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MEMBERS

MEMBERS AND SHAREHOLDERS

THE term "shareholder" refers to a person who holds share in a company, while the term "member" refers to a person whose name appears on the register of members. Section 41 of the Companies Act, 1956, defines a member as a person who has signed the memorandum of association, and every other person who agrees in writing to become a member and whose name in entered in the register of members. Person other than subscribers to memorandum should agree in writing to become members of a company.[1]

Ordinarily, the terms *member* and *shareholder* are synonymous but, precisely, this is so only in the case of a company limited by shares, a company limited by gurantee and having a share capital and an unlimited company whose capital is held in definite shares. However, there are a few exceptional cases where a person may become a member of a company without being its shareholders and *vice versa.*

Members without being shareholders. The circumstances where a person may become a member of the company without being it shareholder are stated below:

1. In the case of companies limited by guarantee or unlimited companies, a member may not be shareholder because such companies may not have share capital.

2. A deceased member continues to be member so long as his name is one the register of members, but he cannot be termed a shareholder of the company.

3. A transferor of shares also continues to be member until the transfer is registered by the company and the name of the transferor is replaced by the name of transferee, though he is no more a shareholder of the company.

[1] *H.H. Manabendra Shaw v. Official Liquidator, Indian Electirc Tools Corporation Ltd. and Others* (1977) 77 Comp. Cas. 356.

4. Subscribers to the memorandum of a company shall be treated as having become members by the very fact of subscription. On the registration of the company, they shall be entered as its members in its register of members even before any shares are allotted to them.

Shareholders without being members. The circumstances where a person may become a shareholder of a company without being its member are stated below:

1. A person who holds a share warrant is a shareholder but not a member because his name does not appear on the register of members after issue of such a share warrant.

2. Similarly, a transferee or legal representative of a deceased or insolvent members is not a member until he applies for registration as one and his name is entered in the register of the memebers although he is shareholder even without being placed on the register of members.

MODES OF ACQUIRING MEMBERSHIP

A person may become a member of a company in the following ways:

(1) **By subscribing to the memorandum.** Subscribers to the memorandum of a company shall be deemed to have agreed to become its members and on its registration shall be entered as its members in its register of members. [Sec. 41 (1)]

"The subscriber of the memorandum is to be treated as having become a member by the very fact or subscription. Neither application from, nor allotment of shares is necessary. Even an absence of entry in the register of members cannot deprive him of his status. He acquires, as soon as the company is registered, the full status of a member with all its rights and liabilities."[2]

The subscriber to the memorandum must take the agreed number of shares directly from the company. He must pay for his shares in cash even if he had entered into an agreeement with the promoters of the company under which he was to receive shares for his legal services rendered in connection with promotion of the company.[3] His obligation to take shares is not satisfied by transfer to him or by an allotment of shares credited as fully paid up to which a third person is entitled.[4] However, if the company had allotted its entire share capital to others, the subscriber is under no liability to take shares.[5]

[2]*Official Liquidator v. Suleman Bhai,* A.I.R. (1955) M.B. 166.
[3]*Kanduri Chetty v. Adoni Electric Supply Co. Ltd.* A.I.R. 1944 Mad. 322.
[4]*Migottis Case* (1867) L.R. 4 Eq. 238.
[5]*Mackley's Case* (1875) 1 Ch. D. 247.

A subscriber cannot rescind the contract for purchase of shares even on grounds of fraud or misrepresentation on the part of promoters.[6] Similarly, he cannot plead that he subscribed to the memorandum subject to certain reservation.[7]

(2) **By agreeing to purchase qualification shares.** Directors who have signed and delivered to the Registrar an undertaking to take up their qualification shares are in the same position as subscribers to the memorandum and are also deemed to have become members on the registration of the company. [Sec. 266 (2)]

(3) **By application and allotment.** Apart from subscribers to the memorandum, every other person wishing to become a member must fulfil two conditions: (a) There must be a written agreement to take shares, e.g. an application for shares and allotment and communication thereof; and (b) in addition to such an agreement the name of the person must appear on the register of members. But where a person applies for shares but withdraws his application before acceptance and the company, nevertheless, allots and puts his name on the register, he may rescind the allotment.[8]

(4) **By transfer.** A person may become a member by buying shares from an existing member and by having the transfer registered and getting his name placed on the register of members., It may be noted here that share are freely transferable under Sec. 82 of the Act, but the mode of transfer is left to be decided by the articles of the company.

(5) **By transmission of shares.** Transmission is the passing of title or property in shares by operation of the law on the happening of such events as the death, bankruptcy or lunacy of a shareholder. A person may become a member if he succeeds to the estate of a deceased member. The official receiver is likewise entitled to be a member in place of a shareholder who has been declared insolvent. In all these cases, however the person does not become a member unless his name has been place on the company's register of members. Moreover, no instrument of transfer of shares need be delivered to the company for the simple reason that transfer and transmission of shares are quite distinct from each other. The former is based upon the act of parties whereas the latter is the result of the operation of law.

(6) **By estoppel.** A person is deemed to be a member if he allows his name, apart from any agreement to become a member, to be on the register of members or otherwise holds himself out or allows himself to

[6]*Re Metal Constituents Co., Lord Lurgan's Case* (1902) 1 Ch. 707.
[7]*Sonardiah Coal Co. v. Parmanand* (1928) 26 A.L.J. 347.
[8]*Hebb's Case* (1867) L.R. 4 Eq. 9, *Truman's Case* (1894) 3 Ch. 272.

be held out as a member. In such cases he is estopped from denying that he is a member and he will be liable as a contributory.

Where the name of a person is improperly entered in the register of member, he may escape the liability by prompt action to have it removed from the register either by an application under Sec. 111 of the Act or by instituting a suit for the purpose, failing which he will forfeit his right in that behalf.

WHO CAN BE MEMBERS?

The Act does not lay down any qualification for persons who can become members of a company. But since membership involves an agreement between the member and the company, it becomes obvious that membership is open to such persons who are competent to enter into a contract according to the provisions of the Indian Contrct Act, 1872. This is again subject to the provisions of the articles of the company which may provide for the exclusion of certain persons. The membership rights of some special categories of persons are discussed below:

(1) **Minor.** A minor is incompetent to enter into any contract and therefore, he cannot be member of a company. Accordingly, where an application is made by the father as guardian of his minor daughter and the company issues shares to, and registers them in the name of his minor daughter describing her as minor, the transaction is void on the face of its and the father cannot be deemed to have contracted for shares and cannot be placed on the list of contributories in the event of the company being wound up.[9]

In case the directors of a company have entered the name of a minor in the company's register of members in ignorance of his minority, they can remove his name when the fact of minority comes to their knowledge. The minor also has the right to repudiate the allotment at any time during his minority. But in both cases the company must repay to the minor all money received on account of shares allotted. The question of whether or not the minor should return the benefits received from the company would be for the court to decide considering the circumstances of each individual case.

On attaining majority, he can still repudiate his liability on the shares within a reasonable time. But if after attaining majority, he receives dividends and raises no objection to his name being included in the register, he cannot deny that he is a member on the ground of estoppel.[10]

[9]*Palaniappa v. Official Liquidator* (1942) A.I.R. Mad. 470.
[10]*Fazalbhoy Jaffer v. The Credit Bank of India* (1914) I.L.R. 39 Bom. 331.

But in a recent case it has been held that the registration of a transfer shares in the name of the minor, acting through his or her guardian, especially when the shares are fully paid, cannot be refused on the ground that the transferee is a minor.[11]

(2) **Partnership firms.** A firm can't be registered as a member as it is not a legal person and the partners may not remain constant. A firm, however, may purchase shares in a company in the individual names of its partners as joint shareholders.

However, a firm may become a membr of an association or a company licensed under Section 25 of the Companies Act, 1956 and its membership will cease on the dissolution of the firm. [Se. 25(4)]

(3) **Foreigners.** A foreigner can also be a shareholder but his voting rights are suspended when he becomes an alien enemy[12] It is also important to note here that Section 19(i) (b) and (d) of the Foreign Exchange Regulation Act, 1973, requires the general or special permission of the Reserve Bank of India for the issue or transfer of shares to foreigners and non-residents.

(4) **Insolvents.** An insolvent remains a member until his name appears on the register of members. He is also entitled to vote even though his shares vest in the Official Assignee[13] and to make use of the rights of a minority shareholder.[14]

(5) **Companies.** A company, if permitted by its articles, can become a member of another company. Section 187 provides for the attendance by a company of meetings by a duly appointed representative. The board of directors of the company holding shares may authorise such person as it thinks fit to act as its representative at any meeting of the company or at any meeting of any class of members of the company. The person authorised shall be entitled to exercise all the rights and powers including the right to vote by proxy.

Restrictions on inter-company investments. In this connection it is important to note certain restrictions placed by Section 372 on the power of the company to invest in shares or debentures of other companies. According to this section, the board of directors a company shall be entitled to invest in shares of any other company upto 25 per cent of the subscribed equity share capital, or the aggregate of the paid-up equity and preference share capital of the investee company, whichever is less. But the aggregate of the investments by the board of directors in all other

[11]*R.Balraman v. Buckingham and Carnatic Co. Ltd.* (1969) 1 Comp. L.J. 81.
[12]*Re Anglo International Bank Ltd.* (1943) Ch. 233.
[13]*Morgan v. Gray* (1953) Ch. 83.
[14]*Birch v. Sullivan* (1957) 1 W.L.R. 1247.

companies shall not exceed 30 per cent of the aggreate of the subscribed capital and free reserves of the investing company, where all the investee companies are not under the same group as the investing company where all the investee companies are under the same group as the investing company, the aggregate of the investments shall not exceed 20 per cent of the aggregate of subscribed capital and free reserves of the investing company.[15]

An investment in excess of the percentage specified above can be made only if it is sanctioned by a resolution of the investing company in the general meeting and with the approval of the Central Government.

Company not to buy its own shares. Section 77 provides that a company cannot acquire its own shares as it amounts to reduction of capital without the consent of the court which is illegal. It further prohibits a company from giving any financial assistance directly or indirectly for the purchase of its own shares. However, financial assistance for the purchase of company's shares may be granted in the cases specified in the section.

Subsidiary company not to be member of its holding company. At the same time a company cannot be a member of its holding company and any allotment or transfer of shares in a company to its subsidiary or nominee for its subsidiary will be void. This does not apply where the subsidiary is concerned as the legal representative of a deceased member of the holding company or where the subsidiary is trustee for some other shareholders and the holding company or its subsidiary is not beneficially interested except as lender of money in the ordinary course of a business. A subsidiary company may continue is membership of holding company if it was acquired before the commencement of this Act, but without any voting right except in the two cases mentioned above. (Sec. 42)

(6) **Hindu undivided families.** Shares in a company can be purchased by a Hindu Undivided Family through its Karta. In this case Karta shall become a member of the company.

(7) **Married women.** There is no objection to a married woman subscribing to a memorandum of association or to be allotted shares in respect of her own property provided she is competent to enter into a contract.

(8) **Trustees.** A trustee, as trustee, cannot be member because a company is not bound to recognise the existence of the trust. Section 153 provides that no notice of any trust (express, implied or constructive) shall be entered by the company on the register of members. Therefore, a trustee who buys shares will be treated as a member in his individual capacity.

[15]*Prescribed vide Rule 11C inserted by the Companies (Central Govt's) General Rules and Forms (Amendment) Rules, 1989, w.e.f. 17 April, 1989.*

(9) **Registered societies.** A society registered under the Societies Registration Act, 1860, can hold shares in a company in its own name and its name may be entered on the register of memers provided it is so authorised by its memorandum or articles.

(10) **Persons taking shares in fictitious name.** A person who takes shares in the name of a fictitious person becomes liable as a member. Moreover, according to Sec. 68-A, a person who makes in application for allotment of shares or for the registration of transfer of shares in a fictitious name, shall be liable to imprisonment which may extend to 5 years.

(11) **Joint holders.** When two or more persons hold shares in a company in a joint name, they are known as joint sareholders. In the case of a public company, every joint shareholder is a separate member. When three or four persons agree to accept shares in a public company jointly, they do not constitute a single member. But in the case of a private company, joint shareholders are not to be considered as separate members but to be treated as a single member. [Sec. 3(1)(iii)]

The rights and obligations of joint shareholders are laid down in the articles of association of the company. If the articles of the company are silent on this point, the following regulations of Table A will apply automatically:

(*i*) The company is not bound to deliver more than one share certificate and the delivery of the certificate to one of several joint holders shall be sufficient delivery to all such holders. [Regn. 7(3)]

(*ii*) The joint shareholders are jointly and severally liable to pay calls on their shares (Regn.15)

(*iii*) On the death of one of the joint holders, only the surviving joint holder or holders are recognised by the company as having any title to his interest in the shares. However, this shall not release the estate of a deceased joint holder from any liability in respect of any share which had been jointly held by him with other presons. (Regn. 25)

(*iv*) In case of joint holders, the joint holder whose name appears first in the register of members has the right to attend and vote in the meetings. (Regn. 57)

(*v*) Any dividend, interest or other moneys payable in cash in respect of shares held jointly may be paid by cheque or warrant sent to the registered address of the joint holder whose name appears first in the register of members or to such person and address as directed by the joint holders in writing. Every such cheque or warrant shall be made payable to the order of the person to whom it is sent. (Regn. 91)

TERMINATION OF MEMBERSHIP

A person may cease to be a member of a company in one of the following ways:

(*i*) by transfer of his shares and the registration of the transferee on the company's register of members;

(*ii*) by forfeiture of shares on account of non-payment of call and interest thereon, if the articles so provide;

(*iii*) by a valid surrender of shares to the company;

(*iv*) by a sale by the company of his shares under some provisions in the articles, e.g., in exercise of its lien over his shares;

(*v*) by all the shares being allotted to others by the company, if he is a subscriber of the memorandum;[16]

(*vi*) by repudiating the contract of membership on the ground of misrepresentation in the prospectus (not applicable to subscribers of the memorandum);

(*vii*) by redemption of redeemable preference shares;

(*viii*) by sale of shares in execution of a decree of court and the purchaser being registered as a member;

(*ix*) by death of the shareholder when his shares are registered in the name of his legal representative;

(*x*) by conversion of share certificates into share warrants in case of fully paid shares;

(*xi*) by insolvency of the members on the shares being transferred by Official Assignee and registered in the name of the purchaser; and

(*xii*) on the winding up of the company.

RIGHTS OF MEMBERS

The members of a company enjoy various rights in relation to the company. These rights are conferred on members of the company either by the Companies Act, 1956 or by the memorandum and articles of association of the company or by the company or by the general law, especially that relating to contracts under the Indian Contract Act, 1872. Some of the more important rights are stated below:

1. He has a right to obtain copies of memorandum of association, articles of association and certain resolutions and agreements on request and payment of the prescribed fees. (Sec. 39)

2. He has a right to have the certificate of shares held by him within three months of the allotment. (Sec. 113)

[16]*Mackley's Case* (1875) 1 Ch. D. 247.

3. He has a right to transfer his shares or other interests in the company subject to the manner provided by the articles of the company. (Sec. 82)

4. He has a right to appeal to the Company Law Board where the company refuses or fails to register the transfer of shares. (Sec. 111)

5. He has the preferential right (i.e. right of pre-emption) to purchase shares on a pro rata basis in case of a further issue of shares by the company. Moreover, he has also the right of renouncing all or any of the shares in favour of any other person. (Sec. 81)

6. He has a right to apply to the Company Law Board for rectification of the register of members. (Sec. 111)

7. He has a right to apply the court to have any variation or abrogation to his rights set aside by the court. (Sec. 107)

8. He has the right to inspect the register and index of members and debentures holders, annual returns, register of charges and register of investments not held by the company in its own name, without any charge. He can also take extracts from any of them.

9. He is entitled to receive notices of general meetings and to attend such meetings and vote thereat either in person or by proxy.

10. He is entitled to receive a copy of the statutory report. (Sec. 165)

11. He is entitled to receive copies of the annual report of directors, annual accounts and authors' report. (Sec. 219)

12. He has the right to participate in the appointment of auditors and the election of directors at the annual general meeting of the company. (Secs. 224 and 225)

13. He has a right to make an application to the Company Law Board for calling annual general meeting if the company fails to call such a meeting within the prescribed time limits. (Sec. 167)

14. He can require the directors to convene an extra-ordinary general meeting by presenting a proper requisition as per the provisions of the Act and hold such a meeting on refusal. (Sec. 169)

15. He can make an application to the Company Law Board for convencing an extraordinary general meeting of the company where it is impracticable to call such a meeting either by the directors or by the members themselves. (Sec. 186)

16. He is entitled to inspect and obtain copies of minutes of proceedings of general meetings. (Sec. 196)

17. He has a right to participate in the declaration of dividends and receive his dividends duly.

18. He has a right to demand poll. (Sec. 179)

19. He has a right to apply to the Company Law Board for investigation of the affairs of the company. (Sec. 235)

20. He has the right to remove a director before the expiry of the term of his office. (Sec. 284)

21. He has a right to make an application to the Company Law Board for relief in case of oppression and mismanagement. (Secs. 397 and 398)

22. He can make a petition to the High Court for the winding up of the company under certain circumstances. (Sec. 439)

23. He has a right to participate in passing of a special resolution that the company be wound up by the court or voluntarily. [Secs. 433 and 484(1)(b)]

24. He has a right to participate in the surplus assets of the company, if any, on its winding up. (Secs. 475 and 511)

LIABILITY OF MEMBERS

The libaility of the members of a company depends on the nature of the company.

Company with unlimited liability. A company not having any limit on the liability of its members is termed an "unlimited company". The shareholders are fully liable for deficiency of assets to the liabilities of the company in proportion to their interests in the companies. Such companies are rarely encountered.

Company limited by shares. In the case of a company limited by shares, the liability of its members is limited to the amount, if any, unpaid on the shares respectively held by them. These types of companies are by far the largest. The main reason is the attraction to investors of knowing beforehand the exact amount of risk involved or maximum limit of the liability.

The amount of shares may not be paid in full at once, but from time to time, as and when the company makes calls on shareholders. All moneys payable by any member to the company under the memorandum or articles shall be a debt due from him to the company. (Sec. 36)

In case of death of a shareholder, his estate remains liable in respect of his shares until some other person is registered as the holder thereof.[17] In case of a transfer of shares, the transferee, on being registered as a holder, becomes liable to pay all moneys thereafter being payable in respect of the shares. In case of insolvency of a member, his shares shall vest in the Official Assignee or the Official Receiver. If the Official Assignee sells these shares, the purchaser will be entered on the register of members and he will be liable in respect of unpaid amount on those shares. Where the Official Assignee disclaims the shares, the company

[17]*Baird's Case* (1870) L.R. 5 Ch. App. 725.

may prove for the amount unpaid on the shares.

Additional liability not to be imposed. Section 38 provides that any alteration made in the memorandum or articles which seeks to impose additional liability on a member of a company to take more shares than what he has already taken or to pay any more money than what he is liable to pay on his shares, shall not be binding upon him unless he agrees in writing, either before or after the alteration.

Directors with unlimited liability in a limited company. Section 322 provides that the liability of the directors or any of them or manager may be unlimited by virtue of the provisions of the memorandum of the company, though the liability of members is limited.

Unlimited liability on reduction of membership below minimum. The liability of members becomes unlimited and several in the case of a limited company if the number of its members falls below seven in the case of a public company, and two in the case of a private company, and the company continues to conduct business for more than six months after the reduction of number of members below the legal minimum. (Sec 45)

Company Limited by Guarantee

In the case of a company limited by guarantee, the liability of its members is restricted to such amount as the members may respectively undertake to contribute in the event of its being wound up. Non-profit earning companies are mostly registered with a guarantee liability. If such a company has a share capital, the members are also liable to pay the amount which remains unpaid on their shares, besides the amount payable under guarantee. The guarantee amount cannot be called up except when the affairs of the company are wound up.

Liability on Winding Up of the Company

If before the liability to pay the whole amount is discharged, the company goes into liquidation, the shareholders become liable as contributories to pay the balance when called up to do so (Sec. 429). If a person has ceased to be a member within one year prior to the winding up of the company, he is liable to be included in the "B" list of past members and pay on the shares which he held to the extent of the amount unpaid thereon, if (*a*) on the winding up, debts exist which were incurred while he was a member, and (*b*) the members of the 'A' list (list of present members) cannot satisfy the contribution required from them in respect of their shares. (Sec. 426)

REGISTER OF MEMBERS

Section 150 of the Companies Act, 1956, requires every company to maintain a register of members which must contain the following particulars: (*a*) the name, address and occupation of each member; (*b*) in the case of a company having share capital, the shares held by each member, distinguishing each share by its number and the extent to which the shares have been paid up; (*c*) the date on which each person was entered in the register as a member; and (*d*) the date on which any person ceased to be a member.

Where the company has converted any of its shares into stock and given notice of the conversion to the Registrar, the register shall show the amount of stock held by each of the members in place of shares.

If any default is made in maintaining the register in the above manner, the company and every officer of the company who is in default, shall be punishable with a fine which may extend to fifty rupees for every day during which the default continues.

Section 164 states that the register or members shall be *prima facie,* but not conclusive, evidence of any matters directed or authorised by the Act to be entered therein. The court will accept the same as correct until rebutted.

Index of Members

Under Section 151, every company with more than fifty members is required to keep an index of members along with the register. The index may be in the form of a card index. If the register of members is in such form as in itself constitutes an index, no separate index of members would be required.

Where the index register is maintained, it shall be kept at the same place as the register of members. It shall contain sufficient indication to enable the entries relating to a member easily found. Any alteration in the register of members must be noted in the index within fourteen days of the alteration.

If default is made in complying with these provisions, the company and every officer of the company who is in default shall be punishable with a fine which may extend up to fifty rupees.

Location of Register of Members

Section 163 of the Companies Act, 1956, requires that the register and index of members be kept at the registered office of the company. These may, however, be kept at any other place within the same city or town in which the registered office of the company is situated provided, (*a*) such

may prove for the amount unpaid on the shares.

Additional liability not to be imposed. Section 38 provides that any alteration made in the memorandum or articles which seeks to impose additional liability on a member of a company to take more shares than what he has already taken or to pay any more money than what he is liable to pay on his shares, shall not be binding upon him unless he agrees in writing, either before or after the alteration.

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Foreign Register of Members

A company with a share capital or one that has issued debentures may, if authorised by its articles, keep in any State or country outside India a branch register of members or debentures holders resident in that State or country. Such a register is called a 'foreign register'. If a company opens a foreign register at a place, it must file with the Registrar of Companies a notice of the location of the office where such a register is kept within thirty days of opening of such register. Notice of any discontinuance or change in situation of such office must be given to the Registrar within one month. (Sec. 157)

The foreign register is a part of the country's principal register of members or of debenture holders, as the case may be. A foreign register shall be kept open to inspection and may be closed and extracts be taken therefrom and copies thereof may be required in the same manner as is applicable to the principal register maintained in India. However, the advertisement before closing the foreign register shall be inserted in some newspaper circulating in the district where the foreign register is kept. The duplicate copy of the foreign register shall be maintained at the head office in India and all entries made in that foreign register should be entered in the duplicate copy as soon as possible. If so directed by the Central Government, the decision of any competent court of the State where the foreign register is kept, shall be as effective as if it were the decision of a competent court in India. The company may at any time discontinue such a foreign register in which case all its entries may either be transferred to some other foreign register kept in the same part of the world or to the principal register. (Sec. 158)

Rectification of the Register of Members

Prior to the Companies (Amendment) Act of 1988, the power to order rectification of register of members was vested in the court under Section 155. The Amendment Act of 1988 seeks to recast Section 111 by assimilating the existing provisions of Section 155 and it vests the Company Law Board with the court's power to order rectification of register of members.

Under the Section 111(4), the Company Law Board has been empowered to order the rectification of the register of members in the following cases; (*a*) where the name of any person is entered in the register of members without any sufficient cause, (*b*) where the name of any person is omitted from the register of members witout any sufficient cause, and (*c*) where default is made or unnecessary delay takes place in entering on the register the fact of any person having become or ceased to be a member.

place has been approved by a special resolution of the company in general meeting, and (*b*) the Registrar has been given a copy of the proposed special resolution in advance.

Inspection of Register of Members

A company's register of members and debenture holders are public documents and are open to public inspection during business hours for at least two hours each day except when the registers are closed under Section 154. In the case of a member or debenture holder, no fee is to be charged for inspection. But in the case of any other person, a fee of rupees ten per inspection may be charged. The right to inspect also includes the right to make extracts from the registers. The company is also bound to supply a copy of the register on demand on payment of rupee one per one hundred words or part thereof, within ten days of the receipt of such demand. This period of ten days excludes non-working days. (Sec. 163)

Section 163 furher lays down that if the company refuses inspection or the taking of any extract from the register of members or fails to supply extracts from the register within the period specified above, every officer of the company who is in default is liable to respect of each offence to a fine which may extend to fifty rupees for each day during which the refusal or default continues.

The court can compel the company to give immediate inspection of the register of members or allow an extract to be taken by a person requiring it or supply forthwith a copy of a portion of the register as may be required.

It may further be noted that the object of inspecting the register is immaterial. Even if it is known that the object is antagonistic to the company, it is illegal to refuse inspection or copy.[18] A member of the company can have an inspection of the register carried out where the circumstances justify it by means of an agent.[19] The right to inspect ceases upon the commencement of winding up, and if an inspection is required after that, an order of the court must be obtained under Section 549.[20]

Closure of Register of Members

Section 154 empowers a company to close the register of members by giving seven days' previous notice by advertisement in a local daily for a period not exceeding 45 days in a year but not exceeding 30 days at any one time.

[18]*Davies v. Gas Light & Coke Co.*, (1900) 1 Ch. 248.
[19]*Bevan v. Webb* (1901) 2 Ch. 59.
[20]*Re Kent Coalfields Syndicate* (1898) 1 Q.B. 754.

Foreign Register of Members

A company with a share capital or one that has issued debentures may, if authorised by its articles, keep in any State or country outside India a branch register of members or debentures holders resident in that State or country. Such a register is called a 'foreign register'. If a company opens a foreign register at a place, it must file with the Registrar of Companies a notice of the location of the office where such a register is kept within thirty days of opening of such register. Notice of any discontinuance or change in situation of such office must be given to the Registrar within one month. (Sec. 157)

The foreign register is a part of the country's principal register of members or of debenture holders, as the case may be. A foreign register shall be kept open to inspection and may be closed and extracts be taken therefrom and copies thereof may be required in the same manner as is applicable to the principal register maintained in India. However, the advertisement before closing the foreign register shall be inserted in some newspaper circulating in the district where the foreign register is kept. The duplicate copy of the foreign register shall be maintained at the head office in India and all entries made in that foreign register should be entered in the duplicate copy as soon as possible. If so directed by the Central Government, the decision of any competent court of the State where the foreign register is kept, shall be as effective as if it were the decision of a competent court in India. The company may at any time discontinue such a foreign register in which case all its entries may either be transferred to some other foreign register kept in the same part of the world or to the principal register. (Sec. 158)

Rectification of the Register of Members

Prior to the Companies (Amendment) Act of 1988, the power to order rectification of register of members was vested in the court under Section 155. The Amendment Act of 1988 seeks to recast Section 111 by assimilating the existing provisions of Section 155 and it vests the Company Law Board with the court's power to order rectification of register of members.

Under the Section 111(4), the Company Law Board has been empowered to order the rectification of the register of members in the following cases; (*a*) where the name of any person is entered in the register of members without any sufficient cause, (*b*) where the name of any person is omitted from the register of members witout any sufficient cause, and (*c*) where default is made or unnecessary delay takes place in entering on the register the fact of any person having become or ceased to be a member.

Persons entitled to apply to the Company Law Board. In all these cases the person aggrieved or the company or any member of the company may apply to the Company Law Board for the rectification of the register of members. A person who claims to have become a member but whose name has not been entered in the register of members may make the application.[21] The Company Law Board has very wide discretionary powers in this regard. It may either reject the application or order rectification of the register and even payment by the company of any damages sustained by the aggrieved party. But no damages can be ordered unless the relief of rectification is granted.[22]

An application for rectification has to be in the form of petition in writing and accompanied by such fee as may be prescribed. [Sec. 111(10)]

Rectification on winding up. Section 467 also empowers the court to rectify a register on the winding up of a company before settling the list of contributories.

It may also be noted that rectification will date back to the date on which a mistake, default or delay which is being rectified was made.[23]

Cases where rectification ordered. The following are a few illustrative cases where the rectification of register of members has been been ordered:

(*i*) where the person was induced to buy shares by misrepresentation;[24]

(*ii*) where the allotment was irregular;[25]

(*iii*) where shares were improperly forfeited;[26]

(*iv*) where the real owner's name was removed by the company acting on a forged transfer;[27]

(*v*) where the shares were improperly surrendered and the shareholder claimed to have his name reinstated;[28]

(*vi*) where the application for shares was conditional and the condition precedent was not fulfilled;[29]

[21]*N.K. Aggrawal v. Hanuman Mills Private Ltd.,* (1973) 71 A.L.J. 518.

[22]*Praga Tools Corp. v. M.R.M. Patny* (1968) 1 Com. L.J. 256.

[23]*Panna Lal Sood v. Jagatjit Distilling* 1952, Pepsu 2.

[24]*Stewart's Case* (1866) L.R. 1 Ch. App. 574.

[25]*Re Portuguese Consolidated Copper Mines* (1889) 42 Ch. D. 160.

[26]*Public Passenger Service Ltd. v. Khadar,* A.I.R. (1966) S.C. 489; *Kota Transport Co. Ltc. v. State of Rajasthan* (1967) Comp. Cas. 288; *Mrs. Promila Bansal v. Wearwell Cycle Co. (India) Ltd.* (1978) 48 Comp. Cas. 204.

[27]*Re Bahia and San Francisco Rly.* (1868) L.R. 3 Q.B. 584; *People's Insurance Co. Ltd. v. C.R.E. Wood & Co.* A.I.R. (1960) Punj. 388.

[28]*Bellerby v. Rowlan and Marwood's Steamship Co.,* (1902) 2 Ch. 14 (C.A.)

[29]*Roger's Case and Harrison's Case* (1968) L.R. 3 Ch. App. 633; *Simpson's Case* (1869) 4 Ch. App. 184.

(*vii*) where the company improperly neglected to register a transfer;[30]

(*viii*) where the allotment was not made within a reasonable time;[31] and

(*ix*) where the allotment is made in violation of the provisions of articles.[32]

The above provisions are applicable to the rectification of the register of debenture-holders also. [Sec. 111(8)]

NO NOTICE OF TRUST ON REGISTER

Section 153, though short, is of very great importance. It clearly states that no notice of any trust, express, implied or constructive, shall be entered on the register of members or debentures holders. For example if A is acting as a trustee of behalf of B, the company must not take any notice that A is a trustee. In the register, the name of A only is to be entered and no mention that he is a trustee on behalf of B, shall be made. The trustee can be entered in the register in his personal capacity and not as a trustee, and he will exercise the rights of a shareholder, and is alone liable for share calls and to be put on the list of contributories. The provision is to relieve the company from taking any notice of equitable interest in shares and to preclude any person claiming an equitable interest in shares from treating the company as a trustee in respect thereof.

The above provision is well illustrated in the case of *Murshidabad Loan Office Ltd. v. Satish Chandra Chakarvarti.*[33] In this case, a lady was the registered holder of certain shares in a company. These shares really belonged to her husband and on learning this the company filed a case against him for the unpaid calls on the shares. It was held that the husband was not liable, although he was the real owner. The court observed; "Assuming that the registered shareholder is not the real owner but if he is the member in the books of the company, it is he alone who would be entitled to the rights of a shareholder and he alone is liable for share calls and to be put on the list of contributories."

Public Trustee

The Act now contains various provisions in respect of shares and debentures held in trust so as to prevent the trustees from misusing the

[30]*Re Stranton Iron and Steel Co.*, (1873) L.R. 16 Eq. 559.

[31]*Indian Co-operative Navigation and Trading Co. Ltd. v. Padamsey Premjit* (1933) 36 Bombay L.R. 32.

[32]*Basudeb Katasuka v. Dhanbad Automobiles Pvt. Ltd.* (1977) 47 Comp. Cas. 68.

[33]A.I.R. (1943) Cal. 440.

rights and privileges attached to such shares and debentures. These provisions are contained in Sections 153A, 153B and 187B.

The Central Government has the power to appoint a public trustee to discharge the functions and exercise the rights and powers conferred on him by or under the Act. (Sec. 153A)

Declaration as to shares and debentures held in trust. Where any shares or debentures are held in trust by a trustee he shall make a declaration to the public trustee in the prescribed form within 60 days from the date on which the shares or debentures are held by him as such. A copy of such declaration is to be sent by the trustee to the company within 21 days after the declaration has been to the public trustee. There is a penalty if the trustee makes a false statement in the declaration or if he fails to make the declaration.

Exemptions. These provisions are not applicable in the following cases: (*a*) where the trust is not created by an insturment in writing; or (*b*)even if it is in writing, where the value of shares or debentures held in trust does not exceed one lakh rupees, or exceeds one lakh but does not exceed five lakhs or twenty-five percent of the paid up share capital of the company concerned, whichever is less. (Sec 153B)

Exercise of voting rights in respect of shares held in trust. Section 187 B lays down the method of exercising voting rights in respect of shares held in trust. The rights and powers (including the right to vote by proxy) exercisable by a trustee shareholder at a meeting of the company cease to be exercisable by the trustee as a member of the company and become exercisable by the public trustee. The public trustee may himself attend the meeting and exercise the rights and powers or appoint an officer of the Government or the trustee shareholder himself to attend the meeting and vote thereat according to his directions. The public trustee may abstain from exercising his rights and powers if in his opinion the objects of the trust or the interests of the beneficiaries of the trust are not likely to be adversely affected by such abstention.

The trustee may inform the public trustee that to safeguard the objects of the trust or the interest of the beneficiaries of the trust, the public trustee should exercise his voting rights. The public trustee may in his discretion either accept such views or reject the same and for his absention no legal proceedings would be maintainable against him.

For the effective exercise of these rights the public trustee shall also be entitled to receive and inspect all books and papers under this Act which a member is entitled to receive and inspect. (Sec. 187B)

Declaration by Benami Shareholders

Section 187C has been inserted by the Companies (Amendment) Act,

1974. The object of this section is that all benami holdings of shares must be declared by the benamidar (the registered shareholder) and the beneficial owner.

Declaration by legal owner. A person whose name is entered in the register of members of a company as the holder of shares in that company, but who does not hold the beneficial interest in such shares, shall make a declaration to the company specifying the name and other particulars of the person who holds the beneficial interest in such shares. The declaration shall be made within such time and in such form as may be prescribed.

Declaration by beneficiary. A person who holds a beneficial interest in a share or a class of shares of a company shall make a declaration to the company specifying the nature of his interest, particulars of the person in whose name the shares stand registered in the books of the company and such other particulars as may be prescribed. Such declaration shall be made within thirty days of the person's becoming such beneficial owner.

Any change in the beneficial interest is to be intimated to the company by the beneficial owner within thirty days of the date of such a change.

The company shall make a note of these declarations in the register of members and is also required to file a return within thirty days of the receipt of the declarations, with the Registrar of Companies.

Penalty for non-compliance. These provisions are intended to disclose the names of actual persons who stand to benefit by particular shares. If a person fails to comply with the above provisions, he shall be punishabie with a fine which may extend to one thousand rupees for every day during which the default continues. If a company fails to comply with the above provisions, the company and every officer of the company who is in default, shall be punishable with a fine which may extend to one hundred rupees for every day during which the default continues.

If a declaration is not made in accordance with the above provisions, any charge, promissory note or any other collateral agreement, or any hypothecation by the ostensible owner of any share, shall not be enforceable by the beneficial owner or any person claiming through him. This is to discourage *benami* transactions.

However, the dividends shall continue to be payable to registered shareholders in accordance with the Section 206. (Sec. 187C)

Investigastion of beneficial ownership in certain cases. Where it appears to the Central Government that there are good reasons to do so, it may appoint one or more inspectors to investigate and report as to whether the provisions of Section 187C have been complied with in regard to any shares. Thereupon the provisions of Section 247 regarding the investigation of ownership of the company shall apply to such investigation.

(Sec. 187D)

Register of directors' shareholdings. Under Section 307, every company shall maintain a register of directors' shareholdings. This shows not only the company's shares registered in the names of its directors but also shares held in trust for them or of which they have any right to become the holder whether on payment or not. This also enables us to know the individuals who really control the affairs of the company.

ANNUAL RETURN

Every company must prepare and file every year with the Registrar of Companies a return known as 'annual return'. The purpose of filing an annual return is to enable the Registrar to record the changes that have taken place in the contitution of the company during the year.

Annual return of a company having a share capital. Section 159 requires that every company having a share capital must prepare and file with the Registrar an annual return within 60 days of the date of the annual general meeting. The return of a company with share capital has to contain the particulars specified in Part I of Schedule V of the Companies Act as they stood on that day regarding: (*a*) its registered office; (*b*) its register of members; (*c*) its register of debenture holders; (*d*) its shares and debentures; (*e*) its indebtedness; (*f*) its members and debenture holders, past and present; and (*g*) its directors, managers and managing directors, past and present.

Section 159(1), as amended by the Companies (Amendment) Act, 1988 provides for the filing of annual return containing full particulars as to the past and present members and share held and transferred by them once in every six years, as against once in every three years prior to the amendment. Annual returns for the intervening five years are required to contain only the changes in the list of shareholders or the number of shares held by a member.

If no annual general meeting is held in a particular year then the annual return has to be filed within 60 days from the last day on which the meeting should have been held, which is normally 6 months from the date of the closing of the accounting year of the company. If no annual general meeting has been held, the company shall file with the annual return, a statement giving the reasons for not holding the annual general meeeting. Therefore not holding the annual general meeting is not an excuse for not filing the annual return.[34] The fact that the company itself did not function could not be a ground by itself for non-compliance of

[34]*State of Bombay v. Bhandhan Ram Bhandari* A.I.R. (1961) S.C. 186.

this section.[35] The annual return shall be filed in the form given in Part II of Schedule V.

Annaul return of a company not having a share capital. Under Section 160, the annual return of a company without share capital must state the following particulars: (*a*) the address of the registered ofice of the company; (*b*) the names of members and the respective dates on which they became members, and the nemes of persons who ceased to be members since the date of the last annual general meeting, and the dates on which they ceased to be members; (*c*) all such particulars with respect to the persons who, at the date of the return, were the company's directors, managers and secretary; and (*d*) a statement containing the particulars of the total amount of indebtedness of the company in respect of all charges which are or were required to be registered with the Registrar under the Act.

Signature and certification of annual return. Under Section 161, the copy of the annual return filed with the Registrar must be signed both by a director and by the manager or secretary of the company. Where there is no manager or secretary, the copy must be signed by two directors, one of whom must be the managing director, if any. As per Amendment Act (1988), the annual return of a listed company shall also be signed by a secretary in whole-time practice, in addition to its certification by the company secretary. Further, the annual return must be accompanied by a certificate signed by signatories of the return stating that information given in the return was correct on the day of the annual general meeting, and that further entries regarding transfer of shares and debentures have been correctly recorded in the proper books. In the case of a private company the certificates should further state that the company has not, during the year, issued any invitation to the public to subscribe for shares or debentures of the company and that where the annual return discloses the fact that the number of members exceeds fifty, the excess consists wholly of persons who are not to be included in reckoning the number of fifty.

In addition to the above certificates, the annual return of a private company shall be accompained by a certificate to the following effect:

(*a*) no public company or companies has or have held twenty-five per cent of its paid-up share capital;

(*b*) it did not have, during the period of three consecutive financial years, an average annual turnover of rupees five crores or more; and

(*c*) it did not hold twenty-five per cent or more of the paid-up share

[35]*Sukhbir Saran v. Registrar of Companies* (1972) 42 Comp. Cas. 408; *Madan Gopal Dey v. State of West Bengal* (1968) 2 Comp. L.J. 22.

capital of one or more public companies. [Sec. 43A(8),(9)]

Penalty. If the company fails to comply with any of the provisions relating to the annual return, the company and every officer of the company who is in default is punishable with a fine extending up to fifty rupees for every day during which the default continues. (Sec. 162)

QUESTIONS

1. Distinguish between a 'shareholder' and a 'member'.
[Delhi, B. Com. (Hons.), 1978, 79, 80, 85, 90]

2. (*a*) Define a member. Distinguish him from a shareholder.
(*b*) Briefly explain the provisions relating to joint shareholders of a company.
[C.A. (Final), May 1977]

3."All shareholders are members of a company but all members need not be shareholders of the company." Discuss. *[Delhi, B.Com. (Hons.), 1974]*

4. How can a person (*i*) become, or (*ii*) cease to be a member of a company?
[Delhi, B.Com. (Hons.), 1976]

5. What are the several ways in which a person can become a member of a company? Are all holders of shares of a company necessarily members of the company? *[Company Secretary (Inter), Oct. 1975]*

6. (*a*) Define 'member of a company'. How does a member differ from a shareholder?
(*b*) Describe the ways of acquiring membership of a public company limited by shares. *[Poona, B.Com. (Part I) 1970]*

7. Please offer your comments as to whether the following can become members in a company. You may give reasons in support of your view: (*a*) A company, (*b*) A firm, (*c*) A foreigner, (*d*) An insolvent.
[Company Secretary (Inter), June 1977]

8. What are the provisions of the Companies Act as regard maintenance, location, inspection and closing of the company's register of members?

9. What is meant by rectification of register of members? What are the remedies open to a person where his request for rectification is refused by the company?
[C.A. (Final), May 1978]

10. What are the provisions of the Companies Act in respect of shares held in trust? How are the voting rights exercised in respect of such shares?

11. Explain the provisions introduced by the Companies (Amendment) Act, 1974, as regards declarations in respect of benami-holdings of shares.

PRACTICAL PROBLEMS

1. An application is made by the father as guardian of his minor daughter for certain shares in a company. The company issues shares to, and registers shares in the name of, the minor describing her as minor. Later on, the company goes into liquidation. Can the father of the minor who signed the application be placed on list of contributories and be held liable as such?

2. A company seeks your advice as to whether it will be proper for it to register a transfer of shares when the transferee is known to be a minor. Record your views.

[*C.A. (Finaol) May 1974*]

3. Miss N.J., a minor, applied for registration in her name of 10.000 fully paid-up equity shares in the company through her father and natural guardian Shri A.K.J. The appellant bought these shares from one Shri M.K.J. The transferor Shri M.K.J. and the transferee, the minor Miss N.J. through her father and natural guardian Shri A.K.J. executed the necessary transfer deed which was presented to the company for registration of the transfer of shares. Can the Board of Directors refuse to register the transfer of shares on the plea that transferee is a minor?

[*Company Secretary (Inter), June 1977*]

4. A company made a call in respect of certain partly paid shares standing in the name of *X* who failed to pay the amount of the call within the stipulated period. Shortly thereafter the company went into liquidation and the liquidator renewed the call. *X* thereupon moved the Court for rectification of the share register to remove his name as contributory on the plea that he was only a nominal holder of the shares. Will *X* succeed? [*C.A., May, 1968*]

5. A company, without passing a resolution in its general meeting and getting sanction of the Court, allotted 500 shares at a discount to *G*, its chairman, and placed his name on the register of members. In the winding up of the company, *G* claimed that he was not liable to be made a contributory as the allotment was made in contravention of the provisions of the Companies Act. Is *G*'s contention justified in any way? [*C.A. May 1969*]

6. *A* had subscribed the memorandum of a company for 200 shares. The company was duly registered, but *A* actually took only 20 shares. Shortly, the company went into liquidation. Explain the liability of *A*?

7. The name of *X* is found entered in the register of members of a company. But *X* contends that he is not a member of the company. The company maintains that *X* had orally agreed to become a member and hence, his name was entered in the register and so he is a member. Is the contention of *X* valid?

[*C.A. (Inter) Nov. 1973*]

11

TRANSFER AND TRANSMISSION OF SHARES

RIGHT TO TRANSFER SHARES

ONE of the greatest advantages of a company from of organisation is that its shares are freely transferable. Section 82 provides that the shares of a member in a company shall be movable property, transferable in manner provided by the articles of the company. The right to transfer shares is a statutory right provided by the Act. However, the articles of the company may impose certain reasonable restrictions regarding the manner in which such transfers will be made, but the right to transfer shares cannot be taken away by any provision in the articles. The latter cannot impose absolute restrictions on the right of the shareholders to transfer their shares. If such absolute restrictions are incorporated in the articles, they will be *ultra vires* the Companies Act.

In the absence of any restrictions in the articles, the shares may be transferred to anybody even though he be a man of straw.

Thus, where a holder of partly paid up shares with a view to escape liabilities transferred his shares and the transfer was duly approved by the Board, it was held to be a valid transfer in the absence of any collusion between the transferor and the directors.[1]

However, in a private company, the right to transfer shares is closely restricted. Section 3 (1)(*iii*) provides that the articles of a private company shall restrict the right to transfer its shares if any.

Statutory Provisions Regarding Transfer of Shares

The statutory provisions regarding transfer of shares are as follows:

1. **Instrument of transfer to the delivered to the company.** A company shall not register a transfer of shares unless a proper instrument of transfer duly stamped and executed by the transferor and transferee has been delivered to the company along with the certificate relating to the

[1] *Re Discoverers Finance Corporation Ltd.* (1910) 1 Ch. 207.

shares. If no such certificate has been issued, the letter of allotment of shares should be submitted to the company. It must specify the name, address and occupation of the transferee.

However, if any instrument of transfer signed both by the transferor and the transferee has been lost, the directors may register the transfer on the application by the transferee on his executing a bond of indemnity. [Sec. 108 (1)]

Proper instrument means an instrument which satisfies all the requirement of the Act, including the stamp duty to be affixed.[2] The instrument of transfer has to be executed by all the joint holders as transferors in the case of shares jointly held.[3]

2. **Instrument of transfer to be in the prescribed form.** Every instrument of transfer should be in the prescribed form and must be presented to the prescribed authority before it is signed by the transferor and before any entry is made in it. The prescribed authority shall stamp or otherwise endorse on the instrument the date on which it is so presented. Thereafter such instrument of transfer must be executed by the transferor and the transferee and completed in all other respects. It must then be delivered to the company if the shares of the company are dealt in on a recognised stock exchange, any time before the date on which the register of members is closed for the first time after the date of presentation or within twelve months of the date of such presentation, whichever is later. In any other case, the instrument of transfer shall be delivered to the company within two months of the date of such presentation. [Sec. 108(1A)]

These provisions intend to restrict the period of currency of blank transfers. However, the above limits shall not apply where shares are held under a blank transfer by State Bank of India or any schedule bank or any approved financial institution or the Central or State Government, by way of security for repayment of any loan or the performance of any obligation. [Sec. 108 (1C)]

Section 108 (1D) empowers the Central Government to extend the periods mentioned above by such further time as it may deem fit in order to avoid hardship in any particular case.

3. **Transfer by legal representative.** Oridinarily, a member of the company whose name appears in the register of members can transfer shares, but any transfer made by a legal representative of a deceased member shall be valid although the legal representative is not a member himself (Sec. 109). The legal representative does not become a member

[2]*Re Paradise Motor Co. Ltd.* (1968) 2 All. E.R. 625.
[3]*Hemalata Saha v. Stadmed Pvt. Ltd.* A.I.R. (1965) Cal. 436.

unless he consents to be treated as such and to be entered on the register of members.

4. **Notice to transferee.** An application for registration of transfer of shares of a member in a company may be made either by the transferor or the transferee. Where the application is made by the transferor and relates to partly paid shares,, the transfer shall be registered only if the company gives notice of the application to the transferee, and the latter makes no objection to the transfer within two weeks of receipt of the notice. (Sec. 110)

The Act does not require the notice to be given to the transferor in case the application is made by the transferee, although in practice the company also gives such notice to the transferor. The transferor is not bound to reply to the notice and if he does not send any reply, he will not be estopped from denying the validity of the transfer.[4]

5. **Refusal by the company to register a transfer.** Although the right to transfer shares is a statutory right granted by the Companies Act, yet it is common for articles to provide that directors shall have the power to refuse to register a transfer on reasonable grounds. When directors have the power to refuse registration of a transfer, the power must be exercised in a *bona fide* and just manner and not arbitrarily or *mala fide* or for collateral motive.[5]

The power to refuse to register a transfer of shares must be exercised by a resolution of the board. Where the board had power to refuse to register a transfer and it was equally divided, there being no casting vote, it was held that the power to refuse had not been exercised and that therefore, it must be registered.[6] And if one of two directors intentionally fails to attend a board meeting so that the quorum of two will not be reached and accordingly transfers cannot be passed for registration, the transfer must be registered.[7]

Once a transfer has been recognised and registered, the directors cannot exercise their power of refusal in respect of such transfer.[8] Similarly directors cannot refuse registration of transfer of fully paid shares unless there is express provision to this effect in the articles.[9]

Usual restriction on transfer of shares. The articles usually empower

[4] *Barton v. L. and N.W. Rly. Co.* 24Q. B.D. 77

[5] *Bajaj Auto Ltd. v. N.K. Firodia* A.I.R. (1971) S.C. 321.

[6] *Re Hackney Pavilion* (1924) 1 Ch. 276 approved in *Moodie v. Shepherd* (Bookbinders) *Ltd.* 1949, 3 All. E.R. 1044.

[7] *Re Copal Varnish Co. Ltd.*, (1917) 2 Ch. 349.

[8] *IronTraders (Pvt.) v. Hira Lal Mithal* (1962) Comp. Cas. 1022.

[9] *Jalpaiguri Cinema Co. Ltd. v. Pramatha Nath Mukherjee* (1917) 14 Comp. Cas. 141.

the directors to refuse registration of transfer of shares on the following grounds:

(*a*) where the calls are in arrears against the shares to be transferred;

(*b*) where the transferor is a debtor of the company and the company has a lien on shares;

(*c*) where partly paid up shares are to be transferred to a minor;

(*d*) where the transferee is a man of unsound mind;

(*e*) where partly paid up shares are to be transferred toa buyer (transferee) who, in the opinion of directors, is financially incapable of paying the remaining unpaid amount on the shares;

(*f*) where the instrument of transfer is incomplete, irregular or defective or is not properly stamped;

(*g*) where the transferee is an undesirable person and his entry in the company would be injurious to the general interest of the company.

Notice of refusal. If a company refuses to register a transfer, whether in pursuance of any power under its articles or otherwise, it shall notice of the refusal to the transferee and transferor within two months of the date on which the instrument of transfer was delivered to the company. Notice of refusal must also state the reasons for such refusal. [Sec. 111(1)]

(6) **Appeal against refusal.** In the case of public company, the transferor or the transferee may appeal to the Company Law Board against the refusal or failure of the company to register the transfer of shares within two months of the transfer being lodged with the company [Sec. 111(2)]

The appeal must be filed within two months of the receipt of the notice of such refusal. Where the company fails to give such notice, the appeal must be lodged within four months from the date on which the instrument of transfer was lodged with the company. [Sec. 111(3)]

The appeal shall be made in writing and shall be accompanied by such fee as may be prescribed. [Sec. 111(10)]

Once the appeal has been made, the Company Law Board shall send notices to the company, transferor and transferee and it shall also give them a reasonable opportunity to make their representations. On the consideration of the whole case, the Company Law Board may either reverse the decision of the company or confirm it. In the former case the company shall register the transfer within ten days of the receipt of the order. [Sec. 111(5)]

The Company Law Board has been empowered to make necessary interim orders, orders as to costs and incidental or consequential orders regarding payment of dividends or allotment of bonus or rights shares. [Sec. 111(6)]

It may be noted here that the above right of appeal against refusal is not available in the case of a private company (including a private company which is a subsidiary of a public company) and a deemed to be public company under Section 43A, to the extent the power to refuse registration is exercised under its articles to enforce the restrictions contained therein. [Sec. 111(13)]

But in the case of a private company which is not a subsidiary of a public company, the decision of the company to refuse registration of a transfer of shares can be challenged in one case. If any share of such a company are sold in execution of a decree of the court or by orders of a public authority and the company refuses to register the purchaser's name, an appeal may be made to the Company Law Board. Such appeal will be dealt with in the same manner as an appeal against a public company with the difference that the Company Law Board may give an option to the company either to accept the purchaser as a member or to get the shares purchased by a member of the company at a reasonable price,to be determined by the Company Law Board. [Sec. 111(11)]

It is important to note here that the aforesaid right of appeal against refusal to register the transfer of shares will not apply to listed securities of public companies. In the case of listed companies, the registration of transfers and their refusal shall be governed by Section 22A of Securities Contracts (Regulation) Act, 1956. These provisions are discussed in this chapter under the next heading.

The Securities Contracts (Regulation) Amendment Act, 1985

The Securities Contracts (Regulation) Act, 1956 has been amended in June, 1985. A new Section 22A has been inserted to ensure free transferability of securities of public limited companies which are listed on the stock exchange. However, the law relating to unlisted securities remains as explained above. The provisions of Section 22A are as follows:

(1) Subject to the provisions of this section, the securities of a company listed on a recognised stock exchange shall be freely transferable. However, it shall not cover a security which is not fully paid up or on which the company has a lien.

(2) Notwithstanding anything contained in its articles or in Section 82 or Section 111 of the Companies Act, 1956 but subject to the other provisions of this Section, a company may refuse to register the transfer of any of its securities in the name of the transferee on any one or more of the following grounds and on no other ground, namely:

(*a*) that the instrument of transfer is not proper or has not been duly stamped and executed or that the certificate relating to the security has not been delivered to the company or that any other requirement under

the law relating to registration of such transfer has not been complied with;

(*b*) that the transfer of the security is in contravention of any law;

(*c*) that the transfer of the security is likely to result in such change in the composition of the Board of Directors as would be prejudicial to the interests of the company or to the public interest;

(*d*) that the transfer of the security is prohibited by any order of any court, tribunal or other authority under any law for the time being in force.

(3) A company shall, before the expiry of two months from the date on which the instrument of transfer of any of its securities is lodged with it for the purpose of registration of such transfer, not only form, in good faith, its opinion as to whether such registration ought not or ought to be refused on any of the grounds mentioned in point number 2 above but also--

(*a*) if it has formed the opinion that such registration ought, not to be so refused, effect such registration;

(*b*) if it has formed the opinion that such registration ought to be refused on the ground mentioned in sub-point (*a*) of clause 2, intimate the transferor and the transferee by notice in the prescribed form about the requirements under the law which has or which have to be complied with for securing such registration; and

(*c*) in any other case make a reference to the Company Law Board and forward copies of such reference to the transferor and the transferee.

(4) Every reference under sub-point (*c*) of clause 3 shall be in the prescribed form and contain the prescribbed particulars and shall be accompained by the instrument of transfer of the securities to which it relates, the documentary evidence, if any, furnished to the company along with the instrument of transfer, and evidence of such other nature and such fees as be prescribed.

(5) On receipt of a reference, the Company Law Board shall, after causing reasonable notice to be given to the company and also to the transferor and the transferee concerned and giving them a reasonable opprotunity to make their representations, if any, in writing by order direct either that the transfer shall be registered by the company or that it need not be registered by it.

(6) Where on a reference, the Company Law Board directs that the transfer of the securities to which it relates--

(*a*) shall be registered by the company, the company will give effect to the direction within ten days of the receipt of the order as if it were an order made on appeal by the Company Law Board in exercise of the powers under Section 111 of the Companies Act, 1956;

(*b*) need not be registered by the company, the company shall, within ten days from the date of such direction, intimate the transferor and the transferee accordingly.

(7) If 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 punishable with fine which may extend to five thousand rupees.

(8) If in any reference, any person makes any 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 be punishable with imprisonment for a term which may extend to three years and shall also be liable to fine.

It will thus be seen that this amendment makes it difficult for companies whose securities are listed on a recognised stock exchange to refuse to register a properly executed transfer of any of its securities without a reference to the Company Law Board whose decision shall be final.

Certification of Transfers

Certification of transfer becomes necessary when a shareholder, who owns a number of shares, wishes to sell part of his holdings, but the company has issued him only one certificate. In such a case the transferor presents the instrument of transfer together with his share certificate before the company. The company gives an endorsement on the instrument of transfer that the share certificate pertaining to the shares has been lodged with the company. This is known as certification of transfer.

The company retains the share certificate for cancellation and the certified instrument of transfer is returned to the transferor with a balance ticket in respect of shares that he retains. This ticket is retained by the transferor and the certified instrument of transfer is given to the transferee.

Statutory recognition. Section 112 of the Companies Act recognises the practice of certification of instruments and such an instrument shall be deemed to be certified, if it bears the words "Certificate Lodged" or words to similar effect.

Effect of certification. The certification shall be taken as a representation by the company to any person acting on the faith of the certification that there have been produced to company such documents as show a *prima facie* title to the shares or debentures in the transferor named in the instrument of transfer. Such certification is not a representation that the transferor has any title to the said shares or debentures. [Sec. 112(1)]

Liability of company. Certification gives neither warranty of the

transferor's title nor any guarantee on the part of the company.[10] But where any person acts on the faith of a false certification made by a company negligently or deliberately, the company will be liable to pay damages or compensation for the loss suffered by him. However, it may be noted that the company is under no legal obligation to certify any instrument of transfer of shares at all.

A certification is deemed to be made by the company when it is signed by a person authorised to do so.

These provisions apply equally to a certification of a transfer of debentures of a company.

Forged Transfer

When an instrument of transfer does not bear the signature of the real owner of shares, any transfer made on the basis of such an instrument is called a forged transfer. In simple words, where the signature of the transferor is forged, it is a forged transfer.

Consequences of forged transfer. If the instrument of transfer is forged and the company issues a certificate to the transferee in good faith, the title of the real owner is not affected. The company must remove the name of the transferee and enter the name of the original owner in the register of members.[11]

Similarly, if the company has registered a forged transfer of debentures, the court will, on an application by the true owner of the debentures, order that name of the original owner be entered in the register of debenture-holders and the transferee would also be liable to pay to the true owner, what he might have received in respect of interest on the said debentures.

If the transferee who has become a member on a forged transfer further sells those shares, the *bona fide* purchaser for the value has no right to be registered as a shareholder. He can, however, claim damages from the company which showed that the transferor was the true owner of the shares.[12] The measure of damages will be the market value of shares at that time.

On the other hand, the company is entitled to get damages from the individual who induced it to issue a share certificate on the basis of a forged instrument.[13]

Precautions to avoid forged transfers. In order to avoid the above hardships, the company must be careful while registering the transfers.

[10]*Longman v. Bath Electric Tramways* (1965) 1 Ch. 646.

[11]*Barton v. L. and N.W. Rly. Co.* 24 Q.B.D. 77.

[12]*Re Bahia Etc. Co.* (1868) L.R. 3 Q.B. 595.

[13]*Sheffield Corporation v. Barclay 1905,* A.C. 392.

Signature of the transferor on the instrument of transfer should be compared with the specimen signatures. Notice of every transfer must be given to the transferor before it is registered by the company.

Bank Transfer

When a transferor merely signs the transfer form, without filling in the name of the transferee, and delivers it to the transferee with a share certificate, he is said to have made a blank transfer.

In this way the secutiry goes from hand to hand in the stock market before it is submitted to the company for registration. Blank transfer thus facilitates negotiability of the security. The shares can be transferred from one person to another merely by delivering the blank transfer form and the related share certificate. This saves the trouble of having a new transfer form for each transfer. When, utilimately, the shares come into the hands of a purchaser who does not wish to sell, he fills up the form by signing his own name as the transferee and sends the completed transfer form to the company for registration. It also saves stamp duty on every sale. It is only the last transferee (who wants to get himself registered as a member) who affixes the stamps and pays a registration fee to the company.

Effect of blank transfer. The delivery of a share certificate with the transfers executed in blank passes not the property in shares but as title, legal and equitable, which will enable the holder to vest himself with the shares, without risk of his being defeated by the registered owner or any other person deriving title from the registered holder.[14]

Until the requisite formalities are complied with, the transferee does not become the legal owner of the shares. Mere delivery of shares along with the blank transfer deed does not by itself make the transferee the owner of the shares.[15]

If the person to whom the share certificates and blank transfers have been handed over, gets himself registered with the company as a holder and then transfers them to an honest purchaser, the title of the latter will be protected.[16]

Blank transfers not negotiable instruments. The blank transfers are not negotiable instruments and if a person obtains them by fraud, possession cannot pass a good title to a *bona fide* purchaser for value.[17]

[14]*Colonial Bank v. Cady* (1890) 14 App. Cas. 267.

[15]*Commissioner of Wealth Tax, W. Bengal v. Smt. Sumitra Devi Jalan* (1975) Tax L.R. 436.

[16]*Abdul Vaheed v. Hasanally* 50 Bomb. 229.

[17]*Hazari Mal Sohan Lal v. Satish Chander Ghosh* (1916), I.L.R. 46, Cal. 331.

Life of blank transfers restricted. In order to curb the abuse inherent in the system of blank transfers and to limit its life, Section 108 lays down certain restrictions. The instrument of transfer must be stamped with a date by the Registrar and the instrument duly executed must be delivered to the company for registration (a) in the case of shares dealt in or quoted on a recognised stock exchange at any time before the register of members is closed for the first time after the stamped date or within twelve months of the date of presentation to the prescribed authority, whichever is later; and (b) in any other case, within two months of the date of presentation to the prescribed authority.

TRANSMISSION OF SHARES

When shares pass by operation of law from one person to another, it is known as transmission of shares. This happens when a member dies, becomes insolvent or goes insane. Transmission thus means the passing of title and right to deal with shares from one person to another by some event such as death, insolvency or lunacy. In all such cases the legal representative or the Official Assignee or Receiver or administrator appointed by the court, shall be entitled to the shares.

Nomination of shares and Debentures

By Section 109-A, inserted by the companies (Amendment) Act, 1999, every holder of shares or debentures may register the name of any person with the company in whom shares or debentures will be vested in the event of the death of the shareholder or debenture holder.

Joint-holders may together nominate a person to whom all the rights in the shares or debentures of the company shall vest in the event of death of all the joint-holders. On the death of the holder of shares or debentures, the nominee shall become entitled to all the rights in the shares or debentures of the company to exclusion of any claimant whether under will or succession unless the nomination is varied or cancelled in the prescribed manner.

Transmission of Shares under Nomination

On the death of the nominating shareholder, the nominee may either get himself registered as the holder of shares or transfer the shares. If the nominee elects to register himself as the holder of shares, he shall send to the company a notice in writing signed by him stating that he so elects and such notice shall be accompanied with the death certificate of the deceased share holder. If he elects to transfer, he shall notify the election by executing a transfer. All the limitations and restrictions with regard to the right to transfer and registration of transfer shall apply to such notice or transfer as aforesaid.

A person, being a nominee, becoming entitled to a share on transmission shall have the same right as to dividend and other advantages and privileges, as if he were the original holder, except that before registration as a member,

he shall not exercise any right as member at the meeting of the company. The board may at any time, give notice to such a person requiring him to make his election as above, and if he does not comply with such notice within ninety days, the board may thereafter withhold payment of all dividends, bonus or other moneys payable in respect of the shares until the requirements of the notice have been complied with.

Differences between Transfer and Transmission of Shares

(i) When shares pass from one person to another by a voluntary act, it is called a transfer. Where shares pass from one person to another by operation of law, it is called transmission.

(2) Transfer is a general method of transferring property in shares, whereas transmission takes place under special circumstances such as death, insolvency or lunacy.

(3) In the case of transfer, an instrument of transfer duly stamped and executed by the transferor and transferee is essential. In the case of transmission, only proof of the title of the legal representative to the shares and letter of request are required. There is no instrument of transfer.

(4) The transfer of shares is generally against consideration, but in transmission there is none.

QUESTIONS

1. Briefly outline the procedure for transfer of shares.
[Delhi, M. Com., 1976]

2. How is a transfer of shares of a company effected, and by whom? Under what circumstances may a company refuse to register such transfer? What is the remedy in case of such refusal? *[I.C.W.A., July 1965]*

3. Explain the provisions relating to transfer and transmission of shares.
[Kerala, B. Com., 1973]

4. Explain the provisions of the Companies Act regarding transfer and transmission of shares. What is the effect of a forged transfer?
[Meerut, M. Com., 1965]

5. Distinguish between transfer and transmission of shares and describe the procedure for the transfer of shares. *[I.C.W.A., June 1974]*

6. How can a valid transfer of shares be made? When can a company refuse to register a transfer of shares? What are the remedies available to the aggrieved party when the transfer of shares is wrongfully refused by the company?
[Delhi, B. Com. (Hons.), 1986]

7. What is a blank transfer? State the procedure prescribed by the Companies Act to curb the practice of holding shares under blank transfers.
[Company Secretary (Final), April 1972]

8. What is forged transfer? State the legal position of the respective parties involved.

9. Write a short note on restrictions on blank transfers.

[*Delhi, M. Com., 1977, 79*]

10. What is transmission of shares? Explain the regulations regarding the transmission of shares as per Table A. [*Kerala, B. Com., 1974*]

PRACTICAL PROBLEMS

1. *A* buys 200 shares in a company from *B* on the faith of a share certificate issued by the company. *A* tenders to the company a transfer to himself from *B* duly executed together with *B*'s share certificate. The company discovers that the certificate in the name of *B* has been fraudulently obtained and refuses to transfer. Advise *A*. Is he entitled to get the registration of transfer?

[*C.A. (Inter) May, 1974*]

2. Mr *K* purchased from Mr *Y*, 1,00,000 fully paid-up equity shares of Rs 10 each, of *ABC* Ltd, and delivered the transfer deed together with the share scrips to the company on 30th April 1970 with an application of even date seeking registration of the shares in his own name. *ABC* Ltd., neither registered the shares in the name of Mr *K* nor communicated the refusal to register the transfer on or before 30th June 1970. An appeal under Sec. 111 of the Companies Act, 1956, was made to the Central Government in December 1972. Is the application valid?

[*Company Secretary (Final), April 1974*]

3. *A* applied for transfer in respect of certain shares in his name. *A* board meeting was held and the transfer documents were considered. The board was evenly divided with no casting vote. Should the transfer be registered?

4. *A* is the registered holder of certain shares in the books of the company. By fraud or theft, *B* obtains possession of *A*'s share certificate, forges *A*'s signatures to the transfer and succeeds in getting himself registered in the books of the company as holder of shares and obtains from the company a new certificate made out in his name. *B* then sells his shares to *C*, an innocent purchaser, who, in reliance upon *B*'s certificate, buys the shares in good faith and without notice of *B*'s fraud. The company then registers *C* as holder of the shares and issues a certificate to him. The fraud is subsequently discovered by *A* and brought to the notice of the company. Discuss the legal position.

12

MANAGEMENT OF A COMPANY

DIRECTORS

A company is an artificial person created by law. It does not have any physical existence. It exists only in the eyes of the law. As such it cannot act by itself and acts instead through human agency. The persons through whom it acts and by whom the business of the company is conducted are known as directors. The directors of a company are collectively known as the "board of directors" or the "board". Section 291(1) lays down that 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 authorised to exercise and do.

Definition. Section 2(13) defines a director as any person occupying the position of a director, by whatever name he is called. It means that a person who performs the duties of a director will be known as a director irrespective of the name by which he is called. It may be pointed out here that a director is a person who is responsible for direction, control and management of the affairs of a company. Since a company is an artificial person, it is the directors who exercise the powers of a company on ths behalf. Jessel, M.R. observed: "It does not matter what you call them so long as you understand what their real position is, which is that they are really commercial men managing a trading concern for the benefit of themselves and of all the shareholders in it."[1]

According to Section 303 [Explanation (1)] any person, in accordance with whose directions or instructions, the board of directors of a company is accustomed to act, shall be deemed to be a director of the company.

Only individuals to be directors. No body corporate, association or firm shall be appointed director of a company. Only an individual shall be appointed as one. (Sec. 253)

Number of Directors

Minimum and maximum number of directors. Every public company

[1]*Re Forest of Dean Coal Mining Co.*, (1878) 10 Ch. D. 450.

shall have at least three directors and every other company (including deemed to be public company under Section 43-A) shall have at least two. (Sec. 252)

Subject to this minimum number of directors, the articles of a company may fix the minimum and maximum number of directors for its board of directors.

Right to increase the number of directors. Within the limits prescribed by the articles, the company may increase or reduce the number of its directors by an ordinary resolution in general meeting. (Sec. 258)

In the case of a public company or a private company which is a subisidiary of a public company, any increase which is beyond the limit fixed by the articles must be approved by the Central Government except where the increase in the number of its directors does not make the total number of directors more than twelve. (Sec. 259)

Appointment of Directors

(1) **First directors.** First directors are usually named in the articles. Alternatively, the articles may provide that the number of directors and the names of the first directors shall be determined in writing by the subscribers of the memorandum or by a majority of them

If the articles neither contain the names of the directors nor any provision for appointing them, subscribers of the memorandum who are individuals shall be deemed to be the directors of the company. They shall hold office until directors are duly appointed in the first annual general meeting. (Sec. 254)

(2) **Subsequent appointment of directors by members.** Section 255 provides that subsequent directors shall be appointed by the company in general meeting. In case of a public company or of a private company which is a subsidiary of a public company, at least two-thirds of the total number of directors shall be those who shall retire by rotation. This means that of the total number of directors only one third can hold permanent directorships. However, the articles may provide for the retirement of all directors at every annual general meeting. In the case of a private company, all directors can be permanent if the articles so provide.

Retirement of directors by rotation. At every subsequent annual general meeting, one-third (or the number nearest to one-third) of such directors as are liable to retire by rotation, shall retire from office. Directors who retire by rotation at every annual general meeting shall be those who have been longest in office since their last appointment. As between persons who became directors on the same day, those who are to retire shall be determined by lot, in default of any agreement among

themselves. [Sec. 256(1)(2)]

Reappointment of retiring directors. At the annual general meeting at which a director retires by rotation, the company may fill the vacancy by appointing the retiring director or some other person in his place. If the place of the retiring director is not filled and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned till the same day in the next week, at the same time and place. If at the adjourned meeting also, the place of the retiring director is not filled and the meeting has also not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been reappointed at the adjourned meeting, unless (*a*) a resolution for reappointment of such a director has been put to the meeting and lost; (*b*) the retiring director has, by a notice in writing addressed to the company or its board of directors, expressed his unwillingness to be so reappointed; (*c*) he is not qualified or is disqualified for appointment and (*d*) a special or ordinary resolution is required for his appointment or reappointment. [Sec. 256 (3)(4)]

Appointment of persons other than retiring directors. A person who is not a retiring director shall be eligible for appointment to the office of director if he or some member intending to propose him has given not less than fourteen day's notice to the company before the date of the meeting. The person sending such notice is also required to deposit Rs 500 with the company which shall be refunded to the depositor if the person gets elected as a director. Otherwise the same will be forfeited by the company. The company shall inform its members of his candidature at least seven days before the date of the meeting by serving individual notices on members. If this is not possible, the company shall advertise such candidature not less than seven days before the meeting in at least two newspapers circulating in the place where the registered office of the company is located. (Sec. 257)

Filing of consent for directorship with the company and the Registrar. Every person (other that a director retiring by rotation) whose name is proposed as a candidate for the office of a director shall sign and file with the company his consent in writing to act as a director, if appointed. Similarly a person who has been appointed as a director for the first time is required to sign and file with the Registrar his consent in writing to act as such within thirty days of his appointment. (Sec. 264)

Appointment of directors to be voted on individually. Every director shall be appointed by a separate resolution put to vote separately. An appointment of two or more persons as directors of the company by a single resolution is not valid unless a resolution that it shall be so made has first been adopted unanimously by the members. It may also be noted

here that appointments of directors are made by ordinary resolutions passed in the general meetings of the shareholders. (Sec. 263)

Proportional representation for the appointment of directors. Section 265 provides that the articles of a company may provide for the appointent of not less than two-third of the total number of the directors according to the principle of proportional representation, whether by the single transferable vote or by a system of cumulative voting or otherwise. Such appointments can be made once every three years. This section intends to provide the minority with an opportunity to place its nominee or nominees on the board.

(3) **Additional directors.** If permitted by the articles, the board of directors may appoint additional directors. Such additional directors shall hold office only up to the date of the company's next annual general meeting. The number of the directors and additional directors together shall not exceed the maximum strength fixed for the board by the articles. (Sec. 260)

(4) **Casual vacancies.** If the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may be filled by the board of directors at a meeting of the board, unless the articles of the company prescribe a different procedure. Any person so appointed shall hold office till director in whose place he is appointed would have held office, had it not been vacated. (Sec. 262)

(5) **Alternate directors.** If authorised by its articles or by a resolution passed by the company in general meeting, the board of directors may appoint an alternate director where the original director is likely to be absent for a period of not less than three months from the state in which the meetings of the board are ordinarily held.

An alternate director shall not hold office as such for a period longer than that permissible to the original director in whose place he has been appointed, and shall vacate office if and when the original director returns to the state in which meetings of the board are ordinarily held. (Sec. 313)

(6) **Appointment of directors by third parties.** Section 255 provides that one-third of the total number of directors of a public company or a private company which is a subsidiary of a public company may be appointed by relevant parties on a non-rotational basis, if the articles so authorise. Articles may give such power to debenture holders, a banking company or a financial corporation that has advanced loans to the company.

(7) **Appointment by the Central Government.** In the case of oppression or mismanagement, the Central Government has the power

to appoint such number of directors on the board of directors of a company as the Company Law Board may direct to effectively safeguard the interests of the company or its shareholders or the public interest. Such persons shall hold office as directors for not more than three years on any one occassion. The Company Law Board can take up the matter for such direction on a reference made to it by the Central Government or on the application of at least one hundred members of the company or of members holding at least one-tenth of the total voting power.

A person appointed by the Central Government to hold office as a director shall not be required to hold any qualification shares nor shall he be liable to retire by rotation. However, the Central Government may remove any such director from his office and another person be appointed by that Government in his place to hold office as a director. For the purpose of reckoning two-third or any other proportion of the total number of directors of the company, a director appointed by the Central Government shall not be taken into account.

No change in the board of directors of a company on which the Central Government has appointed a director or directors shall have effect unless approved by the Company Law Board. (Sec. 408)

Number of Directorships

Limitation on number of directorships. No person shall hold the office of director at the same time in more than twenty companies. Where a person already holding the office of director in twenty companies, is appointed director of any other company, the appointment shall not take effect unless within fifteen days such person effectively vacates his office as director from any of the companies in which he is already a director. His appointment shall become void immediately on the expiry of the fifteen days if he does not effectively vacate his offce as director in any of the other companies.

Exclusion of certain directorships. In calculating the number of twenty companies, the following companies shall be excluded: (*a*) a private company which is neither a subsidiary nor a holding of a public company; (*b*) an unlimited company; (*c*) an association not carrying on business for profit or which prohibits the payment of a dividend; and (*d*) a company in which such an individual is only an alternate director.

Penalty. Any person who holds office or acts as a director of more than twenty companies shall be punishable with fine which may extend to five thousand rupees in respect of each of those companies after the first twenty. (Secs. 275 to 279)

Share Qualification

The Companies Act does not provide for any share qualification for any director. However, Regulation 66 of Table A provides that the qualification of a director shall be holding of at least one share in the company. The articles of a company generally provide for such qualification shares so that directors may have personal interest in the company.[2]

Quantum and time for obtaining qualification shares. Where the articles provide for qualification shares, Section 270 requires that such qualification shares should be obtained within two months of the appointment as director. Any provision in the articles of the company shall be void insofar as it requires a person to hold the qualification shares before his appointment as a director or to obtain them within a shorter time than two months after his appointment as such. It further provides that the nominal value of shares shall not exceed five thousand rupees or the nominal value of one share where it exceeds five thousand rupees.

Consequences of non-compliance. If a director fails to obtain his qualification shares within two months of appointment or thereafter ceases to hold them at any time, he shall cease to be a director. [Sec. 283(1)]

If, after the expirty of the said period of two months, any person acts as a director of the company when he does not hold the qualification shares, he shall be punishable with a fine which may extend to fifty rupees for every day between such expiry and the last day on which he acted as a director. (Sec. 272)

Other requirements. The holding of a share warrant shall not be deemed to be sufficient qualification. Only shares must be held. Until the required number of shares are registered in the name of the director, he is not qualified.[3]

Unless the articles otherwise provide, a joint holding will be sufficient for share qualification.[4]

Disqualifications of Directors

Section 274 provides that a person shall not be capable of being appointed a director of a company, if

(*i*) he has been found to be so unsound mind by a court of competent jurisdiction and the finding is in force;

(*ii*) he is an undischarged insolvent;

[2]*Archer' Case* (1892) 1 Ch. 322.

[3]*Channel Collieries Trust Ltd. v. Dover Light Railway Co.,* (1914) 2 Ch. 506.

[4]*Grundy v. Briggs* 1910, 1 Ch. 444.

(*iii*) he has applied to be adjudicated as an insolvent and his application is pending;

(*iv*) he has been convicted by a court of an offence involving moral turpitude and sentenced to imprisonment for not less than six months and a period of five years has not elapsed from the date of expiry of the sentence;

(*v*) he has not paid any call in respect of shares of the company held by him and six months have elapsed from the last day fixed for such payment; and

(*vi*) he has been disqualified by an order of the court under Section 203 of the Act for the purpose of preventing fraudulent persons from managing companies.

Where a person has been removed from the office of director by the Central Government under Section 388-E, he becomes disqualified to hold the office of director of any company for five years from the date of the order of removal.

Removal of disqualifications by Central Government. The Central Government by notification in the Official Gazette may remove the disqualifications mentioned in clauses (*iv*) and (*v*).

Additional disqualifications in case of private companies. An independent private company may add any other additional disqualifications in its articles for the appointment of directors.

But a public company and its subsidiary private compay cannot adopt any other additional disqualifications in its articles for the appointment of directors.[5]

Vacation of Office by Directors

The office of a director shall become vacant if,

(*i*) he fails to obtain qualification shares within two months of his appointment, or at any time thereafter ceases to hold qualification shares;

(*ii*) he is found to be of unsound mind by a court of competent jurisdiction;

(*iii*) he applies to be adjudicated as an insolvent;

(*iv*) he is adjudged an insolvent;

(*v*) he is convicted by a court of an offence involving moral turpitude and is sentenced in respect thereof to imprisonment for not less than six months;

(*vi*) he fails to pay any call in respect of shares of the company held by him within six months of the last date fixed for payment of the call, unless

[5]*Cricket Club of India v. Madhav L. Apte.* (1975) 45 Comp. Cas. 574.

Central Government has, by notification in the Official Gazette, removed the disqualification incurred by such failure;

(*vii*) he absents himself from three consecutive meetings of the board of directors or from all meetings of the board for a continuous period of three months, whichever is longer, without obtaining leave of absence from the board;

(*viii*) he (whether by himself or by any person for his benefit or on his account), or any firm in which he is a partner or any private company of which he is a director, accepts a loan or guarantee or security for a loan from the company in contravention of Section 295;

(*ix*) he makes a contract with the company in contravention of Section 299, that is, without disclosing his interest in the contract;

(*x*) he becomes disqualified under Section 203 of the Act for the purpose of preventing fraudulent individuals from managing companies;

(*xi*) he is removed in accordance with Section 284;

(*xii*) he was appointed a director by virtue of his holding any office or other employment in the company, and he ceased to hold such office or other employment in the company.

Penalty for non-compliance. If a person functions as a director and knows that this office has become vacant on account of any of the above disqualifications, he shall be punishable with a fine which may extend to five hundred rupees for each day on which he so functions as a director.

Additional grounds in case of private companies. An independent private company may provide additional grounds in its articles for vacation of the office of a director. (Sec. 283)

Removal of directors

A director may be removed from his office (*a*) by the shareholders (Sec. 284); (*b*) by the Central Government (Secs. 388B to 388E); and (*c*) by the Company Law Board. (Sec. 402)

(1) **Removal by shareholders.** Section 284 provides that a company may, by ordinary resolution, remove a director from his office before the expiry of his period of office. But a director appointed by the Central Government under Section 408 or a director of a private company holding office for life on the first day of April, 1952 or a director appointed under the system of proportional representation under Section 265 cannot be removed by the company.

Requirement of special notice. Spectial notice shall be required of any resolution to remove a director under this section. This means that notice of the intention to move the resolution should be given to the company not less than fourteen days before the meeting.

On receipt of notice of a resolution to remove a director the company

shall forthwith send a copy of it to the director concerned and the director (wheter or not he is a member of the compay) shall be entitled to be heard on the resolution at the meeting.

Right of director to make representation. The director concerned may also make a representation and require the company to circulate it among the members. In such a case, the company shall state the fact of a representation having been received in the notice of the resolution given to its members and also send a copy of the representation to every member of the company, unless it is too late for it to do so. If, for any reason a copy has not been sent, the director may require that the representation be read out at the meeting. Such representations need not be sent out and need not be read out at the meeting, if the Company Law Board is satisfied that the rights under this section are being abused to secure needless publicity for defamatory matter.

Filling up of vacancy. A vacancy created by removal of a director may be filled at the same meeting provided special notice of such intention has been given earlier. A director so appointed shall hold office until the date up to which the director removed would have done so had he been not removed. If the vacancy is not filled at the meeting, the board shall fill it as if it were a casual vacancy under Section 262. But in no case shall the director removed from office be reappointed.

Right to compensation. A director removed under this section shall not be deprived of any compensation or damages payable to him in respect of the termination of his appointment as director or of any appointment terminating with that as director.

This section is intended to empower the share holders to remove a director from office even before the expiry of his period of office where his continuance in the office of director is not in the interest of the company.

The resolution removing the director need not state reasons for his removal.

(2) **Removal by the Central Government.** The Central Government has been empowered to remove managerial personnel from office on the recommendation of the Company Law Board under Section 388B to 388E. The Central Government is empowered to make reference to the Company Law Board against any managerial personnel, where in the opinion of the Central Government, there are circumstances suggesting:

(*a*) that any person concerned in the conduct and management of the affairs of a company has been guilty of fraud, misfeasance, persistent negligence in carrying out the obligations and functions under the law or breach of trust; or

(*b*) that the business of a company is not or has not been conducted

and managed by such person in accordance with sound business principles or prudent commercial practices; or

(*c*) that a company is or has been conducted and managed by such person in a manner which is likely to cause or has caused serious injury or damage to the interest of the trade, industry or business to which such company pertains; or

(*d*) that the business of a company is or has been conducted or managed by such person with intent to defraud its creditors, members or any other persons or otherwise for a fraudulent or unlawful purpose or in a manner prejudicial to public interest.

The Central Government may state a case against the person and refer the same to the Company Law Board for an inquiry into the case and record a decision as to whether or not such a person is fit to hold the office of a director or any other office connected with the conduct and management of any company.

In the above circumstances, the power of the Central Government to refer a case to the Company Law Board against any managerial personnel is coupled with duty and that duty must be performed when certain circumstances exist. In such circumstances, the Central Government has no choice but to make a reference.[6]

Effects of removal order. After the case is heard by the Company Law Board, it shall record its decision. If the decision is against the respondent, the Central Government may, by order, remove him from the office of director or any other office connected with the conduct and management of the affairs of the comppany.

Any person against whom an order of removal from office is made shall not hold the office of a director or any other office connected with the conduct and management of the affairs of any company during a period of five years from the date of the order of removal, unless the period is remitted by the Central Government with the previous concurrence of the Company Law Board.

Again, no compensation shall be payable to a person removed from office under this section.

Central Government's approval required to fill up the vacancy. The company may, with the previous approval of the Central Government, appoint another person to that office in accordance with the provisions of the Act.

(3) **Removal by the Company Law Board.** Where an application has been made to the Company Law Board for prevention of oppression and mismanagement (Secs. 397 and 398), the Company Law Board may

[6]*Alok Prakash Jain v. Union of India* (1973) 43. Comp. Cas. 68.

provide for the termination or setting aside of any agreement between the company and its directors. Such an order shall have the effect of the removal of directors from their office. (Sec. 402)

Effect of removal order. Such a director or the managing director shall not be entitled to claim compensation or damages for loss of office. Similarly, he shall not be entitled to hold any managerial office for a period of five years from the date of the Company Law Board's order. [Sec. 407(1)]

Resignation of Office by Directors

There is no provision in the Companies Act, 1956 relating to resignation by a director. The articles may provide that a director may resign his office by sending a notice or resignation at any time in the manner provided in the articles. In such a case, the resignation will take effect without any need for its acceptance by the board of directors or the company in the general meeting. Acceptance of resignation will also not be necessary where the resignation states that it is to take effect immediately, unless the articles or any provision of law makes acceptance a necessary condition.

In the absence of any provision in the articles regarding resignation by a director, a director can resign at any time by giving a reasonable notice to the company, no matter whether the company accepts it or not."[7]

In the absence of any provision in the articles, it is well settled that a resignation once made takes effect immediately when intention to resign is made clear.[8]

The resignation may be oral.[9] Once a director has resigned, he is not entitled to withdraw except with the consent of the company or the directors of the company.[10]

It may be noted here that a resignation will not relieve a director from any liabilities and obligations which he may have incurred while in office.

Legal Position of Directors

The Companies Act does not define the position of directors. Sectrion 2(13) defines a director as any person occupying the position of a director, by whatever name called. There has been considerable controversy regarding the exact legal position of directors. Directors have been described as trustees of the company as well as agents of the company by

[7]*Abdul Haq. v. Katpadia Industries Ltd.* A.I.R. (1960) Mad. 482.
[8]*T. Murari v. State* (1976) 46 Comp. Cas. 613 (Mad.).
[9]*Latchford Premier Cinema Ltd. v. Ennion* (1931) 2 Ch. 409.
[10]*Glossop v. Glossop* (1907) 2 Ch. 370.

some, while still others call them managing partners of a going concern. In this connection Bowen L.J. observed: "Directors are described sometimes as agents, sometimes as trustees and sometimes as managing partners. But each of these expressions is used not as exhaustive of their powers and responsibilities, but as indicating useful points of view from which they may, for the moment and for the particular purpose, be considered.[11] In another case it was observed: "The directors are mere trustees or agents of the company--trustees of the company's money and property: agents in the transactions which they enter into on behalf of company.[12]

Directors as trustees. Although directors are not, properly speaking, trustees, yet directors have been described as trustees of the company. This is because, like trustees, directors in the performance of their duties stand in a fiduciary position in relation to the company. The courts expect from directors the same degree of integrity and standard of conduct as from a trustee.

Directors as trustees of the company's money and property. Directors are trustees of the company's money and property and they are bound to deal with capital under their control as a trust. They must act in good faith and exercise their powers in the interest of the company. As Lindley L.J. observed in *Re Lands Allotment Co.*: "Although directors are not, properly speaking, trustees, yet they have always been considered and treated as trustees of money which comes to their hands or which is actually under their control; and ever since joint stock companies were invented, directors have been held liable to make good moneys which they have misapplied upon the same footing as they were trustees.[13]

For instance, where the directors improperly paid dividend without proper investigation of a company's trading position and profit and loss account, they were held liable to make the amount good to the company.[14]

Similarly, since directors occupy a fiduciary position, they should not make any secret profits. Where the directors make a secret profit, they shall be bound to account to the company for it.[15]

Directors as trustees in respect of powers entrusted to them. The directors are also trustees in respect of powers entrusted to them. They must exercise these powers *bona fide* in the interest of the company. Examples of such powers are: (*a*) the power to make a call,[16] (*b*) the power of

[11]*Imperial Hydropathic Co. v. Hampson* (1882) 23 Ch. D. 1.
[12]*Great Eastern Rly. v. Turner* (1872) L.R. 8 Ch. App. 149.
[13](1894) 1 Ch. at p. 631.
[14]*Rance's Case* (1870) L.R. Ch. App. 104.
[15]*Regal (Hastings) Ltd. v. Gulliver* (1942) 1 All. E.R. 378.
[16]*Alexander v. Automatic Telephone Co.* (1900) 2 Ch. 56.

receiving payment of calls in advance,[17] (*c*) the power of employing the funds of the company.[18] (*d*) the power of forfeiting shares,[19] (*e*) the power of approving transfer of shares,[20] and (*f*) the power of issuing the unissued shares of the company and making allotments thereof.[21]

Trustees of the company and not of individual shareholders. It should further be noted that directors occupy a fiduciary relationship only in relation to the company and not in relation to an individual shareholder. Directors are not trustees for any particular shareholder. This point is well illustrated by the case *Percival v. Wright.*[22] In this case directors bought shares from a shareholder when negotiations were being held by them for sale of the company at a very high price. They did not disclose this fact to the shareholder. It was held that the shareholder could not repudiate the contract on that ground.

Directors not trustees in the legal sense. Although directors have been loosely described as trustees, yet they are not trustees in the legal sense of the term. In *Smith v. Anderson,*[23] James L.J. observed: "A trustee is man who is the owner of property and deals with it as principal, as owner and as master, subject only to an equitable obligation to account to some persons to whom he stands in relation of a trustee. The office of director is that of a paid servant of the company. A director never enters into a contract for himself, but he enters into a contract for his principal, that is, for the company of which he is a director or for whom he is acting."

The position of directors as trustees can be briefly stated as follows:

(*i*) Directors are not trustees in the legal sense of the term.

(*ii*) However, they do occupy a fiduciary position in relation to the company and they are considered trustees with respect to the company's property and money. They are also trustees as regards powers entrusted to them. They must exercise these powers *bona fide* in the interest of the company and they are accountable for secret profits made by them, if any.

(*iii*) They are not trustees of individual shareholders.

Directors as agents. It has already been noted that a company is an artificial person created by law, and has no physical existence. It has to act through its directors who are its agents. The relationship between a company and its directors is that of a principal and its agent, and, as such, the general principles of law governing principals and agents regulate the

[17]*Sykes' Case* (1872) L.R. 13 Eq. 255.
[18]*Re Oxford Building Society* (1886) 35 Ch. D. 502.
[19]*Harris v. North Devon Rly.* (1855) 20 Beav. 384.
[20]*Bennett's Case* (1854) 5 De. G.M. & G. 284, 297.
[21]*Piercy v. S. Mills & Co.* (1920) 1 Ch. 77.
[22](1902) 2 Ch. 421.
[23](1880) 15 Ch. D. 247.

relationship between a company and its directors. In this connection Cairns L.J. observed: "They are merely agents of the company. The company itself cannot act in its own person, for it has no person, it can only act through directors and the case is, as regards those directors, merely the ordinary case of principal and agent, for whenever an agent is liable, those directors would be liable. Where the liability would attact to the principal, and the principal only, the liability is the liability of the company."[24]

In order to bind the company, the directors must act in the name of the company and within the scope of their authority. If the directors enter into a contract which is beyond their powers but within the powers of the company, the company, like any other principal, may ratify it.[25] If the directors enter into a contract which is *ultra vires* the company, the company cannot ratify it and neither the company nor the directors are liable on it. However, the directors may be held liable for breach of implied warranty of authority.[26]

As agents, directors must act honestly and conduct the affairs of the company with reasonable care and diligence.[27]

Interested directors. In order to protect any conflict of interest of a company and a director, Sections 299 and 300 regulate the relationship between the company and its directors. Under Section 299, if a director is interested in any contract or arrangement proposed to be entered into by the company, he must disclose his interest at the first meeting of the board held after he became so interested. Section 300 prohibits such director from taking part in discussions or voting on such a contract or arrangement.

Powers of directors wider than those of an ordinary agent. If may further be noted that the powers of directors are much more than those of an ordinary agent. Once the directors are elected, they derive certain powers from the articles and the Companies Act. Such powers can be exercised by them independently without any interference from or consultation with shareholders. However, in the case of an agency, the agent is always controlled and guided by the principal.

Directors as managing partners. Directors have been described as managing partners because, on the one hand, they are entrusted with management and control of the affairs of the company, and on the other, they are usually important shareholders of the company. It is more nearly

[24]*Ferguson v. Wilson* (1866) L.R. 2 Ch. App. 77.

[25]*Grant v. United Kingdom Switchback Rail Co.* (1889) 40 Ch. D. 135.

[26]*Weeks v Propert* (1827) C.R. 8 C.P. 427.

[27]*Re City Equitable Fire Insurance Ltd.*, 1925 1 Ch. 407.

true to say that they are in the position of managing partners appointed to fill that post by a mutual arrangement between all the shareholders.

Directors as officers. Under Section 2(30) of the Companies Act, directors are officers of the company. As officers, they may be held liable if the provisions of the Companies Act are not complied with.

From the above discussion, one can conclude in the words of Jessel M.R. that," Directors have sometimes been called trustees or commercial trustees, and sometimes they have been called managing partners; it does not matter much what you call them so long as you understand what their real position is which is that they are really commercial men managing a trading concern for the benefit of themselves and of all the shareholders in it.[28]

Managerial Remuneration

Prima facie, directors have no right to claim remuneration for their services.[29] However, the articles of the company generally provide for such remuneration.

Once the articles provide for the payment of remuneration of directors, it operates as an authority to the directors to pay remuneration from the funds of the company. Payment of remuneration is not restricted to payment out of profit.[30] Although articles do not constitute a contract between the company and the directors, yet where the articles provide expressly for payment of remuneration to directors, such express provision operates as an offer accepted by the directors and provides the terms on which the directors are serving the company.[31] They can themselves sue for their remuneration which is agreed upon impliedly or expressly.[32]

The amount of remuneration of directors was held to be a matter of internal management.[33]

Determining directors' remuneration. Section 309(1) provides that remuneration payable to directors shall be determined either by the articles or by a resolution passed by the company in general meeting. The articles may require the resolution to be a special resolution. However, the amount of remuneration and the mode of payment should be in accordance with the provisions of Secions 198 and 309.

[28]*Re Forest of Dean Coal Mining Co.* (1878) 10 Ch. D. 450.
[29]*Dunston v Imperial, Etc. Co.* (1832) 3 Bar & Ad. 125.
[30]*Harvey Lewis* (1872) 26. L.T. 673.
[31]*Swabey v Port Darwin Gold Mining Co.* (1889) 1 Meg. 385.
[32]*Orton v Cleveland, Etc. Co.* (1865) 3 H. & C. 868.
[33]*Normandy v Ind. Coope and Co. Ltd.* (1908) 1 Ch. 84.

Overall maximum managerial remuneration. Section 198 provides that the total managerial remuneration payable by a public company or a private company which is subsidiary of a public company in respect of any financial year shall not exceed eleven per cent of the net profits of that company for that year. The term 'managerial remuneration' means remuneration payable to directors [including managing/whole-time director(s)], and manager.

But sometimes a company may make no profits or make inadequate profits in a financial year. In such a case, the company may make payment of minimum remuneration to a managerial personnel with the approval of the Central Government. However, the approval of the Central Government shall not be required for payment of minimum remuneration to a managerial personnel so long as the appointment and remuneration are in accordance with Schedule XIII (Sec. 269). Schedule XIII has been introduced by the Companies (Amendment) Act, 1988. It lays down conditions for appointment and remuneration of managerial personnel without the approval of the Central Government. The Central Government has amended Schedule XIII twice since 1988 and the amended Schedule has become effective w.e.f. 1st February, 1994. Schedule XIII, *inter-alia*, provides that in the event of loss or inadequacy of profits in any financial year, a company may pay remuneration to a managerial person varying from Rs. 4,80,000 per annum or Rs. 40,000 per month to Rs 10,50,000 per annum or Rs. 87,500 per month, depending upon the effective capital of the company specified in Section II of Part II of Schedule XIII. Such remuneration may be paid as minimum remuneration without the approval of the Central Government so long as the appointment and remuneration are in accordance with Schedule XIII (Sec. 269).

Meaning of the term 'remuneration'. In order to make the limit of eleven per cent more effective, Section 198 provides that 'remuneration' shall include the expenditure by the company-

(i) in providing any rent-fee accommodation or any other benefit or amenity in respect of accommodation free of charge;

(ii) in providing any other benefit or amenity free of charge or at a concessional rate;

(iii) in respect of any obligation or service which otherwise would have been incurred by the directors or manager; and

(iv) to effect any insurance on the life for any director or manager or his spouse or child or to provide any pension, annuity or gratuity for any of them. (Explanation to Sec. 198)

However, the above limit of eleven per cent shall not include any fees payable to directors for attending meetings of board or of committee of the board. [Sec. 198(2)]

Remuneration of managing or whole-time directors. A managing or

whole-time director may be paid remuneration either by way of monthly payment or at a specified percentage of the net profits of the company or partly by one way and partly by other. But such remuneration shall not exceed five per cent of the net profits for one such director and if there is more than on such director, ten per cent for all of them together. [Sec. 309(3)]

No director of a company who is in receipt of any commission from the company and who is either in the whole-time employment of the company or a managing director shall be entitled to receive any commission or other remuneration from any subsidiary of such company. [Sec. 309(6)]

Remuneration of directors. A director who is neither in the whole-time employment of the company nor a managing director may be paid remuneration either (a) by way of a monthly, quarterly or annual payment with the approval of the Central Government; or (b) by way of commission if authorised by special resolution of the company. Where the company has a managing or whole-time director or manager, the total remuneration paid to one or more directors should not exceed one per cent of the net profits of the company. Where the company does not have any such managerial personnel, the total remuneration paid to one or more directors shall not exceed three per cent of the net profits of the company.

However, the company in general meeting with the approval of the Central Government may sanction a higher percentage. [Sec. 309(4)]

Payment of professional services. Section 309(1), as amended by the Companies (Amendment) Act, 1965, provides that remuneration payable to a director in accordance with above rules shall include any remuneration payable to such a director for services rendered by him in any other capacity unless *(a)* the services rendered are of a professional nature; and *(b)* in the opinion of the Central Government the director possesses the requisite qualifications for professional practice.

Payment of sitting fee. For the purpose of the first proviso to Section 310, the amount of remuneration by way of fee for each meeting of the board of directors or a committee thereof, shall not exceed the sum of Rs. 2,000. Within this ceiling of Rs. 2,000, a company shall have discretion to pay such amount by way of sitting fee as may be considered appropriate.

However, the approval of the Central Government is required for paying sitting fee exceeding the above ceiling.

Increase in remuneration. Section 310, as amended by the Companies (Amendment) Act, 1988, provides that in case of a public company

or its subsidiaries, the remuneration of directors cannot be increased in any way without the approval of the Central Government except in those cases where Schedule XIII is applicable and the proposed increase is in accordance with the conditions specified in the Schedule.

Excess payment. If any director receives by way of remuneration any sums in excess of the limits stated above, he will have to refund such sum to the company and until such sum is refunded, he will hold it in trust for the company. The company cannot waive the recovery of any such sum without the approval of the Central Government. [Sec. 309(5)]

Prohibition of tax-free payment. A company is prohibited from making any tax-free payment of remuneration to its officers or employees. (Sec. 200)

It is to be noted that the above provisions do not apply to a private company unless it is a subsidiary of a public company. [Sec. 309(9)]

The overall picture of managerial remuneration is shown in the chart given below:

Chart Showing The Limits Regarding Managerial Remuneration

Different categories of managerial personnel entitled to remuneration	*Maximum percentage of annual net profits*
1	2
(1) Over all limit for total remuneration to all directors, managing director(s) or manager and/or whole-time director(s).	11 per cent
(2) All directors when the company has managing director(s) or manager and/or whole-time director(s)	1 per cent
(3) All directors when the company does not have managing director(s) or manager and/ or whole-time director(s)	3 per cent
(4) Managing director (when there is one managing director)	5 per cent
(5) Manager (there cannot be more than one manager)	5 per cent
(6) Whole-time director (when there is one such director). A whole-time director may be appointed alongwith managing director or a manager. However, simultaneous ap-	5 per cent

pointment of a managing director and manager in a company is prohibited.	
(7) Managing directors or whole-time directors (when there are more than one of either category or of both categories)	10 per cent

Power of the Central Government to Fix Remuneration

The companies (Amendment) Act, 1974, inserted a new section 637-AA. This section empowers the Central Government to fix the remuneration of managerial personnel within the limits specified in this Act, at such amount or percentage of the profits of the company, as it may deem fit. While fixing the remuneration, the Central Government shall have regard to (*a*) the financial prosition of the company; (*b*) the remuneration or commission drawn by the individual concerned in any other capacity, including his capacity as sole selling agent; (*c*) the remuneration or commission drawn by him from any other company; (*d*) professional qualifications and experience of the individual concerned. and (*e*) public policy relating to the removal of disparities in income.

Administrative Ceilings on Managerial Remuneration

As a socio-economic measure, the Central Government framed certain ceilings in respect of remuneration payable to managerial personnel in a public limited company. The first limits were fixed by a circular issued on 11 November 1969, which were later amended in November 1978 and October 1979.

Validity of revised guidelines. The managerial remuneration guidelines issued in 1969 and revised in 1979 by the Central Government have been struck down as unconsitititutional by the Delhi High Court in *Mahindra and Mahindra Limited and Others v. Union of India*[34] and by the Gujrat High Court in *Cibatul Limited and Others v. Union of India*[35] on the ground of non-existence of public policy relating to the removal of disparities in incomes. It has been pointed out that having introduced Section 637-AA in the Act, the Government was bound to follow the provisions of that section. As public policy for removing disparities in incomes was not formulated, sub-clause (*e*) of that section, which requires Government to formulate public policy, could not be implemented.

The courts also examined the guidelines with the object of deciding whether they took into account the factors enumerated in clauses (*a*) to (*d*) of Section 637-AA, viz. the financial position of the company, the

[34](1983) 53 Comp. Cas. 409 (Delhi).
[35](1980) 50 Comp. Cas. 437 (Guj.)

qualification and experience of the director concerned, the remuneration or commission drawn by him from any other company, etc. As the guidelines did not take these into account, the courts came to the conclusion that they were violative of the law.

The Government have gone in appeal in the Supreme Court against these judgements. During the pendency of this appeal, with the leave of the Supreme Court, revised guidelines were issued by the Central Government to be effective from 1st April, 1983. Under the guidelines of 1983, the total maximum remuneration pocket to an individual shall not exceed Rs. 2,02,500 (Salary Rs. 90,000 + Commission Rs. 45,000 + Perquisites Rs. 67,500) per annum from one or more companies put together, subject to the statutory limits placed by the Companies Act, 1956.

Statutory Guidelines on Managerial Remuneration—Sch. XIII

The Companies (Amendment) Act, 1988 has now provided statutory guidelines regarding the managerial remuneration in the Act itself by introducing Schedule XIII. The guidelines regarding managerial remuneration effective from 1st April, 1983 will no more be applicable from 15th June, 1988 when the statutory guidelines specified in Schedule XIII will start operating. Now a public company which is a subsidiary of a public company can appoint a managing or whole-time director or manager and fix their remuneration without the approval of the Central Government, so long the same is in accordance with the conditions laid down in Schedule XIII.

The Central Government has amended Schedule XIII twice since 1988 and the amended Schedule has become effective w.e.f. 1st February, 1994. It has removed monetary ceilings on managerial remuneration payable by companies having profits. The only ceilings on the managerial remuneration are the percentage ceilings laid down in Sections 198, 309 and 387. Schedule XIII is composed of three parts. The provisions of revised Schedule XIII are stated below:

SCHEDULE XIII

PART I

APPOINTMENTS

A person shall be eligible for appointment as a managing or whole-time director or manager of a company without the approval of the Central Government provided the following conditions are satisfied:

(i) he had not been sentenced to imprisonment for any period or to a fine not exceeding one thousand rupees under any of the thirteen economic legislations specified in Schedule XIII;

(ii) he had not been detained for any period under the Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974;

(iii) he has completed the age of 25 years and has not attained the

age of 70 years or the age of retirement, if any, specified by the company, whichever is earlier;

(iv) where he is managerial person in more than one company, he opts to draw remuneration from only one company; and

(v) he is a citizen of India.

PART II

REMUNERATION

Section I - Remuneration payable by companies having profits

Subject to the provisions of Sec. 198 and Sec. 309, a company having profits in a financial year may pay any remuneration, by way of salary, dearness allowance, perquisites, commission and other allowances, which shall not exceed 5 per cent of its net profits for one such managerial person, and if there is more than one such managerial person, 10 per cent for all of them together.

This means that there would be no monetary ceilings at all on the managerial remuneration paid by a company to its managerial personnel in the case of companies having profits. The only ceilings on the managerial remuneration (in the case of companies having profits) are the percentage ceilings laid down in Sections 198, 309 and 387. Remuneration payable by a company to any managerial personnel in the event of absence or inadequacy of net profits during any financial year shall be governed by Section II of Part II of Schedule XIII discussed hereafter.

Section II - Remuneration payable by companies having no profits or inadequate profits

1. Notwithstanding anything contained in this Part, where in any financial year during the currency of tenure of the managerial person, a company has no profits or its profits are inadequate, it may pay remuneration to a managerial person, by way of salary, dearness allowance, perquisites and any other allowance, not exceeding ceiling limit of Rs. 10,50,000 per annum or Rs. 87,500 per month calculated on the following scale:

	Where the effective capital of company is -	*Monthly remuneration payable shall not exceed*
(i)	less than Rs. 1 crore	Rs. 40,000
(ii)	Rs. 1 crore or more but less than Rs. 5 crores	Rs. 57,000
(iii)	Rs. 5 crores or more but less than Rs. 15 crores	Rs. 72,000
(iv)	Rs. 15 crores or more	Rs. 87,500

2. A managerial person shall also be eligible to the following perquisites which shall not be included in the computation of the ceiling on

remuneration specified in Paragraph 1 of this Section:

(a) contribution to provident fund, superannuation fund or annuity fund to the extent these either singly or put together are not taxable under the Income-tax Act, 1961.

(b) gratuity payable at a rate not exceeding half a month's salary for each completed year of service, and

(c) encashment of leave at the end of the tenure.

3. In addition to the perquisites specified in Paragraph 2 of this Section, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Paragraph 1 of this Section:

(a) Children's education allowance: In case of children studying in or outside India, an allowance limited to a maximum of Rs. 5,000 per month per child or actual expenses incurred, whichever is less. Such allowance is admissible upto a maximum of two children.

(b) Holiday passage for children studying outside India/family staying abroad: Return holiday passage once in a year by economy class or once in two years by first class to children and to the members of the family from the place of their study or stay abroad to India if they are not residing in India with the managerial person.

(c) Leave travel concession: Return passage for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India.

PART III

Provisions applicable to Parts I and II of this Schedule

1. The appointment and remuneration referred to in Parts I and II of this Schedule shall be subject to approval by a resolution of the shareholders in general meeting.

2. The auditor or the secretary of the company or where the company has not appointed a secretary, a secretary in whole-time practice shall certify that the requirements of this Schedule have been complied with and such certificate shall be incorporated in the return filed with the Registrar under Sec. 209(2).

Compensation for Loss of Office

Section 318 provides that a company may pay compensation to a managing director or a director holding the office of a manager or a whole-time director for loss of office or for retirement from the office. No such payment shall be made by the company to any other director. Even the above mentioned persons shall not be entitled to any compensation in the following cases:

(i) where the director resigns his office in view of the reconstruction or amalgamation of the company and he is appointed in the company resulting from reconstruction or amalgamation;

(ii) where the director resigns otherwise than no reconstruction or amalgamation of the company;

(iii) where the office of the director is vacated under Section 203 or Section 283 (Section 203 empowers the court to restrain fraudulent persons from managing companies and Section 283 provides grounds on which the office of the director is vacated);

(iv) where the company is being wound up and the winding up is due to negligence or default by the director;

(v) where the director has been guilty of fraud or breach of trust, or gross negligence or mismanagement in the affairs of the company; and

(vi) where the director has instigated or has taken part directly or indirectly in bringing about the termination of his office.

The amount of compensation shall not exceed the remuneration which he would have earned for the unexpired residue of his term or for three years, whichever is shorter.

Directorial Registers

(1) **Register of directors.** Every company shall keep at its registered office a register of its directors, managing director, manager and secretary. The register shall contain the following particulars with respect to each of the above persons:

(1) (*i*) His present name and surname in full.

(*ii*) Any former name or surname in full.

(*iii*) His father's name and surname in full or where the individual is a married woman, the husband's name and surname in full.

(*iv*) His nationality of origin.

(*v*) His usual residential address.

(*vi*) His business occupation, if any.

(*vii*) If he holds the office of a director, managing director, manager or secretary in any other body corporate, the particulars of each such office held by him.

(*viii*) His date of birth.

(2) If any directors have been nominated by a body corporate, its corporate name and the particulars as mentioned above in respect of each director so nominated.

(3) If any directors have been nominated by a firm, the name of the firm, particulars as mentioned above in respect of each director so nominated and the particulars of the firm.

Return to be filled with the Registrar. The company shall send to the Registrar within thirty days of the date of the first appointment of directors, a duplicate copy in the prescribed form of the contents of the register. Similarly any change in the above particulars shall be notified to

the Registrar in the prescribed form within thirty days of the date of the change. (Sec. 303)

Inspection of the register. The above register shall be open to the inspection of any member without charge and of any other person on payment of one rupee for each inspection during business hours, so that no less than two hours in each day are allowed for inspection. (Sec. 304)

(2) **Register of director's shareholdings.** Every company shall keep a register of directors' shareholdings showing, for each director of the company, the number, description and amount of shares or debentures held by him in the company. The register shall also show such particulars in respect of holdings by each director in the company's subsidiaries and holding company and other subsidiaries of the same holding company. The register must also give the details of the shares held in trust for him or of which he has a right to become the holder, whether on payment or not.

Location and inspection of the register. The register shall be kept at the registered office of the company and it shall be open to inspection by members or debenture holders for at least two hours every day during the period of fourteen days before the date of the company's annual meeting and ending three days after the date of its conclusion. During the above period or any other period, it shall be open to inspection of any person acting on behalf of the Central Governemtnt or the Registrar.

The Central Government or the Registrar may require a copy of the said register or any part thereof.

The register must be produced at the commencement of the annual general meeting and must remain open to any person with the right to attend the meeting. (Sec. 307)

Duty of directors to made disclosure of shareholdings. Section 308 provides that every director of a company shall give notice to the company of such matters relating to himself as may be necessary for enabling the company to prepare the above register.

The above provisions shall apply to managers as they apply to directors. (Sec. 308)

(3) **Register of contracts, companies and firms in which directors are interested.** Section 301 provides that every company shall keep one or more registers of such contracts in which a director is interested and of contracts with such firms and companies in which a director is interested. The following particulars shall be entered in the said register: (*a*) the date of the contract; (*b*) the names of the parties; (*c*) the principal terms and conditions; (*d*) the date on which it was placed before the board; and (*e*) the names of the directors voting for and against the contract or arrangement and the names of those remaining neutral.

Location and inspection of the register. The register shall be kept at the registered office of the company and it shall be open to its members for inspection. The members may take extracts therefrom and they may also obtain copies of the same on payment of a prescribed fee.

Contracts by Directors with the Company

Contracts in which a director is interested. Except with the consent of the board of directors of a company, a director shall not enter into any contract with the company for (*a*) the sale, purchase or supply of any goods, materials or services; or (*b*) underwriting the subscription of any shares or debentures of the company. This restriction shall also apply to a relative of a director, a firm in which such a director or his relative is a partner, any partner of such firm, or a private company of which the director is a member or a director.

The Companies (Amendment) Act, 1974, further adds that in the case of a company having a paid-up share capital of not less than rupees one crore, no such contract shall be entered into except with the previous approval of the Central Government. [Sec. 297(1)]

Exceptions. However, the above restriction does not apply in the following cases:

(*i*) contracts for purchase or sale of goods and materials for cash at prevailing market prices;

(*ii*) any contract or contracts for sale, purchase or supply of any goods, materials and services in which either of the parties regularly trades or does business and the total value in a year does not exceed five thousand rupees;

(*iii*) in the case of a banking or insurance company, any transaction in the ordinary course of business of such a company. [Sec. 297(2)]

In circumstances of urgent necessity, a director may enter into a contract with the company for the purchase and sale of goods even for a value beyond Rs 5,000 without obtaining the consent of the board. But in such a case, the consent of the board shall be obtained at a meeting within three months of the date on which it was entered into. (Sec. 297(3)]

Consent must be to specific contracts. Consent under the above provisions must be specific and not a general consent to all contracts.[36]

Effect of non-compliance. If consent is not obtained or is refused, anything done in pursuance of the contract shall be voidable at the option of the board. [Sec. 297(5)]

Disclosure of interests by a director. Section 299 provides that every

[36]*Walchand Nagar Industries Ltd. v Ratan Chand,* A.I.R., 1963 Bom. 285.

director of a company, who is any way concerned or interested in a contract or an arrangement by or on behalf of the company, shall disclose the nature of his concern or interest at a meeting of the board of directors where the question of entering into a contract or arrangement is first considered. If he was not interested in the proposed contract or arrangement at the date of that meeting, he must disclose his interest at the first board meeting held after he becomes so interested or concerned.

Disclosure of interest by notice. A general notice may be given to the board by a director to the effect that he is a director or a member of a specified body corporate or is a member of a specified firm and is to be regarded as concerned or interested in any contract or arrangement which may be entered into between that firm or body corporate and the company. This will be deemed to be a sufficient disclosure of concern or interest in relation to any contract or arrangement so made.

Expiry of the notice. Any such general notice shall expire at the end of the financial year in which it is given, but may be renewed for further periods of one financial year at a time by a fresh notice given in the last month of the financial year in which it would otherwise expire. No such general notice shall have effect unless either it is given at a meeting of the board, or the director concerned takes reasonable steps to secure that it is brought upon and read at the first meeting of the board after it is given.

Exception. The above provisions shall not apply to any contract or arrangement entered into between two companies where any of the directors of the one company or two or more of them together hold not more than two per cent of the paid-up share capital in the company. [Sec. 299]

Consequences of non-compliance. Every director who fails to comply with the above provisions shall be punishable with a fine which may extend to five thousand rupees.

Non-disclosure does not render the contract void or a nulity. It renders the contract voidable at the option of the company and makes the directors liable to account for any secret profits.[37]

Interested directors not to participate or vote in the board's proceedings. Section 300 provides that an interested director shall not take part in the discussion relating to any matter of his interest. He is also prohibited from voting on such a matter. His presence shall not count for the purpose of forming a quorum at the time of any such discussion or vote.

It was held in *Sunderaja Pillai v. Sakthi Talkies Ltd.*,[38] that if an

[37]*Hely-Hutchinson v. Brayhead Ltd.* (1967) 3 All. E.R. 98; *Venkatachalapathy v Guntur Cotton Etc. Mills.* A.I.R., 1929 Mad. 353.

[38](1967) Com. Cas. 463.

interested director votes, his vote will not be counted but it will not invalidate the proceedings either.

Although an interested director is prevented from voting in the board's proceedings, yet he has a right to vote in the general meeting of the shareholders as a shareholder in the proposed contract or arrangement.[39]

Penalty for non-compliance. Every director who knowingly contravenes the provisions of this section shall be punishable with a fine which may extend to five thousand rupees.

Exemption. This section further empowers the Central Government to exempt a public company or a private company which is a subsidiary of a public company from provisions of this section if the Central Government is of the opinion that with regard to the desirability of establishing or promoting any industry, business or trade, it would not be in the public interest to apply all or any of the prohibitions contained in this section.

Assignment of Office

Any assignment of his office by a director of a company shall be held void. (Sec. 312)

Holding Office of Profit

Consent by special resolution. Except with the consent of the company accorded by a special resolution *(a)* no director of a company shall hold any office or place of profit; and *(b)* no partner or relative of such a director, no firm in which such a director or relative is a partner, no private company of which such a director is a director or member, and no director or manager of such a private company shall hold any office or place of profit carrying a total monthly remuneration of ten thousand rupees or more.

If any such appointment is made without the sanction of the company, it will be sufficient if the consent of the company is given by a special resolution passed in the first general meeting held after the appointment. In case a relative of a director is so appointed without the knowledge of the director, the consent of the company may be obtained either in the first general meeting held after the appointment or within three months of the date of the appointment, whichever is later.

It may further be noted that a special resolution according consent shall be necessary for every appointment in the first instance and to every subsequent appointment to such office or place of profit on a higher

[39]*North West Transportation Co. v. Beatty (1887) 12 A.C. 580*

remuneration not covered by the special resolution, except when an appointment on a time scale has already been approved by the special resolution. [Sec. 314(1)]

If a relative, etc. was appointed before the director became a director of the company, the above provisions shall not apply. [Sec. 314(1-A)]

Holding an office or place of profit with a monthly salary of more than Rs 20,000. The Companies (Amendment) Act, 1974, has introduced further restrictions of holding any office or place of profit. It provides that no relative or partner of a director, etc., shall hold any office or place of profit in the company which carries a total monthly remuneration of not less than twenty thousand rupees, except with the prior consent of the company by a spçcial resolution and with the approval of the Central Government. [Sec. 314(1-B)]

Exceptions. No such consent of the company is required for holding the posts of managing director, manager, banker or trustee for the holders of debentures either under the company itself or under any subsidiary of the company unless the remuneration received from such a subsidiary is paid over to the company or its holding company. [Sec. 314(1)]

This section shall also not apply to a person who, though holds any office of profit in the company, has been appointed by the Central Government under Section 408 as a director of the company. [Sec. 314(4)]

Effects of contravention. The office or place of profit held in contravention of the above provisions becomes automatically vacant with a liability to refund to the company any remuneration already received. The company shall not waive the recovery of any sum refundable to it unless permitted to do so by the Central Government. [Sec. 314(2)]

Loans to Directors

Central Government approval. Section 295 provides that without obtaining the approval of the Central Government, a company cannot lend money to (*a*) its directors or to directors of its holding company or to any partner or relative of its directors; (*b*) any firm in which such a director or relative is a partner; (*c*) any private company of which any such director is a director or member; (*d*) any company at a general meeting of which not less than twenty-five per cent of the total voting power may be exercised or controlled by any such director or by two or more such directors together; and (*e*) any company whose board of directors, managing director, or manager is accustomed to act in accordance with the directions or instructions of the board of directors or any director(s) of the lending company. [Sec. 295(1)]

The above restriction is applicable not only in respect of direct lending

of money by a company but also in respect of giving of any guarantee or security for a loan made by some other person to any of the above parties. This section also prohibits the company from giving any guarantee or security for a loan given by a director to any person.

Exceptions. The above provision does not apply to a private company which is not a subsidiary of a public company or to a banking company. It also does not prevent a holding company from making loans to its subsidiary.

Effect of contravention. Every person who is knowingly a party to any contravention of the above provisions is punishable either with a fine which may extend to five thousand rupees or with simple imprisonment for a term which may extend to six months. Where such a loan has been repaid in full, no punishment by way of imprisonment shall be imposed and where the loan has been repaid in part, the punishment shall be proportionately reduced.

Moreover, such persons shall be liable jointly or severally to the lending company for the repayment of the loan or for making good the sum which it may have been called upon to pay in virtue of the guarantee given or security provided by such a company. The defaulting director shall also have to vacate his office.

Sole Selling Agents

Definition. The term 'sole selling agent' has not been defined in the Act, but it can be an individiual, firm or body coprorate having the exclusive right to sell the goods of a company in a particular area.

Prohibition on the appointment of sole selling agents in certain cases. The Companies (Amendment) ACt, 1974 introduced a new section, 294AA which confers powers on the Central Government to prohibit the appointment of sole selling agents in certain cases.

Where the Central Government is of the opinion that the demand for goods of any specified category is substantially in excess of the production or supply of such goods, and that the services of sole selling agents will not be necessary to create a market for such goods, the Central Government may declare that sole selling agents shall not appointed by a company for the sale of such goods for a specified period. [Sec. 294 AA(1)]

Restrictions on the appointment of sole selling agents in other cases. Section 294 provides that the board of directors of a company may appoint a sole selling agent for any area subject to the condition that appointment shall be valid if it is approved by the company in the first general meeting held after the date on which the appointment was made. If the company in general meeting disapproves the appointment, it shall

cease to be valid with effect from the date of that general meeting. The appointment cannot be made at a time for a period of more than five years. However, the sole selling agent may be reappointed or the term of his office may be extended by further periods not exceeding five years on each occassion. [Sec. 294(1)]

If the general meeting disapproves the appointment, the sole selling agent shall be entitled to remuneration for the work done.[40]

A company shall not appoint any individual, firm or body corporate, who or which has a substantial interest in the company, as a sole selling agent of that company unless such appointment has been approved by the Central Government. [Sec. 294 AA (2)]

The term 'substantial interest' is defined as holding the beneficial interest, singly or in aggregate, in shares exceeding rupees five lakhs or five per cent of the paid up share capital of the company, whichever is less, by an individual or any of his relatives, or by one or more partners of the firm, or by a company or one or more of its directors or their relatives. (Explanation to Sec. 294 AA)

No company having a paid-up share capital of rupees fifty lakhs or more shall appoint a sole selling agent except with the consent of the company accorded by a special resolution and the approval of the Central Government. [Sec. 294 AA (3)]

A company seeking approval under the above two sub-sections shall furnish such particulars as may be prescribed. {Sec. 294 AA (5)]

Investigation of terms of appointment. In cases where the approval of the Central Government is not required for the appointment of a sole selling agent, the Central Government may for some good reason require the company to furnish to it such information regarding the terms and conditions of the appointment of the sole selling agent as it considers necessary for the purpose of determining whether or not such terms and conditions are prejudicial to the interests of the company. If the company refuses or neglects to furnish any such information, the Central Government may appoint a suitable person to investigate and report on the terms and conditions of appointment of the sole selling agent. If the terms are found to be prejudicial to the interests of the company, the Central Government may make variations in those terms and conditions so as to make them no longer prejudicial to the interests of the compny. [Sec. 294(5)]

Such variations in the terms and conditions will become effective from the date specified in the order.[41]

[40]*Firestone Tyres and Rubber Co. v. Synthetics and Chemicals Ltd.,* (1970) 41 Comp. Cas. 77.

[41]*Nanavati & Co. Pvt. Ltd. v R.C. Dutt* (1967) 37 Comp. Cas. 171.

Where a company has more than one selling agent in any area or areas, the Central Government may require the company to furnish information regarding the terms and conditions of the appointment of all selling agents to it for the purpose of determining whether any one of them should be declared as the sole selling agent for such an area or any such areas. [Sec. 294(6)]

Compensation for loss of office. A company shall not be liable to pay compensation to its sole selling agent for the loss of his office in the following cases:

(*i*) where the appointment ceases to be valid because it is disapproved by the company in general meeting;

(*ii*) where the sole selling agent resigns his ofice in view of the reconstruction or amalgamation of the company and is appointed sole selling agent in the reconstructed company or amalgamated company;

(*iii*) where the sole selling agent voluntarily resigns his office;

(*iv*) where the sole selling agent has been guilty of fraud or breach of trust or gross negligence in the conduct of his duty as the sole selling agent; and

(*v*) where the sole selling agent has instigated or has taken part directly or indirectly in bringing about the termination of the sole selling agency.

The amount of compensation shall not exceed the remuneration which he would have earned had he been in office for the unexpired residue of his term or for three years, whichever is shorter. (Sec. 294 A)

Power to Make Contributions

Political contributions by companies. Contribution of funds by companies to political parties and for political purposes was totally prohibited before the Companies (Amendment) Act of 1985 was passed.

By substituting a new Section for Section 239A, the Companies (Amendment) Act of 1985 has lifted the blanket ban on political contributions by companies. This has been done with a view to permitting the corporate sector to play a legitimate role within the defined norms in the functioning of our democracy.

The amended provisions permit non-government companies which have been in existence for not less three financial years, to contribute money, directly or indirectly, to any political party or to any political person for political purposes. [Sec. 293A (1)]

The amount contributed in any financial year shall not exceed five per cent of the average net profits of three immediately preceding financial years. Contribution should be authorised by a resolution passed at a meeting of the board of directors of the company. [Sec. 293A (2)]

Donation or subscription or payment given to enable a party to win the public support shall be regarded as contribution, so also the amount of expenditure incurred by a company for the publication of a souvenir, brochure, tract, pamphlet, etc., by or on behalf of a political party or for its advantage. [Sec. 293A (3)]

Such contributions are required to be disclosed by every company in its profit and loss account, giving details of total amount contributed and the name of the party or person to which or to whom such amount has been contributed. Sec. 293A (4)]

Any contribution made by a company in contravention of the provisions of this section will make it punishable with fine which may extend to three times the amount so contributed. Every officer of the company who is in default shall also be punishable with imprisonment which may extend to three years and shall also be liable to fine. [Sec. 293A (5)]

Power to contribute to the National Defence Fund. Section 293BB empowers the board of directors of every company to contribute such amount as it thinks fit to the National Defence Fund or any other fund approved by the Central Government for the purpose of national defence. Every company shall disclose, in its profit and loss account, the total amount or amounts contributed by it to the fund during the financial year to which the amount relates.

Inter-Corporate Loans and Investments

Sections 370 and 372 of the Companies Act, 1956 dealing with inter-corporate loans and investments have been abrogated and replaced by Section 372-A introduced by the Companies (Amendment) Act, 1999. Now this newly introduced Section 372-A consolidates the provisions with respect to inter-corporate loans, guarantees and investments. The provisions of Section 372-A are as follows:

Ceiling on inter-corporate loans and investments. No company shall, directly or indirectly, :

(a) make any loan to any other body corporate;

(b) give any guarantee or provide any security for any loan given or taken by any body corporate; and

(c) acquire, by way of subscription, purchase or otherwise the securities of any other body corporate exceeding (i) 60% of its paid-up share capital and free reserves or (ii) 100% of its free reserves, whichever is more. [Sec. 372-A (1)]

It is worth noting the consolidating effect of Section 372-A as it is the aggregate of the loans, guarantees and investments which cannot exceed the ceiling stated above. Moreover the board of directors of a company can make loans or investments of their own decision upto the aforesaid ceiling.

Authorisation by special resolution. Where the aggregate of the loans and

investments so far made in all other bodies corporate along with the investments, loans or guarantees proposed to be made or given by the board of directors, exceeds the aforesaid limits, no investment or loan shall be made or guarantee shall be given unless previously authorised by a special resolution passed in a general meeting.

The notice of the meeting of share holders called for the purpose of passing the special resolution as aforesaid must disclose clearly: (a) the specific limits; (b) the particulars of the body corporate in which investment is proposed to be made or loan or security or guarantee to be given; (c) the purpose of the investment, etc., and (d) specific sources of funding and such other details.

The board of directors may give guarantee without being previously authorised by a special resolution:

(a) if the Board is authorised to give the guarantee by its own resolution in accordance with the provisions of this section;

(b) if there exists exceptional circumstances which prevent the company from obtaining previous authorisation by a special resolution for giving a guarantee; and

(c) if the resolution of the board is confirmed in a general meeting within 12 months or the annual general meeting held immediately after passing of the board's resolution. [Sec. 372-A (1)]

Unanimous consent of the Board. No loan or investment shall be made or guarantee or security given by the company unless the resolution sanctioning it is passed at a meeting of the Board with the consent of all the directors present at the meeting and the prior approval of the public financial institution is obtained whose term loan with the company is subsisting. Prior approval of the public financial institution is not required where the aforesaid limit of 60% does not exceed and there is no default in repayment of loan instalments or payment of interest thereon towards the public financial institution. [Sec. 372-A (2)]

Rate of interest. No loan shall be made to any body corporate at a rate of interest lower than the prevailing bank rate, which shall mean the standard rate made public under Section 49 of Reserve Bank of India Act, 1934. [Sec. 372-A (3)]

Default in repayment of deposits. A company which has defaulted in payment of deposits on maturity or interest due on them under section 58-A cannot make any loans, investments or provide any guarantee, till such default is subsisting. [Sec. 372-A (4)]

Register of investments and loans. Every company shall keep a register showing the following particulars in respect of every investment, loan, guarantee and security:

(a) the name of the body corporates;

(b) the amount, terms and purpose of the investment or loan or security or guarantee;

(c) the date on which the investment or loan has been made; and

(d) the date on which the guarantee has been given or security has been provided in connection with a loan.

The particulars of investment, loan, guarantee or security shall be entered chronologically in register within 7 days of the making of such investment or loan, etc. This register shall be kept at the registered office of the company and shall be open for inspection to members. Members may also take extracts therefrom and demand copies on payment of the same fees as in the case of register of members of the company. [Sec. 372-A (5) and (6)]

Exceptions. The provisions of Section 372-A do not apply to any investment or loan made or any guarantee or security given in the following cases:

(a) a banking company or an insurance company or a housing finance company in ordinary course of its business or a company established with the object to financing industrial enterprises or for providing infrastructural facilities;

(b) a company whose principal business is the acquisition of shares, stock, debentures or other securities;

(c) a private company, unless it is a subsidiary of a public company.

Investment in shares in pursuance of Section 81 (1) (a) (rights shares) is also exempted from section 372-A. Similarly Section 372-A shall not apply to any loan made by a holding company to its wholly-owned subsidiary; any guarantee given or any security provided by a holding company in respect of loan made to its wholly-owned subsidiary; or acquisition by a holding company, by way of subscription, purchases or otherwise, the securities of its wholly-owned subsidiary. [Sec. 372-A (8)]

Explanation. For the purposes of this section, the term "loan" includes debentures or any deposit of money made by one company with another company, not being a banking company. The term "free reserves" means those reserves which, as per latest audited balance sheet of the company, are free for distribution as dividend and shall include balance to the credit of securities premium account but shall not include share application money.

Director's Powers

General powers of the board. Section 291 defines the general powers of the board and lays down that the board of directors of a company shall be entitled to exercise all such powers and undertake all such acts and things as the company is authorised to exercise and do. However, the board shall not exercise any power or do any act or thing which is directed or required to be exercised or done by the company in general meeting. Moreover, in exercising any power or doing any such act or

thing, the board shall be subject to the provisions contained in that behalf in the Act or in the memorandum or articles of the company and other regulations, not inconsistent therewith made by the company in general meeting.

No interference in the powers exercisable by the board. The directors must act within their powers and for the benefit of the company. But once specific powers of control and management have been granted by the company to its directors, the company, in general meeting, will have no right to interfere with or override the same. In this connection, it is interesting to note the observations of Greer L.J made in *Shaw & Sons (Salford) Ltd. v. Shaw and Shaw:*[42] "A company is an entity distinct alike from its shareholders and directors. Some powers may, according to articles, be exercised by directors, certain other powers may be reserved for the shareholders in general meeting. If the powers of management are vested in the directors, they and they alone can exercise these powers. The only way in which the general body of the shareholders can control the exercise of the powers vested by articles in directors is by altering their articles, or, if opportunity arises under the articles, by refusing to re-elect the directors of whose action they disapprove. They cannot themselves usurp the powers which by the articles are vested in the directors any more than the directors cn usurp the powers vested by the articles in the general body of the shareholders."

In *Automatic Self Cleansing, Etc. v. Cunninghame,*[43] the articles empowered the directors to sell or otherwise deal with the property of the company on such terms as they thought fit. Later, a resolution was passed by shareholders for sale of the company's assets on certain terms, and they required the directors to carry the sale into effect. The latter refused to do so. It was contended that directors are the agents of shareholders and as such they should follow instructions given by the shareholders in the resolution. The court held that, "directors are agents not of a majority of shareholders, but of the company, of the whole entity made up of all the shareholders. And if the whole entity of shareholders has entrusted the directors with a particular power, a simple majority could not interfere in the exercise of it."

Exceptions. But it must be noted here that ultimate control of the company lies in the hands of shareholders. As such shareholders have been successful, in certain cases, in intervening and exercising power vested in the board. Such cases are mentioned below:

(*i*) *Directors acting malafide.* Where the directors act for their personal interest and disregard the interest of the company, the shareholders may

[42](1935) 2 K.B. 113 C.A.
[43](1906) 2 Ch. 34.

intervene. Such a situation arises where there is clash of directors' personal interest and their duties towards the company;[44]

(*ii*) *Deadlock in management.* Where the directors are unable or unwilling to act, the shareholders may intervene to take necessary steps to ensure the working of the company.[45]

(*iii*) *Board becoming incompetent to act.* Where the board has become incompetent to act, the shareholders may intervene. Such a situation will arise if all the directors are interested in a particular transaction. A similar situation will also arise if none of the directors constituting the board has been validly appointed.[46]

Powers to be exercised by the board at meetings. The board of directors of a company shall exercise the following powers on behalf of the company and it shall do so only by means of resolutions passed at meetings of the board: (*a*) the power to make calls on shareholders in respect of money unpaid on their shares; (*b*) the power to issue debentures; (*c*) the power to borrow moneys otherwise than on debentures; (*d*) the power to invest the company's funds; and (*e*) the power to make loans.

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, the power to borrow money, to invest funds of the company and to make loans. The resolution should also specify the extent, nature and purpose in each case.

The shareholders in general meeting may impose restrictions and conditions on the exercise by the board of any of the above powers. (Sec. 292)

In addition to the above powers, there are certain other powers under different sections which can be exercised only by means of resolutions passed at a meeting of the board of directors. These are: (*a*) the power to fill up a casual vacancy in the board of directors under Section 262; (*b*) the power to accord consent to a director to enter into certain contracts with the company under Section 297; (*c*) the power to appoint a person as managing director who is already the managing director or manager in another company under Section 316; (*d*) the power to appoint a person as manager who is already the managing director or manager of another company under Section 386; (*e*) the power to invest in shares and debentures of other companies under Section 372.

[44]*Marshall's Valve Gear Co. Ltd. v Manning Wardle & Co. Ltd.* (1909) 1 Ch. 267.

[45]*Baron v Potter* (1914) 1 Ch. 895.

[46]*Vishwanahan v. Tiffins Barytes Asbestos and Paints Ltd.* A.I.R. (1953) Mad. 520.

Restrictions on the board's powers. The board of directors of a public company, or a private company which is a subsidiary of a public company, shall not, except with the consent of the company in general meeting, either:

(*i*) sell, lease or otherwise dispose of the whole or substantially the whole undertaking of the company.

In case of an improper sale or lease by the directors, the title of a buyer or other individual who buys or takes a lease of any such undertaking shall not be affected if he takes or buys it in good faith and after exercising due care and caution. (This restriction shall not be applicable to a company whose ordinary business consists of such selling or leasing); or

(*ii*) remit or give time for repayment of any debt due by a director except in case of renewal or continuance of an advance made by a banking company to its director in the ordinary course of business; or

(*iii*) invest the amount of compensation received by the company in respect of compulsory acquisition in securities other than trust securities; or

(*iv*) borrow moneys, where the moneys to be borrowed, together with moneys already borrowed by the company (apart from temporary loans obtained from the company's bankers in the ordinary course of business) will exceed the aggregare of the paid-up capital of the company and its free reserves.

The term "temporary loans" means loans repayable on demand or within six months of the date of the loan. It does not include loans raised for the purpose of financing expenditure of a capital nature.

Every resolution passed by the company in general meeting authorising the board to borrow in excess of its paid-up capital and free reserves shall specify the total amount up to which moneys may be borrowed by the board of directors.

Any amount borrowed in excess of the limit imposed by the above resolution shall not be valid or effectual unless the lender proves that he advanced the loan in good faith and without knowledge that the limit imposed has been exceeded; or

(*v*) contribute to charitable and other funds not directly relating to the business of the company of the company or welfare of its employees, any amounts the aggregate of which will, in any financial year, exceed fifty thousand rupees or five per cent of its average net profits during the last three years immediately preceding, whichever is greater.

Every resolution passed by the company in general meeting shall state the total amount which may be contributed to charitable and other funds in any financial year. (Sec. 293)

Powers of the board to be exercised by a unanimous vote. Unless the articles otherwise provide, questions arising at any meeting of the board of directors shall be decided by a simple majority. Each director has one vote for each resolution put to vote at the meeting. In case of an equality of votes, the chairman shall have a second or casting vote. However, the Act requires unanimous consent of all the directors in certain matters under Section 316, 372 and 386. These matters have already been mentioned above.

We have already discussed in details the restrictions on the powers of the board to appoint sole selling agents under Section 294 and 294AA, and to make political contribution under Section 293A. Similarly, restrictions on the powers of board as to loans to other companies under Section 370 and as to investments in shares of other companies under Section 372 have been discussed above.

Directors' Duties

Statutory duties. There are a number of statutory duties attached to the office of a director. The statutory duties begin with the incorporation of a company and continue till the company is liquidated. Directors must carry out all duties placed upon them by the Companies Act, 1956. These duties have been discussed in detail at appropriate places in the book. However, for the sake of information, a few statutory duties of the directors are stated below:

(*i*) It is the duty of directors to see that the prospectus issued by the company makes a disclosure of all matters specified in Schedule II of the Act. (Sec. 56)

(*ii*) It is duty of directors to see that no prospectus is issued to the public unless a copy of such prospectus has been delivered to the Registrar for registration. (Sec. 60)

(*iii*) It is the duty of directors to see that all moneys received from applicants for shares are deposited and kept deposited in a scheduled bank (*a*) until the certificate to commence business is obtained under Section 149; or (*b*) where such a certificate has been obtained, until the entire amount payable on applications for shares in respect of minimum subscription has been received by the company. [Sec. 69(4)]

(*iv*) Directors must file with the Registrar a return as to allotment within 30 days of the allotment of shares. (Sec. 75)

(*v*) Section 113 requires directors to deliver the share certificates of all shares within three months after the allotment.

(*vi*) If director refuse to register a transfer of shares, whether in pursuance of any power under articles or otherwise, they must send notice of refusal to the transferee and transferor within two months of

the date on which the instrument of transfer was delivered to the company. [Sec. 111(2)]

(*vii*) Directors are required to prepare and send to every shareholder a copy of the statutory report at least 21 days before the statutory meeting. The report should be certified as correct at least by two directors and a copy of the report should be sent to the Registrar also. (Sec. 165)

(*viii*) Section 91 requires directors to make calls on shares on a uniform basis on all shares falling under the same class.

(*ix*) Directors are required to call an extraordinary general meeting of the company on the requisition signed by specified number of members. (Sec. 169)

(*x*) At every general meeting of the company, the board of directors shall lay before the company a balance sheet and a profit and loss account. (Sec. 210)

(*xi*) It is the duty of directors to see that dividend is paid to members within 42 days from the date of its declaration. (Sec. 207)

(*xii*) Directors are to make a declaration of solvency in the case of members' voluntary winding up. (Sec. 488)

Duties of general nature. In addition to statutory duties, directors must also carry out certain duties of a general nature imposed by common law. These duties are stated below:

Duty of good faith. We have already seen that directors occupy a fiduciary position in relation to the company. As such the directors should observe utmost good faith towards the company and should act honestly in the exercise of their powers. They must act *bonafide* in the interest of the company. The duty of good faith therefore means that a director of a company should not make use of any money or other property of the company or of any information acquired by virtue of his position as a director or officer of the company or any other corporate opportunities to gain an improper advantage for himself at the expense of the company.

Again, the directors who occupy a fiduciary position in relation to the company should not make any secret profits by virtue of their position. They shall be liable to account for any secret profits made by them by breach of their fiduciary duty.[47]

However, it must be established that (*a*) what the directors did was so related to the affarirs of the company that it can properly be said to have been done in the course of their management and in utilisation of their

[47]*Regal Hastings Ltd. v Gulliver and Others* (1942) 1 All. E.R. 378; *Boston Deep Sea Fishing Co. v Ansell* (1888) 39 Ch. D. 339.

opportunities and special knowledge as directors and (*b*) that what they did resulted in a profit to themselves.

At the same time a director may make a profit by corporate opportunity if the company is insolvent or defunct or if the transaction is *ultra vires* the company. In such cases the directors shall not be liable to account for any corporate profits made by them.

Duty of reasonable care, skill and diligence. The duties of directors have been elaborately described by Romer L.J. in *Re City Equitable Fire Insurance Co.*[48]

"In discharging these duties a director must (a) act honestly; (b) exercise such degree of skill and diligence as would amount to be reasonable care which an ordinary man might be expected to take in the circumstances on his own behalf; but (c) need not exhibit in the performance of his duties a greater degree of skill than what can be resonably expeceted from a person of his knowledge and experience; in other words, he is not liable for mere errors of judgement; (d) he is not bound to give continuous attention to the affairs of his company; his duties are of an intermittent nature to be performed at periodic board meetings and the meetings of any committee to which he is appointed, and though not bound to attend all such meetings, he ought to attend them when reasonably able to do so; and (e) in respect of all duties, which having regard to the exigencies of business and the articles of association, may properly be left to some other official, he is, in the absence of suspicious grounds, justified in trusting that official to perform such duties honestly."

Duty to attend meetings. Directors exercise most of their powers at meeting of the board, but a director is not bound to attend every meeting. He will not be liable for negligence only on grounds of not attending board meetings.[49] However, a director who stays away from board meetings runs the risk of not being reappointed when he next comes up for the re-election. At the same time, he is liable to vacate his office if he fails to attend three consecutive meetings of the board or if he absents himself from all meetings of the board for a consecutive period of three months, whichever is longer.

Duty not to delegate. The maxim *"delegatus non protest delegate"* applies to directors. As such, *prima facie,* directors cannot delegate their powers.[50] But having regard to the exigencies of business and the articles of association, certain duties may properly be left to some other officials.

[48](1925) 1 Ch. 407.
[49]*Marquis of Butes Case* (1892) 2 Ch. 100.
[50]*Cobb v Becke* (1845) 6 Q.B. 930.

In the absence of grounds for suspicion, a director is justified in trusting an official with the honest performance of such duties.

Duty to disclose interest. This has been discussed earlier in the present chapter under Section 299.

Directors' Liabilities

The liability of directors can be studied under two heads:

(1) Civil liability: (i) to outsiders, and (ii) to the company.

(2) Criminal liability.

(1) **Civil liability of directors.** Generally the liability of directors in a limited company is limited in the same way as that of members of the company. But a limited company may make the liability of directors unlimited. In such a case the memorandum of the company shall provide that the liability of directors shall be unlimited. If the liability is unlimited, the member who proposes a person for election or appointment to the office of a director shall add to that proposal a statement that the liability of the person holding that office will be unlimited and a notice that his liability will unlimited shall be given to him by the promoters of the company, its directors and officers or by one of them. (Sec. 322)

If the liability of directors is limited, the company may render their liability unlimited if so authorised by its articles. A special resolution will have to be passed to render unlimited the liability of all or any of its directors. But any such new provision will become effective against an officer only on the expiry of his existing term, unless he has accorded his consent to his liability become unlimited. (Sec. 323)

(i) **Liability to outsiders.** Directors act as the agents of the company. Thus, where the directors enter into contracts in the name and on behalf of the company, they will not be personally liable for these contracts. It is the company which will be liable to third parties for such contracts. It was stated by Lord Cairns in *Ferguson v. Wilson.* [51] that "whereever an agent is liable the directors would be liable; where the liability would attach to the principal and the principal only, the liability is the liability of the company."

However, the directors will be liable to third parties in the following cases:

(a) When they make contracts in their own name and not in the name of the company, they shall be personally liable to third parties who may sue the company or the directors or both, as they like.

In *Dermatine Co. Ltd. v. Ashworth,*[52] a bill of exchange was accepted by

[51](1866) L.R. 2 Ch. App. 77.

[52](1905) 21 T.L.R. 510.

two directors of the company. The bill was drawn on a limited company in its proper name. However, the word "limited" did not appear in acceptance because rubber stamp by which the words of acceptance were impressed was larger than the paper of the bill. On the company's failure to pay the bill, it was held that directors would not be personally liable because of their failure to mention the name of the company properly. The omission of the word "limited" was not deliberate, it was merely accidental.

(b) Where the directors act *ultra vires* the company, neither the company nor the directors can be held liable by third parties. But directors may be held liable for breach of implied warranty of authority.[53]

(c) Directors will also be liable to the third parties who have subscribed for shares on the basis of misstatements in the prospectus. (Sec. 62)

The subscribers may also hold directors and other persons responsible for issue of such prospectus by an action for deceit under general law.

(ii) **Liability to the company.** It was laid down in *Lagunas Nitrate Co. v. Lagunas Syndicate*[54] that "if directors act within their powers, if they act with such care as is to be reasonably expected of them having regard to their knowledge and experience and if they act honestly for the benefit of the company they represent, they discharge both their equitable as well as legal duty to the company."

But the directors may become liable to the company in the following cases:

(a) *Liability for ultra vires acts.* The directors must see that the funds of the company are used for carrying on authorised business as stated in its memorandum. If a director makes an *ultra vires* payment, he can be compelled to make good the funds used.[55]

(b) *Liability for negligence.* Directors will also be liable to compensate the company for any loss caused by their negligence. When the directors acting within their powers fail to use such reasonable skill and diligence as may be expected from persons with their knowledge and experience in the management of the company's affairs, they can be held liable for negligence. However, they will not be liable for mere errors of judgement. It may be noted in this connection that diectors exercise most of their powers at meetings of the board. It is not necessary for every director to attend each meeting. But continuous non-attendance at meetings may render a director guilty of breaches of trust committed by others.[56]

(c) *Liability for misfeasance and breach of trust.* Breach of trust means misapplication of the funds of the company such as: (i) paying dividend

[53]*Weeks v Propert* (1873) 8 CP 427.

[54](1899) 2 Ch. 392.

[55]*Re Sharpe* (1892) 1 Ch. 154.

[56]*Charitable Corporation v Sutton* (1742) 26 E.R. 642.

out of capital, (ii) using funds for an *ultra vires* purpose. Misfeasance means breach of duty in the conduct of the company's affairs which causes loss to the company. The directors will be liable for breach of trust if they fail to act honestly and in the interest of the company. Directors will be liable to account for any secret profits made by them out of their dealings on behalf of the company. The company can also hold directors liable for damages caused by their wilful misconduct.

Section 543 provides that if in the course of winding up a company, it appears that any person who has taken part in the promotion or formation of the company or any past or present director, manager or liquidator or officer of the companyt has (a) misapplied any money or property of the company; or (b) been guilty of misfeasance or breach of trust in relation to the company, the court may examine the conduct of the person, director, manager, liquidator or officer. If he is found guilty he may be required to repay or restore the money or property of the company or contribute such sum to the assets of the company by way of compensation, as the court thinks just. Application to the court may be made by the liquidator, or any creditor or contributory. Application must be within five years of the date of the order of winding up or of the first appointment of the liquidator in the winding up or misfeasance or misapplication or breach of trust, whichever is longer.

(d) *Liability for frandulent conduct of business.* Section 542 provides that where, in the ccourse of winding up a company, it appears that any business of the company has been carried on with the intent to defraud creditors of the company or any other persons or for any fradulent purpose, the court may order that those persons who knowingly were party to the conducting of the business in the manner aforesaid shall be personally responsible without any limitation of liability for all or any of the debts or other liabilities of the company as the court may direct.

Any provision, whether in the articles of a company or in the agreement with the company or in any other instrument, for exempting any officer of the company, or indemnifying him against any liability which would otherwise attach to him in respect of any negligence, default, misfeasance,, breach of duty or breach of trust of which he may be guilty in relation to the company, shall be void. (Sec. 201)

However, Section 633 provides wide protection to directors. It lays down that in any proceedings against any director or officer of the company for negligence, breach of duty, misfeasance, etc., the court can excuse him from any liability if it is of the opinion that such a director or officer has acted honestly and reasonably and that having regard to all the circumstances of the case, he ought fairly to be excused. But in criminal proceedings, the court has no power to grant relief from any civil liability.

(2) **Criminal liability of directors.** For non-compliance of specific provisions of the Companies Act, directors are liable for imprisonment or fine or both. In addition, directors may incur criminal liability under the Common Law or under the Indian Penal Code. It is only in cases where a lapse on the part of directors is of a serious nature that criminal liability has been provided for in the Companies Act, 1956. Following are the cases where directors shall be criminally liable:

(i) Issuing a prospectus which includes any untrue statement--imprisonment upto two years or fine upto Rs 5,000 or both. (Sec. 63)

(ii) Fraudulently inducing persons to invest money-imprisonment upto five years or fine upto Rs 10,000 or both. (Sec. 68)

(iii) Concealing name of creditors, etc.-imprisonment up to one year or fine or both. (Sec. 105)

(iv) Functioning as director by undischarged insolvent, etc.-imprisonment upto two years or fine upto Rs 5,000 or both (Sec. 202)

(v) Contravening order of court that certain fradulent persons shall not act as director, etc. without court's consent-imprisonment upto two years or fine upto Rs 5,000 or both. (Sec. 203)

(vi) Failure to distribute dividends within 42 days of declaration-simple imprisonment upto seven days and fine. (Sec. 207)

(vii) Failure to maintain proper books of accounts as required by the Companies Act, 1956-imprisonment upto six months or fine upto 1,000 or both. (Sec. 209)

(viii) Failure to lay annual accounts and balance sheet at annual general meeting-imprisonemnt upto six months or fine upto Rs 1,000 or both. (Sec. 210)

(ix) Failure to attach board's report with balance sheet-imprisonment upto six months or fine upto Rs 2,000 or both. (Sec. 217)

(x) Failure to provide information to auditors of the company with regard to certain payments-imprisonemnt upto six months or fine upto Rs 5,000 or both. (Sec. 221)

(xi) Being knowingly a party to any contravention of restriction in regard to loans and financial assistance to directors, etc.-simple imprisonment upto six months or fine upto Rs 5,000 or both. (Sec. 295)

(xii) Failure of directors to give company notice of the necessary matters for register of directors' shareholdings-imprisonment upto two years or fine upto Rs 5,000 or both. (Sec. 308)

(xiii) Knowingly acting as managing director/diector/manager when concerned agreement has been terminated or set aside by court-imprisonment upto one year or fine upto Rs 5,000 or both. (Sec. 407)

(xiv) For making a false declaration of company's solvency-imprisonment upto six months or fine upto Rs 5,000 or both. (Sec. 488)

(xv) Making false statements in returs, reports, balance sheets, etc.-imprisonment upto two years and fine. (Sec. 628)

(xvi) Giving intentionally false evidence-imprisonment upto seven years and fine. (Sec. 629)

(xvii) Wrongful withholding of property-imprisonment for two years. (Sec. 630)

In all the penal provisions of the Act, the person sought to be made liable is described as an 'officer who is in default'. The expression 'officer who is in default' means any officer of the company who is knowingly guilty of the default, non-compliance, failure, refusal or contravention mentioned in that provision, or who knowingly and wilfully authorises or permits such default, non-compliance, failure, refusal or contravention (Sec. 5). According to section 2(30), the term 'officer' includes a director also.

Other Managerial Personnel

In addition to the board of directors, a company may employ either a managing director or a manager. Section 197A provides that a company cannot appoint or employ at the same time both a managing director and a manager. Section 197A which was inserted by the Companies (Amendment) Act, 1960, intends to reduce managerial remuneration. However, employment of whole-time director(s) along with managing director (s) or a manager is not prohibited.

MANAGING DIRECTOR

Section 2(26) defines a managing director as a 'a director who, by virtue of any agreement with the company or of a resolution passed by the company in general meeting or by its board of directors or, by virtue of its memorandum or articles of association, is entrusted with substantial powers of management which would not otherwise be exercisable by him, and includes a director occupying the position of a manging director, by whatever name called."

This means that a managing director is a director who is entrusted with substantial powers of management (other than administratibve acts of a routine nature, such as the power to affix the common seal of the company to any document or to draw or endorse any cheques on the account of the company in any bank or to draw and endorse any negotiable instrument or to sign any certificate of share or to direct registration of transfer of any share. Power to perform any of such acts of routine nature shall not be deemed to be included within the substantial powers of management). The substantial powers of

management may be conferred upon a managing director by an agreement, memorandum, articles or resolutions of general meeting or the board of directors.

It is further provided that the managing director of a company shall exercise his powers subject to superintendence, control and direction of its board of directors.

The statutory provisions regarding appointment of managing or whole-time director are discussed below:

(1) **Compulsory appointment of managing or whole-time director or manager.** Section 269, as amended by the Companies (Amendment) Act, 1988, provides that every public company (including a deemed public company under Section 43A) or a private company which is a subsidiary of a public company, having a paid-up share capital of rupees five crore or more shall have managing or whole-time director or manager. [Sec. 269(1)]

(2) **Procedure of appointment.** When the appointment of a managing or whole-time director or manager is in accordance with the conditions specified in Schedule XIII,[57] it does not require the approval of the Central Government. However, a return of the appointment in prescribed form must be made within 90 days from the date of such appointment. But if the appointment does not comply with the conditions specified in Schedule XIII, approval of the Central Government becomes necessary and application seeking approval must be made within 90 days. [Sec. 269 (2), (3)]

The Central Government shall not accord its approval unless it is satisfied that (a) it is in the interests of the company to have a managing or whole-time director; (b) the proposed managing or whole-time director of the company is a fit and proper person and that the appointment of such an individual as managing or whole-time director is not against public interest; and (c) the terms and conditions of the appointment of the proposed managing or whole-time director of the company are fair and reasonable. [Sec. 269 (4)]

The Central Government is also empowered to accord approval to the appointment for a period less than the period for which the person is proposed to be appointed by the company. [Sec. 269 (5)]

If the appointment of a person as a managing or whole-time director is not approved by the Central Government, the person so appointed

[57]*Schedule XIII, inserted by the Companies (Amendment) Act, 1988, deals with the terms and conditions for appointment of managerial personnel. Details of Schedule XIII have already been discussed in this chapter under the heading "Statutory Guidelines on Managerial Remuneration"*

shall vacate his office from the date on which the decision of the Central Government is communicated to the company. If the person omits or fails to do so, he shall be punishable with a fine which may extend to five hundered rupees for every day during which he omits or fails to vacate such office. [Sec. 269 (6)]

Where the Central Government is *prima facie* of the opinion that any appointment made without its approval has been made in contravention of the conditions specified in Schedule XIII, it may refer the matter to the Company Law Board for decision. The Company Law Board, after giving a reasonable opportunity of hearing to the company and the appointee, may make an order declaring whether contravention of the conditions specified in Schedule XIII has or has not taken place. If the Company Law Board comes to the conclusion that such contravention has taken pace, the appointment shall be deemed to have come to an end and the person so appointed shall, in adition to being liable to pay a fine of rupees ten thousand, refund to the company the entire amount of salaries, commissions and perquisties received or enjoyed by him. However, all acts of the appointee, whose appointment is invalidated, will be deemed to be valid. [Sec. 269(7) to (12)]

(3) **Disqualifications for the office of managing director.** A company shall not appoint any person as its managing or whole-time director who (a) is an undischarged insolvent or has at any time been adjudged insolvent; (b) suspends or has at any time suspended payment to its creditors or makes or has at any time made a composition with them; or (c) is or has at any time been convicted by a court of an offence involving moral turpitude. (Sec. 267)

(4) **Term of office.** No company shall appoint any individual as its managing director for a term exceeding five years at a time. There is nothing to prohibit reappointment by a further period not exceeding five years on each occasion. But any such reappointment shall not be sanctioned earlier than two years from the date on which it is to come into force. (Sec. 317)

The restriction regarding the term of appointment does not apply in the case of a whole-time director.

(5) **Amendment of provisions.** In the case of a public company or a private company which is subsidiary of a public company, no change can be made in terms relating to the appointment or reappointment of a managing or whole-time director unless approved by the Central Government. The change shall become void if, and in so far as, it is disapproved by the Government. (Sec. 268)

(6)**Number of managing directorships.** No public company and no private company which is a subsidiary of a public company shall appoint

any person as managing director, if he is either the managing director or the manager of any other company.

However, a public company or a private company which is a subsidiary of a public company may appoint a person as its managing director, if he is the managing director or the manager of only one other company. In such a case appointment must be made or approved by a resolution passed at a meeting of the board with the consent of all the directors present at the meeting. Specific notice of the meeting and the resolution should be given to all the directors then in India.

However, a person may be managing director of any number of independent private companies.

Section 316(4) provides that the Central Government may permit any person to be appointed as a managing director of more than two companies if the central government is satisfied that it is necessary that the companies should, for their proper working, function as a single unit and have a common managing director.

However, the Central Government will not generally approve the appointment of a person as managing director even in two companies which are of a large size unless they are engaged in more or less similar business or situated in the same area.

It is important to note that a person cannot be a whole-time director in more than one company since he is the whole-time employee of the company.

(7) **Remuneration.** A director who is either in whole-time employment of the company or is a managing director may be paid remuneration either by way of a monthly payment or at a specified percentage of the net profits of the company or partly by one way and partly by the other.

Except with the approval of the Central Government such remuneration shall not exceed five per cent of the net profits for one such director, and if there is more than one such director, ten per cent for all of them together. [Sec. 309 (3)]

The Central Government may, while according its approval under Section 269 for appointment or reappointment of a managing or whole-time director, fix the remuneration of the persons so appointed. The remuneration shall be fixed within the limits specified in the Act, at such amount or percentage of profits of the company as its may deem fit. While fixing the remuneration, the Central Government shall have regard to (a) the financial position of the company; (b) the remuneration or commission drawn by the individual concerned in any other capacity, including his capacity as a sole selling agent; (c) the remuneration or commission drawn by him from any other company; (d) the professional qualifications and experience of the individual concerned; and (e) public

policy relating to the removal of disparities in income. (Sec. 637-AA)

Whole-time Director

Definition. A whole-time director means a director employed to devote the whole of his time and attention in carrying on such of the affairs of the company as may be assigned to him by the board of directors or the managing diector, as the case may be. According to explanation given to section 269(1), the term 'whole-time director' includes a director in whole-time employment of the company. A whole-time director is generally known as executive director. He is an employee director of the company. Like the managing dirctor, he occupies dual capacity, namely, that of a director and of an employee.

Appointment. The appointment of a whole-time director is governed by the provisions of Section 269 which incorporates the provisions regarding the appointment of managing directors also. Besides that, the appointment of a whole-time director requires the sanction of shareholders by means of a special resolution since the office of a whole-time director is an office of profit.

Section 197-A prohibits a company from having simultaneously both a managing director and a manager. Since the employment of a whole-time director does not come within the purview of the above section, a company is free to appoint a whole-time director along with a managing diector or a manager.

Distinctions betwen Managing Directors and Whole-time Directors

One must have noticed that most of the provisions of the Companies Act, 1956 which are applicable to the managing directors are also applicable to the whole-time directors. However, there are some marked differences between a managing director and a whole time director. These are:

(1) A managing director is a director who is entrusted with substantial powers of management, whereas a whole-time director is an employee of the company entrusted with powers as per terms of employment.

(2) Section 197-A prohibits a company from having simultaneously both a managing director and manager. But a whole-time director may be appointed along with a manager or a managing director.

(3) No individual can be appointed as managing director for more than five years at a time (Sec. 317); whereas there is no such restriction regarding the appointment of a whole-time director.

(4) A person can be managing director of two companies or even more in certain cases (Sec. 316); whereas a person cannot be a whole-time director of more than one company.

(5) Appointment of a managing director does not necessarily require the consent of the shareholders of the company by means of a special resolution, but for the appointment of a whole-time director the consent of the shareholders of the company by a special resolution is necessary.

MANAGER

Section 2(24) defines a manager as "an individual (not being the managing agent) who subject to the superintendence, control and direction of the board of directors, has the management of the whole or substantially the whole, of the affairs of a company, and includes a director or any other person occupying the position of manager, by whatever name called and whether under a contract of service or not".

A person, in order to be manager, must have the management of the whole or substantially the whole of the affiars of the company. Thus the manager of a branch office will not be within the definition.

The statutory provisions regarding appointment of manager are discussed below:

(1) **Disqualifications for the office of manger.** No firm or body corporate or association can be appointed manager of a company (Sec. 384). No company shall appoint any person as its manager who (a) is an undischarged insolvent or has at any time within the preceding five years been adjudged an insolvent; (b) suspends or has at any time within the preceding five years suspended payment to his creditors; or makes or has at any time within the preceding five years made a composition with them: or (c) is or has at any time within the preceding five years been convicted by the court in India of an offence involving moral turpitude.

The Central Government may remove the above disqualifications either generally or in relation to any company or companies by notification in the Official Gazette. (Sec. 385).

(2) **Restrictions on assignment of office.** Section 312 which prohibits assignment of his office by a director is also applicable to manager. (Sec. 388)

(3) **Number of managerships.** Section 386 provides that no company shall employ any person as manager if he is either the manager or the managing director of more than one other company. With regard to the appointment of a person as manager in the second company, it is essential that such appointment or employment is made or approved by a resolution passed at a meeting of the board with the consent of all the directors present at the meeting. Specific notice of the meeting and the resolution should have been given to all the directors then in India.

The Central Government may permit any person to be appointed

manager of more than two companies, if it is satisfied tht it is necessary that the companies should, for their proper working, function as a single unit and have a common manager. (Sec. 386)

(4) **Appointment, reappointment and term of office of a manager.** In this connection Section 388 provides that the provisions of Section 269 (regarding the procedure of appointment and requirement of approval of the Central Government) and 317 (providing that a managing director shall not be appointed for more than five years at a time) shall be applicable in relation to the manager of a company as they apply to managing director.

(5) **Manager's remuneration.** Section 387 provides that the remuneration payable to a manager shall be subject to the provisions of Section 198. He may receive remuneration either by way of a monthly payment or by way of a specific percentage of the net profits of the company, or partly by one way and partly by the other.

Except with the approval of the Central Governemnt such remuneration shall not in the aggregate exceed five per cent of the net profits.

Under Section 388 (which applies Section 310 to a manager also), any amendment of a provision relating to remuneration payable to a manager which directly or indirectly has the effect of increasing the amount of remuneration shall be void if not approved by the Central Government.

Before according its approval, the Central Government may fix remuneration at such amount or percentage of profits of the company within the limits specified in the Act, as it may deem fit. While fixing the remuneration, the Central Government shall have regard to (a) the financial position of the company; (b) the remuneration or commission drawn by the individual concerned in any other capacity including his capacity as a sole selling agent; (c) the remuneration or commission drawn by him from any othe company; (d) the professional qualifications and experience of the individual concerned; and (e) public policy relating to the removal of disparities in income. (Sec. 637 AA)

The above provisions except for those under Sections 384 and 385 shall not be applicable to a private company unless it is a subsidiary of a public company.

Distinctions between Managers and Managing Directors

There are some marked differences between the two. These are:

(1) A manager may or may not be a director of the company, whereas a managing director must be a director of the company as well.

(2) The powers of a manager are wider than the powers of a managing director. In the case of a manager, Section 2(24) provides that he has the management of the whole or substantially the whole of the affairs of a

company whereas under Sectrion 2(26), a managing director is entrusted with substantial powers of management.

(3) A company cannot have more than one manager but may have more than one managing director.

(4) A manager need not be under a formal contract of service whereas a managing director is appointed by virtue of an agreement with the company or of a resolution passed by the company in general meeting or by its board of directors, or by virtue of its memorandum or articles of association.

(5) In case of appointment or employment of a manager the disqualifications shall operate only if they occurred during the five years immediately preceding the date of his appointment (Sec. 385). In case of appointment or employment of a managing director, the same disqualifications will operate even if they have taken place at any time during the life of that person. (Sec. 267)

(6) In the case of managers, the Central Government may remove the disqualifications incurred by a person either generally or in relation to any company or companies by a notification in the Official Gazette. There is no such provision in the case of managing directors.

SECRETARY

A company secretary is one of the principal officers of the company. With the vast expansion of joint stock from of organistion, his position has become pre-eminent in the industrial and commercial world. In recent times, there has been a growing appreciation of the role of company secretaries in the administration of companies because of the complexities of modern business and the various laws which the management of a company is required to comply with.

Definition

Section 2(45), as amended by the Companies Amendment Act, 1988, provides that the expression "secretary" means a company secretary within the meaning of section 2(1)(c) of the Company Secretaries Act, 1980 and includes any other individual possessing the prescribed qualifications and appointed to perform the duties which may be performed by a secretary under this Act and any other ministerial or administrative duties. As per Section 2(1) (c) of the Company Secretaries Act, 1980, "company secretary" means a person who is a member of the Institute of Company Secretaries of India constituted under the Act.

The Amendment Act of 1988 has also introduced the concept of "secretary in whole-time practice". According to Section 2(45-A),

secretary in whole-time practice means a secretary who shall be deemed to be in practice within the meaning of Section 2(2) of the Company Secretaries Act, 1980 and who is not in full-time enployment.

It is clear from the above that only an individual may be appointed as a company secretary. A firm or body corporate cannot be so appointed. Further, the company secretary should either be a person who is a member of the Institute of Company Secretaries of India or possesses the requisite qualifications prescribed by the Central Government. It is important to note that the nature of work of a company secretary is ministerial and administrative and not managerial.

Certain Companies to have Secretaries

Section 383 A states that every company with a paid-up share capital of rupees fifty lakhs[58] or more is under an obligation to appoint a whole-time secretary. Only an individual with the prescribed qualifications can be appointed secretary of such a company. Further, no individual can hold the office of secretary in more than one such company. The companies having paid-up share-capital of less than rupees fifty lakhs have no obligation to appoint any secretary at all or a qualified secretary or a whole-time secretary. A director may be appointed as secretary in addition to his post as director but where the board of directors of a company has only two members, neither of them can be appointed as secretary.

Appointment of a Company Secretary

The secretary is usually appointed by the board of directors in exercise either of an express power conferred by the articles or of general powers of management which the articles usually give them. Section 314 also states the requirement of the consent of the company by a special resolution where a director of a company is to be appointed as its secretary. Section 303 requires that every appointment of secretary must be recorded in the Register of Directors etc. and a duplicate copy of the contents of the register must also be sent to the Registrar within thirty days from the date of appointment.

Qualifications of a Company Secretary

Under the Companies (Appointment and qualifications of Secretary) Rules, 1988, as amended on 13th April, 1993 vide Amendment Rules, 1993, the qualifications which a person must possess to be eligible for appointment as secretary are as follows:

(a) In the case of a company having paid-up share capital of Rs 50

[58]substituted for Rs 25 lakhs w.e.f. 13th April, 1993.

lakhs or more, the membership of the Institute of Company Secretaries of India, New Delhi.

(b) In the case of any other company, one or more of the following qualifications, namely:

(i) the qualifications specified in clause (a);

(ii) pass in the intermediate examiniation conducted by the Institute of Company Secretaries of India, New Delhi.

(iii) post-graduate degree in Commerce or Corporate Secretaryship granted by any University in India;

(iv) degree in law granted by any university;

(v) membership of the Institute of Chartered Accountants of India;

(vi) membership of the Institute of Cost and Works Accountants of India;

(vii) post-graduate degree or diploma in Management Science granted by any university or the Institute of Management, Ahmedabad, Calcutta, Bangalore or Lucknow;

(viii) post-diploma in Company Secretaryship granted by the Institute of Commercial Practice or diploma in Corporate Laws and Management granted by the Indian Law Institute, New Delhi;

(ix) post-graduate diploma in Company Law and Secretarial Practice granted by Univerty of Udaipur;

(x) membership of the Association of Secretaries and Administrators, Calcutta.

In case the paid-up share capital of such a company is raised to upees fifty lakhs or more, the company shall, within a period of one year rom the date of such increase, have a whole-time secretary who must be member of the Institute of Company Secretaries of India.

The qualifications possessed by a person holding office of whole-time secretary of a company immediately before 30th October, 1980 shall be deemed to be the qualifications which he shall be required to possess in order to be eligible to continue in that office in that company.

Duties and Rights of a Company Secretary

The duties of a company secretary are multifarious. He is the officer of a company, who is charged with the duty of ensuring that the affairs of the company are conducted in accordance with the provisions of the Companies Act, the company's articles and generally in accordance with the law. For contravention of any law by the company, the company secretary is punishable as officer in default. Apart from such statutory duties directly concerning a secretary, he also performs several other duties of a ministerial or administrative nature. The articles of the company or the board of directors determine the duties of a secretary and

sometimes his contract of service defines such duties.

The rights and powers of the company secretary are governed by his service agreement with the company. Being the head of the secretarial department, he has the right to direct, supervise and control the activities of the department. Being a principal officer of the company, he has a right to sign documents requiring authentication of the company. The secretary as an employee is entitled to a reasonable notice of the dismissal or damages in lieu thereof. As an employee, the secretary has also a right to claim four months' salary not exceeding rupees one thousand as a preferential creditor in the winding-up of the company (Sec. 530). In addition, he has the right to do all such acts as authorised by the directors.

In a recent English case,[59] the Court of Appeal considered a company secretary to be the chief administrative officer of the company and held that he regularly makes representations on behalf of the company and enters into contracts on its behalf which come within the day-to-day running of the company's business.

But the secretary, without express authority of the board of directors, cannot make allotment or register transfer of shares of the company. The company secretary has no right to borrow in the name of the company. Similarly, the company secretary, without express authority, cannot call a general meeting, though the board can ratify such action before the meeting.

QUESTIONS

1. (a) In what different ways may a director of a company be appointed?
(b) When does the office of a director fall vacant?

[C.A. (Final), November 1969, 75]

2. What are the different modes of appointing directors of a public company? Can the following be appointed as directors of a public company:
(a) a minor, (b) a bank, (c) a partnership firm, (d) a trust?

[Delhi, B.Com. (Hons.), 1972]

3. When is the office of a director of a public company deemed to be vacated? Can the directors be removed during their term of office?

[Delhi, B.Com. (Hons.), 1976]

4. Can the directors of a public company be removed from their office before the expiry of their term? *[Delhi, B.Com. (Hons.), 1980]*

5. (a) Directors are not only agents, but also in some sense trustees of the company. Discuss.

[59] *Panorma Development (Guildford) v Fidelis Furnishing Fabrics Ltd.* (1971) 3 All. E.R. 16.

(b) "The Companies Act does not provide for any share qualification for the directors". Comment. *[Delhi, B.Com. (Hons.), 1977]*

6. "Directors are described sometimes as agents, sometimes as trustees and sometimes as managing partners. But each of these expressions is used not as exhaustive of their powers and responsibilities, but as indicating useful points of view from which they may for the moment and for the particular purpose be considered." Elucidate this statement with suitable illustrations.

(Delhi, M. Com., 1977)

7. "Directors are described sometimes as agents, sometimes as trustees and sometimes as managing partners." State your view on the position of directors.

(I.C.W.A., December 1973)

8. Discuss the legal position of directors and their powers.

[C.A.(Final), November 1977]

9. Explain the provisions of the Companies Act, 1956, regarding managerial remuneration. *(Delhi, M.Com., 1976)*

10. To what extent and in what manner do the provisions of the Companies Act, 1956, prohibit the appointment in companies of partners and relatives of its directors? [C.A. (Final), November 1976]

11. Explain the duty of a director to disclose his interest in contracts to be entered into by his company. What are the consequences of non-disclosure?

[Company Secretary (Inter), April 1976]

12. "A director can enter into a trading contract with his own company" Comment. *[Delhi, B.Com. (Hons.) 1974]*

13. "The Board of Directors of a company can do all such acts and things and exercise all such powers as the company itself may do and exercise". Discuss this statement. *[Delhi B. Com. (Hons.), 1978, 1979]*

14. The board of directors is entitled to do all that a company can do. Comment.

(Delhi M. Coom., 1978)

15. Discuss the duties and powers of the directors.

(Meerut, M.Com., 1975)

16. What are the powers of directors in respect of the management of a company and what are the limitations imposed on them by the Companies Act.?

[Delhi, B.Com. (Hons.), 1990]

17. "Subject to specific exceptions, the directors of the governing body are entitled to exercise all the powers of the company." Examine the powers of the Board of Directors under the following heads:

(a) Powers exercisable only at the Board meetings.

(b) Powers exercisable only with the consent of the general body.

(c) Other powers.

18. Examine the liabilities of directors of a company (a) for ultra vires act; (b) for negligence; and (c) for torts or frauds of co-directors. To what extent do the provisions in the Articles relieving the directors from the liability absolve them?

[Company Secretary (Inter), October 1975]

19. What are the measures provided in the Companies Act to protect the interests of a company regarding appointment of sole-selling agent?

[Company Secretary (Final), October 1974]

20. State the various ways in which the directors of a company may be appointed. *[Delhi, B.Com. (Hons.), 1986]*

21. Explain briefly the provisions of the Companies Act, 1956 on managerial remuneration, with appropriate case law and administrative guidelines.

(Delhi, M.Com., 1984)

22. How is a managing director appointed? What are his duties and responsibilities? Discuss the role and powers, if any, of the Government in regard to the appointment of managing directors.

[Company Secretary (Inter), December 1977]

23. A person can be appointed managing director of more than one company Comment. *(Delhi, B. com. (Hons.), 1974)*

24. A company can have any number of managing directors but a person cannot be a managing director of more than one company. Comment.

(Delhi, B. Com. (Hons.), 1980)

25. Distinguish between managing director and whole-time director.

[Delhi, B. Com. (Hons.), 1990]

26. Define the term 'Secretary'. State how and who may be appointed as Secretary of a company. What is his legal position?

(Company Secretary (Inter), April 1973)

PRACTICAL PROBLEMS

1. A private company having two directors has just become a public company by virtue of Sec. 43-A. Is it obligatory for the company to appoint a third director?

(I.C.W.A., June 1973)

2. Mr. A is a director in 19 public limited companies. He is offered directorship of the following:

(a) B.C. Private Ltd.

(b) XYZ Limited, a public limited company.

(c) Indian Automobile Association, a company registered under Section 25 of the Companies Act.

State with reasons whether he can accept the above mentioned directorships.

(C.A. (Final), November 1975)

3. Can the following persons be appointed as directors of a public company (a) a minor, (b) a bank, (c) a partnership, (d) a trust.

(Delhi, B. Com. (Hons.), 1972)

4. Who can appoint:

(i) an alternate director,

(ii) an additional director, and

(iii) a director to fill the casual vacancy and when do the above directors vacate their office as directors? (Company Secretary (Final), October 1975)

5. In a public company the following situations have arisen:

(i) One of the directors of the company has died and the Board of Directors wants to fill up the casual vacancy.

(ii) One of the directors of the company proposes to visit USA for four months and the Board of Directors wants to appoint an alternate director in his place.

(iii) According to the articles of association of the company the maxmum number of directors has been fixed at 11. At the relevant time there are only 9 directors. The Board of Directors wants to appoint 2 additional directors.

You are requested to advise the company about the steps to be taken for making the above appointments. *(C.A. (Final), May 1975)*

6. The articles of association of a company provide that the number of directors shall not be less than 3 or more than 12. The present Board consists of 12 directors. The company wants to appoint 3 more directors on the Board. Advise the company about the steps to be taken for the purpose. *[C.A. (Final), May 1975]*

7. Can a company provide that a person shall not be capable of being appointed as a director of the company if he is illiterate?

[Company Secretary (Inter), April 1973]

8. A director of a company, whose articles require the holding of share qualification, has held the shares within the prescribed time but did not get the shares registered in his name within 2 months of his appointment. Is this in order?

[Company Secretary(Inter), June 1979]

9. The directors of a public company passed a resolution to make a call. Subsequently, it transpired that one of the directors present at the meeting had not been validly appointed. Could the call be enforced?

(Delhi, B.Com. (Hons.), 1973)

10. Can a company advance loan to its directors?

11. The directors of a public company have to travel very often for the company's business. The company makes some advances to them for the purpose which sometimes exceed the actual requirements. In such a case, would any provision of the Companies Act be contravened? *(C.A., November 1969)*

12. All the directors of a company are interested in a contract, which the company intends to enter into. What should that company do so that it is enabled to enter into the contract without violating Section 297 of the Companies Act?

(Company Secretary (Final), December 1977)

13. Section 300 debars an interested director from voting at a board meeting. What will be the situation in respect of quorum if all except one director are interested persons? *[Company Secretary (Inter), June 1977]*

14. The usual powers of mangement of a company are vested in the Board of Directors by the articles of assocition, which also include a provision that the powers shall be "subject to such regulations not inconsistent with the articles, as may be prescribed by the company in general meeting". In exercise of their powers the directors filed a suit against an employee of the company for recovery of a loan advanced to him. The general body of shareholders thereupon passed an ordinary resolution to the effect that the loan should be written off in consideration of the employee's meritorious services to the company. Are the directors bound to withdraw the suit or are they at liberty to proceed with the suit? Give reasons for your answer.

(C.A., May 1969)

15. The directors bought shares from a shreholder when negotiations were being held by them for sale of the company at a very high price. They did not disclose this fact to the shareholder. The shareholder sued to have the sale set aside.

Decide.

16. The articles of the company exempted the directors of the company from liability in respect of acts of default and negligence. Due to the negligence of the directors the company was compelled to pay a certain amount of money to a third party. What is the liability of the directors to the company?

[C.A. (Final), May 1975]

17. The board of directors of F.G. Limited have the following proposals to be discussed at the board's meeting:

(i) Appointment of A, relative of one of the directors, on a salary of Rs 25,000 p.m., as Chief Accountant of the company.

(ii) To give guarantee to State Bank of India on behalf of AB Private Ltd. in which a director of the company is also a director.

(iii) To borrow Rs 50 lakhs from State Bank by mortgaging the fixed assets of the company. The company's paid up capital is Rs 25 lakhs and it has no reserves.

Advise the board in respect of above proposals in the light of provisions of the Companies Act.

[C.A. (Final), November 1975]

18. Your company's managing director tells you: "Appoint my brother Shri Chimanlal, as the General Manager of the Company from 1st January, 1999 on a monthly salary of Rs 18,000." Explain the legal provisions.

19. Mr Banerjee is the managing director of a public limited company having a paid up share capital of Rs 2 crores. He is also a director and a member of a private limited company. The public limited company proposes to enter into a contract with the private limited company to sell to the latter goods of the value of Rs 5 lakhs on credit. When can such a contract be entered into?

[Company Secretary (Inter), December 1977]

20. Can a person be appointed a managing director without first being appointed a director?

[Company Secretary (Inter), June 1979]

21. (a) Smt *M* is Managing Director of *A* Private Ltd and *B* Private Ltd., two independent companies. She is appointed as a managing director of *C* Private Ltd., another independent company. Is her appointment in the third company valid?

(b) Will there by any change in your answer if *C* Private Ltd. is a subsidiary of D Ltd.?