

CUET · BUSINESS STUDIES · CLASS XI · CODE 305

Formation of a Company

CUET unit: Formation of a Company (Corporate Organisation, Finance and Trade)

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Snapshot

- Establishes the three stages through which a company comes into legal existence: Promotion, Incorporation, and Capital Subscription (the last applies only to a public company raising funds from the public).
- Defines a promoter, lays down statutory tests under section 69, and details promoter functions from idea-identification to filing documents with the Registrar of Companies (ROC).
- Lists and explains every document required for incorporation — Memorandum of Association (MOA), Articles of Association (AOA), consent of directors, agreements with MD/Manager, statutory declaration, and registration fee receipt.
- Explains why the Certificate of Incorporation is "conclusive evidence" of a company's legal birth, supported by NCERT case-illustrations.
- Covers the SEBI-supervised capital subscription steps — prospectus filing, appointment of bankers/brokers/underwriters, minimum subscription (90%), stock-exchange listing, allotment, and return of allotment.



Detailed Notes

2.1 Core concepts

- Modern business needs large funds and faces high risk, so the company form is preferred for medium and large organisations (NCERT §7.1, p. 153).
- The steps from the origin of a business idea to the legal readiness to commence business are called "stages in the formation of a company"; those who take these steps and bear the associated risks are called **promoters** (NCERT §7.1, p. 153).
- Formation has three distinct stages: (i) Promotion, (ii) Incorporation, and (iii) Subscription of capital. A private company is prohibited from raising funds from the public, need not issue a prospectus, and need not complete minimum subscription — so it skips stage (iii) (NCERT §7.2, p. 153).
- **Promotion** begins with the discovery of a potential business idea by a person, group, or company; on deciding to form a company around it, they become promoters (NCERT §7.2.1, p. 153–154).
- Statutory definition under section 69 — a promoter is a person (a) named as such in a prospectus or identified in the company's annual return under section 92; (b) who

controls the affairs of the company directly or indirectly as a shareholder, director or otherwise; or (c) in accordance with whose advice, directions or instructions the Board is accustomed to act — excluding persons acting purely in a professional capacity (NCERT §7.2.1, p. 154).

- **Functions of a promoter:** (i) identification of business opportunity, (ii) feasibility studies — technical, financial and economic, (iii) name approval, (iv) fixing signatories to MOA, (v) appointment of professionals (merchant bankers, auditors etc.), and (vi) preparation of necessary documents (NCERT §7.2.1, p. 154–156).
- **Name Clause / Name approval:** Three names in order of priority are submitted to the ROC in form INC-1. A name is "undesirable" if it is identical with / too closely resembles an existing company's name, if it is misleading, or if it violates the Emblems and Names (Prevention of Improper Use) Act, 1950 — which protects names/emblems of UNO, WHO, UNESCO, Government of India, State Governments, President, Governor, the National Flag, etc. (NCERT §7.2.1 box, p. 155).
- **Documents to ROC at incorporation:** A. Memorandum of Association; B. Articles of Association; C. Consent of proposed directors; D. Agreement with MD/whole-time director/Manager (if any); E. Statutory declaration; F. Receipt of payment of fee (NCERT §7.2.1, p. 156–158).
- **MOA** — section 2(56) of the Companies Act, 2013 — defines the objects of the company. No company can legally undertake activities outside its MOA. The MOA must be signed by **at least 7** members in a public company and **2** in a private company (NCERT §7.2.1, p. 156–158).
- **MOA clauses:** (i) Name clause, (ii) Registered office clause — names only the state (exact address to be notified to ROC within 30 days of incorporation), (iii) Objects clause (most important — defines purpose; acts essential or incidental to main objects are valid), (iv) Liability clause (limits liability to amount unpaid on shares), (v) Capital clause (specifies maximum/authorised share capital and its division into shares of fixed face value) (NCERT §7.2.1, p. 156–157).
- MOA forms by company type — Table A: limited by shares; Table B & C: limited by guarantee, no share capital; Table D: unlimited, no share capital; Table E: unlimited, having share capital (NCERT §7.2.1 box, p. 157).
- **AOA** — section 2(5) of the Companies Act, 2013 — contains rules for the **internal management** of the company. AOA is subsidiary to the MOA and must not contradict or exceed it. AOA forms are in Tables F, G, H, I, J of Schedule I; companies may adopt their own articles, which then override the Tables (NCERT §7.2.1, p. 158).
- **Qualification Shares:** Articles usually require directors to buy a certain number of shares to ensure they have a stake; payment is required before the Certificate of Commencement of Business is obtained (NCERT §7.2.1 box, p. 159).
- **Statutory declaration** that all legal requirements for registration are complied with may be signed by an advocate, Chartered Accountant, Cost Accountant, Company

Secretary in practice engaged in the formation, **or** a person named in the articles as director, manager or secretary (NCERT §7.2.1, p. 158–160).

- **Position of promoters:** They are **neither agents nor trustees** of the company (the company is not yet incorporated). They are personally liable for pre-incorporation contracts unless ratified. They occupy a **fiduciary position** — must disclose profits, cannot make secret profits; non-disclosure lets the company rescind the contract, recover the purchase price, and claim damages. Promoters are not legally entitled to reimbursement of pre-incorporation expenses, though the company may choose to reimburse them, pay a lump sum/commission, or allot shares/debentures/options (NCERT §7.2.1, p. 160).
- **Preliminary (pre-incorporation) Contracts:** Made by promoters with third parties on behalf of the company before incorporation; **not legally binding** on the company; the company cannot **ratify** them but may enter fresh contracts on the same terms; promoters remain personally liable to third parties (NCERT §7.2.1 box, p. 161).
- **Incorporation:** Promoters apply to the ROC of the state where the registered office is proposed, along with: (1) MOA duly stamped/signed/witnessed (7 signatories for public, 2 for private — with address, occupation, shares subscribed); (2) AOA stamped and witnessed (a public company may adopt Table A — in that case a Statement in Lieu of Prospectus is submitted instead of AOA); (3) Written consent of proposed directors with undertaking to purchase qualification shares; (4) Agreement with proposed MD/Manager/whole-time director, if any; (5) Copy of Registrar's letter approving the name; (6) Statutory declaration; (7) Notice of exact registered-office address (may be submitted later, within 30 days of receipt of certificate of incorporation); (8) Documentary evidence of registration fees paid (NCERT §7.2.2, p. 160–161).
- The ROC must be satisfied that documents are in order and statutory requirements are complied with, but is not duty-bound to investigate authenticity of the facts in them. Once satisfied, the ROC issues the **Certificate of Incorporation** — the "birth certificate" of the company. From **1 November 2000**, the ROC also allots a **CIN (Corporate Identity Number)** (NCERT §7.2.2, p. 161).
- **Effect of Certificate of Incorporation:** The company is legally born on the date printed on the certificate; it acquires perpetual succession and can contract validly. The certificate is **conclusive evidence** of regularity of incorporation — illustrated by (a) Re documents filed 6 Jan but certificate dated 8 Jan: contracts of 6 Jan held valid because of the date on the certificate, and (b) signatures forged on MOA: incorporation still held valid. Even if the company is registered with illegal objects, its birth cannot be questioned — the only remedy is winding up. Both public and private companies must obtain the **Certificate of Commencement of Business within 180 days** of incorporation before undertaking operations (NCERT §7.2.2, p. 162).
- **Director Identification Number (DIN):** Every individual intending to be appointed as director must apply to the Central Government for a DIN in the prescribed form

with fees; the Central Government allots it within one month; no individual may possess more than one DIN (NCERT §7.2.2 box, p. 162).

- **Capital Subscription (public companies only):** Steps are (i) SEBI approval — SEBI regulates disclosure and investor protection; (ii) Filing of prospectus or statement in lieu of prospectus with ROC — prospectus is any document inviting public deposits/offers for securities of a body corporate; (iii) Appointment of bankers (to receive application money), brokers (to encourage applications) and **underwriters (optional)** who undertake to buy unsubscribed shares for a commission; (iv) **Minimum Subscription** — per SEBI Guidelines, **90%** of the issue size; if not received, allotment cannot be made and money must be returned; (v) Application to at least one stock exchange — if listing not granted within **10 weeks** of closure of subscription list, allotment is **void** and money must be returned within **8 days**; (vi) Allotment of Shares — application money kept in a separate bank account till allotment; excess money is returned or adjusted; allotment letters are issued; **Return of Allotment**, signed by a director/secretary, is filed with ROC within **30 days** of allotment (NCERT §7.2.3, p. 163–165).
- **Difference between MOA and AOA** — MOA defines objects; AOA gives internal management rules. MOA is the main document and is subordinate to the Companies Act; AOA is subsidiary and subordinate to both the MOA and the Companies Act. MOA defines the company's relationship with outsiders; AOA defines the relationship of members and the company. Acts ultra vires the MOA are void and cannot be ratified even unanimously; acts beyond AOA can be ratified by members if not violative of MOA. MOA is compulsory for every company; AOA is not compulsory for a public ltd. company (it may adopt Table F) (NCERT §7.2.3 table, p. 164).
- **Provisional Contracts:** Contracts signed after incorporation but before commencement of business (NCERT Summary, p. 169).

2.2 Definitions to memorise

Term	Definition	Page
Promoter	A person who undertakes to form a company with reference to a given project, sets it going, and takes the necessary steps to accomplish that purpose; statutorily defined under section 69.	154
Memorandum of Association	Document defining the objectives of the company; section 2(56), Companies Act, 2013; no company can legally undertake activities outside it.	156
Articles of Association	Rules regarding internal management of a company; section 2(5), Companies Act, 2013; subsidiary to MOA.	158
Qualification Shares	Shares directors must buy and pay for before the Certificate of Commencement of Business is obtained, to give them a stake in the company.	159
Prospectus		163

Term	Definition	Page
	Any document described or issued as a prospectus (notice, circular, advertisement etc.) inviting deposits from the public or offers from the public for subscription/purchase of securities of a body corporate.	
Minimum Subscription	The minimum number of shares the company must receive applications for before allotment; per SEBI Guidelines, 90% of the issue size.	163
Certificate of Incorporation	The "birth certificate" of the company issued by ROC; conclusive evidence of the legal existence of the company.	161
Return of Allotment	Statement signed by a director or secretary, filed with the ROC within 30 days of allotment, giving particulars of shareholders and shares allotted.	165
Preliminary Contracts	Contracts entered into by promoters with third parties on behalf of the company before incorporation; not binding on the company; cannot be ratified.	161
Provisional Contracts	Contracts signed after incorporation but before commencement of business.	169
DIN	Director Identification Number; allotted by Central Government within one month; no individual can hold more than one.	162
CIN	Corporate Identity Number; allotted to the company by ROC with effect from 1 November 2000.	161
Name Clause	MOA clause stating the name of the company; must end with "Limited" or "Private Limited"; subject to ROC approval.	156
Registered Office Clause	MOA clause naming the state where the registered office is to be situated; exact address notified within 30 days of incorporation.	156
Objects Clause	MOA clause defining the purpose for which the company is formed — the most important MOA clause.	156
Liability Clause	MOA clause limiting members' liability to amount unpaid on shares.	157
Capital Clause	MOA clause stating the maximum (authorised) share capital and its division into shares.	157
Underwriter	Person who undertakes to buy unsubscribed shares for a commission.	164
Banker (to issue)	Bank appointed to receive application money from the public on behalf of the company.	164
Allotment	Acceptance of share applications by the company; allotment letters are issued.	164
Statement in Lieu of Prospectus	Document filed with ROC by a public company adopting Table A model articles instead of issuing a prospectus.	161

Term	Definition	Page
Promotion	First stage of company formation — discovery of idea, feasibility study, name approval, signatories to MOA, appointment of professionals, preparation of documents.	153
Incorporation	Second stage — filing of MOA/AOA and other documents with ROC, payment of fee, issuance of Certificate of Incorporation.	153, 160
Capital Subscription	Third stage (public companies only) — SEBI approval, prospectus, minimum subscription, listing, allotment, return of allotment.	153, 163
Fiduciary position	Promoter's legal position — must disclose profits, cannot make secret profits; non-disclosure lets company rescind contract.	160

2.3 Diagrams / processes to remember

- **Three-stage flow of company formation** — Promotion → Incorporation → Capital Subscription (the last only for public companies raising funds from the public) (p. 153, summarised again p. 168–169).
- **Box on the Name Clause** — three grounds on which a proposed name is undesirable (identical/similar, misleading, violative of Emblems and Names Act, 1950) (p. 155).
- **Two boxed tables** — Tables A–E for forms of MOA by company type; Tables F–J for AOA by company type (p. 157).
- **AOA contents checklist** — a 33-item list including issue/allotment of shares, calls, lien, forfeiture, buy-back, voting rights, directors' appointment, borrowing powers, winding up, etc. (p. 159).
- **MOA vs AOA comparison table** — five bases: Objectives, Position, Relationship, Validity, Necessity (p. 164).
- **Table A of Schedule I** — model MOA of a company limited by shares: name, registered office (state), objects (and matters necessary for furtherance), liability, share capital, subscriber list, OPC clauses 7th and 8th (nominee) (p. 166–167).

2.4 Common confusions / NTA trap points

- **Section confusion:** "Memorandum" is defined in **section 2(56)**; "Articles" in **section 2(5)**; the statutory definition of "promoter" cited in this chapter is **section 69**. NTA may swap these.
- **Signatories:** MOA needs **at least 7 signatories for a public company** and **at least 2 for a private company** — students often invert these.
- **Conclusive evidence rule:** Even forged signatures on the MOA or registration with illegal objects do **not** invalidate the certificate of incorporation; the only remedy is winding up. Distractors often say "the certificate becomes void".

- **Minimum subscription is 90% of issue size (SEBI Guidelines)**, not 75% or 100%. The 10-week window for stock-exchange listing and the 8-day refund window are also frequent traps.
- **Promoters' position** — they are neither agents nor trustees; they hold a **fiduciary** position. They are personally liable for pre-incorporation (preliminary) contracts; the company can never **ratify** these (it can only enter fresh contracts).
- **Registered office clause** at incorporation gives only the **state** — the exact address is notified to the ROC within **30 days** of incorporation.
- **AOA may be skipped** by a public company if it adopts Table A (model articles); in that case a **Statement in Lieu of Prospectus** is filed.
- **Functions of management vs functions of a promoter** — both are six-item lists in CUET land and items can be mis-classed. Promoter functions are formation-stage (idea, feasibility, name approval, signatories, professionals, documents); management functions are post-incorporation.
- **180-day window for commencement of business** — both public and private companies must obtain the Certificate of Commencement of Business **within 180 days** of incorporation. Students often confuse this with the 30-day registered office notification.
- **CIN allotment** — Corporate Identity Number has been allotted by the ROC with effect from **1 November 2000**. NTA item-writers sometimes plant earlier years as distractors.

2.5 Case examples

- **Reliance Industries — public issue (NCERT context, § 7.2.3)** — Reliance's marquee 1977 public issue is the canonical Indian example of how a public company moves through the Capital Subscription stage: SEBI-like regulatory approval (then by the Controller of Capital Issues), prospectus filing, public application, allotment and listing on multiple stock exchanges — illustrating equity issues and minimum subscription.
- **One Person Company (OPC) provisions in Table A (NCERT p. 167)** — Table A's clauses 7 and 8 specifically address OPC formation, introduced by the Companies Act 2013. The OPC structure lets a single member form a company with a nominee, so the MOA must include a nominee clause for OPCs.
- **Pre-incorporation contract case illustrations (NCERT p. 160-161)** — a promoter who signs a lease "on behalf of the proposed company" before incorporation remains personally liable; the company can only enter a fresh contract on similar terms after incorporation. This is the canonical CUET stem on promoter liability.
- **Certificate of Incorporation conclusive-evidence cases (NCERT p. 162)** — (a) where documents were filed on 6 January but the certificate was dated 8 January, contracts of 6 January were held valid because the certificate's date is conclusive;

(b) where signatures on the MOA were proved to be forged, incorporation was still held valid. These two illustrations are quoted verbatim in CUET assertion-reason items.

- **DIN/CIN modernisation (NCERT box, p. 162)** — the DIN/CIN framework, introduced from 1 November 2000, modernised Indian company formation, linking formation (CIN) and director governance (DIN).

Practice MCQs

Q1. Which of the following is NOT one of the three stages in the formation of a company?


- A. Promotion
- B. Incorporation
- C. Capital Subscription
- D. Liquidation

Q2. a promoter is statutorily defined under which section?

- A. Section 2(5)
- B. Section 2(56)
- C. Section 69
- D. Section 92

Q3. Match List I (Document/Clause) with List II (Description) and choose the correct answer. | List I | List II | |---|---| | (a) Objects clause | (i) States the maximum capital to be raised by issuing shares | | (b) Capital clause | (ii) Limits members' liability to the unpaid amount on shares | | (c) Liability clause | (iii) Defines the purpose for which the company is formed | | (d) Registered office clause | (iv) States the name of the state where the registered office is to be situated |

- A. a-iii, b-i, c-ii, d-iv
- B. a-ii, b-iv, c-iii, d-i
- C. a-iv, b-iii, c-i, d-ii
- D. a-i, b-ii, c-iv, d-iii

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PYQ Alignment

Formation of a Company has been a consistent CUET Business Studies area, with the Unit-3 (Corporate Organisation, Finance and Trade) yielding around 8–10 MCQs per year across 2023–25 papers. NTA's favourite hooks here are: signatory counts for MOA (7 vs 2), MOA clause vs AOA distinction, minimum subscription (90%), conclusive-evidence rule of the Certificate of Incorporation, and the legal position of promoters (fiduciary, neither agent nor trustee, no automatic right to reimbursement).

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