



LEARNING OBJECTIVES

- Meaning of Forms of Business Organisations
- Sole Proprietorship: Meaning, Features, Merits and Limitations
- Hindu Undivided Family (H.U.F.) Business: Meaning, Types, Merits and Limitations
- Partnership Firms: Definition, Features, Merits, Limitations, Types of Partners and Partnerships, Partnership Deed and Registration
- Cooperative Society: Meaning, Features, Merits, Limitations and Types of Cooperative Societies
- Joint Stock Company: Meaning, Features, Merits, Limitations and Types of Companies
- Formation of a Company: Promotion, Incorporation, Capital Subscription, Commencement
- Documents Used in the Formation of a Company
- Starting a Business: Basic Factors

INTRODUCTION

This chapter deals with the forms of business organisations in the private sector. The organisations in this sector have been classified into five categories. **First** is Sole Proprietorship business which is run and controlled by a single person. **Second** is Hindu Undivided Family Business which is an ancestral business and controlled by the oldest male person of such family business. **Third** is Partnership Business which is started with minimum two partners and normally the maximum partners do not exceed 50 persons. **Fourth** is a Cooperative Society which is started with the cooperative efforts of certain number of persons who may plan to provide goods and services at the most cheapest rates to its members and **fifth** type of business organisation is the Joint Stock Company which is started when the business has to be operated at a very large scale. Funds are raised by inviting public to invest their savings in the company and in return they are allotted shares and securities/certificates.

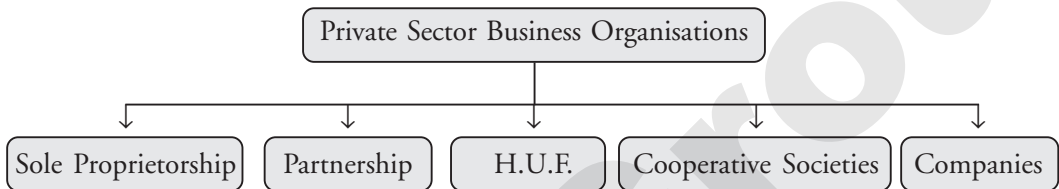
MEANING OF FORMS OF BUSINESS ORGANISATIONS

Business organisations can be owned and organised in several forms. The ultimate right choice of the form or business is a very crucial decision and depends upon the factors like power or control, scale of business (small, medium or large), motive (profit or social service), ownership or management (private, public or both), responsibility, liability (limited or unlimited), capital (limited or huge), risk bearing capacity (restricted or shared) and balancing of the advantages and disadvantages. Being a long-term commitment, the choice of the form of business should be made after considerable

thought and deliberation. Broadly speaking, types of business organisations can be classified into two broad categories:

Nature of Organisations	Private Sector	Public (Government) Sector
Non-Corporate	Sole Proprietorship	Departmental Undertakings
	Partnership firms	
	Hindu Undivided Family Business	
Corporate	Cooperative Society	Statutory/Public Corporations
	Companies	Government Company
	Limited Liability Partnership	

Apart from the above there can be Joint Sector Enterprises which may be formed with the ownership of Government and Private Business Entrepreneurs.



SOLE PROPRIETORSHIP

MEANING OF SOLE PROPRIETORSHIP

Sole means only and proprietor refers to the owner. Hence, sole proprietor is the one who is the only owner of a business. The person who runs this kind of business is known as Sole Trader and the business is known as Sole Trade.

It is the type of a business which is controlled and managed by a single person who invests money in the form of capital, receives profits and bears all losses.

This form of organisation is most suitable for small-scale business and personalised services and accounts for about 95% of the industrial sector in the country.

FEATURES

(i) **Formation and Closure.** Due to least or no legal formality, such business organisation can easily be formed and closed. There may be little legal hurdles in the start-up and continuing the business when it may have to obtain certificate or licence in case of chemist shops, restaurants, hotels, etc.

(ii) **Liability.** The liability of the sole proprietor is always unlimited in the sense that his personal assets can also be used to pay the liabilities of the business if the funds realised on the sale of assets are not sufficient to pay the liabilities of the business in a situation when the business has to be closed down.

(iii) **Sole Risk Bearer and Profit Recipient.** Sole proprietor is the only person who has to bear all losses due to uncertainties and unexpected events and gets the profits as a reward for bearing losses.

(iv) **Control.** As such type of organisation is owned by a single person, there is no scope for external interference. The control of sole proprietorship business always remains in the hands of the owner but can be shared if manager(s) or assistant(s) is/are appointed to expand the business.

(v) **No Separate Entity.** In Accounting terms, the owner and the businessman are distinguished as two different special entities but the law does not make any distinction the sole trader and the business. The owner is assumed to have no separate entity from the business and hence the owner is responsible to pay the debt of the business even out of his private estate.

(vi) **Lack of Business Continuity.** If there is no successor or legal heir of sole trader who can take the control and ownership of such business, such business may get shut down in case of death, insanity, imprisonment, physical ailment, bankruptcy, etc., of the sole trader.

MERITS OF SOLE PROPRIETORSHIP

(i) **Quick Decision Making.** A sole trader enjoys considerable freedom in running the business. He can gain creditworthiness in the financial sector and loyalty of the suppliers.

(ii) **Confidentiality of Information.** As the business is run and managed by a single person, he can retain the trade secrets with himself very easily. Further, the sole proprietor is not required to disclose his financial records to the public.

(iii) **Direct Incentive.** Profit is directly linked with the performance. With more efforts, more benefits are expected to be achieved. Sole proprietor is the single owner who receives the whole profit which motivates him to work hard for higher growth.

(iv) **Sense of Accomplishment.** Due to lack of any external interference, the sole proprietor feels freedom in applying his abilities in his business and obtains personal satisfaction. The success of the business gives him the feeling of accomplishment of the goals of the business.

(v) **Ease in Formation and Closure.** There are no legal formalities required to be fulfilled except for getting licenses and registration certificates in case of businesses relating to health and hazards. Moreover, there is no separate law governing sole proprietorship businesses relating to formation and closure.

LIMITATIONS OF SOLE PROPRIETORSHIP

(i) **Limited Resources.** Resources are generally limited to the availability of personal savings and borrowing from relatives. Banks hesitate to extend credit due to lack of reputation and weak financial position. Lack of resources hinders the growth of sole proprietorship business due to which, it remains small in size.

(ii) **Limited Life of a Business Concern.** Small capital, lack of credit worthiness of the business, reputation, lack of successors, lack of support from law and government,

death, insanity, lunacy of owner, etc., are some of the causes for limited life of such business.

(iii) **Unlimited Liability.** Sole proprietor cannot take too much risks for expansion and growth as the personal assets (belongings) can be used by the money lenders and creditors if the funds from the sale of assets of the business are not sufficient to pay off the liabilities of the business.

(iv) **Limited Managerial Ability.** Sole proprietor has to undertake the responsibility of all managerial functions like sales, purchase, production, marketing, selling, etc. No single person can excel in all fields. He may also not be able to hire competent and talented persons due to lack of funds.

Suitability. It is best suited for the businesses which are carried out on a small scale and the customers demand attention and personal services of the owner.

HINDU UNDIVIDED FAMILY (H.U.F.) BUSINESS

MEANING OF H.U.F. BUSINESS

Joint Hindu Family Business is a business which is run, controlled and managed by the eldest male member known as the Karta (Manager) in a Hindu Family and other male members are known as the coparceners.

Key Elements

- (a) It is also known as Hindu Undivided Family business.
- (b) It is the oldest type of business that prevails only in India.
- (c) It is run, managed and controlled by the eldest male head of the family known as Karta.
- (d) **Karta** is the eldest male member in a H.U.F. business and is also known as the Manager.
- (e) No division of property until all members mutually agree to do so.
- (f) **Coparceners** are male members relating to three successive generations.
- (g) On the death of Karta, next eldest male member becomes the head of H.U.F.
- (h) It comes into existence by the operation of Hindu Law and not out of contract between the coparceners.
- (i) All male members with three successive generations get the right from birth over the ancestral property.
- (j) **Ancestral Property** is the property which a person inherits to receive property or title from ancestor.
- (k) All money goes into a common pool and all property is held jointly.
- (l) Hindu Succession (Amendment) Act, 2005, now empowers female members the equal right in the ancestral property. **Even the female members can be karta.**
- (m) It is governed by Hindu Succession Act, 1956 under Hindu Law.

Conditions for the existence of H.U.F. Business:

- (a) There must be atleast two male members.
- (b) Existence of some ancestral property.

TYPES OF THE H.U.F. FAMILY SYSTEM

There are two types of system on the basis of which H.U.F. business runs.

(a) **Dayabhagha System.** This system prevails in West Bengal in which female members are also entitled to receive the right in the ancestral property. A son gets right in the ancestral property only after the death of his father.

(b) **Mitakshara System:** This system prevails in the whole India except West Bengal in which only male members have the right in the property by birth.

Important Note. *As per Hindu Succession (Amendment) Act 2005, females can become coparceners in the property of HUF. This bill was passed to remove the discrimination as described in Section 6 of Hindu Succession Act, 1956. So, classification of HUF system has no relevance in the real life situations.*

FEATURES OF H.U.F.

(i) **Formation.** For Hindu Undivided Family business there should be atleast two male members in a family and the ancestral property to be inherited by them. There is no need for any mutual agreement among the members. Such business is governed by Hindu Succession Act, 1956.

(ii) **Liability.** Liability of all members known as coparceners is limited to the extent of equal share in the property of Hindu Undivided Family except that of Karta which is unlimited.

(iii) **Control.** Karta also known as the manager holds the control of Hindu Undivided Family business and his decisions are binding on the rest of the members. He can take advice from them but they cannot force the Karta to accept their opinions.

⁽¹⁾ The eldest female member can also be 'Karta'. New law gives equal rights to both male members and female members but does not provide any clarity on the status of a female as 'Karta'. Judgements in different cases have decided whether the eldest female can be Karta or not as the married female belongs to two families and may be involved in the business of two families.

(iv) **Continuity.** In the event of the death of Karta, the next eldest member can take up the charge of Hindu Undivided Family business. Continuity may get affected if all the members mutually agree to the partition of the business.

(v) **Minor Members.** A person in Hindu Undivided Family gets membership by birth. All members have equal rights whether they are major or minor.

ADVANTAGES / MERITS OF H.U.F.

(i) **Effective Control.** The Karta holds the whole control of the business. He can take the decisions independently without consulting other members which saves time and does not miss opportunities.

(ii) **Continued Business Existence.** Death of the Karta does not affect the continuity of the business as the next eldest member can take the charge of the business and continuity is not threatened.

(iii) **Limited Liability of Members.** Except Karta, the liability of Hindu Undivided Family members is limited to the extent of their shares in the business which means, the personal assets of the members cannot be used beyond their share in the business if such business gets dissolved. Personal Assets as well as share in the property of business belonging to the Karta can be used in case of dissolution.

(iv) **Increased Loyalty and Cooperation.** As the business activities are conducted by the members jointly for the benefit of mutual interest, members become loyal to one another. For the growth of the business, they tend to co-operate with the Karta in the functioning of the business.

LIMITATIONS OF H.U.F.

(i) **Limited Resources.** The activities of the Hindu Undivided Family business mainly depends upon the availability of ancestral property. Many lenders may hesitate to extent the credit if there are conflicts on the financial matters among the members.

(ii) **Unlimited Liability of Karta.** Karta is responsible not only for managing and controlling the business but also responsible to repay the debts of the business out of his personal assets if the business is closed.

(iii) **Dominance of Karta.** The Karta himself manages and controls the family business. He takes all decisions without consulting other members, which may at times not be acceptable to other members. This may lead to conflicts among them and consequently working of the business may breakdown.

(iv) **Limited Managerial Skills.** One person cannot be perfect in all areas in managing the business. Karta is selected on the basis of age and the age alone cannot bring managerial talents in the business. So, due to lack of such talents, such business organisations run into losses.

PARTNERSHIP FIRMS

Sole proprietorship suffers from the limitations in terms of capital, managerial skills, specialised or professional knowledge and the ability to share risks of the business. Partnership is the viable option to overcome the limitations of sole proprietorship.

DEFINITIONS OF PARTNERSHIP

“Partnership is the relation between persons who have agreed to share profits of a business carried on by all or any one of them acting for all.” ...Partnership Act, 1932

“Partnership is the relation which subsists between persons who have agreed to combine their property, labour or skill in same business and to share the profits therefrom between them.” ...Indian Contract Act, 1872

FEATURES OF PARTNERSHIP

(i) **Formation.** A partnership firm may be formed with the help of a partnership deed/agreement which may be oral, written or implied. The relationship among the partners in the partnership arises due to such contract. The partnership deed contains terms and conditions governing the relationship among the partners and the manner in which the business will be carried out. Such business must be lawful with the aim to earn profit. Any association of persons with charitable purpose will not form partnership.

(ii) **Liability.** Liability of each partner is unlimited which means the personal assets of the partners can be utilised to pay for the liabilities of the business if the funds realised on the sale of assets of the business (in the event of dissolution) are not sufficient to pay the liabilities of the business.

(iii) **Risk Bearing.** As the profits are shared in their agreed ratio, similarly risks are also borne in the same ratio or any other ratio as agreed in their partnership deed like loss on insolvency of a partner which is borne by the other solvent partners in the capital ratio if there is no special provision for it.

Note: *It should be noted that any person who receives the profits in the firm may not bear the losses like manager receiving certain percentage on profits as commission or minor as a partner.*

(iv) **Decision Making and Control.** Decisions are taken with the mutual consent and the activities of the business are controlled with the joint efforts of the partners.

(v) **Continuity.** Partnership firms suffer with the limitation of continuity which may be affected with death, lunacy, insolvency of one or all partners, insanity or retirement of a partner.

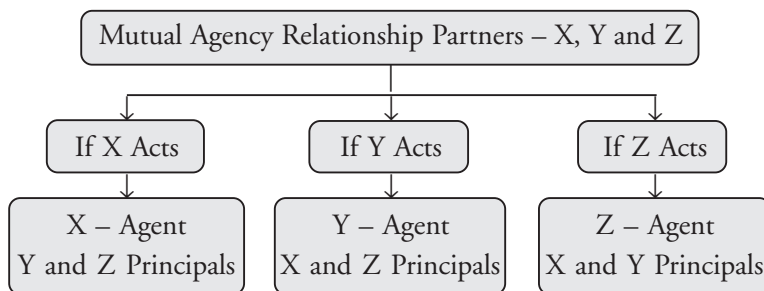
However, the other remaining partners may continue the business with their mutual consent on the basis of a new partnership deed.

(vi) **Number of Partners.** Partnership Act, 1932, specifies the minimum number of partners as two but is silent on the maximum number of partners. According to Companies Miscellaneous Rules, 2014, the maximum number of partners cannot exceed 50.

Note: *Companies Act, 2013 empowers the central government to allow maximum number of partners to 100. Presently, the central government has allowed maximum of partners in a partnership to 50 through Companies Miscellaneous Rules 2014.*

(vii) **Mutual Agency.** Definition of partnership as per Section 4 of the Partnership Act, 1932 clearly defines that 'the business is carried on by all or any one of them acting for all' which means that there is mutual understanding among the partners that the acts of one or more partners are binding on the remaining partners.

A partner acting on the behalf of other partners is called agent and other partners are principals and vice-versa. So, every partner is **principal** as well as **agent** towards one another.



MERITS OF PARTNERSHIP

(i) **Ease of Formation and Closure.** Partnership firms can be formed easily even with the presence of two members with the help of a partnership deed (oral/written or implied). The registration of the name of the firm in the eyes of law is optional. Similarly, such partnership firms can easily be dissolved with the mutual consent of all partners or by all partners except one partner.

(ii) **Balanced Decision Making.** Due to mutual agency relationship, everyone is expected to be competent to hold professional approach for taking wise decisions. Such decisions are also taken with the mutual consent by all partners. Thus, balanced decisions making is maintained.

(iii) **More Funds.** Sole proprietorship does not maintain good reputation and creditworthiness in the market due to higher possibility of risks with regard to repayment of debts and timely payment of interest. But partnership business can collect huge amount of funds from the partners and finds easy market to obtain funds.

(iv) **Sharing of Risks.** Every business is exposed to various kinds of risks. Such risks are unavoidable. It becomes difficult for a sole proprietor to bear huge losses but in case of partnership firms, such risks are shared by all partners.

(v) **Secrecy.** As the registration of partnership firms is optional, partnership firms are not required to publish its accounts publicly. This way, it can maintain confidentiality of financial information to be disclosed.

LIMITATIONS OF PARTNERSHIP

(i) **Unlimited Liability.** The partners are jointly as well as personally responsible to pay the debts of the business. Their liability towards the debts of the firm is unlimited in the sense that their personal assets can be used to repay the liabilities of the business if the funds realised after selling the assets in the event of dissolution are not sufficient to pay liabilities of the business.

(ii) **Limited Resources.** As a partnership firm cannot invite more than 50 persons as partners in its business. So, such kind of business feels the scarcity of funds. Such scarcity hampers the progress of the business. Sometimes, partnership firms get converted into joint stock companies to raise huge capital from the general public.

(iii) **Possibility of Conflicts.** Presence of mutual agency relationship may prove to be a source of conflicts as one or more partners may not agree to the act on the behalf of other partner(s). There may be a difference in opinion in their decision making. Restriction on transferability of interest (share in the firm) to any outsider may lead the firm to dissolution if a partner wishes to leave the firm.

(iv) **Lack of Continuity.** The circumstances like lack of mutual understanding, partnership at will (where a partner may give notice to the firm to dissolve the firm), retirement, death, lunacy, idiotic behaviour, insolvency of one or all partners may lead the firm to dissolve. Except to the situation of insolvency of firm, the remaining partners may continue the business by preparing new agreements.

(v) **Lack of Public Confidence.** As the partnership firms are not required to disclose their financial results to the public and government agencies, the general public, suppliers, banks and financial institution may not judge the financial soundness of such firms and may hesitate to extend any credit or loans.

TYPES OF PARTNERS

As there can be different kinds of partnership, so there can be different types of partners with different authorities, responsibilities and liabilities. It must be clear to all outsiders about the status of the partners (who may claim to be partner but may not be in reality) before entering into any transaction or contract. The following are the types of partners:

(i) **Active/Ostensible Partner.** He is a partner who contributes capital, takes active part in the business affairs, has unlimited liability, conducts the business, is liable for his acts to the outsiders alongwith other partners, shares profits and losses of the business. He is required to give public notice on his retirement.

(ii) **Sleeping or Dormant Partner.** Any partner in a firm who contributes capital, shares the profits and losses of the business, assumes unlimited liability, liable to other parties (outsiders to business) for the debts of the firm but does not take part in the day-to-day activities of the business is known as a sleeping partner.

(iii) **Secret Partner.** As the name indicates, the identity of such partner is not disclosed to the general public. Apart from distinct features, the rest of the features are same like active partner, i.e., he contributes capital, shares profits and losses, takes active part in the management and liable to the outsiders for the debts of the firm with unlimited liability. But charges fee as per his/her services.

(iv) **Nominal Partner.** Such partner lends/allows his/her name to be used as a partner without having any real interest in the firm. He/she does not contribute any capital and shares no profit or loss of the business. He/she does not take any active part in managing the firm and is liable to pay the debts of the firm like other partners with unlimited liability but charges fee as per his/her services.

(v) **Partner by Estoppel.** If any person though actually not a partner styles the character of a partner by words, initiative, conduct or behaviour in front of any outsider of a business firm then he is estopped from denying being a partner and such partner is known as a Partner by Estoppel.

Such partner does not contribute any capital and cannot intervene in the affairs of the business but has liability to repay such debts, if any outsider has given any loan or extended credit due to impression of such person being partner in such a business.

Example. Mr. Kewal is a rich person, good friend of two partners, Mr. Kunal and Mr. Prateek who are running partnership business under the name 'Threebrix Accounting Solutions' impresses Mr. Manish with his words that he is a partner in the firm. Mr. Manish grants loan to the firm. Mr. Kewal will be responsible to repay the debts if the firm is not able to repay loan to Mr. Manish.

(vi) Partner by Holding Out. A person is said to be a partner by holding out in a firm if such person, though not a partner, allows himself/herself as a partner or remains silent on being represented as partner by the actual partners in the firm. Such partner becomes liable to outside creditors for repayment of any debt which has been extended to the firm on the basis of such representation.

Thus, the person to be charged with liability by holding out must have done some thing which amounts to representation that he was a partner in a business. If such a partner wants to save himself from the liability of business, he should immediately issue a denial clarifying his position that he is not a partner in a firm.

Example. In the same example under partner by estoppel, if Mr. Kunal and Mr. Prateek declare Mr. Kewal as partner (in their firm) before Mr. Manish and Mr. Kewal does not react then Mr. Kewal will be responsible to pay such debts which have been extended by Mr. Manish to the firm due to such representation.

Minor as a Partner

Position

As per general rule, a minor cannot enter into valid legal contract with others unless he/she attains the age of maturity (i.e., 18 years) but can be admitted as a partner for the benefits of the firm with the mutual consent of all other partners.

Features

- (i) He/she is incompetent to enter into legal contracts.
- (ii) He/she is admitted as a partner for the benefits of the firm.
- (iii) His/her liability towards the debts of the firm is limited to the extent of his capital and available undistributed profits.
- (iv) He/she is not eligible to take an active part in the management but can inspect books of Accounts.
- (v) He/she can share profits but not bear the losses.
- (vi) On attaining majority, he/she is required to give public notice whether or not he/she would continue as a partner like others failing to which he/she would be treated as a partner with unlimited liability.

TYPES OF PARTNERS (COMPARISON)

Type	Capital	Management Contribution	Shares Profits/ Losses	Liability
• Active Partner	Contributes capital	Participates in management	Shares profits and losses	Unlimited
• Sleeping or Dormant partner	Contributes capital	Does not participate in management	Shares profits and losses	Unlimited
• Secret Partner	Contributes capital	Participates in management but secretly	Shares profits and losses	Unlimited
• Nominal Partner	Does not contribute capital	Does not participate in management	Does not share profits and losses	Unlimited
• Partner by Estoppel	Does not contribute capital	Does not participate in management	Does not share profits and losses	Unlimited
• Partner by Holding Out	Does not contribute capital	Does not participate in management	Does not share profit and losses	Unlimited
• Minor Partner	Contributes capital	Cannot participate in management but can inspect books of accounts	Shares profits only	Limited to Capital Contribution and reserves

TYPES OF PARTNERSHIPS

(a) **On the Basis of Time Duration.** On the basis of time duration, partnership firms can be divided into two categories:

(i) **Partnership at Will.** Where there is no provision in the partnership agreement for the duration of the partnership, the partnership is called 'Partnership at Will'. Such kind of partnership as the partners desire, can be terminated when any partner gives a notice of withdrawal from partnership of the firm.

(ii) **Particular Partnership.** Such partnership firms are formed for a particular venture or particular time period. Such partnership firms come to end automatically when the venture is completed or the time period gets expired. If such partnership is continued even after the expiry of time period, or after the completion of venture, such partnership firm is deemed to be partnership at will [Section 17(6)]. Such partnership firm may be dissolved before the expiry of time period or before the completion of venture only if all partners carry mutual consent to dissolve it.

(b) **On the Basis of Liability.** On the basis of liability, such partnership firms are classified into two categories:

(i) **General Partnership.** In such kind of partnership, the liability of each partner is unlimited and joint with the firm. Each partner enjoys the right to participate in the functioning of the firm and his/her acts are binding on the rest of the partners and the firm. **Registration of the firm is optional and not compulsory.** The survival of the business gets affected due to death, lunacy, retirement, solvency of one partner or all.

(ii) **Limited Partnership.** In limited partnership, the liability of at least one partner (known as General Partner) is unlimited whereas the liability of the other partners (known as Limited Partners) is limited to the extent of capital contributed by them. The continuity of the partnership does not get affected with the death, retirement, insolvency, lunacy of any partner with limited liability. Partners with limited liability also cannot enjoy the right in the management. Their acts do not bind the firm or other partners. **Registration of such firms is compulsory.**

Note: Such type of partnership was permitted in India after the introduction of New Small Enterprise Policy in 1991. The basic purpose of introduction of such kind of partnership was to attract such entrepreneurs who were reluctant to become partner due to unlimited liability.

(c) **Limited Liability Partnership (L.L.P.).** With the growth of Indian economy, the role played by its entrepreneurs as well as its technical and professional manpower has been acknowledged internationally. In this background, a need was felt for a new corporate form that would provide an alternative to the traditional partnership which exposes its partners to unlimited personal liability.



The Government of India with the help of the Ministry of Law and Justice passed an Act in the parliament known as ‘**Limited Liability Partnership Act, 2008**’.

Limited Liability Partnership [LLP] is viewed as an alternative corporate business vehicle that provides the benefits of the limited liability but allows its members the flexibility of organising their internal structure as a partnership based on a mutually arrived agreement.

Meaning: It is a partnership firm like corporate body, artificial person, with separate legal existence, perpetual succession, wherein partners can be individual or corporate body with at least two designated partners.

Examples: Knowledge Media Ventures LLP, Chokriti Chocolates LLP, Alpine Coils LLP, Hemant Shah & Associates LLP, Fabricons Projects LLP and Shakti Clothings LLP.

Activity for students: Students should prepare detailed information on the above LLPs through online search.

Features of Limited Liability Partnership

1. **Corporate Body.** A limited liability partnership is a corporate body, intangible and artificial person which is created by law, ended by law, can enter into contracts in its own name, can sue and be sued and has separate legal existence from its members.

2. **Perpetual Succession.** The existence of the LLP shall not get affected with the entry or exit of the partners like in case of Joint Stock Company. Change in the partners shall not affect the existence, rights or liabilities of limited liability partnerships.

3. **Liability:** Liability of a partner is limited to the extent of capital contribution and share in net reserves. In case, if any event is carried out by LLP or by a partner(s) with the intent to defraud creditors of LLP, the liability of LLP and partner(s) who acted in such events or fraudulent practices, shall be unlimited for all such debts.

[Section 30 of LLP Act, 2008]

4. Partner as an agent: Every partner of LLP is the agent of LLP but not of other partners. So, mutual agency relationship does not exist as it happens in case of general partnership. *[Section 26 of LLP Act, 2008]*

5. Number of Partners. Two or more partners are required to form an LLP. Any individual or a body corporate can be a partner in an LLP. There must be minimum two individuals (who are also known as designated partners) to form LLP. Beyond these two individuals, there can be individual as well as body a body corporate as partner.

There is no limit on maximum number partners (Law does not specify maximum number of partners).

6. Designated partners. LLP shall have at least two “designated partners” who are individuals and at least one of them shall be “resident in India”. In case one or more of the partners of the LLP are corporate bodies, at least two individuals who are partners of such LLP (or nominees of such corporate bodies) shall act as “designated partners”.

7. Incorporation of LLP. Procedure for incorporation of LLP is similar to the procedure for incorporation of a company under the Companies Act, 2013. Applicants are first required to file the application for reservation of name with the Registrar of Companies (ROC). Once the name applied is approved by the ROC, the documents for incorporation of LLP need to be filed.

8. Partnership Act, 1932. Provisions of the ‘Partnership Act, 1932’ shall not apply on the Limited Liability Partnership. LLP will be governed with the provisions of ‘Limited Liability Partnership, Act 2008’ and name of every LLP shall end with the words ‘limited liability partnership or LLP’.

9. Contribution by a Partner:

(a) The contribution of a partner to the capital of LLP may consist of any of the—
tangible, movable or immovable property.

(b) Intangible property.

(c) Other benefit to the LLP including money, promissory notes, contracts for services performed or to be performed.

DIFFERENCE BETWEEN L.L.P. AND PARTNERSHIP

Basis	L.L.P.	Partnership Firm
1. Governing Law	The Limited Liability Partnership Act, 2008 and various Rules made thereunder.	The Indian Partnership Act, 1932 and various Rules made thereunder.
2. Registration	Compulsory	Optional
3. Creation	Created by law	Created by contract
4. Separate Legal Entity	It is separate legal entity, separate from its partners / designated partners.	It is not separate legal entity from partners. Partners are collectively referred as firm.
5. Perpetual succession	It has perpetual succession.	It does not have perpetual succession.

DIFFERENCE BETWEEN LLP AND SOLE PROPRIETORSHIP:

Basis	L.L.P.	Sole Proprietorship
1. Registration	It is registered under Limited Liability Partnership Act, 2008.	There is no law for registration.
2. Name of business	Name of the business ends with 'LLP'.	There are no legal restrictions.
3. Legal Status	Separate legal existence from its members.	No separate legal existence from the owner.
4. Liability	Limited to the extent of capital contribution and surplus in business.	Unlimited, even personal assets can be attached to pay business liabilities.
5. Members	Minimum: Two Maximum: No limit	Only one person governs the entire business.
6. Transferability of ownership	Transferability of share by a member does not affect the business.	Transferability of share by the owner leads to sale of business.

PARTNERSHIP DEED

It is a document containing terms and conditions mutually agreed upon by all partners so that all possible disputes which may arise in future can be avoided. Also known as partnership agreement, it may be expressed as oral, written or implied. It is always desirable to have the deed in a written form to use it as evidence though the law does not require such document in writing. Its contents must not be contradictory to the provisions of Indian Partnership Act.

Contents of Partnership Deed

1. Name of the firm and partners.
2. Address of the office of the business and partners.
3. Nature and location of the business.
4. Duration of the business.
5. Capital contributed by partners.
6. Provision relating to interest on capitals, interest on loans, interest on drawings, salary, commission, etc.
7. Rights and liabilities of partners.
8. Procedure for dissolution of partnership and firm.
9. Method of valuation of goodwill.
10. Mode of settlement in the case of retirement and death of a partner.

REGISTRATION OF A PARTNERSHIP FIRM

Registration of a partnership firm means bringing the name of such firm into existence in the eyes of law. Registration is done in the area in which the place of business of the firm is situated or proposed to be situated.

Partner(s) are required to contact the registrar of firms and submit the relevant documents with the application form. When the registrar is satisfied with the contents and documents, he makes an entry in the 'Register of Firms' and issues a certificate of registration which is a conclusive proof of the firm's existence.

Procedure of Registration

In the registration of firm, following steps are included:

- (1) Contact Registrar of the area in which the place of business is situated or proposed to be situated.
- (2) Obtain and submit the registration form with following particulars:
 - (a) Name of the firm.
 - (b) Principal or main place of business.
 - (c) Name of other places where the firm carries on the business.
 - (d) The date when each partner joined the firm.
 - (e) Name and address of each partner.
 - (f) Duration of partnership firm, if any.
- (3) Get the form verified and signed by each partner.
- (4) Submit the application form with requisite fee.
- (5) Obtain the certificate of registration after the registrar makes an entry in the Register of Firms.

Consequences of Non-Registration

- (1) No partner can file a suit against any other partner or firm in the court of law to recover any amount due to him.
- (2) The firm also cannot file a suit against any partner to recover any dues.
- (3) A firm cannot file suit against the third parties like collection from debtors.

Note: *It is to be noted that creditors can file a case to recover their dues even if the firm is unregistered.*

Need/Benefits of Registration

- (1) Partner can file case against other partners or firm to recover dues.
- (2) Firm can also file case against the partners to recover any dues from them.
- (3) The firm can enforce its claims against third parties in the court of law.
- (4) Any person who wishes to become a partner can get relevant information from the office of the registrar.
- (5) Any supplier before entering into contract can obtain information about the financial soundness of such firm.

COOPERATIVE SOCIETY

MEANING OF COOPERATIVE SOCIETY

The word 'cooperative' means working together and with others for a common purpose.

"The cooperative society is a voluntary association of persons who join together with common social cultural and economic interest through the principles of self and mutual help."

Mutual help means each for one and all for each. Cooperative society can be formed with the mutual consent of at least ten adult members for a common purpose and the funds contributed by them is known as share capital in the form of shares.

Cooperative society is required to be registered under Indian Cooperative Societies Act, 1912 and get separate legal entity from its members with limited liability.

DEFINITIONS OF COOPERATIVE SOCIETY

"Cooperative society is a society which has its objectives for the promotion of economic interests of its members in accordance with cooperative principles."

...Indian Cooperative Society Act, 1912

"Cooperative is a form of organisation wherein persons voluntarily associate together as human beings on the basis of equality for the promotion of its economic interest for themselves."

...E.H. Calvert

FEATURES OF COOPERATIVE SOCIETY

(i) **Voluntary Membership.** Any person who has a common interest with the aims of a society concerned can become a member by purchasing certain number of shares as per his/her wish. Such person can also quit the society by serving a proper notice to the office of society.

(ii) **Separate Legal Existence.** A cooperative society enjoys separate legal status and distinct identity from its members after getting registered under Indian Societies Act, 1912. A society can enter into legal contracts with outsiders in its own name, can sue others and can be sued by others. Its existence is not affected by entry or exit of members.

(iii) **Limited Liability.** The liability of the members to pay the debts of the society (if funds of society are not sufficient to pay its liabilities) is limited to the extent of capital contribution and undistributed profits if any.

(iv) **Control.** Control and management of the cooperative societies remain in the hands of elected members. Such members are elected on the basis of number of members and not on the basis of number of shares held by them. Each member carries one vote irrespective of the total shares held by him/her. This policy ensures democratic management and each member enjoys equal right in electing the members of the management committee.

(v) **Service Motive.** The motive behind setting up of any society is to serve and help its members and society. Earning profit is not the motto of societies but if any

surplus is generated due to its operations, the same is distributed as dividend after retaining certain part of profits towards reserves.

(vi) **Utilisation of Surplus.** According to Indian Cooperative Societies Act, 1912, each society must transfer 1/4th of its total profits to Statutory (General) Reserve. It is required to spend upto 10% of the surplus profit for the welfare of its members and remaining profit is distributed as dividend among the members.

MERITS OF COOPERATIVE SOCIETY

(i) **Equal Voting Rights.** Due to the existence of democratic management in the cooperative societies, each member carries one vote irrespective of the number of shares held by him. '*One man one vote*' is the slogan of cooperative number of societies.

(ii) **Limited Liability.** The liability of each member is limited to the extent of sum of capital invested by the members and undistributed profits. The members cannot be called upon to contribute anything more than the face value of shares held by them. Their personal assets cannot be attached to repay the debts of the cooperative societies if the funds of the society are not sufficient to pay liabilities of the cooperative societies.

(iii) **Stable Existence.** Existence or survival of the business of cooperative societies is not affected by the death, lunacy, bankruptcy or insanity of its members. The members may enter and exit but the cooperative society enjoys its continuity.

(iv) **Economy in Operation.** Members of the cooperative societies generally provide honorary services to the society. The purpose of running any cooperative society is to eliminate the middlemen in the process of production to consumption. They make bulk purchases directly from the manufacturers and sell directly to its members thereby saving a lot of cost of distribution.

(v) **Support/Patronage from Government.** As the cooperative societies run on the principles of democracy, the government does not hesitate while giving grants, loans at low rate of interest, subsidies, concessions in the interest rates, etc.

(vi) **Ease of Formation.** Cooperative societies can be formed with minimum 10 members. Procedure for registration is simple under the provisions of Cooperative Societies Act, 1912 as compared to complex provisions of Companies Act, 2013.

LIMITATIONS OF COOPERATIVE SOCIETY

(i) **Limited Resources.** Social upliftment, self-reliance, common cause, etc., are the governing factors which run cooperative societies. Therefore, profit earning is not the sole motto of cooperative societies. Hence, cooperative societies are unable to pay higher dividend on the capital contributed by the members which do not attract new members whereas suppliers/bankers hesitate to extend credit facilities and loans to the societies.

(ii) **Inefficiency in Management.** As the cooperative societies suffer from the limitation of availability of financial resources, generally members themselves provide honorary services to function the societies. Such members cannot be expected to be

professionally trained and professionals from outside may not be hired due to lack of financial resources.

(iii) **Lack of Secrecy.** Presence of democratic setup, open discussions, meetings and disclosure requirements under the provisions of Cooperative Societies Act, 1912 make it difficult for the cooperative societies to maintain secrecy.

(iv) **Government Control.** Cooperative societies have to comply with various rules and regulations relating to auditing of accounts and the state governments also control the functioning of such cooperative societies which affects the freedom of operation of the societies.

(v) **Differences in Opinions.** The functioning of the cooperative societies is undertaken mainly by the members themselves in their own way. This becomes the source of conflict among the members and sometimes the members may take personal advantage due to autonomy availed by them.

TYPES OF COOPERATIVE SOCIETIES

(i) **Consumers' Cooperative Societies.** Such societies are formed to protect the interest of the members. Such societies buy the goods directly from the producers or wholesalers to eliminate the role of middlemen and to sell such goods directly to its members at the minimum price to cover the cost. Profit known as surplus if any left, is distributed among the members on the basis of capital contribution or purchases made by them.

(ii) **Producers' Cooperative Societies.** Such societies are formed by the small-scale producers who find it difficult to procure raw material and basic inputs required to produce the goods. Society so formed by them buys the required inputs for their members directly from the manufacturers and supply to the members at the basic cost. It also buys the output from the members and sells it in the market. Profit thus earned is divided among the members on the basis of proportion of goods produced or sold by the members.

(iii) **Marketing Cooperative Society.** Such society is formed by the members who find it difficult to sell the products in the market. Small-scale producers cannot spend too much amount on the channels of distribution due to shortage of funds. The office of the society collects the output from its members and performs the activities like packing, packaging, warehousing, branding, labeling, grading, etc., on the behalf of its members and sells the pool of output directly to the retailers or consumers. Profits earned after such process are distributed among the members on the basis of contribution of their output

(iv) **Farmer's Cooperative Societies.** Such society is formed by the farmers holding small fragmented pieces of land which buys the inputs as required by the farmers for cultivation of crops in bulk from the market and supplies to its member farmers according to their requirements. Such inputs are in the form of better quality seeds, fertilisers, chemicals, machineries, tools, etc. This way farmers are benefitted by providing better inputs at reasonable cost to enable large-scale production.

(v) **Credit Cooperative Societies.** Such societies are formed to provide credit or loans to its members at a low rate of interest than banks' rate. Capital contributed and deposits received from the members become the base for extending credit to the members. This way, members are saved from the exploitation of high rate of interest being charged by the banks and private money lenders.

(vi) **Cooperative Housing Societies.** Such societies are formed by people who desire to acquire residential accommodation at the lowest prices. Members contribute their savings as share capital which is utilised in major part of cost of construction by eliminating big builders. Members can also acquire such accommodations by paying the cost in installments and construct the plots in their own way.

JOINT STOCK COMPANY

CONCEPT OF JOINT STOCK COMPANY

When the business entrepreneurs wish to operate at a large scale and don't wish to take too much risk by investing their own funds, they form a company form of organisation.

In the partnership firm, maximum number of partners cannot exceed 50. So there is a limitation relating to contribution of capital, even if the partners are able to contribute large amount of capital, they still wouldn't like to take a risk due to unlimited liability towards the debts of the firm.

Solution to the above problem is the creation of a company form of organisation in which members contribute their savings known as share capital which is divided into a number of units of fixed denomination known as shares. The persons who buy the shares in a company are known as shareholders and in return whatever the profit they receive is known as Dividend. They are the owners in the company to the extent of the number of shares they hold. The members among themselves are elected as Board of Directors in Annual General Meetings who control and manage the activities of the company on the behalf of rest of the shareholders. The liabilities of each shareholder is limited to the extent of face value of shares held by him/her and accumulated past profit minus losses. It means personal assets of the shareholders cannot be used if the company reaches the position of liquidation/winding up.

The company form of organisation has also the privilege to raise funds by issuing debentures and taking loans from the banks, financial institutions and general public. When the loan component is divided into a number of units, such units are called debentures or bonds and the persons (natural or artificial) holding such units are called debentureholders.

COMPOSITION OF CAPITAL EMPLOYED

Capital employed in the company consist of two types of funds:

- (a) **Owners Funds.** It consist of Shares (Equity Shares* + Preference Shares*), Past Undistributed reserves and surplus and unwritten losses.

- (b) **Borrowed Funds.** It is raised by issuing Debentures*, Bonds and Long-Term Loans. As the major part of capital employed is held by the group of persons, such form of organisation is known as 'Joint Stock Companies' or Corporations. *These sources of funds have been discussed in detail under chapter 'Sources of Business Finance'.

IMPACT OF COMPANIES ACT, 2013

The Companies Act, 2013, replaces the decades old Companies Act, 1956, which had been amended several times. The Companies Act 2013 got assent from the President of India on 29th August 2013. The act comprises 29 Chapters, 470 Sections with 7 Schedules. It is substantively a law based on Rules. The changing national and international economic environment, exponential growth of the Indian economy and changes in the stakeholders' expectations necessitated for a need for a new Companies Law.

MEANING OF COMPANY

"A company is an artificial voluntary association of persons created by law for carrying on a lawful business having separate legal entity from its members with perpetual succession and a common seal".

Section 2(20) of Companies Act, 2013, defines a company as 'a company incorporated under this Act or any other previous Company Law'.

FEATURES OF A JOINT STOCK COMPANY

1. **Artificial Person.** Every company is required to be incorporated (registered) under the provisions of Companies Act, 2013. It does not take birth like a natural person. It is an artificial person and is created by law and the only law can end it. Like that of the natural person, it can own property, incur debts, file suits against its debtors, be sued by its creditors, enter into contracts with others under its own name but cannot be imprisoned.

2. **Separate Legal Entity.** A company being created under law has a separate entity from its members. Any of its members can enter into contracts with others. A member cannot bind the company by his acts or dealings with the third parties. The company can file a suit against its members and its members can also sue the company. Further, a shareholder is not liable for the acts of the company even though he may be holding all the shares of that company.

3. **Formation.** Every company is formed and incorporated (registered) under the provisions of Company's Act, 2013 with the help of an officer called registrar. It is only after its incorporation, that the company comes into legal existence. Formation of a company is a very complicated and lengthy process. The promoters of the company have to fulfill various legal formalities, prepare and submit certain important documents* with the registrar.

Members may come, members may go, but the company goes on forever.

*Memorandum of Association and Articles of Association.

4. Perpetual Succession. A company enjoys its continuous existence. The members may come and go but its existence is not affected by admission, death, lunacy or insolvency of its shareholders or directors as in the case in partnership or sole proprietorship. The company can only be liquidated (ended) by the operation of law.

5. Control. Joint stock companies have democratic management and control. That is, even though the shareholders are owners of the company, all of them cannot participate in the management of the company and have no right to be involved in the day to day activities. Normally, the shareholders elect representatives from among themselves known as 'Board of Directors' to manage the affairs of the company. This board of directors elects the top management.

6. Liability. The liability of the shareholders is limited to the extent of total face value of the shares they have subscribed including net of past undistributed profits and losses. The face value can be paid in lump sum or in installments. The shareholders cannot be asked to contribute anything more than the face value of the shares they hold and no personal assets of the shareholders can be attached in the event of liquidation of the company.

Example. Suppose Mr. Sareen buys 2,000 shares of ₹ 100 each in the share capital of Zee Ltd. Company demands ₹ 70 per share which was duly paid by him. His total liability in the share capital of the company stands at ₹ 2, 00,000, paid up value at ₹ 1,40,000 and unpaid liability stands at ₹ 60,000. Beyond this amount the shareholder is not liable to contribute anything towards the debts or losses of the company even if it reaches the situation of winding up. Only the funds realised on the sale of assets will be utilised to pay the liabilities of the company.

7. Common Seal. Since a company is an artificial person, it cannot put its signature on any document. Therefore, it is statutory for every company to have a seal on which the name of the company is engraved. Affixing of seal on any document signifies the signature of the company.

Example. The purchase manager may enter into a contract for buying raw materials from a supplier. Once the contract paper is sealed (stamped in the name of company) and signed by the purchase manager, it becomes valid. If purchase manager may leave the company thereafter or may be removed from the job or may have taken a wrong decision, yet for all purposes the contract is valid till a new contract is made or the existing contract expires.

Note: *Use of common seal is now optional. If a company does not have common seal the authorisation of documents shall be done by two directors or by a director and the company secretary, wherever the company has appointed a company secretary. (Companies Amendment Act 2015)*

8. Risk Bearing. In case of sole proprietorship or partnership firms, it may be difficult for the owners to bear the brunt of losses but it is not so in the case of joint

stock company which can be spread among the large number of shareholders but the limitation of bearing the risk of losses in case of a company is limited to the extent of face value of the shares held by them.

MERITS OF A JOINT STOCK COMPANY

1. **Limited Liability.** The liability of the shareholders is restricted to the extent of the face value of the shares held by them. Their personal assets cannot be used if the funds realised on the sale of assets are not sufficient to pay the liabilities of the business in the event of liquidation.

2. **Transfer of Interest.** It means the ownership of the shares can be transferred at the stock exchange with the help of the stock brokers who charge a certain fixed commission for the transaction. Stock exchange is the place for the sale and purchase of shares and securities.

3. **Perpetual Existence/Succession.** The existence of the company is not affected by the death, lunacy, insolvency of the shareholders. Old members may go and new members may come but the operations of the company always continue. Law can create it and only the law can end it. It still remains alive even if all the shareholders die.

4. **Scope for Expansion.** Such form of organisation is started when the business has to be started on a large scale. Large number of investors (individuals, banks, financial institutions, foreign investors, etc.) pool their financial resources to meet the financial needs of the companies in the form of equity shares, debentures or bonds, loans, etc.

Easy transferability and limited liability, high returns on equity shares, fixed returns on preference shares and committed returns on the loans attract different kinds of investors towards the company's funds.

Note: *There are two kinds of shares viz; Equity Shares on which rate of return fluctuates year to year and others are preference shares on which returns are fixed. Details are given in chapter seven.*

5. **Professional Management.** Company form of organisation does not face the problem of funds. Different departments are created for different functions. Heads of such departments are known as Departmental Managers like Purchase Manager, Sales Manager, Finance Manager, etc., who are highly specialised in their fields and help in achieving higher production, reduce the operating cost and earn high amount of profits.

LIMITATIONS OF JOINT STOCK COMPANY

1. **Complexity in Formation.** The promoters have to prepare various documents, fulfill various legal formalities, and follow rigorous steps to get the certificate, to register in the eyes of laws and to start the business. It is a time consuming process and requires a lot of effort.

Note: *Promoters are expert persons who undertake the responsibility to form the companies.*

2. **Lack of Secrecy.** The provisions of the Companies Act, 2013 requires each company to publish, upload the various financial statements on its website and submit it with the registrar. So, it is difficult to maintain the secrecy of the information which the board of directors may not like to share.

Note: *Financial Statements are the end results which depict the financial position in the form of Statement of Profit/Loss and Balance Sheet.*

3. **Impersonal Work Environment.** Large number of shareholders make it difficult to maintain personal relations. There is completely professional work environment and management is separated from the rest of the shareholder who generally meet in the meetings.

4. **Numerous Regulations.** Every company has to fulfill various requirements as per provisions of Companies Act, 2013, Registrar of the Companies (R.O.C.), SEBI, Banks, Financial Institutions, Government Agencies and so on. Such formalities affect the freedom of functioning, take lot of time and increase the cost of operation.

5. **Delay in Decision Making.** Every company form of organisation follows a hierarchy. Orders and instructions flow from the top level to the bottom level and performance, feedback, grievances flow from bottom level to top level. Following the path of such communications system, some important decisions get delayed and opportunities are lost.

Note: *Hierarchy-A series of managerial positions from top to bottom is called levels of management. A level of management determines the amount of authority and status enjoyed by any managerial position. The chain of command consisting of a series of managerial position is called the hierarchy of management.*

6. **Oligarchic Management.** Company form of organisation is financed by a large number of investors who are scattered all over the country or even the world but is controlled by a small group of persons known as the Board of Directors duly appointed by the rest of the shareholders. All shareholders generally do not attend all meetings due to varied reasons and small investors do not have a say in the decision making. So, the board of directors enjoy considerable autonomy while running the business in the way they feel right.

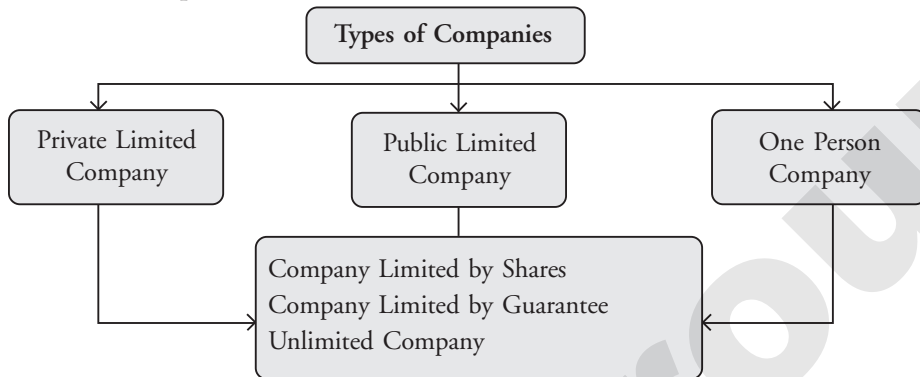
Note: *Oligarchy is a form of power structure in which power effectively rests with a small number of people.*

7. **Conflicts in Interests.** Company form of organisation is associated with numerous number of persons (stakeholders) like shareholders, banks, financial institutions, workers, government agencies, etc. Each stakeholder has own interest in the financial matters of the company. It becomes difficult for the company to satisfy the interest of all stakeholders.

TYPES OF COMPANIES

Companies are broadly classified into three categories:

- Private Limited Company
- Public Limited Company
- One Person Company



COMPANIES LIMITED BY SHARES

It is a company in which its members (shareholders) have the liability to pay the amount of face value of shares subscribed/held by them. They can never be called upon to pay any amount beyond the face value of shares even in the event of liquidation. This is the reason why this form of organisation carries an advantage of limited liability.

Example: A shareholder holds 1,000 shares of ₹ 100 each and has paid to the extent of ₹ 75 per share. In this case, he has a total liability of ₹ 1,00,000, out of which he has already paid ₹ 75,000. At the most, the shareholder can be asked to pay the remaining amount of ₹ 25,000 which can be called by the company any time from being a going concern to being wound up.

Companies limited by shares are the most common and may either be public or private (private limited and OPC).

(A) Private Company / Private Limited Company: ‘Private, Company’ means a company having a minimum paid up share capital as may be prescribed. A private limited company

- (a) restricts the right to transfer its shares;
- (b) except in case of One Person Company, limits the number of its members between 2 and 200;
- (c) has at least two directors;
- (d) prohibits any invitation to the public to subscribe for any securities of the company;
- (e) uses the words ‘private limited’ after its name;

[Ref.: Section 2(68) of Companies Act, 2013 and Companies Amendment Act, 2015]

Examples: Sharp Metal Private Limited, Shri Laxmi Oil Mill Company Private Limited, Breeze Investments Private Limited, Cosmic Renewable Private Limited, Reliance Agency Private Limited and Hindustan Thomson Associates Private Limited.

Activity for students: Students should prepare detailed information on the above Companies through online search.

Privileges to a Private Limited Company

(a) **Share Capital.** A private limited company does not require to maintain any specific minimum paid up share capital as per Companies Amendment Act, 2015 (earlier it was ₹ 100,000 as per Companies Act, 2013).

(b) **Number of Members.** A private limited company can be formed by just two persons as against a minimum of seven persons required for a public limited company.

(c) **Number of Directors.** A private limited company is required to appoint a minimum of 2 directors as against 3 directors in a public limited company.

(d) **Prospectus.** A private limited company need not file Prospectus or Statement in lieu of Prospectus with the Registrar of Companies as such companies are not allowed to issue shares and debentures to raise the funds from the public.

(e) **Index of Members.** Such company is not required to maintain any register of its members which is necessary in case of public company.

(f) **Restriction on Loans and Advances.** Restrictions on loans to directors/relatives, etc., does not apply to Private Ltd. Company.

Conversion of Private Limited Company into One Person Company

A private company having paid up share capital of fifty lakh rupees or less or whose average annual turnover during the relevant period is two crore rupees or less may convert itself into one person company by passing a special resolution in the general meeting. (Ref.: Rule 7 of Companies Incorporation Rules 2014)

(B) Public Company / Public Limited Company: 'A Public Company means a company which is not a private company and has a minimum share capital as may be prescribed'. A Public Company

- (a) has minimum seven members and no limit on maximum number of members.
- (b) has a minimum of three directors.
- (c) is allowed to raise its funds from the general public by issuing securities.
- (d) has no restriction on the transfer of shares (ownership).
- (e) uses the word 'limited' after its name.

(Ref.: Section 2(71) of Companies Act, 2013 and Companies Amendment Act, 2015)

Note: Securities normally include shares, Debentures/Bonds etc.

Examples: Standard Industries Limited, Tata Steels Limited, Raymond Limited, Reliance Infrastructure Limited, Hindustan Unilever Limited, Crompton Greeves Limited, etc.

Activity for students: Students should prepare detailed information on the above Companies through online search.

(C) One Person Company

Origin and Development

One person companies are in existence in certain countries. In India this concept has been mooted by the Ministry of Corporate Affairs by allowing One Person Companies in India in line with UK, China, USA, Australia, Singapore, Qatar, Pakistan and several other countries. In India Single Member Company was first recommended by the Dr. J. J. Irani Committee in 2005, which was set up by the Ministry of Corporate Affairs to suggest changes to the existing framework relatable to the India Corporate Structure.

Meaning of One Person Company

One Person Company is a company which can be formed under the provisions of Companies Act, 2013, to encourage a sole proprietor expand his/her business with limited liability. Under sole proprietorship form of business, the owner's liability towards the debts of the business is unlimited. In the event of closure of his/her business, the personal assets of the sole proprietor can be used to pay the liabilities if the funds realised on selling the assets are not sufficient to pay the liabilities of the business. Now, if a sole proprietor forms his business as OPC, his liability towards the debts of his business will be limited to the extent of business funds and personal assets cannot be used.

Definition of One Person Company

As per section 2(62) of the Companies Act, 2013, 'One Person Company means a company which has only one person as a member'.

Features of One Person Company

- (a) **Incorporation:** It is incorporated under the provisions of Companies Act, 2013.
- (b) **Eligibility to become Member:** Only a natural person who is an Indian citizen and resident in India shall be eligible to incorporate OPC.

Such person is the subscriber to the memorandum of association. If articles of association are silent for the appointment of director(s), then such member (subscriber) shall be deemed to the first director. Number of directors can be raised from one to fifteen which can further be increased by passing special resolution in case of other companies as well.

(c) **Restriction on formation of OPC:** No person shall be eligible to incorporate more than a One Person Company or become nominee in more than one such company.

(d) **Selection of Nominee:** Memorandum of OPC shall indicate the name of the other person (nominee) who shall, in the event of death of the subscriber (director) or his incapacity to contract, become the member of the company.

(e) **Eligibility for Minor:** No minor can become member or nominee.

(f) **Restriction on Business:** OPC cannot carry out Non-Banking Financial Investment activities including investment in securities of any body corporate.

(g) **Suffix to Name:** Every OPC will suffix Private Limited (OPC) with its name.

(h) **Paid-up Capital:** Minimum authorised share capital required for an OPC is ₹ 1,00,000; it cannot exceed ₹ 50 lacs.

(Ref.: Rule 3 of Companies Incorporation Rules 2014)

(i) **Restriction on conversion:** Such company cannot be incorporated or converted into a company under section 8 of Companies Act, 2013 (Companies formed for charitable purposes, etc.)

Note: The term “resident in India” means a person who has stayed in India for a period of not less than one hundred and eighty two days during the year immediately preceding one calendar year.

Examples: Alwandi Agro Farms (OPC) Private Limited, Harika Food Products (OPC) Private Limited, Sansys Enterprises (OPC) Private Limited, Bharpoor Agro (OPC) Private Limited, SVK Minings (OPC) Private Limited, Splenders (OPC) Private Limited, Sunahari Foods (OPC) Private Limited, etc.

Activity for students: Students should prepare detailed information on the above Companies through online search.

Conversion of OPC into Private Limited Company or Public Limited Company

(a) An OPC can get itself converted into a Private or Public company after increasing the minimum number of members and directors to two or minimum of seven members and two or three directors as the case may be, and by maintaining the minimum paid-up capital as per requirements of the Law.

(Ref.: Rule 6 of Companies Incorporation Rules, 2014)

(b) No OPC can convert voluntarily into Private Limited/Limited Company unless two years have elapsed from the date of incorporation of One Person Company, except only in the case where paid up share capital is increased beyond fifty lakh rupees or its average annual turnover of the last three years exceeds two crore rupees.

(Ref.: Rules 3 to 7 of Companies Incorporation Rules 2014)

Advantages of One Person Company

- It is beneficial for those individuals who wish to have personal freedom.
- Minimal paper work and compliances to the Companies Act, 2013.
- There is separate legal entity of the business with one member.
- Provision of conversion into other forms by amending M.O.A.
- Liability of the member is limited in the sense that personal assets cannot be used to pay business liabilities.

Limitations of a One Person Company

- Slower to start than a sole proprietorship
- Greater Compliance responsibility owing to Annual Returns, etc.
- As it is classified as Pvt. Ltd., there is greater Income Tax burden than Sole Proprietorship

ONE PERSON COMPANY VERSUS SOLE PROPRIETORSHIP

Basis	OPC	Sole Proprietorship
1. Entity	Separate legal entity	Not a separate legal entity
2. Liability	Limited liability	Unlimited liability
3. Continuity	Perpetual succession	No perpetual succession
4. Registration	Mandatory	Optional
5. Finance	Finance –credit record of the OPC	Finance –credit record of the owner

DIFFERENCE BETWEEN PUBLIC LIMITED, PRIVATE LIMITED AND ONE PERSON COMPANY

Basis	Public Limited	Private Limited	One Person Company
1. Members			
• Minimum	7	2	1
• Maximum	No limit	200	1
2. Directors			
• Minimum	3	2	1
• Maximum	15	15	15
3. Transfer of Shares	Freely transferable	Restricted	Restricted
4. Invitation to Public	Possible	Not allowed	Not allowed
5. Suffix to Name	Limited	Private Limited	Private Limited ⁽¹⁾ (OPC) ⁽²⁾

(1) As OPC will be considered as Private Limited Company

(2) To be mentioned in bracket

Note: As per Companies Act, 2013, a private limited company was required to maintain minimum paid up capital of ₹ 1,00,000 [as per Section 2(68)] and ₹ 5,00,000 by a public limited company [as per Section 2 (71)]. However, as per Companies Amendment Act, 2015, no specific minimum paid-up capital is required to be maintained by private limited as well as public limited company.

COMPANIES LIMITED BY GUARANTEE

The members of such a company contribute an amount in the company's assets, if there is any shortfall, to settle the debts of the company in case it is being wound up.

Example. Clubs, trade associations and societies for promoting their objectives may be created as a company limited by guarantee.

Companies Limited by Guarantee. A special feature of this type of company is that the liability of members to pay their guaranteed amounts arises only when the company has gone into liquidation and not when it is a going concern. A guarantee company may or may not have a share capital.

- (a) *A guarantee company without any share capital:* It obtains its working capital from sources such as fees or grants.

Examples: Transforming Lives Through Education Foundation, Rotary Mumbai Divas Foundation, World Neem Organization, Rightcust Technologies Private Limited, 36 LA Webtech Private Limited, Advanced Research and Learning Council, etc.

Activity for students: Students should prepare detailed information on the above Companies through online search.

- (b) *A guarantee company having share capital:* It raises its initial capital from its members, while the normal working funds are provided from other sources such as fees, charges, subscriptions etc.

The shareholders have a two-fold liability. One is the liability to pay the amount which remains unpaid on their shares and the other is to pay the amount payable under the guarantee when the company goes into liquidation. The voting power of a guarantee company having share capital is determined by the shareholding and not by the guarantee.

Examples: Infinite Overseas Distributors Private Limited (Share Capital ₹ 1 Lakh), Purple Artech Technologies Private Limited (Share Capital ₹ 1 Lakh), etc.

Activity for students: Students should prepare detailed information on the above Companies through online search.

UNLIMITED LIABILITY COMPANIES

It means a company in which the members are liable for the company's debts in proportion to their respective interests in the company. The liability of its members is unlimited. Thus, the liability might stretch up to the full extent of their assets in the event of being wound up to meet the obligations of the company. The members of an unlimited company are not liable directly to the creditors of the company, as in the case of partners of a firm. It is only the liquidator, who can ask the members to contribute to the assets of the company, which will be used in discharging the debts of the company.

FORMATION OF A COMPANY

There are mainly three stages in the formation of a company:

- I. Promotion
- II. Incorporation
- III. Capital subscription

A private limited company has to undergo first two stages and can start its business immediately after obtaining certificate of incorporation whereas a public company limited by shares has to follow another stage of capital subscription to raise funds from the general public. All three stages have been explained in detail as under:

I. PROMOTION

Promotion is the first step in the formation of a company. It involves the identification of business opportunities prevailing in the business environment, choose the best one which is feasible and best suits the available resources. This work is done by the specialised persons known as promoters who possess the complete knowledge on how to form a company. Such promoter(s) may be individual, group of persons or even a joint stock company.

Meaning: Promotion involves identification of a business opportunity or idea, analysis of its prospects and taking steps to implement it through the formation of a company.

Promoter: A promoter is said to be the one who identifies a business opportunity, idea, analyses its prospects and takes steps to implement it through the formation of a company.

Who is Promoter: The following persons are said to be promoter:

- (a) Promoter is a person who has been named as such in a prospectus or is identified by the company in its annual return; or
- (b) Promoter is a person who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or
- (c) Promoter is a person with whose advice, directions or instructions, the board of directors of the company is accustomed to act.

Functions of Promoters

1. Identification of Business Opportunity. First, the promoters have to conceive the business idea or opportunity. Such opportunity may be in the form of producing a new product or rendering a type of service or making some product available through the different channels of distribution or any other opportunity having investment potential.

2. Feasibility Studies. After deciding the project to be undertaken, the services of different professionals who have the expertise in their respective fields is taken to know the feasibility and future prospects of the project.

COMPARATIVE EVALUATION OF FORMS OF ORGANISATION

Basis of Comparison	Sole Proprietorship	Partnership	Joint Hindu Family Business	Cooperative Society	Company
Formation	Minimal legal formalities, easiest formation.	Registration is optional, easy formation.	Less legal formalities, exemption from registration, easy formation.	Registration compulsory, greater legal formalities.	Registration compulsory, lengthy and expensive formation process.
Members	Only a single owner.	Minimum: 2 Maximum: 50	At least two persons for division of family property, no maximum limit.	At least 10 adults, no maximum limit.	Minimum: Private Company-2; Public Company-7; Maximum: Private Company-200; Public Company-No Limit.
Capital Contribution	Limited Finance	Limited but more than that can be raised in case of sole proprietorship.	Ancestral property.	Limited	Large financial resources.
Liability	Unlimited	Unlimited and joint.	Unlimited (Karta), Limited (Other members).	Limited	Limited
Control and Management	Owner takes all decisions, quick decision making	Partners take decisions, consent of all partners is needed.	Karta takes decisions.	Elected representative, i.e., managing committee takes decisions.	Board of Directors control and manage.
Continuity	Unstable, business and owner are regarded as one.	More stable but is affected by the status of partners.	Stable business, continues even if Karta dies.	Stable because of separate legal status.	Stable because of separate legal status.

Such experts may be like chartered accountant, cost accountants, company secretary, engineers, bankers, human resource managers, and finance managers, etc., who make the detailed study of the proposed project and such studies may relate to:

(a) **Technical Feasibility.** It may be possible, idea for starting a business may be quite sound and profitable but there may be certain constraints to run the business operations smoothly.

Example. The raw material required to produce the goods may be unavailable due to short supply or the technology needed for producing the goods may not be easily available due to strict government norms.

(b) **Financial Feasibility.** The financial analysts are required to estimate long-term funds as well as short-term funds. They need to find out the sources from where and how such funds would be available. For short-term funds, banks, suppliers and financial institutions may be contacted and for the long-term finance, favorable position in the financial markets to issue shares and debentures is needed.

(c) **Economic Feasibility.** Economic feasibility relates to chances of earning profits in the long run. It may be quite possible that the proposed project may be technically viable, financially feasible but there may be certain threats in the business environment beyond the control of the proposed company and may adversely affect the financial position.

3. Name Approval. After the project has been finalised, the promoters have to apply for the name to be registered for the proposed company in the state in which the registered or head office is to be situated. Three names in the order of priority have to be given in the application form to the registrar.

Situations in which the proposed name is considered undesirable:

- (i) If it is identical with or too closely resembles the name of an existing company.
- (ii) If it is misleading, it is so when the company is in a particular business but it is not true.
- (iii) If it violates the provisions of the The Emblem and Names (Prevention of Improper Use) Act, 1950.
- (iv) If it will constitute an offence under any law for the time being in force.
- (v) It is undesirable in the opinion of the Central Government.
- (vi) If it contains any word or expression which is likely to give the impression that the company is in any way connected with or having the patronage of the government, local authority, corporation or any body constituted by the government.

A person may make an application in prescribed form (Form INC1) duly accompanied with requisite fee to the Registrar for the reservation of a name.

4. Fixing up of Signatories/First Directors. The promoters have to decide about the directors who are required to give their consent to become the first directors, to buy qualification shares and sign the Memorandum of Association (discussed later)

for the authenticity of the information contained in the M.O.A., at the time of promotion of the company.

Note: *Qualification shares are the number of shares which a director may have to subscribe as per the provisions stated in the Articles of Association (A.O.A.) before the incorporation.*

Director Identification Number (DIN)

Every individual intending to be appointed as director of a company is required to make an application electronically in form DIR 3 to the Central Government for the allotment of a Director Identification Number (DIN). The form is required and signed and submitted electronically by the applicant using his or her own Digital Signature Certificate (DSC). The Central Government allots a Director Identification Number to an applicant within one month from the receipt of the application.

Note: The Central Government provides an electronic system to facilitate submission of application for the allotment of DIN through the portal on the website of the Ministry of Corporate Affairs.

5. Appointment of Professionals. Different professionals like bankers, solicitors, underwriters, auditors, etc., are required to be appointed who can perform different activities of the proposed company and prepare necessary documents to be submitted with the registrar of the companies.

6. Preparation of Necessary Documents. The main necessary documents which include Memorandum of Association*, Articles of Association*, Agreement, Prospectus Statutory Declaration, Consent of Directors, etc., are required to be prepared and submitted with the registrar of the companies. (*discussed later)

II. INCORPORATION

Incorporation means registration of the proposed company in the eyes of law. When all the necessary documents have been prepared and submitted with the registrar of the companies, the registrar will scrutinise all such documents and when he is satisfied with the correctness and authenticity of the information, he will issue the certificate of incorporation.

The registrar has to rely on the documents and it is his duty to make a thorough investigation about the authenticity of the facts mentioned in the documents.

Documents Needed for Incorporation

1. Memorandum of Association. This is the main document of the company which is also called as the charter of the company which defines its objects and powers beyond which any activity is said to be invalid. It is divided into six parts known as clauses and must be duly signed by the signatories/first directors. (Discussed in detail later in this chapter)

2. Articles of Association. It is a document like partnership deed in case of partnership firms. It is a document which contains the internal rules and regulations of the company duly signed by the signatories of the proposed company. (Discussed in detail later in this chapter)

3. Consent of the Proposed Directors/Signatories. The persons who wish to become the first directors in the proposed company have to give their consent with their addresses to become first directors and agree to subscribe for qualification shares as per the terms of articles of association.

4. Agreement. It is a document which the company proposes to enter with any individual for the appointment as its Managing Director or Whole-time Director or Manager.

5. Statutory declaration. A declaration stating that all legal formalities have been complied with has to be submitted with the registrar of the state. This document can be signed by an advocate, chartered accountant, cost accountant or company secretary in practice who is engaged in the formation of the company and by a person named in the articles as a director or manager or secretary of the company.

6. Receipt of Payment of Fee. Prescribed fee depending upon the share capital of the proposed company has to be deposited in the account of the government as per the rates prescribed in the Companies Act, 2013.

The registrar will scrutinise all the documents and when he will feel satisfied regarding completion and authenticity of the documents submitted, he will issue a certificate known as '*Certificate of Incorporation*' with Corporate Identity Number (C.I.N.). Thus, *a company gets its birth and comes into legal existence as an artificial person.*

INCORPORATION OF A COMPANY

(Promoting ease of doing business, now in just one step, one day & one e-form)

The Ministry of Corporate Affairs (MCA) has taken an initiative in Government Process Re-engineering (GPR) and launched **Simplified Proforma for Incorporating Company Electronically (SPICe) e-Form**, with the specific objective of providing hassle-free and time-saving speedy incorporation-related services in line with international best practices.

(1) Simplified and completely Digital form for Company Incorporation: Stakeholders can avail of 5 different services (Name Reservation, Allotment of Director Identification Number (DIN), Incorporation of New Company, Allotment of PAN and Allotment of TAN) in one form by applying for Incorporation of a new company through SPICe form (INC-32).

(2) e-filing of MOA and AOA as per Companies Act, 2013: The stakeholders can upload e-form for Memorandum of Association and Articles of Association through the forms, namely, eMoA (INC-33) and eAOA (INC-34). In case eMoA and eAoA are not applicable, users are required to attach the pdf attachments of MoA and AoA.

(3) No need to reserve name: There is no need to reserve a name separately before filing SPICe. One name for the proposed company can be applied for in SPICe (INC-32).

(4) **Digital Signature:** It is mandatory to have 'Digital Signature Certificates' (DSCs) of Subscribers and Witnesses in SPICe MOA and SPICe AOA.

(5) **Companies with Charitable Objects:** Companies with charitable objects under section 8 of Companies Act, 2013 can also be incorporated using SPICe form but after reserving a name using INC.

Effects of Certificate of Incorporation

1. **Legal Birth.** A company gets legal birth, comes into legal existence and become artificial person to enter into legal contracts in its own name.

2. **Perpetual Succession.** Such company becomes an artificial person with perpetual succession and working of the company never gets affected with the entry or exit of the members.

3. **Evidence of Existence.** Such certificate is the conclusive proof of the regularity of incorporation of the company even though there might have been some flaws in the process. For such flaws, the promoters remain personally liable for all pre-incorporation contracts.

Existence of the company cannot be challenged even if the company has been incorporated with illegal objects.

Case 1. Documents for registration were filed on 6th January. Certificate of Incorporation was issued on 8th January. But the date mentioned on the certificate of incorporation was 6th January. It was decided that the company was in existence and the contracts signed on 6th January were considered valid. (Jubilee Cotton Mills Ltd. Vs. Lewis)

Case 2. A person forged the signatures of others on the memorandum. The incorporation was still considered valid.

4. **Commencement of Business by Private Limited Company.** A private limited company can start its business immediately after obtaining the certificate of incorporation. It can raise funds from the members, friends, relatives or any other source but is not authorised to go public.

Preliminary Contracts / Pre-incorporation Contracts

The contracts which are entered by the promoters of the company before it gets certificate of incorporation is issued are known as Preliminary Contracts. The liability for the pre-incorporation contracts lies in the hands of the Promoters whereas the liability for Post-incorporation contracts lies with the company. If the company finds certain flaws in the pre-incorporation contracts, it may come up with fresh contracts and with new terms and conditions, but if the flaws cannot be rectified, the company cannot be forced to honour the contracts. Promoters, however, remain personally liable to the third parties for these contracts.

Provisional Contracts / Post-Incorporation Contracts

These are the contracts which are undertaken after the incorporation but before obtaining the certificate to commence the business. These contracts can be enforced on the company only after the company gets a certificate to commence the business.

III. CAPITAL SUBSCRIPTION

After obtaining the certificate of incorporation, a public limited company is required to raise the funds from the general public by issuing shares and debentures. For this purpose, the company persuades the public to apply for the shares and debentures by issuing prospectus which contains all relevant information relating to the company which an investor may require before making any decision to invest money in the company. The series of steps, a company is required to raise the funds from the public are listed below:

1. Approval from SEBI. Securities Exchange Board of India was set up by the Government of India to protect the interests of the general public, issues various guidelines to issue the shares and securities. Every company inviting the funds from the general public is required to take prior approval from SEBI and fulfill the requirements as prescribed by it.

It ensures no relevant and material information has been concealed by the company which may affect the interests of the investors.

2. Filing of Prospectus. A copy of the prospectus is required to be submitted with the Registrar of Companies (ROC). It is a document which contains all relevant information relating to company's position prior to its incorporation, memorandum of association, articles of association, list of directors, promoters and so on which an investor needs to know and analyse before making any investment decision.

It is an invitation to the public to apply for shares or debentures of the company or to make deposits in the company. Investors make up their minds about investment in a company primarily on the basis of information contained in this document. So, there must not any false statement or misleading information.

3. Appointment of Bankers, Brokers and Underwriters. Bankers receive the application money from the public who apply for the shares and debentures. Brokers help purchase and sell the shares and debentures and encourage the public to make investments. Underwriters take the responsibility to sell the shares and debentures in the market and if certain number of shares are not subscribed by public, they agree to buy such unsubscribed shares.

4. Minimum Subscription. Minimum subscription is the amount which, in the opinion of directors, must be sufficient to meet the needs of the business operations of the company. It is the amount which a company must receive by issuing shares.

A company must receive applications for such percentage of the issue as prescribed in the prospectus failing which company will have to return the money received from the applicants. To avoid such situation, the company hires the services of underwriters.

[Section 39(1) of companies Act, 2013]

As per SEBI guidelines, the limit of minimum subscription is 90% of the size of the issue. Practically, the companies willing to raise funds through public issues state minimum as 90% to 100% of the issue in the prospectus.

5. Application to Stock Exchange. An application has to be made to apply for the listing to at least one stock exchange for the purpose of sale and purchase of shares and securities. If permission is not received within ten weeks from the date of closure of subscription list, the allotment shall become void and all money received will be returned to the applicants.

6. Allotment of Shares. Return of allotment of shares to the successful applicants to whom the shares have been issued has to be signed by a director or the company secretary and be submitted with the Registrar of the Companies (ROC) within 30 days of allotment.

Note: Till the time shares are allotted, application money remains in a separate bank account. The system of blocking the application money till the allotment is known as 'Applications Supported by Blocked Amount' (ASBA). It is a better way for the investors to apply for securities as the funds remain blocked till allotment is made.

Attention for teachers on the certificate to commence business: Section 11 of the companies Act 2013 required every company limited by shares to obtain certificate to commence the business by filing various declarations on minimum subscription, paid up value of shares subscribed by directors (if any) and statutory declaration. Now, in the process of ease in doing the business, the government of India has omitted this section through Companies Amendment Act, 2015. Now, no company is required to obtain certificate to commence business.

MAIN DOCUMENTS REQUIRED TO OBTAIN CERTIFICATE OF INCORPORATION

MEMORANDUM OF ASSOCIATION

It is the fundamental document, constitution or charter of the company which defines its objectives and powers beyond which a company is not legally permitted to undertake activities. It determines utmost possible scope of operations. If a company enters into a contract which goes beyond its powers, such a contract will be ultra vires and hence stand void and even consent of all members cannot rectify such contract.

As per section 2 and sub-section 56 of Companies Act, 2013, "*memorandum means the memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this Act*".

Note: A company may adopt the format of Memorandum of Association from its respective Table A, B, C, D or E from the Schedule I of Companies Act, 2013, depending upon the nature of company.

Contents of the Memorandum of Association

(i) **Name Clause.** It states the name approved by the Registrar of the Company by which it will be known to the public. The word 'Limited' is used in case of public limited company and 'Private Limited' in case of private limited company after its name.

(ii) **Registered Office Clause/Situation Clause.** It is also known as ‘Situation Clause’. This clause states about the name of the state in which the registered office of the company is to be situated. Exact address must be notified within 30 days from the date of incorporation to the Registrar of Companies.

The domicile, the nationality of the company and the jurisdiction of the court is determined by the situation of its registered office.

(iii) **Objects Clause.** No company is permitted to undertake any activity beyond the range of the activities mentioned in this clause. It determines the capacity and purpose of the company for which it has been established. The purpose of the objects clause is to enable the persons dealing with the company to know its permitted range of activities. The acts beyond this ambit are *ultra vires* and hence void. Even the entire body of shareholders cannot ratify such acts.

(iv) **Liability Clause.** This clause states the maximum liability of a shareholder on the shares a shareholder has subscribed. It is equal to the number of shares subscribed by a shareholder multiplied with the face value of a share. It is the maximum amount which a company can demand to pay in a single installment or in a number of installments throughout its life from the shareholder.

Note: Refer features of a Joint Stock Company

(v) **Capital Clause.** This clause represents the maximum amount of money a company is authorised to raise by issuing shares. This capital is known as Authorized Capital or Nominal Capital or Registered Capital which is divided into fixed number of units and such unit is known as Par Value or Face Value or Nominal Value. It can be classified into Equity share and Preference shares.

The promoters of the company should keep the authorised capital as much high so as to meet its present as well the future financial needs of the company. A company cannot raise funds by issuing shares beyond the amount specified in the authorised share capital without altering the capital clause which requires a legal, lengthy and complicated procedure.

(vi) **Association or Subscription Clause.** The subscribers/signatories to the Memorandum of Association declare their intention to be associated with the company and give their undertaking to subscribe to the shares mentioned against their names.

The undertaking as per Table A for Memorandum of Articles in case of a company limited by shares is as:

“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 against our respective names”.

The statutory requirements regarding subscription of memorandum are as follows:

- each subscriber must take at least one share;
- each subscriber must write opposite his name the number of shares which he agrees to take. [Section 4(1)(e) of Companies Act, 2013]

Similarly, respective undertakings for different kinds of companies are given in their respective tables under Part I of Companies Act, 2013.

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

Classification of Share Capital

1. Nominal/Authorised/Registered Capital. It refers to the sum mentioned in the capital clause of memorandum of association (M.O.A.). It is the maximum amount which the company can raise by issuing shares (equity and preference, both). This capital is stated in the capital clause of memorandum of association of the company and forms the basis of determining registration fee payable to ROC. To raise capital more than this limit, a company is required to alter its memorandum of association.

Memorandum of association in general meeting and for this, articles of association must have provision. The company is required to file a notice with the registrar of companies within 30 days from the date of such alteration.]

[Section 61(1)(a) & 64 of Companies Act, 2013]

Example. A company is authorised to raise ₹ 10 crores, which is divided into 10,00,000 equity shares of ₹ 100 each.

2. Issued Capital. It refers to that part of authorised share capital, which has been offered for subscription to the persons including general public, promoters, signatories to memorandum of association, directors, employees, local/foreign investors, banks, financial institutions etc. It needs to be noted that issued capital has to be less than the authorised capital and at the most, can be equal to the authorised capital.

Example. A company having authorised capital of ₹ 10 crore divided into 10,00,000 equity shares of ₹100 each offered 2,00,000 shares to the public for subscription. Thus, the issued capital will be ₹ 2 crore (2,00,000 × ₹ 100).

3. Subscribed Capital. It is that part of issued capital, which has actually been subscribed by the persons.

Example: In the above case, if the company receives subscription/acceptance/applications for 1,80,000 shares of ₹ 100 each, then the subscribed capital will be ₹ 1.80 crores.

4. Called Up Share Capital. A company may not call the entire face value of the shares in one installment. The called up share capital is that part of the subscribed capital which has actually been called up by the company till date.

Example. If till date, a company has called up only ₹ 70 per share out of the total face value of ₹ 100 on subscribed capital of 1,80,000 shares, then the called up capital will be ₹ 1,26,00,000.

5. Paid Up Capital. It is the amount out of the called up capital which has been paid by the shareholders. It may be possible that some shareholders fail to pay their dues in time; these dues are known as calls in arrears.

Example. In the above case, if some shareholders holding the aggregate of 10,000 shares are unable to pay ₹ 20 per share, paid up capital would be ₹ 1,24,00,000 (₹ 1,26,00,000 – 10,000* ₹ 20)

Note:

- (a) *Issued capital cannot exceed authorised capital and similarly, subscribed capital cannot exceed issued capital and also, called up capital cannot exceed subscribed capital.*
- (b) *In case of oversubscription, when applications are received for more number of shares than the number of shares offered for subscription, the excess applications are either rejected or the surplus amount of excess shares applied is adjusted on future installments, but subscribed capital is not said to be more than the issued capital.*
- (c) *An amount of authorised, issued and subscribed capital is calculated on the full face value of shares, whereas called up and paid up capitals are calculated on the basis of that part of the face value which has been actually called by the company till date.*

ARTICLES OF ASSOCIATION

Articles of Association are the rules regarding the internal management of a company. The rules stated in this document should not contradict and exceed the limit prescribed in the Memorandum of Association. It is a subsidiary document to M.O.A. This document lays down rules and regulations for the attainment of objects stated in the M.O.A.

As per section 2 and sub-section 5 of Companies Act, 2013, “articles means the articles of association of a company as originally framed or as altered from time to time or applied in pursuance of any previous company law or of this Act”.

Note: A public limited company may either prepare its own Articles of Association or may adopt its respective table, wholly or partly, such as ‘Table F, G, H, I or J’, depending upon the nature of company.

Main Contents of Articles of Association

1. The amount of share capital and types of classes of shares.
2. Procedure for allotment of shares.
3. Procedure for transfer of shares.
4. Procedure for conversion of shares into stock.
5. Procedure of conducting the meetings.
6. Duties, power and remuneration of the directors.
7. Procedure for appointment and removal of the directors.
8. Procedure for declaration of the dividend.

9. Seal of the company.
10. Procedure for the winding of the company.

DIFFERENCE BETWEEN MEMORANDUM OF ASSOCIATION AND ARTICLES OF ASSOCIATION

Basis	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 a subordinate to the Companies Act, 2013.	This is a subsidiary document and is a 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 Limited Company to file Articles of Association. It may adopt its respective Table F to J of the Companies Act, 2013.
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.

RESPECTIVE FORMS FOR MEMORANDUM OF ASSOCIATION AND ARTICLES OF ASSOCIATION

S.No.	Table No.	Description
1.	Table A	MOA of a company limited by shares
2.	Table B	MOA of a company limited by guarantee and not having share capital
3.	Table C	MOA of a company limited by guarantee and having share capital
4.	Table D	MOA of an unlimited company and not having share capital
5.	Table E	MOA of an unlimited company and having share capital
6.	Table F	AOA of a company limited by shares
7.	Table G	AOA of a company limited by guarantee and having share capital
8.	Table H	AOA of a company limited by guarantee and not having share capital
9.	Table I	AOA of an unlimited company and having a share capital
10.	Table J	AOA of an unlimited company and not having share capital

Note: The above respective forms have been given in the Schedule I of the Companies Act 2013.

PROSPECTUS

It is a document including any notice, circular, advertisement or any other document which invites the investors to invest their savings in a company to make deposits, subscribe for shares and securities.

It acts as medium of advertisement to inform about the past, present and future of a company, induces and protects the interests of the prospective investors to make investments, acts as an authentic record of the terms and conditions.

Main Contents of the Prospectus

1. Name and address of the registered office of the company.
2. Opening and closing date of the issue.
3. Name and addresses of the key persons like directors, promoters, chartered accountants, company secretaries, trustees, auditors, bankers, etc.
4. Qualification shares held by the directors.
5. Provisions relating to remuneration of the directors.
6. Capital and capital structure in form of different classes of shares.
7. Amount of minimum subscription.
8. Name of underwriters.
9. Financial information.
10. Main objects and other objects of the company.

STARTING A BUSINESS — BASIC FACTORS THAT INFLUENCE THE CHOICE OF FORM OF BUSINESS ORGANISATION

Running any business is not so much difficult as the business adapts itself to the business environment and learns from it how to cope with the threats and grab the opportunities but when a business is started, a list of problems have to be anticipated and solutions are derived. Following are the some of the factors to be kept in mind while starting a business:

1. Selection of Line of Business. Any business requires some amount of basic knowledge and experience. The owner needs to be aware about the business he intends to start. Knowledge and expertise about the product or service are the key elements for a successful business. In case of limited knowledge, the owner may not be able to sustain the business.

The line of business should be such which can easily be undertaken and is feasible to continue. Like construction and software industry would require expert knowledge whereas the retail business in clothing or shoes can easily be started.

2. Size of the Firm. If the product line is consumer goods, it is likely to have moderate or low demand, small amount of capital will be needed but if the product line is the capital goods with huge demand, large amount of capital will be required. In the former case sole proprietorship and partnership business will be suitable whereas in the latter case, company form of organisation will be more suitable.

3. Choice of Form of Ownership. Where the small amount of capital is required, sole proprietorship business or partnership business may be started but if the business is planned to be started on a large scale, company form of organisation would be suitable. It should also be noted that the liability of the owners in case of sole proprietorship and partnership is unlimited and limited in case of company form of organisation.

4. Location of the Business Enterprise. A good location goes a long way in making the business successful. It should be where the raw materials can be easily sourced, the manpower would be easily available and we can save out on transportation costs. Setting up a business in certain location could lead to subsidy and rebates from the government too.

In the case of a retail business (for consumer goods), one needs to be located in a well populated area and one which is easily accessible whereas in case of industrial goods (capital goods), industry should be located in the industrial area.

5. Financing of Proposition. The financing pattern will be mainly by the way of capital introduction by the owner and borrowed funds. The terms and conditions for borrowing funds will need to be studied such as the cost of borrowing, security required, rate of interest and the repayment terms.

Funds arranged through capital and long-term loans must be utilised in procuring fixed assets whereas short-term funds should be utilised in the working capital requirements. The logic is that if short-term funds are used to purchase fixed assets, then the repayment of short term loan will be difficult if the business does not progress.

6. Physical Facilities. Availability of physical facilities in the form of tangible assets like land, plant, machineries, raw materials, aids to trade are very important. The decision relating to this factor will depend on the nature and size of business, availability of funds and the process of production.

7. Plant layout: After the arrangement of physical assets has been determined, the entrepreneur has to decide how to arrange the machines and equipment on the land and premises available so that goods can be manufactured without any inconvenience and interruption.

8. Competent and committed work force: It's only the human resource that converts the physical resources into desired product and services. The entrepreneur has to search the best skilled, unskilled and managerial workforce available in the industry and provide the best possible wages, salaries and facilities.

9. Tax planning: An entrepreneur has the responsibility to comply with the prevailing laws of the country which affect the growth of the business and income of the nation. Under the Start-up India programme, the government has given several tax benefits to the new start-ups. At present, the new entrepreneurs have been given exemption from tax for 3 years out of the block of 7 years and easy exit (legal procedure) to wind up their operations.

10. Launching the enterprise: After completing the above courses of action, gathering all necessary resources, the entrepreneur can go ahead to start the production, campaign the product and launch the enterprise.

GLIMPSES

- **Sole Proprietorship.** It is a business which is controlled and managed by a single person who invests money in the form of capital, receives profits and bears all losses.

(a) Features of Sole Proprietorship

- Formation and Closure
- Liability
- Sole Risk Bearer and Profit Recipient
- One-man Control
- No Separate Entity
- Lack of Business Continuity

(b) Merits of Sole Proprietorship

- Quick Decision Making
- Confidentiality of Information
- Direct Incentive
- Sense of Accomplishment
- Ease in Formation and Closure

(c) Limitations of Sole Proprietorship

- Limited Resources
- Limited Life of a Business Concern
- Unlimited Liability
- Limited Managerial Ability

- **Hindu Undivided Family Business.** It is a kind of family business which is run and controlled by the eldest male person of such business and the rest of male members are known as coparceners.

(a) Features of HUF

- Formation
- Liability
- Control
- Continuity
- Minor Members

(b) Merits of HUF

- Effective Control
- Continued Business Existence
- Limited Liability of Members
- Increased Loyalty and Cooperation

(c) Limitations of HUF

- Limited Resources
- Unlimited Liability of Karta
- Dominance of Karta
- Limited Managerial Skills

- **Partnership.** It is a relationship between two or more persons who have agreed to share the profits of a business carried on by all or any one of them acting for all.

(a) Features of Partnership

- Formation
- Liability
- Risk Bearing
- Decision Making and Control
- Membership
- Mutual Agency

(b) Merits of Partnership

- Ease of Formation and Closure
- Balanced Decision Making
- More Funds
- Sharing of Risks
- Secrecy

(c) Limitations of Partnership

- Unlimited Liability
- Limited Resources
- Possibility of Conflicts
- Lack of Continuity
- Lack of Public Confidence

(d) Types of Partners

- **Active/Ostensible Partner.** A partner who contributes capital, takes active part in the business affairs, has unlimited liability and shares profits and losses of the business.
- **Sleeping or Dormant Partner.** A partner who contributes capital, shares the profits and losses, has unlimited liability but does not take part in the day-to-day activities of the business.

- **Secret Partner.** A partner who contributes capital, shares profits and losses, takes active part in the management, has unlimited liability but the identity of such partner is kept hidden.
 - **Nominal Partner.** A partner who allows his name to be used in the business, does not contribute any capital, share no profit and loss, does not take active part in management but assumes unlimited liability.
 - **Partner by Estoppel.** A partner who conducts himself as a partner in a firm though he is not a partner in a firm in reality becomes liable for the debts of the firm with unlimited liability.
 - **Partner by Holding Out.** A person who is exposed to be a partner in a firm before the outsiders and does not react and becomes liable with unlimited liability.
 - **Minor Partner.** A partner who has not attained the age of 18 years is taken as a partner for the benefits of a firm and shares only profits.
- (e) **Types of Partnership**
- **Partnership at Will.** A partnership which can be terminated by giving notice by any partner to the firm.
 - **Particular Partnership.** A partnership which is formed for a particular purpose and on the achievement of such purpose, it ends itself.
 - **General Partnership.** An ordinary partnership wherein the liability of each partner is unlimited, every partner shares profits and losses, participates in the management and the acts of the all partners are binding on one another.
 - **Limited Partnership.** It is a kind of partnership in which liability of at least one partner is unlimited whereas the liability of other partners is limited.
- **Limited Liability Partnership (LLP).** It is a partnership firm like corporate body, artificial person, with separate legal existence, perpetual succession, wherein partners can be individual or corporate body or both with at least two designated partners.
 - **Partnership Deed.** It is a document containing terms and conditions mutually agreed upon by all partners in a firm to avoid all possible disputes which may arise in future.
- **Cooperative Society.** “The cooperative society is a voluntary association of persons who join together with common, social, cultural and economic interest through the principles of self and mutual help.”
 - (a) **Features of Cooperative Society**
 - Voluntary Membership
 - Separate Legal Existence
 - Limited Liability
 - Control
 - Service Motive
 - (b) **Merits of Cooperative Society**
 - Equal Voting Rights
 - Limited Liability
 - Stable Existence
 - Economy in Operation
 - Support/Patronage from Government
 - Ease of Formation
 - (c) **Limitations of Cooperative Society**
 - Limited Resources
 - Inefficiency in Management
 - Lack of Secrecy
 - Government Control
 - Differences in Opinions

(d) **Types of Cooperative Societies**

- **Consumers' Cooperative Societies.** Such societies buy goods directly from the manufacturers and provide them to the members at reasonable cost by eliminating the middlemen.
- **Producers Cooperative Societies.** Such societies buy basic materials and inputs directly from the suppliers, provide them to the members at cost and sell their finished output in the market.
- **Marketing Cooperative Society.** Such societies collect the finished output from the members and sell them in the market. Profits earned are distributed among the members on the basis of their output.
- **Farmer's Cooperative Societies.** Such societies buy basic inputs from the market required for cultivation by the farmers and provide them at low cost.
- **Credit Cooperative Societies.** Such societies are formed to provide credit or loans to its members at a low rate of interest than the prevailing rate of interest.
- **Cooperative Housing Societies.** Such societies collect money from the members and construct housing accommodation at their own, eliminate middlemen and provide such accommodation at cost to the members.
- **Joint Stock Company.** "A company can be described as an artificial person having a separate legal personality, perpetual succession and common seal."
 - (a) **Features of a Joint Stock Company**
 - Artificial Person
 - Separate Legal Entity

- Formation
- Perpetual Succession
- Control
- Liability
- Common Seal
- Risk Bearing

(b) **Merits of a Joint Stock Company**

- Limited Liability
- Transfer of Interest
- Perpetual Existence/Succession
- Scope for Expansion
- Professional Management

(c) **Limitations of Joint Stock Company**

- Complexity in Formation
- Lack of Secrecy
- Impersonal Work Environment
- Numerous Regulations
- Delay in Decision Making
- Oligarchic Management
- Conflicts in Interests

(d) **Private Limited Company:** A company which is not authorised to invite the general public to subscribe for any securities, has a minimum of two members but maximum not exceeding two hundred and uses the words 'private limited' after its name is called a Private Limited Company.

(e) **Public Limited Company:** A company which is not a private limited company is authorised to invite general public to subscribe for its securities, has a minimum of two members but there is no limit on maximum members and uses the words 'Public Limited' after its name.

(f) **One Person Company:** One Person Company (OPC) is a company which has only one person as member and the purpose of which is

to encourage a sole proprietor expand his/her business with limited liability.

- **Formation of a Company**

(a) **Promotion:** “Promotion involves identification of a business opportunity or idea, analysis of its prospects and taking steps to implement it through the formation of a company.”

(b) “A **promoter** is said to be the one who identifies a business opportunity, idea, analyses its prospects and takes steps to implement it through the formation of a company.”

(c) **Functions of Promoters**

- Identification of Business Opportunity
- Feasibility Studies
 - Technical Feasibility
 - Financial Feasibility
 - Economic Feasibility
- Name Approval
- Fixing up of Signatories
- Appointment of Professionals
- Preparation of necessary Documents

(d) **Documents Needed for Incorporation**

- Memorandum of Association
- Articles of Association
- Consent of the Proposed Directors
- Agreement
- Statutory Declaration
- Payment of Fee

(e) **Capital Subscription**

- Approval from SEBI
- Filing of Prospectus
- Appointment of Bankers, Brokers and Underwriters

- Minimum Subscription
- Application to Stock Exchange
- Allotment of Shares

(f) **Memorandum of Association.** It is the fundamental document which defines its objectives and powers beyond which a company is not legally permitted to undertake activities

- Name Clause
- Registered Office Clause
- Objects Clause
- Liability Clause
- Capital Clause
- Association or Subscription Clause

(g) **Articles of Association.** Articles of Association are the rules regarding the internal management of a company. The rules stated in this document should not contradict and exceed the limits prescribed in the Memorandum of Association.

(h) **Prospectus.:** It is a document including any notice, circular, advertisement or any other document which invites the investors to invest their savings in a company to make deposits, subscribe for shares and securities.

(i) **Starting a Business - Basic Factors**

- Selection of line of business.
- Size of the firm.
- Choice of form or ownership.
- Location of the business enterprise.
- Financing of proposition.
- Physical Facilities
- Plant Layout
- Competent and Committed work force
- Tax Planning
- Launching the Enterprise

OBJECTIVE TYPE QUESTIONS

MULTIPLE CHOICE QUESTIONS (MCQs)

- The structure in which there is separation of ownership and management is called:
(a) Sole Proprietorship (b) Partnership
(c) Company (d) All Business Organisations
- The Karta in Joint Hindu family business has:
(a) Limited liability (b) Unlimited liability
(c) No liability for debts (d) Joint liability
- In the cooperative society the principle followed is:
(a) One share one vote (b) One man one vote
(c) No vote (d) Multiple votes
- The board of directors of a Joint Stock Company are elected by:
(a) General public (b) Governments bodies
(c) Shareholders (d) Employees
- The maximum number of partners allowed in the partnership business are:
(a) Twenty (b) Ten
(c) Fifty (d) Two
- Profits do not have to be shared. This statement refers to:
(a) Partnership (b) Joint Hindu Family Business
(c) Sole Proprietorship (d) Company
- The capital of a company is divided into number of parts, each one is called:
(a) Dividend (b) Profit
(c) Interest (d) Share
- The head of Joint Undivided Business is called:
(a) Proprietor (b) Director
(c) Karta/Manager (d) Owner
- Provision of residential accommodation to the members at reasonable rates is the objective of:
(a) Producers' Cooperative (b) Consumer's Cooperative
(c) Housing Cooperative (d) Credit Cooperative
- A partner whose association with the firm is unknown to the general public called:
(a) Active partner (b) Sleeping partner
(c) Nominal partner (d) Secret partner
- Minimum number of members to form a private company is
(a) 2 (b) 3
(c) 5 (d) 71
- Minimum number of members to form a public company is
(a) 5 (b) 7
(c) 12 (d) 21

13. 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 state in which company is to be registered.
14. A proposed name of the 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 above
15. 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
16. Stages in the formation of a public company are in the following order:
 - (a) Promotion, commencement of business, capital subscription, incorporation
 - (b) Incorporation, capital subscription, promotion
 - (c) Promotion, incorporation, capital subscription
 - (d) Capital subscription, promotion, incorporation.
17. 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.
18. 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

ANSWERS

- | | | | | | | | | | |
|---------|---------|---------|---------|---------|---------|---------|---------|--------|---------|
| 1. (c) | 2. (b) | 3. (b) | 4. (c) | 5. (c) | 6. (c) | 7. (d) | 8. (c) | 9. (c) | 10. (d) |
| 11. (a) | 12. (b) | 13. (b) | 14. (d) | 15. (b) | 16. (c) | 17. (a) | 18. (b) | | |

FILL IN THE BLANKS WITH CORRECT WORDS

1. _____ partner is admitted to partnership for profits only.
2. The maximum number of partners at present in a firm cannot exceed _____ .
3. Active partner is also known as _____ partner.
4. Partner by _____ styles the character of a partner by words, initiative, conduct or behaviour in front of any outsider.

5. LLP runs as per LLP Act, _____ whereas General partnership runs as per Partnership Act, _____ .
6. Mutual agency relationship does not exist in case of _____ partnership.
7. The cooperative society is a _____ association of persons who join together with common social cultural and economic interest.
8. Cooperative society can be formed with minimum _____ members whereas a public limited company can be formed with _____ members.
9. _____ an artificial person which is created by law and the only law can end it.
10. A company gets its birth and comes into legal existence as an artificial person after getting certificate of _____ .
11. The existence of a _____ is not affected by admission, death, lunacy or insolvency of its shareholders or directors.
12. _____ signifies the signature of a company.
13. _____ is a form of power structure in which power effectively rests with a small number of people.
14. There should be atleast minimum _____ members and _____ directors in a private limited company.
15. Minimum authorised share capital required for an OPC is rupees _____ and it cannot exceed rupees _____ .
16. A private limited company can start its business after first two _____ stages of formation of a company.
17. _____ shares are the number of shares which a director may have to subscribe as per the provisions stated in the Articles of Association.
18. Memorandum of a company is also called _____ of the company.
19. The contracts which are entered by the promoters of the company before it gets certificate of incorporation is issued are known as _____.
20. _____ is the amount which, in the opinion of directors, must be sufficient to meet the needs of the business operations of the company.

ANSWERS

1. Minor	2. 50	3. Ostensible
4. Estoppel	5. 2008, 1932	6. Limited liability
7. Voluntary	8. 10; 7	9. Company
10. Incorporation	11. Company	12. Common seal
13. Oligarchy	14. 2; 2	15. One lac; fifty lacs
16. Two	17. Qualification	18. Charter
19. Preliminary Contracts	20. Minimum subscription	

STATE WHETHER THE FOLLOWING STATEMENTS ARE TRUE OR FALSE

1. Karta in the Joint Hindu Undivided Family can also be a female member.
2. Liability of partners is unlimited in case of general partnership whereas it is limited in case of Limited Liability Partnership.

3. Limited partnership is different from limited liability partnership.
4. The existence of the limited liability partnership firm gets affected with the entry or exit of a partner.
5. Every partner in a agent of LLP but not of other partners.
6. Creditors can file a case to recover their dues even if the firm is unregistered.
7. One man one vote is the slogan of cooperative number of societies.
8. The company can file a suit against its members and its members can also sue the company.
9. Underwriters are expert persons who undertake the responsibility to form the companies.
10. The maximum number of directors in case of OPC is 15.
11. The minimum directors in a public limited company, private limited company and an OPC are _____ , _____ and _____ respectively.
12. The company law is silent on the minimum authorised capital in case of public limited company as well as private limited company.
13. The first directors of a company are also called _____ to the MOA.
14. Existence of the company cannot be challenged even if the company has been incorporated with illegal objects.
15. Provisions of Companies Act are followed to alter Memorandum of Association whereas Articles of Association can be altered with special resolution of members.

ANSWERS

- | | | | | | | | | | |
|----------------------|------|------|-------|-----------------|------|-------|-------|------|-------|
| 1. T | 2. T | 3. T | 4. F | 5. T | 6. T | 7. T | 8. T | 9. F | 10. T |
| 11. Three, two & one | | | 12. T | 13. Signatories | | 14. T | 15. T | | |

REMEMBERING AND UNDERSTANDING QUESTIONS

VERY SHORT ANSWER TYPE QUESTIONS

(1 MARK)

1. Varun is the sole owner of his restaurant. Name the form of business organisation run by him.
Ans. Sole proprietorship.
2. Name the form of organisation which is found only in India.
Ans. Joint Hindu Undivided Family Business
3. Which type of organisation is a one man show?
Ans. Sole proprietorship.
4. Name the organisation where the liability of the owners is limited to the outsiders.
Ans. Cooperative Organisations and Joint Stock Company.
5. Are ownership and control separate for the owner in sole proprietorship business?
Ans. No, both are a single entity for the owner in sole proprietorship business.
6. List two merits of sole proprietorship business.
Ans. (i) Single ownership (ii) Full control.

7. Is female entitled to participate in the functioning of HUF?
Ans. Yes, she is entitled to participate in the functioning of HUF.
8. By what name are the members known as in case of HUF?
Ans. Coparceners.
9. Name any one business in which sole proprietorship is most suitable.
Ans. Tailoring.
10. State any two advantages of partnership firm.
Ans. (a) Balanced decision-making (b) Mutual agency relationship
11. What is the head of the family known as in HUF?
Ans. Karta
12. Name the type of partnership which is formed to accomplish a specific project for a specific time.
Ans. Particular partnership
13. Which bill entitles women to have equal share in ancestral property of HUF?
Ans. Hindu Succession (amendment) Bill, 2005.
14. State any one consequence of non-registration of a partnership firm.
Ans. An unregistered firm cannot file a case against third parties.
15. Who has unlimited liability in the HUF business?
Ans. The Karta has the unlimited liability in the HUF business.
16. Which Act of law governs the functioning of partnership business in general?
Ans. Partnership Act, 1932 governs the functioning of partnership business.
17. Which Act of law governs the functioning of a Joint Stock Company?
Ans. Companies Act, 2013 governs the functioning of a Joint Stock Company.
18. What does 'mutual help' mean in the context of cooperative society?
Ans. Mutual help means each for one and all for each.
19. What is the other name given to an active partner?
Ans. Ostensible Partner.
20. What another name is given to a sleeping partner?
Ans. Dormant Partner.
21. Name the type of company which can invite the public to subscribe for the shares or debentures.
Ans. A Public company limited by shares can invite the public to subscribe for its shares or debentures.
22. Can a minor partner enter into legal contracts?
Ans. No, a minor partner cannot enter into any legal contracts.
23. What is the position of liability of a minor partner towards outsiders?
Ans. The position of liability of a minor partner towards outsiders is limited to the extent of his capital contribution and share in undistributed profit.
24. Name the process by which a joint stock company is registered.
Ans. Incorporation is the process by which a joint stock company is registered.
25. Can a minor partner bear the losses in the partnership firm?
Ans. No, a minor partner cannot bear the losses in the partnership firm.

26. Name the type of partnership under which a partnership can come to an end by giving a mere notice by a partner to the firm.
Ans. Partnership at will.
27. What is the full form of LLP?
Ans. Limited Liability Partnership
28. State any two common features of a company and a LLP.
Ans. (a) Artificial Person (b) Perpetual Succession
29. What document is used in case a company parallel is to partnership deed?
Ans. Article of Association.
30. Name the document which defines the object and powers of the company.
Ans. Memorandum of Association.
31. Is Partnership Act, 1932 applicable to the LLP?
Ans. No, Partnership Act, 1932 is not applicable to the LLP.
32. Which Act is applicable to an LLP?
Ans. Limited Liability Partnership, Act 2008 is applicable to an LLP.
33. Which document is important to settle and avoid all possible disputes among partners?
Ans. Partnership Deed.
34. Is registration of a partnership firm compulsory?
Ans. No, registration of a partnership firm is not compulsory.
35. Which Act of law governs the functioning of cooperative societies?
Ans. Co-operative Societies Act, 1912 governs the functioning of cooperative societies.
36. How many minimum numbers of persons are required to form a cooperative society?
Ans. Ten.
37. How much amount of profit is transferred to the statutory reserve in case of cooperative society?
Ans. One fourth of the total profit.
38. Is cooperative society separate from its members?
Ans. Yes, cooperative society is separate from its members.
39. What is the liability of a member in a cooperative society?
Ans. Limited to the extent of capital contribution and share in the undistributed profits, if any.
40. Who controls the functioning of a cooperative society?
Ans. The elected members control the functioning of a cooperative society.
41. Which document as necessary for incorporation, has to be adapted from companies act?
Ans. Memorandum of Association.
42. What are the maximum number of members in a private limited company?
Ans. 200 members.
43. What does OPC stand for?
Ans. It stands for One Person Company.
44. What is the basic difference between sole proprietorship and OPC?
Ans. Liability of sole proprietor is unlimited in case of sole proprietorship whereas it is limited for the owner of OPC.

SHORT ANSWER TYPE QUESTIONS

(3–4 MARKS)

1. “One man control is the best in the world if that man is big enough to manage everything.” Explain.

Ans. The above statement refers to the advantages of sole proprietorship which are as follows:
Refer: Advantages and Disadvantages of sole proprietorship.

2. How can a Joint stock company being an artificial person sign any official documents? Explain with the help of an example.

Ans. The documents of a company are signed with the help of a common seal.

Common seal: Since a company is an artificial person, it cannot put its signature on any document. Therefore, it is statutory for every company to have a seal on which the name of the company is engraved. Affixing of seal on any document signifies the signature of the company.

Example: A purchase manager may enter into a contract for buying raw materials from a supplier. Once the contract paper is sealed (stamped in the name of company) and signed by the purchase manager, it becomes valid. The purchase manager may leave the company thereafter or may be removed from the job or may have taken a wrong decision, yet for all purposes the contract is valid till a new contract is made or the existing contract expires.

Note: *With the introduction of companies Act, 2013, use of common seal is now optional. Refer features of a company.*

3. When is a company said to be a private limited company?

Ans. A company is said to be a private limited company if:

- it has restricted the right to transfer its shares, if any.
- it has limited the number of its members to 200.
- it has at least two directors.
- it has prohibited any invitation to the public to subscribe for any shares, or debentures of the company.
- it has prohibited any invitation or acceptance of deposits from persons other than its members, directors or their relatives
- it uses the word ‘Private Limited’ after its name.

4. State the reasons for issuing prospectus.

Ans. Reasons for issuing prospectus:

- It serves as an invitation to the public to invest in the shares and debentures of the company.
- It acts as an advertisement for inducing the investors to invest in the company.
- It serves as a record of the terms and conditions on which shares and debentures are issued.

ANALYSIS BASED QUESTIONS

VERY SHORT ANSWER TYPE QUESTIONS

1. Name the organisation which is run, controlled and managed by a single person.

Ans. Sole Proprietorship.

2. Who becomes the next 'Karta' in the event of death of the existing Karta in a H.U.F. business?
- Ans.** The most eldest male member next to the existing Karta.
3. Who are known as coparceners?
- Ans.** All male members except the Karta are known as coparceners.
4. Name the systems which exist in the H.U.F. business.
- Ans.** (a) Dayabhaga System
(b) Mitakshra System.
5. Which system of H.U.F. prevails in the West Bengal?
- Ans.** Dayabhaga System.
6. Name the system of H.U.F. in which both male and female can be members.
- Ans.** Dayabhaga System.
7. Can a minor child be called as a member in H.U.F. business system?
- Ans.** Yes, every child becomes a member in the H.U.F. by birth.
8. Which feature of the partnership binds all partners to the agreement signed by one partner on the behalf of others?
- Ans.** Mutual Agency.
9. There is no compulsion for a partnership to be registered, still the partners prefer to get it registered, why?
- Ans.** The partners prefer to get the firms registered due to the following advantages:
Hint: Write the benefits of registration.
10. Can a minor person be admitted as a partner in a firm?
- Ans.** Yes, a minor child can be admitted as a partner in a partnership business to share profits only.
11. Does a minor partner also assume unlimited liability in the business like other partners?
- Ans.** No, his liability is limited to the extent of share in the capital plus net of undistributed profits.
12. Can a minor partner take part in the activities of management of the partnership business?
- Ans.** No, he is not authorised to take part in the management in the partnership firms.
13. Though a minor partner is not authorised to interact with the management on the issues of partnership firms, can he inspect the books of accounts?
- Ans.** Yes, he can inspect the books of accounts.
14. Name the organisation which is run by the mutual cooperation for social and economic benefit of the members.
- Ans.** Cooperative Society.
15. Name the Act which governs the activities of a cooperative society.
- Ans.** Indian Cooperative Society Act, 1912.
16. Can a member enjoy maximum rights in the cooperative society by holding maximum number shares?
- Ans.** No, every member carries a single vote irrespective of the number of shares held by him/her.
17. Name the common features between a cooperative society and a joint stock company.
- Ans.** (a) Separate Legal Personality; (b) Perpetual Succession.

18. “During the Annual General Meeting of a company, all the shareholders died due to an earthquake.” Do you think the company also died with the death of the shareholders?
- Ans.** No, a company is an organisation which is created by Law and only the Law can end its existence even if there is not a single owner (shareholder) alive in a company.
19. Name the person who brings a joint stock company into existence.
- Ans.** Promoter.
20. ‘It is a document which contains objectives and powers of a company.’ Name such document.
- Ans.** Memorandum of Association.
21. ‘It contains internal rules and regulations of a company.’ Name the document.
- Ans.** Articles of Association.
22. What is essential to obtain to become a director in a company?
- Ans.** Director Identification Number (DIN).
23. What is the minimum limit for raising money through issuing shares?
- Ans.** Certain percentage of the issued capital as stated in the prospectus must be received at the time of raising funds by issuing shares by a company. Generally companies mention 90% of the issued capital as minimum subscription in their prospectus.
24. How is a sole proprietorship business different from one person company as entities?
- Ans.** Sole proprietorship form of business has no separate legal entity whereas OPC enjoys separate legal entity from its member (owner).
25. Name the essential document required for incorporation, which may be adapted from the Companies Act.
- Ans.** Articles of Association.
26. Which document is used to invite the general public to apply for the shares and securities?
- Ans.** Prospectus.
27. What are the directors called who sign the important documents in the formation of a company?
- Ans.** Signatories.
28. How many signatories are required to sign the main documents of a public limited company?
- Ans.** Seven.

SHORT ANSWER TYPE QUESTIONS

1. “One man control is best in the world if that man is big enough to manage everything.” What does this statement signify?
- Ans.** This statement tells about the advantages of the sole proprietorship and it is best in the world because:
- The business is run and controlled by a single person.
 - Proprietor is not required to share his profits and losses.
 - Proprietor does not receive any interference in his business.
 - Proprietor is not required to get his business registered in the eyes of law.
 - Proprietor is not required to disclose his accounts to the public.

2. If a sole proprietorship wishes to expand his business, how can he do so? Give three possible alternatives.

Ans. He can either:

- (a) Appoint manager or assistant.
 - (b) Approach financial institution run by the government meant for small-scale industries.
 - (c) Appoint any partner and convert his sole proprietorship business into partnership.
3. How can you identify an organisation form of a company whether it is limited company or a private limited company on the basis of:

- (a) Name
- (b) Members
- (c) Directors

Ans. A company can be identified with the help of the following information:

Basis	For a Limited Company	For a Private Limited Company
(a) Name	Name must end with the word "Ltd."	Name must end with the word "Private Limited".
(b) Members	It must have minimum 7 members.	It must have minimum 2 members.
(c) Directors	It must have 2 directors.	It must have minimum 3 directors.

4. In which form of organisation is a trade agreement made by one owner binding on the others? Give reasons to support your answer.

Ans. Partnerships form of organisation is an organisation in which a trade agreement made by one owner is binding on the other.

Reason: The mutual agency relationship among the members is the reason. Due to such relationship, every partner is a principal as well as an agent. The acts of one partner as a principal will be binding on the partner(s) as agent(s) and vice-versa.

5. The business assets of an organisation amount to ₹ 50,000 but the debts remain unpaid are ₹ 80,000. What course of action can the creditors take if:

- (a) The organisation is a sole proprietorship firm.
- (b) The organisation is a partnership firm with Anthony and Akber as partners. Which of the two partners can the creditors approach for repayment of debts? Explain giving reasons.

Ans. (a) In case of sole proprietorship, the personal assets can be used to pay the debts of the business if the funds on the sale of the assets of the business are not sufficient to pay the debts of the business.

- (b) Both partners (otherwise all partners) in the present case are responsible for the payment of the debts. Both of them will have to bring the loss of the firm from their personal assets in the agreed ratio as specified in the agreement or in the capital ratio (refer Garner Vs. Murrar Case). If one partner becomes insolvent (it means he cannot bring debit balance in his capital account in the business), the other partner will have to bring for the loss in the business out of his personal assets. If all the partners become insolvent, the creditors will have to bear the loss.

LONG ANSWER TYPE QUESTIONS

1. Name the type of partnership in the following cases:

- (a) A type of partnership business which ends itself on the completion of a project for which it was established.

- (b) The partnership which may be ended by giving a notice by any partner.
- (c) The partnership in which every partner has unlimited liability, every partner shares profits and losses, take active part in the management.
- (d) The partnership in which at least one partner has unlimited liability and rest of the partners have limited liability.
- (e) The partnership which runs on the principles of a joint stock company.

Ans. (a) Particular Partnership, (b) Partnership at Will, (c) General Partnership; (d) Limited Partnership; (e) Limited Liability Partnership.

2. Name the following:

- (a) A person who lends his name for the benefits of a firm.
- (b) A person who contributes capital, shares profits and losses, assumes unlimited liability but does not take active part in the day-to-day activities of the business.
- (c) A person whose name is not disclosed to the outside world but he works like other partners.
- (d) A person who styles himself as a partner though he is not a partner in the business.
- (e) A person whose name is used as a partner, though he is not a partner, by the partners in a firm and he does not object over their claim.

Ans. (a) Nominal Partner, (b) Dormant or Sleeping Partner, (c) Secret Partner, (d) Partner by Estoppel, (e) Partner by Holding Out.

3. Name the society in the following situations:

- (a) A society which buys goods directly from the wholesalers or manufactures to eliminate the role of middlemen and provide them to members at the most reasonable cost.
- (b) A society which buys the inputs for its members in bulk from the market and provide to its members at reasonable cost.
- (c) A society which pools the output of individual members and performs marketing functions.
- (d) A society which aims to gain the benefits of large-scale farming and increase the productivity of agriculture.
- (e) A society which is formed to protect the members from the exploitation of lenders who charge high rates of interest on loans.
- (f) A society which is established to help people with limited income to construct houses at reasonable costs.

Ans. (a) Consumer's Cooperative Society; (b) Producers' Cooperative Society; (c) Marketing Cooperative Society; (d) Farmer's Cooperative Society; (e) Farmers' Cooperative Society; (f) Cooperative Housing Society.

4. In case a business comes to end, can the creditors claim for the recovery from the personal assets of the owners if such business organisation is:

- | | |
|-------------------------------------|----------------------------------|
| (a) Sole Proprietorship | (b) General Partnership Firm |
| (c) Hindu Undivided Family Business | (d) Cooperative Society Business |
| (e) Company | |

Ans.

Type of Business	Liability	Whether personal assets can be used to pay the liabilities of the business?
(a) Sole proprietorship	Unlimited	Yes.
(b) General Partnership firm	Unlimited	Yes.
(c) H.U.F.	Unlimited of the Karta. Limited for Coparceners.	Yes, the assets of <i>Karta</i> only.
(d) Co-operative Societies	Limited to the extent the share in the capital plus surplus profit of the members.	No.
(e) Joint Stock Company Limited Liability Partnership/O.P.C.	Limited to the extent the share in the capital plus surplus profit of the shareholders.	No.

APPLYING AND EVALUATION BASED QUESTIONS (CASE PROBLEMS)

VERY SHORT ANSWER TYPE QUESTIONS

1. In which form of organisation is a trade agreement made by one owner binding on the others? Give reasons to support your answer. (NCERT)

Ans. General Partnership Firm.

Reason: Mutual Agency Relationship but it is not applicable in case of LLP where each partner is the agent of LLP but not of other partners.

Note: As per the definition of partnership laid in the Partnership Act, 1932, “partnership is the relation between persons who have agreed to share the profits of the business carried by all or any one of them acting for all”. Every partner plays double role as an agent as well as principal at the same time. A trade agreement made by a partner is binding on the other partner(s). The acting partner is treated as agent and other(s) is/ are treated as principal and vice-versa.

2. Sameer and Harish are two partners in a partnership firm. Karan is a good friend of Sameer and Namit, who is a well-known rich person. The firm is looking for a lender for the financial requirements of their firm. In a social gathering, Karan impresses Mr. Namit on the financial soundness and growth prospects of the firm. Namit gets impressed with his words and grants loan to the firm.

What type of partner is Mr Karan in the firm? State his liability.

Ans. Mr Karan is a partner by estoppel and he shall remain personally responsible to repay the debt to Namit if the firm fails to repay such debt.

3. Rajan used to sell his products with the help of the selling agents who charged high commission. He formed a cooperative society to pool the output of member producers to sell directly in the market at the best possible price.

Name the cooperative society so formed.

Ans. Marketing cooperative society.

4. Neelima got her pension commuted (lump-sum amount) from her former employer after retirement. Her uncle advised her to invest the sum in the shares. She was unwilling to invest her hard earned income in shares as she knew that her funds would remain blocked permanently with the company till it is liquidated.

State with reason the merit of shares remain unknown to Neelima.

Ans. Merit associated: Transferability of shares.

Reason: She can invest in shares as she can sell the shares in the stock market whenever she needs to liquidate the shares into cash.

5. In 2008, The government of India permitted corporate form of partnership business that provides an alternative to the traditional partnership which exposes its partners to unlimited personal liability.

Name such corporate form of partnership business.

Ans. Limited Liability Partnership.

SHORT ANSWER TYPE QUESTIONS

1. The business assets of an organisation amount to ₹ 50,000 but the debts that remain unpaid are ₹ 80,000. What course of action can the creditors take if:
- The organisation is a sole proprietorship firm.
 - The organisation is a partnership firm with Anthony and Akbar as partners. Which of the two partners can the creditors approach for repayment of debt? Explain giving reasons.
 - The organisation is an LLP with Anthony and Akbar as partners. Which of the two partners can the creditors approach for repayment of debt? Explain giving reasons.

(NCERT, modified)

- Ans.**
- In case of sole proprietorship:** In case of sole proprietorship form of organisation, the proprietor has unlimited liability towards the debts of the business. In the present case, the business funds of ₹ 50,000 can be used to pay the liabilities of the business. The sole proprietor is responsible to bring ₹ 30,000 from his private estates to cover up the deficiency of funds.
 - In case of partnership firm:** In case of general partnership (except Limited Liability Partnership), each partner suffers from the limitation of unlimited liability. Both partners are personally responsible to bring Rs. 30,000 from their private estates in the ratio agreed between them (if already decided in the partnership deed) or in the capital ratio.
 - In case of Limited Liabilities Partnership:** An LLP form of business organisation is a corporate entity and runs on the lines of a joint stock company. The creditors can move to National Company Law Tribunal for insolvency of LLP to get the recovery of their debts.
2. Lalaji, a local vegetable trader, took first mover advantage to sell his vegetables and groceries online. With the help of venture capitalists, he raised funds to grow his business, 'locallalaji.com'. In the first year, the business did well. The industry was flooded with new entrants like, Grofers, Bigbasket etc. In spite of sincere efforts by Lalaji, the business suffered losses. The investors pressurised him for returns. In the third year of operations,

the company stopped paying salaries and loans. The company was served a legal notice and assets were sold to repay the debts. Investors demanded that 'Lalaji's' personal assets should be sold but the auctioneer refused to do so.

- (a) Name the form of business organisation followed by Lalaji.
- (b) Are the investors justified while asking for Lalaji's personal assets to be sold? Explain by highlighting the feature associated with the above situation.
- (c) Identify two values that have affected the spirits of investors when they could not receive their dues from the company.

- Ans.**
- (a) The form of business organisation is '**company**'.
 - (b) Associated Feature is '**Limited Liability**'. The investors are not justified while asking for the personal assets to be sold because the liability of each member in a company form of organisation is limited to the extent of face value of shares held and shared in net reserves.
 - (c) **Values Affected:**
 - Lack of transparency
 - Lack of financial control

3. Mr. James, a promoter of Richi Rich Ltd., submitted all relevant documents with the registrar of companies and obtained the certificate of incorporation. The directors decided to go for capital subscription and took advice of Mr. James who decided to disclose all factual information in the public document on the basis of which the general public will apply for the shares.
- (a) Which document has been referred here by the promoter?
 - (b) Name the stage when the shares are issued.
 - (c) What values are indicated with the advice of the promoter?

- Ans.**
- (a) Prospectus
 - (b) Capital subscription
 - (c) **Values indicated:**
 - Business ethics
 - Respect for law

4. Farmers in the Hoshiarpur district of Punjab set up an organisation which has brought about a revolution in farming. Their project involves increasing the revenue of the small and marginal farmers. The organisation encourages unemployed youth to purchase the crops from the farmers at best possible higher rates and supply it to the consumer at a price lower than market price. As there are no middlemen, the producer and consumers both stand to gain. The farmers get good money after selling it at a higher rate and the consumers get quality products at a lower price.
- (a) Name the business organisation formed by the farmers.
 - (b) What values are generally upheld by such kind of business organisations?

- Ans.**
- (a) Farmer's Cooperative Societies.
 - (b) **Values upheld:**
 - Generation of employment.
 - Protecting farmers from exploitation.
 - Promotion to thrift.
 - Qualitative product at reasonable prices.

5. “He enjoys fiduciary position with the company and is responsible to carry out thorough investigation about the authenticity of the facts mentioned in the various documents submitted with the registrar.” At the time of formation of a company, he did not disclose some of the preliminary contracts to attain some personal gains before he got the certificate of incorporation.

- (a) Who is the person referred to in the above paragraph?
- (b) Can the birth of the company be questioned?
- (c) What values have not been adhered to by such persons?

Ans. (a) The person referred here is the ‘promoter’.
(b) Once a company is incorporated even with illegal objects, its birth stands valid regardless.
(c) **Values not adhered to:**

- Breach of trust of directors and investors
- Professional ethics

6. Annanya, Bharti and Chetna formed a partnership business. Annanya is appointed to carry on the business of the firm on behalf of other partners. Annanya has decided to purchase the goods from a firm in which her husband and her son are partners, at double the rate than the market rate without disclosing this fact to other partners of the firm.

- (a) State and explain which feature of the partnership has been violated here?
- (b) State which values have been violated by Annanya by not disclosing this information to other partners.

Ans. (a) The feature ‘decision making and control’ has been violated. All the decisions are required to be taken with mutual consent.

- (b) **Values ignored by Annanya:**
- Honesty
 - Integrity
 - Truthfulness
 - Violation of mutual agency relationship.

LONG ANSWER TYPE QUESTIONS

1. Kiran is a sole proprietor. Over the past decade, her business has grown from operating a neighbourhood corner shop selling accessories such as artificial jewellery, bags, hair clips and nail art to a retail chain with three branches in the city. Although she looks after the varied functions in all the branches, she is wondering whether she should form a company to better manage the business. She also has plans to open branches countrywide.

- (a) Explain two benefits of remaining a sole proprietor.
- (b) Explain two benefits of converting to a joint stock company.
- (c) What role will her decision to go nationwide play in her choice of form of the organisation?
- (d) What legal formalities will she have to undergo to operate business as a company?

(NCERT)

Ans. (a) The benefits to remain as sole proprietor: (explain briefly)

- **Quick decision making:** Being a sole proprietor, Kiran can always take quick decision without consulting with anyone.
 - **Confidentiality of information:** Kiran can always maintain secrecy of confidential information relating to secrets of her success and finances, with any outsider.
- (b) Benefits of converting sole proprietorship into company: (explain briefly)
- **Limited liability towards outsiders:** After converting the sole proprietorship form of business into a company, Kiran is escaped from the liability of her personal estates to be used to repay the liabilities of her business.
 - **Scope of expansion:** As Kiran plans to open the branches of business nationwide, the company form of organisation would help her raise funds from various sources such as banks, financial institutions and even from general public if it is formed as company limited by shares.
- (c) Kiran's role will be limited to administration and overall management if she plans to operate her business nationwide, she will require.
- additional managerial personnel as she would not be able to manage the large scale of operations at her own individually.
 - additional funds from banks and financial institutions.
- (d) Legal formalities Kiran needs to undertake to form joint stock company:
- Appointment of promoters and legal experts
 - Preparation of necessary documents
 - Submission of above documents with necessary fee with the registrar of companies of the state
 - Obtaining certificate of incorporation
2. Seema is running a business of artificial jewellery, bags, purses, nail art and other fashion accessories. Over the past few years, her business has grown from a local shop to a big business with three branches in the city. Now, she has been finding it tough to manage the affairs of three different branches on her own. She also wants to further expand but is confused how to manage and expand it further.
- (a) Which form of business is being carried by Seema at present?
- (b) Suggest a suitable form of business she should adopt to expand her business.
- (c) Write two merits and demerits each of the business form you suggest.

Ans.

- (a) Seema is running sole proprietorship form of business.
- (b) She can convert her business into General Partnership to expand and manage in better ways.
- (c) **Merits of Partnership:**
- (i) *Easy to form: (explain)*
- (ii) *Mutual Agency Relationship: (explain)*

Limitations of Partnership

- (i) *Lack of continuity: (explain)*
- (ii) *Possibility of conflicts: (explain)*

Alternative 1 to part (b)

(b) She can convert her business into **Limited Liability Partnership** to expand and manage in a better way.

(c) Merits of LLP

(i) *Limited Liability*: (Explain)

(ii) *Corporate Body*: (Explain)

Limitations of LLP

(i) *Complicated Procedure*: LLP is incorporated by following legal procedure under LLP Act 2008.

(ii) *Nationality*: One partner needs to be resident in India can be partner in LLP.

Alternative 2 to part (b)

(C) She can convert his business into **Private Limited Company** to expand and manage in a better way.

(c) Merits of Private Limited Company

(i) *Personal Finance*: A private limited company is not authorised to raise funds from general public, so there is no legal commitment to outsiders.

(ii) *Easy in formation*: A simple procedure is followed to form private limited company as no general public is involved in the management.

Limitations of Private Limited Company

(i) *Limited Finance*: As private company is not authorised to raise funds from the general public, so limited capital can be raised from the members.

(ii) *Difficult to form*: The legal provisions of the companies Act, 2013 have to be complied with to form private limited company.

Alternative 3 to part (b)

(D) She can convert his business into **One Person Company (O.P.C.)** to expand and manage in a better way.

(c) Merits of OPC

(i) *Limited Liability*: As it is formed on the lines of companies, the liability of the member (owner) is limited to the extent of share capital and undistributed profits.

(ii) *Personal Freedom*: The autonomy to run the business is maintained as in case of sole proprietorship.

Limitations of OPC

(i) *Eligibility*: Only a natural person who is citizen in India is eligible form OPC.

(ii) *Restriction on minor*: No minor can become member of nominee in an OPC form of business.

Note: A student is required to mention any one type of organisation with reasons under part (b).

3. Rahim, Krishan, Arjun and Shiva are partners in a partnership business. Rahim shares profits and losses, assumes unlimited liability, but does not take part in the affairs of the business. The public is not aware of the presence of Krishan but in all other respects, he is like an active partner. Arjun enjoys good reputation in the market and has allowed the

firm to use his name but he has neither contributed any capital nor does he take part in the management of the business. Shiva is only 15 years old, and has been admitted for the benefit of the partnership firm with the consent of all partners.

- How many partners can a partnership business have?
- Who is a nominal partner in the above case and how is he liable for the debts?
- What kind of partner is Krishan?
- Is Shiva a legal partner? Can he be held liable to pay the liabilities of the firm?
- Identify the values, which according to you motivated the partners in forming the partnership.

- Ans.**
- A partnership business can have at least 2 members and maximum 50 members.
 - Arjun is a nominal partner. Yes, he is also liable for the payment of debts with unlimited liability.
 - Krishan is a secret partner.
 - No, Shiva is not a legal partner and cannot be held liable to pay the liabilities of the business until he attains the age of majority to enter into a valid contract.
 - Values motivating to form partnership business:**
 - Spirit of cooperation
 - Mutual Agency Relationships

4. Case problem based on unit: Abhay, Binay and Charu are friends. They are pursuing their MBA from IIM, Kolkata. They were discussing their future plans while having coffee. Abhay said that after completing MBA he was planning to join his father's business in which his father is the only owner. Binay, on the other hand, wanted to get a job in some big company through the institute's placement cell. Since Charu loves children, she shared her willingness to join an NGO and use her knowledge and skills to help underprivileged children.

- Identify and give two points of difference between Abhay's and Binay's vocational plans.
- What is the form of business organisation run by Abhay's father?
- How would you classify the activity which Charu is willing to pursue after college?
- By quoting the lines state the value(s) depicted in the above case.

- Ans.**
- While Abhay is planning to join business, his friend Binay is interested in getting employed by a company.

Basis	Business	Employment
1. Nature of Work	Production/purchase and sale of goods and services with the motive to earn profit	Performing services for others
2. Income	Profit earned	Remuneration in return of services performed

- Sole Proprietorship Business.

- (c) Charu is willing to pursue a non-economic activity, which can be defined as an activity performed out of love for children and not with the motive of earning money.
- (d) Value Depicted:
- Sharing Responsibility
Quoted Lines: Abhay said that after completing MBA he was planning to join his father's business in which his father is the only owner.
 - Love and Care for underprivileged children.
Quoted Lines: Since Charu loves children, she shared her willingness to join an NGO and use her knowledge and skills to help underprivileged children.

5. **Case problem based on unit:** Dev runs a successful commercial taxi business in Bengaluru. Private commuters, tourists and business clients are among his customers. Dev has also operates a daily bus service between Bengaluru and Mysore, which has proved to be the most popular service provided by his business to commuters. He is currently operating as sole proprietor. However, he is considering the option of entering into a partnership with his friend Natasha, who is physically challenged. Natasha is very good at managing company's accounts but is unable to find a job.

- (a) While plying, the engine of one of the cars caught fire and was damaged. Name and briefly explain the type of risk.
- (b) Which objective of the business has Dev achieved by including Natasha in his business?
- (c) What should Dev do to avoid the unlimited liability of the business without inviting any partners?
- (d) Define the form of business organisation which Dev is currently operating.
- (e) Which two values is Dev exhibiting by forming a partnership with his physically challenged friend?

Additional Questions:

- (f) Can Dev have a partnership firm and still avoid unlimited liability? Explain how.
- (g) What kind of industry is commercial taxi business?
- (h) State any two merits of the form of business which Dev is planning to enter with his friend Natasha.

Ans.

- (a) **Pure Risk:** Such risks involve only the possibility of losses or no loss.
- (b) Dev has achieved social objective of business and of providing employment opportunity to a physically challenged person.
- (c) Dev can convert his business into a One Person Company (OPC) under the provisions of Companies Act, 2013, to avoid unlimited liability. This way the liability of his business will be paid out of the funds of the business in case the business is closed due to any reason.
- (d) Dev is undertaking **sole proprietorship** form of business. It is the type of the business which is controlled and managed by a single person who invests money in the form of capital, receives profits and bears all losses.

- (e) Value Communicated:
- Humanity
 - Women Empowerment
 - Sensitivity
- (f) Dev can convert his sole proprietorship business into Limited Liability Partnership (LLP) business, which is required to be incorporated under Limited Liability Partnership Act, 2008, to avoid unlimited liability of the partners.
- (g) Tour and Travel industry comes under service/tertiary industry. It is also known as auxiliaries to trade.
- (h) Merits of Partnership
- (a) **Balanced Decision Making:** Due to mutual agency relationship, everyone is expected to be competent to hold professional approach for taking wise decisions with mutual consent. Hence, balanced decision-making is maintained.
- (b) **Sharing of Risk:** It becomes difficult for a sole proprietor to bear huge losses due to business risks but in case of partnership firms, all partners share such risks.



N.C.E.R.T. QUESTIONS



SHORT ANSWER TYPE QUESTIONS

(3–4 MARKS)

1. Compare the status of a minor in a joint Hindu family business with that in a partnership firm.
2. If registration is optional, why do partnership firms willingly go through this legal formality and get themselves registered? Explain.
3. State the important privileges available to a private company.
4. How does a cooperative society exemplify democracy and secularism? Explain.
5. What is meant by 'partner by estoppel'? Explain.
6. Briefly explain the following terms in brief:

(a) Perpetual succession	(b) Common seal
(c) Karta	(d) Artificial person

LONG ANSWER TYPE QUESTIONS

(5–6 MARKS)

1. What do you understand by a sole proprietorship firm? Explain its merits and limitation.
2. Why is partnership considered by some to be a relatively unpopular form of business ownership? Explain the merits and limitations of partnership.
3. Why is it important to choose an appropriate form of organisation? Discuss the factors that determine the choice of form of organisation.
4. Discuss the characteristics, merits and limitation of the cooperative form of organisation. Also describe briefly different types of cooperative societies.
5. Distinguish between a joint Hindu family business and partnership.
6. Despite limitations of size and resources, many people continue to prefer sole proprietorship over other forms of organisation. Why?

APPLICATION QUESTIONS

Refer the section: 'Application Based Questions'.

PROJECT/ASSIGNMENTS

1. Divide students into teams to work on the following:
 - (a) To study the profiles of any five neighbourhood grocery/stationery store.
 - (b) To conduct a study into the functioning of a joint Hindu family business.
 - (c) To enquire into the profile of five partnership firms.
 - (d) To study the ideology and working of cooperative societies in the area
 - (e) To study the profiles of any five companies (inclusive of both private and public companies)

Notes:

- (i) Some of the following aspects can be assigned to the students for undertaking the above mentioned studies.

Nature of business, size of the business measured in terms of capital employed, number of persons working, or sales turnover, problems faced, incentive, reason behind choice of a particular form, decision-making pattern, willingness to expand and relevant considerations, usefulness of a form, etc.
- (ii) Student teams should be encouraged to submit their findings and conclusions in the form of project reports and multimedia presentations.

EXERCISE

VERY SHORT ANSWER TYPE QUESTIONS

(1 MARK)

1. What is the nature of liability in sole proprietorship?
2. State two limitations of sole proprietorship business.
3. For which type of business is the sole proprietorship business suitable?
4. Who is an ostensible partner?
5. Which Act of government governs the functioning of an OPC?
6. How would you differentiate a particular partnership from partnership at will?
7. State the conditions of a HUF business.
8. What is mutual agency relationship in partnership?
9. Who is a nominal partner in a partnership business?
10. Name the partner who does not have interest in the partnership business but lends his name to the firm.
11. Can a minor be a member in a HUF business?
12. What is the main purpose for the formation of cooperative society?
13. Who has the limited liability in HUF?
14. Name two forms of business organisations where the owners have limited liability towards the debts of such business.
15. Name two forms of business organisations where the owners have unlimited liability towards the debts of such business.
16. How does a company put its signature on the documents?
17. How many clauses does a memorandum of association contain?
18. Define Partnership according to Indian Contract Act, 1972.
19. What do you mean by unlimited liability of the owners of a business?
20. Who is partner by holding out?

21. What is meant by 'perpetual succession'?
22. Does a minor bear the losses in a partnership firm?
23. How is 'Limited Partnership' different from 'Limited Liability Partnership'?
24. How is a 'Dormant Partner' different from 'Designated Partner'?
25. How is a 'Provisional Contract' different from a 'Preliminary Contracts'?

SHORT ANSWER TYPE QUESTIONS

(3–4 MARKS)

1. Define sole proprietorship.
2. Discuss the following features of sole proprietorship:
 - (a) No separate entity
 - (b) Sole Risk Bearer and Profit Recipient
3. What do you mean by the term Unlimited Liability?
4. Explain any two limitations of a sole proprietorship business.
5. Define Joint Hindu Family Business.
6. Name the types of HUF business system.
7. Who is a 'Karta'?
8. What is liability of the rest of the members except that of 'Karta' in the HUF business?
9. Can a minor be a member in HUF business?
10. How does the continuity of HUF affect with the death of the manager of such business?
11. Who are coparceners?
12. What is the liability of coparceners?
13. Can rest of the members except 'karta' enforce their suggestions in a HUR business?
14. How does 'Karta' dominate the other members in the HUF business?
15. Define partnership under Partnership Act, 1932.
16. What do you understand by the concept of 'Mutual Agency Relationship' in partnership firms?
17. Are the partnership firms required to disclose their accounts publicly?
18. Do you think the acts of a partner are binding if such partner has to take a decision in the absence of other partners?
19. Who is ostensible partner?
20. Who is dormant partner?
21. Differentiate between 'Partner by Estoppel' and 'Partner by Holding Out'.
22. Can a minor person be admitted into the partnership firm?
23. Under what circumstance can a minor partner share loss in a firm?
Hint: *He cannot share the loss if he is a minor.*
24. How is a general partnership different from the limited partnership?
25. Can a partnership be run without having a written partnership deed?
26. Name the Act which governs the provisions of the partnerships.
27. Define Limited Liability Partnership.
28. Name the Act which governs the provisions of limited liability partnership.
29. Are the partnership firms compulsory to be registered?

30. Detail the benefits of registration of a partnership firm.
31. Can the creditors of a partnership firm file a case against the unregistered partnership firm to recover their dues?
Hint: *Yes*
32. Who are the 'Board of Directors'?
33. Are the shares in a private limited company transferable?
34. Explain how is a company an artificial person?
35. What do you understand by the term 'Perpetual Succession'?
36. What is meant by the term 'Oligarchic Management'?
37. Name the feasibility studies in case of formation of a company.
38. What are the qualification shares?
39. What is minimum subscription?
40. How many names have to be sent to the registrar of the companies for the approval of the name of a proposed company?
41. Explain the situations when a particular name suggested for a company stands undesirable.
42. What are the categories of 'Objects Clause'?
43. What could be the maximum liability of a shareholder?
44. What is association clause?
45. State the procedure to obtain D.I.N.
46. Name the certificate through which a company gets birth.
47. What does CIN stand for?
48. Can the existence of the company be challenged even if the company has been incorporated with illegal objects?
Hint: *No, because the certificate of incorporation is the conclusive proof of regularities in the process of incorporation even if there may be certain flaws during its incorporation and thus incorporation stands valid.*
49. What are the 'Pre-incorporation Contracts'?
50. What is another name of 'Pre-incorporation Contracts'?
Hint: *Preliminary Contracts.*
51. Who is liable for the payments for the pre-incorporation contracts?
52. What are 'Provisional Contracts'?
53. Who is responsible for the payment of Provisional Contracts?
54. Are the promoters responsible for the payment of provisional contracts?
55. When can the provisional contracts be enforced on the company?

LONG ANSWER TYPE QUESTIONS

(5-6 MARKS)

1. Explain how a company form of organisation is in a position to raise huge amount of capital.
2. "Karta is the most powerful person who can flourish as well as ruin the business." Comment.
3. 'One man control is best in the world if that man is big enough to manage the whole business.' Comment.

4. 'A sole proprietorship business cannot be completely abolished even there are so many multinational companies established in India'. Do you agree? Give your views.
5. There are limitations in terms of finance, size, human resources, government patronage; still many people prefer sole proprietary business. Why?
6. Why is partnership considered by some to be a relatively unpopular form of business ownership? Explain the merits and limitations of partnership.
7. Distinguish between 'General Partnership' and 'Limited Partnership'.
8. What is Limited Liability Partnership? Explain its features.
9. 'A company is said to be an artificial person, having separate legal personality and perpetual succession.' Explain.
10. Explain the functions of promoters.
11. Distinguish between Memorandum of Association and Articles of Association.
12. Differentiate between 'Preliminary Contracts' and 'Provisional Contracts'.
13. If the registration of firm is optional, why do partnership firms willingly go through the legal formalities and get their business registered? Explain.
14. What factors would you keep in the mind before starting a business?
15. 'A Private Limited Company is more superior to a Public Limited Company.' Do you agree? Explain with reasons.

Hint: *Explain the privileges to a private limited company.*

