LIST OF IMPORTANT SECTIONS BASED ON COMPANIES ACT WITH COMPLETE SUMMARY OF COMPANIES ACT….PART 2

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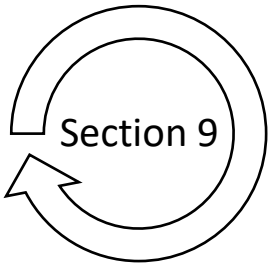
PART 2	
Section 4- Memorandum. + Sec -399+sec2(56)+ Table A TO E	**Meaning** MOA of a Company is its charter and defines the limitations of the powers of a Company. **Definition Sec 2(56)** Memorandum means Memorandum of Association of a Company • As originally framed • As altered from time to time In pursuance of any previous company law or of this act. ➢ A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions contained therein. **Content of MOA** **(a) Name Clause,** ➢ The name of the company **(Name Clause)** with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company. This clause is not applicable on the companies formed under section8 of the Act. **(b) Situation Clause,** ➢ The State in which the registered office of the company **(Registered Office clause)** is to be situated **(c) Object Clause (Main objects / incidental & ancillary objects / other objects),** ➢ The objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof **(Object clause);** **(d) Liability Clause,** ➢ The liability of members of the company **(Liability clause)**, whether limited or unlimited **(e) Capital Clause,** ➢ The amount of authorized capital **(Capital Clause)** divided into share of fixed amounts and the number of shares with the subscribers to the memorandum has agreed to take, indicated opposite their names, which

	shall not be less than one share. A company not having share capital need not have this clause. **(f) <u>Association Clause</u>** ➢ The desire of the subscribers to be formed into a company. The Memorandum shall conclude with the **association clause.** Every subscriber to the Memorandum shall take at least one share, and shall write against his name, the number of shares taken by him. **<u>Forms of MOA</u>** **Form of MOA per Schedule I** – Company limited by shares – **Table A**, Company limited by Guarantee & not having Share Capital – **Table B**, Company limited by Guarantee & having Share capital – **Table C**, Unlimited Company having no share capital – **Table D**, Unlimited Company having share capital – **Table E.**
<u>Section 5- Articles. + SEC 2 (5)+ TABLE F TO J</u>	**<u>AOA Meaning</u>** AOA is bye laws of the Company which lays down the rules and regulation for internal management. **<u>Definition Sec 2(5)</u>** Articles means Articles of Association of a Company • As originally framed • As altered from time to time In pursuance of any previous company law or of this act. **<u>Format</u>** **Table F** – AOA of Company limited by Shares **Table G** – AOA of a Company limited by Guarantee and having SC **Table H** – AOA of a Company limited by Guarantee and not having SC **Table I** – AOA of a Unlimited Company, having share capital **Table J** – AOA of a unlimited company, Not having share capital **<u>General of contents AOA</u>** (a) Regulations for management, (b) Such matters as may be prescribed, (c) Additional matters if considered necessary for its management

	Meaning of Entrenchment Entrenchment means making alteration of AOA more difficult to protect the minority. **Entrenchment provisions in AOA** ➢ Either on the formation of the company; or ➢ Subsequently with the unanimous consent of all the members in the case of private company and by special resolution in the case of public company.
Section 6- Act to override memorandum, articles, etc.	According to Section 6 of the Companies Act, the Act overrides the memorandum and articles of association and any provision contained in these documents repugnant to the provisions of the Companies Act, **is void.**
Section 7- Incorporation of company. +SEC 2(69)+ INCORPORATION RULES 2014	**Promoters – Definition** (a) Named in the prospectus; (b) Identified in the Annual Return; (c) Person who has control over the affairs of the Company; Person with whose advice, directions or instructions the BOD is accustomed to act (Other than professional capacity) **Promoters – Meaning** The person who is interested or engaged in the formation of Company and must have desire to form a Company. Person assisting the promoters in a professional capacity are not promoters. **Section 7** of the Companies Act, 2013 provides for the Procedure to be followed for incorporation of a company. **Documents and information to be filed with the registrar:** **SPICe+ , INC-32 and the following** • The **memorandum and articles** of the company duly signed by all the subscribers to the Memorandum. • a **declaration** by person who is engaged in the formation of the company (**an advocate, a chartered accountant, cost accountant or company secretary in practice**), **and** by a person named in the articles (**director, manager or secretary of the company),** that all the requirements of this Act and the rules made

	there under in respect of registration and matters precedent or incidental thereto have been complied with. • A **declaration from each of the subscribers** to the memorandum and from persons named as the first directors, if any, in the articles stating that- • He is **not convicted of any offence** in connection with the promotion, formation or management of **any company, or** • He has **not been found guilty of any fraud** or misfeasance or of any breach of duty to any company under this Act or any previous company law during the **last five years,** • And that all the documents filed with the Registrar for registration of the company **contain information that is correct and complete and true** to the best of his knowledge and belief; • the **address for correspondence** till its registered office is established; • the **particulars** (names, including surnames or family names, residential address, nationality) **of every subscriber** to the memorandum along with proof of identity, and in the case of a subscriber being a body corporate, such particulars as may be prescribed. • the **particulars** (names, including surnames or family names, the Director Identification Number, residential address, nationality) of the persons mentioned in the articles as the **first directors** of the company and such other particulars including proof of identity as may be prescribed; and • Particulars provided in this provision shall be of the individual subscriber and not of the professional engaged in the incorporation of the company *[The Companies (Incorporation) Rules, 2014]*. **Effect of Incorporation of company by furnishing false information:** **Order of the Tribunal:** where a company has been got incorporated by furnishing false or incorrect information or representation or by suppressing any material fact or information in any of the documents or declaration filed or made for incorporating such company or by any fraudulent action, the Tribunal may, on an application made to it, on being satisfied that the situation so warrants,—

	(a) pass such orders, as it may think fit, for regulation of the management of the company including changes, if any, in its memorandum and articles, in public interest or in the interest of the company and its members and creditors; or (b) direct that **liability of the members shall be unlimited**; or (c) **direct removal of the name** of the company from the register of companies; or (d) pass an **order for the winding up** of the company; or (e) pass such other orders as it may deem fit: Provided that before making any order,— • the company shall be given a reasonable opportunity of being heard in the matter;
Section 9- Effect of registration.	 • **Perpetual succession** • **Legal person separate from the incorporators**
Section 10- Effect of memorandum and articles.	**Binding effect of registration of MOA and AOA** (a) Members bound to Co. – Shares liable for forfeiture upon non payment of call money. (b) Company bound to Members – Allow to caste vote (c) Members bound to other members – Provision in AOA requiring intimation of fact of transfer of shares provides upon transfer of Shares by Member intimation shall be given to them. (d) MOA and AOA do not confer any rights to outsiders. (Person named as auditor of the company in AOA does not bind the Company, the referred person can be removed and some other person be appointed as Auditor)

Section 43- Kinds of share capital.	**(i) Equity share capital** The share capital of a company limited by shares shall be of two kinds, namely:— **(a) equity share capital—** (i) with voting rights; or (ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed; and **(b) preference share capital:** "Preference share capital", with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to— (a) **payment of dividend,** either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax; and (b) **repayment, in the case of a winding up** or repayment of capital, Where any notice, advertisement or other official communication or any business letter, bill head or letter paper of a company states the authorised capital, the subscribed and paid-up capital must also be stated in equally conspicuous characters. A default in this regard will make the company and every officer who is in default liable to pay penalty extending ` 10,000 and ` 5,000 respectively. **bbbb**
Section 44- Nature of shares or debentures.	The shares or debentures or other interests of any member in a company shall be **movable property** transferable in the manner provided by the articles of the company
Section 45- Numbering of shares.	Every share in a company having a share capital, shall be distinguished by its **distinctive number** This shall not apply to a share held by a person whose name is entered as holder of beneficial interest in such share in the records of a depository.
DOCTRINE OF ULTRA VIRES	**Doctrine of Ultra Vires**

	Any purported activity beyond the powers conferred by MOA is ultra vires acts. Ultra means "beyond" and Vires means "powers". **Effect of Ultra vires Acts** (a) Void-ab-initio, (b) Injunction can be issued against performance of ultra vires acts, (c) Personal Liability of Directors, Criminal action for deliberate misapplication **Exceptions to the Doctrine of Ultra Vires** (a) Ultra Vires Directors but Intra Vires AOA and MOA – SH can ratify. (b) Ultra Vires AOA intra vires MOA – SH can ratify by AOA amendment. (c) Ultra Vires MOA intra vires statute – SH can ratify by MOA amendment. (d) Ultra Vires statute – Cannot be ratified. Null and Void (e) Company money used to acquire ultra vires property will be secured Ultra Vires borrowing used to pay Intra Vires debts – Ultra Vires creditor steps into the shoes of intra vires creditor
DOCTRINE OF CONSTRUCTIVE NOTICE	**Doctrine of Constructive Notice** • ***ASSUMOR = COMPANY/DIRECTOR*** • **ASSUMPTION = Outsider dealing with the company has read MOA / AOA** • **FAVOUR =Operates in favour of a Company.** MOA and AOA are public documents. Third party dealing with Company has means of ascertaining and is presumed to know the powers and the extent to which they have been delegated to Directors.
DOCTRINE OF INDOOR MANAGEMENT	**Doctrine of Indoor Management** Persons dealing with the Company can safely presume that internal proceedings have been observed properly or complied with. They need not inquire into the regularity of internal proceedings. **Exceptions to Doctrine of Indoor Management** (a) Knowledge of irregularity,

	(b) No protection for the person who does not rely on MOA and AOA, (c) Forgery / Void Contracts / Illegal Contracts, (d) Not a tool to protect the person who act negligently

Questions Based On Above Summary

Question 1

"The Memorandum of Association is a charter of a company". Discuss. Also explain in brief the contents of Memorandum of Association.

Answer

The Memorandum of Association of company is in fact its charter; it defines its constitution and the scope of the powers of the company with which it has been established under the Act. It is the very foundation on which the whole edifice of the company is built.

Object of registering a memorandum of association:

* It contains the object for which the company is formed and therefore identifies the possible scope of its operations beyond which its actions cannot go.
* It enables shareholders, creditors and all those who deal with company to know what its powers are and what activities it can engage in.

  A memorandum is a public document under Section 399 of the Companies Act, 2013. Consequently, every person entering into a contract with the company is presumed to have the knowledge of the conditions contained therein.
* The shareholders must know the purposes for which his money can be used by the company and what risk she is taking in making the investment.

A company cannot depart from the provisions contained in the memorandum how ever imperative may be the necessity for the departure. It cannot enter into a contract or engage in any trade or business, which is beyond the power confessed on it by the memorandum. If it does so, it would be ultravires the company and void.

Content of the memorandum: The memorandum of a company shall state—

(a) The name of the company **(Name Clause)** with the last word "Limited" in the case of a public limited company, or the last words "Private Limited" in the case of a private limited company. This clause is not applicable on the companies formed under section8 of the Act.

(b) The State in which the registered office of the company **(Registered Office**

clause) is to be situated;

(c) The objects for which the company is proposed to be incorporated and any matter considered necessary in furtherance thereof **(Object clause);**

(d) The liability of members of the company **(Liability clause)**, whether limited or unlimited,

(e) The amount of authorized capital **(Capital Clause)** divided into share of fixed amounts and the number of shares with the subscribers to the memorandum have agreed to take, indicated opposite their names, which shall not be less than one share. A company not having share capital need not have this clause.

(f) The desire of the subscribers to be formed into a company. The Memorandum shall conclude with the **association clause.** Every subscriber to the Memorandum shall take at least one share, and shall write against his name, the number of shares taken by him.

Question 2

Briefly explain the doctrine of "ultra vires" under the Companies Act, 2013. What are the consequences of ultravires acts of the company?

Answer

Doctrine of ultra vires:

The meaning of the term ultra vires is simply "beyond (their) powers". The legal phrase "ultra vires" is applicable only to acts done in excess of the legal powers of the doers. This presupposes that the powers are in their nature limited. To an ordinary citizen, the law permits whatever does the law not expressly forbid.

It is a fundamental rule of Company Law that the objects of a company as stated in its memorandum can be departed from only to the extent permitted by the Act-thus far and no further ***[Ashbury Railway Company Ltd. vs. Riche].*** In consequence, any act done or a contract made by the company which travels beyond the powers not only of the directors but also of the company is wholly void and inoperative in law and is therefore not binding on the company. On this account, a company can be restrained from employing its fund for purposes other than those sanctioned by the memorandum. Likewise, it can be restrained from carrying on a trade different from the one it is authorized to carry on.

The impact of the doctrine of ultra vires is that a company can neither be sued on an ultra vires transaction, nor can it sue on it. Since the memorandum is a "public document" , it is open to public inspection. Therefore, when one deals with a company one is deemed to know about the powers of the company. If in spite of this you enter into a transaction which is ultra vires the company, you cannot enforce it against the company. For example, if you have supplied goods or performed service on such a contract or lent money, you cannot obtain payment or recover the money lent. But if the money advanced to the company has not been

expended, the lender may stop the company from parting with it by means of an injunction; this is because the company does not become the owner of the money, which is ultra vires the company. As the lender remains the owner, he can take back the property in specie. If the ultra vires loan has been utilized in meeting lawful debt of the company then the lender steps into the shoes of the debtor paid off and consequently he would be entitled to recover his loan to that extent from the company.

An act which is ultra vires the company being void, cannot be ratified by the shareholders of the company. Sometimes, act which is ultra vires can be regularized by ratifying it subsequently. For instance, if the act is ultra vires the power of the directors, the shareholders can ratify it; if it is ultra vires the articles of the company, the company can alter the articles; if the act is within the power of the company but is done irregularly, share holder can validate it.

Question 3

Explain in brief the mode of incorporation of a company.

Answer

Mode of registration/incorporation of company: In terms of section 3(1)(a) a public company may be formed for any lawful purpose with 7 or more persons by subscribing their names to a memorandum and complying with the requirements of the Companies Act for the registration of companies.

In exactly the same way, under section 3 (1)(b), 2 or more persons can form a private company. Under section 3 (1)(c) a one person company may be formed by one person in which case the company will be a private company.

Persons who conceive the idea of forming the company and form the same under the provisions of the Act are known as promoters.

They take all necessary steps for its registration.

(a) **Lawful purpose:** The essence of validly incorporated company is that it must consist of a particular number of persons and must be set up for a lawful purpose. Unless the purpose appears to be unlawful ex facie or is transparently illegal or prohibited by way of statute, it cannot be regarded as an unlawful purpose.

(b) **Applying for the name:** The promoters of the company should decide upon at least three suitable names in order of preference in order to afford flexibility to the Registrar in deciding on the availability of the best possible available name.

(c) **Documents to be filed:** After getting the name approved, certain documents along with the application and prescribed fees, should be filed with the Registrar.

(d) **Subscribing their names:** Subscribing the names means signing the names in the Memorandum signifying their intention to jointly form a company and take up the number of shares mentioned against each.

(e) **Certificate of incorporation:** Upon the registration of the documents mentioned earlier under the head "Documents to be filed for registration of the company" and the payment of the necessary fees, the Registrar of Companies issues a certificate that the company is incorporated, and in the case of a limited company that it is limited.

Question 4

The Memorandum of Association of a company was presented to the Registrar of Companies for registration and the Registrar issued the certificate of incorporation. After complying with all the legal formalities a company started a business according to the object clause, which was clearly an illegal business. The company contends that the nature of the business cannot be gone into as the certificate of incorporation is conclusive. Answer the question whether company's contention is correct or not.

Answer

Section 3 of the Companies Act, 2013 states that a company may be formed for any lawful purpose by 7 or more persons in case of public company, 2 or more persons in case of private company and 1 person in case of a one person company. Hence, a company cannot be formed for an unlawful purpose or for carrying on illegal business.

Section 9 of the Act further provides that from the date of incorporation mentioned in the certificate of incorporation, such subscribers to the memorandum and all other persons, as may from time to time, become members of the company, shall be a body corporate capable of exercising all the functions of an incorporated company under this Act. Under this Act a company can be formed for a lawful purpose. Hence, a company cannot be formed in the first place for an illegal business activity.

In the present case the Registrar was at fault in issuing the certificate of incorporation but the issue of the certificate of incorporation does not give the company the right to do illegal business.

Question5

The object clause of the Memorandum of Association of LSR Private Ltd, Lucknow authorized it to do trading in fruits and vegetables. The company, however, entered into a Partnership with Mr. J and traded in steel and incurred liabilities to Mr. J. The Company, subsequently, refused to admit the liability to J on the ground that the deal was 'Ultra Vires' the company. Examine the validity of the company's refusal to admit the liability to J. Give reasons in support of your answer.

Answer

In terms of section 4(1)(c) of the Companies Act, 2013, the powers of the company are limited to:

Powers expressly given in the "Objects Clause" of the Memorandum (which is popularly known as 'express' power), or conferred by the Companies Act, or by any other statute and

powers reasonably incidental or necessary to the company's main objects (termed as "Implied' powers).

The Act further provides that the acts beyond the powers of a company are ultra vires and void and cannot be ratified even though every member of the company may give his consent [Ashbury Railway Carriage Company Vs Richee]

The objects clause enables the shareholders, creditors or others to know what its powers are and what is the range of its activities. The objects clause therefore is of fundamental importance to the shareholders, creditors and every other person who deals with the company in any manner what so ever. A company being an artificial legal person can act only within the ambit of the powers conferred upon it by the Memorandum through the "Objects Clause".
Every who enters into a contractual relationship with a company on any matter is presumed to be aware of its objects and is supposed to have examined the Memorandum of Articles of the company to ensure proper contractual agreement. If a person fails to do so, it is entirely at his own risk.

M/s LSR Pvt. Ltd is authorised to trade directly on fruits and vegetables. It has no power to enter into a partnership for Iron and steel with Mr. J. Such act cannot be treated as being within either the 'express' or 'implied' powers of the company. Mr J who entered into partnership is deemed to be aware of the lack of powers of M/s LSR (Pvt) Ltd. In the light of the above, Mr, J cannot enforce the agreement or liability against M/s LSR Pvt. Ltd under the Companies Act. Mr. J should be advised accordingly.

However, under the Indian Contract Act, 1872 where a person derives any benefit either in the absence of a contract or under a void agreement, will be liable to make a reasonable payment for the value of such benefit. (Please refer to Quasi Contracts and Void Agreements)

Question 6

Explain the steps to be taken by a company for starting a business for which there is no provision in the objects clause of the Memorandum of Association.

Answer

Section 4 (1) (c) of the Companies Act 2013 clearly provides for the Memorandum to include the objects for which the company is formed. A company is therefore, formed to carryon activities only in line with its objects as defined in the Memorandum.

Any act outside the objects clause is termed "ultra vires" and is considered void. Hence, if a company wishes to start a business which is not provided for in its Memorandum, it must first alter its Memorandum to include that business in its objects clause.

This is a simple process defined in section 13 of the Act. It can be done with the approval of the members by a special resolution and the registration of the same with the Registrar.

Question 7

The Articles of Association of a Limited Company provided that 'X' shall be the Law Officer of the company and he shall not be removed except on the ground of proved misconduct. The

company removed him even though he was not guilty of misconduct. Decide, whether company's action is valid?

Answer

Section 5 (1) of the Companies Act, 2013 states that the Articles of a company contain the regulations for the management of a company. Further section 5 (2) provides that the Articles of a company shall contain all matters that are prescribed under the Act and also such additional matters as may be considered necessary for the management of the company.

Removal of Law Officer: The Memorandum and Articles of Association of a company are binding upon company and its members and they are bound to observe all the provisions of memorandum and articles as if they have signed the same [Section 10(1)].

However, the company and members are not bound to outsiders in respect of anything contained in memorandum/articles by which such outsiders have been given any rights. This is based on the general rule of law that a stranger to a contract cannot acquire any right under the contract.

In this case, Articles conferred a right on 'X', the law officer that he shall not be removed except on the ground of proved misconduct. In view of the legal position explained above, 'X' cannot enforce the right conferred on him by the articles against the company. Hence the action taken by the company (i.e. removal of 'X' even though he was not guilty of misconduct) **is valid. However, by altering the Articles by a special resolution under section 14 of the Act and Mr. X can be removed.**

Question 8

What is the meaning of "Certificate of Incorporation" under the provisions of the Companies Act, 2013?

Answer

Certificate of Incorporation: Under section 7 (2) the Registrar shall on the basis of documents and information filed for the formation of a company, shall register the aforesaid documents and information and issue a certificate that the company is incorporated in the prescribed form to the effect that the proposed company is incorporated under this Act.

Section 7 (3) further provides that on and from the date of incorporation mentioned in the certificate of incorporation the Registrar shall allot to the company a Corporate Identification Number(CIN) which shall be the distinct identity of the company and which shall also be included in the certificate of incorporation. The company becomes a legal entity from the date mentioned in the certificate of incorporation and continues to be so till it is wound up

Question 9

What are the effects of registration of a company?

Answer

Section 9 of the Companies Act, 2013 provides that, from the date of incorporation mentioned in the certificate of incorporation, such of the subscribers to the Memorandum and all other persons, as may from time to time become members of the company, shall be a body corporate by the name contained in the memorandum, capable forthwith of exercising all the functions of an incorporated company under this Act and having perpetual succession with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued by the said name. Accordingly, when a company is registered and a certificate of incorporation is issued by the Registrar, three important consequences follow:

- The company becomes a distinct legal entity. Its life commences from the date mentioned in the certificate of incorporation capable of entering into contracts in its own name, acquiring, holding and disposing of property of any nature whatsoever and capable of suing and being sued in its own name.

- It acquires a life of perpetual existence by the doctrine of succession. The members may come and go, but it goes on forever, unless it is wound up.

- Its property is not the property of the shareholders. The shareholders have a right to share in the profits of the company as and when declared either as divided or as bonus shares. Likewise any liability of the company is not the liability of the individual shareholders.

Question 10

X, a chemical manufacturing company distributed 20 lacs (` Twenty Lacs) to scientific institutions for furtherance of scientific education and research. Referring to the provisions of the Companies Act, 2013 decide whether the said distribution of money was "Ultra vires" the company?

Answer

Distribution of Rupees Twenty Lacs by a company engaged in Chemical manufacturing is not 'Ultravires' since it was conducive to the continued growth of the company as chemical manufacturers (Evans vs Brunner, Mood & Co. Ltd.1921). In order for a contract to be ultra vires, it would be essential to refer to its objects clause. Restrictions of the type mentioned in the question are not an item of the Objectives Clause. Hence, the issue of ultra vires does not arise to such a donation.

Question 11

"The Doctrine of Indoor Management always protects the persons (outsiders) dealing with a company." Explain the above statement. Also, state the exceptions to the above rule.

Answer

Doctrine of Indoor Management (the Companies Act, 2013): According to the "doctrine of indoor management" the outsiders, dealing with the company though are supposed to have satisfied themselves regarding the competence of the company to enter into the proposed contracts are also entitled to assume that as far as the internal compliance to procedures and regulations by the company is concerned, everything has been done properly.

They are bound to examine the registered documents of the company and ensure that the proposed dealing is not inconsistent therewith, but they are not bound to do more. They are fully entitled to presume regularity and compliance by the company with the internal procedures as required by the Memorandum and the Articles.

This doctrine is a limitation of the doctrine of "constructive notice" and popularly known as the rule laid down in the celebrated case of Royal British Bank v. Turquand.

Thus, the doctrine of indoor management aims to protect outsiders against the company.

Exceptions:

In the following circumstances an outsider dealing with the company can not claim any relief on the ground of "indoor management":

1. Knowledge of irregularity: Where a person dealing with a company has actual or constructive notice of the irregularity as regards internal management, he can not claim the benefit under the rule of indoor management.

2. Negligence: Where a person dealing with a company could discover the irregularity if he had made proper inquiries, he can not claim the benefit of the rule of indoor management. The protection of this rule is also not available where the circumstances surrounding the contract are so suspicious as to invite inquiry, and the outsider dealing with the company does not make proper inquiry (Anand Bihari Lel v. Dinshaw& Co.), (Under-Wood v. Bank of Liver Pool).

3. Act void ab initio and forgery: Where the acts done in the name of a company are void ab initio, the doctrine of indoor management does not apply. The doctrine applies only to irregularities that otherwise might affect a genuine transaction.

4. Acts outside the scope of apparent authority: If an officer of a company enters into a contract with a third party and if the act of the officer is apparently beyond the scope of his authority, the company is not bound (Kreditbank Cassel v. Schenkers Ltd.).

Question 12

Briefly explain the doctrine of "Constructive Notice" under the Companies Act, 2013. Are there any exceptions to the said doctrine?

Answer

Doctrine of Constructive Notice:

In consequences of the registration of the memorandum and articles of association of the company with the Registrar of Companies, a person dealing with the company is deemed to have constructive notice of their contents (T.R. Pratt (Bombay) Ltd. v. E.D. Sassoon & Co. Ltd.). This is because these documents are construed as 'public documents'.

Accordingly if a person deals with a company in a manner incompatible with the provisions of the aforesaid documents or enters into transaction which is ultra vires these documents, he must do so at his peril. The doctrine of constructive notice is not a positive one but a negative one like that of estoppels of which it forms parts.

It operates only against the person who has been dealing with the company but not against the company itself; consequently he is prevented from alleging that he did not know that the constitution of the company rendered a particular act or a particular delegation of authority ultra vires. There is one limitation to the doctrine of constructive notice of the Memorandum and the Articles of a company.

The outsiders dealing with the company are on their part entitled to assume that as far as the internal proceedings of the company are concerned, everything has been done properly in accordance with the Memorandum and Articles and the Act.

They are only bound to read the registered documents and satisfy themselves that the proposed dealing is not inconsistent therewith, but are not bound to do more; they need not inquire into the regularity of the internal proceedings as required by the Memorandum and the Articles.

This limitation of the doctrine of constructive notice is known as the 'doctrine of indoor management' or the rule laid down in the celebrated case of Royal British Bank v. Turquand. Thus, whereas the doctrine of constructive notice protects the company against outsiders, the doctrine of indoor management seeks to protect outsiders against the company.

Question 13

Explain the doctrine of 'Indoor management' in brief. The Secretary of a Company issued a share certificate to 'A' under the Company's seal with his own signature and the signature of a Director forged by him. 'A' borrowed money from 'B' on the strength of this certificate. 'B' wanted to realise the security and requested the company to register him as a holder of the shares. Explain whether 'B' will succeed in getting the share registered in his name.

Answer

The doctrine of Indoor Management is laid down in the Royal British Bank vs. Turquand case in which the directors of RBB (Royal British Bank) gave a bond to one T (Turquand) without the required resolution being passed.

The Articles empowered the directors to issue such bonds under the authority of a proper resolution. In fact no such resolution was passed. It was decided in the case that notwithstanding the non passing of the required resolution, T could sue on the bonds on the ground that he was entitled to assume that the resolution had been duly passed.

Thus, the persons dealing with the company are entitled to assume that the acts of the directors or the officers of the company are validly performed, if they are within the scope of their apparent authority.

However, this doctrine is not applicable where the person dealing with the company has notice of irregularity or when an instrument purporting to be enacted on behalf of the company is a forgery.

In the instant problem the doctrine of indoor management will not apply as the certificate is a forgery which does not give a good title to A and thereby to B. The title of the buyer cannot be better than that of the seller (Sale of Goods Act, 1930). **Hence, 'B' will not succeed in getting the share registered in his name.**

Question 14

A Managing Director of a company borrowed a sum of money by executing a document in which he forged the signature of two other directors who are required to sign as per requirements of articles. Can the company deny liability to creditors?

Answer

In Ruben v. Great Fingall Consolidated, it was held that Doctrine of Indoor Management could not be extended to cases of forgery. Transaction effected by forgery is void ab initio. However, in Sri Krishan v. Mondal Bros. & Co. it was held that a company may be held liable for any fraudulent Acts of its officers acting under ostensible authority. Therefore, in the instant case, company will not be allowed to deny liability in order to defeat bona fide claims of the creditor.