

## Formation of a Company Class 11 Notes

There are various steps you need to take for legally registering a company which can vary from documentation to sorting out various other details. In this chapter, you will study about essentials required to set up a business process but also the business ethics and corporate governance lessons associated with them. Let's first take a look at the major terms under the topic of Formation of a Company:

### Business Finance

The first step towards setting up a business is finding the means to do so. This is where business finance comes in. To secure finance, one must acquire and conserve capital funds. This fund should be enough to meet the basic requirement of the business and allow it to meet its objectives. There are several types of business finance which play an imperative role in financing the diverse activities carried out by the business.

### Formation of a Company

The formation of a company is a complex process which involves completion of legal formalities and procedures.

There are three steps or stages involved in formation of a company. They are:

- Promotion
- Incorporation
- Subscription of Capital

### Promotion of a Company

As per the chapter on Formation of a Company, promotion is also a vital part of starting a business and can also be termed as the visualization of a company. It is the first stage and involves the formation of the idea, which exploits an opportunity to meet market demand for a product or service.

- Involves the process of formulating a business concept or idea and taking steps towards forming a company
- This is done so that one can avail the business opportunity and exploit it to their benefit
- It is the primary stage in the formation of a company

## Functions of a Promoter

A promoter is an important person in the formation of a company. A promoter is an individual or a team of individuals involved in conceiving the foundational idea on which a company is established. According to the chapter on Formation of a Company, here are the different functions carried out by a promoter:

1. **Identifying and understanding the business opportunity**
  - The opportunity could be making a certain product available through some other channel or capturing an opportunity which has potential
  - The opportunity is then studied and analysed by the promoter for its economic and technical feasibility.
2. **Feasibility studies** - All business opportunities may not have the feasibility or economic capability to be turned into a real project. This is why it is important to undertake feasibility studies. The following feasibility studies may be undertaken:
  - Technical Feasibility - An idea may seem promising but may not be technically viable to execute.
  - Economic Feasibility - An idea may seem promising technically and may have good financial prospects but may not be economically feasible.
  - Financial Feasibility - Every economic idea needs funds to bring it to life. If the promoter is not able to build funds for a business or economic idea then it needs to be given up.
3. **Name of Approval** - The promoter needs to get the company name approved, trademark and registered.
4. **Fixing up Signatories for the Memorandum of Association**
  - It is up to the promoters to decide and choose the members who will be the signatories of the Memorandum of Association of the proposed company.
  - The people who sign the Memorandum of Association are also the First Directors of the company.
5. **Appointment of Professionals** - It is also the job of the promoters to appoint auditors, accountants, technical support and others for specialisations needed to run the company.
6. **Preparation of Necessary Documents** - The promoter has the duty to take up steps to prepare the legal documents which have to be submitted, required under law, to the Registrar of the Companies, for getting the company registered.

## Documentation for the Formation of a Company

The next section under the chapter on Formation of a Company, the following documents must be submitted to register a company or business:

Name of Document	What it Contains
Memorandum of Association	The Memorandum of Association contains: Name Clause, Registered Office Clause, Objects Clause, Liability Clause, Capital Clause
Articles of Association	They are rules related to the internal management of the company. Rules mentioned here are subsidiary to the MoA
Consent of Proposed Directors	Each person who is a director of the company needs to give a written consent confirming that they agree to the Act and undertake or agree to buy and pay for qualification shares
Agreement	The agreement which is signed between the individuals entering in the company as manager and director needs to be submitted to the office of the Registrar, to get the company registered
Statutory Declaration	This is a declaration which states and confirms that all legal formalities and requirements have been met and completed and will be submitted to the Registrar.
Receipt of Payment of Fee	The fees, the amount of which depends on the authorised share capital of the company has to be paid in order to get the company registered



## Promoter Support

Promoters are neither agents nor trustees of the company. They have an important role to play in the formation of a company. However, following guidelines of social responsibility and corporate governance, they undertake every activity needed to get the company afloat.

## Incorporation

After submitting all necessary documents, an application for the incorporation of the company is made by promoters. This is submitted to the Registrar of Companies of the State with which the company is registered. There are many case studies out there following the footsteps of successful companies and how they were formed. It presents a wonderful insight into how the world of business truly works.

## Consequence of getting the Certificate of Incorporation

The chapter on Formation of a Company also explains that a company is legally considered in existence from the day when their certificate of incorporation is printed. Thus, on this date, the company becomes a legal entity. It is also proof that it is a legal business which performs duties, and in spirit upholds all types of business ethics. Business studies deal with both the process and the business ethics of the whole section.

- A company gets its real identity and comes into existence on the date printed on the Certificate of Incorporation
- The Certificate of Incorporation is true evidence of the regularity of the incorporation of a company
- When there is perpetual succession on the date printed on the Certificate of Incorporation, it becomes a legal entity

## Capital Subscription

Now, coming to a public company, it has to raise funds by means of issuing shares and debentures. To get this out there, it releases a prospectus to the public, which is essentially an invitation for the public to buy their shares. The requirements for this action are as follows:

### SEBI Approval

- Taking approval from SEBI - SEBI or the Securities and Exchange Board of India is the regulatory authority in our country and it has issued guidelines for investor protection and disclosure of information



- Any public company which invites fund from the public must make adequate disclosure of all relevant information and must not conceal any information

### **Filling of Prospectus**

- A copy of the prospectus is filed with the Registrar of Companies

### **Appointment of Brokers and Bankers**

- It is not easy to raise funds for the public. The money needed for the application is to be received by the bankers of the company
- The job of the brokers is to encourage the public to buy the shares of the company. They do so by distributing forms and asking the public to apply for the shares

### **Minimum Subscription**

- To prevent companies from beginning with inadequate resources it has been provided that the company must receive a certain minimum number of shares before going ahead with the allotment of shares. This according to the Companies Act is called the Minimum Subscription

### **Application to Stock Exchange**

- An application needs to be made to one stock exchange at least for the permission to deal in its shares or debentures

### **Allotment of Shares**

- The application money should be in a separate bank account till the time, shares are allotted
- Allotment letters are issued to the successful allottees

## **Commencement of Business**

Once the minimum subscription is raised, the next step is to send the application to the registrar of companies for issuance of the certificate. This step is necessary for public companies only, as for private companies, the same is achieved right after incorporation. The application must contain the following documents:

- A declaration that minimum subscription has been met
- A declaration with details of allotment of directors

- A declaration of the money payable to applicants
- A statutory declaration

There are also public companies that raise funds privately. They only have to submit:

- A declaration of the money payable to applicants
- A statutory declaration

Once the registrar is satisfied, they will issue the certificate of commencement of business.

## Continuing the Business as Usual

The chapter on Formation of a Company elaborates on what happens once the business is up and running. Businesses usually form contracts which they must honour and these detailed services to be provided against payments due to those services. Thus, a business starts earning profit from the day of commencement. There are many other ethical aspects of Business Studies. However, in the portion which talks mainly about the Formation of a company, these business ethics lessons are limited. Registering a company, especially a public limited company, successfully might seem like a huge task. But, when broken down to its core components, it is not so.

There are several organizations across the country that are dedicated to easing the way promoters may register a company. However, since the company is someone's brainchild, it is always more prudent to do the registration themselves.

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## Formation of a Company Class 11 Important NCERT Questions

**1. Minimum number of members to form a private company is:**

- (a) 2
- (b) 3
- (c) 5

(d) 7

**Ans: a) 2**

**2. Minimum number of members to form a public company is:**

(a) 5

(b) 7

(c) 12

(d) 21

**Ans: b) 7**

**3. Application for approval of name of a company is to be made to:**

(a) SEBI

(b) Registrar of Companies

(c) Government of India

(d) Government of the State in which Company is to be registered

**Ans. b) Registrar of Companies**

**4. A proposed name of Company is considered undesirable if**

(a) It is identical to the name

(b) It resembles closely with an existing company the name of an existing company

(c) It is an emblem of Government

(d) In case of any of the above of India, United Nations etc.

**Ans. (d) In case of any of the above of India, United Nations etc.**

**5. A prospectus is issued by**

(a) A private company

(b) A public company seeking investment from public

(c) A public enterprise

(d) A public company

**Ans. (b) A public company seeking investment from public**

**6. Stages in the formation of a public company are in the following order**

(a) Promotion, Commencement of Business, Capital Subscription, Incorporation

(b) Incorporation, Capital Subscription, Promotion

(c) Promotion, Incorporation, Capital Subscription, Commencement of Business

(d) Capital Subscription, Promotion, Incorporation

**Ans. (c) Promotion, Incorporation, Capital Subscription, Commencement of Business**

**7. Preliminary Contracts are signed**

(a) Before the incorporation

(b) After incorporation but before the capital subscription

(c) After incorporation but before the commencement of business

(d) After commencement of business

**Ans. (a) Before the incorporation**

## Important Questions

### 1. What is a Memorandum Of Association?

One of the most important documents that are required for the formation of a company is a Memorandum of Association. It mentions the object for which the company is getting incorporated. The rights, privileges and powers of the company are contained in this document. A memorandum of association determines the relationship of the company with outsiders.

### 2. Who is a Promoter of a Company?

The person or organisation responsible for performing the preliminary works and activities that are involved in the process of formation of a company is known as the Promoter of a company.



Different types of activity such as motivating people, incorporation and promotion are performed by the promoter.

### **3. What is a preliminary contract?**

A preliminary contract is a contract which is signed by promoters with third parties before the incorporation of a company.

### **4. What are the functions of a promoter?**

The functions of a promoter include:

Identifying the business opportunity

Conducting feasibility studies

Getting the approval of the name

Fixing up signatories to the Memorandum of Association

Getting the appointment of professionals done

Getting the necessary documents prepared

### **5. How many members should sign a Memorandum of Association with a public company?**

A minimum of seven members are required to sign a memorandum of association successfully with a public company.