SELECTED ARTICLES
ON THE
WORKING AND MANAGEMENT
OF
CORPORATE SECTOR IN INDIA

RESEARCH AND STATISTICS DIVISION
DEPARTMENT OF COMPANY LAW ADMINISTRATION
MINISTRY OF INDUSTRY

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FOREWORD

This brochure contains a number of special articles contributed by the officers of this Department to the first Annual Number of Company News and Notes, issued on the 1st October 1963, the first anniversary of the birth of this departmental journal. A similar brochure was issued on the occasion of the enforcement of the Companies Act in 1956.

A cursory comparison of the contents of this brochure with its earlier prototype will disclose, at a glance, the distance which has been covered by the Department of Company Law Administration in a somewhat unfamiliar and difficult terrain in the years between 1956 and 1963. While the emphasis in the earlier brochure was largely on explanation and elucidation, the key-note of the articles in the present brochure seems to centre round the slowly developing concept of business as a means to a social end. Although this concept has yet to receive general acknowledgement and recognition in this country, one of the major contributions of the new Indian Company Law and its administration during the last eight years has been to give form and shape to this emerging concept in a manner, which will render the widespread appreciation and ultimate acceptance of this concept much easier in the future. It is to be hoped that the articles in the brochure will help to stimulate thinking on the hitherto unexplored problems of business as a way of life.

New Delhi,
4th October, 1963
These articles have been written by the officers of the Department in their personal capacity and therefore the views expressed therein are theirs and the Department of Company Law Administration is in no way committed to them.
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A STATEMENT ON THE PURPOSES AND OBJECTIVES OF THE COMPANIES ACT, 1956

By

D. L. MAZUMDAR, I.C.S.

Secretary to the Government of India

(One of the major tasks of the Department of Company Law Administration since its establishment has been to elucidate the background of the new Company Law and to expound the economic and social philosophy underlying its operative provisions. This has been no easy task. For, although the accredited organs of trade and industry within the country have formally recognised the accepted formulation of the ultimate objects of the country's economic and social policies, the duties and obligations imposed on individual companies by the new law have not been always readily acknowledged as the inevitable consequences of the discipline intended to be enforced on them in pursuance of these objectives. Outside the country, however, the objects underlying the new Company Law have been increasingly much better understood. In this context, we believe the following informal address by the Secretary of the Department of Company Law Administration to the Business International Round Table which met in Delhi in October 1961 will still be of current interest to our readers. The authoritative version of this address is being published for the first time in this Country.—Ed.)

“The briefing memorandum in your hands” has already touched upon the special features of our company law in this country. I would not, therefore, elaborate them any further, except to say a few words to explain the statement contained in the memorandum that “the company law in this country is also used as a mechanism to regulate the economy in the ‘national interest’”. In a very broad sense, this is, of course, as true of this country, as indeed it must be of any other country in the world, including yours, which boasts of an integrated system of mercantile laws. But the statement should not lead you to think that our company law propounds certain a priori principles of corporate conduct or is based on any particular ideological view of the economy, which is not already embodied in the basic economic thinking implicit in the provisions of our Constitution and other fundamental documents bearing on the aims and objects of our economic policy. It

Relevant observations made on the Companies Act and its working in the briefing memorandum circulated by the Business International (Indian) Round Table with which the Secretary of the Department of Company Law Administration dealt in his address above, appended to this article.
may give some conciseness and precision to your thinking if you would paraphrase the words “national interest” in this context. I believe we in this country share with yours and which are embodied in such familiar pronouncements of corporate policy in your country, although they may be phrased differently in ours, e.g., the need for democratic decision-making in a free society, the decentralization of economic power, the regulation of concentration in the corporate field, and the reduction of such inequalities as operate to the detriment of the economy. As you must be aware, these are some of the basic ingredients of our accepted economic and social policy in this country, and all that our Company Law does, in furtherance of our so-called ‘national interest’, is to try and help in the realization of these values, if not as it is possible for this law alone to help in this process. I need only add that in developing countries, where the average standards of current corporate behaviour are ordinarily much below those obtaining in industrially advanced countries, the need for systematic and continuous emphasis in their laws and institutions on the accepted national values is as important to the future growth and expansion of their economy as it is essential for the control of those social tensions and disharmonies, which inevitably accompany the processes of transition from a relatively out-dated and stagnant to a comparatively modern and dynamic economy.

Having said this about the special features of our Companies Act, I shall now briefly touch upon a few facts which have had their impact on the scope, size, form and lay-out of our legislation, because although these matters are now fairly well understood, a few years ago even some informed students of our current economic affairs were puzzling over them. For example, some time in 1957, when an important Indian Industrial Delegation, under the leadership of one of our leading business leaders visited your country, they were presented with a short note by your Department of Commerce on the alleged deterrents to U.S. private investment in India, in which several questions were asked about our company law. As I have already said, similar questions are now rarely asked, and indeed, the latest publication of the Department of Commerce in the U.S.A., released a few months ago, on ‘Investment in India’ itself makes the following heartening observation.

“Although many private business associations in India”—and I would add also some foreign business opinion—“argued at the time of the adoption of the new Companies Act that the State had usurped the place of shareholders by assuming such broad powers of supervision, regulation and direction, the Government has used these powers sparingly. Relatively little interference in the management of domestic business concerns has occurred and only a negligible number of cases have involved the investigation of the management of foreign companies.”

Re-assuring as this assessment is in the light of the widening knowledge and better appreciation of this subject, it may be just as well to say a few words on this aspect of our Company Law. The reasons for the incorporation of detailed regulations in the body of our new Companies Act, dealing with aspects of company management which are admitted to the judgment and discretion of management in the U.S.A. and U.K., were as follows:—

(i) the relatively tardy growth of the sense
of fiduciary responsibility in the average company management in this country—I underline the word 'average';

(iii) the absence in this country of strong and well-recognised financial institutions with long traditions of public service to their credit, similar to those operating in the money and capital markets of many other advanced countries of the world, which oversee company flotation and management, thereby rendering statutory regulation of such matters largely superfluous;

(iv) the absence in this country of a strong and reasonably unbiased financial and economic press, served by competent commentators of knowledge, integrity and independence;

(v) the absence in this country of any strong and well-developed public opinion as regards company matters which is prepared to frown severely upon unwarranted deviations from accepted norms of company behaviour and practice, and

(vi) last, but not the least, the comparatively slow progress so far made in this country towards professionalisation of the management of Joint Stock enterprises which is already an established fact in the leading countries of the West and which has accounted for far-reaching changes in the character and quality of company management in those countries.

I must, however, point out to you that there has been a noticeable growth in company consciousness during the last four or five years, particularly after the enactment of our new company law, largely, I think, as a by-product of the working of the new company law and the activities of the Department of Company Law Administration which administers it. Time does not permit me to go into this aspect of the question further, but the major point which I wish to make in this context is that the differences between company practice and behaviour in this country and in the advanced countries of the world, account largely for the nature and scope of our law and for its admittedly detailed provisions. Commentators who ignore these differences are, indeed, not comparing like with like.

If I may make a generalization, in this context, it is this—the form and manner in which company practice is best regulated in a country depends not so much on any a priori or ideological consideration, as on the state of the country's economic and social development; the current manners and mores of the business community, particularly of the higher echelons of that community; and a series of other objective factors too numerous to mention—not the least important of which, however, are the competence and capacity of the country's voluntary economic institutions to regulate, as a matter of internal discipline, the behaviour pattern of the corporate sector. All this must be obvious to you, gentlemen, who, I assume, are familiar with the conditions and circumstances in which in your own not too remote economic history, the legislative measures of the New Deal were conceived and fashioned by one of your great Presidents of the past. Although contemporary business thinking in your country at that time looked upon some of those restrictive measures with strong feelings of persecution and resentment, that mood has now changed, thanks to the sea-change which business methods and practices and the average standard of business morality in your country has undergone in the intervening years. So will it be, I feel sure, with the business thinking in this country in the years to come.

I have ventured to draw attention to this concept of the relativity of all basic economic legislation, whether in our country or in yours, not only because it helps to explain several facets of our company law, which may seem strange to outsiders, but also because the widespread recognition of this concept would, I believe, add a new
Finally, the law is consciously constructed to weaken centralized private control of Indian industry, particularly as exemplified in the managing agency system. A managing agent was a firm that directed, for a fee, the affairs of many companies in which it might or might not hold a financial interest. These specialized firms worked part-time for many companies and created a series of quasi-monopolistic empires within the country, receiving what many stockholders felt was too great a share of the profits and taking control of the managed company out of the hands of the shareholders.

The law specifically limits the number of firms that a managing agency can control to 10, requires approval by the Department of Company Law for appointment of a managing agency, and limits appointment to a period of 10 years and reappointment to five years. It also sets maximum remuneration scales: 10% of the net profits of a managed company when profits are no more than $210,000 scaling down to 4% when profits are $2 1 million or more. The legal minimum payment is $10,500 a year. Since very few US affiliates have been established in India with managing agencies, these limitations normally do not concern US investors, although they are an important consideration if a US firm licenses a “managed” company in India.
must file its balance sheet and earnings statement with the Registrar of Companies—and these are available to the public.

The Companies Law also gives the GOI wide powers (also rarely used except where there is real abuse) to investigate practically any aspect of management, with or without a complaint from the stockholders. Obviously such things as issuance of duplicate shares or payment of dividends without providing for depreciation are illegal, but the investigatory power extends to such matters as issuance and transfer of shares and debentures in general, voting rights of shareholders and registration of company resolutions and agreements, managerial remuneration, distribution of dividends, maintenance and audit of company records, and liquidation of a company. (Liquidation, in any case, requires approval of 75% of the stockholders, as does a change of capitalization, an increase in top management salaries and even changing an office.) Loans to and investments in other companies under the same management or in the same group are severely restricted. During the first 10 months of 1960, 6,588 prosecutions were launched against 1,009 companies and their officers for infractions of the Company Law, and more than $50,000 in fines imposed. However, apparently no US affiliates were among the large number of companies that failed to comply with the Law. Firms that properly provide for the interests of their stockholders have little reason to anticipate interference from the Government.

Parsons & Whittemore has used a managing agency in which it holds a 50% interest to increase its control over a minority-owned plant.

What does concern US investors in the Company Law is the requirement that all directors be appointed with GOI approval (no man can be a director of more than 20 companies). Furthermore, maximum pay scales for directors and full-time company managers are established by the Law (now Rs. 10,000 per month for full-time managers, not including perquisites). The same person may not be managing director of more than two companies, nor may he be appointed for more than five years at a time. Top executives of global companies who are temporarily stationed in India are still exempted from this provision. A full-time director or managing director may not be paid more than 5% of net profits, nor may all full-time directors combined be paid over 10% of net profits (exceptions may be made with special approval).

The most important change in the Company Law was made in 1960, with the effective elimination of the private form of company for foreign investors. Any Indian concern partly owned by a publicly owned company, either Indian or foreign, is considered a public company. Since there are and will be few wholly owned foreign firms in India, virtually all Indian firms in which there is a foreign interest are now “public” companies. Each year a public company
PROFESSIONALISATION OF MANAGEMENT

By
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Joint Secretary

Department of Company Law Administration.

"The emergence of Management as an essential, a distinct and a leading institution is a pivotal event in social history. Rarely, if ever, has a new basic institution, a new leading group, emerged as fast as has Management since the turn of this century. Rarely in human history has a new institution proven indispensable so quickly; and even less often has a new institution arrived with so little opposition, so little disturbance, so little controversy."

This is what Peter R. Drucker wrote some years ago in his book ‘The Practice of Management’ while describing the role of Management. And, even if the estimate seems to be strong in somewhat superlative phrasing, it underlines the importance and significance of a factor in the corporate sector, which is vital for its very survival. The extra emphasis, if at all, may be justified on the score that not many people outside the ranks of sophisticated economic thinkers, or, ironically enough, hardheaded business practitioners, seem to be conscious of the manner in which the new economic order has seeped to the very roots of our existence, or of the many new calls which it makes on the community’s resources.

If Management is all that important, we need to know what it is, what factors have contributed to its emergence as a dynamic force, and what is being done to train it along the right lines.

What Management means?

What is Management is a question both easy and difficult to answer. A Manager is one who manages, as a leader is one who leads. There is a lot of school-boy sense in these simple definitions; only they do not tell enough and do not satisfy the studious analysts elaborate requirements. It may, therefore, be useful to consider what exactly constitutes management and what elements lie at the roots of this very complex institution.

Functions of Management:

Prof. George W. Robbins of the University of California, in a report submitted to our Government in December 1959, observed that Management could be viewed as a series of functions that are common to all economic enterprise leaders. One may classify them as Planning, Organising, Staffing, Supervising and Control. To some degree, all these functions are performed by all managers, regardless of the nature or setting of the enterprise or firm; and they are the heart of the Manager’s job.

The list of these functions may be chipped and chopped by different writers and there may be shift in emphasis. For instance, Rosemary Stewart introduced motivation as a basic ingredient; according to her, the Manager must be able to motivate or inspire his staff to contribute to the purposes of the organisation, to be loyal to its aims, and to pull their weight in achieving them. Drucker groups motivation with communication. He also prefers to use the word ‘measurement’ rather than ‘control’ which means that. It is not so much a matter of obeying orders as living up to certain standards of performance for which yardsticks must be clearly devised and laid. Some authors like Brech and Urwick like to add co-ordination as yet another function of the Manager though others feel that co-ordination is a thread which must pass through all functions of Management.
rather than be treated as a separate function by itself.

New concept of management:

It is not suggested, of course, that the list should be regarded as laying down the complete code for a Manager's task, or that different situations will not demand qualities of head and heart from this man—who must manage—which defy all definitions and burst all classifications. Bundling one's points in neat numbers and compact categories is an old human weakness, and offers a special temptation in a complicated world which hungers for simple solutions. There need be no facile assumption, therefore, that a complete answer can be found in the above enumeration. However, these functions indicate the many facets of Management. A Manager—even when he acts under the broad supervision of a Board of Directors—must plan—set objectives, forecast, analyse problems and make decisions. He must classify the work, divide it and assign it to groups and individuals. He must motivate and communicate—make a team out of the people who are responsible for various jobs. And he must check performance against plans. All this shows that the old-time concept of the Manager being just the 'boss with the big car' (and now of course, a pretty Secretary) is not enough. To quote Drucker again "The Manager has the task of creating a true whole that is larger than the sum of its parts, a productive entity that turns out more than the sum of the resources put into it. One analogy is the conductor of a symphony orchestra, through whose efforts, vision and leadership individual instrumental parts that are so much noise by themselves become the living whole of music. But the conductor has the composer's score; he is only interpreter. The manager is both composer and conductor."

In this connection, a reference to the elephant story is interesting as well as instructive. Each blind man, feeling only a portion of the elephant, equates it with the elephant itself and considers that it is what he has to cope with. Each departmental man, with similar limits on his vision, regards the problems of his department as the problems of the enterprise. It is the business of the true manager to see the problems in their entirety and in proper perspective, as a clear-sighted man would see the whole elephant. Manager—made, not born:

If such is the man who must manage where can we find him? Perhaps, nowhere. The perfect image exists only in imagination. But can we make him, or at least, his approximation? Can we put him through a course of studies which would be conducive to the development of these essential qualities? The answer to this must be in the affirmative.

Before this answer is elaborated, it is necessary to rid our minds of the 'intuitive Manager' idea. Many people still seem to believe that a good manager is something like a freak of nature, a kind of genius with a generous endowment of the sixth sense. He is a diviner, the correct hunchman, who is born rather than made. Not only this, they seem to think that he can hold all the reins together and run his chariot through a crowded street without such mundane aids as a regular course of study or a programme of training. The various complicated subjects which form the subject matter of seminars and symposia, curricula and courses are, according to them, meant for lesser men who need to employ their poorer faculties to produce low level and ordinary results.

Need for training:

There is no gain-saying that natural aptitude or high flare for a job, which may be
Why professionalisation?

The foremost among these factors is the increasing complexity of modern economic operations. A large-scale enterprise today has depth as well as dimensions. It is an intricate machine with many wheels in motion and a myriad cogs. It has many departments like production, marketing, budgetary control, human relations etc., each one of which is headed by a specialist. A manager must be equipped to have a vision larger than theirs. He must be able to bring an understanding to these specialisations, and yet remain layman enough not to be caught up in the grooves. The complexity of an enterprise is not confined to its own operations; it is linked in various visible and invisible ways with a host of other enterprises, even social systems, both within and outside the country. No individual, howsoever gifted, can properly comprehend all the complex factors in a large-scale enterprise unless he has passed through a sustained course of scientific studies which have sprouted round the subject.

It may be observed in this connection that the need, as always, is rapidly becoming the mother of invention, and in proportion to the advance of industry in a particular country, Management institutions have also been developing there. Thus, the United States can boast of the most advanced institutions for Business and Management training. This, in its own turn, becomes a factor leading to the inevitability of passing the managers through a regular course of training. Where a subject is treated as a science, no quack can be allowed to pass muster as a scientist.

Another factor is the enormous size of a modern enterprise—far beyond the resources of any individual. Consider, for example, the TISCO with a paid-up capital
of nearly forty crores and its assets amounting to over one hundred and fifty crores. It is supposed to be a Tata concern and, in many ways, it is so. And yet, all the money has not come from the Tatas. It has flown in from different directions, from hundreds and thousands of shareholders who are part investors, even if the myth of their being part-owners has been blown. These several investors run the risk of losing all the money invested by them. Even the limited liability concept does not protect them against the loss of their capital. Would they contract for a swim-or-sink proposition with people whom they have not even met, if they did not have faith in the organisation? And what does this faith in the organisation amount to? That they believe in the capacity and will of its managers to produce results which will be profitable to them and to the shareholders. Where a large number of unrelated persons enter a bond, contributing their moneys, but leaving the management in the hands of a few, the fiduciary aspect becomes inevitable. No one can be entrusted with a joint business venture unless the shareholders believe that its management is adequately equipped for the job. If the management sometimes still plays ducks and drakes with the shareholders' money, it is not the prodigal's or the profligate's way of doing things; nor even a case of nincompoopery. The reason: often enough, is that the management possesses the skills in abundance, but lacks the other indispensable quality of management—character and integrity.

Add to the size of the organisation, its life-span. A corporate body has no set period of life before it, it can live in perpetuity. In any case, its life may extend over many generations. It is, therefore, very different from a personal business whose life co-extends with that of its owner. There is, therefore, an inescapable need to build up an impersonal and objective organisation—one which would survive individual demises and failures. How else can it do so except by a team of competent and devoted managers, who, as an institution, are capable of absorbing all shocks, and of lending the quality of impersonal perpetuity to the organisation. In a way, the system has to be necessarily bureaucratic (a much misinterpreted and therefore much maligned term which has many virtues), and the success of bureaucracy, it may be said, rests with a cadre of interchangeable managers.

The number of enterprises requiring services of a sound cadre of top managers is increasing almost daily with phenomenal speed. The demands come not only from the private sector but also from the area of State activity. In a way, there is no leading country where, considering the funds employed in technological developments, the State does not have its finger—and often its big thumb—in the industrial pie. Not even the United States of America. The way giant companies, million and billion dollar corporations, crop up every now and then is remarkable. All of them need men who can manage. And these managers can be produced only through well-organised courses of study and education.

Enough has, I hope, been said about the factors which make it necessary to professionalise Management. The question we now face is whether the available facilities for such professionalisation are in step with the requirements.

Facilities:

In India, these facilities are still at the nascent stage as, indeed, they come generally in the wake rather than the vanguard of the first stage of industrialisation. That stage may be said to have been reached now and we can see distinct beginnings of Management education in India. Even more marked is the rapidly growing awareness of the need for such education.

Until recently, the work in this field was...
In this connection, I am tempted to make a special mention of a somewhat novel experiment in executive training which the Ahmedabad Institute has planned for the coming winter. It is to be a three-tiered relay programme for middle management, senior executives and the top management. The novelty is to be found in the fact that all the three levels will be drawn from the same organisation. The middle management will have a six-weeks’ course with emphasis on Management and decision-making in the functional fields of Business, Cost and Financial Control, Marketing and Production. The top management will have a seven-day seminar which will be attended by the senior executives who will then attend a seven-day seminar on the same subject. The middle management will then attend a seven-weeks’ course on the same subject which will be followed by a seven-day seminar on the same subject. The senior executives will then attend a seven-weeks’ course on the same subject which will be followed by a seven-day seminar on the same subject. The top management will then attend a seven-weeks’ course on the same subject which will be followed by a seven-day seminar on the same subject. This deficiency should be remedied when the two All India Institutes of Management at Calcutta and Ahmedabad, which were launched in 1961, set full sail. Their programme includes two years’ postgraduate professional education in Management subjects and comparatively short-term executive development residential courses. They are also expected to provide adequate library and research facilities and maintain a live contact with the realities of industrial world by taking a reasonable amount of consultancy work. The two Institutes have been fortunate in securing the technical collaboration of M.I.T. (for Calcutta) and of the Business School of Administration of Harvard (for Ahmedabad) and financial support from the Ford Foundation as well as from Industry and Government—both at the Central and State levels. The M.B.A. course, which is to commence next year. These Institutes will, therefore, be pioneers in preparing young men for full-fledged Management careers through regular post-graduate courses of study. The Institutes are presently engaged in recruiting and training faculty members, drawing up detailed programmes and curricula of the M.B.A. course, and, in the meanwhile, in organising some extremely useful executive development programmes.
Conclusion:
As in many other fields, our country is still toddling its first steps in the area of Management Training. The idea that a cadre of professional managers is essential for industrial expansion no less than technical equipment or other types of technical personnel, has already been sold. There is no doubt, therefore, that Management in this country will also get professionalised. However, it is important to remember that the 'man' in Manager will always come first. No amount of training will make a competent Manager of him if he lacks the essential qualities which go into the making of an intelligent man of character.
SOCIAL OBLIGATIONS OF THE CORPORATE SECTOR

BY
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One of the most striking features of recent times has been the phenomenal development of the corporate form of business organisation. The growth of joint stock enterprise has been so rapid and joint stock companies now cover so large an area of the industrial and commercial fields in the country's economy that their structure and mechanics have become a subject of great practical importance and public discussion. The operations of companies now embrace by far the largest part of the economic life of the community. The vast expense of this form of organisation is seen from the fact that it touches the individual at several points. As a producer of goods, as an investor or lender of surplus funds, as an employer or employee, and, above all, as a consumer of the goods produced, the individual is closely linked to the corporate sector. Perhaps it may not be an exaggeration to say that the welfare of the community is to a large extent conditioned by the manner in which the corporate sector in that country functions. This incidentally explains the powerful and abiding influence that the corporate sector has on the other fields of human activity.

Company as a purely commercial institution

Rapid though its own growth and influence has been, the evolution of the concept of obligations and duties of the corporate sector to the community at large has not been equally rapid or sudden. It is quite likely that at the earlier stages of the growth of joint stock enterprise none could visualize that this form of organization would have to assume enormous responsibilities. The accepted view then was that this form of organization could and should have nothing to do with the community as such except in so far as its economic activities were concerned. Justification for the existence of joint stock Companies was sought to be found in its ability to make profits which itself was based on two inter- connected traits of normal human-being viz., his acquisitive nature and love of private property. In short, so long as a company was able to satisfy the 'greedy little investor' with 'the appetising smell of promised dividends at rates which Shylock would have condemned' it was all right. Every other consideration was extraneous to it. Thus, essentially the Joint Stock Organisation was regarded as a purely commercial institution subserving a very limited purpose.

Profits not the sole object

Obviously, this absurdly narrow concept could not endure for long. In the context of expanding commerce and industry, political ideas and economic thinking underwent drastic changes. While all these forces contributed to the growth of the corporate sector, they also simultaneously brought about a fundamental change in the view regarding its content and meaning. No longer could this form of organisation claim to work in isolation. It influenced and was in turn influenced by political, economic and social ideas. No longer could it rest satisfied with enabling its protagonists to get rich quicker. As its sphere of activity and influence expanded so did its duties and obligations to the community. Social values altered so rapidly and basically that the narrow view taken of the Joint Stock Companies as merely an instrument for profit making became an anachronism.

Social welfare equally important

This is not to say that profit making was entirely given up or that it came to occupy a comparatively insignificant place. Far from it. Even to-day profit making is considered to be the basic and a legitimate
of what he terms the "general purposes" clause in addition to the object clause. He lists them as follows:

(a) The necessity of the corporation to be economically viable and to pay a reasonable return on its invested capital;
(b) The public interest, viz., the object of the company being to provide service or goods of the highest quality and lowest price commensurate with (a) above;
(c) The interest of employees, viz., to provide the best possible conditions of employment for workers in the corporation with reasonable opportunities for advancement and reasonable security for employment subject always to (a) and (b);
(d) In all matters in which companies activities affect the community to act as far as possible in the same manner as a responsible citizen could reasonably be expected to act in like circumstances.

Social Audit

Another novel feature envisaged by him is the provision for "social audit" along with the normal financial audit. The social audit, according to Goyder, is an obvious way by which the public may be informed of the manner in which a large business with a position bordering on monopoly is discharging its social responsibilities in the field of labour relations, pricing policies and local interests. According to him this "social" audit will be conducted by a special and competent party once in, say, every 3 years and will consist of a report to the Annual General Meeting of the way the company could discharge its new responsibilities. Apart from theoretical exposition of this view it is interesting to see that it has found sufficient recognition in legislation also. Taking for instance our Companies Act, we find that the importance of the corporate sector as an agency for promoting social well being is abundantly realised. Ours is a developing economy with planning as the

Advocates of social obligations

The view that the corporate sector has certain definite social obligations to discharge as part of its legitimate duty and as justification for its continuance has been advocated by many. In his absorbing book "The Responsible Company", George Goyder has made out a brilliant case in favour of what he calls a 'participating company' that is, in short, a company conscious of its responsibilities not only to the shareholders or directors but also conscious of the need to safeguard the interests of the investor, consumers and the community.

The author envisages the translation of this consciousness of the new found responsibility into concrete terms by the adoption
basis of development. We are committed to the achievement of a socialistic pattern of society and we aim to reach this goal by democratic means. Accordingly, our Constitution has laid down certain directive principles to serve as guiding factors for the evolution of any policy. One other consideration that has to be borne in mind in this connection is the time-factor combined with insufficient resources at our command to attain our end. Having regard to all these considerations mentioned above it is but natural that our company legislation, like all our other legislations, should aim at securing the maximum well being of the Nation. It is not necessary for the purpose of this article to go into the several provisions of the Act having a direct or indirect bearing on this aspect of the question. Suffice it to say, that in the context of things obtaining today, the Companies Act affords ample facilities to the corporate sector to fully discharge its social obligations to the community at large. Indeed the scope of the Act in this regard is very much wider than what is necessary.

**Social obligations—How discharged?**

We may now examine briefly the means by which or the manner in which the corporate sector can discharge its social obligations with particular reference to our own country. To me it appears that there are at least two ways in which this can be done. Firstly, the corporate organisation may in the process of its functioning itself promote social welfare; and secondly it can do so through the medium of resources—financial and otherwise—of which it gets command as a result of its functioning. In regard to the first method, it may be said that broadly speaking if the companies satisfy two or the general purposes caluses given above as envisaged by Mr. Goyder in regard to the labour employed and its consumer they may be said to have achieved substantial compliance. In other words this calls for an enlightened labour policy—a policy which regards labour as essentially human and invests them with certain individuality and dignity. In regard to the consumer it calls for an efficient system of production that ensures to the consumer quality goods at reasonable prices. The view should be that goods are produced because there are consumers and not that consumers are there because goods are produced.

The second way of dealing with this question consists in the corporate sector playing a positive role. It cannot be denied that it has at its command large resources. A good part of it may be utilised for fostering institutions which cater to the basic needs and amenities of our teeming millions, especially in the fields of education, medicine and the like. Corporate sector can no doubt take justifiable pride in having sponsored and nurtured several trusts foundations and the like, to advance education and to provide medical facilities. The beneficial utilisation of surplus funds available can go a long way particularly in an under developed country like ours in promoting the welfare of the masses.

Before concluding it may perhaps be necessary to touch upon one more aspect. Constructive development at times involves certain hardships which are not always avoidable. Industrialisation brings in its wake certain social and hygienic problems, the solutions to which are not always easy to find. It is here that one finds a fertile field for the corporate sector to discharge its social obligations. Firstly it can do this by not allowing the problems to multiply. Secondly, the corporate sector should devise urgent measures to solve these problems once they invariably do arise. A prudent and sagacious out-look coupled with careful planning in the matter of location of the industry, in the matter of discharge of waste products, and in the matter of hygienic designing of its premises should all contribute to the mitigation, it not complete elimination of the problems that generally vex
To conclude, it has now become an accepted fact that the corporate sector has to justify its existence not merely by its being productive and profitable, but at the same time by being generative of social well-being. Responsibilities of no mean order have developed on those who control the corporate sector. It is up to them to reconcile the apparently conflicting interests of the different parties involved. Again it is up to them to harness the increasing power and resources at the disposal of the corporate sector in such a way as to secure the greatest good of the greatest number. It has already been said that a company should act in all matters in which the company's activities affect the community as far as possible in the same manner as a responsible citizen can reasonably be expected to act in like circumstances. This guiding principle is worthy of being followed by the various units that go to constitute the corporate sector.
The Companies Act is a unique piece of legislation which not only regulates the administration of industry and trade in the corporate sector but helps the country in building up its national economy. It has dual functions—legal and social. In its social aspect, it attempts to build up a sound code of conduct for the management in relation to the society. It is, therefore, often said that the Companies Act has bridled unproductive venture of the management. The unsolicited encomium showered on the Companies Act does not, however, represent a view which is universal; there is a feeling in some quarters that the Government have taken too many and wide-ranging powers which often result in unnecessary interference with the normal working of corporate enterprises and thus hamper the growth of national economy in the country.

**Socio-economic objectives**

The traditional concept of Company Law that it is essentially a legal code for the formal systematization of the structure and mode of operation of a special type of economic institution and of a complete nexus of relationship which binds and holds together the different interests which enter into the formation and management of joint stock companies has undergone radical change in the present circumstances of our life, where in our Constitution, we have undertaken to build up a Welfare State and value human interest more than anything else. Apart from the knowledgeable circles in our country even foreign lawyers and academicians specializing in Indian Company and Income Tax Laws have expressed appreciation for the Annual reports prepared by the Department which enabled them to grasp the socio-economic meaning of the new Companies Act which was missing in the available contemporary treatises on the Indian Company Law.

**A real partnership**

"Shareholders are not, in the eyes of Law" says Lord Evershed "part owners of the undertaking. The undertaking is something different from the totality of its shareholdings". If this is accepted as true concept of joint stock companies in the legal theory, even the eminent lawyers must admit that the fundamental interest of joint stock companies is a matter of utmost concern not merely of shareholders but of the management but also of the entire community. This is not to deny the vital say of the shareholders in joint stock companies or their paramount responsibility for its good management, but underlines a fact which has been always implicit in the legal concept of a company joint stock company viz. that a company is essentially a partnership in the widest sense of the word between the promoters, organizers and shareholders and the wider community must be secured by the activities of the corporate organization in the equal manner as the interests of those who engage in production, distribution and marketing. Thus, the joint stock company represents in the present age of living, vital and dynamic social organism with a firm and deep rooted affiliations with the rest of the community in which it functions. These affiliations may not always be visible. The persons who are responsible 'to do' must also be aware of these affiliations and the significance of what they 'do'. It is
Average investor comes from the middle class who does not possess the necessary background of Company Law and Company Management.

Lack of time, money and experience to exercise control over the directors.

Widely spread number of shareholders, and

Lack of proper co-operation among the shareholders for want of proper organisation to ventilate their grievances.

It is always not possible for an individual shareholder to keep a constant watch on the activities of a company which might be situated at a place thousand miles away from him. It would be desirable that the companies educate their shareholders by giving sufficient information at intervals to enable them to decide whether they should keep on the investments or to switch over to another or to retain or remove the management. They should be treated neither as sheep nor as sacred cows.

Government is anxious that a shareholder
such cases, the concept of group management was being honoured by the managing agents more in its breach than its observance as these companies were not making available to the managed companies the services of their specialised personnel in the particular line of trade or manufacture in which the managed company was engaged. If the functions of the Managing Agents were limited to giving day-to-day advice to the officers of the managed companies and assist the Board in the taking of decisions on matters of policy, then the managing agent might be occupying the positions of management consultants, rather than managing agents in the accepted sense of the term. The Government also came across several cases in which the expenses debited to the profit and loss account of the managing agency companies were almost insignificant; the inference being that the managing agents were not incurring any expenditure themselves in connection with the management of the affairs of the managed company.

The Law cannot possibly lay down all the duties of the managing agents. The definition of managing agents in sub-Section (25) of Section 2 of the Act entitles the managing agents to the management of the whole or substantially the whole of the affairs of the company by virtue of an agreement with the company or by virtue of its memorandum or articles of association. The managing agents should however manage the affairs of the company to the extent and in the manner which will ensure correct balancing of interest among the partners and the management.

Let us take another illustration, say sales of a company. The point is whether organisation of sales of a company is a part of management. And if organisation of sales of the products of the company is a duty undertaken by the managing agents in terms of the managing agency agree-
Judicious use of the powers

Here it will be quite pertinent to mention that the Government have given an assurance in Parliament that the use of the powers under the provisions of the Act would be used judiciously. The then Finance Minister gave this assurance in the following words in the Lok Sabha during the discussions on the Companies Bill in 1955.

"The vesting of these powers of regulation in Government does not mean that they will be exercised or need to be exercised every now and then. While it may be true that uncontrolled power corrupts, it is no less true that the possession of power itself often obviates the necessity of its exercise. And that has been borne out by our experience of the working of the temporary amendment Act of 1951. I am not aware of any serious complaints having been made by the interests concerned either of delay or of harassment or of oppressive decisions."

There are about 98 Sections which deal with the powers of the Central Government under various circumstances. The provisions conferring such powers on the Central Government relate mostly to approval for change in name, modifications in form of balance sheet or a statement to be appended to accounts, grant of loans to directors, inter-company investments, appointment and fixation of remuneration of managerial personnel etc. That these powers for the Government are necessary to balance conflicting interests, can hardly be denied.
SOME REFLECTIONS ON CORPORATE MANAGEMENT

By

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The industrial and commercial wealth of a nation is to a large extent held and controlled by corporate enterprise, and hence the problem of corporate management is of utmost significance. Corporate management has at least three main aspects namely, legal, economic and social. The area being thus wide, the present article is just an attempt to arouse interest on the vast subject.

Main objectives

The main function of the corporate management is to control and regulate corporate enterprise which produces goods and services for the consumer and gives suitable return to the shareholders. While many a management expert opine that the motive of a company should not always be to maximise its profit, yet it can hardly be doubted that if a business is to survive and provide against future risks it must produce adequate profit. Thus it is one of the prime functions of a manager to see that the wealth producing capacity of the organisation is kept in trim. At the same time, the motto of those who deal with the corporate management should be, similar to that of the Harvard School of Business Administration, as stated by Prof. Adolph Berle Jr.—“Its main purpose has been and is to make the businessmen into professionals instead of privateersmen, and to make business the economic service of supply... instead of the simpler art of exploiting human need for private profit”.

Thus it is essential to have some sort of control on the dealings of corporate management, because important centres of private power are concentrated in a few hands. The responsibility of those who exercise this corporate power to the community is undefined and vague, and great vigilance is therefore required, by all those who participate, to see that the management acts in the best interests of all the participants of corporate structure namely Investors, Consumers, Employees and the Community at large. This conception would be apparent when we realise that the modern joint stock company is a social and economic institution and that it touches upon our habits of foods, health, education, employment, labour welfare, and sometimes even shaping of the governmental policy. In short, the modern society is one conditioned by the dictates of those who manage the means of production and distribution of goods, and services, to the community.

Organisation

In so far as the organisation of management is concerned, in the beginning, there was not much difference between the corporator and the manager, because shareholders were few and they not only owned but themselves managed and controlled the joint stock enterprise. But, industrial expansion has completely revolutionised the growth and structure, and so also the purpose of the joint stock enterprise. The expansion of industrial activity to meet the diverse needs of the modern age has made the shareholders a mere investor, separated physically and financially from the management as such. Hence, the need to have a well-defined and controlled corporate management structure to safeguard the interests of the various participants of the enterprise.

The internal division of the corporate management has three levels namely, Lower ministerial, Middle executive, and
Top managerial policy making. Corporate management, as is known generally, is a description of the Board of Directors as contemplated under the Company Law. Section 291 of the Companies Act, 1956 contemplates the Board of Directors as the supreme executive of the democratic conception of the joint stock company organisation. Appointment of directors to the Board differs in the procedure in the case of public, private and Government companies. The law in India recognizes some other managerial executive as well, managing director, managing agents, secretaries and treasurers, and manager. But our statute prohibits a multi-managerial executives for the management of joint stock company.

Outsider-Insider concept

In considering the organisation of management, one has also to see as to whether it is advantageous to have outsider or insider for holding the office of director. In view of the large scale of employment in the sphere of industrial management, a managerial class has already come into existence in India, and top men from this class are slowly turning out to be professional directors. It has even been found that some of the big enterprises have the services of specialist executives; but how far such specialists can be good policy makers, sitting on the Board of Directors, is still too early to predict. There are some companies, which have appointed top executives on their Boards, the knowledgeable circles however opine that a specialist should be an adviser, and not a manager. On this aspect the following observations of Sir Walter Puckey are of great interest to us. He says, "There is a slight trend today towards the promotion of specialists within the company to chief executive and Board membership, thus giving recognition to the possibility that specialists can in fact become generalists, and very successful ones too. Some Boards hold the view that if the main function of the company is, say, engineering, then an engineer should hold the top job. Rolls Royce is (or was) such a company. Another company, such as I.C.I., might well say that as the principal products of the company are chemical goods, then chemist should be at the head. One difficulty with this approach is that in these days of diversification and take over exercises, an engineering company may become a non-engineering company, or vice-versa." He further adds, as his considered opinion on this question, that "As one who has had a pretty varied experience of Board membership, both as a so-called executive and as a non-executive Director, I state with complete conviction my view that every Board should have a reasonable balance between the two. Let me first comment on titles. Many Directors describe themselves in what I believe to be incorrect terms. Directors as such have special responsibilities as members of a Board. They have legal and general obligations which have little or nothing to do with the executive duties they may perform in the organisation. As Directors, too, they have Board policy-making responsibilities which arise out of departmental duties; in fact, situations often occur where someone wearing his Director's top hat may wish, objectively, to oppose a plan which, wearing his Manager's bowler hat, he might subjectively support. Director's titles should emphasize this difference in outlook, and it might be better, as some companies do, to describe a person as Director and Sales Manager, rather than Sales Director. There really is no such animal as the latter": Many other management experts have also expressed views to the same effect. Thus according to the western experience, best type of management organisation is the one with a majority persons who are not whole time servants of the company, as chief executive etc.,
but persons, who have sufficient knowledge and business acumen, who can lay down policy for the executives to carry on. This will not be achieved if the majority of the members of the Board of Directors is composed of the servants of the company. Whatever may be the western experience, our Company Law is not an impediment in the way of a portion of the Board being composed of specialist executives.

**Trust, Skill and Care**

In so far as the duties, rights and fiduciary responsibilities of the management are concerned, they extend to the company, its shareholders, employees, customers, creditors, to the community and the State as well. In order to faithfully discharge their duties, the directors are expected to devote great care and skill in the affairs of the company. The duty to exercise care and skill was first propounded in well defined terms by Mr. Justice Romer in his judgment in *City Equitable Fire Insurance Co. Ltd.* Position has further advanced and to-day, it is almost recognised in the light of the subsequent judicial decisions, Indian, English and American that the board of directors collectively and the directors individually, is a Trustee for the various participants of the corporate entity. That being the modern view, the director’s fiduciary responsibility “affects every action he takes as a director. He is trusted by the shareholders to manage their investment; he is trusted by the employees to ensure, as far as he is able, their security; he is trusted by the company’s creditors; he is trusted by his fellow directors. Break that trust to any one of this number and he has compromised himself and worse he will almost certainly have compromised the company. That is why it is vital that every director of every company, public or private, great or small, should realise the full implications of this duty. It is an essential part of the fabric of the joint stock company. Any director who infringes this principle damages the system by which he exists. It is an extremely serious matter: A man who takes on a directorship without realising the trust which the office automatically implies may sometimes be knave, but he is always a fool”. The directors who are the top managers, should therefore devote reasonable time and attention to the business of the company.

**Corporate purpose**

Another important function of the corporate management is to fully understand the purpose, which they have to serve. Every company has its basic documents of incorporation. These documents define and delimit, in a general way, the objects, the powers and the regulatory provisions governing the corporate entity, so as to give the necessary legal guidance to the management. Undoubtedly, it is the duty of the managerial personnel to study the constitutional records, but it is no secret that, these basic documents are rarely consulted by top managers, unless unavoidable circumstances demand. However, even if the memorandum and articles are read, the real purpose of the company will not be fully found, as the purpose visualised in the context is the very aim of the company’s existence in the society. It may not, perhaps, be easy to express such a social purpose in a document executed to satisfy legal requirements of incorporation. It is this social aim conceived within the formal statement of objects, which the management should realise. In order to have this comprehension, as stated by Peter Drucker, in his book “The Practice of Management,” “the first responsibility of top management is to ask the question “what is our business”. In this view, every company director should ensure to ask this query when he accepts the office, and endeavour to understand the objectives and aspirations...
of the company, and then ponder over the standard of performance expected of him for the achievement of these aims.

There is no gainsaying the fact that corporate management should show fidelity to the interests of the company and thus keep the best of relations with the shareholders, creditors, employees and customers. On this score, the management should be guided by the following essential principles:

**Essential Principles and tests**

1. Utilise the profits and corporate funds of the company as required by the law and the company's regulations;
2. Corporate power vested in the management should be used for the purpose for which it has been vested and not others;
3. The distinction should always be kept between the personal interest of the individual directors and that of the company and in case of conflict, it should be disclosed; and
4. The administrative, trading and financial information of the enterprise should not be misused for the personal gain, or trade in these inside information, in self-interests.

It should always be borne in mind that the management is dealing with other people's money. Corporate acts and dealings with corporate funds have, therefore, to be tested to see whether the technical rule governing the matter under this statute, memorandum and articles of association have been complied with, and whether equitable rules analogous to those available to a *cestui que trust* to the trustees' exercise of the powers have been borne in mind? Unless corporate acts pass these essential tests, it would not be deemed that the managerial responsibilities have been honestly discharged.
NEED FOR A CODE OF CONDUCT FOR COMPANY DIRECTORS

By

V. SATYAMURTI, I. R. S.
Deputy Secretary

It is no truism to say that the burden cast on the administration by the need to oversee and supervise the working of the corporate sector could be greatly lightened if there were to be a greater awareness of their responsibilities on the part of company directors. Thanks to the assimilation over a century or so of the principles of Anglo-Saxon law by trade and industry, there is no doubt some realisation of the fiduciary obligations of directors to the shareholders of a company. This realisation was in fact responsible for the willing acceptance of certain salutary principles laid down by the Companies Act, 1956 which regulate the conduct and behaviour pattern of corporate management. But the need still remains for directors of public companies as a class to lay down for themselves a code of conduct which not only takes into account their fiduciary responsibilities to the shareholders but also their wider obligations to the employee, the consumer, the community and the State—obligations which are being increasingly emphasised and stressed by distinguished thinkers on the subject. In fact, in recent times, a new image of the corporate enterprise has emerged, an image of a social organism which has not only a vital role to play in the economic life of the country, but has a significant influence on the social life as well.

Community of interest.

As Justice Douglas, a former Chairman of the Securities Exchange Commission of America, observed, "Today it is generally recognised that all corporations possess an element of public interest. A corporation director must think not only of the stockholders but also of the labourer, the supplier, the purchaser and the ultimate consumer. Our economy is but a chain which can be no stronger than any one of its links; we all stand together or fall together in our highly industrialised society of today. One function of the good director is to harmonise these various elements as far as possible. For, although these elements may superficially appear to conflict, the fundamental interests of all social groups are identical over the long term."

And Peter Drucker, the distinguished expert on management states: "No discussion on the practice of management can leave out those functions and responsibilities of management that arise out of the social character and public existence of even the most private of enterprises.... The public responsibility of the management must underlie all its behaviour. Basically, it furnishes the ethics of management."

Nature of obligations:

What then are these obligations and how is a code of conduct to be drawn up? It is difficult either to be precise or to be exhaustive on this point. Judicial decisions in U.K. and America, especially in the latter country, have time and again been making references to the high and lofty traditions of thought and behaviour that company directors should set up. The trusteeship concept of a director has become part of the law of the land in all progressive countries and the need for utmost disclosure to the shareholders of the financial and other relevant aspects of management through properly drawn up statements has been recognised in the corporation laws of all these countries. While strict and honest compliance with these laws would automatically ensure in most of
Obligations:

In all these, as observed earlier, it is not the legal requirements that are listed out but what might be called the moral obligations, which are beyond the pale of statutory law but which are enjoined by a higher law seeking to sustain the lofty traditions of trusteeship which a director by virtue of the high office he holds is bound to observe. The very recognition of the need to obey such a higher law would render observance of the statutory restriction a mere child’s play and if such a recognition were to become universal, there would be no need to spell out in detail what the obligations of the directors to the shareholder, the consumer and the community are, and in any case, as observed by the Jenkin’s Committee, “any such attempt to define the duties of directors more clearly would involve the risk that since it would be impossible to define such duties exhaustively there would be inevitable lacunae which might well make it more difficult in any particular set of circumstances what these duties were”.

It is, therefore, of paramount importance that the more enlightened among the company directors in this country should set certain commercial transactions. It lays down what his relations in general should be with the shareholder, the employee, the customer and the creditor. It prescribes a course of action which should invariably be followed by directors in all cases of takeover bids and recommends strict adherence to what are known as ‘The Queensberry Rules’ designed to keep the entire transaction above suspicion. It seeks to define the duties and responsibilities of the various types of directors, the managing director, the executive director, the outside or part-time director etc. and recommends the line that should be adopted by them in regard to matters affecting their remuneration and other benefits, including expense account operation.

The British Pattern:

Nor is it a difficult task to evolve such a code of conduct for company directors. The British Institute of Directors has brought out two books, one on the legal responsibilities of directors, which is of great use to this class of persons enabling them to steer clear of the pitfalls created by law and avoid the wrath of the courts for any act of commission or omission on their part. It is, however, in bringing out its companion volume under the title “Standard Board Room Practice” that the British Institute of Directors has rendered a distinct service to corporate management, as this book provides guidance to directors in regard to matters which are not subject to any legislative restraints but which have a direct bearing on their fiduciary relationship to the shareholders. In effect, it enjoins on them to observe a code of conduct in regard to these matters, not because such conduct is required by law, but because dictates of honesty, decency, moral sense and good conscience require adherence to such a code conduct. For ought I know a similar publication might have come out in America too.

This book prescribes what a director should do and what he should not do in certain circumstances and in regard to certain commercial transactions. It lays down what his relations in general should be with the shareholder, the employee, the customer and the creditor. It prescribes a course of action which should invariably be followed by directors in all cases of takeover bids and recommends strict adherence to what are known as ‘The Queensberry Rules’ designed to keep the entire transaction above suspicion. It seeks to define the duties and responsibilities of the various types of directors, the managing director, the executive director, the outside or part-time director etc. and recommends the line that should be adopted by them in regard to matters affecting their remuneration and other benefits, including expense account operation.

Moral obligations:

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about to evolve a code of conduct for themselves somewhat on the lines of what has been done in the U.K. and do their utmost to secure strict adherence to it. Thus alone can they keep in tune with progressive thought on this subject and also keep abreast of the times, a requirement rendered necessary not only in their own interest, but in the interests of our national well-being and economic prosperity which require a strong and stable corporate sector in this country, based on certain sound and well-defined moral principles and functioning in a healthy and virile manner. The spotlight turned on the behaviour of the corporate sector in recent times underlines the urgency for such action if public opinion is not to be irrevocably alienated because of the unsocial practices of the unscrupulous among company managements.
INTERLOCKING OF DIRECTORSHIPS BETWEEN BANKING AND OTHER COMPANIES

By
DR. RAJ K. NIGAM
Director of Research & Statistics

Following up the all-India Survey of Company Directorship pertaining to big-sized companies completed in 1961, a study of the interlocking of directorships in marketing and manufacturing companies was made in 1963 jointly by the author and one of his colleagues. Now, we extend the study on this subject to the interlocking of directorships between banking and other companies in our country. The purpose of this study is to find out the extent of close relationship of banks with other corporate bodies through common directors. Over the years, as a result of the growth of banking industry in the country and of the growth of the financial needs of the corporate enterprises consequent on the enlargement of their size and diversification of their activities which in turn led to diffusion of ownership and centralised control in a few hands, a close inter-relation has come to exist between the banks and other corporate enterprises. Not only this, other financial institutions like the investment trusts insurance Companies etc. which garner the savings of the community have also acquired significant importance in the corporate sphere. Apart from acting as important sources of supply of funds, banks and financial institutions including insurance companies or corporations have emerged as big institutional investors in the joint stock companies wielding greater power and influence as a more organised and cohesive group than the 'individual investors'. The banks, as yet are not quite "risk-capital minded" but nevertheless they invest in shares of corporate bodies and wield decision-making power on behalf of their clients. With the emergence of this phenomenon, there has been a shift in 'power situation'. As Berle says, "in terms of law, nothing apparently has changed. The corporation is still the familiar corporation. The stockholder is still the stockholder. His rights are the same as before. His vote is still a vote. The new element is that the shareholders' votes have now been more or less permanently concentrated in a relatively small number of institutions—pension trusts and (to a far less extent) insurance companies and mutual funds. This means that the nuclei of power have emerged so constructed that they cannot be readily challenged or changed."

In this connection, another phenomenon now noticed in the country is that some of the leading business groups have either their own banks, insurance companies or investment trusts ostensibly formed to make use of the pool of funds collected by them from the various sections of the society. This is of course not to suggest that any misuse of funds necessarily follows such arrangements. The advantage accruing from such financial institutions in their lap is that the needs of the various constituents of a group are met conveniently and possibly they enjoy a priority over those of other bodies as well. Here too, there are no clear indications to suggest that any high degree of integration of 'finance and credit with 'production and trade' has taken place within the group.

Notes 1. For earlier studies the attention of the readers is invited to the book "The Pattern of Company Directorships in India (Second Enlarged Edition) by Raj K. Nigam and N. D. Joshi published by the Department of Company Law Administration.

2. The author was assisted in the preparation of this article by P. D. Sharma, Investigating Officer in the Research & Statistics Division of the Department.
Position of banking companies vis-a-vis corporate sector:

In India today, according to the latest available statistical data for 1961, there were 304 banks in the country whose paid-up capital aggregated Rs. 40 crores. Excluding the State Bank of India and its subsidiaries, the numbers of banks and their paid up capital were 295 and Rs. 30 crores. As against this, the number of banks in 1951 was 398 and their paid up capital Rs. 39 crores. Excluding the Imperial Bank of India, the number of banks came to 397 and their total paid up capital to Rs. 34 crores. Going still further back to the beginning of the century itself, in respect of which only the combined figures of banks and other financial companies are available, there were 407 such companies with a total paid up capital of Rs. 4 crores. Over the last 60 years, there has been a ten-fold increase in the paid up capital of banks while in comparison to that, their number has not increased much. In between the period 1900 and 1961, the number of banks increased very impressively particularly during the period of the Wars. Later, the process of compulsory mergers started. Many banks small in size also switched on to activities other than banking on the revocation of their licences by the Reserve Bank of India under the Banking Companies Act as a result of the banks being found not satisfying the conditions prescribed by law and by the Reserve Bank. Apart from the disappearance of the small banks, the leaders of the banking sector acquired enormous size during the last two decades and the result of these trends was that there was concentration in the banking sector in the country. However in juxtaposition with the above statistics relating to banks, if we see the growth of the other joint stock companies, we find that their number increased from about 900 to about 26,000 in 1961 and their paid up capital from Rs. 31 crores to nearly Rs. 1,250 crores. The figures for 1961 however exclude Government companies. It is thus seen that the number of companies other than banking companies increased nearly 30 times and their paid up capital by 40 times. During the decade 1951—61, the total capital and reserves of the banks in the country increased from Rs. 69 crores to Rs. 81 crores whereas their total deposits rose from Rs. 974 crores to Rs. 2,125 crores. During the same period, loans and advances made by them to industry increased from Rs. 194 crores to Rs. 669 crores. The total loans and advances during 1961 amounted to Rs. 1,302 crores as against Rs. 581 crores in 1951. Total paid up capital and reserves of the banks excluding the State Bank of India and its subsidiaries in 1961 aggregated Rs. 60 crores whereas total deposits of Banks excluding State Bank of India and its subsidiaries came to Rs. 1,464 crores. The total amount of capital and reserves of the first five biggest banks in the country excluding the State Bank of India, viz., the Punjab National Bank, the Bank of India, the Bank of Baroda, the Central Bank of India and the United Commercial Bank amounted to Rs. 25 crores in 1961 as against Rs. 20 crores in 1951. Their total deposits were Rs. 697 crores in 1961 as against Rs. 296 crores in 1951. The total loans and advances given by them in these years were respectively Rs. 491 crores and Rs. 165 crores.

Coverage:

The coverage of the present study is of 20 leading banks in the banking spheres of the corporate sector selected on the basis of their total deposits and total assets. The total paid up capital and reserves of these 20 banks aggregated Rs. 41 crores while their total deposits came to Rs. 1,034 crores in 1961. The proportion of their total capital and reserves, and deposits to the corresponding heads for the entire private banking sector works out to 68% and 71% respectively. Thus, our study has a nearly 3/4 coverage of the private banking sector. Apart from studying the interlocking of
directorships between these banks and other companies, an attempt has been made in this study to assess the position relating to the inter-connection of the first five biggest banks and other bodies in the corporate sector. The last part of the study studies also the interlocking of directorships between 14 financial institutions viz., the Life Insurance Corporation of India, the Industrial Credit and Investment Corporation of India, the National Industrial Development Corporation, Refinance Corporation of India, the Industrial Finance Corporation of India, the Film Finance Corporation and the State Bank of India with its seven subsidiaries. The details for the eighth subsidiary i.e. State Bank of Travancore, of the State Bank of India were, however, not available to us for our study.

Restrictions on appointment of directors:

Before we come to the discussion of the interlocks of directorships in banks and other joint stock companies, it may be mentioned here that like the Companies Act, 1956, the appointment of managing directors and directors under the Banking Companies Act, 1949 also is governed by certain stringent conditions. Firstly, Section 16(1)(c) of the Banking Companies Act, 1949, says that no banking company shall be managed by a person who is a director of any other company not being a subsidiary of a banking company or a company registered under Section 25 of the Companies Act, 1956. Secondly, no banking company shall be managed by any person who is engaged in any other business or vocation and thirdly, it shall not be managed by a person who has a contract with a company for its management for a period exceeding five years at any one time.

As regards the directors, Section 16 of the Banking Companies Act says that no banking company formed in India shall have as a director any person who is a director of any other banking company or of companies which among themselves are entitled to exercise the voting rights in excess of 20% of the total voting rights of all the shareholders of the banking company. The rationale behind the provisions of Section 10 of the Act is that the Managing Director or General Manager of a banking company is expected to give his full time attention to the bank and as such cannot be expected to undertake any extra burden of work on himself. The reasoning behind the provisions of Sec. 16 of the Act is somewhat different from the above insofar as these restrain the director of a banking company to serve as such on any other banking company. This aims at checking the forging of inter-bank links through common directorships which could result in concentration of economic power in the hands of a few people or business groups through the use of funds of more than one banking company.

The only relaxation which the Reserve Bank allows in the case of a General Manager or the Managing Director of a banking company is that they can be appointed as directors of other banking companies under certain special circumstances such as when a particular bank has advanced huge loans to another bank which require to be duly protected. In the case of directors when the new restrictions imposed upon their appointment under the provisions of Sec. 16(1) of the Act came into force consequent on the passing of the Banking Companies (Amendment) Act, 1956, the persons who were acting as directors of more than one banking company were given the option to retain any one directorship and resign the rest and where the restrictions imposed under clause (ii) of sub-section (1) of Section 16 were applicable, they were given the option to choose such number of companies as among themselves would not be entitled to exercise
Forms of inter-connection:
The inter-connection between the banking companies and other corporate bodies and institutions arises under four principal situations. Firstly, by virtue of huge blocks of shareholdings in the corporate bodies, either on their own or as nominees of their clients, the banks secure the right to put their own men on the latter’s boards of directors. Secondly, very often long-term credit supplying banks secure a right to nominate some directors on the companies’ boards for protecting their interests. This is done through the signing of an agreement with the debtor-company. Even among the Government financial institutions like the Industrial Finance Corporation of India and the state financial corporations, it is a prevalent practice and in fact, there is an express provision in regard to that in their respective laws. Thirdly, sometimes the bank management invite directors of other companies to serve on the boards of their banks, which is, among various reasons, for bringing prestige to the bank or creating confidence among the public or establishing close connections with other prominent business houses for business reasons etc. Fourthly, when some companies enter upon a greatly increased scale of operation which they cannot finance themselves or even if they can, wish to ensure themselves of financial help in case of need as also win the confidence of the public as ‘sound propositions’, they join up with some financial institution or group and invite their directors on their boards.

Extent of inter-locking:
(i) between leading banks and other companies:
According to our survey of directorships of the twenty banking companies whose names are given elsewhere in this article, depicting the position as at the end of the year 1961, a total of 188 persons served as directors on the boards of these 20 banks covered in the study. The total number of directorships held by these 188 persons in the banks and other companies aggregated 1,640. Excluding the 188 directorships held by them in the 20 banks, their total directorships in the other non-banking corporate sector and other institutions including co-operative banks is seen to be 1,452. The total number of companies including the banks on the boards of which the 188 persons served as directors, was 1,309 (of which 20 were banks and the rest, other companies). The 1,289 companies apart from including joint stock companies both public and private, independent private companies as well as private companies which are subsidiary of public companies, also cover non-profit making associations and co-operative institutions registered under the Co-operative Societies Act. After removing the duplications among companies the number of companies (including 20 Banks) with which the 188 Bank Directors were connected came to 1120, and without the banks the number was 1100. This study of directorships therefore, relates to corporate bodies engaged in profit-making activities as well as others which are either engaged in non-profit making activities or co-operative institutions. It is for this reason that the average calculations made in this paper should not strictly be related to the provisions of Section 275 of the Companies Act which permits the holding of a maximum of 20 directorships only by a person. As far as the banking sector is concerned, the situation of multiple directorships does not arise in view of the provisions of Sections 70 and 16 of the Banking Companies Act. The average number of directorships held by these 188 directors works out as 9; excluding the directorships held in the banks, the average comes to 8. In com-
comparison to the average of 6.5 directorships held by a director belonging to the big-size companies as revealed in our previous study on the subject, the average directorship of the 188 directors serving on the 20 banks is found to be higher. Also the average holding of directorships of the 'bank directors' in India works out higher than that of the directors of the big tea banks of the U.K. According to a survey made in the U.K. in 1957, the total number of directors of the 10 leading banks, viz., Barclay Bank, Midland Bank, Westminister Bank, Lloyds Bank, National Provincial Bank, Martins Bank, District Bank, Cly Bank, William Deacon's Bank and Royal Bank of Scotland, was 235 and they among themselves held 1982 directorships of which 355 were in the banks and 1647 in other companies. The average directorships held by the directors thus worked out as 8 in all and 7, excluding the directorships in the banks.

Size of the Board:

The total number of directors serving on the boards of directors of the 20 banks covered in the study aggregated 188, the average size of the board in the banking sector being 9 directors. The size of the board varied between 4 directors and 13 directors. Ten banks had a board of ten directors or more each, whereas 8 banks had boards of 6 to 9 directors each. Of the remaining two, one had four and the other five directors. The average size of the board of directors of the banks is found to be bigger than that for the big-sized companies having paid up capital of Rs. 50 lakhs and above noticed in a previous study on the subject.

A study of the frequency distribution of directorships held by the bank directors discloses that about 12.8% of them held one directorship, whereas 12.2% held more than 20 directorships. It is further seen that 55.3% of directors held between 2 to 10 directorships, 19.7% between 11 and 20 directorships. The distribution pattern in terms of total directorships held by the directors is that 1.4% were single directorships, 31.9% multiple directorships ranging between 2 to 10, 32.2% multiple directorships ranging between 11 to 20 and 34.5%, more than 20 directorships. A comparison of the frequency distribution of directorships held by bank directors with those studied for the directors of big-sized companies and of the directors belonging to marketing companies discloses that the phenomenon of multiple directorships was more marked among the bank directors, notwithstanding the fact that within the banking sector they could not hold more than one directorship subject to certain exemptions. The following Table brings out the comparative position of the frequency distribution of directorships in respect of the three groups of companies.

### TABLE 1

FREQUENCY DISTRIBUTION OF DIRECTORSHIPS OF THE DIRECTORS OF THE 20 BANKS COVERED IN THE STUDY

<table>
<thead>
<tr>
<th>No. of directorships</th>
<th>No. of persons holding the directorships</th>
<th>Percentage</th>
<th>Total directorships</th>
<th>Perentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>24</td>
<td>12.8</td>
<td>24</td>
<td>1.4</td>
</tr>
<tr>
<td>2-10</td>
<td>104</td>
<td>55.5</td>
<td>528</td>
<td>31.9</td>
</tr>
<tr>
<td>11-20</td>
<td>37</td>
<td>19.7</td>
<td>527</td>
<td>32.2</td>
</tr>
<tr>
<td>21 and above</td>
<td>23</td>
<td>12.2</td>
<td>566</td>
<td>34.5</td>
</tr>
<tr>
<td></td>
<td>188</td>
<td>100.0</td>
<td>1640</td>
<td>100.0</td>
</tr>
</tbody>
</table>

31
### TABLE 2

**FREQUENCY DISTRIBUTION OF DIRECTORSHIPS HELD BY DIRECTORS OF LARGE COMPANIES**

<table>
<thead>
<tr>
<th>No. of directorships</th>
<th>No. of persons holding the directorships</th>
<th>Percentage</th>
<th>Total directorships held</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>399</td>
<td>26.6</td>
<td>399</td>
<td>4.0</td>
</tr>
<tr>
<td>2—10</td>
<td>799</td>
<td>53.2</td>
<td>3963</td>
<td>49.5</td>
</tr>
<tr>
<td>11—20</td>
<td>217</td>
<td>14.4</td>
<td>3196</td>
<td>32.7</td>
</tr>
<tr>
<td>21 and above</td>
<td>87</td>
<td>5.8</td>
<td>2227</td>
<td>22.8</td>
</tr>
<tr>
<td>Total</td>
<td>1302*</td>
<td>100.0</td>
<td>9785</td>
<td>100.0</td>
</tr>
</tbody>
</table>

*This includes a few duplication of names also.

### TABLE 3

**FREQUENCY DISTRIBUTION OF DIRECTORSHIPS HELD BY DIRECTORS OF MARKETING COMPANIES**

<table>
<thead>
<tr>
<th>No. of directorships</th>
<th>No. of persons holding the directorships</th>
<th>Percentage</th>
<th>Total directorships held</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>101</td>
<td>32.1</td>
<td>101</td>
<td>6.5</td>
</tr>
<tr>
<td>2—10</td>
<td>175</td>
<td>55.6</td>
<td>789</td>
<td>51.0</td>
</tr>
<tr>
<td>11—20</td>
<td>25</td>
<td>7.9</td>
<td>355</td>
<td>23.0</td>
</tr>
<tr>
<td>21 and above</td>
<td>14</td>
<td>4.4</td>
<td>302</td>
<td>19.5</td>
</tr>
<tr>
<td>Total</td>
<td>315*</td>
<td>100.0</td>
<td>1547</td>
<td>100.0</td>
</tr>
</tbody>
</table>

*This includes a few duplication of names also.
Interlinking of companies through common directors:

The following Table 4 presents the picture of interlinking of companies through one or more bank directors. It is seen that of the total of 1289 companies other than banks which are connected with the 20 banks through common directors, 121 companies are connected through more than one director, accounting for, among themselves, a total of 282 directorships. It is seen that 88 companies were connected through two directors, 25 companies through three directors, 7 companies through four directors and one company through 5 directors. The remaining, 1168 companies excluding the banks were interlinked with the banks through one common director.

**Table 4**

<table>
<thead>
<tr>
<th>Name of the bank</th>
<th>Number of companies connected through</th>
<th>Total directorships held</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>One dr.</td>
<td>Two drs.</td>
</tr>
<tr>
<td>1. Andhra Bank</td>
<td>30</td>
<td>1</td>
</tr>
<tr>
<td>2. Bank of Baroda</td>
<td>172</td>
<td>11</td>
</tr>
<tr>
<td>3. Bank of Bihar</td>
<td>31</td>
<td>2</td>
</tr>
<tr>
<td>4. Canara Bank</td>
<td>20</td>
<td>4</td>
</tr>
<tr>
<td>5. Bank of India</td>
<td>151</td>
<td>9</td>
</tr>
<tr>
<td>6. Bank of Madura</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>7. Bank of Maharashtra</td>
<td>58</td>
<td>4</td>
</tr>
<tr>
<td>8. Bank of Rajasthan</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>9. Canara Banking Corp.</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>10. Canara Industrial and Banking Syndicate</td>
<td>11</td>
<td>3</td>
</tr>
<tr>
<td>11. Central Bank of India</td>
<td>87</td>
<td>9</td>
</tr>
<tr>
<td>12. Devkaran Naaji  Banking Company</td>
<td>32</td>
<td>3</td>
</tr>
<tr>
<td>13. Hindustan Commercial Bank</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td>14. Indian Bank</td>
<td>38</td>
<td>3</td>
</tr>
<tr>
<td>15. Indian Overseas Bank</td>
<td>40</td>
<td>4</td>
</tr>
<tr>
<td>16. Oriental Bank of Commerce</td>
<td>38</td>
<td>14</td>
</tr>
<tr>
<td>17. Punjab National Bank</td>
<td>61</td>
<td>2</td>
</tr>
<tr>
<td>18. Union Bank of India</td>
<td>104</td>
<td>3</td>
</tr>
<tr>
<td>19. United Bank of India</td>
<td>116</td>
<td>11</td>
</tr>
<tr>
<td>20. United Commercial Bank</td>
<td>134</td>
<td>5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>1168</td>
<td>88</td>
</tr>
</tbody>
</table>
The Frequency distribution of Directors:

The Frequency distribution of Directors of 20 leading banks according to their directorships in companies is shown in Table 5 below. A study of the Table would reveal that of the 188 directors, 24 directors did not hold any directorships in companies other than the banks. As against this, sixty directors held directorships in ten and more companies each. Eighteen directors held directorships in one company each, 43 directors between two and four companies and an equal number between five and nine companies. It is thus seen that 87% of the directors held multiple directorships and the rest were merely the bank directors.

### TABLE 5

**FREQUENCY DISTRIBUTION OF DIRECTORS OF 20 BANKS ACCORDING TO THEIR DIRECTORSHIPS IN OTHER COMPANIES**

<table>
<thead>
<tr>
<th>Name of the Bank</th>
<th>Number of directors who held directorships in</th>
<th>Total directors</th>
<th>Total directorships</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>no other company</td>
<td>One co.</td>
<td>2-4 cos.</td>
</tr>
<tr>
<td>1. Andhra Bank</td>
<td>2</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>2. Bank of Baroda</td>
<td>3</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>3. Bank of Bihar</td>
<td>3</td>
<td>..</td>
<td>2</td>
</tr>
<tr>
<td>4. Canara Bank</td>
<td>3</td>
<td>..</td>
<td>3</td>
</tr>
<tr>
<td>5. Bank of India</td>
<td>..</td>
<td>3</td>
<td>..</td>
</tr>
<tr>
<td>6. Bank of Madura</td>
<td>..</td>
<td>3</td>
<td>..</td>
</tr>
<tr>
<td>7. Bank of Maharashtra</td>
<td>1</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>8. Bank of Rajasthan</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>9. Canara Banking Corporation</td>
<td>4</td>
<td>..</td>
<td>3</td>
</tr>
<tr>
<td>10. Canara Industrial and Banking Syndicate</td>
<td>2</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>11. Central Bank of India</td>
<td>..</td>
<td>1</td>
<td>..</td>
</tr>
<tr>
<td>12. Devkaran Nanjee Banking Company</td>
<td>2</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>13. Hindustan Commercial Bank</td>
<td>1</td>
<td>..</td>
<td>2</td>
</tr>
<tr>
<td>14. Indian Bank</td>
<td>1</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>15. Indian Overseas Bank</td>
<td>..</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>16. Oriental Bank of Commerce</td>
<td>2</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>17. Punjab National Bank</td>
<td>..</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>18. Union Bank of India</td>
<td>1</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>19. United Bank of India</td>
<td>..</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>20. United Commercial Bank</td>
<td>..</td>
<td>..</td>
<td>2</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>24</td>
<td>18</td>
<td>43</td>
</tr>
</tbody>
</table>
The following Table 6 presents the distribution pattern of directorships held by the bank directors in other companies classified according to their activities. The companies have been classified into four major groups, viz., financial companies, manufacturing and other companies, trading companies and associations not for profit.

### Table 6
**DISTRIBUTION PATTERN OF DIRECTORSHIPS HELD IN OTHER COMPANIES BY THE BANK DIRECTORS**

<table>
<thead>
<tr>
<th>Name of the Bank</th>
<th>Number of directors</th>
<th>Number of companies held in other companies classified under major groups, viz., financial companies, manufacturing and other companies, trading companies and associations not for profit.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Andhra Bank</td>
<td>12</td>
<td>124</td>
</tr>
<tr>
<td>2. Bank of Baroda</td>
<td>12</td>
<td>19</td>
</tr>
<tr>
<td>3. Bank of Bihar</td>
<td>7</td>
<td>1</td>
</tr>
<tr>
<td>4. Canara Bank</td>
<td>9</td>
<td>2</td>
</tr>
<tr>
<td>5. Bank of India</td>
<td>11</td>
<td>20</td>
</tr>
<tr>
<td>6. Bank of Madaura</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>7. Bank of Maharashtra</td>
<td>9</td>
<td>11</td>
</tr>
<tr>
<td>8. Bank of Rajasthan</td>
<td>6</td>
<td>11</td>
</tr>
<tr>
<td>9. Canara Banking Corporation</td>
<td>8</td>
<td>11</td>
</tr>
<tr>
<td>10. Canara Industrial and Banking Syndicate</td>
<td>11</td>
<td>1</td>
</tr>
<tr>
<td>11. Central Bank of India</td>
<td>10</td>
<td>8</td>
</tr>
<tr>
<td>12. Devkaran Nanjee Banking Co.</td>
<td>9</td>
<td>15</td>
</tr>
<tr>
<td>13. Hindustan Commercial Bank</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>14. Indian Bank</td>
<td>11</td>
<td>4</td>
</tr>
<tr>
<td>15. Indian Overseas Bank</td>
<td>7</td>
<td>9</td>
</tr>
<tr>
<td>16. Oriental Bank of Commerce</td>
<td>12</td>
<td>9</td>
</tr>
<tr>
<td>17. Punjab National Bank</td>
<td>9</td>
<td>6</td>
</tr>
<tr>
<td>18. Union Bank of India</td>
<td>10</td>
<td>9</td>
</tr>
<tr>
<td>19. United Bank of India</td>
<td>13</td>
<td>17</td>
</tr>
<tr>
<td>20. United Commercial Bank</td>
<td>13</td>
<td>16</td>
</tr>
</tbody>
</table>

| Total                                  | 188                 | 154                                                                                                                                                    | 1227                                                                | 45       | 26       | 1452  |
A perusal of the above Table shows that the largest number of directorships are held by the directors of the Bank of Baroda (198) followed by those of the Bank of India (174) United Bank of India (150), and the United Commercial Bank (144). Two other banks whose directors held more than 100 directorships are the Union Bank of India (110) and Central Bank of India (108). Of the total directorships held, an overwhelming number of directorships was in the manufacturing and other companies, the percentage being 25.5%, whereas 19.6% were in financial companies, 3.1% in trading companies and 1.8% in associations not for profit.

(ii) Interlocking between first five banks and other companies

The Bank of India, the Central Bank of India, the Bank of Baroda, the United Commercial Bank and the Punjab National Bank constitute the first five of the private Indian banking sector, the State Bank of India being a Government bank. The foregoing five banks have been selected on the basis of their total deposits; the total number of directors on the boards of these five banks aggregated 55. Their total directorships including those in the banks totaled 744 and if their 55 directorships in the banks are removed, they would seem to have 689 directorships in the corporate sector. The average directorships held by a bank director in other companies works out to 13 as against the average of 9 directorships in respect of the directors of all the 20 banks covered in the study. The average directorships held by the directors of the Bank of India and the Bank of Baroda work out as 16, those of the Central Bank of India and the United Commercial Bank 11 and those of the Punjab National Bank, 7. The directorships of the five banks forms 45% of the total directorships of all the 20 banks, whereas the directors of the five banks constitute 29% of the total number of directors.

A detailed study of the directorships held by the directors of these 5 leading banks reveals that through common directors, these five banks are connected to 33 insurance companies, 6 financial companies and 25 investment trusts. Further these banks were connected to 584 manufacturing and other companies and 26 trading companies and 15 associations not for profit. The detailed position in regard to each of the five banks is shown in the Table given below:

### Table 7: Distribution of Directorships Held by the Directors of the Leading Five Banks

<table>
<thead>
<tr>
<th>Name of the Bank</th>
<th>No. of Directors</th>
<th>No. of Directorships held</th>
<th>Directorships held in</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Insurance</td>
</tr>
<tr>
<td>Bank of India</td>
<td>11</td>
<td>174</td>
<td>10</td>
</tr>
<tr>
<td>Central Bank of India</td>
<td>10</td>
<td>108</td>
<td>4</td>
</tr>
<tr>
<td>Bank of Baroda</td>
<td>12</td>
<td>198</td>
<td>9</td>
</tr>
<tr>
<td>United Commercial Bank</td>
<td>13</td>
<td>144</td>
<td>2</td>
</tr>
<tr>
<td>Punjab National Bank</td>
<td>9</td>
<td>65</td>
<td>4</td>
</tr>
</tbody>
</table>

| Total            | 55               | 689                      | 33        | 6              | 25                 | 584                  | 26         | 15                        |
(iii) Interlocking between 14 financial institutions and other companies:

The fourteen financial institutions named here have on their boards 171 directors of which 38 are common directors. Thus the boards of these institutions are manned by 133 persons. Of the total, 103 were the non-Govt. directors and after removing the common directorships, their number comes to 93. The number of Government directors, after removing duplication, comes to 40. Here it may be mentioned that unlike the banks, the directors of the financial institutions have no restriction on holding more than one directorship. And this explains the existence of 38 common persons on the boards of the financial institutions. The total directorships of the 93 non-Govt. directors came to 959 and after excluding the 93 directorships held by them on the financial institutions, the total directorships in other corporate bodies came to 866. The total number of companies excluding the financial institutions on which the 93 non-Govt. directors held directorships was 811. The average number of directorships held by each such director worked out as 10 and excluding the financial institutions, to 9.

As for the Government and foreign directors, it is seen that these 40 directors held in all 118 directorships; excluding the 40 directorships in the financial institutions, the number of directorships held by them in other corporate bodies comes to 78. The average number of directorships held by them thus works out as 3. Excluding those on the financial institutions it comes to 2.

The frequency distribution of directorships held by the 93 non-Govt. directors of the financial institutions is given in Table 8 below. The table reveals the prevalence of plural directorships among these directors to a very marked extent.

### TABLE 8

**FREQUENCY DISTRIBUTION OF DIRECTORSHIPS ON THE BOARDS OF FINANCIAL INSTITUTIONS**

<table>
<thead>
<tr>
<th>Number of directorships</th>
<th>No. of directors holding the directorships</th>
<th>Percentage to total</th>
<th>No. of directorships held</th>
<th>Percentage to total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>9</td>
<td>9.7</td>
<td>9</td>
<td>1.0</td>
</tr>
<tr>
<td>2–10</td>
<td>43</td>
<td>46.2</td>
<td>216</td>
<td>22.5</td>
</tr>
<tr>
<td>11–20</td>
<td>28</td>
<td>30.1</td>
<td>412</td>
<td>42.9</td>
</tr>
<tr>
<td>21 and above</td>
<td>13</td>
<td>14.0</td>
<td>322</td>
<td>33.6</td>
</tr>
<tr>
<td></td>
<td>93</td>
<td>100.0</td>
<td>959</td>
<td>100.0</td>
</tr>
</tbody>
</table>
A further study of the industrial breakdown of companies in which the 103 non-Government directors of the financial institutions reveal that they held directorships in 46 banks (of which 8 were in the Reserve Bank and 9 in the State Bank of India, leaving the number of directorships in the private sector banks to 29). The number of directorships held in other financial institutions were finance and investment companies (131), manufacturing companies (766), trading (44) and associations not for profit (57). Table below gives the details in respect of each of the financial institutions studied by us.

### TABLE 9

DISTRIBUTION OF DIRECTORSHIPS HELD BY THE DIRECTORS OF 14 FINANCIAL INSTITUTIONS

<table>
<thead>
<tr>
<th>Name of the financial institution</th>
<th>Number of directors</th>
<th>Total No. of directorships held in other cos.</th>
<th>Number of directorships held in banks</th>
<th>Investment cos.</th>
<th>Manufacturing and other cos.</th>
<th>Trading cos.</th>
<th>Associations not for profit</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Life Insurance Corporation.</td>
<td>12</td>
<td>146</td>
<td>8(3)</td>
<td>22</td>
<td>104</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>2. Industrial Credit and Investment Corporation</td>
<td>8</td>
<td>136</td>
<td>7(4)</td>
<td>14</td>
<td>106</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>3. National Development Corporation.</td>
<td>8</td>
<td>90</td>
<td>3(7)</td>
<td>7</td>
<td>76</td>
<td>4</td>
<td>..</td>
</tr>
<tr>
<td>4. Industrial Finance Corporation of India.</td>
<td>10</td>
<td>138</td>
<td>9(2)</td>
<td>26</td>
<td>98</td>
<td>7</td>
<td>8</td>
</tr>
<tr>
<td>5. State Bank of India.</td>
<td>32</td>
<td>378</td>
<td>9(5)</td>
<td>42</td>
<td>277</td>
<td>16</td>
<td>34</td>
</tr>
<tr>
<td>Seven subsidiaries of the State Bank of India.</td>
<td>25</td>
<td>124</td>
<td>6(3)</td>
<td>14</td>
<td>94</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>6. Film Finance Corporation of India.</td>
<td>5</td>
<td>26</td>
<td>3(1)</td>
<td>2</td>
<td>21</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>7. Refinance Corporation for Industry.</td>
<td>3</td>
<td>6</td>
<td>1(4)</td>
<td>..</td>
<td>..</td>
<td>..</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>103</strong></td>
<td><strong>1044</strong></td>
<td><strong>46(18)</strong></td>
<td><strong>131</strong></td>
<td><strong>766</strong></td>
<td><strong>44</strong></td>
<td><strong>57</strong></td>
</tr>
</tbody>
</table>

Excluding common directors | 93 | 866 | 38(12) | 102 | 640 | 35 | 51 |

**Notes:**
1. Figures in brackets indicate directorships in Reserve Bank of India and the State Bank of India.
2. Details for the eighth subsidiary of the State Bank of India i.e. State Bank of Travancore not included.
Conclusion:

In conclusion, it may be said that the present study of the interlocking of directorships between the banking sector and the rest of the corporate sector as well as the previous two studies on this subject referred to at the beginning of this article show that an elaborate network of interlocking directorships exists in India also as in the other industrial societies of the West having a corporate sector within themselves. It is a solid feature of the facts of business life. The minimum inference that can be drawn from its existence is that such arrangements permit an exchange of views in a convenient and more or less formal way among those who share the interests of 'corporate elite' and at the maximum, one may say that it consolidates 'corporate power' against the State and the Society. Be that as it may, the phenomenon of interlocking directorship has to be kept under control and observation in a country like ours which is wedded to the achievement of social justice and equality.
COMPANIES ACT AND THE REMUNERATION OF MANAGING AGENTS

By

N. PARASURAMAN

Under Secretary

One of the distinguishing features of the Indian Company Law is that, unlike similar laws in other countries like U.K. and U.S.A., it imposes a ceiling on the maximum managerial remuneration payable by public companies and also restrictions on the remuneration of various categories of managerial personnel within the overall ceiling. The origin of this may be traced back to the extensive amendments to the Company Law enacted in 1956, when for the first time some element of regulation in regard to various aspects of corporate management was written into the statute under which all future appointments of managing agents—an institution peculiar to India—could be made only on the basis of remuneration calculated on a fixed percentage of the net annual profits of the concerned company with a provision for a minimum payment in the case of inadequate profits. The manner of computing the net profits was also prescribed. Subsequently in 1951, in order to check abuses and curb the growing malpractices which had crept into the fast developing corporate sector as a result perhaps of World War II and its aftermath, the Indian Companies (Amendment) Act, 1951 added some important provisions to the law which inter alia made it obligatory on public companies to seek approval of Government in regard to any increase in the remuneration of existing managing agents and managing directors as also the terms of appointment of new managerial personnel.

About a year later, in February, 1952, the Company Law Committee under the Chairmanship of Shri C. H. Bhabha (a former Minister of Commerce)—one of whose terms of reference included “the measures necessary to promote efficient and economic management of companies”—made its recommendations to Government and based on these recommendations, a comprehensive Bill for the consolidation and amendment of the Company Law was enacted by Parliament in 1955 and the Companies Act, 1956 containing detailed provisions for regulating the remuneration payable to managing agents and other categories of managerial personnel, was brought into force on 1st April, 1956. The further amendments affecting managerial remuneration enacted by the Companies (Amendment) Act, 1960 were based on the recommendations of the Companies Act Amendment Committee presided over by Shri A. V. Viswanatha Sastry and with a view mainly to ensuring the better fulfilment of the purposes underlying the 1956 Act.

The main objects of the remuneration provisions were the promotion of efficient management and to ensure that the managerial expenses would not be out of tune with the resources and profit-making capacity of the company.

Nature and scope of the regulatory provisions:

In the case of a public company or a private company which is a subsidiary of a public company, an overall maximum of managerial remuneration is fixed at 11 per cent of its annual net profit to be computed in the manner laid down in sections 349 to 351 of the Act. “Remuneration” includes monetary equivalent of amenities and perquisites. In the event of absence or inadequacy of profits in any year, a minimum remuneration up to Rs. 50,000/- per annum can be paid to all managerial
From what is stated above, it would be reasonable to infer that flexibility—and not rigidity—is the key-note of the regulatory provisions.

It may be pertinent to point out here that Government's approval to the remuneration of managerial personnel is accorded on the advice of the Company Law Advisory Commission, a statutory body set up under the Companies Act, composed of a Chairman and four Members, representing the interests of trade and industry, labour, shareholders and the accountancy profession.

The interposition of Advisory Commission between the public and Government was considered desirable because it was felt that in the exercise of their large discretionary powers, Government should have the advantage of a careful assessment of the pros and cons of individual cases, which called for the exercise of Government's discretionary authority, by a body of competent people, who were generally familiar with company methods and practices, and could be expected at the same time to take a broad view of the legal and social responsibility of company management and also of the pervasive public interest implicit in the manner in which the companies carried on their work.

The Commission have evolved certain broad guiding principles on the basis of which they advise on remuneration payable to individual cases.

From what is stated above, it would be reasonable to infer that flexibility—and not rigidity—is the key-note of the regulatory provisions.
Impact of the regulatory provisions on the remuneration of managing agents:

Against the general background of the regulatory provisions briefly outlined above, it would now be useful to examine in greater detail the provisions in the Companies Act affecting the remuneration payable to managing agents of public companies or private companies which are subsidiaries of public companies. For facility of reference, it may be stated that these provisions are contained in sections 348 to 355 of the Act.

Section 348 of the Act provides that a company shall not pay to its managing agents in respect of any financial year by way of remuneration, whether for services rendered as such or in any other capacity, any sum exceeding ten per cent of the net profits of the company for that year. For this purpose, any remuneration paid to the following persons should be deemed to be included in the remuneration of the managing agents:

(i) Where the managing agent of the company is a firm, every partner in the firm;
(ii) Where the managing agent is a public company, every director of that company;
(iii) Where the managing agent is a private company, every director and member of that private company.

The said section further lays down that the above restrictions will not affect the operation of sections 352, 354 and 356 to 360 of the Act. Accordingly, payments made to managing agents under the provisions of the latter sections are outside the remuneration payable under section 348.

As pointed out earlier, the limit of ten per cent specified in section 348 is only the maximum remuneration statutorily admissible, but the actual remuneration payable to the managing agent of a company within the maximum limit has to be fixed with the approval of the Central Government. Since the middle of 1959, Government have been generally sanctioning remuneration of managing agents on the basis of a sliding scale of commission so that on higher slabs of net profits of a company, the percentage of commission is reduced gradually from 10 per cent on the first Rs. 10 lakhs to 4 per cent on the net profits over rupees one crore. This sliding scale has been fixed on the advice of the Company Law Advisory Commission, after considering the various issues involved and the basic objectives underlying the regulatory provisions, and also keeping in view the accepted social and economic policies of the country and the "ethos" of the times. In exceptional cases, however, where the Government in consultation with the Advisory Commission are satisfied that it would be in the interest of the managed companies concerned to deviate from the sliding scale, remuneration may be sanctioned on a higher scale but within the limit of 10 per cent of the net profits. It may also be mentioned that in the event of absence or inadequacy of profits in any year, a company can pay to its managing agent such minimum remuneration within the maximum of Rs. 50,000 per annum as may be sanctioned by the Central Government. As indicated in the annual reports on the working and administration of the Companies Act, the minimum remuneration is usually fixed ranging from Rs. 7,500 per annum for a company with a total effective capital of Rs. 5 lakhs or less to Rs. 50,000 per annum for a company with a total effective capital of over Rs. 150 lakhs, the actual amount being dependent on the nature of the business of the company, its financial resources, the performance of the managing agents in the past and other relevant factors.

The Companies Act also imposes certain restrictions in regard to payments to managing agents for services other than...
those of managing agents rendered by them to the managed companies, vide sections 356 to 360. Under these provisions, a managing agent or his associate is prohibited from receiving any payment by way of commission or other remuneration from the managed company for acting as selling agent of goods produced by the company or as buying agent for the company, but such payment can be made to him for acting as selling agent or buying agent outside India subject to certain conditions. Contracts between a managed company and its managing agent or the associates of the latter for the supply or rendering of any service other than that of managing agent, are required to be approved by a special resolution and also by Government. Contracts for sale or purchase of property between a managed company and its managing agent are also required to be approved by means of a special resolution. These restrictions have been introduced with a view to curbing certain malpractices and ensuring that the managements of companies do not supplement their managerial remuneration in other forms.

Whether the restrictive provisions have produced the desired results:

There can be no doubt that the operation of the restrictive provisions of the Companies Act, 1956 has in most cases resulted in a reduction in the quantum of remuneration of the managing agents as compared to the remuneration paid to them in the past when there was no statutory ceiling on their remuneration. Whether or not it has also produced the desired result of economy in the overall cost of management of companies managed by managing agents is, however, a debatable question. It is difficult to find a ready answer to this question as the answer would largely depend on the nature and extent of the services actually rendered by managing agents to their managed companies and the value of such services cannot always be determined in precise monetary terms.

The rationale behind the provision for remunerating the managing agent at a higher rate than that admissible to an individual managing director or manager was that a managing agent would be expected to render not only services of a purely managerial nature but also some additional services relating to the organisation of certain essential management facilities, consistent with modern management techniques, required by progressive industrial undertakings, provision of and/or procuring finance required by the managed companies at reasonable rates of interest, promotional services, etc. Obviously, a managing director or manager could not be ordinarily expected to render such additional services. It therefore follows that if a managing agent is not adequately equipped to provide the requisite management facilities and render the other additional services expected of him, the payment of a higher rate of remuneration to him than that paid to a managing director or manager cannot be justified.

According to the figures given by Dr. Raj K. Nigam in his article "The Impact of the Companies Act on the Managing Agency System" appearing in the September 2 issue of "Company News and Notes", of the total number of 1044 managing agents functioning as at 31st March, 1963, about 900 are managing only one company each. Are these "one company" managing agents in a position to render comprehensive services to their managed companies? It is reasonable to assume that most of them cannot afford to provide the type of modern management facilities which a large managing agency house can provide as the latter could share the cost of such facilities over a number of companies under their management. Even in the case of large managing agency houses maintaining a central organisation staffed with skilled and qualified executives, if the executives were entrusted with duties which
had the effect of reducing the work and responsibility of the managing agents and the salaries of such executives were recovered from the managed companies, the cost of management of the companies would be excessive. In this connection, the following observation made in para 113 of the sixth Annual Report on the Working and Administration of the Companies Act, 1956 is pertinent:

"There seems to be an increasing tendency for delegation (often indirectly) of management functions properly within the direct responsibilities of managing agents to the officers of the managed companies separately remunerated by these companies resulting in an increase in their management costs. In fact, the Department has come across cases, in which the expenses debited to the profit and loss account of managing agency companies were almost insignificant, the obvious inference being that the managements concerned were not incurring any expenditure themselves in connection with the management of the affairs of the managed companies."

Admittedly, the concept of management is changing fast and the services of a functional and executive nature are generally entrusted to the 'middle management', with power to take decisions on many matters pertaining to the day-to-day management of a company. If the managing agents perform only top management functions involving overall supervision and co-ordination of the different activities of a company and advice on all policy matters, the question arises whether the higher rate of remuneration payable to them at present could be reasonably justified. As this is an important issue affecting the growth of the corporate sector on healthy lines, it deserves careful thinking and detailed study by all concerned. What seems to be needed is careful assessment of the comparative costs of management of a representative cross-section of comparable companies (particularly of the large and medium size companies) having different forms of management, taking into account the contents of managerial functions of each form of management and all other relevant factors and making due allowance for any services which are not capable of being evaluated in monetary terms. The results of such a study might throw useful light on various aspects of the problem.
COMPLAINTS BY SHAREHOLDERS AND THE ROLE OF
REGISTRARS OF COMPANIES

By
S. K. BHATTACHARYYA
Registrar of Companies, Delhi

Types of Complaints
It is not as popularly realised as could be the case that the functions of the Registrar of Companies go much beyond routine administration of the provisions of the Companies Act. Quite apart from the legal functions allotted to him under the Statute, a Registrar has effectively to deal with, as an administrator and a legal functionary, complaints by shareholders, and to take appropriate steps by way of remedial measures.

Such complaints flow in from three directions:

(a) directly from the shareholders themselves and/or others associated with the corporate sector, or
(b) Complaints received by the Central Government or the Regional Director from shareholders etc., and transmitted to the Registrar, or
(c) Complaints received by the various other authorities viz. State Governments and such like from shareholders etc., and forwarded to the Registrar.

Some of the complaints more commonly received are enlisted below:

(a) Complaints alleging criminal action on the part of management,
(b) Complaints alleging impropriety by management,
(c) Complaints regarding unsatisfactory working of company,
(d) Complaints regarding contravention of laws other than Company Law by management,
(e) Complaints regarding non-holding of annual general meeting and non-circulation of accounts; denial of rights of inspection and information; non-payment of dividends,
(f) Complaints alleging contravention of the provisions of Companies Act.

Function of the Registrar—Nature of Functions
Complaints under (a) and (b) listed above attract the law directly, and the Registrar has to deal with them in the manner prescribed by law. Those under (c), (d) and (e), are attended to by him in his administrative capacity so as to ensure removal of genuine grievances and hardships suffered by shareholders in their dealings with Companies. It being the statutory duty of the Registrar to take legal actions against contraventions of the Companies Act, the complaints under (f) above are merely ancillary to his statutory duties.

The Registrar is clothed with specific statutory powers for those complaints as attract the law, more fully described in the subsequent paragraph. As for others, his role is essentially that of an administrator, and he exercises persuasion, mediation or other remedial action, as applicable from case to case. One or the other of these measures in most cases, adequately serves in achieving desired results.

Powers available under the Law for Discharging of Functions
Law directly arms the Registrar, inter alia, with the following powers vis-a-vis his duties towards complaints by shareholders:

Section 234(1) of the Companies Act empowers the Registrar to call for, by a written order, any information or explanation with respect to any matter included
in documents or returns filed with him viz. balance sheets and profit & loss accounts, annual returns, etc. This power is invoked by co-relating the complaint with documents or returns filed, for obtaining such information or explanation as is necessary to enable him to come to a judgment regarding the *prima facie* merits of the complaints. If such information or an unsatisfactory state of affairs, the explanation is not furnished on it discloses the Registrar has to report in writing the circumstances of the case to the Central Government, so as to enable them to decide whether one or more competent persons should be appointed as inspectors to investigate the affairs of the company, and to report thereon to the Central Government. In addition, refusal or neglect to furnish such information or explanations may result in prosecution of the company and the persons responsible therefor. Where the Registrar is satisfied that the information or explanations obtained disclose impropriety rather than criminality, he may, at his discretion, suggest to the Central Government that a special audit be ordered in terms of Section 233A of the Companies Act.

Having obtained the information or explanations as above, the Registrar has power to annex those or extracts thereof, to the relevant document. Once so annexed, the information or explanations or extracts thereof become subject to like provisions as to inspection, the taking of extracts and the furnishing of copies by any person in the office of the Registrar of Companies, as that document is subject. These additional information and the rights attendant thereon frequently dispose of complaints by shareholders satisfactorily.

Section 209(4) provides the Registrar with the right of inspection of books of account of companies, and this power is of great help to him in deciding the merits of complaints by making a searching scrutiny of the accounts in relation to the complaint. An alternative power to him in this behalf is the right to order production of books of account before him by companies in certain given circumstances.

If it is alleged that a company has not furnished to its shareholders all the information with respect to its affairs which they might reasonably expect, the Registrar may request the company to provide such information, failing which he may recommend to the Central Government that one or more competent persons be appointed as inspectors to investigate the affairs of the company and to report thereon in terms of powers available to the Central Government under Section 237(b) (iii) of the Companies Act.

If, upon information that the books and papers of any company are likely to be destroyed, altered, falsified or secreted in order to suppress evidence of any act of impropriety or criminality, the Registrar has reasonable grounds to believe that such an eventuality is possible, he may present an application to the magistrate that books and papers of such company be seized. After obtaining the necessary order of the magistrate for search and seizure of such books and papers as he considers necessary, he may take possession of them and before returning those, take copies or extracts from such books and papers as might be necessary, in accordance with Section 234A of the Companies Act.

Such appointments as managing agents, secretaries and treasurers, managing directors or whole-time directors, managers, in case of public companies, require the prior approval of Central Government. Applications for approval in this behalf are also required to be forwarded simultaneously, as per Rule 13A of the Companies (Central Government’s) General Rules and Forms, 1956, to the Registrar. This enables the Registrar to look into the past performance and record of the company, particularly in relation to prosecutions for contraventions of the Companies Act and complaints.
by shareholders and other, if any, before deciding whether he could recommend that the proposed appointments be approved by the Central Government. This extremely effective administrative tool makes it possible for the Registrar to put an end to any departures in the past from the norms of corporate behaviour by undesirable persons occupying positions of management.

Processing of various types of complaints and actions taken

Processing of complaints must necessarily vary from case to case in accord with their varying natures. The next few lines are an attempt to set out the processing techniques and the actions taken in the Registrar's Office:

Complaints regarding criminal action:

If the Registrar receives a representation from a shareholder or creditor, etc., and on materials placed before him, comes to a prima facie conclusion that the business of the company is being carried on in fraud or otherwise for a fraudulent purpose, he is duty bound, u/s 234(7) of the Companies Act, to give an opportunity to the company of being heard, before considering further action. It is important at this stage to bring in sharp focus the legal requirement of the existence of the dual elements underlined above before the Registrar can entertain a complaint u/s 234(7). Vague allegations regarding the management or dissatisfaction arising out of continued losses or unsatisfactory working of a company cannot be deemed to be adequate grounds in this behalf. Informed legal opinion holds that while the material contemplated in section 234(7), need not be "evidence", within the meaning of the Indian Evidence Act, it is certainly necessary that adequate documentary evidence must be placed before the Registrar before he can take action under that section. It has also been held that the second element of fraud must be construed in its legal connotation. Mention has been made before that the company must be given an opportunity of being heard, a step which cannot be circumscribed in law. The company may, however, at its option, avail of this opportunity and thereafter, if the Registrar comes to the prima facie conclusion that the provisions of Section 234(7) are attracted, he must, by a written order, call on the company to furnish in writing any information or explanation in respect of matters specified by him in the order. If such information or explanation is not furnished, or if it discloses an unsatisfactory state of affairs, the Registrar may send a report in writing to the Central Government recommending investigation of the affairs of the company by appointing Inspectors.

It is, however, necessary at this stage, to recognise that in most cases it would not be reasonable to expect the complainant to produce or place before the Registrar documentary evidence as visualised in Section 234(7), as shareholders and others are handicapped in obtaining the information which is by no means easy of access. However, the Registrar is not precluded, in his administrative capacity, from entertaining complaints even though they may not be backed by full documentary evidence. In fact, he does consider and examine such complaints by making effective use of his powers for obtaining information and explanation from the company in relation to documents like balance sheets and profit and loss accounts as per Section 234(1) on the lines indicated above. Following this, the Registrar considers whether in all circumstances of the case, he should recommend an investigation into the affairs of the company by the Central Government under section 235 or alternatively, suggest that a special audit be ordered under section 233A of the Companies Act.

Complaints regarding impropriety:

Complaints in this regard generally relate to
companies are indicative of gross inefficiency of management. Such complaints are usually processed by a thorough scrutiny of the balance sheets and profit and loss accounts filed by the companies. In this context, wide use is made of the accounting technique for preparation of comparative profit and loss accounts which essentially consists of comparing various heads of expenditure of 3 to 5 years as percentage of the relative sales of those years. This serves to localize attention to possible areas of inefficiency which is then subjected to a meticulous enquiry: by issuing a questionnaire in this behalf in exercise of the powers conferred on the Registrar u/s 234(1) of the Act in relation to the balance sheets and profit and loss account filed by the company in question. Another technique which is largely used is preparation of accounting ratios from balance sheets and profit and loss account to make a thorough study of the financial soundness and profitability of the operations of the company.

If the examination outlined above shows that the financial position of the company is such as to endanger its solvency, it is open to the Registrar to recommend to the Central Government that a special audit be ordered of the company’s accounts in exercise of the powers conferred on that authority by Section 233A (1) (c) of the Act. However, before doing so, an opportunity is invariably accorded to the company to explain its case and to present its proposals, if any, for improving its future financial position. If however, the financial health of the company is beyond redemption, as evidenced by the fact that the liabilities of the company exceed its assets as shown in the balance sheet, it is open to the Registrar to present a petition to the appropriate high court for compulsorily winding up the company in exercise of the powers available to him u/s 439(5), read with Section 433(e) of the Act on the ground that “the company is unable to pay its debts.”
Complaints regarding contravention of other laws: It is not unusual for the Registrar to receive complaints of contravention of laws other than the Companies Act, viz:

i. Income Tax and Sales Tax Acts,
ii. Import Control Regulations,
iii. Licences granted by State or Central Governments,
iv. Foreign Exchange Regulations,
v. Custom and Excise Laws,
vi. Capital Issue (Control) Act,
vii. Stock Exchange Regulations.

Normally, such complaints are forwarded to the authorities concerned with the administration of the relative laws, and the complainants are asked to contact them accordingly.

Complaints regarding non-holding of annual general meeting and non-circulation of accounts; denial of rights of inspection and information; non-payment of dividends:

If, on receipt of a complaint, it is noticed that a company has not held its annual general meeting in accordance with the provisions of Section 166 of the Companies Act, or has not laid its balance sheet and profit and loss account before its shareholders as required by Section 210 of the Act, or further it has not circulated to its shareholders, the relative balance sheet, profit and loss account, auditors' report and directors' report as required by Section 219, invariably notices are issued to the company and its directors, asking them to make good the defaults in this behalf and, on non-compliance thereof, prosecutions are lodged against the company and its directors in accordance with the provisions of the law.

It is not widely known that an alternative remedy which is open to a shareholder is that he can request the Regional Director concerned to call or direct calling of a general meeting of the company, and give such ancillary or consequential direction as may be expedient.

Frequently complaints are also received that balance sheets and profit and loss accounts alleged to have been circulated to the shareholders by the companies concerned have not in fact been received. It is the experience of the Registrars that such allegation is invariably countered by the companies by production of their despatch registers showing issuance of the above documents. However, in such cases, the companies concerned are as a rule requested to make available fresh copies of the balance sheets etc., and such request is usually met.

It is worthwhile to mention here that a shareholder has a right to receive documents under certificate of posting or by registered post provided he has intimated his wish in this regard to the company in advance, and has deposited a sum sufficient to defray the expenses for that purpose. In fact, it would amount to a contravention of law if these requirements are not complied with when the shareholder concerned has paid for such specific mode of despatch.

Rights of inspection and information available to a shareholder can be briefly summarised as follows:

(i) The right to receive, within seven days, a copy of the memorandum and articles of association, agreements regarding appointment of managerial personnel and other agreements referred to in Section 192, on payment of rupee one by way of fee,—vide Section 39;

(ii) The right of inspection of the register of members and debenture holders, and the relative indices, and copies of all annual returns prepared under Section 159/160,—vide Section 163 (2);

(iii) The right of taking extracts without fee from any register mentioned in (ii) above, and the further right of requiring copies on payment of prescribed charges;

(iv) The right to receive reasonable information with respect to the affairs of the company including information relating to the calculation of the commission payable to managerial personnel,—vide Section 237 (c) (iii).
Complaints regarding contravention of the provisions of the Companies Act:

Complaints regarding violation of the substantive provisions of the Companies Act wherever proved by the requisite evidence, lead to legal action being taken against the companies concerned, under the relative provisions of law by the Registrar. However, it is necessary to point out that procedural requirements of law, e.g., regarding validity of notices of meetings, presence of quorum, etc., are best dealt with by the shareholders themselves in consultation with their own legal advisers as it is not legitimate to expect the Registrar to acquire evidence in this regard and assess their legal validity, without acting as a court of law—a function which is neither contemplated in the law nor visualised in the administrative principles underlying his duties. The same observations hold good in relation to departures from the provisions regarding procedures embodied in the articles of association.

Rights of Shareholders under the Companies Act

Amongst the many rights available to the shareholders under law, the following deserve special mention in the context of the present discussion:

(i) The right to launch prosecution for contravention of the provisions of the Companies Act in the appropriate court of law vide Section 621.

(ii) The right to present a petition for relief in cases of oppression and of mismanagement by shareholders holding not less than one-tenth of the issued share capital of the company, or one hundred members, whichever is less—vide Sections 397 and 398; this power may be exercised by shareholders falling below the required minimum above, subject to an authorization by Central Government—vide Section 399(4).

(iii) The right to apply to Central Government for appointing two persons as directors for preventing oppression or mismanagement, by shareholders holding not less than one-tenth of the total voting power, or by one hundred shareholders—vide S. 408.

(iv) The right to apply to the Central Government to prevent changes in the constitution in the board of directors consequent on a change or a likely change in the ownership of shares held by the company by directors/managing directors/managing agents, etc., on behalf of shareholders—vide S. 409.
(v) The right to present an application to Central Government to order an investigation into the affairs of a company provided the application is presented by not less than two hundred shareholders or shareholders holding one-tenth of the total voting power, vide S. 235(a)

(vi) The right of an application to the appropriate court for compulsorily winding up of the company on grounds listed in Section 433 including the ground that the company is unable to pay its debts, vide Section 439.

(vii) The right to make references to the Central Government regarding their grievances against the company and its management after publication of notice in newspapers in terms of Section 412 of the Companies Act relating to applications to Central Government for approval of proposed appointments of managerial personnel in case of public companies.

The foregoing rights are in supplement to the general rights of the shareholders to attend and participate in the company meetings, to receive copies of balance sheets and profit and loss accounts and other financial reports, to exercise voting rights in relation to appointments of various categories of managerial personnel and resolutions regarding the business activities of the company. These rights can be given meaning and content only if they are exercised in an intelligent manner by making continuous assessment of the performance of the company in general and the management in particular, on the basis of searching scrutiny of the various matters which require their sanction and a thorough analysis of the annual accounts placed before them at the time of the annual general meeting.

Role of Shareholders' Association
The average shareholder is often unaware of the rights to which he is entitled under law and being uninitiated in the intricacies of corporate finance, can hardly be expected to play an effective role in redressing the grievances he has. It is here where the shareholders' association comes into its own field, and by the concerted action of its members, it can step in and effectively intervene wherever the rights of the individual shareholder are not honoured for private gains of management. In order effectively to render this service, it must develop proper expert service within its own shell, with particular emphasis to enforcement of the legal rights of the members, shareholders, and continuous assessment of the financial stability and profitability record of the company with which the members are concerned.

Conclusion
Summing up, the Registrar can, within the bounds of the rights, do a great deal to help the shareholders in genuine cases of grievances, but this is no warrant for the mistaken belief widely held that the shareholders must look to the Registrar and the Central Government only to cure all the ills of the corporate sector. This expectation however, must be matched on the part of the shareholders by a sustained effort to rise above the present state of inertia and assert their legitimate rights.

It is necessary, at this stage, to strike a note of caution regarding certain undue and illogical expectations that might result out of a cursory study of this article. It must be very clearly understood that a Registrar cannot interfere where complaints are vexatious or frivolous in nature. Indeed, the law casts a duty upon him, as would be apparent from a reading of Section 234(7) of the Companies Act, that he should disclose the name of such complainants to the company concerned so that it can take such action as it may be advised. It must also be equally understood that it is no part of the duty of the Registrar to intervene or mediate in purely factional fights between two groups of shareholders and management, and that such disputes should be properly settled by references to the appropriate court of law.
RIGHTS OF MEMBERS UNDER THE COMPANIES ACT, 1956
By
A. P. ROY
Solicitor

From the date of incorporation of a company, the subscribers of its memorandum of association or other persons as may from time to time be its members become a body corporate by the name contained in the memorandum. A company after incorporation, therefore, acquires a personality which is independent of its members; it can own property, sue and be sued in its own name. From a practical standpoint, however, a company means 'an association of many persons who contribute money or money's worth to a common stock and employ it for a common purpose. The common stock so contributed is denoted in money and is the capital of the company. The persons who contribute it or to whom it belongs are members. The proportion of capital to which each member is entitled is his share.' In a loose sense, it can be said therefore that a company belongs to the members or the members of a company are its owners. It is not possible for every member who may be large in number to take active part in the management of the affairs of the company. The Companies Act, therefore, has made elaborate provisions for the management of the affairs of a company by the representatives of its members who are referred to as the Board of directors. Due to the divorce between the members and the management and the large number of instances of abuses of power on the part of the latter which came to light, the Companies Act has conferred bundle of rights on the members and also remedies to enforce the same.

To become a member:
Before we discuss in detail the various classes of rights which a member has in relation to a company we may refer to the

modes whereby a person can become a member. A person can become a member by subscribing to the memorandum of association before registration or thereafter by obtaining allotment of shares from the company or the registration in his own name of the transfer of share by an existing member or by operation of law. Thus, the expressions 'a subscriber', 'a member', 'a shareholder' or 'a contributory' of a company limited by shares are almost synonymous. But a company may not have a share capital and a person may be member of such a company. A member in relation to a company, however, does not include the bearer of a share warrant issued in pursuance of section 144 of the Act.

Protection of minority:
A proper balance of the rights of majority and minority members is essential for a smooth functioning of a company. The Companies Act attempts to maintain that balance by admitting normally the rule of majority but limits the same by making exceptions in a number of cases in the interest of minority members. The rule of majority operates only in the area of corporate membership rights and the individual membership rights are not affected by the will of the majority irrespective of its size.

The rights of a member are either—
(a) statutory;
(b) given by the memorandum and articles of association; and
(c) conferred by the general law especially that relating to contracts.

The rights conferred by the statute cannot be taken away or modified by any provi-
sions in the memorandum or articles. The other classes of rights however, can be varied by consent.

The memorandum of association of a company is its charter. A company can exercise only such powers which are either expressly stated therein or as may be implied therefrom including matters incidental to the powers so conferred. The articles of association of a company are its internal regulations and lay down mode and manner in which the business of a company is to be conducted. The articles of a company are always subject to the memorandum and do not in any case confer powers wider than those enjoyed by the company under its memorandum. The memorandum and articles of association have the effect of a contract as between the company on the one hand and the members on the other in their capacity as such as well as among the members inter se.

By his contract with the company a member undertakes with respect to most of the rights which his membership carries to accept the decision of the majority of members. These membership rights are known as corporate membership rights. There are, however, certain rights of a member according to his contract with the company which cannot be taken away or modified unless he consents and if such rights are in question even a single member can defy the majority consisting of all the other members. The rights of this class are known as individual membership rights.

**Important Rights:**

It is not possible to give a complete list of all the individual membership rights. However, the outstanding examples are given below:

(a) The right to maintain himself in full membership with all the rights and privileges appertaining to that status. As a result of this right even an individual shareholder can insist on the strict observance of the statutory provisions and the legal rules, and the provisions in the memorandum and articles cannot be waived by a bare majority of members.

(b) The rights of a shareholder not to be compelled to take or subscribe for more share or to have his liability increased without his consent in writing (S. 38).

(c) The right to petition for compulsory winding up (S. 439).

(d) If so authorised by the Central Government the right to petition in case of oppression of minority by the majority of when the affairs of a company are conducted in a manner prejudicial to its interest (Ss. 397 and 398).

(e) The right to apply to the Central Government for calling an annual general meeting when the Board of directors make default in holding such a meeting (S. 167).

(f) The right to object to the appointment of two or more directors by a single resolution in the absence of a prior unanimous resolution to follow such a procedure (S. 263).

(g) The right to object to shorter notice than the statutory twenty-one days in respect of convening of an annual general meeting (S. 171).

(h) The right to represent to the Court where an act of the company requires confirmation or sanction by the Court (S. 186).

(i) The right to object to the compulsory transfer of shares in case of takeover bid.

(j) If the share carries a vote the right to have the vote recorded.

(k) The right to petition to Court for an order that the meeting of a company be called (S. 186).

(l) The right to use his vote differently.

**Supremacy of Majority:**

Corporate membership rights as have been stated above are those rights which the member has agreed to submit to the will of the majority, i.e. with respect to the said
The rule discussed above evolved in the expropriation cases in which the issue was whether a special resolution altering the articles of a company providing that a minority shareholder holding a small number of shares could be compelled upon the request of majority to sell out his shares at fair value to the nominee of the majority was valid or not. In Sidebottom Vs. Kershaw Leese and Co. Ltd. (1920) 1 Ch. 154, the company was carrying on the business of cotton spinners. A special resolution was passed to amend the articles to compel the member carrying on a business which is in direct competition with the business of the company to sell out his shares to the nominee of the directors upon payment of fair value. The Court of appeal held that it was in the interest of the company as a whole to be protected against competition and upheld the resolution. In Brown Vs. British Abrasive Wheel Co. (1919) Ch. 290 a contrary decision was arrived at. The majority held 98% of shares and the minority 2%. A resolution was passed to the effect that a shareholder upon the request of the members holding 90% of the issued shares would be bound to sell and transfer his shares to the nominees of such members at a fair value. It was held that the alteration was not for the benefit of the company as a whole but for the benefit of the majority and an injunction was granted against the company whereby it was prohibited from carrying on the resolution. In either case an element of dishonesty or at least impropriety must always be present if it is alleged that the resolution constituted a fraud on the majority.

Exceptions:

However, there are some well recognised exceptions to the rule in Foss Vs. Horbottle e.g. the majority cannot confirm—(i) an act which is ultra vires the company or illegal; (ii) an act which constitutes a fraud against the minority and the wrongdoers are themselves in control of the company; and (iii) a resolution which requires a qualified majority has been passed by a simple majority.

It is not possible to state with certainty as to when an act qualifies as fraud on the minority. However, it has been held that a resolution constitutes a fraud on the minority if it is not passed bona fide for the benefit of the company as a whole—Shuttleworth V. Cox Bros & Co. (Maidenhead) Ltd. (1927) 2 K.B. 918. Evershed M. R. in Greenhalgh Vs. Ardeyne Cinemas Ltd. (1950) 2 All E. R. 112, 1126. In either case an element of dishonesty or at least impropriety must always be present if it is alleged that the resolution constituted a fraud on the majority.
full and frank disclosure to the shareholders of the facts upon which they are asked to vote.

Where a statute or articles require a qualified majority for the passing of the resolution as in the case of a special resolution the rule in Foss v. Harbottle cannot be invoked to override these requirements by passing an ordinary resolution. Certain matters concerning the business of the company as enumerated in sections 17, 21, 31, 99, 100, 196, 208, 237, 261, 309, 314, 323, 338, 352, 356, 357, 358, 360, 370, 375, 484, 494 and 590 of the Companies Act, now require a qualified majority. The requirements of a special resolution are—

(a) The notice convening the general meeting should be duly given and the intention to propose the resolution as a special resolution should be specified in the notice. A statement setting out all material facts concerning each item of business including in particular the nature of the concern or interest, if any, of every director, secretary or treasurer managing agent and manager in the resolution is required to be annexed to the notice convening the meeting.

(b) The votes cast in favour of the resolution by members should not be less than 3 times the number of votes cast against the resolution. It must be noted, however, that when the vote is taken by show of hands and not by poll, the declaration of the Chairman that the resolution has been carried unanimously or by a particular majority is normally conclusive. (s. 178).

Qualified Minority Rights:
The rule of 'supremacy of the majority' usually referred to as the rule in Foss v. Harbottle are subject to the qualifications specified below:—

(a) exceptions properly called to the rule;
(b) individual membership rights; and
(c) qualified minority rights.

There is distinction between qualified minority rights and individual membership rights. Individual membership rights can be exercised by an individual shareholder. The qualified minority rights, however, require the cooperation of a minority group of a specified size, within the corporate body. The term 'qualified minority rights' refers to the rights enabling a minority of specified size to take particular action. Some illustration of a qualified minority rights are given below:—

(i) Members holding not less than 1/10th paid-up capital of a company may put up a requisition to the Board of directors to call an extraordinary general meeting, and if the Board does not convene a meeting within 21 days from the date of the deposit of a valid requisition then the requisitionists may themselves convene a meeting. (s. 169).

(ii) Five members in the case of a public company and one member in the case of a private company having the right to vote may demand a poll to be taken on a resolution before or on the declaration of the result of voting thereon on a show of hands. (s. 179).

(iii) Members holding not less than 10% of issued shares of a class may apply to the Court to have a variation cancelled.

(iv) Two hundred members or members holding not less than 1/10th of the total voting power in a company having a share capital and not less than 1/5th of the total number of members of a company not having a share capital may apply to the Central Government for investigation into the affairs of the company.

By far the most important qualified minority rights have been conferred by sections 397 and 398 of our Act. A petition under section 397 or 398 can be made in the case of a company having a share capital by not less than hundred members or 1/10th of the total number of members or any member holding not less than 1/10th of
the matters complained of or apprehended, the court may, if the facts and circumstances of the case so require, make such order as it thinks fit, notwithstanding the other provisions of the Act. The members, in the alternative, may apply to the Central Government for appointment of two individuals as directors of the company or for directing the company to amend its articles to adopt proportional representation for the appointment of directors.
PROSECUTIONS UNDER THE COMPANIES ACT
SOME SUGGESTIONS TO REDUCE THEIR INCIDENCE

By MAN MOHAN SINGH,
Asst. Editor.

"Why is our Government so keen and hasty in launching prosecutions under the Companies Act?" is a question sometimes posed in the corporate sector. That the Department of Company Law Administration is following a policy of persecution under which so-called innocent officers of the company are dragged to the law courts is another fear lurking in some quarters. And those who are cautious enough to realize that the Department is only faithfully discharging the duties imposed upon it by the Parliament find fault with the Companies Act itself, not only because it is so voluminous and complicated but also because it lays virtually in every section a trap, which leads the unwary officers of the company only to the door of the law courts. It was perhaps this class of people who found further objection in the enactment of Section 629A providing for an omnibus penalty clause.

That all these are unfounded misapprehensions and baseless beliefs and that neither the legislature nor the executive is anxious to launch prosecution, as an end in itself, is one of the objects of this article to explain. It is also the object to explain that reduction in the number of prosecutions is something which is both feasible and desirable, not only for its own sake but for the sake of establishing a healthy corporate sector.

While no statistics for the number of prosecutions launched under the Indian Companies Act, 1913 is readily available, it is evident that, with the gradual strict enforcement of the provisions of the Companies Act, 1956 by the Central Government, the number of prosecutions steadily went up from 572 in 1956-57 to 6272 in 1960-61 showing an increase of 996.5 per cent. The number of companies prosecuted also went up from 165 in 1956-57 to 1220 in 1960-61. This was perhaps one of the causes for alarm in the corporate sector. Yet the reality is that most of the prosecutions were as a result of the legacies of the Department to clear the backlog in respect of past defaults. The evidence of this lies in the steep fall in the number of prosecutions from 6272 in 1960-61 to 3990 in 1961-62 and to approximately 3690 in the year 1962-63. Hence increase in the number of prosecutions in 1960-61 was not at all any justification for the fear.

At the same time, the comparison of the number of prosecutions under the company law in India to the number of prosecutions under the Companies Act, 1948 in the U.K. shows that, while in the U.K. the percentage of companies prosecuted to the total number of companies at work as on 31st December, 1961 was 0.02, in India it was 4.6 per cent on 31st March, 1961 and 3.6 per cent on 31st March, 1962. While the trend is towards decline, yet it appears necessary to enquire as to whether lies the reason for the high rate of company prosecutions in India?

Reasons for prosecutions:
Surely, it does not lie in the Department, in so far as the percentage of convictions** by the Courts of law to the total number of cases decided was as high as 86 per cent in 1960-61 during the year when the maximum

**Convictions by the law courts can be said to be the prima facie proof of the fact that the prosecutions were justified.
number of prosecutions was launched. Even allowing of margin for the time lag between the launching of the prosecutions and their final disposal by the courts, does not make the position any worse as far as the number of convictions in 1961-62 came to be 84 per cent and in fact went up to 87 per cent during 1962-63. It is interesting to observe that the relevant percentage of convictions to total number of prosecutions in the U.K. was only 79 per cent, thus showing comparative justification for launching of prosecutions in India.

That the Government is not interested in launching prosecutions simply for the sake of prosecutions, is evident from the fact that, in spite of absence of any mandatory duty on the part of the Department to issue any warnings it had been issuing, and continues to issue, two default notices by registered post to the erring companies and their officers to make good the defaults. It is only in case of non-compliance even after the issue of the default notices that the Department, considering that persuasions and warnings have had no effect, has to perform its painful duty.

Here also, the Department appears not to be causing more harassment to the defaulting companies than is absolutely essential. For instance, for defaults punishable under sections 162/159, 168/166, 210 and 220 (accounting for a majority of prosecutions) the Department has not usually been launching prosecutions simultaneously for sections 168/166 and 210 along with sections 162/159 and 220 on the grounds inter alia that, in that case, the accused will have to undergo the torture of appearing almost simultaneously in different sets of courts, situated at different distant stations.

It may be mentioned that the Government's desire to reduce the number of prosecutions (of course consistent with the due compliance of the law) is a natural one because the high rate of prosecutions, while proving the vigilance and vigorous watchfulness of the Department as an enforcement agency, also means a little reflection on the success of the policy pursued by it to lower the incidence of defaults. Indeed, it is only the minimum code of conduct which the Act prescribes and which the Department is enforcing, and it is no part of policy of the Department to encourage litigation.

**Does Management want prosecutions?**

But, at the same time, saying that the officers of the companies themselves invite prosecutions would be an uncharitable tribute paid to the corporate management. After all why should the companies, by going to the law courts, attract a blot on their otherwise fair name, and why should the corporate management, allow itself to be brought down in the eyes of the public for being convicted by the law courts? The answer to these questions need a mention of the most important defences strongly relied upon by the officers in the law courts: (i) Due to group feuds in the management the law could not be complied with (ii) The Company is not carrying on any business and is virtually a defunct one (iii) The accounts are in the process of being audited, (iv) The managing director/manager alone was responsible to look after compliance with the law.

That these defences are of no avail to the accused is fully borne out by the long list of company cases decided by the various courts throughout the country. An additional plea which the accused, for fear of ignorantia juris non excusat, seldom put forward before the Court but plead with loud voice outside, is that the Companies Act is a very bulky and complicated piece of legislation and that they were unaware of the duties to be performed by them. The hollowness of this argument becomes amply clear if we realise that, out of 15,899 prosecutions launched during the 5 financial years ending 31.3.61, 14706 or 92.49 per
percent of the prosecutions were for defaults only under five sections of the Act, viz. non-holding of annual general meeting, non-placing of accounts thereat, non-filing of annual returns, balance-sheet, and liquidators' annual statements. The relevant percentages for the years 1961-62 and 1962-63 were 92.56 and 92.94 respectively. Thus the bulkiness of the Act or the complexity of its provisions has nothing to do with at least 95 percent of prosecutions under the Companies Act, in so far as learning of five sections of the Act cannot be said to present any formidable task. Thus the reasons commonly put forward by the officers of the companies are not causes but excuses; apathy and indifference to the need for compliance being the real ones.

**Solution:**

Then whither lies the solution? To my mind, a four-pronged attack appears to be necessary to tackle the situation:

(i) **Management.**—Firstly, none can reduce the number of prosecutions more effectively than the men who make the defaults and thus make the Department set the ball of prosecution rolling. No doubt the corporate management in India has since realized that the provisions of the Act cannot be contravened except on the pain of prosecution and/or payment of additional fee, yet the realization of the need for voluntary and spontaneous compliance, more as a sacred and moral duty than as a statutory or legal obligation, is still lagging behind. In fact once that sense of duty comes into being, the number of prosecutions will automatically go down.

This sense of duty has however to be coupled with the vigilance on the part of the management to ensure that secretarial staff engaged by them for the purpose of compliance with the provisions of the law are not slackening in their efforts.

(ii) **Shareholders.**—Lack of interest on the part of shareholders till something actually goes wrong with the company, is well-known. Yet, being not at all oblivious of this fact, it is suggested that the shareholders should at least ensure that within 6 months of the close of the financial year of the company, they receive its accounts. If they do not so receive, it is obvious that the company would either pay additional fee and/or its officers along with the company would be prosecuted. Knowing this, the shareholders can ask at the next annual general meeting as to what prevented the company from complying with the provisions of the law; whether the company paid additional fee and/or was prosecuted and if so, whether the company has been made to bear the amount and, finally, what steps are being taken to avoid recurrence of such defaults in future. It is felt that this little vigilance on the part of shareholders would not only drastically reduce the number of prosecutions but would also goad the sense of managerial accountability, so important in corporate sector.

(iii) **Auditors.**—Thirdly, the auditors, who are sometimes blamed, though undeservedly, for delay in auditing the accounts and thereby contributing to the making of defaults, can also aid the solution of the problem. While it is felt that it is delay on the part of the company management and/or their staff which is really responsible for the defaults, yet it would be better if the auditors do not allow their fair names to be tarred by the same brush. This they can do by mentioning in the audit report itself the factum of gross delay in submission of accounts by the management. Consistent with the work load and otherwise practicability of the work, the auditors should perhaps insist for audit of the accounts simultaneously they are being written up. Although there is no statutory obligation in this respect, yet the suggestion, if followed, would not only reduce the
workload of the auditors at the close of the financial year but would also contribute to the prompt and up-to-date writing of the accounts by the management. Indeed the constant poking on the part of the auditors for expeditious presentation of accounts to them, would make the corporate sector more alert in compliance with the provisions of the law and thereby leave no scope for evils, such as fraud, misappropriation, cheating and fabrication of false accounts etc.

(iv) Courts.—Lastly, the Courts have also an important role to play. The Parliament has vested them with wide powers and discretion in the matter of quantum of fines which they might impose within the maximum limit provided under the Act. While it is unfortunate that in a few cases an erroneous belief is still lurking that the majority of the prosecutions under the Companies Act are technical defaults, it is gratifying to note that most of the Courts have since realised the importance of what the Hon'ble Mr. Justice Ramaswamy of Madras High Court observed in a case before him:

"The important check on a company is the balance-sheet which has to be prepared by a qualified auditor, and it is that which has been described as the red light which shows the investing public as well as shareholders and directors what the affairs of the company are. Therefore, it is a matter of considerable importance that the balance sheet should be prepared and submitted in proper time. It is the neglect to do this that is the cause of many avoidable scandals. Therefore the Magistrate should have taken an adequate and grave view of the offence which is destructive of commercial morality."

Similar was the reaction of the Hon'ble Mr. Justice Lodge of the Calcutta High Court when he observed that the directors of the companies not complying with the provisions of the Companies Act deserved to be "substantially penalised."

While the deterrent theory of punishment is giving way to the reformatory theory, yet the fact remains that non-compliance with the provisions of the Act, in spite of default notices, shows that the malady in respect of the particular accused deserves a stronger dose especially the one provided by the deterrent theory. That being the case, the Courts can break the causal relationship between the low fines and the higher incidence of default by imposing heavier fines and thus making its repetition less probable.

Regarding the quantum of fine, it would be instructive to mention what Kerala High Court held as early as in 1958:

"The Court must be guided by a sense of proportion in fixing the quantum of fine in a particular case. It must bear some reasonable proportion to the upper limits sanctioned by the Statute. To disregard this and to award only nominal sentence would have the result of reducing the prosecution itself to mockery and thus defeating the very object of this penal provision".

To this may be added the need for imposing daily fines (instead of consolidated ones) in respect of offences where the Act so prescribes.

Thus the Courts, by imposing suitable fines for non-presentation and non-filing of accounts and various other returns which provide enormous opportunities to the corporate management to forget their corporate accountability and play havoc with the fund of the shareholders and the creditors, can show that justice is being done to those for whom the courts along with the Department have been made the guardian under the Companies Act.

Conclusion:

In conclusion, it may be mentioned that the chances of reduction in the number of prosecutions and so also of building a
healthy corporate sector lie in the allround vigilance and cooperation on the part of the management, the shareholders, the auditors and the Courts. Once they ensure that the preparation, presentation and filing of accounts are not being delayed, not only a substantial majority of the 93 per cent of the prosecutions would not be there but in addition we shall be having an ideal management whose love and respect for fiduciary obligations and sense of corporate accountability would be above suspicion. Then why delay?
Although the accounting year is not uniform in respect of all the five companies, it will be seen that two companies had adopted the calendar year as their accounting year and that all the five companies had at least their accounts of nine months reflected in the calendar year 1961. Apart from this, in view of the wide differences in the economic climate of each country and the variation in the size of each company, only a very broad comparison of some of the salient financial aspects of the working of the companies has been attempted here. An idea of the size of each company can be obtained from the sales figure of the company given above.

**Rate of Profit:**

The rate of profit before tax on the total capital employed (total net assets) and the sales income is given in Table I.
Tatas occupy the third position in this regard, it will be seen from Table II that tax provision is lowest in the case of Tata Iron. This is due to the development rebate allowed under the Indian Income Tax Act and that also accounts for the higher amount of profits retained by the Tata. The largest amount of profits are being distributed by the Republic Steel and the Tatas occupy the third position in this regard.

### TABLE I
**RATE OF PROFIT**

<table>
<thead>
<tr>
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<th>Rate of profit on total capital employed</th>
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<tbody>
<tr>
<td>Tata</td>
<td>6.8</td>
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<tr>
<td>Wales</td>
<td>2.0</td>
</tr>
<tr>
<td>Republic</td>
<td>5.3</td>
</tr>
<tr>
<td>Canada</td>
<td>14.2</td>
</tr>
<tr>
<td>A.T.H.</td>
<td>10.2</td>
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</tbody>
</table>

### Allocation of Profits:
Table II shows how the profit before tax is being used by all these companies.

### TABLE II
**ALLOCATION OF PROFITS** (Percentages)

<table>
<thead>
<tr>
<th></th>
<th>Tax Provisions</th>
<th>Dividends</th>
<th>Retained Profits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tata</td>
<td>8</td>
<td>46</td>
<td>46</td>
</tr>
<tr>
<td>Wales</td>
<td>16</td>
<td>58</td>
<td>26</td>
</tr>
<tr>
<td>Republic</td>
<td>34</td>
<td>65</td>
<td>1</td>
</tr>
<tr>
<td>Canada</td>
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<td>22</td>
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</tr>
<tr>
<td>A.T.H.</td>
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<td>34</td>
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</tbody>
</table>

It will be seen from Table II that tax provision is lowest in the case of Tata Iron. This is due to the development rebate allowed under the Indian Income Tax Act and that also accounts for the higher amount of profits retained by the Tata. The largest amount of profits are being distributed by the Republic Steel and the

### Structure of Assets and Liabilities:
Table III shows the importance of some of the main assets and liabilities in the finances of the five companies.
It would be seen that net fixed assets form a more important part of the net total assets in the case of Wales and Tatas, compared with the other companies. As regards the structure of liabilities, paid-up share capital was more important in the case of ATH and Tatas than in the case of other three companies. Reserves were more important in Republic and Canada, while borrowings were more important in the case of Tata and Wales. Share Capital and Reserves were less than net fixed assets in the case of Tata, Wales and ATH, indicating that net fixed assets could not have been fully financed from these sources, whereas in the case of Republic and Canada, reserves and Share Capital exceeded net fixed assets. Borrowings were relatively higher in the case of Tata and Wales compared to the others.

Rate of Growth of Assets

Table IV shows the rate of growth in net fixed assets and total net assets.

TABLE IV
GROWTH OF ASSETS IN 1962

<table>
<thead>
<tr>
<th></th>
<th>Rate of growth in net total assets</th>
<th>Rate of growth in net fixed assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tata</td>
<td>-1.4</td>
<td>-5.3</td>
</tr>
<tr>
<td>Wales</td>
<td>2.5</td>
<td>1.1</td>
</tr>
<tr>
<td>Republic</td>
<td>-1.5</td>
<td>-1.8</td>
</tr>
<tr>
<td>Canada</td>
<td>8.1</td>
<td>24.5</td>
</tr>
<tr>
<td>A.T.H.</td>
<td>7.1</td>
<td>22.6</td>
</tr>
</tbody>
</table>
It will be seen from the Table IV that whereas Tata and Republic showed a fall in assets formation, Canada, and ATH marked a fairly high rate of growth in assets.

It will be seen from Table V that net fixed assets formation was negative in Tata and Republic. The negative fixed asset formation occurred in Republic in spite of additions to reserves.

**Tata Iron and Steel Company**

In conclusion the main points of advantage/disadvantage to the Tata may be brought together.

1. The rate of profit earned by the Tata Steel is higher than the Steel Company of Wales and Republic Steel Corporation (U.S.A.) although it is lower than the Steel Company of Canada and ATH of West Germany.

2. Taxes form the lowest part of profit before tax in the case of the Tata Steel Co.

3. Retained profits as a percentage of profit before tax is highest in the Tata Steel.

4. Share Capital and Reserves do not fully cover net fixed assets in the Tata Steel whereas in Republic and Canada this is not so.

5. Assets formation declined in the Tata Steel Co.

6. Borrowed Capital is fairly high in the Tata Steel.

---

**TABLE V**

**SOURCES AND USES OF FUNDS**

(Amount in millions of national currencies)

<table>
<thead>
<tr>
<th>Sources and Uses</th>
<th>Tata (Rs.)</th>
<th>Wales ($)</th>
<th>Republic ($)</th>
<th>Canada ($)</th>
<th>ATH (D.M.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sources:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Capital</td>
<td>65.6</td>
<td>11</td>
<td>277.8</td>
<td>12.4</td>
<td>45.9</td>
</tr>
<tr>
<td>Reserves</td>
<td>-94.5</td>
<td>-19.6</td>
<td>2.6</td>
<td>-5.8</td>
<td></td>
</tr>
<tr>
<td>Total (Including Others)</td>
<td>-22.5</td>
<td>5.3</td>
<td>-15.1</td>
<td>30.0</td>
<td>120.2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Uses:</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net fixed assets</td>
<td>-57.4</td>
<td>1.8</td>
<td>-11.8</td>
<td>40.7</td>
<td>174.2</td>
</tr>
<tr>
<td>Inventory</td>
<td>15.8</td>
<td>1.5</td>
<td>-11.8</td>
<td>6.0</td>
<td>-9.4</td>
</tr>
<tr>
<td>Cash</td>
<td>6.9</td>
<td>-3.3</td>
<td>0.4</td>
<td>-21.5</td>
<td></td>
</tr>
<tr>
<td>Total (Including Others)</td>
<td>-22.5</td>
<td>5.3</td>
<td>-15.1</td>
<td>30.0</td>
<td>120.2</td>
</tr>
</tbody>
</table>
Length of the Indian Companies Act, 1956, with 674 sections and 13 schedules including the insertions made by the Amendment Act of 1960, is sometimes mentioned at certain quarters, though not always as an excuse for failure to comply with the procedural requirements of the Act. The critics very often forget that, apart from a series of complicated statutes directly bearing on the corporate sector which the Securities and Exchange Commission in the USA administers, the provisions in the Corporation Laws in different States in the USA are also numerous. The cumulative effect of all these statutory provisions is not merely to curb very materially the discretion of company management in many fields but also to exercise over many aspects of company policies a control which is unknown both in the U.K. and this country.

Diversity in State Laws—An instance

An instance of the detailed statutory regulation which has no comparable counterpart in the Indian or the U.K. Act to the same extent is found in the Corporation Laws in the USA in regard to the right of inspection by a stockholder, or by his agent or attorney, at any reasonable time or times, for any proper purpose, the books of account, minutes, records of stockholders and taking of extracts therefrom. However, the right of inspection is limited by statute in some of the States. For instance, in Alabama, any person who is a stockholder of record for at least 6 months immediately preceding his demand for inspection or who is the holder of record of at least 5% of all the outstanding shares of the Corporation may demand inspection either in person or by his agent or attorney. But in California any shareholder or holder of a voting trust certificate may demand inspection. The Californian law further provides that the right of the shareholders to inspect the corporate records may not be limited by the articles or by-laws. Refusal by an officer of the Corporation incorporated in Alabama to allow inspection to such stockholder or his agent renders him liable to the stockholder to a penalty of a specified percentage of the value of the shares owned by the latter, in addition to any other damages or remedy available to him by law. Detailed provisions have been made in many of the State laws so as to make it difficult both for the Corporation to refuse a legitimate request of the stockholder for inspection and also for the stockholder to misuse the right conferred on him by the statute. Again, in many States it is immaterial whether the shares are registered in his name, unless application is under a statute which by its terms is limited to “stockholders on record”. The right to inspect books of account, minutes, etc., is a substantive right and the courts in the USA have allowed inspection to stockholders so as to enable them to ascertain whether the affairs of the Corporation are being prudently and properly managed, to determine the advisability of a receivership, to determine the true value of the shares, etc. There are numerous other instances of divergence in the Corporation Laws of different States.

Trend towards uniformity—Model Business Corporation Act

While such variations in statutes in Sovereign States may have historical reasons, the need for a uniform law has been widely felt in that country. In order to provide...
State Commissions and Bar Association Committees with a working model for revision and modernisation of their corporate laws, the American Bar Association sponsored the preparation of a Model Business Corporation Act in 1930s. The initial draft of the Model Act, which was ready in 1946, was revised substantially in 1950 and 1953. The Model Act has been adopted almost without change in eleven jurisdictions.

**Compass of the Model Business Corporation Act.**

While the number of sections in the Corporation Laws in several States exceeds 400, there are only 143 sections in the Model Business Corporation Act. The first 46 of these sections are devoted to substantive provisions, such as objects, powers, corporate name, authorized and issued shares, directors, officers, meetings, books and records, etc. The next 52 sections cover procedures for incorporation, amendment, change in capital structure, merger, consolidation, sale of assets, dissolution, receivership and liquidation. 19 sections are devoted to the status, admission, withdrawal and ouster of foreign corporations. 10 sections deal with annual reports, fees, franchise taxes, and miscellaneous charges payable to the State. The remaining 18 sections cover penalties and miscellaneous matters. No provisions have been made in regard to several obsolete provisions noticed in the State Laws regarding the use of corporate seal, residential qualifications of directors, etc. While discarding the obsolete provisions of the existing law, the Committee, which prepared the draft of the Act, has also discarded "many of the liberal provisions found in States that have been bidding for corporate business."

"For example, it is possible in one State for a single individual to incorporate for all lawful purposes without specification, thus creating a one-man corporation in law as well as in fact, with statutory authority to transact any lawful business anywhere he chooses. The Model Act retains the requirements of three incorporators, a specification of purpose or purposes in the articles of incorporation, and at least 3 directors, because they are formally established in most States, even though regarded as fictional in many cases."

Some of the important provisions made in the Act with indications as to the provisions made in some of the State Laws in regard to the corresponding matters are stated in the succeeding paragraphs.

**Purpose**

The purposes for which business under a corporate shell could be organised are indicated in all State Acts. Corporation Act of one State (namely New York) contains a novel provision. That Act prohibits the formation of a corporation for the purpose of conducting any branch of the practice of law or of retaining or employing an attorney to furnish legal advice, draw legal documents, etc., for persons or corporations for whose use such services are rendered. Under the Model Act, banking and insurance corporations and corporations not for profit cannot be organised. The purposes for which a corporation may be organised must be stated in the articles of incorporation.

**Doctrine of Ultra Vires**

Section 6 of the Model Act abolishes the doctrine of ultra vires as to corporations except to the extent that the lack of corporate capacity and power can be asserted.—

(a) in proceedings by shareholders against a corporation,

(b) in proceedings against officers or directors, or

(c) in dissolution or injunction proceedings instituted by the Attorney-General.

**Corporate Name**

Restrictions on the use of certain words as part of name by a corporation vary from.
deal with these matters recognise the current provisions in all the States. Under Sec. 33 directors need not be residents of any particular State unless the articles or bye-laws so require. Sec. 34 fixes the minimum number of directors of a corporation at three. Retirement of one-third of directors at the annual meeting of shareholders has been prescribed under sec. 35.*

**Role of Shareholders**

The State Laws contain provisions entitling shareholders to participate in corporate activities through four channels, viz. election of directors, approval of certain operations which are void or voidable unless so ratified, approval of amendment to articles (and bye-laws if so provided in the articles of incorporation) which constitute the contract between the corporation and its shareholders and disposal of all assets not in the regular course of business, merger, consolidation or dissolution. Prof. Hornstein has summed up the position in regard to shareholders direct and indirect control in the following words:

"In areas not ordinarily within the directorial province, shareholders' control is indirect unless by unanimous vote the shareholders attempt to require action by the directors. In sharp contrast is the area of direct control, where the power in a majority of the shareholders extend even to cutting down the contractual rights and property rights of their fellow shareholders. In these latter areas of direct control principles of equity supply the variable factor.

"We must turn to statutes and articles and bye-laws to ascertain whether 100% or some lesser percentage of the voting shareholders determines their will as a body ("body politic"). The specific statutory percentage and the problem whether it is inflexible or may be lowered or raised ("super-statutory" majority) is crucial in

*Note: A detailed article on the "Powers of Directors" by S. M. Dugar follows this article.—Ed.
States require a foreign corporation to obtain authorization from the Secretary of State before doing any business, to file instruments designating agent and place of business with the State authority. Subject to local variations, the pattern followed in the State Laws in the matter is the same as that envisaged in sections 591-608 of the Indian Companies Act, 1956. The provisions in some of the statutes in this regard are largely based on those of the Model Act which are inspired in turn by an earlier Uniform Foreign Corporation Act. Sec. 99 of the Model Act indicates that the following activities shall not be considered "doing business in the qualification sense".

(a) Maintaining or defending any action or suit or any administrative or arbitration proceeding, or effecting the settlement thereof or the settlement of claims or disputes.

(b) Holding meetings of its directors or shareholders or carrying on other activities concerning its internal affairs.

(c) Maintaining bank accounts.

(d) Maintaining offices or agencies for the transfer, exchange and registration of its shares, or for any other purpose in relation to its shares or business.

Political Contributions
Under the Corporation Laws of several States (viz. Colorado, Connecticut, Georgia, New York, etc.), business corporations are prohibited from making political contributions. Under sec. 4 of the Model Act each corporation is empowered to make donations for the public welfare or for charitable, scientific or educational purposes; and in time of war to make donations in aid of war activities. Donation for other purposes is not permissible in terms of sec. 4.

Dissolution
Under the State Laws, the termination of the Corporation's existence as a juristic personality may be automatic or voluntary or involuntary. Life of a corporation comes to an end automatically at the conclusion of the period specified in the articles of incorporation. Many States provide for voluntary dissolution of a corporation earlier than the time fixed in its articles of incorporation. The circumstances in which the corporate life of a corporation may be terminated involuntarily are not uniform in all the States. While in some States the power in a court of equity to wind up a corporation at the suit of a minority shareholder is asserted when it is just and equitable to do so, other States disagree. Uniformity in this regard is sought to be secured under sections 75-94 which deal with various modes of dissolution, qualifications and powers of receivers, deposit with the State Treasury of amounts due to certain shareholders, survival of remedy after dissolution, etc. Some of the requirements specifically laid down in Part VII of the Indian Companies Act, 1956 are sought to be regulated by sections 77, 78, 87, 90 and 91 of the Model Act.

Foreign Corporation
States Laws require a foreign corporation to obtain authorization from the Secretary of State before doing any business, to file instruments designating agent and place of business with the State authority. Subject to local variations, the pattern followed in the State Laws in the matter is the same as that envisaged in sections 591-608 of the Indian Companies Act, 1956. The provisions in some of the statutes in this regard are largely based on those of the Model Act which are inspired in turn by an earlier Uniform Foreign Corporation Act. Sec. 99 of the Model Act indicates that the following activities shall not be considered "doing business in the qualification sense".

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Securities, or appointing and maintaining trustees or depositaries with relation to its securities.

(e) Effecting sales through independent contractors.

(f) Soliciting or procuring orders, whether by mail or through employees or agents or otherwise, where such orders require acceptance without this State before becoming binding contracts.

(g) Creating evidences of debt, mortgages, or liens on real or personal property.

(h) Securing or collecting debts or enforcing any rights in property securing the same.

(i) Transacting any business in interstate commerce.

(j) Conducting an isolated transaction completed within a period of thirty days and not in the course of a number of repeated transactions of like nature.
U.S. CORPORATION LAWS AND THE CORPORATION DIRECTORS

By
S. M. DUGAR
Senior Accounts Officer

Preliminary

In the United States there is no Federal Corporation Law as obtaining in India in the form of a Companies Act. The United States is a federation of many States which have delegated only a limited measure of authority to the Federal Government under their jealously guarded Constitution. Hence each individual State has jurisdiction over Corporations formed or operating within the State. There is a considerable variation in the nature and strictness of the various State laws dealing with the control of the business corporations. In the recent years, the Federal Government has been exerting an increasing influence over corporations through its power to tax, to regulate interstate commerce etc. A move for uniformity in inter-State laws for control of business corporations formed in various States has also been sponsored by the American Bar Association. The Model Business Corporation Act provides the basis for re-modelling the existing corporate laws in the different States. In this article the position obtaining in the United States has been discussed mainly with reference to the provisions of the ABA Model Business Corporation Act and a particular attention has been paid to only notable departures or certain salient features in the other State Statutes.

A particularly important feature which deserves to be mentioned at this stage is that the Indian law recognises more than one category of companies viz., public and private. In respect of companies falling in the latter category (which are neither subsidiaries of public companies nor deemed public companies within the meaning of Section 43A of the Indian Act), the provisions of the Indian law are much less stringent and have a considerable amount of flexibility too. In the matter of drawing comparison with the Indian law, reliance has been placed only on the provisions which are applicable to public companies.

Constitution of the Board and term of Office of Directors

The ABA Model Business Corporation Act provides that every corporation must have at least 3 directors. Subject to this limitation, the number of directors is left to be fixed by the by-laws, except as to the number constituting the initial Board of Directors which is required to be fixed by the Articles of Incorporation. The names and addresses of the first Board of Directors are to be stated in the Articles of Incorporation and such persons hold office until the first annual meeting of the shareholders and until their successors are elected and qualified. Most of the State laws contain provisions on the above lines; the few exceptions being Arizona, Iowa, Mississippi, Rhode Island, South Carolina and South Dakota where no minimum is prescribed and Missouri, Montana, North Dakota, South Carolina and Utah where the statute provides for the maximum number ranging from 13 to 25. Half the States require that the articles should list the names and addresses of the directors until the first meeting of the shareholders; the effect is not different under the other statutes which vest management in the incorporators until the directors are elected. The object in either case is to assure that the enterprise will have directors from the moment of its incorporation.

As regards the classification of directors (meaning rotation of directors in the Indian
Qualifications

The qualifications of directors are allowed to be provided by the Articles of Incorporation or by-laws under the Model Business Corporation Act. The requirement of State residence or United States citizenship or both appears only in about a dozen State statutes. The requirement that directors be natural persons of "full age" appears in only half a dozen State statutes: elsewhere minors conceivably may qualify as directors. Most State statutes provide that a director need not be a shareholder, unless required by the articles or by-laws: the opposite approach is taken by two States which demand that a director should be a shareholder unless otherwise provided in the certificate of incorporation or in a by-law; a third type of statute prescribes share-ownership by a director and does not permit it to be negatived.

In the Indian law the provisions relating to the qualifications of directors are contained in sections 270 and 271. These provisions only prescribe the maximum limit of the shareholding which could be...
provided in the articles of association of a company and require a director to file a declaration with the Registrar of Companies specifying the qualification shares held by him. There is, however, no statutory requirement that a director must hold any shares at all and it is left to the articles of association of the company to prescribe a regulation in this regard. The Indian law does not contain any restriction as to residence of persons who could be directors.

**Filling of vacancies**

The Model Business Corporation Act provides that the vacancies in the Board have to be filled by the affirmative vote of a majority of the remaining directors, may be less than a quorum of the Board of Directors. A director elected to fill a vacancy holds office for the unexpired term of his predecessor in office. The additional directors can, however, be appointed only by election at an annual meeting or at a special meeting of the shareholders called for that purpose.

The provision relating to filling of casual vacancies in the United States law is almost in line with the provision of Sec. 262 of the Indian Companies Act. As regards the appointment of additional directors, the Indian law, however, is rather liberal inasmuch as it empowers the Board to make the appointment, provided the number does not exceed the maximum fixed by the articles of association. Such additional directors are permitted to hold office only up to the date of the next annual general meeting of the company.

**Consent of Directors**

In the United States laws there are no provisions corresponding to sections 264 and 266 of the Indian Act. It is, however, recognised that election to office as a director does not ipso facto make one a director. As essential as election is acceptance. His acceptance of the office, unless formal, is therefore implied from his first act as a director.

**Remuneration**

Directors (unless also officers) are presumed to act gratuitously in performing services within the scope of the duties as directors. The rationale suggested is that they are acting as trustees for the shareholders or that they are motivated by the prospect of increasing return on their shares. They are entitled to compensation, however (i) if remuneration was agreed upon in advance, expressly or by implication, or (ii) without prior agreement, if services are outside the scope of the duties as directors. Of course, ratification by the shareholders can always authorise payment of compensation to a director. A director who is also an officer is an employee and is regarded as entitled to compensation for services. Under the Model Act, the Board of Directors have the authority to fix the compensation of directors unless otherwise provided in the Articles of Incorporation. The United States laws do not contain any provisions on the lines of sections 309, 318 and 319 of the Indian Act which lay down the ceiling on remuneration or compensation that could be paid to a director.

**Disqualifications of directors**

Unlike the provisions of Sec. 274 of the Indian Companies Act, there are no disqualifications specifically enumerated in the United States laws. Suggestive disqualifications are, however, found for special classes of corporations. In New York, for example, the insurance law disqualifies as a director a person convicted of any crime involving fraud, dishonesty or like moral turpitude or is an untrustworthy person. Amongst the Federal statutes, the Investment Companies Act prohibits a person from serving as an officer or director to perform certain other functions for an investment company registered under that statute if he has been convicted of certain crimes involving security transaction, or if by reason of similar misconduct he has been enjoined from specified activities.
Removal of directors without court process

A director is removable without court process and without cause prior to the expiration of his term of office only if authorization is found in the statute or the articles or by-laws. This power of removal is granted by the statutes in some States and in other States developing law and practice now tends to sustain such a provision in the articles or by-laws. Under the Model Business Corporation Act the provision relating to such removal of directors has been provided as an optional clause. The provisions of the Model Business Act *inter alia* provide that for the removal of directors with or without cause a meeting has to be called expressly for the purpose and that the entire Board of Directors can also be removed by a vote of the holders of majority of the shares then entitled at an election of directors.

It appears that for cause (e.g. misconduct or action inimical to the Corporation) a director is removable even in the absence of any specific provision in the articles or by-laws; the inherent power to remove for misconduct is regarded one of the oldest common law doctrines in the United States. The removal, however, must be either by the Board or by a majority of the shareholders. Though no specific procedure is provided under the common law, it appears that the accused director must be given notice of the charge against him and an opportunity to be heard in his own defence.

In the Indian law, the corresponding provisions appear in Section 284 which provides for the procedure to be adopted in the event of removal of a director before the expiry of his period of office. Such removal has to be effected by an ordinary resolution for which a special notice is required and the director concerned is entitled to make a representation to the shareholders against his removal.

Removal of directors by court process

Removal of directors by court process is not specifically provided in the Model Business Corporation Act. Statutory provisions in a few States, however, authorize a court to remove a director for cause where majority of the shareholders are unwilling to act. California, North Carolina, and Pennsylvania empower minority shareholders owning at least a specified percentage of the outstanding shares (e.g. 5% or 10%) to institute proceedings for the ouster of directors guilty of fraudulent or dishonest acts or gross abuse of authority or discretion; it is immaterial whether the movant's shares have voting rights. The Michigan statute permits judicial relief to be invoked by any shareholder—without specifying any such minimum, or by any director, officer or creditor or receiver or trustee in bankruptcy or by Attorney-General. In New York, only the last named appears to be so empowered by the statute. He *must* sue where he has reason to believe that—the public interest requires such action to be brought; also he *must* sue upon an application by a creditor, stockholder or director if the Attorney General has reason to believe that an action can be maintained in behalf of the people. Isolated statutes, e.g. SEC, etc. also authorize removal of a director in special situations.

Quorum at Board meeting

A majority of the number of directors fixed by the by-laws, or in the absence of a by-law fixing the number of directors, then of the number stated in the Articles of Incorporation, constitute a quorum for transaction of business under the provisions of the Model Act. The Articles of Incorporation or the by-laws may, however, provide a greater number than bare majority. The provisions of most of the State statutes are on similar lines. In a few cases, the determination of the quorum is made subject to the provision in the articles or by-laws so as to enable to have the quorum (i) a percentage less than a majority, (ii) a percentage
either more or less than a majority, provided that a lesser percentage be not less than one-third or two directors, (iii) a lesser number than a majority, but not less than one-third. Still another variation is found in an isolated case which does not state what percentage constitutes the quorum but directs the by-laws to do so.

The provisions of the Indian law in this regard are contained in sec. 287. According to the said provisions, at least 2 disinterested directors or one-third of the total strength, whichever is higher, must be present at the meeting in order to constitute the quorum.

Necessity for formal Board meeting and designation of committees

Statutes in 3/4ths of the States declare that the business of a corporation shall be managed by its Board of Directors. This statutory provision has long been construed to permit directors to bind the corporation only when they act as a body. The judicial principle recognised in the United States is that the power envisaged in directors to control and manage the affairs of the Corporation is not joint and several but joint only. The judicial analysis goes further to provide that even purported authority in the Corporation's Charter was ineffective to permit action without a meeting. A dozen statutes, however, expressly declare that any action required or permitted to be taken at any meeting of the Board of Directors may be authorised by written consent of all directors without a meeting. Even though informal procedure by directors (i.e., written consent in place of meeting) is not recommended in the Model Business Corporation Act (perhaps a deliberate omission, especially significant because the Model Act does permit unanimous consent in writing in place of shareholders meeting) the Model Act, however, does provide for delegation of authority to committees. Subject to the provision in the Articles of Incorporation or by-laws, the Board by resolution adopted by a majority of the full Board of Directors, may designate from among its members an Executive Committee and one or more other committees, each of which may exercise all the authority of the Board of Directors. Delegation of certain powers is, however, expressly prohibited, viz. (i) amending the Articles of Incorporation or the by-laws, (ii) adopting a plan of merger or consolidation, (iii) recommending to the shareholders sale, lease, exchange, mortgage, pledge or other disposition of all or substantially all the property and assets of the Corporation otherwise than in the regular course of its business, or (iv) recommending to the shareholders a voluntary dissolution of the Corporation. The designation of any such committee and delegation thereto of authority does not operate to relieve the Board of Directors or any member thereof of any responsibility imposed by law.

In this context attention might be invited to the provisions of sections 292 and 293 of the Indian Act which impose restrictions on the general powers of directors. Under Sec. 292 certain powers, e.g., power to make calls, to issue debentures, to borrow moneys, to invest the funds of the company, and to make loans are exercisable only at a meeting of the Board; in respect of investment and loans, delegation is, however, allowed if the Board so decides. Sec. 293 deprives the directors of certain powers, e.g., to sell, lease or otherwise dispose of whole or substantially the whole of the undertaking of the company, remit any debt due by a director, borrow moneys beyond a specified quantum and contribute to charitable or other funds not directly related to the business of the company beyond the specified limit; the law provides that these powers shall be exercised by the company in general meeting.

Individual rights of a Director

Although most directorial powers are exercisable collectively and only by the Board as a unit, a few rights do exist for directors
as individuals. Since, a director cannot properly perform his duties without being well informed about the Corporation's affairs, he has the co-relative right to inspect the corporate books and records. No specific provision in this regard appears in the Model Act or the other State statutes, though this right is universally recognised in the United States. In the Indian law, however, there is a specific provision in sec. 209 providing the director with the right to inspect the books of account during the business hours.

**Powers, duties and liabilities of Directors**

The Model Act provides that business of the Corporation shall be managed by the Board of Directors. Many State statutes have also a provision on the same lines. Whether expressly provided in the statute or not, the principle recognised in the United States is that the function of the Board of Directors is to manage the business of the Corporation and in order to do so it may exercise all necessary powers. Accordingly, directors ordinarily formulate the policy of the Corporation. It is expected of them to delegate or assign to the officers the duty of actually operating the Corporation. Among other powers is the power to declare dividends which is regarded in all States as a function of the directors, leaving open only the question of the extent to which it may be controlled by the shareholders' action. Sharp division is found, however, among the States as to whether the shareholders or directors shall laws. The States are roughly divided into four groups; The first group (e.g. Ohio) vests this power exclusively in the shareholders; the second group (e.g. New York) vests it in the shareholders but allows delegation to directors subject to overriding control by the shareholders; the third group (e.g. Maryland, Texas) vests it in the shareholders unless and to the extent to which it is vested in the directors by the Articles of Incorporation; and the fourth group (e.g. Illinois) has changed the approach and gives this power to the directors unless reserved to the shareholders in the Articles of Association (corresponding to is the provision recommended by the Model Act. This is in contrast to the Indian law which specifically prescribes for Articles of Incorporation. This fourth type by-laws in the U.S. context) to be altered only by a special resolution of the shareholders.

Co-extensive with the directors' powers are certain responsibilities. He is under an obligation to exercise his powers and to do so properly, he is required to be honest and to act in good faith; he is also expected to be diligent and this responsibility is not overlooked by the Courts in the United States. In practice, complaints concerning corporate misconduct are grounded upon violation of equitable principles and not upon rights accorded by any specific statute. These standards have been enforced by the courts in the United States with little or no aid from legislature.

Most of the States have no legislation setting forth standards for directorial conduct other than to prevent asset distribution which might prejudice creditors (e.g. loans to directors, officers, shareholders, dividends, stock purchases). Half a dozen States stimulated by the recommendation in the Model Act have now spelled out directorial liability in a single section. The statutory limitations brought together in the Model Act prescribe liability for (i) commencing business before a specified amount (e.g. $1,000) has been paid in, (ii) loans to shareholders on the security of the shares or to a director or officer, (iii) declaration by law of dividends out of a source not sanctioned by law., (iv) purchase by the Corporation of its own shares out of a source not sanctioned by law., and (v) distribution of assets without adequate provision for payment of debts. Similar restrictions also find place in the Indian law e.g. in Sections 69, 77, 205 and 295.
One noteworthy provision contained in the Model Act is that a director of a Corporation who is present at a meeting of the Board of Directors at which decision on any corporate matter is taken, is presumed to have assented thereto unless his dissent is entered in the minutes of the meeting or unless he files his written dissent to such action with the person acting as Secretary of the meeting. It appears that this provision lays down the onus on a director to repudiate his liability to a decision at a Board meeting. This wholesome provision does not find place in the Indian law.