lease of any property of the company where the ordinary business of the company consists of, or comprises, such selling or leasing.

(4) Any special resolution passed by the company consenting to the transaction as is referred to in clause (a) of sub-section (1) may stipulate such conditions as may be specified in such resolution, including conditions regarding the use, disposal or investment of the sale proceeds which may result from the transactions:

Provided that this sub-section shall not be deemed to authorize the company to effect any reduction in its capital except in accordance with the provisions contained in this Act.

(5) No debt incurred by the company in excess of the limit imposed by clause (c) of sub-section (1) shall be valid or effectual, unless the lender proves that he advanced the loan in good faith and without knowledge that the limit imposed by that clause had been exceeded.

11.22 Ultra Vires Borrowing

The power to borrow money is specified by the memorandum and articles of association of the Company and directors cannot go beyond such authority, if the director borrow beyond the power prescribed by the MOA and AOA then the borrowings is considered as ultra-vires borrowings.

Borrowing by a company may be --

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1. A borrowing which is ultra vires the company, or
2. A borrowing which is intra vires the company but ultra vires the directors.

Borrowings ultra- vires the company: Consequences

When a company has no borrowing powers, or where the memorandum of association fixes a limit on the borrowing powers of the company, any borrowing in the first case and any borrowing in excess of such limit in the other case is ultra- virus the company.

In such a case: -

- The contract is void ab initio –and the lender cannot sue the company for the return of the loan.
- The lender will also be under an obligation to return back the securities, if any.
- The company cannot ratify the ultra vires loan by resolution in general meeting.

Borrowings ultra- vires the company: Remedies of Lender

- Injunction
- Subrogation
- Identification and tracing
- Recovery of Damages

1. Injunction. If a lender intervenes before the money has been spent, he has a right to follow his money and to obtain an injunction restraining the company from parting with it.

2. Subrogation. If the money borrowed ultra vires has been used to pay off legitimate debts of the company (whether incurred before or after the money was borrowed), the lender is entitled to treat his loan as intra-vires to the extent to which the money was so applied. He can sue the company by virtue of principle of subrogation.

Here subrogation is allowed for the simple reason that when a company which borrows to pay off existing debts, does not thereby, increase its general indebtedness because there is merely replacement of one debt by another of the same amount.

The right of subrogation does not entitle the lender to any security held by the original creditor or to any priority that the original creditors may have had over the other creditors of the company.

However, the lender can retain the securities given to him by the company because his security will be good to the extent to which money was so applied for intra vires debts.

3. Identification and tracing. If the money lent to the company can be traced in the hands of the company in original form or even if it has been employed for the purchase of property which is still capable of identification, the ultra vires lender can obtain a tracing order and may claim that asset or money.

But when the lender's money and that of the company have become mixed up and the two cannot be separated from each other, the lender may claim paripassu distribution of the assets with the shareholders in the event of the winding up of the company.

4. Recovery of Damages. The lender may hold the directors personally liable for contracting an ultra vires loan of the company. The directors are liable for damages to the lender for the breach of the implied warranty of authority.

Borrowing intra vires the company but ultra vires the directors: Consequences

A distinction must be drawn between borrowing ultra vires the company i.e., outside the objects set out in the memorandum and borrowing ultra vires the directors. Borrowing in the first category is void and cannot under any circumstances be ratified by the company.

Borrowing ultra vires, the directors, but within the power conferred by the memorandum, is voidable only and may be ratified by the company. If the borrowing is ratified, the company becomes liable to repay the money.

Borrowing intra vires the company but ultra vires the directors: Remedies of Lender

Where such borrowing is not ratified by the company, the remedies available to lender are:

- Doctrine of indoor management
- No notice for unauthorized business

1. Doctrine of indoor management. By relying on the rule in *Royal British Bank v. Turquand* he can recover the amount of loan from the company provided the borrowing was due to non-compliance with some internal regulations of the company.

2. No notice for unauthorized business. A lender is deemed to have notice of the limitations imposed by the memorandum and articles on the borrowing powers of the directors. A company can avoid the liability on the ground that borrowing was known or deemed to be known to be *ultra vires*. Further, where money is borrowed and used for the benefit of the company either in paying its debts or for its legitimate business, the company cannot avoid its liability on the ground that the agent had no authority from the company to borrow.

But if restrictions on the director's authority are secret or not obvious from these documents, or otherwise the lender does not know of it from some other source, the company will be bound.

11.23 Debentures: Sec. 2(30)

"Debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not:

Provided that--

- (a) the instruments referred to in Chapter III-D of the Reserve Bank of India Act, 1934 (2 of 1934); and
- (b) such other instrument, as may be prescribed by the Central Government in consultation with the Reserve Bank of India, issued by a company,

Shall not be treated as debenture.

Debentures: Sec. 71

(1) A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption:

Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting.

- (2) No company shall issue any debentures carrying any voting rights.
- (3) Secured debentures may be issued by a company subject to such terms and conditions as may be prescribed.
- (4) Where debentures are issued by a company under this section, the company shall create a debenture redemption reserve account out of the profits of the company available for payment of dividend and the amount credited to such account shall not be utilized by the company except for the redemption of debentures.
- (5) No company shall issue a prospectus or make an offer or invitation to the public or to its members exceeding five hundred for the subscription of its debentures, unless the company has, before such issue or offer, appointed one or more debenture trustees and the conditions governing the appointment of such trustees shall be such as may be prescribed.
- (6) A debenture trustee shall take steps to protect the interests of the debenture-holders and redress their grievances in accordance with such rules as may be prescribed.
- (7) Any provision contained in a trust deed for securing the issue of debentures, or in any contract with the debenture-holders secured by a trust deed, shall be void in so far as it would have the effect of exempting a trustee thereof from, or indemnifying him against, any liability for breach of trust, where he fails to show the degree of care and due diligence required of him as a trustee, having regard to the provisions of the trust deed conferring on him any power, authority or discretion.

Provided that the liability of the debenture trustee shall be subject to such exemptions as may be agreed upon by a majority of debenture-holders holding not less than three-fourths in value of the total debentures at a meeting held for the purpose.

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(8) A company shall pay interest and redeem the debentures in accordance with the terms and conditions of their issue.

(9) Where at any time the debenture trustee comes to a conclusion that the assets of the company are insufficient or are likely to become insufficient to discharge the principal amount as and when it becomes due, the debenture trustee may file a petition before the Tribunal.

The Tribunal may, after hearing the company and any other person interested in the matter, by order, impose such restrictions on the incurring of any further liabilities by the company as the Tribunal may consider necessary in the interests of the debenture-holders.

(10) Where a company fails to redeem the debentures on the date of their maturity or fails to pay interest on the debentures when it is due, the Tribunal may, on the application of any or all of the debenture-holders, or debenture trustee and, after hearing the parties concerned, direct, by order, the company to redeem the debentures forth with on payment of principal and interest due thereon.



Sub-section (11) omitted by Act 29 of 2020, s. 15 (w.e.f. 21-12-2020).

(12) A contract with the company to take up and pay for any debentures of the company may be enforced by a decree for specific performance.

(13) The Central Government may prescribe the procedure, for securing the issue of debentures, the form of debenture trust deed, the procedure for the debenture-holders to inspect the trust deed and to obtain copies thereof, quantum of debenture redemption reserve required to be created and such other matters.

11.24 Charge: Sec. 2(16)

"Charge" means an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage.

11.25 Duty to register charges, etc.: Sec. 77

(1) It shall be the duty of every company creating a charge within or outside India, on its property or assets or any of its undertakings, whether tangible or otherwise, and situated in or outside India, to register the particulars of the charge signed by the company and the charge-holder together with the instruments, if any, creating such charge in such form, on payment of such fees and in such manner as may be prescribed, with the Registrar within
Provided that the Registrar may, on an application by the company, allow such registration to be made –

(2) (a) in case of charges created before the commencement of the Companies (Amendment) Act, 2019, within a period of three hundred days of such creation: or thirty days of its creation:

(b) in case of charges created on or after the commencement of the Companies (Amendment) Act, 2019, within a period of sixty days of such creation,

on payment of such additional fees as may be prescribed:

Provided further that if the registration is not made within the period specified –

(a) in clause (a) to the first proviso, the registration of the charges shall be made within six months from the date of commencement of the Companies (Amendment) Act, 2019,

on payment of such additional fees as may be prescribed and different fees may be prescribed for different classes of companies.

(b) in clause (b) to the first proviso, the Registrar may, on an application, allow such registration to be made within a further period of sixty days after payment of such ad valorem fees as may be prescribed.

Provided also that any subsequent registration of a charge shall not prejudice any right acquired in respect of any property before the charge is actually registered:

Provided also that this section shall not apply to such charges as may be prescribed in consultation with the Reserve Bank of India.

(2) Where a charge is registered with the Registrar under sub-section (1), he shall issue a certificate of registration of such charge in such form and in such manner as may be prescribed to the company and, as the case may be, to the person in whose favor the charge is created.

(3) Notwithstanding anything contained in any other law for the time being in force, no charge created by a company shall be taken into account by the liquidator appointed under this Act or the Insolvency and Bankruptcy Code, 2016 (31 of 2016), as the case may be, or any other creditor unless it is duly registered under sub-section (1) and a certificate of registration of such charge is given by the Registrar under sub-section (2).

(4) Nothing in sub-section (3) shall prejudice any contract or obligation for the repayment of the money secured by a charge.

11.26 Application for registration of charge: Sec. 78

Where a company fails to register the charge within the period specified in section 77, without prejudice to its liability in respect of any offence under this Chapter, the person in whose favor the charge is created may apply to the Registrar for registration of the charge along with the instrument created for the charge, within such time and in such form and manner as may be prescribed and the Registrar may, on such application, within a period of fourteen days after giving notice to the company, unless the company itself registers the charge or shows sufficient cause why such charge should not be registered, allow such registration on payment of such fees, as may be prescribed.

Provided that where registration is affected on application of the person in whose favor the charge is created, that person shall be entitled to recover from the company the amount of any fees or additional fees paid by him to the Registrar for the purpose of registration of charge.

11.27 Applicability of Sec. 77: Sec. 79

The provisions of section 77 relating to registration of charges shall, so far as may be, apply to--

- (a) a company acquiring any property subject to a charge within the meaning of that section; or
- (b) any modification in the terms or conditions or the extent or operation of any charge registered under that section.

11.28 Date of notice of charge: Sec. 80

Where any charge on any property or assets of a company or any of its undertakings is registered under section 77, any person acquiring such property, assets, undertakings or part thereof or any share or interest therein shall be deemed to have notice of the charge from the date of such registration.

11.29 Register of charges to be kept by Registrar: Sec. 81

(1) The Registrar shall, in respect of every company, keep a register containing particulars of the charges registered under this Chapter in such form and in such manner as may be prescribed.

(2) A register kept in pursuance of this section shall be open to inspection by any person on payment of such fees as may be prescribed for each inspection.

Summary

- A share determines the rights to a specified amount of the share capital of a company. It carries with it certain rights and liabilities during the lifetime of the company and also when it is being wound up.
- A company can have Equity Share Capital and Preference Share Capital.

- The shares or debentures or other interest of any member in a company shall be movable property transferable in the manner provided by the articles of the company.
- Every share in a company having a share capital shall be distinguished by its distinctive number as per Sec. 45.
- A certificate, issued under the common seal, if any, of the company or signed by two directors or by a director and the Company Secretary, wherever the company has appointed a Company Secretary, specifying the shares held by any person, shall be prima facie evidence of the title of the person to such shares.
- Every member of a company limited by shares and holding equity share capital therein, shall have a right to vote on every resolution placed before the company as per Sec. 47.
- Where a share capital of the company is divided into different classes of shares, the rights attached to the shares of any class may be varied with the consent in writing of the holders of not less than three-fourths of the issued shares of that class or by means of a special resolution passed at a separate meeting of the holders of the issued shares of that class.
- Where any calls for further share capital are made on the shares of a class, such calls shall be made on a uniform basis on all shares falling under that class.
- A company may, if so, authorized by its articles, pay dividends in proportion to the amount paid-up on each share.
- No company limited by shares shall, after the commencement of this Act, issue any preference shares which are irredeemable.
- A limited company having a share capital may, if so, authorized by its articles, alter its memorandum in its general meeting to--

(a) increase its authorized share capital by such amount as it thinks expedient.

(b) consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares.

- A company may further issue the share capital as per provisions of Sec. 62.
- A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of--

(i) its free reserves;

(ii) the securities premium account; or

(iii) the capital redemption reserve account:

Provided that no issue of bonus shares shall be made by capitalizing reserves created by the revaluation of assets.

- The company shall file a notice in the prescribed form with the Registrar within a period of thirty days of such alteration or increase or redemption, as the case may be, along with an altered memorandum.
- The power to borrow money is specified by the memorandum and articles of association of the Company and directors cannot go beyond such authority, if the director borrow beyond the power prescribed by the MOA and AOA than the borrowings is considered as ultra-vires borrowings.
- A power to borrow, whether express or implied, includes the power to charge the assets of the company by way of security to the lender.
- The power to borrow money is generally exercised by the directors but Articles normally provide for certain restrictions on their power to borrow.

Keywords

Borrowing: A power to borrow, whether express or implied, includes the power to charge the assets of the company by way of security to the lender.

Charge: "Charge" means an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage.

Cumulative Preference Share: If a preference share carries the right for payment of arrears of dividend from future profits, then such a share is known as cumulative preference share.

Equity Share: 'Equity share' means a share which is not a preference share (s.85). The rate of dividend is not fixed.

Non-voting Share: 'Non-voting shares' as the term suggests, are shares which carry no voting rights. These are contemplated as altogether a different class of shares which may carry additional dividends in lieu of the voting rights.

Redeemable Share: A preference share which can be redeemed upon the resolution of the board of directors, if the articles so provide, is known as redeemable preference share.

Share: A share is the share capital of a company and includes stock except where a distinction between stock and share is expressed or implied.

Stock: The term 'stock' may be defined as the aggregate of fully paid-up shares of a member merged into one fund of equal value.

Self Assessment

1. Preference shareholders get preferential rights concerning:
 - A. payment of dividend
 - B. repayment, in the case of a winding-up
 - C. both payment of dividend and repayment in the case of a winding-up
 - D. either payment of dividend or repayment in the case of a winding-up

2. Every share's distinctive number shall distinguish every share in a company having a share capital.
 - A. True
 - B. False

3. A duplicate certificate of shares may be issued, if original certificate:
 - A. is proved to have been lost or destroyed
 - B. has been defaced, mutilated, or torn and is surrendered to the company
 - C. either certificate is proved to have been lost/destroyed or has been defaced, mutilated, or torn and is surrendered to the company
 - D. is not proved to have been lost or destroyed

4. In case of issue of duplicate shares to defraud, then:
 - A. the company shall be punishable with a fine which shall not be less than five times the face value of the shares involved in the issue of the duplicate certificate
 - B. the company shall be punishable with a fine which may extend to ten times the face value of such shares or rupees ten crores, whichever is higher
 - C. every officer of the company who is in default shall be liable for action under section 447
 - D. all of above

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5. Where any calls for additional share capital have to be made on the shares of a class, such calls shall be made on a:
 - A. uniform basis on all shares falling under that class.
 - B. varied basis on all shares falling under that class.
 - C. inconsistent basis on all shares falling under that class.
 - D. Any discretionary basis on all shares falling under that class.

6. A company may accept from any member the whole or a part of the amount remaining unpaid on any shares held by him, even if no part of that amount has been called up.
 - A. If so, authorized by its articles
 - B. If so, authorized by its memorandum
 - C. If so, authorized by its prospectus
 - D. If so, authorized by its share certificate

7. The company may apply the securities premium account:
 - A. towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares
 - B. in writing off the preliminary expenses of the company
 - C. in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company
 - D. all of above

8. A company may issue sweat equity shares of a class of shares already issued if the following condition/s is/are fulfilled:
 - A. the issue is authorized by a special resolution passed by the company
 - B. the issue is authorized by an ordinary resolution passed by the company
 - C. the special resolution does not specify the number of shares, the current market price, consideration if any,
 - D. the ordinary resolution specifies the class or classes of directors or employees to whom such equity shares are to be issued

9. A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of:
 - A. its free reserves
 - B. the securities premium account
 - C. the capital redemption reserve account
 - D. all of the above

10. No issue of bonus shares shall be made by capitalizing reserves created by the revaluation of assets as per Sec. 63.
 - A. True
 - B. False

11. Borrowing ultra-vires the company means:
 - A. when a company has no borrowing powers, but the company still borrows the funds

- B. where the memorandum of association fixes a limit on the borrowing powers of the company, and the company opt to borrow within such limit
- C. when a company has borrowing powers, but the company borrows the funds
- D. all of above

12. The consequences of the borrowings that are ultra-vires the company is/are:

- A. The contract is void ab initio
- B. The lender will also be under an obligation to return the securities if any
- C. The company cannot ratify the ultra vires loan by resolution in general meeting
- D. All of above

13. A lender can exercise any or all of the following remedy/remedies in case of borrowings ultra-vires the company:

- A. Injunction
- B. Subrogation
- C. Recovery of Damages
- D. All of above

14. Borrowing ultra vires the directors, but within the power conferred by the memorandum, is

- A. voidable
- B. may be ratified by the company
- C. voidable and may be ratified by the company
- D. valid and need not be ratified by the company

15. _____ means an interest or lien created on the property or assets of a company or any of its undertakings or both as security and includes a mortgage.

- A. Charge
- B. Borrowing power
- C. Share
- D. Debenture

Answers for Self Assessment

1. C	2. A	3. C	4. D	5. A
6. A	7. D	8. A	9. D	10. A
11. A	12. D	13. D	14. C	15. A

Review Questions

1. Define a share.
2. What are the different types of shares which a company can issue?
3. Discuss the kinds of capital a company can issue.
4. Explain the provisions related to certificate of shares.
5. Discuss the circumstances in which variation of shareholders' rights can happen.

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6. Can any company issue its shares at discount on its discretion? Discuss.
7. Give the legal provisions related to issue and redemption of preference shares.
8. Do limited companies have capacities to alter its share capital? Discuss.
9. Can a company further issue share capital? Justify.
10. What remedies, if any, are open to a lender if a company resorts to ultra vires borrowing?
11. What do you mean by Charge? Is it required to register charges by every company creating such charges? Elaborate.
12. Explain ultra-vires borrowing and its types. Further provide details about consequences and legal remedies available to lender in case of ultra-vires borrowings.
13. Differentiate between Bonus Shares and Sweat Equity Shares.
14. Illustrate the meaning and related provisions of Issue of Bonus Shares.
15. Describe Sweat Equity Shares and discuss the related provisions.

**Further Reading**

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**Web Links**

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Unit 12: Company Management

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Summary

Keywords

Self Assessment

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Further Reading

Objectives

After studying this unit, you will be able to:

- illustrate the meaning of directors.
- explain the provisions related to number of directorships.
- explain the provisions related to qualification and disqualification of directors.
- explain the meaning and provisions related to independent directors.
- illustrate the procedure of appointment of various types of directors.
- explain the provisions relating to the vacation of the office of directors.
- explain the provisions relating to the resignation of Directors.
- review the provisions relating to the removal of directors.
- explain the duties of directors.
- review the role of directors in managing a company.

Introduction

Though a legal entity in the eyes of the law, a company is an artificial person, existing only in contemplation of law. It bears no physical existence and has neither soul nor body of its own. Therefore, a company cannot act in its person. It can work only through some human agency.

The persons in charge of the management of the affairs of a company are termed as directors and collectively are known as the board of directors or the board. Thus, the directors are the brain of a company occupying a pivotal position in the company's structure.

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Directors collectively decide on the company's management in their meetings, known as board meetings, or at the meetings of their committees constituted for certain specific purposes.

Directors of a company hold the most crucial position in the company. The Companies Act, 2013 does not provide an exhaustive definition of the term "Director." But the Act has clearly defined their qualification, disqualification, appointment procedure, resignation, removal of directors, duties, and liabilities. In the present unit, provisions of the Companies Act, 2013 related to appointment and removal of directors, their qualification and disqualification, duties of directors are discussed.

12.1 Directors: Meaning and Definition

A director is a person appointed to perform the duties and functions of the company's director as per provisions of this Act. Their position has become even more significant and critical due to provisions of the Company Act, 2013.

Sec. 2(34) of the Company Act describes the term director as:

"Director" means a director appointed to the Board of a company.



Sec. 2(51) has formally included the directors within the definition of "Key Managerial Personnel" or "KMP," which was not the case before

.Board of Directors: Sec. 2(10)

"Board of Directors" or "Board," concerning a company, means the collective body of the company's directors.

12.2 Company to have Board of Directors: Sec. 149

Minimum/Maximum Number of Directors in a company: Sec 149(1)

(1) Minimum Number of Directors

- Public Company - 3
- Private Company - 2
- One Person Company – 1

Maximum Number of Directors: 15

A company may appoint more than fifteen directors after passing a special resolution.

Provided further that such classes or companies as may be prescribed shall have at least one woman director.

(2) Minimum/Maximum Number of Directors in a company in case of an existing company: Sec 149(2)

Every company existing on or before the date of commencement of this Act shall comply with the provisions of sub-section (1) requirements within one year from such commencement.

(3) Residence of a Director in India: Sec. 149(3)

Every company shall have at least one director who stays in India for a total period of not less than one hundred and eighty-two days during the financial year.

Provided that in case of a newly incorporated company, the requirement under this subsection shall apply proportionately at the end of the financial year in which it is incorporated;

(4) Number of Independent Directors: Sec. 149(4)

In case of Listed Public Company:

Every listed public company shall have at least one-third of the total number of directors as independent directors. The Central Government may prescribe the minimum number of independent directors in any class of public companies.

For this sub-section, any fraction contained in such one-third number shall be rounded off as one.

Sec.149 (5) Every company existing on or before the date of commencement of this Act shall, within one year from such commencement or from the date of notification of the rules in this regard as may be applicable, comply with the requirements of the provisions of sub-section (4).

12.3 Independent Directors: Meaning- Sec. 149(6)

An independent director concerning a company means a director other than a managing director-- or a whole-time director or a nominee director,

(a) who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience;

(b) (i) who is or was not a promoter of the company or its holding, subsidiary, or associate company;

(ii) who is not related to promoters or directors in the company, its holding, subsidiary, or associate company;

(c) who has or had no financial relationship, other than remuneration as such director or having transaction not exceeding ten percent. of his total income or such amount as may be prescribed, with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year;

3(d) none of whose relatives--

(i) is holding any security of or interest in the company, its holding, subsidiary, or associate company during the two immediately preceding financial years or during the current financial year:

Provided that the relative may hold security or interest in the company of face value not exceeding fifty lakh rupees or two percent of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed;

(ii) is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors, more than such amount as may be prescribed during the two immediately preceding financial years or during the current financial year;

(iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for such amount as may be prescribed during the two immediately preceding financial years or during the current financial year; or

(iv) has any other pecuniary transaction or relationship with the company, its subsidiary, or its holding or associate company amounting to two percent or more of its gross turnover or total income singly or in combination with the transactions referred to in sub-clause (i), (ii) or (iii);]

(e) who, neither himself nor any of his relatives

(i) holds or has held the position of key managerial personnel or is or has been an employee of the company or its holding, subsidiary, or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed;

In the case of a relative who is an employee, the restriction under this clause shall not apply for his employment during the preceding three financial years.

(ii) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of

(A) a firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary, or associate company; or

(B) any legal or consulting firm that has or had any transaction with the company, its holding, subsidiary, or associate company amounting to ten percent or more of the gross turnover of such firm;

(iii) holds together with his relatives two percent or more of the total voting power of the company; or

(iv) is a Chief Executive or director, by whatever name called, of any nonprofit organization that receives twenty-five percent or more of its receipts from the company, any of its promoters,

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directors or its holding, subsidiary or associate company or that holds two percent or more of the total voting power of the company; or

(f) who possesses such other qualifications as may be prescribed.

Criteria of independence: Sec. 149(7)

Every independent director shall at the first meeting of the Board in which he participates as a director and after that at the first meeting of the Board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director, give a declaration that he meets the criteria of independence as provided in sub-section (6).

For this section, nominee director means a director nominated by any financial institution in pursuance of the provisions of any law for the time being in force, or of any agreement, or appointed by any Government, or any other person to represent its interests.

The company and independent directors shall abide by the provisions specified in Schedule IV.- Sec. 149(8)

Remuneration of Independent Director: Sec. 149(8)

Notwithstanding anything contained in any other provision of this Act, but subject to the provisions of sections 197 and 198, an independent director shall not be entitled to any stock option and may receive remuneration by way of fee provided under sub-section (5) of section 197, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members.

Provided that if a company has no profits or its profits are inadequate, an independent director may receive remuneration, exclusive of any fees payable under sub-section (5) of section 197, following the provisions of Schedule V.

Term of Office of Independent Director: Sec. 149(10)

Subject to the provisions of section 152, an independent director shall hold office for a term up to five consecutive years on the Board of a company but shall be eligible for reappointment on the passing of a special resolution by the company and disclosure of such appointment in the Board's report.

As per Sec. 149(11), Notwithstanding anything contained in sub-section (10), no independent director shall hold office for more than two consecutive terms, but such independent director shall be eligible for appointment after the expiration of three years of ceasing to become an independent director:

During the said period of three years, an independent director shall not be appointed in or be associated with the company in any other capacity, either directly or indirectly.

For sub-sections (10) and (11), any tenure of an independent director on the date of commencement of this Act shall not be counted as a term under those sub-sections.

Liability of an independent director: Sec. 149(12)

Notwithstanding anything contained in this Act, --

(i) an independent director;

(ii) a non-executive director not being promoter or key managerial personnel,

shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

As per Sec. 149(13), The provisions of sub-sections (6) and (7) of section 152 in respect of retirement of directors by rotation shall not apply to the appointment of independent directors.

12.4 Number of directorships: Sec. 165

(1) No person, after the commencement of this Act, shall hold office as a director, including any alternate directorship, in more than **twenty companies** at the same time:

The maximum number of public companies in which a person can be appointed as a director shall not exceed ten.

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For reckoning the limit of public companies in which a person can be appointed as director, directorship in private companies that are either holding or subsidiary companies of a public company shall be included.

For reckoning the limit of directorships of twenty companies, the directorship in a dormant company shall not be included.

(2) Subject to the provisions of sub-section (1), the members of a company may, by special resolution, specify any lesser number of companies in which a director of the company may act as directors.

(3) Any person holding office as director in companies more than the limits as specified in sub-section (1), immediately before the commencement of this Act shall, within one year from such commencement, --

(a) choose not more than the specified limit of those companies, as companies in which he wishes to continue to hold the office of director;

(b) resign his office as director in the other remaining companies; and

(c) intimate the choice made by him under clause (a), to each of the companies in which he was holding the director's office before such commencement and to the Registrar having jurisdiction in respect of each such company.

(4) Any resignation made in pursuance of clause (b) of sub-section (3) shall become effective immediately on the dispatch thereof to the company concerned.

(5) No such person shall act as director in more than the specified number of companies, --

(a) after dispatching the resignation of his office as director or non-executive director thereof, in pursuance of clause (b) of sub-section (3); or

(b) after the expiry of one year from the commencement of this Act, whichever is earlier.

(6) If a person accepts an appointment as a director in violation of this section, he shall be liable to a penalty of two thousand rupees for each day after the first during which such violation continues, subject to a maximum of two lakh rupees.

12.5 Appointment of directors

- Appointment of First Director: By promoters
- Appointment of Directors by Directors
- Appointment of directors to be voted individually
- Appointment of director elected by small shareholders
- Appointment of managing director, whole-time director, or manager

Appointment of First Director: Sec. 152

Situation	Appointment of First Director
1. Named in the Company's AOA	Usually named in the company's articles and are appointed by promoters in the manner laid down in AOA. (Until the appointment of directors in the first AGM)
2. If the Company's AOA is silent about the First Director, but articles prescribe the appointment of directors.	The subscribers to the memorandum who are individuals shall be deemed the first directors of the company until the directors are duly appointed.
3. In the case of One Person Company	An individual being a member shall be deemed its first director until the director or directors are duly appointed by the member following the provisions of this section.



The above provisions apply to all companies, whether public or private.

Appointment of First Director: General Provisions as per Sec. 152

- **Appointment in General meeting – Sec. 152(2)**

Save as otherwise expressly provided in this Act, the company shall appoint every director in general meeting.

- **Requirement of DIN – Sec. 152(3)**

No person shall be appointed as a company director unless he has been allotted the Director Identification Number under section 154 or any other number as may be prescribed under section 153.

- **Declaration of Qualification – Sec. 152(4)**

Every person proposed to be appointed as a director by the company in general meeting or otherwise shall furnish his Director Identification Number or other numbers as may be prescribed under section 153 and a declaration that he is not disqualified from becoming a director under this Act.

- **Consent to hold the office of director – Sec. 152(5)**

A person appointed as a director shall not act as a director unless he gives his consent to hold the office as director. Such consent has been filed with the Registrar within thirty days of his appointment in such manner as may be prescribed.

Provided that in the case of appointment of an independent director in the general meeting, an explanatory statement for such appointment, annexed to the notice for the general meeting, shall include a statement that in the opinion of the Board, he fulfills the conditions specified in this Act for such an appointment.

- **Provisions for Retirement – Sec. 152(6)(a)**

Unless the articles provide for the retirement of all directors, at every annual general meeting, not less than two-thirds of the total number of directors of a public company shall:

- (i) be persons whose period of office is liable to determination by retirement of directors by rotation; and
- (ii) save as otherwise expressly provided in this Act, be appointed by the company in general meeting.

- **Provisions for Retirement by Rotation – Sec. 152(6)(c)**

At the first annual general meeting of a public company held next after the date of the general meeting at which the first directors are appointed following clauses (a) and (b) and at every subsequent annual general meeting, one-third of such of the directors for the time being as are liable to retire by rotation, or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office.

Provisions for Retirement by Rotation – Sec. 152(6)(d)

The directors to retire by rotation at every annual general meeting shall be the longest in office since their last appointment. Still, as between persons who became directors on the same day, those who are to retire shall be determined by lot in default of and subject to any agreement among themselves.

- **Filling up the Vacancy – Sec. 152(6)(e)**

At the annual general meeting at which a director retires as aforesaid, the company may fill the vacancy by appointing the retiring director or another person thereto.

For this sub-section, "a total number of directors" shall not include independent directors, whether appointed under this Act or any other law for the time being in force, on the company's board.

Filling up the Vacancy – Sec. 152(7)(a)

Suppose the vacancy of the retiring director is not so filled-up and the meeting has not expressly resolved not to fill the vacancy. In that case, the meeting shall stand adjourned till the same day in

the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day, which is not a holiday, at the same time and place.

Filling up the Vacancy – Sec. 152(7)(b)

Suppose at the adjourned meeting also, the vacancy of the retiring director is not filled up, and that meeting also has not expressly resolved not to fill the vacancy. In that case, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless:

- (i) at that meeting or the previous meeting, a resolution for the reappointment of such director has been put to the meeting and lost;
- (ii) the retiring director has, by a notice in writing addressed to the company or its Board of directors, expressed his unwillingness to be so re-appointed;
- (iii) he is not qualified or is disqualified for appointment;
- (iv) a resolution, whether special or ordinary, is required for his appointment or reappointment under any provisions of this Act; or
- (v) section 162 (related to the appointment of directors to be voted individually) applies to the case.

Appointment of Directors by Directors: Sec. 161

The Board of Directors of a company, subject to the authority given by the Company's articles, is empowered to appoint different types of directors in a company. Such appointment includes the appointment of:

- Additional Director
- Alternate Director
- Nominee Director
- Appointment of directors in Casual Vacancy

Additional Director – Sec. 161(1)

The articles of a company may confer on its Board of Directors the power to appoint any person, other than a person who fails to get appointed as a director in a general meeting, as an additional director at any time who shall hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

Alternate Directors: Sec. 161(2)

The Board of Directors of a company may if so authorized by its articles or by a resolution passed by the company in general meeting, appoint a person to act as an alternate director for a director during his absence for not less than three months from India.

Such a person should not hold any alternate directorship for any other director or holding directorship in the same company.

No person shall be appointed as an alternate director for an independent director unless he is qualified to be appointed as an independent director under the provisions of this Act.

An alternate director shall not hold office for a period longer than that permissible to the director in whose place he has been appointed and shall vacate the office if and when the director in whose place he has been appointed returns to India.

If the term of office of the original director is determined before he so returns to India, any provision for the automatic reappointment of retiring directors in default of another appointment shall apply to the original and not to the alternate director.

Nominee Directors: Sec. 161(3)

Subject to the articles of a company, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or by the Central Government or the State Government under its shareholding in a Government company.

Casual Vacancy: Sec. 161(4)

Suppose the office of any director appointed by the company in general meeting is vacated before the term of office expires in the ordinary course. In that case, the resulting casual vacancy may, in default of and subject to any regulations in the company's articles, be filled by the Board of Directors

at a meeting of the Board, which members shall subsequently approve in the immediate next general meeting.

Any appointed person should hold office only up to the date up to which the director in whose place he is appointed would have held office if it had not been vacated.

Appointment of directors to be voted individually: Sec. 162

(1) At a general meeting of a company, a motion for the appointment of two or more persons as directors of the company by a single resolution shall not be moved unless a proposal to move such a motion has first been agreed to at the meeting without any vote being cast against it.

(2) A resolution moved in contravention of sub-section (1) shall be void, whether or not any objection was taken when it was moved.

(3) A motion for approving a person for an appointment or nominating a person for an appointment as a director shall be treated as a motion for his appointment.

Principle of proportional representation for appointment of directors: Sec. 163

Notwithstanding anything contained in this Act, the articles of a company may provide for the appointment of not less than two-thirds of the total number of the directors of a company under the principle of proportional representation, whether by the single transferable vote or by a system of cumulative voting or otherwise and such appointments may be made once in every three years, and casual vacancies of such directors shall be filled as provided in subsection (4) of section 161.

Appointment of director elected by small shareholders: Sec. 151

A listed company may have one director elected by such small shareholders and with such terms and conditions as may be prescribed.

For this section, "small shareholders" means a shareholder holding shares of the nominal value of not more than twenty thousand rupees or such other sum as may be prescribed.

Appointment of managing director, whole-time director, or manager: Sec. 196

(1) No company shall appoint or employ a managing director and a manager at the same time.

(2) No company shall appoint or re-appoint any person as to its managing director, whole-time director, or manager for a term exceeding five years at a time:

No reappointment shall be made earlier than one year before the expiry of his term.

(3) No company shall appoint or continue the employment of any person as managing director, whole-time director, or manager who --

(a) is below the age of twenty-one years or has attained the age of seventy years:

Provided that appointment of a person who has attained the age of seventy years may be made by passing a special resolution in which case the explanatory statement annexed to the notice for such motion shall indicate the justification for appointing such person;

Provided further that where no such special resolution is passed but votes cast in favor of the motion exceed the votes, if any, cast against the motion and the Central Government is satisfied, on an application made by the Board, that such appointment is most beneficial to the company, the appointment of the person who has attained the age of seventy years may be made;

(b) is an undischarged insolvent or has at any time been adjudged as an insolvent;

(c) has at any time suspended payment to his creditors or makes, or has at any time made, a composition with them; or

(d) has at any time been convicted by a court of an offence and sentenced for more than six months.

(4) Subject to section 197 and Schedule V provisions, a managing director, whole-time director, or manager shall be appointed. The Board approves the terms and conditions of such appointment and remuneration payable of Directors at a meeting, which shall be subject to approval by a resolution at the company's next general meeting. By the Central Government in case such appointment is at variance to the conditions specified in Part I of that Schedule:

Provided that a notice convening Board or general meeting for considering such appointment shall include the terms and conditions of such appointment, remuneration payable and such other matters including interest, of a director or directors in such appointments if any:

A return in the prescribed form shall be filed within sixty days of such appointment with the Registrar.

(5) Subject to the provisions of this Act, where the company does not approve an appointment of a managing director, whole-time director, or manager at a general meeting, any act done by him before such approval shall not be deemed invalid.

12.6 Disqualifications for appointment of director: Sec. 164

(1) A person shall not be eligible for appointment as a director of a company, if --

- (a) he is of unsound mind and stands so declared by a competent court;
- (b) he is an undischarged insolvent;
- (c) he has applied to be adjudicated as an insolvent, and his application is pending;
- (d) he has been convicted by a court of any offence, whether involving moral turpitude or otherwise, and sentenced in respect thereof to imprisonment for not less than six months. A period of five years has not elapsed from the date of expiry of the sentence:

Provided that if a person has been convicted of any offence and sentenced in respect thereof to imprisonment for seven years or more, he shall not be eligible to be appointed as a director in any company;

- (e) a court or Tribunal has passed an order disqualifying him for appointment as a director, and the order is in force;
- (f) he has not paid any calls in respect of any shares of the company held by him, whether alone or jointly with others, and six months have elapsed from the last day fixed for the payment of the call;
- (g) he has been convicted of the offence of dealing with related party transactions under section 188 at any time during the last preceding five years; or
- (h) he has not complied with subsection (3) of section 152.

1(i) he has not complied with the provisions of sub-section (1) of section 165.

(2) No person who is or has been a director of a company which--

- (a) has not filed financial statements or annual returns for any continuous period of three financial years; or
- (b) has failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay the interest due thereon or pay any dividend declared and such failure to pay or redeem continues for one year or more--

--shall be eligible to be re-appointed as a director of that company or appointed in another company for five years from the date on which the said company fails to do so:

Provided that where a person is appointed as a director of a company which is in default of clause (a) or clause (b), he shall not incur the disqualification for six months from the date of his appointment.

(3) A private company may by its articles provide for any disqualifications for appointment as a director in addition to those specified in sub-sections (1) and (2).

Provided that the disqualifications referred to in clauses (d), (e), and (g) of sub-section (1) shall continue to apply even if the appeal or petition has been filed against the order of conviction or disqualification.

12.7 Vacation of office of director: Sec. 167

(1) The office of a director shall become vacant in case--

- (a) he incurs any of the disqualifications specified in section 164:

Provided that where he incurs disqualification under sub-section (2) of section 164, the office of the director shall become vacant in all the companies, other than the company which is in default under that sub-section;

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- (b) he absents himself from all the meetings of the Board of Directors held during twelve months with or without seeking leave of absence of the Board;
- (c) he acts in contravention of the provisions of section 184 relating to entering into contracts or arrangements in which he is directly or indirectly interested;
- (d) he fails to disclose his interest in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of section 184;
- (e) he becomes disqualified by order of a court or the Tribunal;

(f) he is convicted by a court of any offence, whether involving moral turpitude or otherwise, and sentenced in respect thereof to imprisonment for not less than six months:

Provided that the office shall not be vacated by the director in case of orders referred to in clauses (e) and (f)--

- (i) for thirty days from the date of conviction or order of disqualification;
- (ii) where an appeal or petition is preferred within thirty days as aforesaid against the conviction resulting in sentence or order until expiry of seven days from the date on which such appeal or petition is disposed of; or
- (iii) where any further appeal or petition is preferred against order or sentence within seven days until such further appeal or petition is disposed of.
- (g) he is removed in pursuance of the provisions of this Act;
- (h) he, having been appointed a director under his holding any office or other employment in the holding, subsidiary, or associate company, ceases to hold such office or other employment in that company.

(2) If a person functions as a director even when he knows that the office of director held by him has become vacant on account of any of the disqualifications specified in sub-section (1), he shall be punishable with a fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

(3) Where all the directors of a company vacate their offices under any of the disqualifications specified in sub-section (1), the promoter or, in his absence, the Central Government shall appoint the required number of directors who shall hold office till the directors are appointed by the company in the general meeting.

(4) A private company may, by its articles, provide any other ground for the vacation of the office of a director in addition to those specified in sub-section (1).

12.8 Resignation of director: Sec. 168

(1) A director may resign from his office by giving a notice in writing to the company, and the Board shall note the same on receipt of such notice. The company shall intimate the Registrar in such manner, within such time and in such form as prescribed. It shall also place the fact of such resignation in the report of directors laid in the immediately following general meeting by the company:

Provided that a director may also forward a copy of his resignation and detailed reasons for the resignation to the Registrar within thirty days of resignation in such a manner as may be prescribed.

(2) The resignation of a director shall take effect from the date on which the notice is received by the company or the date, if any, specified by the director in the notice, whichever is later:

The director who has resigned shall be liable even after his resignation for the offences that occurred during his tenure.

(3) Where all the directors of a company resign from their offices or vacate their offices under section 167, the promoter or, in his absence, the Central Government shall appoint the required number of directors who shall hold office till the directors are selected by the company in general meeting.

12.9 Removal of Directors: Sec. 169

(1) A company may, by ordinary resolution, remove a director, not being a director appointed by the Tribunal under section 242, before the expiry of the period of his office after giving him a reasonable opportunity of being heard:

Provided that an independent director re-appointed for the second term under sub-section (10) of section 149 shall be removed by the company only by passing a special resolution and after giving him a reasonable opportunity of being heard:

Provided further that nothing contained in this sub-section shall apply where the company has availed itself of the option given to it under section 163 to appoint not less than two-thirds of the total number of directors according to the principle of proportional representation.

(2) A special notice shall be required of any resolution to remove a director under this section or appoint somebody in place of a director so removed at the meeting at which he is removed.

(3) On receipt of notice of a resolution to remove a director under this section, the company shall forthwith send a copy thereof to the director concerned, and the director, whether or not he is a member of the company, shall be entitled to be heard on the resolution at the meeting.

(4) Where notice has been given of a resolution to remove a director under this section, and the director concerned makes with respect thereto representation in writing to the company and requests its notification to members of the company, the company shall, if the time permits it to do so,--

(a) in any notice of the resolution given to members of the company, state the fact of the representation having been made; and

(b) send a copy of the representation to every member of the company to whom notice of the meeting is sent (whether before or after receipt of the representation by the company). If a copy of the representation is not sent as aforesaid due to insufficient time or for the company's default, the director may without prejudice to his right to be heard orally require that the representation shall be read out at the meeting:

Provided that a copy of the representation need not be sent out. The representation need not be read out at the meeting if, on the application, either of the company or any other person who claims to be aggrieved, the Tribunal is satisfied that the rights conferred by this sub-section are being abused to secure needless publicity for the defamatory matter. The Tribunal may order the company's costs on the application to be paid in whole or in part by the director, notwithstanding that he is not a party to it.

(5) A vacancy created by the removal of a director under this section may, if the company had appointed him in general meeting or by the Board, be filled by the appointment of another director in his place at the meeting at which he is removed, provided special notice of the intended appointment has been given under sub-section (2).

(6) A director so appointed shall hold office till the date up to which his predecessor would have held office if he had not been removed.

(7) If the vacancy is not filled under sub-section (5), it may be filled as a casual vacancy following the provisions of this Act:

The director who was removed from office shall not be re-appointed as a director by the Board of Directors.

(8) Nothing in this section shall be taken--

(a) as depriving a person removed under this section of any compensation or damages payable to him in respect of the termination of his appointment as director as per the terms of contract or terms of his appointment as director, or of any other appointment terminating with that as director; or

(b) as derogating from any power to remove a director under other provisions of this Act.

12.10 Duties of Directors: Sec. 166

- 1) Subject to the provisions of this Act, a director of a company shall act in accordance with the articles of the company.
- (2) A director of a company shall act in good faith to promote its objects for the benefit of its members as a whole and in the best interests of the company, its employees, the shareholders, the community, and the protection of the environment.
- (3) A company director shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.
- (4) A director of a company shall not be involved in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the company's interest.
- (5) A company director shall not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates. If such a director is found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company.
- (6) A company director shall not assign his office, and any assignment so made shall be void.
- (7) If a director of the company contravenes the provisions of this section, such director shall be punishable with a fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.



BSE LTD V. Sureshchandra

- Petitioner: BSE LTD
- Respondents: Mr. Sureshchandra V. Parekh and Ms. Nila S. Parekh
- The issue revolves around: Mr. Keki M. Mistry

Facts of the Case

In 2012, BSE filed a petition to get exempted from the publication, circulation, or reading out at the forthcoming Extraordinary General Meeting (EGM) or the next Annual General Meeting (AGM) for the financial year ending 31/03/2013 and 31/03/2014 (AGM), whichever is earlier, the Notice carrying a resolution proposed to be moved by respondents.

The said notice issued by respondents that acts as a special notice within the meaning of section 190 of the Act, to move at the extraordinary General Meeting (EOGM) or the next Annual General Meeting 2013/2014, resolution for removal of Mr. Keki M. Mistry, a shareholder director of petitioner company, under the provisions of section 284 of the Act.

Respondents Arguments for such notice

That petitioner company had not helped the respondents resolve their grievances with Housing Development Finance Corporation Limited (HDFC) in the last 18 years.

Respondents other Arguments against the petition

The petitioner had not come clean-handed, so BSE Ltd. had not furnished all required details and documents to the Company Law Board (CLB) related to the present case.

BSE Ltd Arguments

Respondents seek to abuse the process of law to secure needless publicity for defamatory matters, and those directions be passed permanently restraining the respondents from sending notices under Sec. 284 of the Act to the BSL Ltd., the petitioner company was raising the same issues.

BSE Ltd. stated that both respondents (Mr. Sureshchandra V. Parekh and Ms. Nila S. Parekh) jointly hold five equity shares of one each of the BSE Ltd. The equity shareholding of respondents represents 0.000005% of the petitioner company's total issued and paid up share capital.

It was pointed out that their shareholding is "insignificant holding" and is pertinently below the statutory and numerical requirements of section 188 of the Act for any shareholder to any resolution at General Meeting.

Moreover, all required documents have been annexed to the petition.

It was further pointed out that the respondents are habitual of regularly issuing baseless, defamatory, and unsubstantiated vexatious notices for inclusion of resolutions under section 284 of the Act and merely seek to abuse the process of law and seek to secure needless publicity for the defamatory matter.

Point of Discussion

Who would have won in this petition?

Solution:

Court Contentions

The petitioner has elaborately given all the necessary and relevant details of the previous litigation and the facts of the present case. The petitioner has pleaded with all the relevant facts. Thus, the court does not find any force in the submission advanced by the respondent that the petitioner has not come with a clean hand, and the respondent's arguments are liable to be dismissed on this ground.

A perusal of the provision of section 188 makes it abundantly clear that a member who intends to propose resolutions included for circulation to members must have not less than 1/20th of the total voting power of the requisition or must be not less than 100 members in number to exercise such a right. This provision is mandatory.

Thus, the court is inclined to accept the petitioner's contention that under holding only five shares, the respondent is not entitled to insist on the inclusion of his proposed resolution in the AGM or EGM to be held.

Further, the facts of the present case and documents revealed that the issue of notice for removal of a director is nothing but to secure needless publicity and defaming the petitioner company. It is an act of abuse of the process of law.

As indicated by the petitioner in the petition that the respondent in the past also issued several notices for removal of the Chairman and directors of Petitioner company under section 284 of the Act, thereby the respondent compelled the petitioner to approach this bench (court) seeking relief against the frivolous notices.

Thus, the court had no hesitation in holding the respondents were abusing the process of law, and their conduct was highly condemnable. Therefore the company needs not to entertain the impugned notice.

Judgement

The petitioner company was exempted from publication, circulation, or reading out at the forthcoming Annual General Meeting; respondents issued the said notice. Thus, BSE Ltd. had won the petition.

Summary

- The persons in charge of the management of the affairs of a company are termed as directors and collectively are known as the board of directors or the board.
- The maximum number of directors that a company can have is fifteen. A company may appoint more than fifteen directors after passing a special resolution.
- Each company shall have at least one woman director.
- Every company shall have at least one director who stays in India for a total period of not less than one hundred and eighty-two days during the financial year.
- Every listed public company shall have at least one-third of the total number of directors as independent directors.
- An independent director means a director other than a managing director, a whole time director, or a nominee director who does not have any material or pecuniary relationship with the company or its directors.
- An independent director shall hold office for a term up to five consecutive years on the Board of a company but shall be eligible for reappointment on the passing of a special resolution by the company and disclosure of such appointment in the Board's report.

- After the commencement of this Act, no person shall hold office as a director, including any alternate directorship, in more than twenty companies at the same time.
- No person shall be appointed as a company director unless he has been allotted the Director Identification Number under section 154 or any other number as may be prescribed under section 153.
- At every subsequent annual general meeting, one-third of such directors, for the time being, are liable to retire by rotation, or if their number is neither three nor a multiple of three, then the number nearest to one-third shall retire from office.
- The directors to retire by rotation at every annual general meeting shall be the longest in office since their last appointment.
- No company shall appoint or employ a managing director and a manager at the same time.
- A director may resign from his office by giving a notice in writing to the company, and the Board shall note the same on receipt of such notice.
- A company may, by ordinary resolution, remove a director, not being a director appointed by the Tribunal under section 242, before the expiry of the period of his office after giving him a reasonable opportunity of being heard.

Keywords

Board: All directors collectively are known as the board of directors or the board.

Director: The persons in charge of the management of the affairs of a company are called directors.

Independent Director: An independent director means a director other than a managing director, a whole-time director, or a nominee director who does not have any material or pecuniary relationship with the company or its directors.

Key Managerial Personnel: Key Managerial Personnel in a company are Chief Executive Officer (CEO) or the Managing Director, Chief Financial Officer (CFO), Manager, Company Secretary (CS); and Whole-time Director.

Whole-time Director: A whole-time director is a director rendering his services on a whole-time basis to the company.

Self Assessment

1. The minimum number of directors in the case of a private company should be:
 - A. one
 - B. two
 - C. three
 - D. four
2. A company should have at least ____ woman director in its board.
 - A. one
 - B. two
 - C. three
 - D. four
3. Every company shall have at least _____ director who stays in India for a total period of not less than _____ during the financial year.

-
- A. One, 180 days
B. Two, 180 days
C. One, 182 days
D. Two, 182 days
4. Every listed public company shall have at least _____ of the total number of directors as:
- A. one-third, independent directors
B. one-fourth, independent directors
C. one-fourth, whole-time directors
D. one-third, whole-time directors
5. The maximum number of public companies in which a person can be appointed as a director shall not exceed _____.
A. Five
B. Ten
C. Twelve
D. Fifteen
6. No person shall be appointed as a director of a company unless:
- A. he has provided a declaration that he is not disqualified from becoming a director under this Act
B. he has been allotted the Director Identification Number
C. he has given his consent to hold the office as director
D. all of above
7. At the annual general meeting at which a director retires as aforesaid, the company may fill up the vacancy by appointing the:
- A. retiring director
B. some other person
C. retiring director or some other person
D. representative of management
8. An additional director shall hold office up to the date of:
- A. the next annual general meeting
B. the last date on which the annual general meeting should have been held
C. the next annual general meeting or the last date on which the annual general meeting should have been held
D. the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier
9. The Board of Directors of a company may, if so authorized by its articles or by a resolution passed by the company in general meeting, appoint a person to act as _____ for a director during his absence for not less than three months from India.
- A. Additional Director
B. Alternate Director

- C. Nominee Director
 - D. Appointment of directors in Casual Vacancy
10. No company shall appoint or continue the employment of any person as managing director, whole-time director, or manager who is below the age of _____ or has attained the age of _____.
- A. twenty-one years, seventy years
 - B. thirty-five years, sixty years
 - C. twenty-one years, sixty years
 - D. twenty-five years, sixty-seven years
11. The office of a director shall become vacant in case he absents himself from all the meetings of the Board of Directors held during _____ with or without seeking leave of absence of the Board.
- A. ten months
 - B. twelve months
 - C. fifteen months
 - D. one hundred eighty-two days
12. In case all the company directors vacate their offices under any of the disqualifications specified in section 167(1). Then the following person/s shall hold office till the directors are appointed by the company in the general meeting.
- A. the promoter
 - B. the required number of directors as appointed by the central government
 - C. the required number of directors as appointed by the state government
 - D. the promoter/s or in the absence of the promoters, the required number of directors as appointed by the central government
13. The director who has resigned shall be liable even after his resignation for the offences which:
- A. were occurred during his tenure
 - B. were occurred after his resignation
 - C. were occurred before and after his resignation
 - D. were occurred at any time
14. An independent director who is re-appointed for the second term under sub-section (10) of section 149 shall be removed by the company only by:
- A. Passing a special resolution
 - B. After giving him a reasonable opportunity of being heard
 - C. Passing a special resolution and After giving him a reasonable opportunity of being heard
 - D. Passing a special resolution or After giving him a reasonable opportunity of being heard
15. If a director of the company contravenes the provisions of Sec. 166, then such director shall be punishable with a fine of not less than one lakh rupees but which may extend to_____.
- A. two lakh rupees
 - B. three lakh rupees
 - C. five lakh rupees

D. seven lakh rupees

Answers for Self Assessment

1. B	2. A	3. C	4. A	5. B
6. D	7. C	8. D	9. B	10. A
11. B	12. D	13. A	14. C	15. C

Review Questions

1. What is the limit decided by the Companies Act, 2013 for the number of directorships a person can hold? What is the maximum and the minimum number of directors a company is required to have, discuss the related sections in detail?
2. Who are independent directors? Briefly discuss the provisions related to an independent director as laid down in the Companies Act, 2013.
3. Briefly discuss the procedure of appointment of directors.
4. Explain the duties of a director.
5. How a director can be removed from his position and under which circumstances?
6. Who is disqualified to act as a director under the Companies Act, 2013?
7. Explain the circumstances in which the office of the directors stands vacant. Discuss in detail.
8. Explain the provisions related to retirement by rotation of directors in brief.



Further Reading

- Bhandari, C. C. (2021). *A Handbook on Corporate and Other Laws* (25 ed.). Bestword Publications Pvt. Ltd.
- Gogna, P. P. S. *A Textbook of Company Law*. S. Chand Publishing.
- Gupta, P. *Legal aspects of Business: Concept and Applications*. Vikas Publishing House Pvt. Ltd.
- Kapoor, N. (2020). *Elements of Mercantile Law* (38 ed.). Sultan Chand & Sons



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Unit 13: Company Meetings

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Objectives

After studying this unit, you will be able to:

- explain the various essentials of a valid meeting.
- review the provisions related to multiple requirements of a valid meeting.
- explain the different kinds of meetings.
- explain the provisions relating to Annual General Meeting.
- explain the provisions relating to Extraordinary General Meeting.
- review the importance of holding general meetings in a company.
- comment on the need on fulfilling the various essentials of a valid meeting.

Introduction

A company is an artificial person and, therefore, cannot act itself. It must act through some human intermediary. The various provisions of law empower shareholders to do certain things. They are specifically reserved for them to be done in the company's general meetings. Section 291 authorizes the Board of directors to manage the affairs of the company. In this context, meetings of shareholders and directors become necessary. The Act has made provisions for the following different types of meetings of shareholders: (i) Annual General Meeting; (ii) Extraordinary General Meeting; and (iii) Class Meetings. The Act has also made provisions for the following different types of meetings of Directors, Debenture-holders and Creditors: (i) Board Meetings; (ii) Meetings of Debenture-holders and (iii) Meetings of Creditors.

A Company Meeting is defined as "A Gathering of two or more persons to transact the lawful business of the company." Ordinarily, a single-member present cannot form a quorum, as a single member cannot constitute a meeting. It is because meeting *prima facie* means coming together of two or more than two persons. The Companies Act also uses the expression "members," which shows that more than one member is expected to be present. In the current unit, the essentials of a valid meeting such as notice, Quorum, resolution, proxy, voting and polling, minutes of the meeting, etc., and legal provisions related to various kinds of meetings have been discussed briefly.

13.1 Essentials of a Valid Meeting

- Proper Authority
- Proper Notice: Sec. 101
- Statement to be annexed to notice: Sec. 102

- Quorum: Sec. 103
- Chairman of the Meeting: Sec. 104
- Proxies: Sec. 105
- Voting rights: Sec. 106
- Circular of resolution: Sec. 111
- Representation of President and Governors in meetings: Sec. 112
- Ordinary and Special resolution: Sec. 114
- Minutes of proceedings of Meeting

Proper Authority

The meeting though any should be convened by the proper authority. The proper authority hereby means which is allowed to call such meetings as per the Companies Act, 2013.

Proper Notice: Sec. 101

(1) A general meeting of a company may be called by giving not less than clear twenty-one days' notice either in writing or through electronic mode in such manner as may be prescribed:

A general meeting may be called after giving shorter notice than that specified in this sub-section if consent, in writing or by electronic mode, is accorded to it--

(i) in the case of an annual general meeting, by not less than ninety-five percent of the members entitled to vote thereat; and

(ii) in the case of any other general meeting, by members of the company--

(a) holding, if the company has a share capital, the majority in the number of members entitled to vote and who represent not less than ninety-five percent of such part of the paid-up share capital of the company as gives a right to vote at the Meeting; or

(b) having, if the company has no share capital, not less than ninety-five percent of the total voting power exercisable at that Meeting;

Where any member of a company is entitled to vote only on some resolution or resolutions to be moved at a meeting and not on the others, those members shall be taken into account for this subsection in respect of the former resolution or resolutions and not in respect of the latter.

(2) Every notice of a meeting shall specify the place, date, day, and the hour of the Meeting and contain a statement of the business to be transacted at such Meeting.

(3) The notice of every meeting of the company shall be given to--

(a) every member of the company, legal representative of any deceased member or the assignee of an insolvent member;

(b) the auditor or auditors of the company; and

(c) every director of the company.

(4) Any accidental omission to give notice to, or the non-receipt of such notice by, any member or other person who is entitled to such notice for any meeting shall not invalidate the proceedings of the meeting.

Statement to be annexed to notice: Sec. 102

(1) A statement setting out the following material facts concerning each item of special business to be transacted at a general meeting shall be annexed to the notice calling such meeting, namely:--

(a) the nature of concern or interest, financial or otherwise, if any, in respect of each items of--

(i) every director and the manager, if any;

(ii) every other key managerial personnel; and

(iii) relatives of the persons mentioned in sub-clauses (i) and (ii);

(b) any other information and facts that may enable members to understand the meaning, scope, and implications of the business items and make a decision thereon.

(2) For subsection (1),--

(a) in the case of an annual general meeting, all business to be transacted thereat shall be deemed special, other than--

- (i) the consideration of financial statements and the reports of the Board of Directors and auditors;
- (ii) the declaration of any dividend;
- (iii) the appointment of directors in place of those retiring;
- (iv) the appointment of, and the fixing of the remuneration of, the auditors; and
- (b) in the case of any other meeting, all business shall be deemed to be special:

Where any item of special business to be transacted at a meeting of the company relates to or affects any other company:

the extent of shareholding interest in that other company of every promoter, director, manager, and other key managerial personnel of the first-mentioned company, if any, shall, if the extent of such shareholding is not less than two percent of the paid-up share capital of that company, also be set out in the statement.

(3) Where any item of business refers to any document to be considered at the meeting, the time and place where such document can be inspected shall be specified in the statement under sub-section (1).

(4) Whereas a result of the non-disclosure or insufficient disclosure in any statement referred to in sub-section (1), being made by a promoter, director, manager, or other key managerial personnel, if any:

- any benefit which accrues to such promoter, director, manager or other key managerial personnel or their relatives, either directly or indirectly, the promoter, director, manager or other key managerial personnel, as the case may be, shall hold such benefit in trust for the company, and shall, without prejudice to any other action being taken against him under this Act or any other law for the time being in force, be liable to compensate the company to the extent of the benefit received by him.

(5) Without prejudice to the provisions of sub-section (4), if any default is made in complying with the provisions of this section. Then, every promoter, director, manager, or other key managerial personnel of the company who is in default shall be liable to:

- a penalty of fifty thousand rupees or five times the amount of benefit accruing to the promoter, director, manager, other key managerial personnel, or any of his relatives, whichever is higher.



Did you know? What is the Agenda of a meeting?

The word 'agenda' indicates the business to be transacted at a meeting. It is prepared for all kinds of meetings so that the meeting may be conducted systematically. The secretary generally prepares the Agenda in consultation with the chairman. It is drafted in such a manner as to help the chairman to conduct the meeting smoothly. In drafting the Agenda, the secretary should bear in mind the following: (i) the Agenda should be clear and explicit; (ii) it should be drafted in a summary manner; (iii) all items of routine business should be put down first, and the contentious matters later; and (iv) all items of similar nature should be placed in a continuous order. An Agenda of the meeting also acts as an essential of a valid meeting.

Quorum: Sec. 103

(1) Unless the articles of the company provide for a larger number,--

(a) in case of a public company,--

(i) five members personally present if the number of members as on the date of the meeting is not more than one thousand;

(ii) fifteen members personally present if the number of members as on the date of the meeting is more than one thousand but up to five thousand;

(iii) thirty members personally present if the number of members as on the date of the meeting exceeds five thousand;

(b) in the case of a private company, two members personally present shall be the Quorum for a company meeting.

(2) If the Quorum is not present within half-an-hour from the time appointed for holding a meeting of the company--

(a) the meeting shall stand adjourned to the same day in the next week at the same time and place, or to such other date and such other time and place as the Board may determine; or

(b) the meeting, if called by requisitionists under section 100, shall stand canceled:

In case of an adjourned meeting or of a change of day, time, or place of meeting under clause (a), the company shall give not less than three days notice to the members either individually or by publishing an advertisement in the newspapers (one in English and one in vernacular language) which is in circulation at the place where the registered office of the company is situated.

(3) If at the adjourned meeting also, a quorum is not present within half an hour from the time appointed for holding the meeting, the members present shall be the Quorum.

Chairman of the Meeting: Sec. 104

(1) Unless the company's articles otherwise provide, the members personally present at the meeting shall elect one of themselves to be the Chairman thereof on a show of hands.

(2) If a poll is demanded on the election of the Chairman, it shall be taken immediately following the provisions of this Act. The Chairman elected on a show of hands under sub-section (1) shall continue to be the Chairman of the meeting until another person is elected as Chairman due to the poll. Such other person shall be the Chairman for the rest of the meeting.

Proxies: Sec. 105

(1) Any member of a company entitled to attend and vote at a meeting of the company shall be entitled to appoint another person as a proxy to attend and vote at the meeting on his behalf:

- A proxy shall not have the right to speak at such meeting and shall not be entitled to vote except on a poll:
- Unless the articles of a company otherwise provide, this subsection shall not apply in the case of a company not having a share capital:
- The Central Government may prescribe a class or classes of companies whose members shall not be entitled to appoint another person as a proxy:
- A person appointed as proxy shall act on behalf of such member or number of members not exceeding fifty and such number of shares as may be prescribed.

(2) In every notice calling a meeting of a company which has a share capital, or the articles of which provide for voting by proxy at the meeting, there shall appear with reasonable prominence a statement that a member entitled to attend and vote is entitled to appoint a proxy, or, where that is allowed, one or more proxies, to attend and vote instead of himself, and that a proxy need not be a member.

(3) If the default is made in complying with sub-section (2), every officer of the company in default shall be liable to a penalty of five thousand rupees.

(4) Any provision contained in the articles of a company which specifies or requires a more extended period than forty-eight hours before a meeting of the company, for depositing with the company or any other person any instrument appointing a proxy or any other document necessary to show the validity or otherwise relating to the appointment of a proxy so that the appointment may be effective at such meeting, shall have effect as if a period of forty-eight hours had been specified in or required by such provision for such deposit.

(5) If for any meeting of a company, invitations to appoint as proxy a person or one of a number of persons specified in the invitations are issued at the company's expense to any member entitled to have a notice of the meeting sent to him and to vote thereat by proxy, every officer of the company who issues the invitation as aforesaid or authorizes or permits their issue, shall be liable to a penalty of fifty thousand rupees:

An officer shall not be liable under this subsection by reason only of the issue to a member at his request in writing of a form of appointment naming the proxy or of a list of persons willing to act as

proxies if the form or list is available on request in writing to every member entitled to vote at the meeting by proxy.

(6) The instrument appointing a proxy shall--

(a) be in writing; and

(b) be signed by the appointer or his attorney duly authorized in writing or, if the appointer is a body corporate, be under its seal or be signed by an officer or an attorney duly authorized by it.

(7) An instrument appointing a proxy, if in the form as may be prescribed, shall not be questioned on the ground that it fails to comply with any special requirements specified for such instrument by the articles of a company.

(8) Every member entitled to vote at a meeting of the company, or on any resolution to be moved thereat, shall be allowed during the period beginning twenty-four hours before the time fixed for the commencement of the meeting and ending with the conclusion of the meeting, to inspect the proxies lodged, at any time during the business hours of the company, provided not less than three days' notice in writing of the intention so to inspect is given to the company.

Voting rights: Restrictions of Voting rights- Sec.106

(1) Notwithstanding anything contained in this Act, the articles of a company may provide that no member shall exercise any voting right in respect of any shares registered in his name on which any calls or other sums presently payable by him have not been paid, or regarding which the company has exercised any right of lien.

(2) A company shall not, except on the grounds specified in sub-section (1), prohibit any member from exercising his voting right on any other ground.

(3) On a poll taken at a meeting of a company, a member entitled to more than one vote, or his proxy, where allowed, or other person entitled to vote for him, as the case may be, need not, if he votes, use all his votes or cast, in the same way, all the votes he uses.

Voting by show of hands: Sec. 107

(1) At any general meeting, a resolution put to the vote of the meeting shall, unless a poll is demanded under section 109 or the voting is carried out electronically, be decided on a show of hands.

(2) A declaration by the Chairman of the meeting of the passing of a resolution or otherwise by show of hands under sub-section (1) and an entry to that effect in the books containing the minutes of the meeting of the company shall be conclusive evidence of the fact of passing of such resolution or otherwise.

Voting through electronic means: Sec. 108

The Central Government may prescribe the class or classes of companies and manner in which a member may exercise his right to vote by electronic means.

Postal ballot: Sec. 110

(1) Notwithstanding anything contained in this Act, a company

(a) shall, in respect of such items of business as the Central Government may, by notification, declare to be transacted only through postal ballot; and

(b) may, in respect of any item of business, other than ordinary business and any business in relation of which directors or auditors have a right to be heard at any meeting, transact by means of postal ballot, in such manner as may be prescribed, instead of transacting such business at a general meeting;

Any item of business required to be transacted by means of the postal ballot under clause (a) may be transacted at a general meeting by a company that is necessary to provide the facility to members to vote by electronic means under section 108, in the manner provided in that section.

(2) If a resolution is assented to by the requisite majority of the shareholders through postal ballot, it shall be deemed to have been duly passed at a general meeting convened on that behalf.

Circular of resolution: Sec. 111

(1) A company shall, on the requisition in writing of such number of members, as required in section 100--,

- (a) give notice to members of any resolution which may properly be moved and is intended to be moved at a meeting; and
- (b) circulate to members any statement concerning the matters referred to in the proposed resolution or business to be dealt with at that meeting.
- (2) A company shall not be bound under this section to give notice of any resolution or to circulate any statement unless--
- (a) a copy of the requisition signed by the requisitionists (or two or more copies which, between them, contain the signatures of all the requisitionists) is deposited at the registered office of the company,
- (i) in the case of a requisition requiring notice of a resolution, not less than six weeks before the meeting;
- (ii) in the case of any other requisition, not less than two weeks before the meeting; and
- (b) there is deposited or tendered with the requisition, a sum reasonably sufficient to meet the company's expenses in giving effect to it:
- If, after a copy of a requisition requiring notice of a resolution has been deposited at the registered office of the company, an annual general meeting is called on a date within six weeks after the copy has been deposited, the copy, although not deposited within the time required by this subsection, shall be deemed to have been properly deposited for the purposes thereof.
- (3) The company shall not be bound to circulate any statement as required by clause (b) of subsection (1), if on the application either of the company or of any other person who claims to be aggrieved, the Central Government, by order, declares that the rights conferred by this section are being abused to secure needless publicity for the defamatory matter.
- (4) An order made under sub-section (3) may also direct that the cost incurred by the company under this section shall be paid to the company by the requisitionists, notwithstanding that they are not parties to the application.
- (5) If any default is made in complying with the provisions of this section, the company and every officer of the company who is in default shall be liable to a penalty of twenty-five thousand rupees.

Representation of President and Governors in meetings: Sec. 112

- (1) The President of India or the Governor of a State, if he is a member of a company, may appoint such person as he thinks fit to act as his representative at any meeting of the company or at any meeting of any class of members of the company.
- (2) A person appointed to act under subsection (1) shall, for this Act, be deemed to be a member of such a company and shall be entitled to exercise the same rights and powers, including the right to vote by proxy and postal ballot, as the President or, as the case may be, the Governor could exercise as a member of the company.

Ordinary and special resolution: Sec. 114

- (1) A resolution shall be an ordinary resolution if the notice required under this Act has been duly given. It is required to be passed by the votes cast, whether on a show of hands, or electronically or on a poll, as the case may be, in favour of the resolution, including the casting vote, if any, of the Chairman, by members who, being entitled so to do, vote in person, or where proxies are allowed, by proxy or by postal ballot, exceed the votes, if any, cast against the resolution by members, so entitled and voting.
- (2) A resolution shall be a special resolution when--
- (a) the intention to propose the resolution as a special resolution has been duly specified in the notice calling the general meeting or other intimation given to the members of the resolution;
- (b) the notice required under this Act has been duly given; and
- (c) the votes cast in favour of the resolution, whether on a show of hands or electronically or on a poll, as the case may be, by members who, being entitled so to do, vote in person or by proxy or by postal ballot, are required to be not less than three times the number of the votes, if any, cast against the resolution by members so entitled and voting.

Resolutions requiring special notice: Sec. 115

Where, by any provision contained in this Act or in the articles of a company, special notice is required of any resolution, a notice of the intention to move such resolution shall be given to the company by such number of members holding not less than one percent of the total voting power or holding shares on which such aggregate sum not exceeding five lakh rupees, as may be prescribed, has been paid-up and the company shall give its members notice of the resolution in such manner as may be prescribed.

Resolutions passed at the adjourned meeting: Sec. 116

Where a resolution is passed at an adjourned meeting of--

- (a) a company; or
- (b) the holders of any class of shares in a company; or
- (c) the Board of Directors of a company,

the resolution shall, for all purposes, be treated as having been passed on the date on which it was in fact passed, and shall not be deemed to have been passed on any earlier date.

Minutes of proceedings of Meeting: Sec. 119

The provisions related to Minutes of proceedings of general meeting, meeting of Board of Directors and other meeting and resolutions passed by postal ballot are as follows:

- (1) Every company shall cause minutes of the proceedings of every general meeting of any class of shareholders or creditors, and every resolution passed by postal ballot and every meeting of its Board of Directors or of every committee of the Board, to be prepared and signed in such manner as may be prescribed and kept within thirty days of the conclusion of every such meeting concerned, or passing of a resolution by postal ballot in books kept for that purpose with their pages consecutively numbered.
- (2) The minutes of each meeting shall contain a fair and correct summary of the proceedings thereat.
- (3) All appointments made at any of the meetings aforesaid shall be included in the minutes of the meeting.
- (4) In the case of a meeting of the Board of Directors or of a committee of the Board, the minutes shall also contain--
 - (a) the names of the directors present at the meeting; and
 - (b) in the case of each resolution passed at the meeting, the names of the directors, if any, dissenting from or not concurring with the resolution.
- (5) There shall not be included in the minutes, any matter which, in the opinion of the Chairman of the meeting,--
 - (a) is or could reasonably be regarded as defamatory of any person; or
 - (b) is irrelevant or immaterial to the proceedings; or
 - (c) is detrimental to the interests of the company.
- (6) The Chairman shall exercise absolute discretion concerning the inclusion or non-inclusion of any matter in the minutes on the grounds specified in sub-section (5).
- (7) The minutes kept following the provisions of this section shall be evidence of the proceedings recorded therein.
- (8) Where the minutes have been kept following subsection (1), then, until the contrary is proved, the meeting shall be deemed to have been duly called and held. All proceedings thereat to have duly taken place, and the resolutions passed by postal ballot to have been duly passed. In particular, all appointments of directors, key managerial personnel, auditors, or company secretary in practice shall be valid.
- (9) No document purporting to be a report of the proceedings of any general meeting of a company shall be circulated or advertised at the company's expense unless it includes the matters required by this section to be contained in the minutes of the proceedings of such meeting.

(10) Every company shall observe secretarial standards concerning general and Board meetings specified by the Institute of Company Secretaries of India constituted under section 3 of the Company Secretaries Act, 1980 (56 of 1980), and approved as such by the Central Government.

(11) If any default is made in complying with the provisions of this section in respect of any meeting, the company shall be liable to a penalty of twenty-five thousand rupees, and every officer of the company who is in default shall be liable to a penalty of five thousand rupees.

(12) If a person is found guilty of tampering with the minutes of the proceedings of the meeting, he shall be punishable with imprisonment for a term which may extend to two years and with a fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

Inspection of minute-books of general meeting: Sec. 119

(1) The books containing the minutes of the proceedings of any general meeting of a company or of a resolution passed by postal ballot shall--

(a) be kept at the registered office of the company; and
(b) be open, during business hours, to the inspection by any member without charge, subject to such reasonable restrictions as the company may, by its articles or in general meeting, impose, so, however, that not less than two hours in each business day are allowed for inspection.

(2) Any member shall be entitled to be furnished, within seven working days after he has requested in that behalf to the company, and on payment of such fees as may be prescribed, with a copy of any minutes referred to in sub-section (1).

(3) If any inspection under sub-section (1) is refused, or if any copy required under sub-section (2) is not furnished within the time specified therein, the company shall be liable to a penalty of twenty-five thousand rupees and every officer of the company who is in default shall be liable to a penalty of five thousand rupees for each such refusal or default, as the case may be.

(4) In the case of any such refusal or default, the Tribunal may, without prejudice to any action being taken under sub-section (3), by order, direct an immediate inspection of the minute-books or direct that the copy required shall forthwith be sent to the person requiring it.

Maintenance and inspection of documents in electronic form: Sec. 120

Without prejudice to any other provisions of this Act, any document, record, register, minutes, etc.,-

(a) required to be kept by a company; or
(b) allowed to be inspected or copies to be given to any person by a company under this Act, may be kept or inspected or copies given, as the case may be, in electronic form in such form and manner as may be prescribed.

13.2 Kinds of Meetings

1. Meetings of the Shareholders

- General Meetings
 - ✓ Annual General Meeting (AGM)
 - ✓ Extraordinary General Meeting (EGM or EOGM)
- Class Meetings

2. Meetings of the Directors

3. Meetings of the Debenture holders

4. Meetings of the Creditors

Annual General Meeting: Sec. 96(1)

(1) Every company other than a One Person Company shall in each year hold, in addition to any other meetings, a general meeting as its annual general meeting and shall specify the meeting as such in the notices calling it. Not more than fifteen months shall elapse between the date of one annual general meeting of a company and that of the next:

In case of the first annual general meeting, it shall be held within nine months from the date of closing of the first financial year of the company and in any other case, within six months, from the date of closing of the financial year:

Suppose a company holds its first annual general meeting as aforesaid. In that case, it shall not be necessary for the company to hold an annual general meeting in the year of its incorporation:

For any particular reason, the Registrar may extend the time within which any annual general meeting, other than the first annual general meeting, shall be held by a period not exceeding three months.

(2) Every annual general meeting shall be called during business hours, that is, between 9 a.m. and 6 p.m. on any day that is not a National Holiday and shall be held either at the registered office of the company or at some other place within the city, town or village in which the registered office of the company is situated:

An annual general meeting of an unlisted company may be held at any place in India if consent is given in writing or by electronic mode by all the members in advance:

The Central Government may exempt any company from the provisions of this sub-section subject to such conditions as it may impose.



Notes

For this sub-section, National Holiday means and includes a day declared as National Holiday by the Central Government.



Caution

An extension of three months is not available for holding First AGM.

Power of Tribunal to call an annual general meeting: Sec. 97

(1) If any default is made in holding the annual general meeting of a company under section 96, the Tribunal may, notwithstanding anything contained in this Act or the articles of the company, on the application of any member of the company, call, or direct the calling of, an annual general meeting of the company and give such ancillary or consequential directions as the Tribunal thinks expedient:

Provided that such directions may include a direction that one member of the company present in person or by proxy shall be deemed to constitute a meeting.

(2) A general meeting held in pursuance of sub-section (1) shall, subject to any directions of the Tribunal, be deemed to be an annual general meeting of the company under this Act.

Punishment for default in complying with provisions of sections 96 to 98: Sec. 99

If any default is made in holding a meeting of the company in accordance with section 96 or section 97 or section 98 or in complying with any directions of the Tribunal, then

- the company and every officer of the company who is in default shall be punishable with a fine which may extend to one lakh rupees and in the case of continuing default, with a further fine which may extend to five thousand rupees for every day during which such default continues.

Extraordinary General Meeting: Sec. 100(1)

(1) EGM by Board

The Board may, whenever it deems fit, call an extraordinary general meeting of the company.

An extraordinary general meeting of the company, other than the wholly owned subsidiary of a company incorporated outside India, shall be held in India.

(2) EGM by board on requisition

The Board shall, at the requisition made by,--

(a) in the case of a company having a share capital, such number of members who hold, on the date of the receipt of the requisition, not less than one-tenth of such of the paid-up share capital of the company as on that date carries the right of voting;

(b) in the case of a company not having a share capital, such number of members who have, on the date of receipt of the requisition, not less than one-tenth of the total voting power of all the members having on the said date a right to vote, call an extraordinary general meeting of the company within the period specified in sub-section (4).

(3) Content of requisition

The requisition made under sub-section (2) shall set out the matters for the consideration of which the meeting is to be called and shall be signed by the requisitionists and sent to the company's registered office.

(4) EGM by requisitionists

If the Board does not, within twenty-one days from the date of receipt of a valid requisition concerning any matter, proceed to call a meeting for the consideration of that matter on a day not later than forty-five days from the date of receipt of such requisition, the meeting may be called and held by the requisitionists themselves within three months from the date of the requisition.

(5) A meeting under sub-section (4) by the requisitionists shall be called and held in the same manner in which the meeting is called and held by the Board.

(6) Any reasonable expenses incurred by the requisitionists in calling a meeting under sub-section (4) shall be reimbursed to the requisitionists by the company, and the sums so paid shall be deducted from any fee or other remuneration under section 197 payable to such of the directors who were in default in calling the meeting.

Power of Tribunal to call meetings of members, etc.: Sec. 98

EGM by Tribunal

(1) If for any reason it is impracticable to call a meeting of a company, other than an annual general meeting, in any manner in which meetings of the company may be called, or to hold or conduct the meeting of the company in the manner prescribed by this Act or the articles of the company, the Tribunal may, either suo motu or on the application of any director or member of the company who would be entitled to vote at the meeting,--

(a) order a meeting of the company to be called, held and conducted in such manner as the Tribunal thinks fit; and

(b) give such ancillary or consequential directions as the Tribunal thinks expedient, including directions modifying or supplementing concerning the calling, holding and conducting of the meeting, the operation of the provisions of this Act or articles of the company:

Provided that such directions may include a direction that one member of the company present in person or by proxy shall be deemed to constitute a meeting.

(2) Any meeting called, held, and conducted in accordance with any order made under sub-section (1) shall, for all purposes, be deemed to be a meeting of the company duly called, held, and conducted.

Class Meetings

Such meeting is convened by a particular class of shareholders only and only if they think that their rights are being altered or if they want to vary their attached rights, as mentioned u/s 48 of the Companies Act, 2013, and u/s 232 also, if under Mergers and Amalgamation scheme, meetings of particular shareholders and creditors can be convened if their rights/privileges are being varied to their interests in such company.

At such meetings, these members discuss the pros and cons of the proposal and vote accordingly. Class meetings are held to pass a resolution that will bind only the members of the class concerned, and only members of that class can attend and vote.

Unless the articles of the company or a contract binding on the persons concerned otherwise provide, all provisions about calling a general meeting and its conduct apply to class meetings in like manner as they apply concerning general meetings of the company.

**Task**

A company served a notice of a general meeting to its members. The notice stated that a resolution to increase the company's share capital would be considered at such meeting. A shareholder complains that the amount of the proposed increase was not specified in the notice. Is the notice valid?

Other Meetings

- (a) Meetings of Directors
- (b) Meeting of Debenture holders
- (c) Meeting of Creditors

Meetings of Directors

Board of Directors Meeting: As per Sec. 173 of the Companies Act 2013, every company needs to convene the first board meeting within 30 days of its incorporation, and then a minimum of four meetings in each calendar year, with a time gap of not more than 120 days (at present it is 180 days because of COVID-19) between two board meetings.

Meeting of Debenture holders

A company issuing debentures may provide for the holding of meetings of the debenture holders. At such meetings, matters about the variation in terms of security or alteration of their rights are generally discussed. All of the issues connected with the holding, conduct, and proceedings of the meetings of the debenture holders are normally specified in the Debenture Trust Deed. The decisions at the meeting made by the prescribed majority are valid, lawful, and binding upon the minority.

Meeting of Creditors

Sometimes, a company, either as a running concern or in the event of winding up, has to make certain arrangements with its creditors. Meetings of creditors may be called for this purpose.

For Example, a company may enter into arrangements with creditors with the sanction of the Court for reconstruction or any arrangement with its creditors under section 230.

Summary

- A Company Meeting is defined as "A Gathering of two or more persons to transact the lawful business of the company."
- Ordinarily, a single member cannot constitute a meeting.
- A company's general meeting may be called by giving not less than a clear twenty-one days' notice either in writing or through electronic mode.
- Every notice of a meeting shall specify the place, date, day, and the hour of the Meeting and contain a statement of the business to be transacted at such Meeting.
- A statement setting out the specific material facts concerning each item of special business to be transacted at a general meeting shall be annexed to the notice calling such meeting.
- If the Quorum is not present within half-an-hour from the time appointed for holding a meeting of the company--
 - ✓ the meeting shall stand adjourned to the same day in the next week at the same time and place, or to such other date and such other time and place as the Board may determine; or
 - ✓ the meeting, if called by requisitionists under section 100, shall stand canceled.
- Unless the company's articles otherwise provide, the members personally present at the meeting shall elect one of themselves to be the Chairman thereof on a show of hands.
- Any member of a company entitled to attend and vote at a company meeting shall be entitled to appoint another person as a proxy to attend and vote at the meeting on his behalf.

- The articles of a company may provide that no member shall exercise any voting right in respect of any shares registered in his name on which any calls or other sums presently payable by him have not been paid or regarding which the company has exercised any right of lien.
- Every company shall cause minutes of the proceedings of every general meeting of any class of shareholders or creditors, and every resolution passed by postal ballot and every meeting of its Board of Directors or of every committee of the Board, to be prepared and signed in such manner as may be prescribed and kept within thirty days of the conclusion of every such meeting concerned, or passing of a resolution by postal ballot in books kept for that purpose with their pages consecutively numbered.
- The minute book must be open, during business hours, to the inspection by any member without charge, subject to such reasonable restrictions as the company may, by its articles or in general meeting, impose, for not less than two hours in each business day.
- Every company other than a One Person Company shall in each year hold, in addition to any other meetings, a general meeting as its annual general meeting and shall specify the meeting as such in the notices calling it. Not more than fifteen months shall elapse between the date of one annual general meeting of a company and that of the next.
- Extraordinary General Meeting may be called by Board itself or on requisition, requisitionists, and Tribunal.
- A company may conduct class meetings, board meetings, meetings of debenture-holders and creditors from time to time for smooth conduct of its operations.

Keywords

Agenda: It indicates the business to be transacted at a meeting. It is prepared for all kinds of meetings so that the meeting may be conducted systematically

Annual General Meeting: An annual general meeting (AGM) is a yearly gathering of a company's interested shareholders. At an AGM, the company's directors present a yearly report containing information for shareholders about the company's performance and strategy.

Extraordinary General Meeting: An extraordinary general meeting (EGM) is a shareholder meeting other than a company's scheduled annual general meeting (AGM). An EGM is also called a special general meeting or emergency general meeting.

Meeting: A gathering of two or more persons to transact the lawful business of the company.

Minutes: Meeting minutes are notes that are recorded during a meeting. They highlight the key issues discussed, motions proposed or voted on, and activities to be undertaken.

Notice: A notice of meeting is a written document that informs a board of directors and other company members that a shareholders meeting, or corporate action, will take place.

Proxy: A proxy is an agent legally authorized to act on behalf of another party. The proxy may also allow an investor to vote without being physically present at the annual shareholder's meeting.

Postal Ballot: It means voting by post or through any electronic mode. It is a system of voting in which people send their votes by post when they cannot be present.

Quorum: A 'Quorum' in simple words means the minimum number of members to be present in a meeting.

Tribunal: It means the National Company Law Tribunal constituted under section 408.

Voting right: It means the right of a member of a company to vote in any meeting of the company or through postal ballot

Self-Assessment

1. A general meeting of a company may be called by giving not less than clear _____.

A. Fifteen days

-
- B. Eighteen days
 - C. Twenty days
 - D. Twenty-one days
2. Every notice of a meeting shall specify the:
- A. place, and date of the Meeting
 - B. day and the hour of the Meeting
 - C. business to be transacted at such Meeting
 - D. all of above
3. Any accidental omission to give notice to any member entitled to such notice for any meeting shall invalidate the meeting proceedings.
- A. True
 - B. False
4. The declaration of any dividend in an annual general meeting is deemed as:
- A. Ordinary business
 - B. Special business
 - C. Normal business
 - D. Extraordinary business
5. In the case of a public company with 3460 members as of the meeting date, how many members should form a quorum for a valid meeting?
- A. Two
 - B. Five
 - C. Fifteen
 - D. Thirty
6. If the quorum is absent within _____ from the time appointed for holding a company meeting, the Meeting shall stand adjourned to the same day in the next week at the same time and place.
- A. 30 minutes
 - B. 45 minutes
 - C. 60 minutes
 - D. 90 minutes
7. Any member of a company entitled to attend and vote at a meeting of the company shall be entitled to appoint his/her _____ to attend and vote at the Meeting on his /her behalf.
- A. Proxy
 - B. Quorum
 - C. Director
 - D. Chairman
8. Which of the following matter should not be included in the minutes?

- A. Any matter that is or could reasonably be regarded as defamatory of any person
 - B. Any matter that is relevant to the proceedings
 - C. Any issue that is material to the proceedings
 - D. Any issue that is in favour of the company's interests
9. The books containing the minutes of the proceedings of any general meeting of a company shall-
- A. Not be kept at the registered office of the company
 - B. Not be open, during business hours, to the inspection by any member without charge
 - C. be allowed for inspection for not less than two hours in each business day
 - D. all of above
10. The notice of every Meeting of the company shall be given to:
- A. every member of the company, legal representative of any deceased member or the assignee of an insolvent member
 - B. the auditor or auditors of the company
 - C. every director of the company
 - D. all of above
11. The First Annual General Meeting shall be held within a period of _____ from the date of closing of the first financial year of the company.
- A. six months
 - B. nine months
 - C. ten months
 - D. twelve months
12. Registrar can extend the time limits for holding First AGM if requested by the promoters.
- A. True
 - B. False
13. Subsequent AGMs must be held within a period of _____, from the date of closing of the financial year.
- A. six months
 - B. nine months
 - C. ten months
 - D. twelve months
14. EGM can be called by:
- A. Board
 - B. Board on Requisition
 - C. Requisitionists
 - D. all of above
15. _____ is convened by a particular class of shareholders only and only if they think that their rights are being altered.

- A. Annual General Meeting
- B. Extraordinary General Meeting
- C. Class Meeting
- D. Directors Meeting

Answer for Self Assessment

1. D	2. D	3. B	4. A	5. C
6. A	7. A	8. A	9. C	10. D
11. B	12. B	13. A	14. D	15. C

Review Questions

1. Discuss the requisites of a valid meeting in brief.
2. What are the different kinds of general meetings of a company?
3. Explain the key provisions related to Annual General Meeting.
4. Who can call Extraordinary General Meeting, and in which situations? Explain in detail.
5. Explain the information to be annexed with notice of a meeting.
6. Explain the provisions related to notice of a meeting.
7. Discuss the Statement to be annexed to notice in detail.
8. State the provisions related to the Quorum of a meeting.
9. What do you mean by Proxy? Explain the provisions related to the same.
10. What is meant by postal ballot? State the related provisions in brief.
11. Discuss ordinary and special resolutions.
12. What are the minutes of the meeting? Explain the provisions related to the same.
13. Can anyone inspect minutebooks of various meetings? Justify.



Further Reading

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Web Links

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Unit 14: Company Winding Up

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- 14.21 Liquidation Process
- 14.22 Voluntary liquidation of corporate persons: Sec. 59

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Reading

Objectives

After studying this unit, you will be able to:

- illustrate the meaning of winding up a company.
- explain the circumstances for winding up a company.
- explain the persons entitled to file a petition for winding up a company.
- review the powers and role of the Tribunal in winding up a company under the Companies Act, 2013.

- assess Company Liquidator's powers, duties, and function in winding up a company under the Companies Act, 2013.
- explain the liquidation of a company under the Insolvency and Bankruptcy Code, 2016.
- review the Corporate Insolvency Resolution Process under IBC, 2016.
- review the provisions related to Voluntary Liquidation of a corporate Person under IBC, 2016.
- comment on the legal provisions involved in the winding-up of a company under the Companies Act, 2013.
- comment on the legal provisions related to Corporate Insolvency Resolution Process and Voluntary Liquidation under the IBC, 2016.

Introduction

Winding up or liquidation of a company represents the last stage in its life. It means a proceeding by which a company is dissolved. The company's assets are disposed of, the debts are paid off out of the realized assets (or from contributions from its members), and the surplus is then distributed among the members in proportion to their holdings in the company. The two terms "Winding up" and "Liquidation" are used interchangeably.

According to Prof. Gower, the winding-up of a company is a process whereby its life is ended, and its property is administered to benefit its creditors and members. An administrator, called a liquidator, is appointed. He takes control of the company, collects its assets, pays its debts, and finally distributes any surplus among the members according to their rights.

The term insolvency is used for both individuals and organizations. For individuals, it is known as bankruptcy, and for corporate it is called corporate insolvency. Both refer to a situation when an individual or company cannot pay the debt in the present or near future, and the value of assets held by them is less than liabilities.

While insolvency is a situation that arises due to the inability to pay off the debts due to insufficient assets, bankruptcy is a situation wherein application is made to an authority declaring insolvency and seeking to be declared as bankrupt, which will continue until discharge.

Thus, it is evident that insolvency is a state and bankruptcy is a conclusion. A bankrupt would be a conclusive insolvent, whereas all insolvencies will not lead to bankruptcies. Typically, insolvency situations have two options – resolution and recovery or liquidation. In this unit, the legal provisions related to winding up a company under the Companies Act, 2013 and laws about Insolvency in India under Insolvency and Bankruptcy Code, 2016 are briefly discussed.



Difference between Insolvency and Bankruptcy

- Insolvency refers to a situation, whereas bankruptcy refers to a legal state.
- If you are insolvent, you are simply not in the position to pay off your debts.
- Whereas, if you are declared bankrupt, you have to pay off your debts by either selling off your assets or restructuring payment processes with governments' help.

14.1 Winding up: Meaning and Modes under the Companies Act, 2013

Winding up: Sec. 2(94A)

"Winding up" means winding up under this Act or liquidation under the Insolvency and Bankruptcy Code, 2016 (31 of 2016), as applicable.

Winding up proceedings are governed by the Companies Act, 2013 and Insolvency and Bankruptcy Code, 2016.

Winding Up: Modes – Sec. 270

Winding up by Tribunal

Under the Companies Act, 2013, the winding up of the companies can be done by the Tribunal. Thus, Part I's provisions shall apply to the winding up of a company by the Tribunal under this Act.

14.2 Grounds or Circumstances for winding up of a company by Tribunal: Sec. 271

A company may, on a petition under section 272, be wound up by the Tribunal, --

- (a) if the company has, by special resolution, resolved that the Tribunal will wind the company up;
- (b) if the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality;
- (c) if on an application made by the Registrar or any other person authorized by the Central Government by notification under this Act, the Tribunal believes that:
 - the affairs of the company have been conducted in a fraudulent manner or
 - the company was formed for a fraudulent and unlawful purpose or
 - the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and
 - that it is proper that the company be wound up;
- (d) if the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or
- (e) if the Tribunal believes that it is just and equitable that the company should be wound up.

14.3 Petition for winding up: Sec. 272

(1) Subject to the provisions of this section, a petition to the Tribunal for the winding up of a company shall be presented by--

- (a) the company;
- (b) any contributory or contributories;
- (c) all or any of the persons specified in clauses (a) and (b);
- (d) the Registrar;
- (e) any person authorized by the Central Government in that behalf; or
- (f) in a case falling under clause (b) of section 271, by the Central Government or a State Government.

(2) Right to present a petition by Contributory: Sec. 272(2)

A contributory shall be entitled to present a petition for the winding-up of a company, notwithstanding that

- he may be the holder of fully paid-up shares, or
- that the company may have no assets at all or
- may have no surplus assets left for distribution among the shareholders after the satisfaction of its liabilities, and
- shares in respect of which he is a contributory or some of them were either allotted initially to him or have been held by him, and registered in his name, for at least six months during the eighteen months immediately before the commencement of the winding-up or have devolved on him through the death of a former holder.

(3) The Registrar shall be entitled to present a petition for winding up under section 271, except on the grounds specified in clause (a) of that section:

Registrar can present the petition if:

- the Registrar shall obtain the previous sanction of the Central Government to the presentation of a petition:
- the Central Government shall not accord its sanction unless the company has been given a reasonable opportunity of making representations.

(4) A petition presented by the company for winding up before the Tribunal shall be admitted only if accompanied by a statement of affairs in such form and such manner as may be prescribed.

(5) A copy of the petition made under this section shall also be filed with the Registrar, and the Registrar shall, without prejudice to any other provisions, submit his views to the Tribunal within sixty days of receipt of such petition.

14.4 Powers of Tribunal: Sec. 273

(1) The Tribunal may, on receipt of a petition for winding up under section 272, pass any of the following orders, namely: --

- (a) dismiss it, with or without costs;
- (b) make any interim order as it thinks fit;
- (c) appoint a provisional liquidator of the company till the making of a winding-up order;
- (d) make an order for the winding-up of the company with or without costs; or
- (e) any other order as it thinks fit:



Notes

- An order under this subsection shall be made within **ninety days** from the date of presentation of the petition:
- Before appointing a provisional liquidator under clause (c), the Tribunal shall give notice to the company and afford a reasonable opportunity to it to make its representations, if any, unless, for special reasons to be recorded in writing, the Tribunal thinks fit to dispense with such notice:
- The Tribunal shall not refuse to make a winding-up order on the ground only that the company's assets have been mortgaged for an amount equal to or above those assets or that the company has no assets.

(2) Where a petition is presented on the ground that it is just and equitable that the company should be wound up, the Tribunal may refuse to make an order of winding up, if it is of the opinion that some other remedy is available to the petitioners and that they are acting unreasonably in seeking to have the company wound up instead of pursuing the other remedy.

14.5 Directions for filing statement of affairs: Sec. 274

(1) Where a petition for winding up is filed before the Tribunal by any person other than the company, the Tribunal shall, if satisfied that a prima facie case for winding up of the company is made out, by an order direct the company to file its objections along with a statement of its affairs within thirty days of the order in such form and in such manner as may be prescribed:



Notes

- The Tribunal may allow a further period of thirty days in a situation of contingency or special circumstances:
- The Tribunal may direct the petitioner to deposit such security for costs as it may consider reasonable as a precondition to issue directions to the company.

(2) A company, which fails to file the statement of affairs as referred to in sub-section (1), shall forfeit the right to oppose the petition and such directors and officers of the company as found responsible for such non-compliance shall be liable for punishment under sub-section (4).

(3) The directors and other officers of the company, in respect of which the Tribunal passes an order for winding up under clause (d) of sub-section (1) of section 273, shall, within thirty days of such order, submit, at the cost of the company, the books of account of the company completed and audited up to the date of the order, to such liquidator and in the manner specified by the Tribunal.

(4) If any director or officer of the company contravenes the provisions of this section, the director or the officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.

(5) The complaint may be filed in this behalf before the Special Court by Registrar, provisional liquidator, Company Liquidator or any person authorized by the Tribunal.

14.6 Company Liquidators and their appointments: Sec. 275

(1) To wind up a company by the Tribunal, the Tribunal, at the time of the passing of the order of winding up, shall appoint an Official Liquidator or a liquidator from the panel maintained under sub-section (2) as the Company Liquidator.

(2) The provisional liquidator or the Company Liquidator, as the case may, shall be appointed by the Tribunal from amongst the insolvency professionals registered under the Insolvency and Bankruptcy Code, 2016 (31 of 2016);

(3) Where the Tribunal appoints a provisional liquidator, the Tribunal may limit and restrict his powers by the order appointing him or it or by a subsequent order, but otherwise, he shall have the same powers as a liquidator.

(5) The terms and conditions of appointment of a provisional liquidator or Company Liquidator and the fee payable to him or it shall be specified by the Tribunal based on the task required to be performed, experience, qualification of such liquidator and size of the company.

(6) On appointment as provisional liquidator or Company Liquidator, as the case may be, such liquidator shall file a declaration within seven days from the date of appointment in the prescribed form. In the form, he should disclose conflict of interest or lack of independence regarding his appointment, if any, with the Tribunal. Such obligation shall continue throughout the term of his appointment.

(7) While passing a winding-up order, the Tribunal may appoint a provisional liquidator, if any, appointed under clause (c) of sub-section (1) of section 273, as the Company Liquidator for the conduct of the proceedings for the winding up of the company.



Caution

Subsection 4 has been omitted w.e.f 15-11-2016.

14.7 Removal and replacement of liquidator: Sec. 276

(1) The Tribunal may, on a reasonable cause being shown and for reasons to be recorded in writing, remove the provisional liquidator or the Company Liquidator, as the case may be, as liquidator of the company on any of the following grounds, namely: --

(a) misconduct;

(b) fraud or misfeasance;

(c) professional incompetence or failure to exercise due care and diligence in the performance of the powers and functions;

(d) inability to act as provisional liquidator or, as the case may be, Company Liquidator;

(e) conflict of interest or lack of independence during the term of his appointment that would justify removal.

(2) In the event of death, resignation or removal of the provisional liquidator or, as the case may be, Company Liquidator, the Tribunal may transfer the work assigned to him or it to another Company Liquidator for reasons to be recorded in writing.

(3) Where the Tribunal is of the opinion that any liquidator is responsible for causing any loss or damage to the company due to fraud or misfeasance or failure to exercise due care and diligence in the performance of his or its powers and functions, the Tribunal may recover or cause to be recovered such loss or damage from the liquidator and pass such other orders as it may think fit.

(4) The Tribunal shall, before passing any order under this section, provide a reasonable opportunity of being heard to the provisional liquidator or, as the case may be, Company Liquidator.

14.8 Intimation to Company Liquidator, provisional liquidator and Registrar: Sec. 277

(1) Where the Tribunal makes an order for appointment of a provisional liquidator or the winding up of a company, it shall, within a period not exceeding seven days from the date of passing of the order, cause intimation thereof to be sent to the Company Liquidator or provisional liquidator, as the case may be, and the Registrar.

(2) On receipt of the copy of the order of appointment of a provisional liquidator or winding-up order, the Registrar shall make an endorsement to that effect in his records relating to the company and notify in the Official Gazette that such an order has been made. In the case of a listed company, the Registrar shall intimate about such appointment or order, as the case may be, to the stock exchange or exchanges where the company's securities are listed.

(3) The winding-up order shall be deemed to be a notice of discharge to the company's officers, employees, and workmen, except when the company's business is continued.

(4) Within three weeks from the date of passing of winding up order, the Company Liquidator shall make an application to the Tribunal for constitution of a winding-up committee to assist and monitor the progress of liquidation proceedings by the Company Liquidator in carrying out the function as provided in sub-section (5), and such winding-up committee shall comprise of the following persons, namely:--

(i) Official Liquidator attached to the Tribunal;

(ii) nominee of secured creditors; and

(iii) a professional nominated by the Tribunal.

(5) The Company Liquidator shall be the convener of the meetings of the winding-up committee, which shall assist and monitor the liquidation proceedings in following areas of liquidation functions, namely: --

(i) taking over assets;

(ii) examination of the statement of affairs;

(iii) recovery of property, cash or any other assets of the company including benefits derived therefrom;

(iv) review of audit reports and accounts of the company;

(v) sale of assets;

(vi) finalization of the list of creditors and contributories;

(vii) compromise, abandonment and settlement of claims;

(viii) payment of dividends, if any; and

(ix) any other function, as the Tribunal may direct from time to time.

(6) The Company Liquidator shall place before the Tribunal a report along with minutes of the committee meetings monthly duly signed by the members present in the meeting for consideration until the final report for dissolution of the company is submitted before the Tribunal.

(7) The Company Liquidator shall prepare the draft final report to consider and approve the winding-up committee.

(8) The final report so approved by the winding-up committee shall be submitted by the Company Liquidator before the Tribunal to pass a dissolution order in respect of the company.

14.9 Effect of winding up order: Sec. 278

The order for the winding up of a company shall operate in favour of all the creditors and all contributories of the company as if it had been made out on the joint petition of creditors and contributories.

14.10 Submission of report by Company Liquidator: Sec. 281

(1) Where the Tribunal has made a winding-up order or appointed a Company Liquidator, such liquidator shall, within sixty days from the order, submit to the Tribunal, a report containing the following particulars, namely: --

(a) the nature and details of the assets of the company, including their location and value, stating the cash balance separately in hand and at the bank, if any, and the negotiable securities, if any, held by the company;

Provided that the valuation of the assets shall be obtained from registered valuers for this purpose;

(b) amount of capital issued, subscribed and paid-up;

(c) the existing and contingent liabilities of the company including names, addresses and occupations of its creditors, stating the amount of secured and unsecured debts separately, and in the case of secured debts, particulars of the securities given, whether by the company or an officer thereof, their value and the dates on which they were given;

(d) the debts due to the company and the names, addresses and occupations of the persons from whom they are due and the amount likely to be realized on account thereof;

(e) guarantees, if any, extended by the company;

(f) list of contributories and dues, if any, payable by them and details of any unpaid call;

(g) details of trademarks and intellectual properties, if any, owned by the company;

(h) details of subsisting contracts, joint ventures and collaborations, if any;

(i) details of holding and subsidiary companies, if any;

(j) details of legal cases filed by or against the company; and

(k) any other information which the Tribunal may direct or the Company Liquidator may consider necessary to include.

(2) The Company Liquidator shall include in his report how the company was promoted or formed and whether in his opinion any fraud has been committed by any person in its promotion or formation or by any officer of the company in relation to the company since the formation thereof and any other matters which, in his opinion, it is desirable to bring to the notice of the Tribunal.

(3) The Company Liquidator shall also report on the viability of the company's business or the steps which, in his opinion, are necessary for maximizing the value of the company's assets.

(4) The Company Liquidator may also, if he thinks fit, make any further report or reports.

(5) Any person describing himself in writing to be a creditor or a contributory of the company shall be entitled by himself or by his agent at all reasonable times to inspect the report submitted following this section and take copies thereof or extracts therefrom on payment of the prescribed fees.

14.11 Directions of Tribunal on the report of Company Liquidator: Sec. 282

(1) The Tribunal shall, on consideration of the report of the Company Liquidator, fix a time limit within which the entire proceedings shall be completed, and the company be dissolved:

Provided that the Tribunal may, if it is of the opinion, at any stage of the proceedings, or on examination of the reports submitted to it by the Company Liquidator and after hearing the Company Liquidator, creditors or contributories or any other interested person, that it will not be advantageous or economical to continue the proceedings, revise the time limit within which the entire proceedings shall be completed, and the company be dissolved.

(2) The Tribunal may, on examination of the reports submitted to it by the Company Liquidator and after hearing the Company Liquidator, creditors or contributories or any other interested person, order sale of the company as a going concern or its assets or part thereof:

Provided that the Tribunal may, where it considers fit, appoint a sale committee comprising such creditors, promoters and officers of the company as the Tribunal may decide to assist the Company Liquidator in a sale under this subsection.

(3) Where a report is received from the Company Liquidator or the Central Government or any person that a fraud has been committed in respect of the company, the Tribunal shall, without prejudice to the process of winding up, order for investigation under section 210.

Considering the report of such investigation, it may pass order and give directions under sections 339 to 342 or direct the Company Liquidator to file a criminal complaint against persons involved in the commission of fraud.

(4) The Tribunal may order to take such steps and measures, as may be necessary, to protect, preserve, or enhance the value of the company's assets.

(5) The Tribunal may pass such other order or give such other directions as it considers fit.

14.12 Custody of company's properties: Sec. 283

(1) Where a winding-up order has been made or where a provisional liquidator has been appointed, the Company Liquidator or the provisional liquidator, as the case may be, shall, on the order of the Tribunal, forthwith take into his or its custody or control:

- all the property, effects and actionable claims to which the company is or appears to be entitled to and
- take such steps and measures, as may be necessary, to protect and preserve the company's properties.

(2) Notwithstanding anything contained in sub-section (1), all the property and effects of the company shall be deemed to be in the custody of the Tribunal from the date of the order for the winding up of the company.

(3) On an application by the Company Liquidator or otherwise, the Tribunal may, at any time after the making of a winding-up order, require any contributory for the time being on the list of contributories, and any trustee, receiver, banker, agent, officer or other employees of the company, to pay, deliver, surrender or transfer forthwith, or within such time as the Tribunal directs, to the Company Liquidator, any money, property or books and papers in his custody or under his control to which the company is or appears to be entitled.

14.13 Promoters, directors, etc., to cooperate with Company Liquidator: Sec. 284

(1) The promoters, directors, officers and employees, who are or have been in the company's employment or acting or associated with the company shall extend full cooperation to the Company Liquidator in the discharge of his functions and duties.

(2) If any person required to assist or cooperate with the Company Liquidator under sub-section (1) does not help or cooperate, the Company Liquidator may make an application to the Tribunal for necessary directions.

(3) On receiving an application under sub-section (2), the Tribunal shall, by an order, direct the person required to assist or cooperate with the Company Liquidator to comply with the instructions of the Company Liquidator and to cooperate with him in discharging his functions and duties.

14.14 Settlement of list of contributories and application of assets: Sec. 285

(1) As soon as may be after the passing of a winding-up order by the Tribunal, the Tribunal shall settle a list of contributories, cause rectification of register of members in all cases where rectification is required in pursuance of this Act and shall cause the assets of the company to be applied for the discharge of its liability:

Provided that where it appears to the Tribunal that it would not be necessary to make calls on or adjust the rights of contributories, the Tribunal may dispense with the settlement of a list of contributories.

(2) In settling the list of contributories, the Tribunal shall distinguish between those who are contributories in their own right and those who are contributories as being representatives of, or liable for the debts of, others.

(3) While settling the list of contributories, the Tribunal shall include every person, who is or has been a member, who shall be liable to contribute to the assets of the company an amount sufficient for payment of the debts and liabilities and the costs, charges and expenses of winding up, and for the adjustment of the rights of the contributories among themselves, subject to the following conditions, namely: --

(a) a person who has been a member shall not be liable to contribute if he has ceased to be a member for the preceding one year or more before the commencement of the winding-up;

(b) a person who has been a member shall not be liable to contribute in respect of any debt or liability of the company contracted after he ceased to be a member;

(c) no person who has been a member shall be liable to contribute unless it appears to the Tribunal that the present members are unable to satisfy the contributions required to be made by them in pursuance of this Act;

(d) in the case of a company limited by shares, no contribution shall be required from any person, who is or has been a member exceeding the amount, if any, unpaid on the shares in respect of which he is liable as such member;

(e) in the case of a company limited by guarantee, no contribution shall be required from any person, who is or has been a member exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up but if the company has a share capital, such member shall be liable to contribute to the extent of any sum unpaid on any shares held by him as if the company were a company limited by shares.

14.15 Powers and duties of Company Liquidator: Sec. 290

(1) Subject to directions by the Tribunal, if any, in this regard, the Company Liquidator, in a winding up of a company by the Tribunal, shall have the power--

(a) to carry on the business of the company so far as may be necessary for the beneficial winding up of the company;

(b) to do all acts and to execute, in the name and on behalf of the company, all deeds, receipts and other documents, and for that purpose, to use, when necessary, the company's seal;

(c) to sell the immovable and movable property and actionable claims of the company by public auction or private contract, with power to transfer such property to any person or body corporate, or to sell the same in parcels;

(d) to sell the whole of the undertaking of the company as a going concern;

(e) to raise any money required on the security of the assets of the company;

(f) to institute or defend any suit, prosecution or other legal proceedings, civil or criminal, in the name and on behalf of the company;

(g) to invite and settle the claim of creditors, employees or any other claimant and distribute sale proceeds in accordance with priorities established under this Act;

(h) to inspect the records and returns of the company on the files of the Registrar or any other authority;

(i) to prove rank and claim in the insolvency of any contributory for any balance against his estate, and to receive dividends in the insolvency, in respect of that balance, as a separate debt due from the insolvent, and rate ably with the other separate creditors;

(j) to draw, accept, make and endorse any negotiable instruments including cheque, bill of exchange, hundi or promissory note in the name and on behalf of the company, with the same effect concerning the liability of the company as if such instruments had been drawn, accepted, made or endorsed by or on behalf of the company in the course of its business;

(k) to take out, in his official name, letters of administration to any deceased contributory, and to do in his official name any other act necessary for obtaining payment of any money due from a contributory or his estate which cannot be conveniently done in the name of the company, and in all such cases, the money due shall, to enable the Company Liquidator to take out the letters of administration or recover the money, be deemed to be due to the Company Liquidator himself;

(l) to obtain any professional assistance from any person or appoint any professional, in the discharge of his duties, obligations and responsibilities and for protection of the assets of the company, appoint an agent to do any business which the Company Liquidator is unable to do himself;

(m) to take all such actions, steps, or to sign, execute and verify any paper, deed, document, application, petition, affidavit, bond or instrument as may be necessary, --

(i) for winding up of the company;

(ii) for distribution of assets;

(iii) in the discharge of his duties and obligations and functions as Company Liquidator; and

(n) to apply to the Tribunal for such orders or directions as may be necessary for the winding up of the company.

(2) The exercise of powers by the Company Liquidator under sub-section (1) shall be subject to the overall control of the Tribunal.

(3) Notwithstanding the provisions of sub-section (1), the Company Liquidator shall perform such other duties as the Tribunal may specify in this behalf.

14.16 Payment of debts by contributory and extent of set-off: Sec. 295

(1) The Tribunal may, at any time after passing of a winding-up order, give an order requiring any contributory for the time being on the list of contributories to pay, in the manner directed by the order, any money due to the company, from him or from the estate of the person whom he represents, exclusive of any money payable by him or the estate by virtue of any call in pursuance of this Act.

(2) The Tribunal, in making an order, under sub-section (1), may, --

(a) in the case of an unlimited company, allow to the contributory, by way of set-off, any money due to him or to the estate which he represents, from the company, on any independent dealing or contract with the company, but not any money due to him as a member of the company in respect of any dividend or profit; and

(b) in the case of a limited company, allow any director or manager whose liability is unlimited, or to his estate, such set-off.

(3) In the case of any company, whether limited or unlimited, when all the creditors have been paid in full, any money due on any account whatever to a contributory from the company may be allowed to him by way of set-off against any subsequent call.

14.17 Dissolution of company by Tribunal: Sec. 302

(1) When the affairs of a company have been completely wound up, the Company Liquidator shall make an application to the Tribunal for dissolution of such company.

(2) The Tribunal shall on an application filed by the Company Liquidator under sub-section (1) or when the Tribunal believes that it is just and reasonable in the circumstances of the case that an order for the dissolution of the company should be made, make an order that the company be dissolved from the date of the order, and the company shall be dissolved accordingly.

(3) The Tribunal shall, within thirty days from the date of the order, --

(a) forward a copy of the order to the Registrar who shall record in the register relating to the company a minute of the dissolution of the company; and

(b) direct the Company Liquidator to forward a copy of the order to the Registrar, who shall record in the register relating to the company a minute of the dissolution of the company.

14.18 Insolvency and Bankruptcy Code, 2016: Introduction

1) This Code may be called the Insolvency and Bankruptcy Code, 2016.

(2) It extends to the whole of India.

(3) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint:

Provided that different dates may be appointed for various provisions of this Code and any reference in any such provision to the commencement of this Code shall be construed as a reference to the beginning of that provision.



Notes

As per Sec. 4, This Part shall apply to matters relating to the insolvency and liquidation of corporate debtors where the minimum amount of the default is **one crore rupees**.

Purpose of the Code

- a) To consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time-bound manner.
- b) To promote entrepreneurship and availability of credit and
- c) To improve the ease of doing business and facilitate more investments leading to higher economic development.

14.19 Liquidation of Company under the Insolvency and Bankruptcy Code, 2016

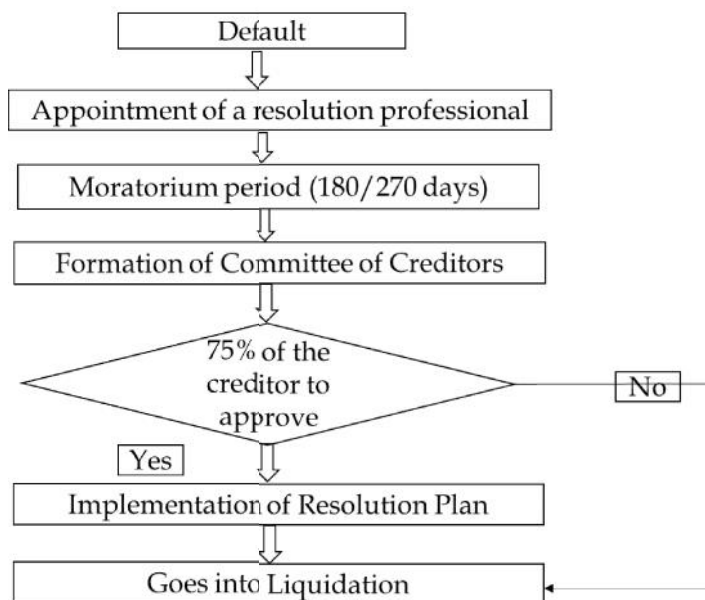
Insolvency situations have two options, i.e., resolution and recovery or liquidation. Under IBC, 2016, two recourses are available for a corporate with excess debts over its assets.

A. Corporate Insolvency Resolution Process

B. Voluntary Corporate Liquidation

Let's discuss them each in brief.

14.20 Corporate Insolvency Resolution Process: Sec. 6 to 22



Source: Kapoor, N. (2020). *Elements of Mercantile Law* (38 ed.). Sultan Chand & Sons.



Notes

1. Default: Creditors can apply for insolvency on default of debt or interest payment.
2. Appointment of resolution professional: An insolvency professional is to be appointed by the regulator. From the date of appointment of Insolvency Professional, the power of directors of the company will be suspended and vested with the Insolvency Professional.

3. Moratorium: It is a temporary stopping of activity, especially by official agreement.

The adjudicating authority shall by order declare a moratorium period during which a resolution plan will be prepared. This plan is also required to be approved by the creditor's committee.

The moratorium order shall affect from the date of such order until the corporate insolvency resolution process competition.

4: Credit Committee: A credit committee of creditors shall be constituted. If 75% of creditors approve the resolution plan, it shall be implemented. The committee recommended that the voting share be reduced from 75% to 66% in certain critical matters, such as approval of the resolution plan.

5: Liquidation: A liquidation process will be initiated if the credit committee does not approve the resolution plan within the specified time.

Persons who may initiate corporate insolvency resolution process: Sec. 6

Where any corporate debtor commits a default, a financial creditor, an operational creditor, or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor in the manner as provided under this Chapter.

Initiation of corporate insolvency resolution process by the financial creditor: Sec. 7

1. Filing Application:

A financial creditor, either by itself or jointly with other financial creditors, or any other person on behalf of the financial creditor, as may be notified by the Central Government, may apply for initiating corporate insolvency resolution process against a corporate debtor before the Adjudicating Authority when a default has occurred.

The financial creditor shall apply under sub-section (1) in such form and manner and accompanied with such fee as may be prescribed.

2. Information to be furnished with Application:

The financial creditor shall, along with the application, furnish:

- (a) record of the default recorded with the information utility or such other record or evidence of default as may be specified;
- (b) the name of the resolution professional proposed to act as an interim resolution professional; and
- (c) any other information as may be specified by the Board.

3. Determination of default by Adjudicating Authority (AA):

The Adjudicating Authority shall, within fourteen days of the receipt of the application under sub-section (2), ascertain the existence of a default from-

- a) The records of an information utility or
- b) Other evidence furnished by the financial creditor.

Provided that if the Adjudicating Authority has not ascertained the existence of default and passed an order under sub-section (5) within such time, it shall record its reasons in writing for the same.

4. Order of Adjudicating Authority: Where the Adjudicating Authority is satisfied that—

a) *When the Application is Complete: A default has occurred, and the application under sub-section (2) is complete, and no disciplinary proceedings is pending against the proposed resolution professional, it may, by order, admit such application; or*

b) *When the Application is Incomplete: default has not occurred, or the application under sub-section (2) is incomplete, or any disciplinary proceeding is pending against the proposed resolution professional, it may, by order, reject such application.*

The Adjudicating Authority shall, before rejecting the application under clause (b) of sub-section (5), give a notice to the applicant to rectify the defect in his application within seven days of receipt of such notice from the Adjudicating Authority.

5. Commencement of Corporate Insolvency Resolution Process (CIRP): The corporate insolvency resolution process shall commence from the date of admission of the application under sub-section (5) by the Adjudicating Authority.

6. Communication of order by Adjudicating Authority:

The Adjudicating Authority shall communicate within seven days of admission or rejection of such application, as the case may be.

(a) When Application is Complete: Communicate the order to the financial creditor and the corporate debtor;

(b) When Application is Incomplete: Communicate the order to the financial creditor.

Corporate Insolvency Resolution Process by the operational creditor: Sec. 8 to 9

1. **Demand Notice:** An operational creditor may, on the occurrence of a default, deliver a demand notice of unpaid operational debt copy of an invoice demanding payment of the amount involved in the default to the corporate debtor.



Did you know? **What is meant by a demand notice?**

A "demand notice" means a notice served by an operational creditor to the corporate debtor demanding payment of the operational debt regarding the default.

2. Receipt Demand Notice by Corporate Debtor: The corporate debtor shall, within ten days of the receipt of the demand notice or copy of the invoice, bring to the notice of the operational creditor.

(a) existence of a dispute, if any, or record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice concerning such dispute;

(b) the payment of unpaid operational debt.

(i) by sending an attested copy of the record of electronic transfer of the unpaid amount from the bank account of the corporate debtor; or

(ii) by sending an attested copy of a record, the operational creditor has cashed a cheque issued by the corporate debtor.

3. Filing an application before the Adjudicating Authority for initiating a CIRP by Operational Creditor:

After the expiry of the period of ten days from the date of delivery of the notice or invoice demanding payment under sub-section (1) of section 8, if the operational creditor does not receive payment from the corporate debtor or notice of the dispute under sub-section (2) of section 8, the operational creditor may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process.

The application under sub-section (1) shall be filed in such form and manner and accompanied with such fee as may be prescribed.

4. Information to be furnished with Application: The operational creditor shall, along with the application, provide--

(a) a copy of the invoice demanding payment or demand notice delivered by the operational creditor to the corporate debtor;

(b) an affidavit to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt;

(c) a copy of the certificate from the financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor; if available;

(d) a copy of any record with information utility confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available; and

(e) any other proof confirming that there is no payment of an unpaid operational debt by the corporate debtor or such other information, as may be prescribed.

5. Interim Resolution Professional: Under this section, an operational creditor initiating a corporate insolvency resolution process may propose a resolution professional to act as an interim resolution professional.

6. Order of Adjudicating Authority: The Adjudicating Authority shall, within fourteen days of the receipt of the application under sub-section (2), by an order

(i) Admit the application: Admit and communicate such decision to the operational creditor and the corporate debtor if, --

- (a) the application is complete;
- (b) no payment of the unpaid operational debt;
- (c) the operational creditor has delivered the invoice or notice for payment to the corporate debtor;
- (d) the operational creditor has received no notice of dispute, or there is no record of dispute in the information utility; and
- (e) no disciplinary proceeding is pending against any resolution professional.

ii) Reject the Application: reject the application and communicate such decision to the operational creditor and the corporate debtor, if--

- (a) the application is incomplete;
- (b) there has been payment of the unpaid operational debt;
- (c) the creditor has not delivered the invoice or notice for payment to the corporate debtor;
- (d) the operational creditor has received notice of dispute, or there is a record of dispute in the information utility; or
- (e) any disciplinary proceeding is pending against any proposed resolution professional.

The Adjudicating Authority, shall before rejecting an application under sub-clause (a) of clause (ii), give a notice to the applicant to rectify the defect in his application within seven days of the date of receipt of such notice from the Adjudicating Authority.

7. Commencement of CIRP: The corporate insolvency resolution process shall commence from the date of admission of the application by the Adjudicating Authority.

Corporate Insolvency Resolution Process by Corporate Applicant: Sec. 10

1. Default: Where a corporate debtor has committed a default, a corporate applicant thereof may apply for initiating corporate insolvency resolution process with the Adjudicating Authority.

2. Information to be furnished with Application: The corporate applicant shall, along with the application, provide the information relating to--

- (a) its books of account and such other documents relating to such period as may be specified; and
- (b) the resolution professional proposed to be appointed as an interim resolution professional.
- (c) the special resolution passed by shareholders of the corporate debtor or the resolution passed by at least three-fourth of the total number of partners of the corporate debtor, as the case may be, approving the filing of the application.

3. Order of Adjudicating Authority: The Adjudicating Authority shall, within fourteen days of the receipt of the application, by an order--

(a) When the Application is Complete: admit the application, if it is complete; and no disciplinary proceeding is pending against the proposed resolution professional; or

(b) When the Application is Incomplete: reject the application, if it is incomplete or any disciplinary proceeding is pending against the proposed resolution professional.

The Adjudicating Authority shall, before rejecting an application, give a notice to the applicant to rectify the defects in his application within seven days from the date of receipt of such notice from the Adjudicating Authority.

4. Commencement of CIRP: The corporate insolvency resolution process shall commence from the date of admission of the application by Adjudicating Authority.

Time-limit for completion of insolvency resolution process: Sec. 12

(1) Subject to subsection (2), the corporate insolvency resolution process shall be completed within a period of one hundred and eighty days from the date of admission of the application to initiate such process.

(2) The resolution professional shall apply to the Adjudicating Authority to extend the period of the corporate insolvency resolution process beyond one hundred and eighty days, if instructed to do so by a resolution passed at a meeting of the committee of creditors by a vote of sixty-six percent of the voting shares.

(3) On receipt of an application under sub-section (2), if the Adjudicating Authority is satisfied that the subject matter of the case is such that corporate insolvency resolution process cannot be completed within one hundred and eighty days, it may by order extend the duration of such process beyond one hundred and eighty days by such further period as it thinks fit, but not exceeding ninety days.

Declaration of the moratorium and public announcement: Sec. 13

(1) The Adjudicating Authority, after admission of the application under section 7 or section 9 or section 10, shall, by an order –

- (a) declare a moratorium for the purposes referred to in section 14;
- (b) cause a public announcement of the initiation of the corporate insolvency resolution process and call for the submission of claims under section 15; and
- (c) appoint an interim resolution professional in the manner as laid down in section 16.

(2) The public announcement referred to in clause (b) of sub-section (1) shall be made immediately after the appointment of the interim resolution professional.

Appointment and tenure of the interim resolution professional: Sec. 16

(1) The Adjudicating Authority shall appoint an interim resolution professional on the insolvency commencement date.

(2) Where the application for corporate insolvency resolution process is made by a financial creditor or the corporate debtor, as the case may be, the resolution professional, as proposed respectively in the application under section 7 or section 10, shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

(3) Where an operational creditor and--make the application for the corporate insolvency resolution process

(a) no proposal for an interim resolution professional is made, the Adjudicating Authority shall make a reference to the Board for the recommendation of an insolvency professional who may act as an interim resolution professional;

(b) a proposal for an interim resolution professional is made under sub-section (4) of section 9; the resolution professional, as proposed, shall be appointed as the interim resolution professional, if no disciplinary proceedings are pending against him.

(4) The Board shall, within ten days of the receipt of a reference from the Adjudicating Authority under sub-section (3), recommend the name of an insolvency professional to the Adjudicating Authority against whom no disciplinary proceedings are pending.

(5) The term of the interim resolution professional shall continue till the date of appointment of the resolution professional under section 22.

Committee of creditors: Sec. 21

(1) The interim resolution professional shall constitute a committee of creditors after collating all claims received against the corporate debtor and determining the financial position.

(2) The committee of creditors shall comprise all financial creditors of the corporate debtor.

Caution

You can refer to subsection 3-10 of section 21 for other provisions related to the committee of creditors.

Appointment of resolution professional: Sec. 22

- (1) The first meeting of the committee of creditors shall be held within seven days of the constitution of the committee of creditors.
- (2) The committee of creditors, may, in the first meeting, by a majority vote of not less than sixty-six percent of the voting share of the financial creditors, either resolve to appoint the interim resolution professional as a resolution professional or to replace the interim resolution professional by another resolution professional.
- (3) Where the committee of creditors resolves under sub-section (2) –
- (a) to continue the interim resolution professional as resolution professional, it shall communicate its decision to the interim resolution professional, subject to written consent from the interim resolution professional in the specified form] it shall communicate its decision to the interim resolution professional, the corporate debtor and the Adjudicating Authority; or
- (b) to replace the interim resolution professional, it shall file an application before the Adjudicating Authority for the appointment of the proposed resolution professional. (along with written consent from the proposed resolution professional in the specified form).
- (4) The Adjudicating Authority shall forward the name of the resolution professional proposed under clause (b) of sub-section (3) to the Board for its confirmation and shall make such appointment after confirmation by the Board.
- (5) Where the Board does not confirm the name of the proposed resolution professional within ten days of the receipt of the name of the proposed resolution professional, the Adjudicating Authority shall, by order, direct the interim resolution professional to continue to function as the resolution professional until the Board confirms the appointment of the proposed resolution professional.

Approval of resolution plan: Sec. 31

- (1) If the Adjudicating Authority is satisfied that the resolution plan as approved by the committee of creditors under sub-section (4) of section 30 meets the requirements as referred to in sub-section (2) of section 30,
- it shall by order approve the resolution plan which shall be binding on the corporate debtor and its employees, members, creditors, including the Central Government, any State Government or any local authority to whom a debt in respect of the payment of dues arising under any law for the time being in force, such as authorities to whom statutory dues are owed, guarantors and other stakeholders involved in the resolution plan.

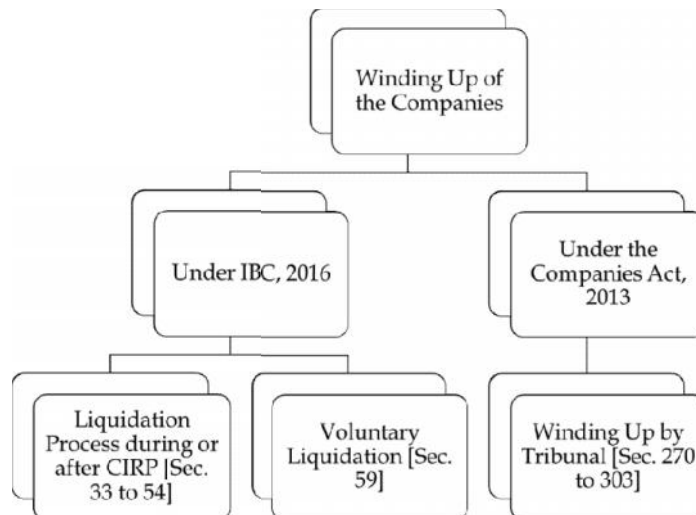
The Adjudicating Authority shall, before passing an order for approval of the resolution plan under this sub-section, satisfy that the resolution plan has provisions for its effective implementation.

- (2) Where the Adjudicating Authority is satisfied that the resolution plan does not confirm to the requirements referred to in sub-section (1), it may, by an order, reject the resolution plan. (3) After the order of approval under sub-section (1), --
- (a) the moratorium order passed by the Adjudicating Authority under section 14 shall cease to have effect; and
- (b) the resolution professional shall forward all records relating to the conduct of the corporate insolvency resolution process and the resolution plan to the Board to be recorded on its database.

2[(4) The resolution applicant shall, pursuant to the resolution plan approved under subsection (1), obtain the necessary approval required under any law for the time being in force within a period of one year from the date of approval of the resolution plan by the Adjudicating Authority under sub-section (1) or within such period as provided for in such law, whichever is later:

Provided that where the resolution plan contains a provision for combination, as referred to in section 5 of the Competition Act, 2002 (12 of 2003), the resolution applicant shall obtain the approval of the Competition Commission of India under that Act before the approval of such resolution plan by the committee of creditors.

14.21 Liquidation Process



Source: Kapoor, N. (2020). *Elements of Mercantile Law* (38 ed.). Sultan Chand & Sons.

The process of liquidation under IBC, 2016, has been briefly stated under the following points. Sec. 33-54 of the IBC, 2016 comprises the provisions relating to the corporate debtors.

Initiation of liquidation: Sec. 33

(1) Where the Adjudicating Authority, --

(a) before the expiry of the insolvency resolution process period or the maximum period permitted for completion of the corporate insolvency resolution process under section 12 or the fast track corporate insolvency resolution process under section 56, as the case may be, does not receive a resolution plan under sub-section (6) of section 30; or

(b) rejects the resolution plan under section 31 for the non-compliance of the requirements specified therein, it shall--

(i) pass an order requiring the corporate debtor to be liquidated in the manner as laid down in this Chapter;

(ii) issue a public announcement stating that the corporate debtor is in liquidation; and

(iii) require such order to be sent to the authority with which the corporate debtor is registered.

(2) Where the resolution professional, at any time during the corporate insolvency resolution process but before confirmation of resolution plan, intimates the Adjudicating Authority of the decision of the committee of creditors approved by not less than sixty-six percent of the voting share to liquidate the corporate debtor, the Adjudicating Authority shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

(3) Where the resolution plan approved by the Adjudicating Authority is contradicted by the concerned corporate debtor, any person other than the corporate debtor, whose interests are prejudicially affected by such contravention, may make an application to the Adjudicating Authority for a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

(4) On receipt of an application under sub-section (3), if the Adjudicating Authority determines that the corporate debtor has contravened the provisions of the resolution plan, it shall pass a liquidation order as referred to in sub-clauses (i), (ii) and (iii) of clause (b) of sub-section (1).

(5) Subject to section 52, when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor:

It is provided that a suit or other legal proceeding may be instituted by the liquidator, on behalf of the corporate debtor, with the prior approval of the Adjudicating Authority.

(6) The provisions of sub-section (5) shall not apply to legal proceedings concerning such transactions as may be notified by the Central Government in consultation with any financial sector regulator.

(7) The order for liquidation under this section shall be deemed to be a notice of discharge to the corporate debtor's officers, employees, and workmen, except when the corporate debtor's business is continued during the liquidation process by the liquidator.

Powers and duties of liquidator: Sec. 35

(1) Subject to the directions of the Adjudicating Authority, the liquidator shall have the following powers and duties, namely: –

- (a) to verify claims of all the creditors;
- (b) to take into his custody or control all the assets, property, effects, and actionable claims of the corporate debtor;
- (c) to evaluate the assets and property of the corporate debtor in the manner as may be specified by the Board and prepare a report;
- (d) to take such measures to protect and preserve the assets and properties of the corporate debtor as he considers necessary;
- (e) to carry on the business of the corporate debtor for its beneficial liquidation as he considers necessary;
- (f) subject to section 52, to sell the immovable and movable property and actionable claims of the corporate debtor in liquidation by public auction or private contract, with power to transfer such property to any person or body corporate, or to sell the same in parcels in such manner as may be specified;

Provided that the liquidator shall not sell the immovable and movable property or actionable claims of the corporate debtor in liquidation to any person who is not eligible to be a resolution applicant.

- (g) to draw, accept, make and endorse any negotiable instruments including bill of exchange, hundi, or promissory note in the name and on behalf of the corporate debtor, with the same effect concerning the liability as if such instruments were drawn, accepted, made, or endorsed by or on behalf of the corporate debtor in the ordinary course of its business;
- (h) to take out, in his official name, letter of administration to any deceased contributory and to do in his official name any other act necessary for obtaining payment of any money due and payable from a contributory or his estate which cannot be ordinarily done in the name of the corporate debtor, and in all such cases, the money due and payable shall, to enable the liquidator to take out the letter of administration or recover the money, be deemed to be due to the liquidator himself;
- (i) to obtain any professional assistance from any person or appoint any professional, in the discharge of his duties, obligations, and responsibilities;
- (j) to invite and settle claims of creditors and claimants and distribute proceeds following the provisions of this Code;
- (k) to institute or defend any suit, prosecution or other legal proceedings, civil or criminal, in the name of or on behalf of the corporate debtor;
- (l) to investigate the financial affairs of the corporate debtor to determine undervalued or preferential transactions;
- (m) to take all such actions, steps, or to sign, execute and verify any paper, deed, receipt document, application, petition, affidavit, bond, or instrument and for such purpose to use the common seal, if any, as may be necessary for liquidation, distribution of assets and in the discharge of his duties and obligations and functions as liquidator;
- (n) to apply to the Adjudicating Authority for such orders or directions as may be necessary for the liquidation of the corporate debtor and to report the progress of the liquidation process in a manner as may be specified by the Board; and
- (o) to perform such other functions as may be specified by the Board.

(2) The liquidator shall have the power to consult any of the stakeholders entitled to a distribution of proceeds under section 53:

Provided that any such consultation shall not be binding on the liquidator:

Provided further that the records of any such consultation shall be made available to all other stakeholders not so consulted, in a manner specified by the Board.

14.22 Voluntary liquidation of corporate persons: Sec. 59

(1) A corporate person who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings under the provisions of this Chapter. (2) The voluntary liquidation of a corporate person under sub-section (1) shall meet such conditions and procedural requirements as may be specified by the Board.

(3) Without prejudice to sub-section (2), voluntary liquidation proceedings of a corporate person registered as a company shall meet the following conditions, namely: –

(a) a declaration from the majority of the directors of the company verified by an affidavit stating that –

(i) they have made a full inquiry into the affairs of the company, and they have formed an opinion that either the company has no debt or that it will be able to pay its debts in full from the proceeds of assets to be sold in the voluntary liquidation; and

(ii) the company is not being liquidated to defraud any person;

(b) the declaration under sub-clause (a) shall be accompanied with the following documents, namely: –

(i) audited financial statements and record of business operations of the company for the previous two years or for the period since its incorporation, whichever is later;

(ii) a report of the valuation of the assets of the company, if any prepared by a registered valuer;

(c) within four weeks of a declaration under sub-clause (a), there shall be –

(i) a special resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily and appointing an insolvency professional to act as the liquidator; or

(ii) a resolution of the members of the company in a general meeting requiring the company to be liquidated voluntarily as a result of the expiry of the period of its duration, if any, fixed by its articles or on the occurrence of any event in respect of which the articles provide that the company shall be dissolved, as the case may be and appointing an insolvency professional to act as the liquidator:

Provided that the company owes any debt to any person, creditors representing two-thirds in value of the company's debt shall approve the resolution passed under sub-clause (c) within seven days of such resolution.

(4) The company shall notify the Registrar of Companies and the Board about the resolution under sub-section (3) to liquidate the company within seven days of such resolution or the subsequent approval by the creditors, as the case may be.

(5) Subject to the approval of the creditors under sub-section (3), the voluntary liquidation proceedings in respect of a company shall be deemed to have commenced from the date of passing of the resolution under sub-clause (c) of sub-section (3).

(6) The provisions of sections 35 to 53 of Chapter III and Chapter VII shall apply to voluntary liquidation proceedings for corporate persons with such modifications as may be necessary.

(7) Where the affairs of the corporate person have been completely wound up, and its assets completely liquidated, the liquidator shall make an application to the Adjudicating Authority for the dissolution of such corporate person.

(8) The Adjudicating Authority shall, on an application filed by the liquidator under sub-section (7), pass an order that the corporate debtor shall be dissolved from the date of that order and the corporate debtor shall be dissolved accordingly

(9) A copy of an order under sub-section (8) shall be forwarded to the authority with which the corporate person is registered within fourteen days from the date of such order.

Summary

- Under the Companies Act, 2013, the winding up of the companies can be done by the Tribunal.
- On a petition under section 272, a company may be wound up by the Tribunal if any of the circumstances mentioned in Sec. 271 is met.

- Subject to the provisions of this section, a petition to the Tribunal for the winding up of a company shall be presented by the company; any contributory or contributories; all or any of the persons specified in clauses (a) and (b) of Section 272; the Registrar; any person authorized by the Central Government in that behalf; or in a case falling under clause (b) of section 271, by the Central Government or a State Government.
- The Tribunal may, on receipt of a petition for winding up under section 272, pass any of the following orders, namely: --
 - (a) dismiss it, with or without costs;
 - (b) make any interim order as it thinks fit;
 - (c) appoint a provisional liquidator of the company till the making of a winding-up order;
 - (d) make an order for the winding-up of the company with or without costs; or
 - (e) any other order as it thinks fit.
- To wind up a company by the Tribunal, the Tribunal, at the time of the passing of the order of winding up, shall appoint an Official Liquidator or a liquidator from the panel maintained under sub-section (2) as the Company Liquidator under Sec. 275.
- On a reasonable cause being shown and for reasons to be recorded in writing, the Tribunal may remove the provisional liquidator or the Company Liquidator, as the case may be, as liquidator of the company on any of the grounds mentioned in Sec. 276.
- When the affairs of a company have been completely wound up, the Company Liquidator shall apply to the Tribunal for dissolution of such company under Sec. 302.
- Insolvency situations have two options, i.e., resolution and recovery or liquidation. Under IBC, 2016, two recourses are available for a corporate with excess debts over its assets.
 - A. Corporate Insolvency Resolution Process
 - B. Voluntary Corporate Liquidation

Keywords

Bankruptcy: It is a legal declaration of one's inability to pay off debts. When an individual cannot pay off his liabilities and debts, he generally files for bankruptcy. It can be of 2 types: Reorganization Bankruptcy and Liquidation Bankruptcy.

Financial Creditor: Financial creditor means any person to whom a financial debt is owed and includes a person to whom such debt has been legally assigned or transferred.

Insolvency: It is a situation where the liabilities of an individual or an organization exceeds its assets, and that entity is unable to raise enough cash to meet its obligations or debts as they become due for payment.

Liquidation: It is the process of winding up of the corporation.

Liquidation bankruptcy: Under liquidation bankruptcy, debtors sell certain assets to make money they can use to pay off their creditors.

Moratorium: It is a temporary stopping of activity, especially by official agreement.

Operational Creditor: It means any person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred.

Reorganization bankruptcy: Under reorganization bankruptcy, debtors restructure their repayment plans to make them more easily met.

Winding-up: It means a proceeding by which a company is dissolved.

Self Assessment

1. A company may, on a petition, be wound up by the Tribunal if:

-
- A. the company has resolved by special resolution that the Tribunal would wind the company up
B. the company has decided by ordinary resolution that the Tribunal would wind the company up
C. the company has acted in favour of the interests of the sovereignty of India
D. all of above
2. The Tribunal may order the winding up of a company if, on an application made by the Registrar, the Tribunal has the opinion that:
- A. the affairs of the company have been conducted in a fraudulent manner
B. the company was formed for an unlawful purpose
C. the persons concerned in the formation or management of its affairs have been guilty of misfeasance or misconduct in connection therewith
D. all of above
3. The Tribunal may order the winding up of a company if the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding _____ consecutive financial years.
- A. two
B. three
C. four
D. five
4. A petition to the Tribunal for the winding up of a company may be presented by-
- A. any contributory
B. the Registrar
C. any person authorized by the Central Government in that behalf
D. all of above
5. The Tribunal may, on receipt of a petition for winding up may pass any of the following orders, namely: --
- A. dismiss it, with or without costs
B. make any interim order as it thinks fit
C. appoint a provisional liquidator of the company till the making of a winding-up order
D. any of above
6. The Tribunal must pass an order concerning the petition of winding up the company within _____ days from the date of presentation of such petition.
- A. Thirty
B. Fifty
C. Sixty
D. Ninety
7. In case of professional incompetence of the provisional liquidator, the Tribunal may remove the provisional liquidator.
- A. True
B. False

8. The Company Liquidator shall have the following power/s in a winding up of a company by the Tribunal:
- A. Not to carry on the business of the company so far as may be necessary for the beneficial winding up of the company
 - B. to inspect the records and returns of the company on the files of the Registrar or any other authority
 - C. to buy the whole of the undertaking of the company as a going concern
 - D. all of above
9. When the affairs of a company have not been completely wound up, the Company Liquidator shall make an application to the Tribunal for dissolution of such company.
- A. True
 - B. False
10. It is a legal declaration of an individual's inability to pay off debts.
- A. Insolvency
 - B. Bankruptcy
 - C. Winding-up
 - D. Liquidation
11. It is the process of winding up the corporation.
- A. Insolvency
 - B. Bankruptcy
 - C. Winding-up
 - D. Liquidation
12. If 75% of creditors approve the resolution plan, it:
- A. shall be implemented
 - B. shall not be implemented
 - C. depends upon the will of the company to implement or not to implement
 - D. none of above
13. Corporate Insolvency Resolution Process (CIRP) apply to matters relating to the insolvency and liquidation of corporate debtors where the minimum amount of the default is _____.
- A. fifty lakhs rupees
 - B. seventy lakhs rupees
 - C. ninety lakhs rupees
 - D. one crore rupees
14. Who may initiate the corporate insolvency resolution process regarding a corporate debtor if such corporate debtor commits a default?
- A. A financial creditor

- B. An operational creditor
- C. The corporate debtor
- D. All of above

15. The term of the interim resolution professional shall continue till:

- A. the date of appointment of the resolution professional under Sec. 22 of IBC, 2016.
- B. the date of actual liquidation of the company
- C. the date decided by the committee of creditors
- D. the date fixed by the adjudicating authority

Answers for Self Assessment

1. A	2. D	3. D	4. D	5. D
6. D	7. A	8. C	9. B	10. B
11. D	12. A	13. D	14. D	15. A

Review Questions

1. What do you understand by the winding up of a company? Explain the circumstances under which the Tribunal can wind up a company.
2. Who are the persons entitled to present a petition for the winding up of a company by the Tribunal?
3. Explain the powers of the Tribunal in context to winding up of a company.
4. Who can apply for initiation of the Corporate Insolvency Resolution Process under the IBC, 2016? Explain in detail the process to be followed by the Financial creditor and Corporate Applicant.
5. Explain the voluntary liquidation process of corporate persons under IBC, 2016.
6. What are the powers and duties of liquidators under IBC, 2016?
7. Briefly discuss the initiation of liquidation as per Sec. 33 of IBC, 2016.
8. State the appointment of the interim resolution professional and resolution professional under IBC, 2016.
9. Briefly discuss the appointment of company liquidators by the Tribunal for winding up a company.
10. Explain the reasons for the removal and replacement of the liquidator by the Tribunal.
11. State the contents of a report to be submitted by the company liquidator to the Tribunal.
12. Briefly discuss the provisions relating to the settlement of the list of contributories and application of assets by the Tribunal.
13. Explain the powers and duties of company liquidators.
14. Discuss the dissolution of the company by the Tribunal.

**Further Reading**

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**Web Links**

https://www.indiacode.nic.in/handle/123456789/2114?view_type=browse&sam_handle=123456789/1362

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<https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf>

<https://www.mca.gov.in/Ministry/pdf/TheInsolvencyandBankruptcyofIndia.pdf>

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