

# **FORMATION OF A COMPANY**



**Class 11**

**BUSINESS STUDIES**

**STAGE - I - PROMOTION**

**FORMATION OF A JOINT STOCK COMPANY**

**Joint stock company has to follow a certain specified legal procedure for its formation. Planned action and conscious efforts are required.**

**Formation of a company involves the following stages:**

- Promotion**
- Incorporation**
- Capital subscription stage**
- Commencement of business**

## **Promotion**

- **Promotion stage includes all the steps right from conception of idea to starting the company, till it is formed. It is the process of planning and organising all the resources required to form a company.**

- **Promotion involves the discovery of business idea, its investigation and assembling, necessary resources to set up the business. The person who performs all the activities during the promotion stage is known as Promoter. The promoter conceives the business idea and takes all initiatives to form a company.**
- **The promoter can be an individual, a group of persons or an institution.**
- **The promoter performs the following functions. These functions are also known as steps in promotion stage.**

**Steps in the promotion stage are:**

**1. Identification of Business Opportunity:**

- **The promotion stage begins with the discovery of an idea to set up a business. It can be an idea to set up a new business or an idea to expand the existing business.**
- **The promoter identifies the profitability of the idea by analysing the opportunities available in that area. The promoter also analyses the various resources required, amount of capital required and the degree of risk involved.**

## **2. Name Approval:**

- **Two companies cannot have identical names. It is necessary for every company to get its name approval from the registrar so that it does not match with any other company's name. Generally, company gives these names in order of priority to the registrar.**
- **The registrar matches the name with the names of other companies and if it is not identical then the registrar approve the name.**

### **3. Fixing up Signatories to Memorandum of Association:**

- **Promoters have to decide about the people who will be signing the memorandum.**
- **Usually the signatories of memorandum become the first directors of the company. Promoters also take their written consent to act as directors and ask them to buy qualification shares.**

#### **4. Appointment of Professionals:**

- **The promoter appoints the brokers and underwriters to ensure the availability of capital by sale of a company's securities and solicitors are appointed to deal with the legal matters of the company. Bankers are appointed to have smooth financial dealings.**



**5. Preparation of Necessary Documents:**

- **A promoter takes up the steps to prepare some legal documents of the company which have to be submitted to the registrar at the time of incorporation. The common documents which are prepared by a promoter are Memorandum of Association, Article of Association, Prospectus etc.**

# FORMATION OF A COMPANY



**Class 11**

**BUSINESS STUDIES**

**STAGE - II - INCORPORATION**

➤ **Incorporation**

**Incorporation of a company is the second stage in the formation of a company. Incorporation refers to the registration of the company under Companies Act, 2013.**

**The main steps under the incorporation stage:**

### **1. Filing of Necessary Documents:**

- **Once the registrar approves of the name, the following documents have to be submitted with the registrar:**
  - i. Memorandum of Association**
  - ii. Articles of Association**
  - iii. Statement of Authorised Capital**
  - iv. A list of directors with their names, addresses, occupation and age**
  - v. The written consent of the directors to act as directors**

- vi. Notice of the address of the registered office of the company**
- vii. A statutory declaration stating that all the formalities related to the formation of the company are duly completed.**

## **2. Payments of Fees:**

**Along with filing of the above documents the prescribed fees of registration also have to be deposited.**

**The amount of registration fees depends on the amount of authorised capital.**

### **3. Registration:**

**The registrar verifies all the documents submitted and he also checks the receipt of fees deposited. If he is satisfied with the validity and authenticity of the documents submitted then the registrar enters the name of the company in his register.**

#### **4. Certificate of Incorporation:**

**After entering the name of the company in the register, the registrar issues a certificate of incorporation. From this date onwards the company is considered as a separate legal entity.**

## **Specimen of Certificate of Incorporation**

**I hereby certify that ..... (Name of the Company) is this day incorporated under the companies Act 1956, and that the company is limited given under my hand at Delhi, this twenty-fourth day of August, two thousand and twelve.**

**Fees: Deed Stamp**

**Rs.....**

**Stamp Duty on Capital**

**Rs.....**

**SEAL**

**Sd/-**

**Registrar of Companies  
Delhi**

**Corporate identity Number 1930 of 2015.**



- ❑ **Effect of the Certificate of Incorporation:**
  - ❖ **A company is legally born on the date printed on the Certificate of Incorporation.**
  - ❖ **It is considered as a separate legal entity with perpetual succession only from this date.**
  - ❖ **The certificate of incorporation is the conclusive evidence of the legal existence of the company.**

**Following points will make it more clear.**

- 1. The certificate of incorporation was issued on 24<sup>th</sup> August whereas on the certificate date was written as 22<sup>nd</sup> August. The company is considered to be born on 22<sup>nd</sup> August only and so all dealings carried on 23<sup>rd</sup> August will be considered legal although the certificate was issued only on 24<sup>th</sup> August.**

2. After issue of registration certificate, it was found that a person had forged signature on the memorandum but then also the incorporation will be considered valid.

# FORMATION OF A COMPANY



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**BUSINESS STUDIES**

**STAGE - III –  
CAPITAL SUBSCRIPTION STAGE**

- **After getting the certificate of incorporation the private companies get formulated and can commence their business activities but a public limited company has to perform a third stage and get the certificate of commencement.**

**The steps involved in stage of commencement of business are:**

**1. SEBI Approval :**

**SEBI (Securities and Exchange Board of India) is a regulatory body, which controls the capital market of India to protect the interest of investors. The Public Ltd. companies must submit all the relevant information with the SEBI before issuing its securities in the capital market.**

**Companies should not hide any material fact from SEBI, else their registration can be cancelled according to “guidelines for disclosure and investor protection 2000”.**

## **2. Prospectus for a Statement in Lieu of Prospectus:**

- **A public company has to prepare another important document called prospectus.**
- **It is a circular or invitation issued to invite the general public for subscribing to the shares of the company.**
- **This document has to be deposited with the registrar.**



### **3. Minimum Subscription.**

- **To make sure that company does not have shortage of funds, it is made compulsory that company must receive applications for some minimum number of shares. This is called minimum subscription.**
- **A public limited company cannot make allotment of shares unless a minimum subscription is received.**

- **As per the rules of SEBI (Securities Exchange Board of India), a company must receive 90 per cent of the issued amount within 120 days of issue of prospectus.**
- **For example. If a company plans to issue 10,000 shares of Rs.10 each then it must receive applications for minimum 9,000 shares (90% of 10,000) before allotment.**

- In case the minimum subscription is not received then the company must send back or return the application within the next ten days (130 days from the issue of prospectus).

#### **4. Application to Stock Exchange :**

- A firm must get itself listed in a stock exchange before selling its securities to the general public.

- **The company may apply in any of the recognised stock exchanges to get the permission.**
- **The stock exchange authorities verify the financial soundness and other aspects of the company and if they are satisfied then the name of the company is listed.**
- **If a firm does not get permission from a stock exchange within ten weeks from date of closure of subscription list then the allotment will become void and the money received from applicant must be returned.**

### **5. Allotment of Shares.**

- **After getting the name listed, the company prepares a return of allotment.**
- **Return of allotment is a statement giving details about the names and addresses of all the shareholders.**
- **The company has to submit a return of allotment with the registrar stating the names, addresses and the number of shares allotted to each shareholder.**

# **FORMATION OF A COMPANY**



**Class 11**

**BUSINESS STUDIES**

**STAGE - IV –  
COMMENCEMENT OF BUSINESS**

**After subscription the securities, and receiving the minimum subscription, the company applies to the registrar to issue the Certificate of Commencement of Business. Along with the application, a company must file the following documents:**

- i. A declaration that shares payable in cash have been subscribed for and minimum subscription has been received.**
- ii. A declaration that every director has paid in cash the application and allotment money on his shares.**
- iii. A declaration that no money is pending to pay back to the applicants.**



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

- ✓ The registrar will verify all the documents and declaration submitted by the company.**
- ✓ If he is satisfied with the authenticity or validity of these documents then he will issue a Certificate for Commencement of Business.**
- ✓ The company can start its business activities from the date of issue of the certificate.**

**Specimen of Certificate of Commencement of Business**

**I hereby certify that..... Ltd. Of..... which was incorporated under the companies Act. 1956, on the ..... day of ..... 20 .... and which has this day filed a statutory declaration in the prescribed form that the conditions of Section 149 have been complied with, is entitled to commence business.**

**Given under my hand at.....this day of.....two thousand.....**

**SEAL**

**Sd/-Registrar**

**Joint Stock Companies**

**.....(State)**

**All the business dealings after issue of certificate of commencement are binding on company.**

# FORMATION OF A COMPANY



**Class 11**

**BUSINESS STUDIES**

**MEMORANDUM OF  
ASSOCIATION (MOA)**

**There are three basic documents, which are required to be filed with the registrar of companies in the formation of a public company.**

**These are:**

- ✓ Memorandum of Association**
- ✓ Articles of Association**
- ✓ Prospectus.**

## **Memorandum of Association (MoA)**

- **The Memorandum of Association is the principal document of a company. It is considered as the charter of the company.**
- **It contains the powers and objectives of the company. It also describes the scope of operations of the company.**
- **It can be altered only according to the provisions made in the Companies Act regarding its alterations.**

- **Memorandum of Association provides information to outsiders such as creditors, suppliers, etc. to know the limitations and scope of a company's dealings. It is also known as the doctrine of outdoor management.**

## **Contents of Memorandum of Association**

➤ **The Memorandum of Association contains the following clauses:**

**1. Name Clause :**

**This clause contains the complete name of the company. The company can choose any name subject to the following restrictions:**

- i. The name of the company must end with the word ‘Limited’ in case of public limited company and with the word ‘Private Limited’ in case of Private Limited Company.**
- ii. The name should not be similar or identical to the name of the any other company.**
- iii. The name should not contain the word “Cooperative:”.**
- iv. The name should not convey any connection or link of the company with a government department.**



## **2. Situation/Domicile Clause :**

- **This clause contains the name of the state in which the registered office of the company is to be situated. It is necessary because a company gets the registration from that state only.**
- **The registered office is a place where all the important documents of the company are kept. A company must have a registered office when it starts its business activities or within thirty days of its registration, whichever is earlier.**

## **ALTERATION OF SITUATION CLAUSE:**

**The Situation clause can be altered in the following ways:**

- (i) By passing a special resolution and by obtaining sanction of the registrars of both the states if the office is to be shifted from one state to another.**

- (ii) By passing a special resolution only if the office is to be shifted from one town to another in the same state.**
- (iii) By passing an ordinary resolution if office is to be shifted from one locality to another within the same town.**

### **3. Objects Clause :**

- **It is the most important clause of the Memorandum of Association.**
- **It contains the main object of the company and other secondary objectives which the company may pursue.**
- **This clause defines the scope and limitations of the activities of the company.**

**The objects must be defined and stated keeping in mind the following conditions :**

- i. The objects of the company must be legal.**
- ii. The objects should not be contrary to the provisions of any law.**
- iii. The objects must not be immoral.**

**ALTERATION IN OBJECTS CLAUSE :**  
In order to alter its object clause, a company must pass a special resolution and obtain the permission of the Company Law Board.

#### **4. Liability Clause :**

- **This clause defines the liability of the members of the company. In case of companies limited by shares, the liability of the members is limited to the extent of unpaid amount of their share capital.**

- For example, if a person is having 1000 shares of the face value of Rs.10 each and he has paid Rs. 7 per share then at the time of winding up his liability will be Rs.3,000 [Rs.3 (unpaid amount) x Number of shares].



**ALTERATION OF LIABILITY CLAUSE :**

**If a company wants to make an alteration in its liability clause then it must pass a unanimous resolution in a meeting of its members.**

### **5. Capital Clause :**

- **This clause specifies the amount of share capital with which company is to be registered.**
- **The capital with which a company is registered is called registered/authorised or nominal capital.**

- **A company can issue only that number of shares which are authorised by its memorandum.**
- **Alteration of Capital Clause. A company can alter its capital clause by passing a special resolution and by obtaining the approval of Company Law Board.**

# FORMATION OF A COMPANY



**Class 11**

**BUSINESS STUDIES**

**ARTICLES OF  
ASSOCIATION (AOA)**

## **ARTICLES OF ASSOCIATION (AOA)**

**Articles of Association contains rules and regulations regarding the management of a company's internal affairs.**

**In case companies do not want to prepare their own articles of association, then they can select any one article of association given in Table F of the Companies Act.**

- **In Table F of Companies Act 99 model sets of articles of associations are given. Companies can select any one from these ninety-nine sets.**
- **The Articles of Association must be signed by all the directors of the company. It must be duly attested by any two witnesses.**

- **Articles of Association is also known as byelaws of a company or Doctrine of Indoor Management. The contents of the articles are divided into paragraphs and paragraphs are numbered.**

**The main Contents of Articles of Association are:**

- 1. The amount of share capital and different classes of shares**
- 2. Rights of each type of shareholders**
- 3. Procedure for making allotment of shares**
- 4. Procedure for issuing share certificates**



- 5. Procedure for transfer of shares**
- 6. Procedure for forfeiture of shares**
- 7. Procedure for reissue of forfeited shares**
- 8. Procedure for conducting meetings**

- 9. Procedure for appointment and removal of directors**
- 10. Duties, powers and remuneration of directors**
- 11. Procedure for declaration and payment of dividend**
- 12. Procedure regarding winding up of the company**
- 13. Procedure regarding keeping of books of accounts and their audit.**

**14. Seal of the company.**

**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.**

## **ALTERATION OF ARTICLES OF ASSOCIATION :**

**A company may change its Articles of Association by passing a special resolution, subject to the following conditions:**

- 1. The alteration must not be contrary or against the provisions of Memorandum of Association and Companies Act.**
- 2. It must not result in breach of contract with outsiders.**

- 3. It must be in the interest of the company.**
- 4. It must not result in increasing the liability of its members.**
- 5. If the alteration involves conversion of public company into private company, then the approval of the central government must be obtained.**

# FORMATION OF A COMPANY



**Class 11**

**BUSINESS STUDIES**

**DIFFERENCE BETWEEN MEMORANDUM OF  
ASSOCIATION AND ARTICLES OF ASSOCIATION**

## **DIFFERENCE BETWEEN MEMORANDUM OF ASSOCIATION AND ARTICLES OF ASSOCIATION**

<b>Basis of Distinction</b>		<b>Memorandum of Association</b>	<b>Articles of Association</b>
<b>1.</b>	<b>Nature</b>	<b>MoA is the charter or the constitution of the company.</b>	<b>AoA refers to the type-laws of the company for smooth and internal management of the company</b>
<b>2.</b>	<b>Scope</b>	<b>It defines the objects and powers of the company</b>	<b>It contains rules and regulations for carrying out day-to-day operations.</b>

<b>3.</b>	<b>Status</b>	<b>It is the fundamental document of a company. It supersedes the articles.</b>	<b>It is a supplementary document of a company.</b>
<b>4.</b>	<b>Legal effect</b>	<b>Acts done beyond the scope of memorandum are void.</b>	<b>Acts done beyond the articles can be ratified by the shareholders.</b>



<b>Basis of Distinction</b>		<b>Memorandum of Association</b>	<b>Articles of Association</b>
<b>5.</b>	<b>Compulsion</b>	The preparation and filing of Memorandum of Association is compulsory.	The preparation of Articles of Association is not compulsory. A company may adopt Table F of the Companies Act.
<b>6.</b>	<b>Alteration</b>	Alteration in Memorandum of Association is a difficult and lengthy process. The approval of the government is necessary for alteration.	Alteration of Articles of Association is an easy and simple process. The approval of the government is not necessary.

# FORMATION OF A COMPANY



**Class 11**

**BUSINESS STUDIES**

**PROSPECTUS**

**PROSPECTUS :**

- **A public limited company, limited by shares, must issue the prospectus if it wants to make an appeal to the public to subscribe to its shares or debentures.**
- **According to the Companies Act, 2013, “A prospectus is any document (including any notice, circular, advertisement or other documents) that invites deposits or offers from public for the subscription or purchase of shares or debentures of a body corporate.”**

**The essential elements of a prospectus are as follows:**

- 1. There must be an invitation to the public at large.**
- 2. The invitation must be made by or on behalf of the company.**
- 3. The invitation must be to subscribe to or purchase its shares or debentures.**