

Licenced Companies Under Section 25 of Companies Act, 1956

ASHISH MAKHIJA

An association having objects to promote commerce, art, science, religion, charity or any other useful purpose and not having any profit motive can be registered as non-profit company under section 25 of the Companies Act, 1956. This section empowers the Central Government to grant a licence directing that such an association may be registered as a company with limited liability, without the addition of the words 'Limited' or 'Private Limited' to its name.

The so-called non-profit organizations can alternatively be formed as a Public Trust or a Society under the Societies Registration Act, 1860. The question then arises why to form a company under the Companies Act, 1956 and simultaneously obtain licence under Section 25 of the Act, which involves enormous paperwork and stricter provisions relating to maintenance of accounts and audit? The most obvious answer is provided by the advantages of having an incorporated company, namely, independent corporate entity, limited liability, perpetual succession etc. Section 25 companies enjoy greater privileges in the form of concessions allowed under the Act to such companies.

Statutory provisions

Section 25 empowers the Central Government to issue a

licence to a company which is proposed to be incorporated provided it complies with conditions, as to its objects, application of its profits/income and distribution of its profits, enumerated as under: -

- (i) it is being formed for *promotion of commerce, art, science, religion, charity or any other useful object*;
- (ii) it intends to *apply its profits or other income in promotion of its objects*;
- (iii) it intends to *prohibit payment of dividend to its members*.

The grant of licence is not only restricted to 'proposed companies' but also extends to 'existing companies' registered under the Companies Act, 1956. Such existing companies must make compliance of the aforesaid conditions through its Memorandum of Association prior to being eligible for grant of such a licence.

A license under this section can be granted by the Central Government through four Regional Directors namely, Regional Director (Eastern Region) at Kolkata, Regional Director (Northern Region) at Kanpur, Regional Director (Western Region) at Mumbai and Regional Director (Southern Region) at Chennai. The application for grant of licence is to be made to the Regional Director of the region, in case of proposed companies in the State where the registered office is proposed to be situated and in case of existing companies in the State where its registered office is situated, falls.

Any other useful object

The presence of words 'any other useful object' in Section 25 leads to an inference that a company which is promoted for any useful object other than those specified in

the section namely, promotion of commerce, art, science, religion or charity shall also be eligible for grant of licence under the section. The question, however, remains what could be considered as '*any other useful object*'? The application of cardinal rule of '*ejusdem generis*' provides the answer. According to this rule, when particular words pertaining to a class, category or genus are followed by general words, they are construed as limited to the things of same kind as those specified. Thus, in construing the words '*any other useful object*', the objects enumerated contemplate objects that are for the benefit of the society as a whole. Thus, even promotion of sports, education, research activities etc. would fall under the category of '*any other useful object*'.

The Non-profit or 'No Profit - No Loss'

The companies registered under section 25 of the Act are also known as '**Non-Profit**' or '**No Profit - No Loss**' companies. These terms are often given literal meaning that such

companies cannot earn any profits. Assigning such a meaning leads to unrealistic and impractical situations, as it would be impossible to maintain a situation of no profit and no loss. The words 'Non-Profit' or 'No Profit - No Loss' essentially signify that such companies cannot distribute the profits earned in the form of dividends to its members and the income/profit earned has to be applied for furtherance of the objects for which it has been formed.

Exemptions & privileges on grant of licence

Once a license is granted, such companies can be formed without the words 'Limited' or 'Private Limited' as part of their name. The existing companies can also take benefit of this provision and on grant of licence by the Central Government, can proceed to change its name by omitting the words 'Limited' or 'Private Limited' from its name. In addition to the privilege as to non-inclusion of the words 'Limited' or 'Private Limited' in its name, such companies enjoy numerous exemptions under the Act.

Section 263A provides protection to section 25 companies from the applicability of provisions of sections 177, 255, 256 & 263 of the Act, if the articles of such a company provide for election by ballot of all its directors at each Annual General Meeting. The protection provided by section 263A is enumerated as under: -

No minimum paid-up capital

The Companies Amendment Act, 2000 introduced the concept of minimum paid-up capital. Thus all the companies i.e. existing companies as well as the companies registered after the commencement of the Companies Amendment Act, 2000 were obligated to increase their paid-up capital to the required minimum - Rs. 1 lac for private limited companies & Rs. 5 lacs for public limited companies. The companies registered under Section 25 of the Act either before or after the commencement of Companies Amendment Act, 2000, have, however, been exempted from the requirement of minimum paid-up capital. This is a privilege exclusively for companies registered under section 25 of the Act.

Section	Matter	Exemption
177	Resolutions put to vote at general meetings to be decided on show of hands unless poll is demanded u/s 179	Whole, if the articles provide for election by ballot
255	Retirement of directors by rotation	Whole, if the articles provide for election by ballot
256	Ascertainment of directors retiring by rotation and filing of vacancies	Whole, if the articles provide for election by ballot
263	Appointment of directors to be voted on individually	Whole, if the articles provide for election by ballot

The Central Government, in exercise of the power conferred by sub-section (6) of Section 25 has also granted following exemptions to companies under section 25: -

Section	Matter	Exemption
2(45)	Appointment of qualified company secretary	In so far as it requires the appointment of an individual to perform the duties which may be performed by a secretary under the said Act and any other administrative duties only if he possesses the prescribed qualifications
147	Publication of name of company	Whole
160(1)(aa)	Name of the members, date on which they became members, they ceased as members since the date of annual general meeting of the immediately preceding year	Entire
166(2)	Holding of Annual General Meeting during business hours, not on a public holiday, in the city where the Registered Office of the company is situated	Entire provided time, date and place of each Annual General Meeting is decided upon before hand by the Board of Directors having regard to the directions, if any, given in this regard by the company in the general meeting
171(1)	Length of notice for calling general meeting	A general meeting can be called by giving a notice of not less than 14 days in writing
193	Recording of minutes within 30 days of conclusion of every meeting	Earlier the section provided for 14 days for recording of the minutes. The time period allowed to section 25 companies was 30 days. However, Section 193 was amended in 1965 to allow 30 days to all the companies.
209(4A)	Preservation of Books of Account and other papers for 8 years	The period for preservation of books of account and other papers in case of section 25 companies is 4 years immediately preceding the current year
219	Annual Accounts to be sent to the members at least 21 days before the date of meeting	The annual accounts can be sent not less than 14 days before the date of the meeting
257	Right of persons other than retiring director to stand for directorship	Not to apply to companies whose Articles provide for voting by ballot
259	Approval of Central Government for increase in number of directors beyond 12	Entire
264(1)	Filing of consent of director to act as director	Entire
285	Holding of at least one meeting in every three calendar months and at least four meetings in a year	At least one meeting within every six calendar months
287	Quorum for Board meetings - 1/3rd of strength of Board with minimum of 2	1/4th or 8 whichever is less with minimum 2
292	Certain powers to be exercised in Board Meetings only like to make calls, issue debentures, borrow money, invest funds, make loans	Power to borrow money, invest funds and make loans can be done by circulation
299	Disclosure of Interest by a director	Not applicable except for contracts to which 297(1) & (3) applies
301	Register of contracts, companies and firms in which directors are interested	Applicable for contracts to which Section 297(1) or (3) applies
303(2)	Intimation to Registrar of change in directorship	Entire

Lower registration fee & exemption from stamping

Another privilege, which such a company enjoys, is that though such a company can have share capital like any other company but the registration fees payable is lower as compared to companies not having a licence under section 25. The fee payable is fixed irrespective of the amount of authorized share capital.

The companies registered under section 25 of the Act enjoy another privilege as these companies are not required to have their Memorandum & Articles of Association stamped under section 39 of Indian Stamp Act, 1899.

Non-application of Companies Auditor's Report Order 2003

Section 25 companies are exempt from the applicability of Companies Auditor's Report Order 2003 (CARO). CARO was notified by the Central Government on 12.06.2003 to be applicable for financial years ending on or after 1st July, 2003. The Central Government vide its circular no. 32/2003 dated 10th November, 2003 has made it mandatory for financial years ending on or after 1st January, 2004. For the financial years ending between 1st July, 2003 and 31st December, 2003, the Central Government has advised all Registrar of Companies to take a lenient view provided, however, either a report in CARO or earlier MAOCARO (Manufacturing and other Companies (Auditor's Report) Order 1988), if applicable, is attached. *CARO expressly exempts section 25 companies from its applicability vide Clause 2(iii) of Para 1 of the Order.* Earlier also, Manufacturing and other

Companies (Auditor's Report) Order 1998 was not applicable to section 25 companies vide Clause 2(b)(iii) of the said Order.

Firm can be a member

A unique feature of Section 25 companies is that even a 'firm' can also be a member of such a company in its own name. It may be recalled that a firm, not being distinct and separate from its partner(s), cannot hold shares in any company in its own name. But in a section 25 company, a firm can become a member of such a company in its own name. An interesting question which arises is whether a proprietary firm can become a member of such a company? This issue is important since many such companies have enrolled proprietary firms as its members. This has eventually led to a situation where an individual being a proprietor of more than one firm has been enrolled as a member as many times as he has floated the proprietary firms. This seems to be a blatant violation of the privilege granted to such companies in order to control the management of the such companies. The word 'firm' has to be given a meaning as defined in Indian Partnership Act, 1932 as '*persons who have entered into partnership with one another are collectively called as a firm*'. Therefore, for a firm, **existence of partnership** is a must which is not possible in case of a proprietary firm. If such a contention is permitted, a single person being a proprietor of two or more firms can form a private company under this section which does not seem to be the intention of the Act.

Conditions for grant of license under section 25

The licence is granted subject to fulfillment of various conditions by such companies. The conditions, subject to which the licence is granted by the Central Government, are enumerated as under: -

- (a) That the profit/income earned by the company shall be applied by the company for the promotion of its objects;
- (b) That the company by its articles shall prohibit distribution of its profit in the form of dividend, bonus etc. to its members;
- (c) That the company shall not alter its object clause without the prior approval of the Central Government in writing. The licence issued by the Regional Directors normally contains the prohibition regarding amendment of any clause of Memorandum of Association without their previous permission;
- (d) That the company shall not amend its Articles without the permission of the Central Government; and
- (e) That the company shall not pay remuneration or other benefit to any of its members. This is applicable even though they are officers/servants/office bearers. Any member working for the association has to work in an honorary capacity. What can be paid is reimbursement of expenses, interest on loan, rent for premises lent to the company. However, such payment can be made to a members for services rendered by them which are not of the kind ordinarily expected to be rendered by him as member, with the previous approval of the

Central Government.

Revocation of licence

In the event of the company contravening any of the aforesaid conditions, the Central Government has been empowered to revoke the licence so granted. But before revoking the licence, the Central Government shall give a notice in writing of its intention to the company and shall afford an opportunity of being heard in opposition to the revocation. The Central Government is expected to use this power bonafide based on the principles of natural justice. Upon revocation, the company shall cease to enjoy the privileges and exemptions granted under section 25 of the Act. It shall also be obliged to add the words 'Limited' or 'Private Ltd. as the case may be to its name.

Procedure for obtaining License

The procedure for obtaining licence from the Central Government and subsequent incorporation of the company involves the following steps: -

- (i) Obtain name availability letter from the Registrar of Companies after making application in Form 1-A stating the fact that the company is proposed to be registered under section 25 of the Act.
- (ii) Make an application for grant of license. The application is to be made by the promoter(s) in case of a proposed company and by any director under authorization of the Board, in case of an existing company. Such an application is to be made on a plain paper and generally contains the background of promoters, activities to be



undertaken by the company etc. The application is to be made to the concerned Regional Director enclosing the following documents: -

- Three copies of Memorandum & Articles of Association duly executed by the promoters.
- Three copies of list of names, description, addresses of promoters/ directors with the name of organization in which they are holding responsible positions.
- Three copies of statement showing estimates of future Income & Expenditure and Balance Sheet (for new company). For existing companies, besides the estimated Income & Expenditure Account and Balance Sheet, past three years' annual accounts, report on working of the company and a statement showing in detail the assets and liabilities of the company as on the date of application or within seven days of that date are also to be attached.
- Three copies of statement giving in brief description of work proposed to be carried out after incorporation.
- Three copies of the statement specifying the grounds on which the application is made.
- Declaration, on a non-judicial stamp paper of appropriate value duly notarized, by all the directors of the company (Prescribed Performa is given in Annexure V of the Companies Regulation, 1956) that he is not of unsound mind, not an undischarged insolvent, has not applied for adjudication as insolvent, and has not been convicted by any court, and is not disqualified to act as a director.
- Declaration, on a non-judicial stamp paper of appropriate value duly notarized, by a Chartered Accountant or an Advocate of a Supreme Court or of a High Court, an attorney or a pleader entitled to appear before a High Court or a Company Secretary that Memorandum & Articles of Association have been drawn up in accordance with the provisions of the Act and that all the requirements of the Act and the rules made there under have been duly complied with in respect of registration or matters incidental or supplementary thereto.
- Application fee of Rs. 500/- (Revised from Rs. 60/- in July 1999) by way of a demand draft in favour of

- Regional Director, Northern/Eastern/Western/Southern Region and payable at the place where the concerned Regional Director's office is situated.
- Copy of name-availability letter issued by the Registrar of Companies.
 - Documentary evidence in support of addresses of promoters.
 - If the company is being established at the instance/collaboration of some foreign charitable organization, then certified copy of the charter of that organization with its translation in English or Hindi, if the charter is not in English or Hindi.
- (iii) Within seven days of making the application, a notice is to be published once in English language in English Newspaper and once in vernacular language in local newspaper circulating in the district in which the registered office is proposed to be situated or is situated inviting objections to the application for grant of licence. The public notice shall be in the prescribed format as given in Annexure II to the Companies Regulations, 1956. Such a notice has to provide minimum 21 days for receipt of objections and the Regional Director shall consider all objections received by him before grant of licence.
- (iv) A copy of the application for grant of licence is also required to be submitted to the concerned Registrar of Companies with all enclosures.

- (v) Registrar of Companies shall scrutinize the documents and suggest modifications, if any, to the Regional Director within 15 days. The Registrar of Companies can seek the views of District Magistrate of the State where the Registered Office of the company is either situated or proposed to be situated about the desirability of such a company. Regional Director can also make a reference to State Government and can also consult the ministries concerned to determine objections, if any, to the grant of licence.
- (vi) The Regional Director shall proceed to grant the licence on being satisfied regarding desirability of such companies.

The Department of Company Affairs, in order to facilitate quicker disposal of applications received for grant of licence under section 25 of the Act, has issued instructions to the Regional Directors to complete all the formalities within a period of eight weeks from the receipt of the application and to issue the licence applied for within a period of 10 or 12 weeks of receipt of the application.

Procedure for incorporation of Company

Normal procedure for incorporation of proposed company is to be followed except that Memorandum of Association and Articles of Association as approved/modified by the Regional Director has to be printed and submitted to the concerned Registrar of Companies alongwith a copy of the licence issued by the Regional Director and other documents as normally filed

at the time of incorporation of companies.

Income Tax Provisions

The income earned by Section 25 companies is taxable under the provisions of the Income tax Act, 1961. The income tax return of such companies must be filed in Form-3A before 31st October every year. However, such a company can get itself registered u/s 12A of the Income Tax Act and can get the benefit of accumulation of its income to some extent for utilization in future years. Such a company can also get itself registered u/s 80G of the Income Tax Act and the donor donating the amount to such a company shall be entitled to a deduction to the extent of 50% of the sum donated from its income. Section 12A(b) of the Income Tax Act provides for mandatory audit of accounts of such companies provided the total income without giving effect to the provisions of section 11 & 12 exceeds Rs. 50000/- in any year. The audit report is to be submitted in Form No. 10B and must be duly signed by a chartered accountant holding certificate of practice.

There are certain restrictions as to investment of funds by such entities registered u/s 12A of the Income Tax Act. The investment by such companies must be made in approved forms and modes of investment as specified in Section 11(5) of the Income Tax Act. All voluntary donations received by such a company are treated as income. Any amount applied out of such income is eligible for deduction be it a revenue expenditure or a capital expenditure. However, any donation received with the intent of forming a corpus is not treated as income. ■