CHAPTER III

PROSPECTUS AND DOCTRINE OF DISCLOSURES

1. PROSPECTUS

1-A. PROSPECTUS IN GENERAL

Joint stock companies are the main work centres of a modern economy. The modern joint stock companies have emerged out of the vast financial requirement of large scale production. In this type of business, large number of individuals pool their resources with a view to draw maximum benefit under the protection of limited liability. Thus joint stock companies is a convenient device by which economic activities can be organised. In order to finance these activities a company is required to have capital. This capital can be raised by the company, either from private resources or from the public. If the company opt for the later method, it is required to approach the general public. The prospectus is the device of attracting public funds.

The basic objectives of issuing a prospectus is to arose public interest in the company and to induce the general public to subscribe for its shares or debentures. It is a 'market show' so as to attract investors for putting money into the securities of the company. It is the only
window through which a prospective investor can look into the soundness of a company's venture. This may tempt the promoters and directors of a company to present a rosy picture of the company by giving all possible prospects and good points of the company and concealing its week points and limitations.

In order to protect the interests of prospective investors, the Companies Act, 1956 requires every company issuing prospectus to observe a large number of regulations.

In this chapter I have tried to analyse the provisions relating to information requires to be disclosed in the prospectus.

(I) IMPORTANCE OF PROSPECTUS

Prospectus is one of the devices of attracting public funds. It may be described as a document which indicates and holds out the prospects of the company to the prospective shareholders or debenture holders and invites them to subscribe for shares in or debentures of the company.

This document is relevant only to a public company. A private company cannot issue prospectus. One of the attributes of a private company is that its articles prohibit any invitation to the public to subscribe for any
shares in or debentures of the company. However, a periodical reporting has to be done by a private company by rendering a certificate in its Annual Returns requires to be filed with the Registrar of Companies that no public invitation have been made since (1) the last annual general meeting or (ii) since incorporation of the company, if the Annual Return pertains to the first annual general meeting held after incorporation. 2

A public company, on the other hand, is at liberty to invite the public to subscribe for its shares or debentures. Public subscription, indeed, open up a parenthetical source of finance for public limited companies. This source is limited only by the provisions of law i.e. Capital Issue (Control) Act and the Company own reputation. It can be considered as most potential advantage enjoyed by a company over a private company.

Public funds at stake in such companies thus become the foundation stone of the concept of public interest which in turn, is the raison de être for greater regulation and control of public limited company through legislation as compared to that of private company. The concept of public interest is not static and limited to investment of public moneys. Recognizing that substantial consumers
and labour interest is also involved in companies having large turn-over, the Companies (Amendment) Act, 1974 extends the concept of public interest to such companies and treats them as public companies under section 43 A (IA) of the Act.

A public company will also have initially to give a considerable amount of financial informations in its prospectus or statement in lieu of prospectus. This information is valuable to anyone contemplating investment in a public issue, or on the initial formation of the company or its conversion into a public company.

Sometimes, but rarely a public company is formed to start a new business. Most large commercial concerns, however, have grown from small family business which are originally incorporated as private companies, if incorporated at all. At some stage in the company's development the family decided to sell out in whole or in part, perhaps because they could no longer provide from their own resources the capital required for further expansion. At this stage the concern was converted into a public company and its securities offered to the public.

In case the promoters are confident of obtaining the required capital from their private resources, a public company need not issue prospectus, but in such a case it
will have to file a statement in lieu of prospectus, with the Registrar of companies. A private company is prohibited from making any invitation to the public to subscribe for shares in or debentures of the company. Further in the following cases also, though the shares are issued, a prospectus containing all the details as required by the Act is not necessary:

1. Where the shares or debentures are offered to the existing members or debenture-holders of the company, whether or not they have a right to renounce in favour of other persons,

2. When the shares or debentures are not offered to the public,

3. When the offer is made in connection with a bonafide invitation to a person to enter into an underwriting agreement with respect to the shares or debentures; and

4. When the shares or debentures offered are in all respect uniform with shares or debentures previously issued and quoted in a recognised stock exchange.

(II) DEFINITION AND MEANING OF PROSPECTUS

The definition of prospectus contained in Sec.2(36) of the Companies Act, 1956 as amended by the Companies
Prospectus means any document described and issued as a prospectus and includes any notice, circular, advertisement or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of any shares in or debentures of a body corporate.

According to English Companies Act, 1948,

prospectus means any prospectus, notice, circular, advertisement or other invitation, offering to the public for subscription or purchase of any shares or debentures of a company.

From the Public:

A part of the definition given under Section 2 (36) has been construed in Section 67. Invitation to public include as provided in Sub-Section (1) 'to any section of the public whether selected as members or debenture-holders of the company concerned or as clients of the person issuing the prospectus'. It is conceived that the first part relates to invitation by the company and latter party by stock-brokers, issuing houses, etc. to their clients. This provision is again subject to Sub-Section (3), the net result of which is that even if
the invitation is made to a section of the public, it will not be treated so, if it is held in all the circumstances of the case, not calculated to result directly or indirectly in shares becoming available to persons other than those receiving the offer.

The nature of the offer or invitation, it is conceived, has to be judged on the criterion whether it is purely and wholly a private communication not capable of being acted upon by anyone else than the addressee or it has some measure of openness so that it can form the basis of an offer by anyone else, who, though not addressed, satisfies the stipulations. A prospectus issued to the public or a section of the public and one not so issued appears to bear something like the same distinction as between a general offer and a specific offer under the Contracts Act.

In the light of the foregoing discussion it appears that applications received in response to personal negotiations or private correspondence fell outside the ambit of prospectus. But an issue to existing members with right to renounce the right in favours of others may be regarded as offer to public as it results indirectly in the shares becoming available to those not receiving the offer or invitation. (Nevertheless such a case has been
specifically exempted in so far as application of section 56 is concerned, irrespective of the offer being renounceable or non-renounceable).

An invitation to selected persons will also appear to fall within the term 'public' if the document so issued may form the basis of an offer from those who were not addressed. However, the offering of shares to the kith and kin of a director is not an invitation to the public to buy shares.⁴

In England before the Act of 1948 it was held that a company had not invited the public to subscribe where the directors without authority from the company, had issued to their friends a prospectus marked "private and confidential not for publication", with a view to obtaining subscriptions.⁵ However in the case of Lybde v. Nash⁶ it was held that an offer to a single member of the public might be an offer to the public. Viscount Sumner observed,

'The public' in the definition is, of course, a general word. No particular numbers are prescribed. Anything from two to infinity may serve, perhaps even one, if he is intended to be the first of subscribers; but makes further proceedings needless by himself subscribing the whole. The point is that the offer is such as to be open
to any one who brings his money and applies in due form whether the prospectus was addressed to him on behalf of the company or not.

Introduction of section 55 of the English Companies Act, 1948 corresponding to Section 67 of Companies Act, 1956 Buckley\(^8\) observes "renders obsolete, the authorities under the earlier act as to the meaning of the word public". On the other hand according to Palmer\(^9\) Section 55 provides an aid for construction of the phrase, 'offer shares or debenture to the public' but that aid is flexible and enables the Courts to deal with each case according to its surrounding circumstances. The view expressed by Palmer appears more reasonable. It is still left to the Courts to judge the issue in all the circumstances of the case. In India Sub-section (1) of Section 67 is designed to extend the meaning of 'public' beyond the popular meaning of that word as pointed by Palmer. If Sub-Section (1) is viewed in isolation even pre-emptive offer of a new issue of shares or debentures to the existing share-holders will amount to an issue to the public. However, it may be stated that not all doubt are settled by the section as the word "or in any other manner" in Sub-Section (1) renders its meaning indefinite. If shares or debentures are offered to a class of persons, such as the employees
of the company. Buckley's view that it would presumibly constitute an offer to a section of the public selected in any other manner. Buckley has raised further doubts. For example, if the offer is made to some employees selected by the directors, but not all of the employees, would this constitute an offer to a section of the public? If the offer is made only to a selected few or to a single client, would this be an offer to a section of the public? And if the offer is made by the brokers, to some, but not all, their clients would this be an offer to a section of the public? Buckley adds: "The difficulty is to know where to draw the line between one or two persons selected in some arbitrary manner and a section of the public... selected in any other manner." Buckley views the question to the one of fact and degree to be decided in the particular circumstances of the each case.

Buckley's difficulties, it may be submitted can be traced to his looking at Sub-Section (1) in isolation. After casting a wide net in Sub-Section (1), the legislature proceeds to lay down two guidelines in Sub-Section (3) to judge whether an offer or invitation shall be treated as made to the public or not. The question has not, been left entirely to act and degree, certain guidelines have been laid down to determine the question vide Sub-
sections (1) and (2). If the offer can properly be regarded in all the circumstances of the case:

(i) as not being calculated to result, directly or indirectly, in the shares or debentures becoming available for subscription or purchase by persons other than those receiving the offer or invitation; or

(ii) otherwise as being a domestic concern of the persons making and receiving the offer or invitation.

The clause seem to indicate that if the offer is specific, so that it can be accepted only by the persons to whom it is made, it is not to be regarded as an issue to the public. Palmer support the point when he says that the issue is not to the public if it is addressed to specified person. Palmer has, therefore, no difficulty like, Buckley, in saying that the issue would not be public where:

(i) an issuing house places the whole or part of a new issue privately with a few institutional investors; or

(ii) where a business is covered into a company and shares are offered by the vendors to a small circle of friends, relations and select customers.
In Government Stock and Other Securities investment Company Ltd. v. Christopher\textsuperscript{11} where the offer was made to all the shareholders of two companies who alone were entitled to accept such offer, as noted by Palmer, Wynn-Pery J. accepted the proposition put forth by counsel "that the test is not who receives the circular but who can accept the offer put forward".

The expression 'calculated to result' seems to suggest that an offer or invitation will be regarded as having been made to public if the scheme was so devised as to result in the securities becoming available to persons other than those to whom the offer or invitation was made. But if the scheme was not calculated to be so but it actually did result in the securities becoming so available, the issue may not be regarded public. This view is supported by Buckley\textsuperscript{12} "it is not necessary to show that the offer could not result in the way mentioned but only that it is not calculated to so result". The Court has to take into account all the circumstances of the case. This view reconciles with Palmer's proposition with which Gower\textsuperscript{12a} also concurs: where the offer or invitation is made to the existing holders of shares or debentures:

(a) if non renounceable offer is made, it cannot be
regarded as calculated to result directly or indirectly in shares becoming available to persons other than those to whom it was made and hence it is not an offer to public; but

(b) if the offer is renounceable, the circle of original allottees can easily be broken by renouncing the complete strangers may become allottees, hence the offer will, normally, be regarded as public.

Pennigton also agrees that if the letter of rights is non-renounceable, that is, if the recipient cannot sell or transfer his right to the securities to anyone else, it is not a prospectus. Pennington has delved deeper and tried to lay down a criterion: whether it would amount to a prospectus or not depends on what the recipient transfers by renouncing: if he transfers his right to apply for or accept an offer of securities, the invitation addressed to the recipient in someone other than himself subscribing for the securities, that is applying for them or accepting an offer of them, and is consequently a prospectus. For example, where a letter or rights informs the recipient that he is entitled to so many new shares or debentures, but that he may renounce them in favour of any other person by completing the attached form of
renunciation, and that the shares will be allotted to the person who completes and returns to the company the attached form of acceptance, the letter of rights is merely an offer which may be accepted by the recipient or anyone to whom the transfers it by renouncing, and is consequently a prospectus”.

The other exception carved out of the wide net of Sub-Section (1) of Section 67 is that an offer or invitation shall not be treated as made to the public if in all the circumstances of a case it can be regarded as being a domestic concern of the persons making and receiving the offer or invitation. The expression ‘domestic concern’ needs elucidation. Pennigton makes two points in this regard:

Firstly, he suggests that an offer or invitation which may be accepted by persons other than those to whom it is addressed may nevertheless be regarded as a case of domestic concern. This view is opposed by Buckley who thinks that the term domestic concern must be given a restricted interpretation, having a similar effect to clause (a).

He seems to suggest an ejusdem generis construction of both the exceptions contained in Sub-Section (3) of section 67.

Secondly, Pennington observes that the expression 'domestic concern' cannot be precisely denied, yet in the
same sentence be adds: "but clearly what is contemplated is private negotiations". Thus a private placing, where the company's directors or brokers approach one or a few likely investors with a request that they, or someone else whom they suggest, should subscribe for the company's securities, will not involve the issue of a prospectus. But a prospectus addressed to the public is shown to one person only because it is expected that he will be willing to subscribe all the capital required by himself, it is nevertheless a prospectus.

Buckley has suggested that an offer to existing members with freedom to dispose of the shares to others may be regarded as 'domestic concern'. And that the reference in Sub-Section (1) to 'a section of the public selected as members of the company' is intended to apply to an offer of sale made by anyone other than the company.

It may be observed that where the intention is to exempt cases of offer to existing member, e.g. in Sub-Section (5) of Section 56, it has explicitly been so mentioned in clear terms. If the intention, therefore, were to extend the exemption to section 67, the same expression as used in sub-section (5) of section 56 would have been used and there was no need to coin an altogether, different terms, viz. domestic concern. Again, if domestic concern meant
issue to existing members, there was no need to judge
the issue in all the circumstances of the case as laid
down in section 67.

Similarly, the equation between 'domestic concern'
and 'private negotiation' suggested by Pennington may not
be acceptable for the simple reason that the provisions
relating to prospectus are not at all applicable where the
prospectus is not issued and deals are struck by private
negotiations. The definition of prospectus itself is based
on the existence of a document which is issued as opposed
to private negotiations. If the equation suggested were
correct there was no need of clause (b) of sub-section (3)
of section 67 of the Act at all.

It may be submitted that 'domestic concern' is not a
word of art and should therefore, be given its popular
meaning. It appears to be akin to family concern. If
family concern is limited to a family, a domestic concern
may be confined to similar but larger circle with some
common bond, say, of family members, friends and relatives.
Whether in a given case, the issue is one of domestic
concern of the person making and receiving the offer or
invitation has again to be judged in all the circumstances
of the case and hence it may not be reasonable to lay down
any firm criteria for such judgement.
In Sleigh v. Glasgow and Transval Options, an offer by promoter to a few of his friends, relations, and customers has been held not to be an offer to the public. On the other hand, in Re South of England Natural Gas and Petroleum Co., distribution of 3,000 copies of prospectus to all the existing members of certain gas companies has been held to be an offer to the public.

In another case, a new company offered to buy all the shares in two existing companies and to issue its own shares in return. A circular was sent to the members of the existing companies accompanied by a "form of acceptance and transfer." It was held that the circular was not an offer to the public as it neither involved an offer for the purchase of shares nor invited subscriptions for shares since subscription meant taking shares for cash. Furthermore, although the circular offered shares it did not offer them to the public.

But Section 67 is not essentially dependent on members, as it is on all the circumstances of a case. It is not so in the United States where the Federal Securities Act, 1933 (Section 4 (1) exempts from the rules governing prospectuses all transactions not involving a 'public offering' of securities, a phrase akin to 'domestic concern.' It is the practice of the American Securities and Exchange Commission, accepted as proper by the Courts to treat
invitations to subscribe addressed to twentyfive or fewer persons as non-public offerings. If invitation is made to more than twentyfive persons, is character is judged by whether the addressees need the protection of the statutory rules as to the contents of prospectus in order to be adequately informed about the company's affairs, or whether they are likely to be adequately informed already because of their connection with the company.

For Subscription or Purchase

The term 'subscription' has not been defined in the Act. However, section 12 of the Act refers to subscribing to the Memorandum of Association. Persons who want to form an incorporated company, may by subscribing their names to the M.A. and otherwise complying with the requirements of the Act form an incorporated company. Subscription denotes taking of the shares directly from the company. Where as 'purchase' denotes taking of shares not from the company directly out of its unallotted shares but from others for consideration.

Body Corporate

The last significant term used in the definition of prospectus is 'body corporate' which is of wider import. The term 'company' unless the context otherwise requires means a company formed and registered under the companies
Act, 1956 or any previous Companies Act. On the other hand, 'body corporate' includes a company incorporated outside India but does not include:

(a) a corporation sole,
(b) a cooperative society registered under any law relating to co-operative societies, and
(c) any other body corporate, which the Central Government may by notification in the Official Gazette, specify in this behalf.

The provisions of prospectus would therefore, apparently apply equally to foreign companies as it applied to the Indian Companies.

(III) KINDS OF PROSPECTUS:

Prospectus may be classified into three categories from the point of view of their contents prescribed under the Act.

(1) Prospectus issued generally:

Prospectus issued by or on behalf of a company, or by or on behalf of any person who is or has been engaged or interested in the formation of a company; in relation to shares or debentures offered to the public, referred to by Gower and Pennigton as prospectus issued generally wherein the matters specified in Schedule II shall be stated;
(2) Exempted category of prospectus wherein the information prescribed in Schedule II need not be furnished; and

(3) Prospectus containing offer of sale under Section 64, referred to by Gower as 'sale prospectus' wherein besides the information prescribed under Schedule II, additional informations shall also be furnished.

(a) Prospectus issued generally

Sub-Section (1) of section 56 prescribes the matters to be stated and reports to be set-out in the prospectus issued to the public (a) by or on behalf of a company or (b) by or on behalf of any person who is or has been engaged or interested in the formation of a company.

A question arise, whether the disclosure prescribed under sub-section (1) of section 56 are necessary in case of a prospectus of an intended company or a prospectus issued before incorporation.

In this connection it may be submitted that the words 'intended company' found in the immediately preceding section 55, are conspicuous by their absence in section 56. It would, therefore, appears to be inapplicable to companies which are intended and not yet incorporated. The obvious
reason for this is that before a company is incorporated most of the informations prescribed in schedule II can hardly be furnished.

In this connection Buckley\(^\text{20}\) observes that "the language of Sub-Section (1) seems at first sight to limit the section to prospectuses issued after incorporation but the concluding words of Sub-Section (5) seems to extend it to prospectuses issued before incorporation". The learned author obviously relies on the following words in sub-section (5):

>'This section shall apply to a prospectus or a form of application whether issued on or with reference to the formation of a company or subsequently'.

It is respectfully submitted that the provision cited above, contains nothing to suggest that section 56 is applicable to prospectuses issued before a company is formed. 'On formation' cannot mean 'before formation', just as 'on time' cannot mean 'before time'. Similarly the expression with reference to formation conceivably refers to formation as an accompanied fact and cannot mean with reference to proposed formation.

The forgoing discussion is not, however, to suggest that a prospectus cannot conceivably be issued in relation to an intended company. Section 60 requires, inter-alia, a prospectus issued in relation to an intended company to be
delivered to the Registrar of companies for registration.

The cumulative effect of the provisions of section 56 and 60 appears to be that though a prospectus issued in relation to an intended company need not contain all the information prescribed in Schedule II, a copy thereof shall be delivered to the Registrar before its publication.

In this connection a question arise, what information actually need be furnished in a prospectus issued in relation to an intended company?

The answer is partly, found in clause (a) and (b) of Sub-Section (1) of Section 60 which specify the copies of contracts and consent of experts etc. to be endorsed on or attached to every prospectus delivered to the Registrar, and partly in the Golden Rule\textsuperscript{21} as to drafting of prospectus. The rule is important as even the civil and criminal liabilities under section 62 and 63 arise out of untrue statements defined in section 65 as in omission of any matter calculated to mislead or the inclusion of any statement in the prospectus which is misleading in the form and context in which it is included.

Yet another question arise, Does it suffice to furnish the information prescribed in Sub-Section (1) of section 56 in cases where it is applicable?

The possible answer is indicated by Sub-Section (6)
which declares that nothing in the section shall limit
or diminish any liability which any person may incur
under the general law or under any other provisions of the Act.

The other two provisions of section 56 require to be noted are:

Firstly, Sub-Section (3) which provides that 'no one shall issue any form of application for shares in or
debentures of a company unless the form is accompanies by
a prospectus which complies with the requirements of section
56. Buckley put it, thus 'where a prospectus is issued
offering shares or debentures to the public, no form of
application issued for such shares or debentures shall be
unaccompanied by the prospectus. There are two exceptions
to the rule viz.

(a) for entering into an underwriting agreement and
(b) for an issue not to public.

Indeed the words used in Sub-Section (3) 'no one shall
issue' any form of application unless accompanies by a
prospectus complying with Section 56, are so wide as to
transcend the limits of Sub-section (1). As a result
no invitation constituting a prospectus shall be issued
to public:

(a) By or on behalf of a company, or
(b) By or on behalf of any person who is or has been engaged or interested in the formation of a company, or

(c) By any other person issuing any form of application for shares or debentures without complying with the requirements of the section.

A comparison of sections 417 and 56 is revealing. The forms is limited to cases of subscription. There is no such expression limiting the scope of section 56. It is, therefore, conceived that the provisions of Section 56 apply to all prospectus whether for subscription or purchase and whether falling within the ambit of Section 64 or not. Additional information specified in Section 64 has to be furnished in case of sale-prospectus falling under that section and in no other case. This view is supported by Buckley and appears to be just in practice and reasonable in construction.

Secondly, Sub-section (2) which provides that any condition binding on the applicant for shares or debentures in a company to waive compliance with any requirements of the Act as to disclosure in the prospectus or purporting to affect him with notice of any contract, document, matter not specifically referred to in the prospectus shall be
void. This section suggests that a person may be deprived of his contractual freedom or liberty by a provision of the statute, with a view of protecting his interest.

(b) Exempted Category of Prospectus:

Notwithstanding that an issue to existing members or debentureholders may, under section 67, amount to a public issue, sub-section (5) of section 56 lays down that the requirements of the section including Schedule II shall not apply:

(a) To the issue to existing members or debentureholders of a company of a prospectus or form of application relating to shares in or debentures of the company whether they will or will not have the right to renounce in favour of other persons, or

(b) To the issue of a prospectus or form of application relating to shares or debentures which are, or are to be in all respect uniform with shares or debentures previously issued and for the time being dealt in or quoted on a recognised stock exchange.

It is therefore, clear that the distinction made by the authorities between renounceable and non-renounceable offer of shares to existing members or debentureholders
is irrelevant in regard to the information to be furnished in a prospectus for their benefit. Such a prospectus eventhough it may be regarded as a case of public issue need not contain the information prescribed by Section 56 in Schedule II. If the right offer is non-renounceable indeed if falls outside the definition of prospectus.

(c) Unlike Companies Act, 1956, Section 39 of the English Companies Act, 1948, contains a third exemption.

It provides where (a) it is proposed to offer any shares or debentures of a company to the public by a prospectus issued generally (that is to say issued to persons who are not existing members of debentureholders) of the company), and (b) application is made to a prescribed stock exchange, for permission for those shares or debentures to be dealt in or quoted on that stock exchange, there may, on the request of the applicant by or on behalf of that stock exchange a certificate that, having regard to the proposals (as stated in the request) as to the size and other circumstances of the issue of shares or debentures and as to any limitations on the number and class of persons to whom the offer is to be made, compliance with the requirements of the Fourth Schedule to this Act would be unduly burdensome."
It further provides that "if a certificate of exemption is given, and if the proposals aforesaid are adhered to and the particulars and information required to be published in connection with the application for permission made to the stock exchange are so published, then

(a) a prospectus giving the particulars and information aforesaid in the form in which they are so required to be published shall be deemed to comply with the requirements of the Fourth Schedule to this Act, and

(b) the last foregoing section shall not apply to any issue, after the permission applied for is granted, of a prospectus or form, if application relating to the shares or debentures".

In short, Section 39 of the English Act provides that if an application is to be made for a quotation, the stock-exchange may certify that, having regard to the size and other circumstances of the issue and to the person to whom it is to be made, compliance with the Schedule would be unduly burdensome. If this certificate is granted and an advertisement complying with the regulations of the stock exchange is duly published, the advertisement will be deemed to be a prospectus complying with the schedule.
The Jenkin Committee recommended that Section 39 should be extended so as to enable partial, as well as complete exemption from compliance with Schedule IV to be given and so as to empower the Board of Trade to grant exemption when no quotation was being sought, but that it should be provided that any form of application must be accompanied by a prospectus complying with the conditions of the exemption.

The rational for these exemptions is not far to seek. The prescribed information in the schedule need not be furnished. When a prospectus is issued to existing members or debentureholders as they should be sufficiently informed about their company's affairs by the periodic accounts and reports sent to them to require no further protection. The underwriters are assumed to be astute enough to protect themselves.

In regard to shares and debentures of a class already issued and quoted on a stock exchange, the prospectus issued at the time of the first issue of that class of securities will be available for inspection in the Registrar's office. Besides, the quotations on the stock exchange also help the investors to form an opinion about the value of the securities.
(c) Sale Prospectus:

Where a company allots or agrees to allot any shares in or debentures of the company with a view to all or any of those shares or debentures being offered for sale to the public any document by which the offer for sale to the public is made shall, for all purposes be deemed to be prospectus issued by the company. To such a prospectus shall apply "all enactments and rules of law". The provision is a bit unusual in as much as it explicitly makes applicable besides enacted law, also rules of law, that is all the judge made law and other rules which fall within the ambit of law. This indicate the determined approach of the legislature to bring such indirect issues within the ambit of law relating to prospectus.

The expression with a view to all or any of those shares or debentures being offered for sale to the public used in sub-section (1) has not been totally left to be ascertained by Courts, Sub-section (2) lists two factors which shall, unless the contrary if proved, evidenced that an allotment or agreement to allot was made by a company with such view:

(a) if within six months after the allotment or agreement to allot made by a company, an offer
of the shares or debentures or any of them is made for sale to the public, or

(b) if it is shown that the whole consideration to be received by the company had not been received by it at the date when the offer was made to the public.

The persons who takes shares or debentures from a company and thereafter make the offer to public as envisaged in Section 64 are deemed by Sub-Section (4) to be directors named in the prospectus and thus they have as required under section 60 (1) to deliver to the Registrar for registration a copy thereof signed by every such person. Where such a person is a company or a firm, the prospectus may be signed as in Sub-Section (5) of Section 64.

Under Sub-Section (1) of section 64, a document by which any offer for sale of shares or debentures as envisaged in section 64 is made, is firstly deemed to be a prospectus and secondly it is treated at par with the prospectus issued by a company in so far as the requirements of law as to contents of prospectus and as to liability in respect of the statements in and omissions from the prospectus or otherwise relating to prospectus are concerned.

Thus all the informations prescribed under section 56 & 60 or elsewhere has to be furnished in such a prospectus.
Besides certain additional information is also required to be furnished in such a prospectus as prescribed in Sub-Section (3) of section 64 viz.

(i) the net amount of the consideration received or to be received by the company irrespect of the shares or debentures to which the offer relates; and

(ii) the place and time at which the contract under which the said shares or debentures have been or are to be allotted may be inspected.

Disclosure of this additional information is obviously, designed to make it known to the prospective investors the profits, if any that the offerer is to make in the deal. This may help to indicate whether the price demanded is reasonable or not.

Thus, it becomes clear that by utilising the device of placing of shares through an intermediary or intermediaries a company cannot evade or circumvent the requirements of law as to disclosure in prospectus, if the placing was made with a view to the shares or debentures being offered for sale to the public. In fact the law makes it more difficult for the company or the intermediaries to pass on the shares to the public without proper disclosures; etc.
(IV) MAIN REQUIREMENTS OF SCHEDULE II

Following the pattern of the English Companies Act, 1948 schedule II (corresponding to Schedule IV of the English Act) is divided into three parts:

Part I lays down the matters to be specified in the prospectus.

Part II states the Reports to be set out in prospectus;

and

Part II deals with interpretation, explanations and exemptions relating to provisions applying to Part I and II of Schedule II.

Contents

(a) Objects of the company and particulars of signatories to memorandum of Association:

Sub-Clause (1) of Clause 1 of Part I of the Schedule requires that the main objects of the company with the name, addresses, description and occupations of the signatories to the Memorandum of Association, and the number of shares subscribed for by them shall be specified in the prospectus. The term 'description' here would appear to cannot father or husband name. Where any prospectus is published as a newspaper advertisement, section 66 exempts inclusion of particulars of signatories to the memorandum of association in the advertisement.
The particulars of the signatories to the M.A. and the shares subscribed by them need not be given in the case of a prospectus issued more than two years after the date on which the company is entitled to commence business.

The disclosure as to the signatories of the K.A. may help the prospective investor to form an opinion about the persons who have brought the company into being and whether they can be relied upon. There is, therefore, no reason why this information should not be necessary two years after the company is entitled to commence business. Here it may be noted that a private company becomes entitled to commence business immediately after its incorporation, and if it is converted into a public company after two years, it would not be required to furnish the information. On the other hand many public companies are not able to actually commence business in any noticeable manner even after lapse of three to four years from the date when they become entitled to commence business. Thus in most of the cases, the required information will not have to be furnished.

It is therefore, suggested that the requirement may be modified so that the date of actual commencement of substantial business rather than the date of entitlement to commence business is made relevant. After a company has
launched itself into business it would have made its character and antecedents known by its dealings and there would be no need to furnish particulars of its promoters and hence the exemption would be justified but not until then.

Sub-Clause (2) requires to specify in the prospectus:

"the number and classes of shares, if any, and the nature and extent of the interest of the holders in the property and profits of the company". This provision does not make an easily intelligible reading. But the meaning becomes clear by a look at paragraph 1 of Part I of the Fourth Schedule appended to English Companies act, 1948 from which it seems to have been adopted. That paragraph requires to be specified: "The number of founders or management or deferred shares, if any, and the nature and extent of the interest of the holders in the property and profits of company". The object is to specify the number of, and rights in profits of founders shares or management shares or deferred shares which were usually allotted to promoters with special rights to participate in profits left over after distribution of dividend to ordinary shareholders. The other requirements in this regard appears to be to specify the interest of the holders of such shares namely the promoters in the property of the company. For instance if a promoters
has leased his factory or building to the company, it would appear that his interest will have to be disclosed in the prospectus.

Again, clause 13 and 15 require, inter-alia disclosure of any benefit or commission on shares paid within the two preceding years or interest to be paid to any promoter, or officer along with other relevant details. Clause 18 also requires full particulars of the nature and interest of every promoter in the formation of the company or in any property acquired by the company within two years preceding the date of the prospectus or proposed to be acquired.

The Pieces of Information required to be furnished under various Clauses are:

Share Capital - Redeemable Preference shares

Sub-Clause (3) of clause 1 requires the particulars to be furnished in respect of 'redeemable preference shares' intended to be issued'. This provision is new and no similar provision is found in the fourth schedule of the English Act. This is an important information and is rightly required to be provided under the Indian Law.

A doubt may be raised as to whether the expression 'intended to be issued' means intended to be issued by the prospectus under consideration or intended to be issued in future. It would appear that it deals with the intended to
be issued by the prospectus under consideration and if redeemable preference shares are being presently issued by the prospectus under consideration. The terms of issue including the date of redemption or the period of notice required for redemption and the proposed method of redemption are necessarily to be given. On the other hand if the shares are not being presently issued and no decision has been taken so far to issue such shares, it would appear to be unreasonable to expect the information to be furnished on the basis of the intention in the minds of the promoters or directors.

**Disclosure in respect of directors:**

The particulars of directors and proposed directors and manager and proposed manager along with the names of other companies in which they hold either of these offices are also to be furnished in terms of clause (3) besides provisions in Articles or any contract entered into as to their appointment and remuneration. The number of shares, if any, fixed by the Articles as the qualification of a director has also to be disclosed as per clause (2).

Any benefit given or proposed to be given to any officer of the company, which includes a director, are again required to be furnished in terms of clauses 13 and 15.
Besides, particulars of contracts entered into with the managing director or manager (alongwith time and place at which any such contract or copy thereof may be inspected) is again required to be stated under clause 16.

Clause 18 again requires full particulars to be furnished in respect of the nature and extent of interest of every director or promoter in the promotion of the company and in any property acquired by the company within two years of the date of the prospectus or proposed to be acquired.

**Disclosure in respect of minimum subscription**

The term minimum subscription is of great importance from the practical point - as it denotes the minimum amount estimated by directors which must be raised by the issue of shares capital offered to the public for subscription, in order to provide for the various requirements, e.g. purchase of property, preliminary expenses and working capital etc. The minimum subscription should cover the amount of any preliminary expenses which is intended, the company shall pay whether such payment is enforceable under a contract or not. The object of stating minimum subscription is to inform the prospective investor about the project without making arrangements for adequate finance, the investor's money, be he a shareholder, is likely to
fall in jeopardy. Clause 5 of Schedule II, therefore, indicates that due inquiry must be made, by the directors in this regard.

"It would be inequitous" says Gower 25 "to force an applicant, who has accepted an invitation to participate in a £1 Million issue for the purpose of buying Wentley Stadium, to sink his capital in a company which has only raised enough money to buy a suburban villa".

The Act does not indicate the quantum of minimum subscription and leaves it to the judgement of directors. "An unreasonable error in judgement by them constitutes a material mis-statement in the prospectus and may have civil and criminal consequences". 26

Section 69, therefore, prohibits allotment of shares and ordains repayment of application money, unless within 120 days of the issue of prospectus, enough shares are subscribed to raise the capital contemplated in the director's scheme of finances specified under minimum subscription. An allotment made in contravention of section 69, including the requirements as to minimum subscription, is voidable at the option of the applicant within two months of the holding of statutory meeting or where it is made after that meeting within two months of allotment.
The requirement as to minimum subscription, prohibition as to allotment and repayment of shares money aforesaid applies only to the first allotment of shares to the public for subscription and not to any subsequent issue. There is no reason why the requirements should not apply to subsequent issues as the company may not necessarily take to its legs after the first public issue. It is impossible that unscrupulous promoters make a small public issue of whose minimum subscription they are assured, followed by a bigger second issue being exempt from the provisions of Section 69, the company may proceed to allot shares even though the subscription is insufficient to take up the project. The shareholders money may then be found to be misplaced.

However, the provisions of 69 and clause 5 of Schedule II do not apply to issue of debentures. Debentures holders being creditors look to the share capital as their guarantee fund and they are sought to be protected by ensuring that the debtor company has adequate capital, through the provisions as to minimum subscription and the safeguards against reduction of capital.

Disclosure in respect of Material Contracts

Clause 16 of Schedule II is based on a similar provision in Para 14 of the Fourth Schedule to the English Companies
The requirement as to minimum subscription, prohibition as to allotment and repayment of shares money aforesaid applies only to the first allotment of shares to the public for subscription and not to any subsequent issue. There is no reason why the requirements should not apply to subsequent issues as the company may not necessarily take to its legs after the first public issue. It is impossible that unscrupulous promoters make a small public issue of whose minimum subscription they are assured, followed by a bigger second issue being exempt from the provisions of Section 69, the company may proceed to allot shares even though the subscription is insufficient to take up the project. The shareholders money may then be found to be misplaced.

However, the provisions of 69 and clause 5 of Schedule II do not apply to issue of debentures. Debentures holders being creditors look to the share capital as their guarantors fund and they are sought to be protected by ensuring that the debtor company has adequate capital, through the provisions as to minimum subscription and the safeguards against reduction of capital.

Disclosure in respect of Material Contracts

Clause 16 of Schedule II is based on a similar provision in Para 14 of the Fourth Schedule to the English Companies...
Act, 1948. It requires the dates of parties to and general nature of every contract appointing or fixing the remuneration of a managing director or manager to be furnished in the prospectus, whenever the contracts may have been entered into.

A question that arise as to whether this applies even to contracts which are no longer subsisting. The answer appears to lie in the negative for two reasons:

(i) that continuous tense has been used in the expression 'appointing or fixing, and

(ii) the object of this information is to apprise the investors of the commitments the company has have which are going to have a bearing on the company's investment-worthiness. It, therefore, appears that such of the contracts which were entered into in the past but are not subsisting need not be specified.

Similar particulars have to be furnished in regard to every other material contract entered into within two years preceding the date of the prospectus. The term 'material contract' has not been defined in the Act. The clause only indicates that a contract entered into in the ordinary course of business is not a material contract. Buckley points out that the corresponding section 38 of the Companies Act, 1867, of the U.K. used the words 'any
contract' instead of 'material contract' which included within its literal meaning every contract entered into by the company, or by its promoters, directors or trustees, and non-disclosure was deemed fraudulent. Some limitation was therefore felt necessary to be placed thereon. On the other hand, there was a tendency of the Courts to refuse, so to limit the section as to include within it only contracts by which an obligation was imposed upon the company to the exclusion of contracts entered into by promoters, and company inter se relating to the formation or affairs of the company. On the other hand some judges held that the section referred only to those contracts which put an obligation on the company, and which either bound the company or might be adopted or assumed by the company and bind it when formed. On a balance... the prospectus had to disclose... contracts... which were material for intending applicant to know. On the authority of Broom V. Speak 28 affirmed in Shepherd v. Broome 29, Buckley observes that a material contract is one which, whether deterrent or not, an intending investor ought to have an opportunity of considering.

According to Gower "presumably the test is whether mention of the contract would be likely to affect in any way (however slight) an intelligent approval of the securities offered". He goes to the extent of suggesting "if those
issuing the prospectus are anxious to omit any reference to a particular contract this is cogent evidence that it is material.

Section 60 of the Act, inter-alia, requires a copy of every contract falling under clause 16 of Schedule II or in the case of a contract not reduced into writing; a memorandum giving full particulars thereof, to be endorsed on or attached to the prospectus delivered to the Registrar for registration, failing which the Registrar shall not register it.

A copy of each of such contracts has to be kept open for inspection for a reasonable time. The time and place for inspection has to be specified in the prospectus.

A contract falling within the clause 16 assumes special importance in view of the provisions contained in section 61 of the Act: which reads as "a company shall not, in any time, vary the terms of a contract referred to in the prospectus or statement in lieu of prospectus, except subject to the approval of or except on authority given by the company in general meeting."

It may be submitted that the scope of Section 61 is not limited to 'material contracts' or other contracts falling under clause 16 of Schedule II. The expression
'referred to in the prospectus' suggest that even a contract falling outside the scope of clause 16 of schedule II, may nevertheless be covered within the ambit of section 61, if it is even otherwise referred to in the prospectus. The rational of including every material contracts within the scope of section and putting fetters on the power of the Board to vary terms is not very clear. It may be based more on extra caution than on expediency. The requirement appears to be unreasonable more so as the terms cannot be varied at any time, except on authority of the company in general meeting.

It may be mentioned that the corresponding provisions in section 42 of the English Companies Act, which provides that 'a company limited by shares or a company limited by guarantee and having a share capital shall not previously to the statutory meeting vary the terms of a contract referred to in the prospectus except subject to the approval of the statutory meeting', is restricted to variation in the terms before the holding of the statutory meeting.

Disclosure in respect of discount:

Section 79 lays down provisions for issue of shares at discount. In order to bring the fact of discount to the notice of the public, particularly prospective investors, sub-section (4) of section 79 provides that every prospectus
relating to the issue of shares shall contain particulars of the discount allowed on the issue of the shares or of much of that discount as has not been written off at the date of the issue of the prospectus. It further provides that if default is made in complying with this sub-section, the company and every officer of the company who is in default shall be punishable with fine.

Miscellaneous Provisions

These are the provisions which are related with the dating and signing of the prospectus, expert's consent and other documents to be attached thereto as also provisions relating to filing of prospectus with the Registrar of Companies.

(1) **Signing of Prospectus** :

The prospectus to be filed with the Registrar has to be signed by every person who is named therein as a director or proposed director of the company or by his agent authorised in writing. Generally investors relies on the reputation of the persons who are named in the prospectus as directors. The law, therefore, ensured that all of them must sign the copy of the prospectus filed with the Registrar so that none of them can, later on plead that the prospectus was
filed with the Registrar, containing facts and statements, without his knowledge, particularly when facts turns out to be false one.

The words 'or proposed director of the company' give rise to a doubt whether this expression is applicable to the prospectus issued in relation to an intended company only, or in case of an existing company too. It may be submitted that the expression 'company' as defined in section 3 of the Act means one which is already formed and registered and thus it cannot mean an intended company. But this proposition does not appear to be correct for the reason that the definition in section 3 applies 'unless the context otherwise requires' and in the context of Sub-Section (1) of section 60 both a company and intended company are explicitly covered. Thus the proposed directors also have to sign the prospectus, if so named in the prospectus, irrespective of the fact whether it is an already formed and registered company or an intended company. The reason de etre for this proposition is that the investors relies not only on the reputation of present directors but also of the proposed directors the benefit of whose association is to become available to the company on their co-option as directors.
The above proposition is also supported by section 56 which read vide schedule II clause 3 prescribes specifically information to be furnished in regards to names, addresses, descriptions and occupations also of proposed directors/managing director/manager.

(2) DATING OF PROSPECTUS

Section 55 lays down that a prospectus must be dated. Unless the contrary is proved, the section raises a presumption that the publication of the prospectus coincides with the date of the prospectus, but the presumption is rebuttable by proof to the contrary. The date of the prospectus is important for a copy of the prospectus has to be delivered to the Registrar of companies under section 60 on or before the date of its publication. The issue of a prospectus shall not precede the delivery of a copy thereof to the Registrar of companies for registration.

In case of a prospectus sent to the Registrar for registration by post, the date of the prospectus would precede the date of delivery to Registrar due to the time lost in transit, resulting in apparent contravention of section 60. It should, therefore, be ensured that (1) the prospectus is not actually published before delivery to the Registrar and,
(2) it should be notified to the Registrar in advance that the prospectus has not been published until a certain date falling beyond the date of delivery of copy to Registrar.

(3) **EXPERT AND HIS CONSENT**

Section 58 provides that if a prospectus includes a statement purporting to be made by an expert, unless

(a) the expert has given his consent to the issue of the prospectus and

(b) a statement that he has given and has not withdrawn his consent appears in the prospectus.

Section 59 provides that the expression 'expert' includes an engineer, a valuer, an accountant and any other person whose profession gives authority to a statement made by him.

As observed by Pennington "except in the case of letters or right, prospectus always contains at least one report or statement by an expert... if it contains such a report or statement, the prospectus may not be issued unless the expert has given and not withdrawn his consent to the inclusion of his report or statement in the form in which it appears and the copy of the prospectus delivered to the Registrar must have the written consent attached to it.

The report which a prospectus inevitably contains is the report by the company's additor on its financial position.
Other reports may be by surveyors or valuers on the condition and market value of the company's property, or by specialists such as oil or mining engineer.

The above extract support the view that the report of the company's auditor on its financial position included in a prospectus is the report of an expert. However, section 57 provides that the expert whose statement is included in a prospectus shall be a person who is not and has not been engaged or interested in the formation or promotion or management of the company.

Here a question arise, as to whether a Chartered Accountant who got the company incorporated, inter alia, by filing the declaration of compliance under section 33 of the Act, may be deemed to be unconnected within the meaning of section 57 so as to be able to give his report on the company's financial position for inclusion in the prospectus as per the requirement of item 24 of Schedule II.

Section 33 of the Act permits, inter alia, a Chartered Accountant, practicing in India who is engaged in the formation of a company to file a declaration with Registrar of companies that all the requirements of the Act and the rules thereunder have been complied with in respect of registration and matter precedent and incidental thereto.
While a Chartered Accountant who is engaged in the formation of a company is entitled to file the declaration of compliance under section 33, a person who is so engaged is declared incompetent to make an expert's statement under section 57. The answer to the question posed above has therefore, to be in the negative.

Endorements and Enclosures to Prospectus and Delivering a copy to Registrar:

Section 60 lays down the documents required to be endorsed on or attached to every prospectus issued by or on behalf of a company or in relation to an intended company. A copy of such a prospectus duly signed and complete with enclosures and endorements has to be delivered to the Registrar, for registration before it is issued. However, the list of enclosures, etc. differs with, whether the prospectus falling under section 60 is issued generally or not. Distinction is also made between the enclosures to the copy of the prospectus delivered to Registrar and copies issued.

The requirements applicable to all prospectuses falling under section 60 are that the prospectus

(1) shall on the face of it;

(a) state that a copy has been delivered for
registration as required by section 60; and

(b) specify any documents required by section 60
to be endorsed on or attached to the copy so
delivered, or refer to statements included
in the prospectus which specify these documents;

and

(2) shall have endorsed therein or attached there to
any consent to the issue of the prospectus required
by section 58 from any person as an expert.

The additional requirements in regard to a prospectus
falling under section 60 and issued generally, that is
to persons irrespective of their being existing members or
debentureholders is that the prospectus shall have
endorsed thereon or attached thereto a copy of every
contract or in case of oral contract memorandum giving
full particulars thereof required by clause 16 of Schedule
II.

Further it must also be accompanied by the consent in
writing of the person, if any, named therein as the auditor,
banker or broker of the company or intended company to act
in that capacity.
As mentioned earlier, a prospectus is an invitation to the public to subscribe to the shares or debentures of a company. It is on the basis of the contents of a prospectus that a prospective investor decides to invest money in the company. As such a prospectus must give full, accurate and a fair picture of the state of affairs and prospects of the company and a heavy responsibility therefore, rest on those who issues it.

In this connection Kindersley V.C. observed "those who issue a prospectus holding out to the public the great advantages which will accrue to persons who will take shares in a proposed undertaking and inviting them to take shares on the faith of the representation therein contained, are bound to state everything with strict and scrupulous accuracy, and not only to abstain from stating a fact which is not so, but to omit no one fact within their knowledge, the existence of which might in any degree affect the nature of extent or quality of the privileges and advantages which the prospectus holds out as inducement to take shares".

It was further held that "a prospectus is the only window through which a prospective investor can look into
the soundness of a company's venture. This may tempt the promoters and directors of a company to present a rosy picture by giving all possible prospects and good points and conceal its weak points and limitations. In order to protect the prospective investors against fraud of the promoters, etc. Companies Act has provided a large number of regulations seeking fullest disclosure of all material and essential particulars in the prospectus.

In another case it was held that "truth, whole truth and nothing but truth must be disclosed. Half truth is no better than a downright falsehood. A prospectus must make all statements with scrupulous accuracy and not state a fact which are not strictly correct. A statement may be false not because of what it states but also because what it conceals, omits or implies."

A contract made with a company to purchase shares is a Uberrima fidei contract. The intending purchasers of shares are entitled to true and correct disclosure of all the facts in the prospectus. Neither any information which the law requires to be disclosed to the public be concealed or omitted to be stated from the prospectus nor the information given should be false and misleading. Persons responsible for the issue of prospectus should not only abstain from stating as fact that which is not so, but should
also not omit any fact within their knowledge, the existence of which is likely to affect any degree the nature, extent or quality which the prospectus holds out as inducement to take shares.

In this connection Lord Chemsford observed that "no mis-statement or concealment of material facts or circumstances out to be permitted. In my opinion the public, who are invited by a prospectus to join in any new venture, ought to have the same opportunity of judging of everything which has a material bearing on its true character as the promoters themselves possess. The utmost candour and honesty ought to characterise their published statement."

In another case it was held that "omission must be such which makes that which is stated absolutely false. However, the law was further refined in relation to positive mis-statement. Where a half truth was represented as a whole truth, it was declared a false statement. Lord Halsbury observed that "if by a number of statement you intentionally give a false impression, and induce a person to act upon it, it is not the less false, although, if one takes each statement by itself there may be difficulty in showing that any specific statement is untrue".

If the prospectus contains a misleading or false
statement or omits to disclose a material fact which amounts to misrepresentation, the shareholders acquires right against:

(a) the directors and person responsible for the issue of the prospectus; and
(b) the company.

The liability of the directors, promoters and others who authorise the issue of the prospectus containing false or misleading statements is civil as well criminal. They also becomes liable under the general law of contracts. Section 62 deals with civil liability where as section 63 deals with the criminal liability.

It may be mentioned that civil liability under section 62 is not an absolute liability as it also provides for certain defences to the directors, promoters etc. However, it may be stated that criminal liability i.e. criminal punishment prescribed under section 63 is certainly a potent protection to the public but is a poor consolation to the individual investor who has been cheated.

Liability of the Company:

The shareholders who has purchased share on the basis of the misleading or false prospectus has two rights against the company, under the general law of contracts;
(a) Right of recession of the contract, and
(b) Right of action for damages.

In India Sections 17 and 19 of Indian Contracts Act lays down provisions relating to the right of the party to caused the contract whose consent has been by misrepresentation or fraud etc.

1-B. PROVISIONS RELATING TO PUBLIC DEPOSITS:

In order to ensure that the effectiveness of the monetary policy of the Government may not be blurred by unrestricted growth of deposits and to protect depositor's interest by checking undue accumulation of short term liabilities, the Companies (Amendment) Act, 1974 has introduced two new sections 58 A and 58 B, so as to regulate and control the acceptance of deposits by the companies from the public or from their members. So far, these deposits were being regulated by the provisions of chapter III-B of the Reserve Bank of India Act, 1934. It has been practice of the companies to take deposits from the public at high rate of interest and experience has shown that in many cases deposits taken by the companies were not refunded on due dates. In many cases either the companies have gone into liquidation or the funds were depleted to such an extend that the companies were not in a position to refund the deposits. The object of these new provisions is to check this tendency.
The law on the subject is of recent origin in our country, but at the same time deposits are being increas­ingly relied upon by companies big and small as an important source of financing.

Section 58 extends the provisions of the Act, relating to prospectus, so far as may be, to advertisement for deposits under section 58A. Besides this, the definition of prospectus contained in Section 2 (36) of the Act has also been amended to include invitation for deposits within purview of the Act.

Before these amendments i.e. insertion of section 58A and 58B, the only provision in the companies Act 1956 in regard to deposits was found in section 219. It provides that 'Any person from whom the company has accepted a sum of money by way of deposit shall on demand accompanied by the payment of fee of one rupee, be entitled to be furnished with a copy of the last balance-sheet of the company and of every documents required by law to be annexed or attached thereto, including the profits and loss account and auditor's report. The default is made punishable. The section further provides that, the Court may also by order direct that the copy demanded shall forthwith furnished to the person concerned.
The provisions relating to prospectus did not apply to deposits until the above amendments, for the reason that right to the repayment of money deposited with a company are not per se debentures.

It may be mentioned that in England, even the Prevention of Fraud (Investment) Act, 1958 did not control deposits as they did not fall within the definition of securities. This means as pointed by Gower that finance companies, however dubious their antecedent, could freely advertise for deposits, a freedom which led to a number of grave scandals until it was controlled by the Protection of Deposits Act, 1963. As per the provision of this Act the companies are required to furnish copies of balance sheets periodically to the depositors. They have also to inform the depositors if some other business than that included in the advertisement is carried on. In such an event the depositor becomes payable on demand. Moreover, the Act provides certain additional grounds on which such a company may be compulsorily wound up.

In India there is no legislation corresponding to the Protection of Depositors Act, 1963 of U.K. notwithstanding the fact that a quite a number of unscrupulous companies accepted deposits from public and failed to repay. The
purpose served by the English Act in England is now sought to be served by the new provisions of Sections 58A and 58 B of the Act.

**Advertisement for Deposits and Discloser:**

Now as per the provisions of section 58-A (2) a company is required to issue advertisement for inviting deposits. If any other person invites deposits on behalf of the company nevertheless the advertisement has to be issued for and on behalf of the company, on the authority and in the name of the Board of Directors.

In the advertisement the company is required to disclose the financial condition, management structure and other particulars of the company, as may be prescribed. The contents of advertisement have been widened by the Amendment in the Rules of Deposits in 1978. Now the statement of financial position of companies required to be included in the advertisement gives more relevant information about the credibility/solvency of the companies. Three new sub-clauses have been added to rule.

(4) As a result, the advertisement must disclose:

(a) the amount of deposit accepted on the last day preceding the financial year.

(b) a statement of over-due deposit, and

(c) a statement that the compliance with the rule
does not necessarily imply that the repayment of deposit is guaranteed by the Central Government and that the deposits rank pari passu with other unsecured creditors of the company.

**Mis-Statement in the Advertisements for Deposits**

The definition of 'prospectus' has been amended to include an advertisement for deposits. Besides, section 58 also lays down that the provisions of the Act relating to a prospectus shall so far as may be, apply to an advertisement for inviting deposits.

The provisions contained in section 62, 63 and 68 of the Act relating to civil and criminal liability for mis-statement in prospectus, and penalty for fraudulently inducing persons to invest money, therefore, ought to apply equally to advertisement for deposits. However, on a closer look at these provisions the apparent does not appear to be real.

Here it may be mentioned that section 62 is applicable, where a prospectus invites persons to subscribe for shares in or debentures of a body corporate. Advertisement for deposits is a prospectus. It may be submitted that section 62 applies only to such prospectus which invites persons to subscribe for shares or debentures. It is therefore, doubtful whether section 62 applies to advertisements for
deposits. This section would better have been amended in line with the amendment of the definition of prospectus so to include advertisement for deposits. Whereas section 63 is applicable 'where a prospectus issued... includes any untrue statement'. This section does not contain any qualifying words as in section 62. Therefore, it appears to apply to advertisement for deposits.

Sacher Committee's Recommendations

This committee not satisfying with the existing provisions has made following recommendations:

(1) that in the advertisement, inviting deposits from the public, must be made compulsory for companies to disclose the contents of the Return, which companies are required to file with the Registrar pursuant to rule 10 of the Rules, particularly the details of amount of deposits which has become repayable during the year and have not been paid eventhough claimed by the depositors,

(2) that the director's report and the application for deposit should also contain the above informations,

(3) to prohibit private companies from accepting deposits or borrowing money from the public,

(4) in order to plug the lacuna found in section 58A it has recommended for the amendment of section.
At there is no penalty in case of default of companies in paying deposits as and when they mature for payment, if the deposits were accepted in accordance with the Reserve Bank of India's direction. Sub-Section (5) which lays down penal provisions would not cover of such default. In order to remove this, it has recommended for the amendment of the section on the following lines:

(i) In case where ten percent of deposits which have matured for repayment, and in respect of which, inspite of claims having been made by the depositors, the same have remained unpaid for over a period of six months, the company, the company and its directors should be deemed to be in default, and the company should be subjected to penalties unless, before the expiry of the said period the companies applies to the Court and makes out a case that inspite of all reasonable efforts by the directors, the company may not be able to repay the debts and therefore, seeks extension of time for repayment. The court at this stage should hear the Registrar and the depositors who are affected and make appropriate orders which the Court may in the circumstances and having regard to all the matter consider it necessary. The company should bear all costs and expenses in giving effect to the order of the Court. In the event the company and its directors
neglecting to apply to the Court, it should be also treated as default for which the company should be penalised.

(ii) A depositor who has not been paid either the interest or the principal or both should have right to move the Court without any authorisation as presently required under section 621 of the Act.

(iii) Companies which have defaulted in paying either interest or the principal or both should be prohibited from inviting or accepting further deposits notwithstanding that the further deposits so invited or accepted are within the prescribed percentage. No company should be allowed to invite or accept deposits only with a view to pay off the earlier deposits accepted by the company.

Here attention may be drawn to the Committee's recommendation in the chapter of winding up, wherein it has recommended that a company which accepts further deposits should be deemed to be unable to pay its debts, and on this ground liable to be wound on a petition by the Registrar.

(iv) that the percentage for acceptance of deposits should be worked out with reference to free reserve.

Further in order to keep watch on brokers, it has asked the Stock Exchanges for looking after activities of the brokers.
It may be submitted that in all these recommendations the Committee has put great emphasis on greater disclosures in respect of company's affairs with a view to provide sufficient safeguards to the unwary depositors.

Unfortunately these recommendations are yet not implemented.
References

1. New Brunswick, etc. Co. V. Muggeridge (1860) 1 Dr. and SM. 383.

2. Sections 159 & 160 of the Act.


5. Sherwell V. Combined Incandescent Mantles Syndicate (1907) W.N. 110, Sleigh V. Glassglow and Transwal option (1904) 6 F. 420.

6. (1928) 2 K.B. 93.

7. Section 285 of the English Companies Act, 1908.


11. (1956) 1 All E.R. 490


13(a) Principles of Modern Company Law 3rd Edn. 296.


14. Pennington on company Law p.203 see also Nash V. Lynde (1929) A.C. 158.

15. 99 Company Law p. 139.
16. (1904) 6 F 420 Cf. of See also Sherwell V. Combined Incandescent Mantles Syndicate (1907) 23 T.L.R. 482.
17. (1911) Ch. 573.
18. Government Stock & Other Securities Investment Co. Ltd. V. Christopher (1956) 1 All E.R. 490
20. Buckley's on Company Law p. 94.
21. See Brunskick, etc. Co. V. Muggeridge (1860) 1 Dr. & S.M 383.
23. Section 64 of the Act.
24. Section 149 (7) of the Act.
25. Principles of Modern Company Law p. 300
27. Buckley on Company Law pp. 95-96.
28. (1903) 1 Ch. 586.
29. (1904) A.C. 342.
30. New Brunswick, etc. Co. V. Muggeridge (1860) 1 Dr. & S.M 383.
32. Central Railway Co. of Venezuela V. Kisch (1866) L.R. 2 H.L. 99
33. Peek V. Gurney (1873) L.R. H.L. 377 p. 403.