

Need to amend Section 560 of Companies Act

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Until recently it was considered to be an easy task to incorporate a company as a company could be incorporated with paid-up capital as low as Rs 700. This has resulted in the formation of a large number of companies which do not commence any business after registration with Registrar of Companies (ROC). In order to get rid of such non-functional companies, Section 560 of the Companies Act, 1956 (the act), empowers ROC to strike off names of these companies from the register maintained by ROC; but this has not proved to be an effective remedy as very rarely an action is initiated by ROC. Therefore, in order to altogether eradicate such companies and also to restrain non-serious promoters from incorporating companies, Companies (Amendment) Act, 2000, has amended Section 3 of the Companies Act, 1956, and the amended Section requires every private and public company to raise its paid-up share capital to at least Rs 1 lakh or Rs 5 lakh, respectively, within a period of two years from the commencement of the Companies (Amendment) Act, 2000, in case the existing paid-up share capital is below the aforesaid limits. Section 3(5) of the act further provides that in case any such company fails to enhance its paid-up share capital within the stipulated time period, it shall be deemed to be a defunct company within the meaning of Section 560 of the act, and its name shall be struck off from the register by ROC.

The purpose of Section 560 of the act is to weed out non-functional companies which do not carry any business or operation. Section 560 prescribes a procedure to be followed before the name of a company can be struck off from the register, maintained by ROC, as a defunct company. The aforesaid procedure requires ROC to send two notices to the company to enquire whether it is carrying any business or operation. In case ROC does not receive any reply to the notices or the company itself confirms that it is not carrying any business or operation, a notice may be published in the official gazette notifying that at the expiry of three months from the date of publication of the notice, ROC will strike off the name of company from register unless a cause is shown to the contrary. On striking off the name in the aforesaid manner, the company gets dissolved.

The purpose of following this lengthy and time consuming procedure is to provide adequate opportunity to the company as well as to others who may be interested in the functioning of the company to present their case before ROC. Therefore, as per Section 560, names of only those companies are to be struck off from the register, which do not carry any business or operation, whereas Section 3(5) provides that names of all private and public companies which fail to raise their paid-up share capital to Rs 1 lakh or Rs 5 lakh, as the case may be, will be struck off from the register, irrespective of the fact whether the company is carrying on any business or operation. The striking off of names of companies in this manner is not only harsh as it is against the interests of members, creditors and employees of companies, but also against the letter and spirit of Section 560 of the act.

Therefore, there seems to be a contradiction between the provisions of Section 3(5) and Section 560 of the act, as Section 3(5) deems a company to be defunct if it does not fulfil the requirements of minimum paid-up share capital, whereas Section 560 deems a company to be defunct if it does not carry on any business or operation. For instance, if a public company carries on business activities with paid-up share capital of Rs 4 lakh only, it will be deemed to be defunct under section 3(5), but it will not be deemed to be defunct under section 560, so how can ROC have the power to strike off the name of such a company from the register?

The only solution to this problem is an amendment of Section 560 of the act, so as to enable the ROC to strike off the names of even those companies which are functional but are having paid-up share capital below the limits specified under section 3(3) and 3(4) of the act. Moreover, recently, the department of company affairs had also introduced a scheme namely, 'Fast Track Section 560 Scheme', which provided an easy exit route to companies not carrying any business or operation. The scheme required such companies to file an application with ROC in prescribed forms, along with duly executed indemnity, affidavits and other related documents, requesting ROC to strike off the name of company from the register as a defunct company. Therefore, the scheme required companies to take the first step of initiating action instead of an action being initiated by ROC as required by Section 560. Therefore, in view of the practical problems as discussed above, it is necessary to amend Section 560 of the act.