

LL.B IV SEMESTER

Subject- Company Law, 2013

Topic –Meaning ,Definition and Characteristics of Company

The concept of 'Company' or 'Corporation' in business is not new but was dealt with, in 4th century BC itself during 'Arthashastra' days. Its' shape got revamped over a period of time according to the needs of business dynamics. Company form of business has certain distinct advantages over other forms of businesses like Sole Proprietorship/Partnership etc. It includes features such as Limited Liability, Perpetual Succession etc.

After reading this lesson, you would be able to understand the historical development in the evolution of corporate law in India and England, emerging regulatory aspects including Companies Act, 2013, besides dealing with basic characteristics of the company and how it differs from other forms of businesses

I. Meaning of a Company

The word 'company' is derived from the Latin word (Com=with or together; panis =bread), and it originally referred to an association of persons who took their meals together. In the leisurely past, merchants took advantage of festive gatherings, to discuss business matters.

Nowadays, business matters have become more complicated and cannot be discussed at festive gatherings. Therefore, the company form of organization has assumed greater importance. It denotes a joint-stock enterprise in which the capital is contributed by several people. Thus, in popular parlance, a company denotes an association of likeminded persons formed for the purpose of carrying on some business or undertaking. It is called a body corporate because the persons composing it are made into one body by incorporating it according to the law and clothing it with legal personality. The word 'corporation' is derived from the Latin term 'corpus' which means 'body'. Accordingly, 'corporation' is a legal person created by a process other than natural birth. It is, for this reason, sometimes called an artificial legal person. As a legal person, a corporation is capable of enjoying many of the rights and incurring many of the liabilities of a natural person.

An incorporated company owes its existence either to a special Act of Parliament or to company law. Public corporations like Life Insurance Corporation of India, SBI etc., have been brought into existence by special Acts of Parliament, whereas companies like Tata Steel Ltd., Reliance Industries Limited have been formed under the Company law i.e. Companies Act, 1956 which is being replaced by the Companies Act, 2013.

II. Definition of Company

In the legal sense, a company is an association of both natural and artificial persons (and is incorporated under the existing law of a country). In terms of the Companies Act, 2013 (Act No.

18 of 2013) a “company” means a company incorporated under this Act or under any previous company law [Section 2(20)].

A company is not merely a legal institution. It is rather a legal device for the attainment of the social and economic end. It is, therefore, a combined political, social, economic and legal institution. Thus, the term company has been described in many ways. “It is a means of cooperation and organization in the conduct of an enterprise”.

It is “an intricate, centralized, economic and administrative structure run by professional managers who hire capital from the investor(s)”

The persons who contributed in it or form it, or to whom it belongs, are members. The proportion of capital to which each member is entitled is his “share”. The shares are always transferable although the right to transfer them may be restricted.”

From the foregoing discussion, it is clear that a company has its own corporate and legal personality distinct which is separate from its members. A brief description of the various attributes is given here to explain the nature and characteristics of the company as a corporate body

III. Nature and Characteristics of a Company

Since a corporate body (i.e. a company) is the creation of law, it is not a human being, it is an artificial juridical person (i.e. created by law); it is clothed with many rights, obligations, powers, and duties prescribed by law; it is called a ‘person’.

Being the creation of law, it possesses only the powers conferred upon it by its Memorandum of Association which is the charter of the company. Within the limits of powers conferred by the charter, it can do all acts as a natural person may do.

The most striking characteristics of a company are:

(i) Corporate personality

A company incorporated under the Act is vested with a corporate personality so it redundant bears its own name, acts under a name, has a seal of its own and its assets are separate and distinct from those of its members. It is a different ‘person’ from the members who compose it. Therefore it is capable of owning property, incurring debts, borrowing money, having a bank account, employing people, entering into contracts and suing or being sued in the same manner as an individual.

Its members are its owners however they can be its creditors simultaneously. A shareholder cannot be held liable for the acts of the company even if he holds virtually the entire share capital.

A Company is an artificial person created by law. It is not a human being but it acts through human beings. It is considered as a legal person which can enter into contracts, possess properties in its own name, sue and can be sued by others etc. It is called an artificial person since it is invisible, intangible, existing only in the contemplation of law. It is capable of enjoying rights and being subject to duties.

(ii) Limited Liability

The privilege of limited liability for business debts is one of the principal advantages of doing business under the corporate form of organization. The company, being a separate person, is the owner of its assets and bound by its liabilities.

The liability of a member as a shareholder extends to the contribution to the capital of the company up to the nominal value of the shares held and not paid by him. Members, even as a whole, are neither the owners of the company's undertakings nor liable for its debts. There are various *exceptions to the principle of limited liability*.

(iii) Perpetual Succession

An incorporated company never dies, except when it is wound up as per law. A company, being a separate legal person is unaffected by death or departure of any member and it remains the same entity, despite the total change in the membership. A company's life is determined by the terms of its Memorandum of Association. It may be perpetual, or it may continue for a specified time to carry on a task or object as laid down in the Memorandum of Association. Perpetual succession, therefore, means that the membership of a company may keep changing from time to time, but that shall not affect its continuity.

The membership of an incorporated company may change either because one shareholder has sold/transferred his shares to another or his shares devolve on his legal representatives on his death or he ceases to be a member under some other provisions of the Companies Act.

Thus, perpetual succession denotes the ability of a company to maintain its existence by the succession of new individuals who step into the shoes of those who cease to be members of the company. Professor L.C.B. Gower rightly mentions

(iv) Separate Property

A company is a legal person and entirely distinct from its members, is capable of owning, enjoying and disposing of property in its own name. The company is the real person in which all its property is vested, and by which it is controlled, managed and disposed of

(v) Transferability of Shares

The capital of a company is divided into parts, called shares. The shares are said to be a movable property and, subject to certain conditions, freely transferable, so that no shareholder is permanently or necessarily wedded to a company. When the joint-stock companies were established, the object was that their shares should be capable of being easily transferred, [**In Re. Balia and San Francisco Rly., (1968) L.R. 3 Q.B. 588**].

Section 44 of the Companies Act, 2013 enunciates the principle by providing that the shares held by the members are movable property and can be transferred from one person to another in the manner provided by the articles.

If the articles do not provide anything for the transfer of shares and the Regulations contained in Table "F" in Schedule I to the Companies Act, 2013, are also expressly excluded, the transfer of shares will be governed by the general law relating to the transfer of movable property.

Further, as of now, in most of the listed companies, the shares are also transferable through Electronic mode i.e. through Depository Participants in dematerialized form instead of physical transfers. However, there are restrictions with respect to transferability of shares of a Private Limited Company which are dealt in chapter 2.

(vi) Common Seal

Upon incorporation, a company becomes a legal entity with perpetual succession and a common seal. Since the company has no physical existence, it must act through its agents and all contracts entered into by its agents must be under the seal of the company. The Common Seal acts as the official signature of a company. The name of the company must be engraved on its common seal.

However, a person duly authorized to execute documents pursuant to a power of attorney granted in his favour under the common seal of the company may execute such documents and it is not necessary for the common seal to be affixed to such documents.

The person, authorized to use the seal, should ensure that it is kept under his personal custody and is used very carefully because any deed, instrument or a document to which seal is improperly or fraudulently affixed will involve the company in legal action and litigation.

(VII) Capacity to sue or be sued

A company is a body corporate, can sue and be sued in its own name. To sue means to institute legal proceedings against (a person) or to bring a suit in a court of law. All legal proceedings against the company are to be instituted in its name. Similarly, the company may bring an action against anyone in its own name.

A company's right to sue arises when some loss is caused to the company, i.e. to the property or the personality of the company. Hence, the company is entitled to sue for damages in libel or slander as the case may be [**Floating Services Ltd. v. MV San Fransceco Dipaloo** (2004) 52 SCL 762 (Guj)]

Where video cassettes were prepared by the workmen of a company showing, their struggle against the company's management, it was held to be not actionable unless shown that the contents of the cassette would be defamatory. The court did not restrain the exhibition of the cassette. [**TVS Employees Federation v. TVS and Sons Ltd., (1996) 87 Com Cases 37**]

(viii) Contractual Rights

A company, being a legal entity different from its members, can enter into contracts for the conduct of the business in its own name. A shareholder cannot enforce a contract made by his company; he is neither a party to the contract nor be entitled to the benefit derived from of it, as a company is not a trustee for its shareholders.

Likewise, a shareholder cannot be sued on contracts made by his company. The distinction between a company and its members is not confined to the rules of privity but permeates the whole law of contract. Thus, if a director fails to disclose a breach of his duties towards his company, and in consequence, a shareholder is induced to enter into a contract with the director on behalf of the company which he would not have entered into had there been disclosure, the shareholder cannot rescind the contract.

(ix) Limitation of Action

A company cannot go beyond the power stated in its Memorandum of Association. The Memorandum of Association of the company regulates the powers and fixes the objects of the company and provides the edifice upon which the entire structure of the company rests

In order to enable it to carry out its actions without such restrictions and limitations in most cases, sufficient powers are granted in the Memorandum of Association. But once the powers

have been laid down, it cannot go beyond such powers unless the Memorandum of Association, itself altered prior to doing so.

(x) Separate Management

As already noted, the members may derive profits without being burdened with the management of the company. They do not have effective and intimate control over its working and they elect their representatives as Directors on the Board of Directors of the company to conduct corporate functions through managerial personnel employed by them.

In other words, the company is administered and managed by its managerial personnel.

(xi) Voluntary Association for Profit

A company is a voluntary association for profit. It is formed for the accomplishment of some stated goals and whatsoever profit is gained is divided among its shareholders or saved for the future expansion of the company. Only a Section 8 company can be formed with no profit motive.

(xii) Termination of Existence

A company, being an artificial juridical person, does not die a natural death. It is created by law, carries on its affairs according to law throughout its life and ultimately is effaced by law. Generally, the existence of a company is terminated by means of winding up. However, to avoid winding up, sometimes companies adopt strategies like reorganization, reconstruction, and amalgamation.