

5. ARTICLES OF ASSOCIATION & DOCTRINES

5.1. ARTICLES OF ASSOCIATION

ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER

Q NO.	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M-19 (O)	M-19 (N)	N-19 (O)	N-19 (N)	N-20 (O)	N-20 (N)
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ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER FOR PRACTICAL QUESTIONS

Q NO.	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M-19 (O)	M-19 (N)	N-19 (O)	N-19 (N)	N-20 (O)	N-20 (N)
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CHAPTER OVERVIEW

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SECTION 1: THEORY FOR CLASSROOM DISCUSSION

Q.No.1. What is the meaning and nature of Articles of Association? (C) (NEW & OLD SM)

- 1) **DEFINITION 2(5):** Articles means
 - a) “the Articles of Association of a comp any
 - b) as originally framed or as altered from time to time or
 - c) applied in pursuance of any previous company law or of this Act”.
- 2) **MEANING:** Articles are the regulations framed by the company for its own governance. It deals with the internal affairs of the company.

3) CONTENTS OF ARTICLES:

- a) AOA contains the byelaws or the rules and regulations of the company.
- b) It contains such matters as may be prescribed under the rules.
- c) A company may also include any additional matter in its articles which is considered necessary for the management of the company.

Note:

- a) **Forms of articles:** The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company¹.
- b) **Model articles:** A company may adopt all or any of the regulations contained in the model articles applicable to such company.
- c) **Applicability of Model Articles:** If the registered articles of a company do not exclude or modify the regulations contained in the model articles then regulations stated in model articles will apply to such company.

SIMILAR QUESTIONS:

1. Every company which is registered under the Companies Act, 2013, need not have their own articles. Comment?
 - A. Yes. A company may either frame its own articles or may adopt all or any of the regulations contained in Table F of Schedule I of Companies Act, 2013.
2. In order to borrow money from outsiders, beyond the prescribed limits, the BOD has to take approval from members by way of 'OR' in GM. Shareholders want to modify the requirement of OR as SR in AOA. Can shareholders do so?
 - A. Yes. A company may either frame its own articles or may adopt all or any of the regulations contained in Table F. Thus, members can modify the Articles.

Q.No.2. Explain the procedure for alteration of Articles of Association (A) (NEW SM, OLD SM)

ALTERATION TO AOA MAY BE REQUIRED IN THE FOLLOWING CASES:

- 1) Increase Authorised Share Capital in MOA.
- 2) Issues of shares,
- 3) Increase in borrowing limits of company.
- 4) Increase in the number of directors,
- 5) Conversion of a private company into a public company and a public company into a private company².

PROCEDURE FOR ALTERATION OF "AOA" [SEC 14]:

- 1) **Alteration by Special Resolution:** Special Resolution is required for every alteration of articles. Such alteration must comply with the Provisions of Companies act and powers of MOA.
- 2) **Filing of alteration with the ROC:** Copy of Special Resolution (MGT-14), copy of the altered AOA and copy of the NCLT order (*in case of conversion of public to private*) shall be filed with the ROC within 15 days, and the ROC shall register the same.

- 1) **FORMS OF ARTICLES:** The articles of a company shall be in respective forms specified in Tables, F, G, H, I and J in Schedule I as may be applicable to such company.

	TABLE	CONTAINS
AOA	F	Articles of association of a company limited by shares
	G	Articles of association of a company limited by guarantee and having a share capital
	H	Articles of association of a company limited by guarantee and not having share capital
	I	Articles of association of an unlimited company and having a share capital
	J	Articles of association of an unlimited company and not having share capital

- 2) A private company may get converted into a public company by removing the restrictions and limitations specified u/s 2(68) in AOA of private company. The conversion from private to public shall take effect from the date of alteration of AOA
The conversion of a public company into a private company shall not take effect except with the approval of the Tribunal. The NCLT may make such order as it may deem fit.

- 3) **Effect of alteration:** Every alteration of AOA which is registered by the ROC shall be valid as if it were originally contained in the articles.
- 4) **Alteration noted in Every Copy:**
- Every alteration made in articles of a company shall be noted in every copy of the articles, as the case maybe.
 - If a company makes any default in complying with the stated provisions, the company and every officer who is in default shall be liable to a penalty of one thousand rupees for every copy of the articles issued without such alteration. [Sec 15].

SIMILAR QUESTIONS:

- Mr. Vikas, Managing Director of M/s Alpha limited has borrowing power of Rs.50 Lakhs for the company. Company requires Rs.60 lakhs for the purpose of one project. Can a company borrow Rs.60 lakhs with the approval of MD? If not, explain the procedure to obtain the loan of Rs.60 Lakhs.
 - No. The Managing Director of the Company can't borrow more than 50 lakhs, as restricted by its AOA. Of course, Company can first alter its AOA to increase the limit of borrowing powers of Directors. Alternatively, the Company can borrow 60 lakhs after taking approval from its members.
- The AOA of a company can be altered by passing an 'OR' in the meeting of the Shareholders. Comment.
 - False. It can be altered only by 'SR' u/s 14 of the Companies Act, 2013.

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 4)

Q.No.3. What restrictions are applicable under the Companies Act, 2013 with respect to alteration of Articles of Association of a company? (A) (OLD PM)

Every company has right to alter its Articles by following a simple process laid down in section 14 of the Companies Act, 2013, subject to following restrictions:

- Alteration must be within the powers of MOA.
- It should not be inconsistent with the provisions of the companies act.
- It should not be against any court orders.
- It must not include any thing which is illegal or opposed to public policy or unlawful.
- It must not cause a breach of contract, or a fraud on minority shareholders.
- It must not increase the liability of the members which has been already defined in the MOA.

SIMILAR QUESTION:

- The gambling is forbidden by the law of the country. A company, by special resolution, altered its articles and added a clause authorizing the directors to allow gambling in the office building after working hours, and to earn commission thereon.
 - In this case, the alteration is invalid as it sanctions an act which is illegal.
- A was the holder of 500 shares of Rs 100 each of a public limited company. On these shares, A has already paid Rs 80 per share to the company. In this company, B was also the holder of 100 fully paid up shares. The company was in financial difficulties, and it need further funds. The company, by special resolution, altered its articles and added a clause providing that the holder of fully paid up shares would be liable to pay Rs 10 more on each share, and those holding shares on which Rs 80 and been paid would be liable to pay Rs 30 more on each share. The shareholders did not give their consent to this alteration.
 - In this case, alteration is invalid as it increases the liability of shareholders.
- A company does not have unlimited powers to alter its AOA. Comment.
 - The given statement is correct.

Every company has powers to alter its Articles by following a simple process laid down in Section 14 of the Companies Act, 2013, but subject to certain restrictions stated below.

- Now write down the restrictions stated above.

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Q.No.4. AOA may contain provisions for entrenchment. Briefly explain the provisions of entrenchment? (B)
(NEW SM, OLD PM)

ENTRENCHMENT³ [SECTION 5(3)]:

- a) **MEANING:** Usually an article of association may be altered by passing special resolution but entrenchment makes it more difficult to change it. So, entrenchment means making something more protective.
- b) The articles may contain provisions for entrenchment to the effect that specified provisions of the articles may be altered only if conditions or procedures as that are more restrictive than those applicable in the case of a special resolution, are met or complied with⁴.

***Example:** For removal of any of the Directors of the Company it is sufficient to pass a SR. But through entrenchment provisions, AOA may require consent from all the members rather than passing a SR.*

c) SUCH PROVISIONS SHALL BE MADE:

- i) At the time of formation of the company (*in case of new company*); or
- ii) By an amendment of articles (*in case of existing company*)
- With the consent of all the members, in case of a private company.
 - By passing a Special Resolution, in case of a Public company.

d) FILING NOTICE WITH ROC:

- i) If AOA contains the entrenchment provisions then the company shall file notice of such provisions with the ROC, in prescribed form and manner⁵.
- ii) Notice to the ROC shall be given irrespective of the fact as to whether the provisions for entrenchment were contained in the articles -
- At the time of formation of the company, or
 - Were included in the articles afterwards, by way of an amendment.

***NOTE:** Entrenchment provisions shall not apply to the articles of a company registered under any previous company law, unless amended under this Act.*

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 1, 2)

Q.No.5. Explain how Companies act over-rides the provisions and contents of MOA, AOA?
(B) (NEW SM, OLD PM)

ACT TO HAVE OVER-RIDING EFFECT (SECTION 6): The provisions of the Companies act, 2013 shall have, over-riding effect, notwithstanding anything to the contrary contained in -

- 1) Memorandum of a company; or
- 2) Articles of a company; or
- 3) Any agreement executed by a company; or
- 4) Any resolution passed by the company in the GM; or
- 5) Any resolution passed by the company in Board Meeting.

- 3) As per the oxford dictionary 'Entrenchment' means to apply additional legal safeguards, "to protect something"
- 4) Mr. Tarun promoted an education start up and got it registered as a private limited company. Initially he and his family are holding all shares in the company. In the article of association of company, It is written that Mr. Tarun will remain director of the company for lifetime. But he has a fear that tomorrow if 75% or more shares in the company are held by non-family members then by passing a special resolution article may be changed and he may be removed from the post of director. Therefore, it was also written in the article that he can be removed from the post of director only if 95% votes are cast in favour of the resolution. This is entrenchment.
- 5) Where articles contains provisions for entrenchment, either on formation or subsequently, the company shall give notice to the ROC of such provision in Form no: INC 2 or INC 7 with fee as provided in the companies rules 2014. It shall be filed within 30 days from the date of formation of the company.

INCONSISTENT PROVISIONS TO BE VOID: If a provision contained in

- 1) Memorandum of a company; or
- 2) Articles of a company; or
- 3) Any agreement executed by a company; or
- 4) Any resolution passed by the company in the GM; or
- 5) Any resolution passed by the company in Board Meeting.

is inconsistent with the provisions of the Act then such provisions shall be void to the extent of such inconsistency⁶.

Q.NO.6. Write about conversion of companies already registered?

(NEW SM)

CONVERSION OF COMPANY (SEC. 18): A company may convert itself in some other class of company by altering its memorandum and articles of association. Following is the law with respect to the conversion of the companies already registered.

- 1) **Alteration of Memorandum and Articles:** A company of any class registered under this Act may convert itself as a company of other class under this Act by alteration of memorandum and articles of the company in accordance with the provisions of this Chapter.
- 2) **File an application with ROC:** Wherever such conversion of companies is required to be done, the company shall file an application to the Registrar, who shall after satisfying himself that the provisions applicable for registration of companies have been complied with, close the former registration of the company.
- 3) **Issue Certificate of Incorporation:** After registering the required documents, issue a certificate of incorporation in the same manner as its first registration.
- 4) **No effect on the Debts, Liabilities etc. incurred before conversion:** The registration of a company under this section shall not affect any debts, liabilities, obligations or contracts incurred or entered into, by or on behalf of the company before conversion and such debts, liabilities, obligations and contracts may be enforced in the manner as if such registration had not been done.

Q.No.7. Explain the binding effects of Memorandum and Articles of a company.

(B) (NEW SM, OLD SM)

BINDING EFFECTS OF MOA AND AOA (Sec 10):

- 1) Upon registration, MOA and AOA shall bind the company and members as if they have been signed by the company and each member respectively.
- 2) All monies payable by any member to the company under MOA or AOA shall be a debt due from him to the company.
- 3) As a result, number of legal relationships are formed between different parties and the company which are described below:
 - a) **Members bound to the Company:**
 - i) Each member of the company is bound to comply with the provisions of the MOA & AOA.
 - ii) In case of non-compliance, the company may sue a member.

(Boreland Trustees vs. Steel Brothers & Co. Ltd.)

6) NOTE: In simple words, the provisions of this Act shall have overriding effect. But keep in mind that this section starts with "Save as otherwise" It means that if any other section of the Act says that article is superior then we will treat it accordingly.

E.g., Sec. 139(2) says Rotation of auditors is not applicable to private company. Suppose if AOA of the company voluntarily adopted rotation of auditors through its articles then AOA will be overriding Sec. 139(2) of companies act, 2013.

b) Company bound to its members:

- i) Just like members are bound to the company, similarly company is also bound to the members to observe and follow the articles.
- ii) Any member can bring an injunction when company is about to commit a breach of MOA & AOA. *(Wood vs. Odessa Water Works Co)*

c) Member bound to Member:

- i) Members of the company, among themselves, are also bound by the provisions of MOA and AOA.
- ii) However, a member can only sue the other member through the company and not in his own name. *(Ray filed vs. Hands and Others)*

d) Company and its members are not bound to outsiders:

- i) The term 'outsider' signifies a person who is not a member of the company. Even director or solicitor of the company is also an outsider if he is not a member.
- ii) The AOA do not constitute a contract between a company and outsiders.
- iii) Thus, an outsider cannot take advantage of any provision contained in these documents and bring an action upon the company.

SIMILAR QUESTIONS:

1. The 'articles of association' of a company contained a clause providing that the remuneration of the company's secretary would be Rs 1,250 per month. A accepted the post of company secretary on the basis of the terms contained in the articles. Subsequently, the company altered its articles and reduced the secretary's remuneration to Rs 1,000 per month. Is that alteration valid?
 - A. It was held that the alteration was valid and operative. In this case A's appointment as company secretary was not on the basis of a separate contract, but on the basis of company's articles.
2. In what respects does the MOA differ from the AOA? How far shall the provisions of these documents have a binding authority upon the contractual relations between different parties on registration of a company?
 - A. Refer above answer
3. On registration of MOA & AOA, what contractual relationship is established between different parties? Comment.
 - A. Refer above answer.

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 3)

Q.No.8. Copies of MOA and AOA are to be given to its members. Comment

(C) (NEW SM, OLD SM)

- 1) As per Sec 17, every company, when requested by its member, shall send copies of the following documents, within 7 days of the request and on the payment of fees-
 - a) MOA & AOA;
 - b) Every agreement and every resolution referred u/s 117 (Sec.117 states the Resolutions and agreements to be filed with the ROC)
- 2) **CONSEQUENCES OF DEFAULT:** In case of default, the company and every officer who is in default are liable to pay a penalty of Rs. 1,000 for each day during which such default continues or Rs.1 lakh, whichever is less.

Q.No.9. Who can authenticate Company documents, proceedings and contracts

(NEW SM)

As per section 21, a document or proceeding requiring authentication by a company or contracts made by or on behalf of a company may be signed by -

- 1) any key managerial personnel (KMP), or
- 2) an officer or employee of the company of the company duly authorised by the Board in this behalf. (In case of Specified IFSC Public and Private Company - An officer or any other person or employee authorized by the Board)

DEFINITION OF KMP [SEC. 2(51)]: In relation to a company, means—

- 1) The CEO or the MD or the manager.
- 2) The company secretary.
- 3) The whole-time director.
- 4) The CFO.
- 5) Such other officer, not more than one level below the directors who is in whole-time employment, designated as key managerial personnel by the Board and
- 6) Such other officer as may be prescribed.

Q.No.10. Write about authorisation of a person to act as attorney of the company to execute hundi, bills, promissory notes and other documents. (NEW SM)

Section 22 prescribes the law with respect to execution of the negotiable instruments and the deeds. It says that

- 1) A bill of exchange, hundi or promissory note shall be deemed to have been made, accepted, drawn or endorsed on behalf of a company if made, accepted, drawn, or endorsed in the name of, or on behalf of or on account of the company, by any person acting under its authority, express or implied.
- 2) **COMMON SEAL:** A company may, by writing under its common seal, if any, may authorise any person, either generally or in respect of any specified matters, as its attorney to execute other deeds on its behalf in any place either in or outside India.
- 3) **NO COMMON SEAL:** In case Company does not have a common seal, the authorisation shall be made by two directors or by a director and a Company Secretary, if company appointed Company Secretary.

A deed signed by such an attorney on behalf of the company and under his seal shall bind the company and have the effect as if it were made under its common seal.

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 12)

Q.No.11. Explain the procedure for conversion of a Public Company into a Private Company. (A) (OLD SM, OLD PM, M18 (O) - 4M)

PUBLIC COMPANY CAN BE CONVERTED INTO PRIVATE COMPANY BY TAKING FOLLOWING STEPS:

Section 14 (1) states that subject to the provisions of the Companies Act 2013 and the conditions contained in the Memorandum, a company may, by special resolution, alter its Articles including alterations which may have the effect of converting a public company into a private company (or vice versa).

Further any alteration which has the effect of converting a public company into a private company will not have any effect except with the approval of the Central Government which may pass such order as it deems fit.

Hence, the broad procedure for conversion of a public company into a private company would comprise of the following steps:

- 1) Check that the Memorandum of Association does not contain any restrictive clause. If yes, alteration of the Memorandum will be necessary through a special resolution;
- 2) Alteration of the Articles to incorporate the restrictions required u/s 2 (68) by a special resolution
- 3) Application to the Central Government for approval of the change
- 4) After the approval of the Central Government, every alteration of the articles and a copy of the order of the Tribunal approving the alteration shall be filed with the Registrar, within a period of fifteen days, who shall register the same.
- 5) Any alteration of the articles registered as above shall be valid as if it were originally in the articles.

NOTE: In case of Company having more than 200 members, the resolution to covert public company into private company is required to be passed through postal ballot.

5.2. DOCTRINES

Q.No.12. Explain the concept of doctrine of Ultra vires and state its implications

(A) (NEW SM, OLD SM, OLD PM)

OBJECTIVE THIS DOCTRINE: The objective of this doctrine is to protect the interest of the shareholders' and creditors.

MEANING OF DOCTRINE OF ULTRA VIRES:

- 1) The term 'Ultra' means "beyond" or "in excess of" and the term vires means "powers". Thus, the term Ultra vires means an act or transaction beyond the powers of the company.
- 2) An act or transaction shall be treated as ultravires if -
 - a) It is not permitted or authorised by the Companies Act, 2013;
 - b) It falls outside the object's clause of MOA of the Company.

EFFECTS OF ULTRA VIRES TRANSACTIONS:

1) Void ab initio:

- a) Ultravires acts are null and void. The company is not bound by these ultravires acts.
- b) The Company cannot sue or be sued upon ultravires acts.
- c) Even ratification of an ultravires act by the whole body of shareholders does not make an ultravires act valid or enforceable.

2) Injunction against the company: Where a company is about to undertake an ultravires act, any member can file a suit for injunction (stay order) against proposed activities which are ultravires the company.

3) Personal liability of directors to the company:

- a) If funds of the company are misapplied or wasted by entering into ultravires transactions, then the directors shall be personally liable to the company for ultravires act.
- b) It is the duty of directors to ensure that company's funds are used only for the legitimate objectives of the company.

4) Property acquired under ultravires transaction: If a company acquires some property under an ultravires transaction, then the company has the right to hold that property (since it represents company's money) and protect it against the damage by other parties.

ADVANTAGE: The main advantage of Doctrine of Ultra-Vires is that it provides protection to the members and creditors.

DISADVANTAGE:

- 1) It prevents the company from changing its activities in a direction which is agreed by all.
- 2) Since the object clause can be easily altered by passing a special resolution, the purpose of doctrine of ultravires has been defeated.

However, disadvantages of this doctrine outweigh its main advantage i.e. protection to the shareholders and creditors. **(Ashbury Railway Carriage and Iron Co. Ltd. v. Riche)**

SIMILAR QUESTIONS:

1. An ultra vires transaction will not affect the right to acquire the property of a company. Comment.
 - A. Refer point 4 under Effects of ultravires transactions.
2. The Doctrine of Ultra vires is the protection to shareholders and a pitfall (*danger*) to outsiders. Comment.
 - A. No, it provides protection to the members and creditors.
3. The Directors of a Company borrowed Rs 50,000/- from Mr. A on a transaction which is ultra vires the Company. Discuss the rights of Mr. A against the Company and its Directors.
 - A. A does not have any right against the company. Company is not responsible for ultravires acts even though such acts are beneficial to the company. (*However, if the company is having possession of money obtained under Ultravires act then it can be recovered*) Directors are personally responsible to the Outsiders. In case company incurs any loss due to such ultravires acts then Directors are held responsible to reimburse such loss also.

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 5, 6)

Q.No.13. Briefly explain the doctrine of “Constructive Notice and its exceptions under the Companies Act, 2013. (A) (OLD PM, MTP N16, N18 (N)-6M)

- 1) **MOA AND AOA ARE PUBLIC DOCUMENTS AND CAN BE INSPECTED BY ANY PERSON:** MOA & AOA of every company are registered with the ROC. Upon registration, they become public documents. They can be inspected by any person on payment of a nominal fee at the ROC.
- 2) **PURPOSE OF DOCTRINE OF CONSTRUCTIVE NOTICE:**
 - a) This doctrine protects “the company against the outsiders”.
 - b) This doctrine is a continuation of doctrine of ultravires.
 - c) It is presumed that every person dealing with the company has read MOA & AOA.
 - d) Further it is presumed that he has understood the provisions of Memorandum and Articles correctly i.e. in the right sense. This is known as “Doctrine of Constructive Notice”.
- 3) **EFFECT:** This doctrine presumes that every person dealing with the company is presumed to have read the MOA & AOA. Further, such other person can't plead that he is not aware of the provisions of MOA & AOA. **(Kotla Venkatswamy vs. Chinta Ram Murthy)**
- 4) **EXCEPTION TO DOCTRINE OF CONSTRUCTIVE NOTICE:**
 - a) There is one exception to the doctrine of constructive notice. Outsiders dealing with the company are not required to enquire into the internal proceedings of the company.
 - b) An outsider dealing with the company can assume that as far as the internal proceedings of the company are concerned, everything has been properly done, in accordance with MOA, AOA and the Act.
Note: *The is an assumption and hence rebuttable.*
 - c) This exception of doctrine of constructive notice is also known as ‘doctrine of indoor management’ or the rule laid down in the case of Royal British Bank v. Turquand.
 - d) Thus, doctrine of constructive notice protects the company from outsiders, whereas doctrine of indoor management protects outsiders from the company.

Q.No.14. Briefly explain the doctrine of “Indoor Management” Or TURQUAND’S Rule and its exceptions. (A) (NEW SM, OLD SM, OLD PM, M15 - 5M, N18 (O) - 6M))

- 1) **DOCTRINE OF INDOOR MANAGEMENT / OSTENSIBLE AUTHORITY:**
 - a) This doctrine is an exception to doctrine of constructive notice.
 - b) It acts as a protection to outsiders dealing with the company.
 - c) An outsider dealing with the company can assume that all the internal proceedings of the company are properly followed.
 - d) Outsiders need not enquire into the regularity of internal proceedings of the company. This is called as Doctrine of Indoor Management. It is also known as Turquand rule. **(Royal British Bank Vs. Turquand)**
- 2) **EFFECT OF DOCTRINE:**
 - a) In the absence of this doctrine, company could escape its liabilities or obligations by denying the authority of officials who acted on its behalf.
 - b) This doctrine is a safeguard against the possibility of abusing the doctrine of constructive notice. **(Howard vs. Patent Ivory Manufacturing Co, Mahony vs. East Holyford Mining Co)**
- 3) The benefit of Doctrine of Indoor Management can be availed only if the person dealing with the company,
 - a) Has knowledge of MOA and AOA; and
 - b) Has no Knowledge of internal irregularity

- 4) **EXCEPTIONS:** In the following circumstances an outsider dealing with the company cannot claim any relief on the ground of doctrine of indoor management. In other words, doctrine of constructive notice will apply in the following situations.
- a) **Knowledge of irregularity:** If a person dealing with a company has actual knowledge of an internal irregularity then he cannot claim the benefit under the rule of indoor management.
 - b) **Negligence / Suspicious circumstances:** If there are suspicious grounds surrounding a transaction, but the person dealing with the company fails to make reasonable inquiry then the benefit of doctrine of indoor management will not be available.
(Underwood vs. Bank of Liverpool)
 - c) **Forgery:** Since forgery is regarded as nullity, such acts done in the name of a company are void ab initio. The doctrine of indoor management does not apply to such forged transactions.
(Ruben vs. Great Fingall Consolidated & Co)
- 5) **DISTINCTION BETWEEN DOCTRINE OF CONSTRUCTIVE NOTICE AND DOCTRINE OF INDOOR MANAGEMENT:** The doctrine of constructive notice protects a company against outsiders whereas the doctrine of indoor management protects outsiders against the actions of a company.

SIMILAR QUESTIONS:

1. Explain the doctrine of indoor management as applicable in case of companies. Explain also the circumstances in which an outsider dealing with the company cannot claim any relief on the basis of doctrine of 'Indoor Management'. (M12 - 8M)
 - A. Refer answer to the above question.
2. The Persons (not being members) dealing with the company are always protected by the doctrine of Indoor management. Explain. Also explain when doctrine of constructive notice will apply (N18-6M)
 - A. First write about Doctrine of Indoor Management.
There are certain exceptions to Doctrine of Indoor Management and in all such situations Doctrine of Constructive Notice will apply. So, write the exceptions to Doctrine of indoor management.
3. A sole director and principal shareholder of a company gave instruction to the banker to deposit company cheques into his own Bank Account. Banker without proper enquiry deposited the same into director's account. Whether banker takes protection under Turquand case?
 - A. In the present case, a cheque was drawn in favour of company. One of the directors gave instruction to the bank to deposit the cheque in his personal bank account instead of Company's bank account.
The Banker without proper enquiry deposited the company cheques into director personal account. Here the banker acted negligently. As per exceptions of doctrine of Indoor Management, Outsider will not be protected as he acted negligently.

(IMMEDIATELY REFER PRACTICAL QUESTIONS CRD 7, 8, 9, 10, 11)

SECTION 2: DIFFERENCES FOR STUDENTS SELF STUDY

Q.No.15. Explain the differences between 'MOA' and 'AOA'? (C)

THE DIFFERENCES BETWEEN "MOA" AND "AOA" ARE AS FOLLOWS:

Difference	MOA	AOA
Object	To state the purposes for which the company has been established.	To provide the manner in which the objects are to be carried out.
Contents	In total it contains 6 clauses. It mainly defines the scope of the activities of the company.	This contains the rules and regulations for the internal management of the company.
Members Approval for Alteration	SR is required. In certain cases, OR is sufficient.	SR is required always.
Position / Importance	It is equivalent to the 'Constitution' of the company. (Supreme document)	It is equivalent to 'bye-laws'. It is subordinate to MOA (*). If there is a conflict between AOA & MOA, the latter shall prevail.

Action Ultravires	Any act of the Companies which is ultravires the MOA is fully void and <u>cannot</u> be ratified even by the whole body of shareholders.	Any act of the company which is ultravires the Articles (but intravires the MOA) can be ratified by the shareholders
Subsidiary to	Subsidiary to Act.	Subsidiary to Act and MOA.
Relationship	Between company and outsiders.	Between company and insiders.

**Of course, both are subordinate to any law, particularly to Companies Act, 2013.*

SECTION 3: PRACTICAL QUESTIONS FOR CLASSROOM DISCUSSION

Q.No.1. The AOA 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? **(NEW SM)**

(OR)

The AOA of ABC Company provided that 'X' shall be the Manager of the company and he shall be vacated on the ground of proved fraud. The company removed him even though his guilty of fraud not proved. Decide, whether company's action is valid? **(OLD PM)**

PROVISION: Sec 5(1) of the Companies Act, 2013 states that the articles of a company contain the regulations for the management of a company. Further sec 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 MOA & AOA of a company are binding upon company and its members and they are bound to observe all the provisions of MOA & AOA as if they have signed the same [Sec 10(1)].

However, the company and members are not bound to outsiders in respect of anything contained in MOA & AOA 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.

ANALYSIS: 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. So 'X' cannot enforce the right conferred on him by the articles against the company.

CONCLUSION: Hence the action taken by the company (i.e. removal of 'X' even though he was not guilty of misconduct) is valid. However, Mr. X can be removed by altering the AOA by a SR.

Q.No.2. Yadav dairy products Private limited has registered its articles along with memorandum at the time of registration of company in December, 2019. Now directors of the company are of the view that provisions of articles regarding forfeiture of shares should not be changed except by a resolution of 90% majority. While as per section 14 of the Companies Act, 2013 articles may be changed by passing a special resolution only. One of the directors said that they cannot make a provision against the Companies Act. You are required to advise the company on this matter.

PROVISION: As per section 5 of the Companies Act, 2013 the article may contain provisions for entrenchment to the effect that specified provisions of the articles may be altered only if more restrictive conditions than a special resolution, are met.

The provisions for entrenchment shall only be made either on formation of a company, or by an amendment in the articles agreed to by all the members of the company in the case of a private company and by a special resolution in the case of a public company.

Where the articles contain provisions for entrenchment, whether made on formation or by amendment, the company shall give notice to the Registrar of such provisions in prescribed manner.

ANALYSIS AND CONCLUSION: In the present case, Yadav dairy products Private Limited is a private company and wants to protect provisions of articles regarding forfeiture of shares. It means it wants to make entrenchment of articles, which is allowed. But the company will have to pass a resolution taking permission of all the members and it should also give notice to ROC regarding entrenchment of articles.

Q.No.3. The AOA of a Company provided that the shares of a member who became bankrupt would be offered for sale to other shareholders at a certain price. Is the provision binding on the shareholders?

PROVISION: As per Sec10 of the Companies Act, 2013, the MOA & AOA shall, when registered, bind the company and the members to the same extent as if they respectively had been signed by the company and by each member to observe all the provisions of the MOA & AOA

ANALYSIS: By applying the above provisions it is clear that provisions of the AOA are held to be binding on members. Members of the company having been purchased the shares on those terms and conditions are bound by the provisions contained in AOA.

CONCLUSION: Shareholders are bound by the stated provisions in the Articles.

Q.No.4. The Board of Directors of Sindhu Limited wants to make some changes and to alter some Clauses of the Articles of Association which are to be urgently carried out, which include the increase in Authorized Capital of the company, issue of shares, increase in borrowing limits and increase in the number of directors. Discuss about the provisions of the Companies Act, 2013 to be followed for alteration of Articles of Association. **(RTP Nov' 18, (May' 18)**

Section 14 of the Companies Act, 2013, vests companies with power to alter or add to its articles. The company has to fulfill the following conditions for such alteration:

- 1) The company may alter its articles by passing a special resolution. However increase in authorized capital can be done by an ordinary resolution.
- 2) For any alteration having the effect of conversion of a public company into a private company shall be valid only when approved by the Central Government (power delegated to regional director) on an application made in such form and manner as may be prescribed.
- 3) The company shall file within 15 days file with the registrar.
 - i). every alteration of the articles, and
 - ii). a copy of the order of the Central Government
- 4) The Registrar shall register the change
- 5) As per section 15 every alteration made in articles of a company shall be noted in every copy of the articles. If a company makes any default in complying with the stated provisions, the company and every officer who is in default shall be liable to a penalty of one thousand rupees for every copy of the articles issued without such alteration.

Q.No.5. The principal business of XYZ Company Ltd was the acquisition of vacant plots of land and to erect the houses. In the course of transacting the business, the Chairman of the Company acquired the knowledge of arranging finance for tile development of land 'The XYZ Company introduced a financier to another company ABC Ltd and received an agreed fee of 2 lakhs for arranging the finance. 'The memorandum of Association of the company authorizes the company to carry on any other trade or business which can in the opinion of the board of directors, be advantageously carried on by the company in connection with tile company's general business. Referring to the provisions of the Companies Act, examine the validity of the contract carried out by XYZ Company Ltd. with ABC Ltd.

PROVISIONS: An act or transaction shall be treated as ultravires if it is not permitted or authorised by the Companies Act, 2013 or it falls outside the object's clause of MOA of the Company.

ANALYSIS & CONCLUSION: Arranging finance or finance or financier is an ultra vires act since-

- a) The company has no power to arrange finance or financier:
- b) Board cannot take the defense that the memorandum authorizes the company to carry on any business which can be advantageously carried on in connection with company's present business (since, it is a 'specified purpose' given u/s 13 for alteration of object clause, but it cannot be the ground or basis for carrying on a business which is outside the object clause);

However, company may enter into finance contract after altering the memorandum (by complying with the requirements of Sec. 13).

Q.No.6. The object clause of the MOA of LSR Private Ltd, Lucknow authorised 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.
(OLD PM, M10 - 5M, RTP N16)

PROVISION: An act or transaction shall be treated as ultravires if it is not permitted or authorised by the Companies Act, 2013 or it falls outside the object's clause of MOA of the Company.

However, if a company wishes to start a business which is not provided for in its MOA, it must first alter its MOA to include that business in its objects clause. It can be done with the approval of the members by a SR and the filing of it with the ROC.

ANALYSIS: M/s LSR Pvt. Ltd is authorised to trade fruits and vegetables. It has no power to enter into a partnership with Mr. J for Iron and steel business.

Such an act cannot be treated as within the 'express' or 'implied' powers of the company. Mr. J who entered into partnership is deemed to be aware of objects (powers) of M/s LSR (Pvt) Ltd *i.e. Doctrine of Constructive Notice.*

CONCLUSION: Mr. J cannot enforce the agreement or liability against M/s LSR Pvt. Ltd. Therefore, M/s LSR Pvt. Ltd. shall either return the steel purchased from Mr. J or shall make the reasonable payment for the value of steel purchased from Mr. J.

Q.No.7. The plaintiffs contracted with a director of the defendant Company and gave him a cheque under the contract. The Director could have been authorised under the Company's articles, but was not in fact so authorized. The plaintiff had not seen the Articles. The Director misappropriated the cheque and the plaintiffs sued the Company. Is the Company liable?

RELEVANT CASE LAWS: Kotla venkata swamy Vs Ram murthy's case.

PROVISION: According to Doctrine of indoor management, persons dealing with the company are presumed to have read the MOA & AOA and to see that the proposed dealing is not inconsistent there with but they need not do more *i.e.* they need not enquire into the regularity of internal proceeding as required by MOA & AOA. They can presume that all this was done regularly.

However, it has been held that the rule of indoor management cannot be invoked in favour of a person who had no knowledge of the AOA of the company.

ANALYSIS: In the given case, the plaintiff had not seen the Articles. Therefore, protection under Doctrine of Indoor Management is not available.

CONCLUSION: Company shall not be held liable by the Act of the director who has transacted without authority and plaintiff had not seen the Articles.

Q.No.8. Under the Articles of Association of Sunshine Ltd. Company directors had power to borrow up to Rs. 10,000 without the consent of the general meeting. The directors themselves lent Rs. 35,000 to the company without such consent and took debentures of the Company. Decide under the provisions of the Companies Act, whether the company is liable? If so, what is the extent of liability of the company in this case?

PROVISION: An outsider dealing with the company can assume that all the internal proceedings of the company are properly followed. Outsiders need not enquire into the regularity of internal proceedings of the company. This is called as Doctrine of Indoor Management.

However there are some exceptions to this rule.

A) Knowledge of Irregularity.

B) Negligence.

C) Forgery.

ANALYSIS: Directors were having knowledge of the fact that the limit of borrowing specified under Articles was Rs. 10,000. If company wants borrow more than Rs. 10,000, it needs to obtain consent of General Meeting. Directors lent Rs. 35,000 without consent of General Meeting.

Now, directors cannot take benefit of Doctrine of indoor management. Benefit of Doctrine of indoor management is not available to outsider when person has knowledge of irregularity in the internal management of company.

CONCLUSION: Therefore, company is liable to the extent of Rs. 10,000.

Q.No.9. A Company issued a bond under its common seal signed by 2 Directors. The Articles provided that the directors might borrow on bond such sums as they should be authorized by an "OR" of the Company. No such resolution was passed. Is the Company liable on the bond?

(OR)

Articles of Association of XYZ Ltd. provides the Board of Directors has authority to issue bonds provided such issue is authorised by the shareholders by a necessary resolution in the General Meeting of the company. The company was in dire need of such of funds and therefore, it issued the bonds to Mr. X without passing any such resolution in General Meeting. Can Mr. X recover the money from the company? Decide referring the relevant provisions of the Companies Act, 2013.

(N16 - 4M)

RELEVANT CASE LAW: Royal British bank Vs. Turquand.

PROVISION: Refer PQ.No.4

ANALYSIS: In the given case the Articles of the company provided that the Directors can borrow on bond such sums by passing on 'OR'. But the company issued the bond without passing such resolution.

The outsiders dealing with the company are entitled to assume that "OR" has been passed and they have a right to recover the amount mentioned on the bond.

CONCLUSION: The Company is liable on the bond.

Q.No.10. 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 realize 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.

(OLD PM, RTP M17, MTP M17)

RELEVANT CASE LAW: Royal British Book Vs. Turquand

PROVISION AND ANALYSIS: Refer PQ.No.4

ANALYSIS: In the instant problem the doctrine of indoor management will not apply as the certificate was forged 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*)

CONCLUSION: B will not succeed in getting the share registered in his name because the share certificate issued by way of forgery is invalid.

Q.No.11. A Managing Director of a company borrowed a sum of money by executing a document in which he forged the signature of 2 other directors who are required to sign as per requirements of articles. Can the company deny liability to creditors?

(OLD PM)

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.

Q.No.12. Parag Constructions Limited is a leading infrastructure company. One of the directors of the company Mr. Parag has been signing all construction contracts on behalf of company for many years. All the parties who ever deal with the company know Mr. Parag very well. Company has got a very important construction contract from a renowned software company. Parag constructions will do construction for this site in partnership with a local contractor Firozbbhai. Mr. Parag signed partnership deed with Firozbbhai on behalf of company because he has an implied authority. Later in a dispute company denied to accept liability as a partner. Can the company deny its liability as a partner?

As per section 22 of the Companies Act, 2013 a company may authorise any person as its attorney to execute deeds on its behalf in any place either in or outside India. But common seal should be affixed on his authority letter or the authority letter should be signed by two directors of the company or it should be signed by one director and secretary. This authority may be either general for any deeds or it may be for any specific deed.

A deed signed by such an attorney on behalf of the company and under his seal shall bind the company as if it were made under its common seal.

In the present case company has not neither given any written authority nor affixed common seal of the authority letter. It means that Mr. Parag is not legally entitled to execute deeds on behalf of the company. Therefore, deeds executed by him are not binding on the company. Therefore, company can deny its liability as a partner.

SECTION 4: PRACTICAL QUESTIONS FOR STUDENTS SELF PRACTICE

Q.No.1. The Board of Directors of PV Limited wants to make some changes and to alter some Clauses of the Articles of Association which are to be urgently carried out, which include the increase in Authorized Capital of the company, issue of shares, increase in borrowing limits and increase in the number of directors. Please advise the company about the procedure to be followed for alteration of Articles of Association. **(M 18(O) - 4M)**

ALTERATION IN ARTICLES OF ASSOCIATION: Section 14 of the Companies Act, 2013, vests companies with power to alter or add to its articles. The law with respect to alteration of articles is as follows:

- 1) **Alteration by Special resolution:** Subject to the provisions of this Act and the conditions contained in its memorandum, if any, a company may, by a special resolution alter its articles.
- 2) **Filing of alteration with the registrar:** Every alteration of the articles and a copy of the order of the tribunal approving the alteration, shall be filed with the Registrar, together with a printed copy of the altered articles, within a period of fifteen days in such manner as may be prescribed, who shall register the same.
- 3) **Any alteration made shall be valid:** Any alteration of the articles registered as above shall, subject to the provisions of this Act, be valid as if it were originally contained in the articles.
- 4) **Alteration noted in every copy:** Every alteration made in articles of a company shall be noted in every copy of the articles, as the case may be. If a company makes any default in complying with the stated provisions, the company and every officer who is in default shall be liable to a penalty of one thousand rupees for every copy of the articles without such alteration. [Section 15].

Q.No.2. The AOA of a Public Company clearly states that Mr. A will be the solicitor of the company. The Company in its GM of the shareholders resolved unanimously to appoint B in place of A as the solicitor of the company by altering the AOA. Examine, whether the company can do so? State the reasons clearly. **(OLD PM, M13 - 5M, RTP M15, M17, MTP M18(O))**

PROVISION AND ANALYSIS: Upon registration, MOA and AOA shall bind the company and members as if they have been signed by the company and each member respectively. All monies payable by any member to the company under MOA or AOA shall be a debt due from him to the company. [Sec.10 (1)].

Special Resolution is required for every alteration of articles. Such alteration must comply with the Provisions of Companies act and powers of MOA.

A Copy of Special Resolution (MGT-14), copy of the altered AOA and copy of the NCLT order (*in case of conversion of public to private*) shall be filed with the ROC within 15 days, and the ROC shall register the same.

Every alteration of AOA which is registered by the ROC shall be valid as if it were originally contained in the articles.

CONCLUSION: In the present case, the company has altered the Articles by a unanimous resolution of the members passed at GM. Hence, the alteration is valid and after registration of the altered Articles, the appointment of B will stand and A will be terminated.

Q.No.3. X, a chemical manufacturing company distributed Rs.10 lakhs to fine arts and science institutions for furtherance of knowledge of arts and science. Referring to the provisions of the Companies Act, 2013 decide whether the said distribution of money was 'Ultra Vires' the company? **(OLD PM)**

PROVISION: Refer Doctrine of Ultra vires.

ANALYSIS & CONCLUSION: 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.

Q.No.4. The object clause of the memorandum of Association of the XYZ (Pvt) Ltd., New Delhi, authorized to do trading in mangoes. The company, however, entered into partnership with Mr. A and traded in mangoes and incurred liabilities to Mr. A. The Company subsequently refused to admit the liability to "A" on the ground of "ultra vires" the company".

In terms of Companies Act, 2013, the powers of the company are limited to:

- 1) Powers expressly given by the Memorandum (which is popularly known as 'express' power or conferred by the Companies Act 2013, or other statute and
- 2) Powers reasonably incidental or necessary to the company's main purpose (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 object clause enable shareholders, creditors or others to know what its powers are and what is the range of its activities and enterprises

The objects clause therefore is of fundamental importance to the shareholder, creditors and others. 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 can never be treated as '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. Mr. J should be advised accordingly. This conclusion is supported by the decision reported in the case of 'The Ganga Mata Refinery Company (Pvt) Ltd CIT

Q.No.5. The directors of a company were authorised "to make payments towards any charitable or any benevolent object or for any general public or useful object". In accordance with shareholders resolution the directors paid Rs. 2 lacs formed for the purpose of promoting technical and business knowledge. The company's business having been taken over by L.C., it had no business left of his own.

PROVISION: Refer Doctrine of Ultra vires.

ANALYSIS AND CONCLUSION: The Supreme Court held that the payment was ultra vires the company. Directors could not spend company's money on any charitable or general objects. They could spend for the promotion of only such charitable objects as would be useful for the attainment of the company's own objects.

Q.No.6. With the approval of the board, an amount of Rs. 50 crore was spent by Speed Jet Led., in producing a commercial film, not covered under its objects clause. The film was a complete flop and the company lost an amount Rs. 40 crore. Some of the members of the company objected to such investments not covered by the objects clause of the company. They filed a suit in the court of law making the directors personally responsible and to make good the loss. Will they succeed? Support your answer with reasons.

PROVISION: Refer Doctrine of Ultra Vires.

ANALYSIS AND CONCLUSION: Board of directors of company has invested an amount of Rs. 50 crores in producing commercial film not covered under its object clause. The act of the directors is ultra vires and the person responsible for entering into this project is personally liable. Members will succeed in suit.

Q.No.7. The object clause of the MOA of RST limited authorises it to publish and sell text books for students. The Company, however, entered into an agreement with Q to supply 100 laptops of worth Rs. 5 Lakh for resale purposes. Subsequently, the company refused to make payment on the ground that the transaction was ultravires the company. Examine the validity of the company's refusal for payment to Q under the provisions of companies act, 2013?

PROVISION: Refer Doctrine of Ultra Vires.

ANALYSIS & CONCLUSION: The main object of RST Limited is to publish and sell textbooks for students. It therefore has no power to enter into an agreement with Q to supply 100 laptops. Such act can never be treated as express or implied power of the company. Q is deemed to be aware of the lack of powers of RST limited. Thus, Q cannot enforce the agreement or liability against RST limited. Hence the refusal of the company for the payment to Q is valid.

Q.No.8. Under the AOA, the Directors of a Company had power to borrow up to Rs.1,00,000 without the consent of the GM. The Directors themselves lent Rs. 2,00,000 to the Company without such consent and took Debentures. Is the Company liable for Rs. 2,00,000?

PROVISION: An outsider dealing with the company can assume that all the internal proceedings of the company are properly followed. Outsiders need not enquire into the regularity of internal proceedings of the company. This is called as Doctrine of Indoor Management.

An outsider dealing with the company cannot claim any relief on the ground of doctrine of indoor management if a person dealing with a company had actual knowledge of an internal irregularity.

ANALYSIS AND CONCLUSION: Company is not liable to repay the loan of Rs. 2,00,000, since the directors lent money without approval from members. Here the directors cannot take the benefit of Turquand rule as they have knowledge of irregularity.

SECTION 5: CASE LAWS

ASHBURY RAILWAY CARRIAGE AND IRON CO. LTD. V. RICHE:

1) **Extract of Object clause:** The object clause of an industrial company contained the following objects besides the other objects:

- a) To make, sell or lend on hire, railway carriages and wagons.
- b) To carry on the business of mechanical engineers and general contractors.
- c) To purchase, lease, work and sell ~~mine~~ minerals, land and buildings.

2) **Nature of Contract made by company:** The company entered into a contract with Richie, for the financing of a construction of a railway line in Belgium.

3) **Decision of the Court:**

- a) The court held that the general contractors had to be given a restricted meaning.
- b) Only such contractors could be covered in the term general contractors as are in some way related or connected with the mechanical engineering.
- c) Therefore, the company could not finance the construction of a railway line by alleging that such a business falls under the business of general contractors.

KOTLA VENKATSWAMY VS. RAM MURTHY

In this case, the Articles provided that all deeds, etc., were to be signed by the Managing Director, Secretary, and a Working Director.

- 1) A deed signed by the Working Director and Secretary was held to be inoperative and the party was not allowed to seek exemption on the plea that he had not read the Articles.
- 2) Accordingly, if a person deals with a company and the transaction turns out to be beyond the powers of the company or its officers as contained in these documents, he cannot enforce it against the company and he shall be personally liable to bear the consequences of such dealings.

ROYAL BRITISH VS. TURQUAND: Doctrine of Indoor Management was first laid down in the case of Royal British Bank vs. Turquand. In this case, the directors of a company issued a bond to Turquand. They had the power to issue such bonds but only subject to the resolution passed at a General Meeting of the company.

- 1) In this case no such resolution had been passed.

- 2) It was held that Turquand could recover the amount of the bond from the company on the ground that he was entitled to assume that the resolution had been passed.
- 3) It was observed that 'outsiders are bound to know the external position of the company, but are not bound to know its indoor management'.

MAHONY VS. EAST HOLYFORD MINING CO:

- 1) In the case of Mahony vs. East Holyford Mining Co., Articles of company suggesting that cheques were to be signed by two named directors and countersigned by the named secretary.
- 2) The secretary of company sent to their banker what purported to be copy of the board resolution naming the directors and secretary.
- 3) The banker accordingly honored the cheques. Subsequently, it was found that the directors and the secretary were never appointed. No Board Meeting was ever held.
- 4) It was held that bankers were bound to inspect the Articles which they did. Beyond that they were neither bound nor entitled to look into the regularity of appointment of the directors and the secretary.)

HOWARD VS. PATENT IVORY MANUFACTURING CO:

- 1) The directors had the power under the Articles to borrow on behalf of the company up to £ 1,000.
- 2) For any amount exceeding this sum, the sanction of the shareholders in the General Meeting was required.
- 3) The directors themselves lent £3,500 to the company without the sanction of the shareholders in the General Meeting. It was held that the company was liable for £ 1,000 only

UNDERWOOD VS. BANK OF LIVERPOOL:

- 1) Certain cheques drawn in favour of company were deposited by director in his personal account.
- 2) The bank credited the cheques in the account of director instead of company's account.
- 3) The bank argued that they acted on direction of director of company.
- 4) The Court held that cheque of company could not be given credit to personal account of director. It case of gross negligence on part of banker.

RUBEN VS. GREAT FINGALL CONSOLIDATED & CO:

- 1) Share certificate was issued under common seal of company.
- 2) However, signature of two directors thereon was forged.
- 3) Shareholder argued that he cannot determine forgery but on the ground of forgery is nullity, certificate was held to be invalid.

ANAND BIHARI LAL VS. DINSHAW & CO:

- 1) The plaintiff accepted a transfer of the company's property from its accountant, the transfer was held void.
- 2) The plaintiff should have seen the power of attorney executed in favour of the accountant by the company.

BORELAND TRUSTEES VS. STEEL BROTHERS & CO. LTD.

- 1) The Articles of the company provided that the shares of any member who became bankrupt should be sold to some other persons at a price to be fixed by 'directors
- 2) B became bankrupt and his trustee in bankruptcy claimed that he was not bound by the Articles of Association and could, therefore, sell the shares as he liked.
- 3) It was held that the trustee in bankruptcy was bound by the Articles of Association and could not claim the shares against the company.

WOOD VS. ODESSA WATER WORKS CO.

- 1) The Articles empowered the company to declare a dividend to the shareholders with the sanction of the company at General Meeting.

- 2) Instead of paying the dividend in cash, a resolution was passed whereby the dividend was to be paid by issue of debenture bonds.
- 3) A member filed a suit restraining the company from acting on the resolution.
- 4) The Court granted an injunction restraining the company from acting on the resolution.

RAY FILED VS. HANDS AND OTHERS:

- 1) The Articles provided that every member who intends to transfer shares shall
- 2) Inform the directors who will take the said shares equally between them at a fair value.
- 3) On their refusal to take the shares, it was held that the directors as members were bound to take shares.

LENARDS CARRYING CO. LTD. V. ASIATIC PETROLEUM CO. LTD. [1955] AC 705.

- 1) Viscount Haldane propounded the `alter ego` theory and distinguished it from vicarious liability.
- 2) The House of Lords stated that the default of the managing director who is the directing mind and will of the company, would be attributed to him and he be held for the wrong doing of the company.

LAKSHMANASWAMI MUDALIAR V. L.I.C., A.I.R. 1963

- 1) S.C. 1185 upheld the doctrine of ultravires. In this case, the directors of the company were authorised `to make payments towards any charitable or any benevolent object or for any general public or useful object`.
- 2) In accordance with shareholders resolution the directors paid Rs. 2 lacs to a trust formed for the purpose of promoting technical and business knowledge.
- 3) The company's business having been taken over by L.I.C., it had no business left of its own.

SECTION 6: TRUE OR FALSE STATEMENTS – FOR STUDENTS SELF PRACTICE

- 1) The purpose of Doctrine of Ultra vires has been defeated as the members can alter the object clause by passing a special resolution (T).
- 2) Doctrine of ultra-vires provides that in case of emergency, having regard to the benefits, company may slightly deviate from MOA (F).
- 3) The company cannot make ultravires contract as valid even if they passed a special resolution or unanimous resolution (T).
- 4) Alteration of articles shall be filed with ROC within 30 days (F).
- 5) Copies of MOA/AOA shall be given to members within 15 days of request (F).
- 6) Model form of articles contained in Table "F" relates to company limited by guarantee (F).
- 7) An ultravires transaction will not affect the right to acquire the property of a company (T).
- 8) The articles of association of a company can be altered by passing an ordinary resolution in the meeting of the shareholders (F).
- 9) The original Articles of a Company contained no powers to issue preference shares. Later, the articles were altered by a special resolution so as to assume the necessary power, and preference shares were issued accordingly. This is a valid alteration (T).
- 10) Regulations provided for in the articles must not exceed the powers of the company as laid down by its memorandum (T).
- 11) The Articles of Association are subsidiary both to the Companies Act and the Memorandum of Association (T).
- 12) In case of model articles and registered Articles sets conflicted, the registered Articles shall apply (T).

THE END

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