
PART-II

**Corporate Organisation,
Finance and Trade**

CHAPTER 7

FORMATION OF A COMPANY

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- specify the important stages in the formation of a company;
- describe the steps involved in each stage of company formation;
- specify the documents to be submitted to the registrar of companies; and
- state the need of certificate of incorporation and certificate to commence business.

Avtar, a brilliant automobile engineer, has recently developed a new carburettor in his factory which he is running as a sole proprietor. The new carburettor can cut down petrol consumption of a car engine by 40 percent. He is now thinking of producing it on a large scale for which he requires a large amount of money. He is to evaluate different forms of organisations for doing the business of manufacturing and marketing his carburettor. He decides against converting his sole proprietorship to partnership as the requirement of funds for the project is large and the product being new, there is a lot of risk involved. He is advised to form a company. He wants to know about the formalities required for the formation of a company.

7.1 INTRODUCTION

Modern day business requires large amount of money. Also, due to increasing competition and fast changing technological environment, the element of risk is increasing. As a result, the company form of organisation is being preferred by more and more business firms, particularly for setting up medium and large sized organisations.

The steps which are required from the time a business idea originates to the time, a company is legally ready to commence business are referred to as stages in the formation of a company. Those who are taking these steps and the associated risks are promoting a company and are called its promoters.

The present chapter describes in some details the stages in the formation of a company and also the steps required to be taken in each stage so that a fair idea about these aspects can be made.

7.2 FORMATION OF A COMPANY

As discussed in an earlier chapter on 'Forms of organisations', formation of

a company is a complex activity involving completion of a lot of legal formalities and procedures. To fully understand the process one can divide the formalities into four distinct stages, which are: (i) Promotion; (ii) Incorporation; (iii) Subscription of capital; and (iv) Commencement of business.

It may, however, be noted that these stages are appropriate from the point of view of formation of a public limited company. As far as the private limited companies are concerned only the first two stages mentioned above are appropriate. In other words, a private company can start its business immediately after obtaining the certificate of incorporation. As it is prohibited to raise funds from public, it does not need to issue a prospectus and complete the formality of minimum subscription. A public company, on the other hand, goes through the capital subscription stage and then receives the certificate of commencement. Thus, it has to undergo all the four stages.

In the next section, we shall discuss these four stages in the formation of a company in some detail.

7.2.1 Promotion of a Company

Promotion is the first stage in the formation of a company. It involves conceiving a business opportunity and taking an initiative to form a company so that practical shape can be given to exploiting the available business opportunity. Thus, it begins with somebody having discovered a potential business opportunity. Any person or a group of persons or even a company may have discovered an opportunity. If such a person or a group of persons or a company proceeds to form a company, then, they are said to be the promoters of the company.

There is no statutory definition of a promoter. A promoter is said to be the one who undertakes to form a company with reference to a given project and to set it going and who takes the necessary steps to accomplish that purpose. Thus, apart from conceiving a business opportunity the promoters analyse its prospects and bring together the men, materials, machinery, managerial abilities and financial resources and set the organisation going.

After thoroughly examining the feasibility of the idea, the promoters assemble resources, prepare necessary documents, give a name and perform various other activities to get a company registered and obtain the necessary certificate enabling the company to commence business. Thus, the promoters perform various functions to bring a company into existence.

Functions of a Promoter

The important functions of promoters may be listed as below:

(i) Identification of business opportunity: The first and foremost activity of a promoter is to identify a business opportunity. The opportunity may be in respect of producing a new product or service or making some product available through a different channel or any other opportunity having an investment potential. Such opportunity is then analysed to see its technical and economic feasibility.

(ii) Feasibility studies: It may not be feasible or profitable to convert all identified business opportunities into real projects. The promoters, therefore, undertake detailed feasibility studies to investigate all aspects of the business they intend to start. Depending upon the nature of the project, the following feasibility studies may be undertaken, with the help of the specialists like engineers, chartered accountants etc., to examine whether the perceived business opportunity can be profitably exploited.

(a) Technical feasibility: Sometimes an idea may be good but technically not possible to execute. It may be so because the required raw material or technology is not easily available. For example, in our earlier story suppose Avtar needs a particular metal to produce the carburettor. If that metal is not produced in the country and because of poor political relations, it can not be imported from the

country which produces it, the project would be technically unfeasible until arrangements are made to make the metal available from alternative sources.

- (b) Financial feasibility:** Every business activity requires funds. The promoters have to estimate the fund requirements for the identified business opportunity. If the required outlay for the project is so large that it cannot easily be arranged within the available means, the project has to be given up. For example, one may think that developing townships is very lucrative. It may turn out that the required funds are in several crores of rupees, which cannot be arranged by floating a company by the promoters. The idea may be abandoned because of the lack of financial feasibility of the project.
- (c) Economic feasibility:** Sometimes it so happens that a project is technically viable and financially

feasible but the chance of it being profitable is very little. In such cases as well, the idea may have to be abandoned. Promoters usually take the help of experts to conduct these studies. It may be noted that these experts do not become promoters just because they are assisting the promoters in these studies.

Only when these investigations throw up positive results, the promoters may decide to actually launch a company.

(iii) Name approval: Having decided to launch a company, the promoters have to select a name for it and submit, an application to the registrar of companies of the state in which the registered office of the company is to be situated, for its approval. The proposed name may be approved if it is not considered undesirable. It may happen that another company exists with the same name or a very similar name or the preferred name is misleading, say, to suggest that the

Name Clause

A name is considered undesirable in the following cases:

- (a) If it is identical with or too closely resembles the name of an existing company
- (b) If it is misleading. It is so considered if the name suggests that the company is in a particular business or it is an association of a particular type when it is not true
- (c) If it is violative of the provisions of 'The Emblem and Names (Prevention of Improper Use) Act 1950, as given in the schedule to this Act. This schedule specifies, inter alia, the name, emblem or official seal of the UNO and its bodies like WHO, UNESCO etc. Government of India, State Governments, President of India or Governor of any State, the Indian National Flag. The Act also prohibits use of any name which may suggest patronage of Government of India, or any state government or any local authority

company is in a particular business when it is not true. In such cases the proposed name is not accepted but some alternate name may be approved. Therefore, three names, in order of their priority are given in the application to the Registrar of Companies. (Performa Application for availability of names (Form 1A) is given at the end of the chapter.)

(iv) Fixing up Signatories to the Memorandum of Association:

Promoters have to decide about the members who will be signing the Memorandum of Association of the proposed company. Usually the people signing memorandum are also the first Directors of the Company. Their written consent to act as Directors and to take up the qualification shares in the company is necessary.

(v) Appointment of professionals:

Certain professionals such as mercantile bankers, auditors etc., are appointed by the promoters to assist them in the preparation of necessary documents which are required to be with the Registrar of Companies. The names and addresses of shareholders and the number of shares allotted to each is submitted to the Registrar in a statement called return of allotment.

(vi) Preparation of necessary documents:

The promoter takes up steps to prepare certain legal documents, which have to be submitted under the law, to the Registrar of the Companies for getting the company registered. These documents are Memorandum of Association, Articles of Association and Consent of Directors.

Documents Required to be Submitted

A. Memorandum of Association:

Memorandum of Association is the most important document as it defines the objectives of the company. No company can legally undertake activities that are not contained in its Memorandum of Association. The Memorandum of Association contains different clauses, which are given as follows:

(i) The name clause: This clause contains the name of the company with which the company will be known, which has already been approved by the Registrar of Companies.

(ii) Registered office clause: This clause contains the name of the state, in which the registered office of the company is proposed to be situated. The exact address of the registered office is not required at this stage but the same must be notified to the Registrar within thirty days of the incorporation of the company.

(iii) Objects clause: This is probably the most important clause of the memorandum. It defines the purpose for which the company is formed. A company is not legally entitled to undertake an activity, which is beyond the objects stated in this clause. The object clause is divided into two sub-clauses, which are:

- **The main objects:** The main objects for which the company is formed are listed in this sub-clause. It must be observed that an act which is either essential or incidental

for the attainment of the main objects of the company is deemed to be valid, although it may not have been stated explicitly in the sub-clause.

- **Other objects:** Objects not included in the main objects could be stated in this sub-clause. However, if a company wishes to undertake a business included in this sub-clause, it has to either pass a special resolution or pass an ordinary resolution and get central government's approval for the same.

(iv) Liability clause: This clause limits the liability of the members to the amount unpaid on the shares owned by them.

For example, if a shareholder has purchased 1000 shares of Rs. 10 each and has already paid Rs. 6 per share, his/her liability is limited to Rs. 4 per share. Thus, even in the worst case, he/she may be called upon to pay Rs. 4, 000 only.

(v) Capital clause: This clause specifies the maximum capital which the company will be authorised to raise through the issue of shares. The authorised share capital of the proposed company along with its division into the number of shares having a fixed face value is specified in this clause. For example, the authorised share capital of the company may be Rs. 25 with divided

into 2.5 lakh shares of Rs. 10 each. The said company cannot issue share capital in excess of the amount mentioned in this clause.

(vi) Association clause: In this clause, the signatories to the Memorandum of Association state their intention to be associated with the company and also give their consent to purchase qualification shares.

The Memorandum of Association must be signed by at least seven persons in case of a public company and by two persons in case of a private company.

A copy of a Memorandum of Association is given at the end of the chapter.

B. Articles of Association: Articles of Association are the rules regarding internal management of a company. These rules are subsidiary to the Memorandum of Association and hence, should not contradict or exceed anything stated in the Memorandum of Association. A public limited company may adopt Table A which is a model set of articles given in the Companies Act. Table A is a document containing rules and regulations for the internal management of a company. If a company adopts Table A, there is no need to prepare separate Articles of Association. For companies not

Association Clause

The association clause reads as under:

"We, the several persons whose names and addresses are subscribed, are desirous of being formed into a company in pursuance of this Memorandum of Association, and we respectively agree to take the number of shares in the capital of the company set opposite our respective names."

adopting Table A, a copy of the Articles of Association, stamped and duly signed by signatories to the Memorandum of Association is required for registration.

C. Consent of Proposed Directors:

Apart from the Memorandum and Articles of Association, a written consent of each person named as a director is required confirming that they agree to act in that capacity and undertake to buy and pay for qualification shares, as mentioned in the Articles of Association.

D. Agreement: The agreement, if any, which the company proposes to enter with any individual for appointment as its Managing Director or a whole time Director or Manager is another document which is required to be submitted to the Registrar for getting the company registered under the Act.

E. Statutory Declaration: A declaration stating that all the legal requirements pertaining to registration have been complied with is to be submitted to the Registrar with the above mentioned documents for getting the company registered under the law. This statement can be signed by an advocate of High Court or Supreme Court or by a Chartered Accountant in full time practice or by a person named in the articles as a director

or manager or secretary of the company. Performa of statutory declaration given.

F. Payment of fee: Along with the above-mentioned documents, necessary fees has to be paid for the registration of the company. The amount of such fees shall depend on the authorised share capital of the company.

Position of Promoters

Promoters undertake various activities to get a company registered and get it to the position of commencement of business. But they are neither the agents nor the trustees of the company. They can't be the agents as the company is yet to be incorporated. Therefore, they are personally liable for all the contracts which are entered by them, for the company before its incorporation, in case the same are not ratified by the company later on. Also promoters are not the trustees of the company.

Promoters of a company enjoy a fiduciary position with the company, which they must not misuse. They can make a profit only if it is disclosed but must not make any secret profits. In the event of a non-disclosure, the company can rescind the contract and recover the purchase price paid to the promoters. It can also claim damages

Qualification Shares

To ensure that the directors have some stake in the proposed company, the Articles usually have a provision requiring them to buy a certain number of shares. They have to pay for these shares before the company obtains Certificate of Commencement of Business. These are called Qualification Shares.

Performa for Statutory Declaration**“FORM NO.1”****The Companies Act. 1956**

Declaration of Compliance with requirements of the Companies Act, 1956
on Application for Registration of a Company.

PURSUANT TO SECTION 33 (2)

NAME OF THE COMPANY : M/S.

PRESENTED BY : SUSHIL KR.

CHARTERED ACCOUNTANT.

I,(NAME OF CA).....Partner of... (NAME OF CA FIRM & ITS ADDRESS)....
do solemnly and sincerely declare that I am a Chartered Accountant in whole
time practice in India, who is engaged in the formation of the company
“M/s.————— PRIVATE LIMITED”.

And that all the requirements of the Companies Act, 1956 and the rules
thereunder in respect of matters precedent to the registration of the said
company and incidental thereto have been complied with and I make this
solemn declaration conscientiously believing the same to be true.

PLACE : NEW DELHI

(NAME OF CA)

DATED :

CHARTERED ACCOUNTANTS

for the loss suffered due to the
non-disclosure of material information.

Promoters are not legally entitled to
claim the expenses incurred in the
promotion of the company. However,
the company may choose to reimburse
them for the pre-incorporation
expenses. The company may also
remunerate the promoters for their
efforts by paying a lump sum amount

or a commission on the purchase price
of property purchased through them
or on the shares sold. The company
may also allot them shares or
debentures or give them an option to
purchase the securities at a future date.

7.2.2 Incorporation

After completing the aforesaid
formalities, promoters make an

application for the incorporation of the company. The application is to be filed with the Registrar of Companies of the state within which they plan to establish the registered office of the company. The application for registration must be accompanied with certain documents about which we have already discussed in the previous sections. These may be briefly mentioned again:

1. The Memorandum of Association duly stamped, signed and witnessed. In case of a public company, at least seven members must sign it. For a private

statement in lieu of the prospectus is submitted, instead of Articles of Association.

3. Written consent of the proposed directors to act as directors and an undertaking to purchase qualification shares.
4. The agreement, if any, with the proposed Managing Director, Manager or whole-time director.
5. A copy of the Registrar's letter approving the name of the company.
6. A statutory declaration affirming that all legal requirements for registration have been complied

Preliminary Contracts

During the promotion of the company, promoters enter into certain contracts with third parties on behalf of the company. These are called preliminary contracts or pre-incorporation contracts. These are not legally binding on the company. A company after coming into existence may, if it so chooses, decide to enter into fresh contracts with the same terms and conditions to honour the contracts made by the promoters. Note that it cannot ratify a preliminary contract. A company thus cannot be forced to honour a preliminary contract. Promoters, however, remain personally liable to third parties for these contracts.

company however the signatures of two members are sufficient. The signatories must also give information about their address, occupation and the number of shares subscribed by them.

2. The Articles of Association duly stamped and witnessed as in case of the Memorandum. However, as stated earlier, a public company may adopt Table A, which is a model set of Articles, given in the Companies Act. In that case a

with. This must be signed by an advocate of a High court or Supreme Court or a signatory to the Memorandum of Association or a Chartered Accountant or Company Secretary in whole time practice in India.

7. A notice about the exact address of the registered office may also be submitted along with these documents. However, if the same is not submitted at the time of incorporation, it can be submitted

within 30 days of the receipt of the certificate of incorporation.

8. Documentary evidence of payment of registration fees.

The Registrar upon submission of the application along with the required documents has to be satisfied that the documents are in order and that all the statutory requirements regarding the registration have been complied with. However, it is not his duty to carry out a thorough investigation about the authenticity of the facts mentioned in the documents.

When the Registrar is satisfied, about the completion of formalities

for registration, a Certificate of Incorporation is issued to the company, which signify the birth of the company. The certificate of incorporation may therefore be called the birth certificate of the company.

With effect from November 1, 2000, the Registrar of Companies allots a CIN (Corporate Identity Number) to the Company.

Effect of the Certificate of Incorporation

A company is legally born on the date printed on the Certificate of

SPECIMEN OF

CERTIFICATE OF INCORPORATION

I hereby certify that (name of the company) is this day incorporated under the Companies Act 1956, and that the Company is limited.

Given under my hand at Delhi, this seventh day of November, two thousand and five.

Fees: Deed Stamp

Rs.

Stamp Duty on Capital

Rs.

SEAL

Sd/-

Registrar of Companies
Delhi

Corporate Identity Number
of Company : 1352 of 2005

Incorporation. It becomes a legal entity with perpetual succession on such date. It becomes entitled to enter into valid contracts. The Certificate of Incorporation is a conclusive evidence of the regularity of the incorporation of a company. Imagine, what would happen to an unsuspecting party with which the company enters into a contract, if it is later found that the incorporation of the company was improper and hence invalid. Therefore, the legal situation is that once a Certificate of Incorporation has been issued, the company has become a legal business entity irrespective of any flaw in its registration. The Certificate of Incorporation is thus conclusive evidence of the legal existence of the company. Some interesting examples showing the impact of the conclusiveness of the Certificate of Incorporation are as under:

- (a) Documents for registration were filed on 6th January. Certificate of Incorporation was issued on 8th January. But the date mentioned on the Certificate was 6th January. It was decided that the company was in existence and the contracts signed on 6th January were considered valid.
- (b) A person forged the signatures of others on the Memorandum. The Incorporation was still considered valid.

Thus, whatever be the deficiency in the formalities, the Certificate of Incorporation once issued, is a conclusive evidence of the existence of the company. Even when a company

gets registered with illegal objects, the birth of the company cannot be questioned. The only remedy available is to wind it up. Because the Certificate of Incorporation is so crucial, the Registrar has to go very carefully before issuing it.

On the issue of Certificate of Incorporation, a private company can immediately commence its business. It can raise necessary funds from friends, relatives or through private arrangement and proceed to start business. A public company, however, has to undergo two more stages in its formation.

7.2.3 Capital Subscription

A public company can raise the required funds from the public by means of issue of shares and debentures. For doing the same, it has to issue a prospectus which is an invitation to the public to subscribe to the capital of the company and undergo various other formalities. The following steps are required for raising funds from the public:

(i) SEBI Approval: SEBI (Securities and Exchange Board of India) which is the regulatory authority in our country has issued guidelines for the disclosure of information and investor protection. A company inviting funds from the general public must make adequate disclosure of all relevant information and must not conceal any material information from the potential investors. This is necessary for protecting the interest of the investors.

Difference between Memorandum of Association and Articles of Association

| Basis of Difference | Memorandum of Association | Articles of Association |
|----------------------------|--|--|
| Objectives | Memorandum of Association defines the objects for which the company is formed. | Articles of Association are rules of internal management of the company. They indicate how the objectives of the company are to be achieved. |
| Position | This is the main document of the company and is subordinate to the Companies Act. | This is a subsidiary document and is subordinate to both the Memorandum of Association and the Companies Act. |
| Relationship | Memorandum of Association defines the relationship of the company with outsiders. | Articles define the relationship of the members and the company. |
| Validity | Acts beyond the Memorandum of Association are invalid and cannot be ratified even by a unanimous vote of the members. | Acts which are beyond Articles can be ratified by the members, provided they do not violate the Memorandum. |
| Necessity | Every company has to file a Memorandum of Association. | It is not compulsory for a public ltd. company to file Articles of Association. It may adopt Table A of the Companies Act. |
| Alteration | Alteration of Memorandum of Association is quite difficult and in many cases, approval of certain statutory authority is required. | Articles can be altered by passing a special resolution by the members. |

Prior approval from SEBI is, therefore, required before going ahead with raising funds from public.

(ii) Filing of Prospectus: A copy of the prospectus or statement in lieu of prospectus is filed with the Registrar of Companies. A prospectus is 'any document described or issued as a prospectus including any notice,

circular, advertisement or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of any shares or debentures of, a body corporate'. In other words, it is an invitation to the public to apply for shares or debentures of the company or to make deposits in the company.

Provisional Contract

These are contracts which are signed after incorporation but before the commencement of business. These become enforceable only after the company gets the Certificate of Commencement of Business.

Investors make up their minds about investment in a company primarily on the basis of the information contained in this document. Therefore, there must not be a mis-statement in the prospectus and all significant information must be fully disclosed.

(iii) Appointment of Bankers, Brokers, Underwriters: Raising funds from the public is a stupendous task. The application money is to be received by the bankers of the company. The brokers try to sell the shares by distributing the forms and encouraging the public to apply for the shares. If the company is not reasonably assured of a good public response to the issue, it may appoint underwriters to the issue. Underwriters undertake to buy the shares if these are not subscribed by the public. They receive a commission for underwriting the issue. Appointment of underwriters is not necessary.

(iv) Minimum Subscription: In order to prevent companies from commencing business with inadequate resources, it has been provided that the company must receive applications for a certain minimum number of shares before going ahead with the allotment of shares. According to the Companies Act, this is called the 'minimum subscription'. The limit of minimum subscription is 90 per cent of the size

of the issue. Thus, if applications received for the shares are for an amount less than 90 per cent of the issue size, the allotment cannot be made and the application money received must be returned to the applicants.

(v) Application to Stock Exchange: An application is made to at least one stock exchange for permission to deal in its shares or debentures. If such permission is not granted before the expiry of ten weeks from the date of closure of subscription list, the allotment shall become void and all money received from the applicants will have to be returned to them within eight days.

(vi) Allotment of Shares: In case the number of shares allotted is less than the number applied for, or where no shares are allotted to the applicant, the excess application money, if any, is to be returned to applicants or adjusted towards allotment money due from them. Allotment letters are issued to the successful allottees. Return of allotment, signed by a director or secretary is filed with the Registrar of Companies within 30 days of allotment.

A public company may not invite public to subscribe to its shares or debentures. Instead, it can raise the funds through friends, relatives or some private arrangements as done by

a private company. In such cases, there is no need to issue a prospectus. A 'Statement in Lieu of Prospectus' is filed with the Registrar at least three days before making the allotment.

7.2.4 Commencement of Business

If the amount of minimum subscription is raised through new issue of shares, a public company applies to the Registrar of Companies for the issue of Certificate of Commencement of Business. The following documents are required:

1. A declaration that shares payable in cash have been subscribed for and allotted up to the minimum subscription mentioned in the prospectus;
2. A declaration that every director has paid in cash, the application and allotment money on his shares in the same proportion as others;
3. A declaration that no money is payable or liable to become

payable to the applicants because of the failure of the company to either apply for or obtain permission to deal in its securities on a stock exchange; and

4. A statutory declaration that the above requirements have been complied with. This declaration can be signed by a director or secretary of the company.

A public company raising funds privately, which has earlier filed a Statement in lieu of prospectus, has to submit only documents 2 and 4 listed above.

The Registrar shall examine these documents. If these are found satisfactory, a 'Certificate of Commencement of Business' will be issued. This certificate is conclusive evidence that the company is entitled to do business. With the grant of this certificate the formation of a public company is complete and the company can legally start doing business.

| | |
|--|---------------------------------------|
| Certificate of commencement of Business | |
| (Specimen) | |
| I hereby certify that ltd. of which was incorporated under The Companies Act, 1956, on the day of 200..... and which has this day filed a statutory declaration in the prescribed form that the conditions of section 149 have been complied with, is entitled to commence business. | |
| Given under my hand at this day of two thousand | |
| <div style="border: 1px solid black; padding: 5px; display: inline-block;">SEAL</div> | Registrar |
| | Joint Stock Companies(State) |

**Memorandum of Association
(Specimen)**

1. Name: The name of the company is Excellent Educational Services Limited. It is hereinafter referred to as EES Ltd.
2. Registered Office: The Registered office of the company shall be situated in the NCT of Delhi and at present it is at: Sri Aurobindo Marg, New Delhi-16.
3. **(A) Main Objectives:**
 - (a) To engage in the design, development and delivery of world class service products in the sphere of education for domestic as well as global markets.
 - (b) To establish and strengthen presence/market share in the various segments representing various stages in the education/re-education process in the life-long learning context, viz., identification of prospects, curriculum-design, pedagogy, examination and evaluation, anticipating societal/market needs, content-delivery, placement services and human resource development and renewal.
 - (c) To develop, publish/produce teaching, training and study materials, journals, periodicals, reports, books, monographs and other multilingual literature/multimedia products for promoting the objectives of the company.
 - (d) To organise programmes, conferences, lectures, seminars, symposia and workshops on issues impacting education, industry, business and society.
- (B) Ancillary Objectives:**
 - (a) To develop special competencies and capabilities for designing, developing and delivering service products for persons with physical and mental disabilities;
 - (b) To liaison and network with various individuals and institutions in government and non-government sectors and fostering mutually beneficial relationship in the field of education;
 - (c) To host a website for virtual learning;
 - (d) To build up a research and reference library and to undertake documentation services;
 - (e) To own, purchase, lease, movable and immovable property in furtherance of the aims and objectives of the company;
 - (f) To offer prizes, grants, stipends and scholarships in furtherance of the objectives of company;
 - (g) To provide a forum for raising, discussing and resolving of issues, problems and challenges in the field of education; and
 - (h) To do generally all such other lawful things as are conducive or incidental to the attainment of the above objectives.
4. Liability Clause: Liability of the members would be limited to the amount of unpaid value of the share.
5. Capital Subscription Clause: The company shall be registered with a capital of Rs. 2.5 crore divided into Rs. 25 lakh shares of Rs.10 each.

| | |
|---|-------------|
| We the following persons voluntarily agreed to be the signatories to the Memorandum of Association: | |
| Sunita | Vinita |
| Anil Kumar | Sunil Kumar |
| Avtar Singh | Renu |
| Anita | Usha |
| The name and address of the company signatures to Memorandum have been modified. | |

| | |
|---|----------------------------|
| <p>FORM NO. 1-A The Companies Act. 1961 (Application Form for Availability of Names*)</p> | |
| The Registrar of Companies, | |
| _____ | |
| _____ | |
| Sir, | |
| Subject: Availability of Names-information Furnishing of: | |
| We, the following applicants are desirous of forming a company to be registered under the Companies Act, 1956, in the State Union Territory of _____ | |
| <ol style="list-style-type: none"> 1. Name and full address of the person(s) applying for availability, of the name (IN BLOCK LETTERS). 2. Proposed name of the Company. 3. State whether Public or Private. 4. In case the proposed name mentioned in item 2 is not available, 3 names to be considered, in the order of preference. 5. Main objectives of the proposed Company. 6. Name and address of the prospective Directors of Promoters, etc. 7. Particulars of the names and situation of registered office of other companies in the same group or under the same management. 8. Proposed authorised capital. 9. Please furnish particulars and results of any application moved to this or any other Registrar previously for availability of name. 10. Particulars of remittance of fee | |
| Situation _____ | _____ |
| Dated _____ | Signature of the applicant |
| * Refer Rule 4 A of the Companies/Central Government's/General Rules and Forms, 1956 | |

Key Terms

| | | |
|-----------------------|-------------------------|-----------------------------|
| Promotion | Articles of Association | Prospectus |
| Incorporation | Capital subscription | Memorandum of Association |
| Preliminary contracts | Statutory declaration | Certificate of Commencement |

SUMMARY

There are two stages in the formation of a private company, promotion and incorporation. A public company has to undergo capital subscription stage and then get certificate of commencement of business, to begin operations.

1. **Promotion:** It begins with a potential business idea. Certain feasibility studies e.g. technical, financial and economic, are conducted to determine whether the idea can be profitably exploited. In case, the investigations yield favourable results, promoters may decide to form the company. Persons who conceive the business idea, decide to form a company, take necessary steps for the same, and assume associated risks, are called promoters.

Steps in Promotion

- i. Approval of company's name is taken from the Registrar of Companies
- ii. Signatories to the Memorandum of Association are fixed
- iii. Certain professionals are appropriated to assist the promoters
- iv. Documents necessary for registration are prepared

Necessary Documents

- a. Memorandum of Association
 - b. Articles of Association
 - c. Consent of proposed directors
 - d. Agreement, if any, with proposed managing or whole time director
 - e. Statutory declaration
2. **Incorporation:** An application is made by promoters to the Registrar of Companies alongwith necessary documents and registration fees. The Registrar, after due scrutiny, issues certificate of incorporation. The registration may be refused only in case of a major defect in the documents. The certificate of incorporation is a conclusive evidence of the legal existence of the company. Even if there has been a major

defect in the incorporation, legal existence of the company can not be rejected.

3. **Capital Subscription:** A public company raising funds from the public needs to take following steps for fund raising:
 - (i) SEBI approval;
 - (ii) File a copy of prospectus with the Registrar of Companies;
 - (iii) Appointment of brokers, bankers and underwriters etc.;
 - (iv) Ensure that minimum subscription is received;
 - (v) Application for listing of company's securities;
 - (vi) Refund/adjust excess application money received;
 - (vii) Issue allotment letters to successful applicants; and
 - (viii) File return of allotment with the Registrar of Companies (ROC).

A public company, raising funds, raising funds from friends/relatives (not public) has to file a statement in lieu of prospectus with the ROC at least three days before allotment of shares and returns of allotment after completing the allotment.

4. **Commencement of Business:** A public company raising funds from public has to apply to the Registrar of Companies for the certificate of commencement of business alongwith the following documents.
 - (i) A declaration about meeting minimum subscription requirement;
 - (ii) A declaration about details in respect of allotment to directors;
 - (iii) A declaration about no money being payable to applicants; and
 - (iv) A statutory declaration.

A public company raising funds privately has to submit only documents (ii) and (iv) listed above.

The Registrar, upon satisfaction, issues Certificate of Commencement of Business. This certificate is also a conclusive evidence of completion of formation requirements.

Preliminary Contracts: Contracts signed by promoters with third parties before the incorporation of company.

Provisional Contracts: Contracts signed after incorporation but before commencement of business.

EXERCISES**Multiple Choice Questions**

1. Minimum number of members to form a private company is
 - (a) 2
 - (b) 3
 - (c) 5
 - (d) 7
2. Minimum number of members to form a public company is
 - (a) 5
 - (b) 7
 - (c) 12
 - (d) 21
3. Application for approval of name of a company is to be made to
 - (a) SEBI
 - (b) Registrar of Companies
 - (c) Government of India
 - (d) Government of the State in which Company is to be registered
4. A proposed name of Company is considered undesirable if
 - (a) It is identical with the name of an existing company
 - (b) It resembles closely with the name of an existing company
 - (c) It is an emblem of Government of India, United Nations etc.
 - (d) In case of any of the above
5. A prospectus is issued by
 - (a) A private company
 - (b) A public company seeking investment from public
 - (c) A public enterprise
 - (d) A public company
6. Stages in the formation of a public company are in the following order
 - (a) Promotion, Commencement of Business, Incorporation, Capital Subscription
 - (b) Incorporation, Capital Subscription, Commencement of Business, Promotion
 - (c) Promotion, Incorporation, Capital Subscription, Commencement of Business
 - (d) Capital Subscription, Promotion, Incorporation, Commencement of Business
7. Preliminary Contracts are signed
 - (a) Before the incorporation
 - (b) After incorporation but before capital subscription
 - (c) After incorporation but before commencement of business
 - (d) After commencement of business

8. Preliminary Contracts are

- | | |
|---|---|
| (a) binding on the Company | (b) binding on the Company, if ratified after incorporation |
| (c) binding on the Company, after incorporation | (d) not binding on the Company |

True/False Answer Questions

1. It is necessary to get every company incorporated, whether private or public.
2. Statement in lieu of prospectus can be filed by a public company going for a public issue.
3. A private company can commence business after incorporation.
4. Experts who help promoters in the promotion of a company are also called promoters.
5. A company can ratify preliminary contracts after incorporation.
6. If a company is registered on the basis of fictitious names, its incorporation is invalid.
7. 'Articles of Association' is the main document of a company.
8. Every company must file Articles of Association.
9. A provisional contract is signed by promoters before the incorporation of the company.
10. If a company suffers heavy issues and its assets are not enough to pay off its liabilities, the balance can be recovered from the private assets of its members.

Short Answer Questions

1. Name the stages in the formation of a company.
2. List the documents required for the incorporation of a company.
3. What is a prospectus? Is it necessary for every company to file a prospectus?
4. Explain the term, 'Minimum Subscription'.
5. Briefly explain the term 'Return of Allotment'.
6. At which stage in the formation of a company does it interact with SEBI.
7. Distinguish between 'preliminary contracts' and 'provisional contracts'.

Long Answer Questions

1. What is meant by the term 'Promotion'. Discuss the legal position of promoters with respect to a company promoted by them.
2. Explain the steps taken by promoters in the promotion of a company.
3. What is a 'Memorandum of Association'? Briefly explain its clauses.
4. Distinguish between 'Memorandum of Association' and 'Articles of Association.'
5. What is the effect of conclusiveness of the 'Certificates of Incorporation' and 'Commencement of Business'?
6. Is it necessary for a public company to get its share listed on a stock exchange? What happens if a public company going for a public issue fails to apply to a stock exchange for permission to deal in its securities or fails to get such permission?

Projects/Assignment

Find out from the office of the Registrar of Companies, the actual procedure for formation of companies. Does it match with what you have studied. What are the obstacles which companies face in getting themselves registered.