

## Principle of Separate Legal Personality of A Company In India

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### Introduction

Ever since the dawn of industrial revolution, the size of business has been to grow day after day. Every growing business requires ever increasing amount of finance and a large number of people to manage its affairs. The proprietorship and partnership firms of business organizations cannot always be found suitable to the needs of growing business. Therefore, company form of organization gradually became popular and preferred choice over the other forms of business organizations. For the large business companies are inevitable. The most outstanding feature of a company is its separate legal personality. It means a Company has a separate personality from its members. By incorporation under the Companies Act, the Company is invested with a corporate personality quite distinct from the individuals who are its members. Being a separate legal personality, it bears its own name and acts under a corporate name. Its assets are separate and distinct from those of its members. It is a different 'person' from the members who compose it. The company acquires its own personality. It becomes impersonalized. No one can say that he is the owner of the company. By the provisions of law, a Company is clothed with a Separate Legal Personality, yet in reality it is an association of persons who are in fact, in a way, the beneficial owners of the property of the Company. A Company, being a legal person, cannot act on its own, it can act only through natural persons.

### Principle of Separate Legal Personality

Principle of Separate Legal personality or Corporate personality is an entrenched legal principle of the English company law. According to the principle, when a company is incorporated under the company, it is recognized as a legal person and have distinguished features, namely perpetual succession, right to enter into legal proceedings, and deals with property under its own name and ability to limit the liability of its members. By law, the company is clothed with the personality which is totally distinct and separate from that of its members The principle of Separate legal Personality was firmly established by the House of Lords in the well-known case of **Salomon v. Salomon & Co. Ltd.** In Salomon case Lord Macnagthen observed: "The company is at law a different person altogether from the subscribers to the memorandum; and, though it may be that alter incorporate the business is precisely the same as before, the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustee for them. Nor and the subscribers as members liable, in any shape or form, except to the extent and in the manner provided by the Act".

The principle of separate legal personality of a company was again confirmed in **Lee v. Lee's Air Farming Ltd.** In this case, Lee formed a company for the purpose of carrying on business of Ariel top-dressing. He was the beneficial owner of the shares and also the sole governing director of the company. He got himself appointed as chief pilot of the company on a salary. He died in a flying accident while working for the company. His widow claimed compensation under the Workmen's Compensation Act for the death of her husband during the course of his employment. The company opposed the claim on the ground that both Lee and the company were one and the same person. The

Privy Council held that Lee and his company were distinct legal entities and the widow of Lee was entitled for compensation.

### **Position In India**

The principle of separate legal personality had been recognized in India even before the Salomon's case. The Calcutta High Court is believed to be the first in India to recognize the principle of Separate Legal Personality of the company in **Kondoli Tea Co. Ltd., Re.** In this case, certain persons transferred a tea estate to a company and claimed exemptions from ad valorem duty on the ground that they themselves were the shareholders in the company and, therefore, it was nothing but a transfer from them in one to themselves under another name. The Court observed that the company was a separate person altogether from the shareholders and the transfer was a transfer of property from other person to the company. In another important case **Dhulia Amalner Motor Transport Ltd. v. R.R. Dharamsi.**, The Court upheld the position that a company is a separate legal person distinct from its members.

The Indian Companies Act 2013 also recognizes principle of separate legal personality of the company. **Section 9** of the Companies Act 2013 says the "from the date of the incorporation mentioned in the certificate, such the subscribers to the memorandum and all other person who may from time to time, become the members of the company, shall a body corporate by the name contained in the memorandum, capable of exercising all the functions of an incorporated company and having perpetual succession with power to acquire, hold and dispose of property both movable and immovable, tangible and intangible to contract and to sue and be sued by the said name". Thus, in India, a company is vested with separate legal personality by its incorporation under the Companies Act. From the date mentioned in the Certificate of Incorporation, a Company acquires a legal personality distinct and separate from its members.

In **State Trading Corporation of India Ltd. V. Commercial Tax Officer 5**, it was held that a company is a legal person having nationality in accordance with the country of incorporation but it is not a citizen. Further the Supreme Court of India affirming principle of separate legal personality of company in India as laid down in Salomon case, in **Tata engineering & Locomotive Company Ltd. v. State of Bihar**, described the legal position of Company in following words: "The Corporation in law is equal to a natural person and as a legal entity of its own. The entity of the Corporation is entirely separate from that of its shareholders" Recently in **State of Karnataka v. Salve J. Jayalalitha**, the Supreme Court emphasized that the Company is a separate entity from members subject to the exception when company is a mere sham or clock used to misdirect shareholders and authorities.

### **Ignorance of Separate Legal Personality**

Indeed, the theory of separate legal personality is the basic principle on which the whole law of corporations is based. But as the separate legal personality of the company is a statutory privilege, it must be used for legitimate purposes only. Where a fraudulent and dishonest use is made of separate legal personality, the individuals concerned will not be allowed to take the shelter behind the separate personality. The court will breakthrough separate personality. This is known as "lifting of corporate veil". The court will look behind the separate entity and take action as though no entity separate from the members and make the members or controlling persons liable for debts and obligations of the company.

### **Circumstances Where Court Can Ignore Separate Legal Personality**

The court can ignore the corporate personality of company and lift the corporate veil in following circumstances-

- (1) Under Judicial interpretations

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(2) Under Statutory provisions

#### **Under Judicial Interpretations**

Under judicial interpretations, following grounds are well established where Separate Legal Personality may be ignored the courts-

- (a) Where determination of character of the company becomes essential.
- (b) Where the Separate Legal Personality has been used for the commission of fraud or improper conduct.
- (c) Where the sole purpose for which the company was formed was to evade taxes.
- (d) Where the sole purpose for the formation of new company was to use it as a device to avoid compliance of Welfare legislation.
- (e) Agency, where no functioning autonomy granted to the subsidiary company.
- (f) Failure of state to perform Constitutional duties and functions of public sector Undertakings.

#### **Under Statutory Provisions**

In the following cases Separate Legal personality may be ignored as per the express provisions of the Companies Act 2013-

- (a) Misrepresentation in the Prospectus.
- (b) Failure to return application money.
- (c) Misdescription of the name of the company.
- (d) To investigate the ownership and affairs of the Company.
- (e) Fraudulent conduct of business.
- (f) Non-compliance of requirements of incorporation.

#### **Conclusion**

Thus, it can be said the principle of the separate legal personality of company is not applicable in all case. There are instances where the court moves beyond this principle and ignores it. However, the grounds for ignoring or lifting of corporate veil are not exhaustive. It depends on the facts and circumstances of each case. Apart from the statutory provisions, the Courts in India have time and again ignored the separate legal personality of company in cases of fraud, sham, tax evasion and other obligations to impute the liability to the shareholders or directors who are real beneficiaries of the Company. But whether or not, a case is fit for ignoring the separate legal personality, it depends on the facts of each case and the Court is to decide the same. The Position in India and outside India is almost the same.

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