Non-Trading Concerns

Non-trading is an accounting term used to describe a company's activities that do not result in the generation of income or the incurrence of expenses. In other words, non-trading means that a company is not conducting any business operations. Non-trading can be caused by several factors, such as a company being in the process of being sold or being wound up.

There are a few benefits to non-trading, including the following: First, it can help a company's Cash Flow position by preventing it from incurring any expenses. It can make it easier for a company to be sold or wound up. It can help a company's Financial Statements from being clouded by irrelevant activity. Lastly, it can help to improve a company's financial position by reducing its liabilities and increasing its assets.

There are a few drawbacks to non-trading, including the following: First, it can lead to a company becoming dormant, which can have negative consequences such as a loss of tax exemptions. It can make it more difficult for a company to raise capital. It can impact a company's ability to compete in the market. It can make it more difficult for a company to attract and retain employees. It can lead to a decrease in the value of a company's shares. It can result in a company being sued by its creditors. Lastly, it can result in a company being investigated by the authorities.

There is no definitive answer to this question as it will depend on the specific circumstances of each case. However, it is generally recommended that a company should try to move out of non-trading as soon as possible to avoid any negative consequences.

A company can be in non-trading and trading at the same time, but this would be rare. Normally, if a company is conducting any business activities, it will be considered to be trading and not non-trading.

Service Organizations

An organization providing intangible services rather than tangible goods is termed as **Service organization**. In the standard industrial classification, **service organizations** include hotels, restaurants and other lodging and eating establishments, barber shops, beauty parlors and other personal services, repair services, motion picture, television and other amusement and recreational services, legal services and accounting, engineering, research/development, architecture and other professional organization. **Service organizations** also includes educational organizations, banks, insurance companies and other financial institutions. Also government agencies and most other non-profit organizations are **service organizations**.

A service organization is when two or more people are engaged in a systematic effort to provide services to a customer - the objective being to *serve* a customer. For any service to be provided, there has to be a customer. Without a customer, and *interaction* between customer and the service organization, the objective of providing service cannot happen. The degree of intensity of interaction between the customer and people of a service organization varies, and depends on the type of service offered. For example, a specialist medical consultant will have a high degree of face-to-face interaction with the customer, and so will a hairdresser. Further down the scale of face-to-face interaction comes a restaurant, where the customer judges the quality of service by the level of interaction (knowledge of wine waiter, attentiveness of waiting staff) as well as by the standard of the goods provided (wine and food). The restaurant in turn will, however, have a higher degree of personal interaction than does a fast food takeaway (see Figure 7.1). At the bottom of the scale in Figure 7.1 is automatic cash-point banking, where customer interaction is purely with a machine.

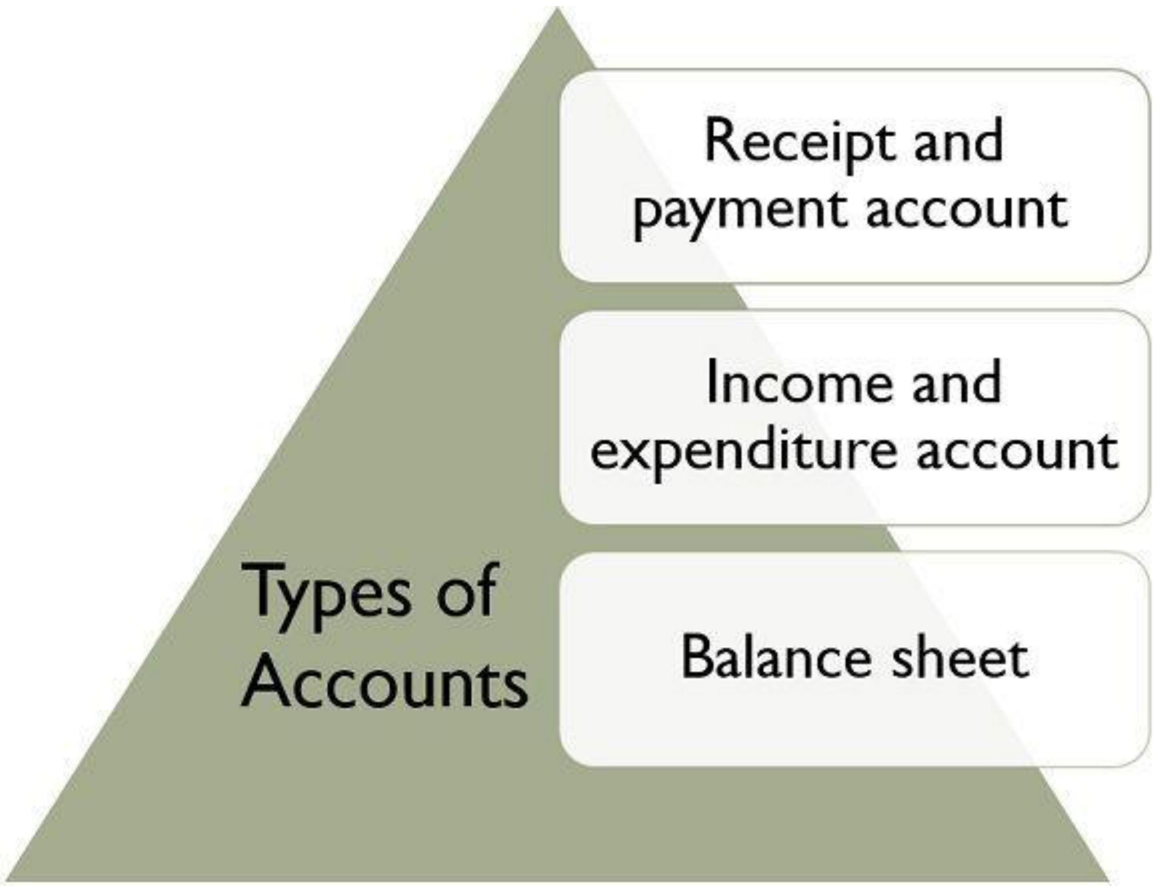
Characteristics of Service Organizations

- **Quantity Measurement**: It is easy to keep track of the quantity of tangible goods, both during the production process and when the goods are sold, but it is not easy to measure the quantity of many services. We can measure the number of patients that a physician treats in a day, for example, and even classify these visits by type of complaint, but this is by no means equivalent to measuring the amount of service that the physician provides to each of these patients. For many services the amount rendered can be measured only in a crude terms, if at all.
- **Absence of inventory:** Goods can be held in inventory and this inventory is a buffer that dampens the impact on production activity of fluctuations in sales volume. Services cannot be stored. If the services available today are not sold, the revenue from these services is lost forever. Resources available for sale in many service organizations are essentially fixed. In the short run, a hotel can't increase the number of rooms that it offers for rent and it does not reduce costs substantially by closing down some of its rooms. These facts cause a great stress to be placed on planning for an amount of available services that is not in excess of what can be sold currently and on marketing efforts to sell these resources each day. The loss from unsold services is such an important factor that it normally is a key variable in service organizations of all types
- **Quality Measurement**: The quality of tangible goods can be inspected, and in most cases the inspection can be performed before goods are released to the customer. If the goods are defective there is physical evidence of the nature of the defect. The quality of a service can't be inspected in advance at best it can be inspected during the time that the service is being rendered to the clients. Judgments as to the adequacy of the quality of the most services are subjective measuring instruments and objective quality standards do not exist. An accounting firm can measure the number of hours spent on an audit, but not the thoroughness of the work done during those hours. A consulting firm has no objective way of appraising the soundness of its recommendations.

Non-profit organization are **established to provide aid to society**, such as developing charity, commerce and religion. However, it has a separate legal entity other than its members, and their primary objective is to provide services without the intention of earning profits in return like trading organizations. The main source of earning for such organizations are “**Donations**” and “ **Government Grants**” which are not certain.

Thus, the fund received is treated as “**Surplus**” and not a profit in the organization’s income and expenditure account. This surplus fund will be utilized for the further betterment of the organizations and providing more facilities to the society.

Types of Accounts in a Non-Profit Organization



Since, these organizations don’t work for profit-making, preparing trading and profit and loss account is not relevant for them, these organizations prepare:

1. Receipts and Payments Account

Numerous charitable organizations prepare receipt and payment account, which **shows the random cash transactions that occurred throughout the year**. It is competent for small organizations, but it has a disadvantage that pre-payments and accrual payments are not recorded in it; however,

- It only debits the account with all the receipts and credits the account with all the payments irrespective of its nature.
- It can be revenue or capital nature payments for the current year, previous year, successive year, and at last, it displays only bank or cash balance.

Format of Receipt and Payment Account

XYZ Limited
For the year ended 31, December 2019

Receipts	₹	Payments	₹
To balance b/d cash xx bank xx	xxx	By wages	xxx
To subscription -Previous year -Current year -successive year	xxx	By electricity	xxx
To life membership fees	xxx	By stationery	xxx
To donations	xxx	By bank charges	xxx
To interest	xxx	By travelling expenses	xxx
To dividend	xxx	By sundry expenses	xxx
To entrance fees	xxx	By repairs	xxx
To sundry receipts	xxx	By balance c/d cash xx bank xx	xxx
	-------- XXXX --------		-------- XXXX --------

2. Income and Expenditure Account

Income and expenditure account is the final account for the non-profit organization which deals with the revenue receipts and expenses. It is prepared on the basis of the accrual concept of accounting, i.e., **it displays the summary of only current accounting year transactions** regardless of whether received/paid in the current year or not.

All the incomes are recorded on the credit side, and all the expenses are recorded on the debit side of the statement. If the credit side exceeds debit side it would be a surplus and vis-a- versa if debit side exceeds credit side it would be considered as a deficit. At last, the remaining balance, whether deficit or the surplus gets transferred to Capital account of the proprietor. It is like a profit and loss account of the trading organizations.

Format of Income and Expenditure Account

XYZ Limited
For the year ended 31, December 2019

Expenditure	₹	Income	₹
To salary and wages (+) Previous Year Prepaid (-) Current Year Prepaid	------- xxx	By donation	xxx
To depreciation	xxx	By dividends	xxx
To repairs	xxx	By interest on deposits	xxx
To bad debts	xxx	By subscription (-) Previous year outstanding (+) Current Year outstanding	------- xxx
To printing and stationery	xxx	By entrance fees	xxx
To rent	xxx	By all revenue receipts	xxx
To all revenue payments	xxx	By grants received	xxx
To surplus *(excess of income over expenditure)	xxx	By deficit *(excess of expenditure over income)	xxx
	------- XXXX -------		------- XXXX -------

3. Balance sheet

After preparing receipt and payment and income and expenditure account, the non-profit organization prepares balance sheet **stating the position of the organization's assets and liabilities**. Such organizations' balance sheet is similar to the other trading organizations prepare at the end of the financial year. Capital fund in it is the overall excess capital after reducing all assets from all the liabilities, which includes revenue earned as well as surplus earned throughout the year by the organization.

Format of Balance sheet

XYZ Limited
As at 31, December 2019

Liabilities	₹	Assets	₹
Capital account			
(+)surplus		Current assets	
(-)deficit			xxx

(+)entrance fees		Cash and bank balance	
	xxx		
(+)life membership			xxx
	-----		
subscription		Fixed deposit	------
(capitalized)		----------------	xxxx
---------------------			------
		Fixed assets	
		Building	
Bank overdraft	xxx	(+)addition	xxx
		(-)depreciation	

		Furniture	
		(+)addition	
Outstanding expenses	xxx	(-)depreciation	xxx
		(-)sale of furniture	

		Investments	
Creditors	xxx	Prize funds	xxx
		Government securities	xxx

Liabilities	₹	Assets	₹

Inventory	xxx	Machinery (+)addition (-)depreciation ---------------------	xxx
	------------- xxx -------------		------------- xxx -------------

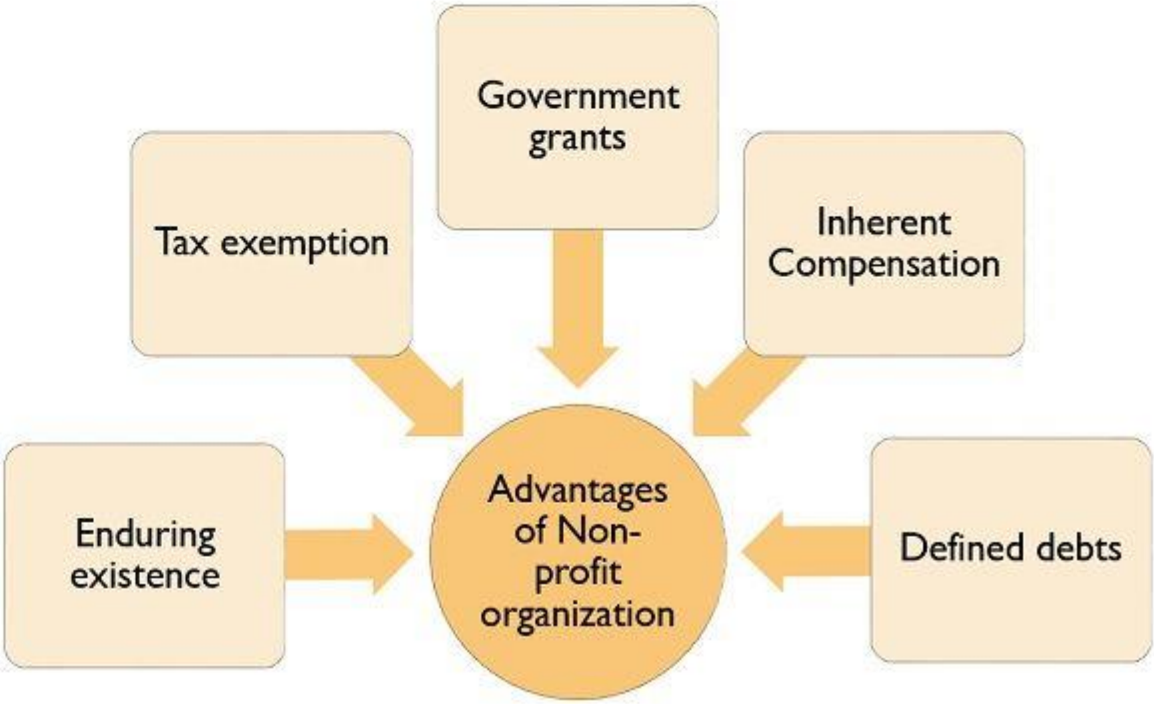
Features of Non-profit Organization

Following are the features of the Non-Profit Organization:

1. The primary objective of such organizations is to serve society.
2. No surplus gets distributed among its members.
3. Major funding is done by donation and contribution in the non-profit organization.
4. The non-profit organization also considered as a separate legal entity.
5. The elected members of the organization handle the administration.
6. Numerous non-profit organizations are dependent on the active assistance of the volunteers.

Advantages of Non-Profit Organization

Following are some of the advantages of Non-Profit Organization:



1. **Enduring existence:** Non- profit organizations have life even if the promoter or donour leaves the organization. They are always admissible to make revenue from other donours.
2. **Tax exemption**: Non- trading organization are exempted from paying taxes to the government; thus, they can regulate their whole income back in the organization's advancement.
3. **Government grants:** Non- profit organizations get various allocations from the government in the form of government grants for the betterment of the organization and to benefit society.
4. **Defined debts:** In case of any dispute creditors have explicit rights for suing on the organization; they can only recover their debts with the organization's assets, and the owner is not liable to pay any indebtedness with his personal assets.
5. **Inherent Compensation:** Non- profit organization administer services and favour to the overlooked or neglected section of the society, such as impoverished children.

Disadvantages of Non-profit Organization

Following are the disadvantages of the Non-Profit Organization:

1. **Time and Money:** For starting a non-profit organization, it takes a lot of money and devotion towards work, without any intention of earning profit in return.
2. **Maintenance Expenses:** Non-profit organization have to maintain the costs incurred during the year from the limited available funds so that the organization continues for long run efficiently.
3. **Public Enquiry:** Anyone from the general public can ask for the non-profit organization's fillings and can review their incomes and expenditures. If you have a broad public-facing organization, you become liable to answer their questions to maintain your organization's image.
4. **No Gain:** Non-profit organizations don't offer any profit to its members; thus, it becomes difficult sometimes to bring out concern from the likely investors.
5. **Filling Burden:** To maintain the active and exempt status, the non-profit organization's need to acknowledge annual fillings to the government.

Receipt and Payment Account Vs Income and Expenditure Account

Basis of comparison	Receipt and Payment account	Income and Expenditure account
Initiation	It automatically initiates with the opening balance carried forward from the previous year.	It does not have any opening and closing balance.
Nature	It is summary of the overall cash affairs of the organization of the current accounting year.	It is an analysis of income and expenses of the organization.
Items	It comprises of both capital and revenue	It only consists of revenue items.

Basis of comparison	Receipt and Payment account	Income and Expenditure account
	receipts and payments.	
Balancing	At the time of closing accounts the balance left in this account is treated as cash-in-hand or bank balance.	It shows the surplus or the deficit at the end of the year.
Recordings	In receipt and payment accounts subscriptions, Life membership fees, donations are recorded.	Provisions,bad debts, and depreciation is recorded is this account.
Debit/Credit	Receipts are debited and payments are credited in this account.	All expenses and losses are debited whereas; all incomes and gains are credited in this account.
System	Cash system of accountancy is used for preparing this account.	Mercantile system of accountancy is used for making of this account.
Accounts	It is treated as a real account.	It is treated as a nominal account.
Outstanding balances	Outstanding expenses and incomes are not considered in this account,it only deals with cash transactions.	All the outstanding expenses and incomes are considered in this account.

Conclusion

Non-profit organization work for the betterment of humanity without any hope of rewards in monetary and non-monetary form. Members in it work with devotion towards society and provide various charitable services for which government and different investors offer a fund to these organizations.

These organizations are free from the tax burden, i.e. they do not have to pay taxes to the government in the form of income tax, but they need to maintain proper records of their works in the organized format for getting this advantage.

Section 8

A company is referred a to as **Section 8 Company** when registered as a Non-Profit Organization (NPO) i.e. when it the has motive of promoting arts, commerce, education, charity, protection of the environment, sports, science, research, social welfare, religion and intends to use its profits (if any) or other income for promoting these objectives.

The income of NPO can not be used for paying out dividends to the company's members and has to be for the promotion of charitable objectives. Such companies obtain an incorporation certificate from the central government and are liable to adhere to the rules specified by the government.

According to the rules, failure to comply with the responsibilities stated by the Central Government may lead to the winding up of the company on the orders of the government. Besides, strict legal action will be taken against all the members of the company if the objectives laid down by the company prove to be bogus.

Eligibility to Apply for Section 8 Company

An individual or an association of individuals are eligible to be registered as a Section 8 Company if it holds the below-mentioned intentions or objectives. The objectives have to be confirmed to the satisfaction of the Central Government.

- When the company intends to promote science, commerce, education, art, sports, research, religion, charity, social welfare, protection of the environment or alike other objectives;
- When the company holds an intention to invest all the profits (if any) or any other income generated after incorporation in the promotion of such objects only;
- When the company does not intend to pay any dividend to its members.

Incorporation of a Section 8 Company

Companies Act, 2013 deals with the procedure of Incorporation of a Section 8 Company and as per this section, an application in Form No. INC.12 has to be submitted along with the below-mentioned documents to the Registrar of Companies.

orm no. INC – 13 – Company's Draft Memorandum of Association (MOA) and Articles of association (AOA) in Form No. INC – 13 (as specified in Act) along with the affixation of subscribers' photographs.

Form no. INC-14 – A Declaration is to be affixed in Form no. INC-14 that the draft MOA & AOA are compliant with the provisions & norms of section 8 and the requirements as per Section 8 have been duly taken care of.

Note: The declaration has to be made on stamp paper & should be notarized by an Advocate, a Company Secretary, a Chartered Accountant or a Cost Accountant, practising the profession.

Form no. INC-15 – A declaration in Form no. INC-15 on stamp paper & notarized by each member of the company who is applying.

Form no. INC-9 – Form no. INC-9 form first directors as well as each subscriber, on the relevant State's stamp paper and appropriately notarized.

An estimation of the company's future annual income and expenditure for the next three years, mentioning the sources of the income and the purpose of the expenditure.

New & Simplified Process of Incorporation of Section 8 Companies

Companies (Incorporation) Sixth Amendment Rules, 2019 dated 7th June 2019 to ease the Incorporation process has knocked off the need for filing Form no. INC 12, which was initially needed.
This amendment has made the Process of Incorporation of Section 8 Companies as easy & simple as that of other companies.

Section 8 Companies can be incorporated by reserving names in part A of Spice+ followed by part B of the Spice+ form or by directly filing Spice+. License No. shall be given to the section 8 company during the incorporation.

When the Company Already Have the License Number

Stakeholders having License Numbers already before the filing of the SPICe form may file the form at their ease. However, one thing should be noted form processing takes time to let the workflow changes be effective.

Documents Requirement for the Registration of Section 8 Company

- Digital Signature Certificate
- Memorandum of Association
- Articles of Association
- Passport Size Photographs
- Members' Id Proof such as Aadhar Card, Passport, Voter Id
- Details of Director (When the Members Are Other Companies/LLPs)
- Address Evidence
- Director Identification Number

Most Important Advantages for the Incorporation of Section 8 Company

- Through building the section-8 company the intention or goal of the company would perform any activity and obtain integrity and commitment because the same is being approved made through the Union government.
- Towards operations because of its strict rules, the same pose a trustful image in front of internal and external users of the details with respect to the communities.
- The reliability of section 8 company has much more with respect to the communities and the additional kinds of charitable firms.
- Grants and subsidies via the government and the additional institutions were acknowledged to the section-8 company according to the communities of trust.

Section 8 Company Total Exemptions and Reliefs

Companies Act 2013:

- The directorship under section 8 companies shall not come under the computation of the ceiling towards the highest number of the directorships which has been mentioned beneath Section 165 of the Act.
- Through furnishing the notice of not less than 14 exact days rather than 21 exact days a general meeting has been conducted.
- Section 8 firm would conduct at least one meeting every 6 calendar months rather than holding 4 meetings for a year.
- Recording of Minutes of General Meetings, Board Meeting along with additional resolutions shall not be subjected to apply upon the section 8 company. But the minutes of meetings might be recorded within 30 days of the outcome of the meeting towards the cases in which the firm articles furnish towards the confirmation through the method of circulation of minutes.

- A company would be a member of a section 8 company.
- Section 149(1) of the Act will not apply towards Section 8 company as per Section 8 company shall not need to hire an Independent director. From the reasons above the Audit committee under section 8 company will not be needed to have independent directors similar to its board members.
- Section 8 firms shall not be needed to hire a qualified CS professional as its company secretary.
- From the applicability of secretarial standards, the same gets privileged.
- Section 8 firms shall not be needed to appoint a Nomination and Remuneration Committee and nor a Stakeholders Relationship Committee.

Number of Directors in a Section 8 Company

Section 149(1) of the Companies Act 2013 – prescribed minimum of 3 & 2 directors for public limited & private limited companies respectively and a maximum of 15 directors.
But there is no minimum or maximum prescription for section 8 company.

The second proviso to section 149(1) – prescribes a woman director in a specified class of companies.

Section 149(3) of the Companies Act 2013 – prescribes resident directors in every company.

Section 165 of the Companies Act, 2013 – says Directorship in Section 8 Companies will not be summed up when the total number of directorships will be calculated i.e. it will not be counted while adhering to the maximum limit of twenty Directorship as prescribed in the Act.

Section 149(1) of the Companies Act, 2013 – vide exemption notification dated June 05, 2016, stated that Section 8 Companies are not under obligation to appoint an independent director and are free from all the consequential provisions concerned with Independent directors.

Under Section 149(3) – Section 8 company must have a minimum of one Resident Director i.e. a director who has resided in India at least for a total period of 182 days (one hundred and eighty-two days) or more within the previous calendar year.

Total Number of Board Meetings and its Quorum

As per the exemption notification read with sections 173(1) and 174(1), Section 8 companies must have at least one meeting within a period of 6 calendar months and the quorum for its board meetings is 8 directors or 1/4th of its total strength, whichever is less, respectively. However, the quorum should have a minimum of at least two members.

Some Misleading Facts About Incorporation of Section 8 Company

- Directors in form no INC 15 affidavit is required.

    - The matter concerned with form no INC 15 be self-declaration should be accepted and properly executed.
- Section 8 company applicability of INC 33 and 34.
    - A duly signed copy of the MOA and AOA by the witnesses and members (professionals) along with the expenditure statement and estimated income of 3 years must be attached.
- Notarized Memorandum and Articles of Association.
    - Notarization of Memorandum and Articles of Association not compulsory.
- Government fees are on the higher side.
    - The stamp duty of Section 8 Company if compared to the stamp duty of MOA and AOA is neutral.

Annual, Quarterly and Monthly Compliance for Section 8 Company

Here are providing a list of Monthly, quarterly and annual compliance for section 8 company under MCA (Ministry of Corporate Affairs)

Annual Compliance Under Section 8 Company

- **Appointment of an auditor:** Under section 139 of the Companies Act 2013, it is essential for the firms to hire an auditor within 30 days from the start date. The book of accounts and manual returns of the company will get audited through the statutory auditor who would be hired for a duration of 5 years.
- **Maintenance of Statutory Registers:** It is obligated for the company to maintain a statutory register consisting of members, loans received, charges made, its directors, and others. as listed under section 8 of the companies act 2013.
- **Calling board meet:** Section 8 companies will have at least one meeting every 6 calendar months.
- **Statutory Audit:** Every entity who would enrol under the companies act would need to audit their books of accounts every year from a CA.(refer to point 1).
- **GM notice:** A section 8 company could hold a general meeting i.e whether yearly or extraordinary with min 14 days notice.
- **Calling AGM:** Annual general body meeting would be held once a year within 6 months of the finish of the fiscal year. But, in the case of the first annual general meeting, the company could hold AGM in less than 9 months from the finish of the first fiscal year. You must learn that the time duration between 2 annual general meetings need not surpass 15 months.
- **Board Reports:** The Board of directors of the company will furnish their board's report in a specific way, it comprises all the financial statements and additional annexure. The board report would be needed to get furnished in Form AOC-4.
- **Making of Financials Statement of the Company:** The organization would obtain the balance sheet, profit, loss A/C, cash flow statement as well as additional financial statements audited via statutory auditor i.e is to be furnished with ROC.
- **Tax returns:** Income tax returns would be needed to get furnished during the finish of every assessment year prior to the date 31st Oct.

- **Tax audit:** Tax audit report in Form 10B would get filed through a charitable or religious trust or institution that would be enrolled u/s 12A or who has submitted an application for registration by filing Form 10A. Form 10B is an audit report which is provided by a CA upon nomination by the taxpayer.
- **Filing Financial Statements:** The financial statement would get furnished in the suitable form (E-FORM AOC-4), within 30 days from the date of the annual general meeting (Discussed in point 7 above).
- **Annual Return Filing:** The annual return filing consists of all the details such as management details, and shareholders' information would be filed in Form MGT-7 with the Registrar of Companies (ROC), within 60 days of the annual general meeting.
- **DIN KYC:** Every person who would be provided with a DIN dated 31st March of the fiscal year should submit his KYC on or prior to September 30 of the next fiscal year.
- **GST Annual Return:** Beneath GST, the enrolled assessee needed to file GSTR-9 i.e the annual return. 31st December of the year will be the last date following the related fiscal year.

Form No	Compliance	Due date	Last date
AOC-4	Director report	Within 30 days of AGM	29th October
MGT-7	Annual returns	Within 60 days of AGM	28th November
Form ITR-6	Income tax returns	31st October	31st October
GSTR-9	GST Annual Return	31st December	31st December
Form- 10B	Tax Audit	31st September	31st September

Monthly or Quarterly Due Date

- GSTR-1 (return to be filed towards reporting details of all outward supplies of goods and services incurred)
- Monthly, by the 11th of every month- The business poses a yearly aggregate turnover exceeding Rs 5 cr or would not opt in the QRMP scheme.
- Quarterly, by the 13th of the month following every quarter of the QRMP scheme, the business has opted.
- GSTR- 3B (for filing summarised information regarding all outward supplies incurred, input tax credit claimed, tax liability ascertained, and taxes filed).
- Monthly, 20th of every month- For the assessee, an aggregate turnover in the former fiscal year exceeds Rs 5 cr or is eligible while still opting out of the QRMP scheme.
- Quarterly, 24th of the month following the quarter- To the assessee with aggregate turnover equivalent to or less than Rs 5 crore, eligible and remain opted into the QRMP scheme.

Quarter ending	Month of deduction	The last date towards the payment of tax deducted	Last date towards filing the TDS return

30th June	April May June	7th May 7th June 7th July	31st July
30th September	July August September	7th August 7th September 7th October	31st October
31st December	October November December	7th November 7th December 7th January	31st January
31st March	January February March	7th February 7th March 30th April	31st May

Additional Compliance

Besides the list of compliance specified above, a section 8 company might need to function additional compliance chores relying on the situation.

- For the case when the company chooses donations or funding via donors, the incomes would be qualified for the tax exemptions. For claiming the same exemptions the company needed to follow the conditions mentioned under section 11 and enrol beneath Sections 80G and 12A.
- Director's approval form (Form DIR 2) to occupy the office within 30 days from the appointment of the director.
- Returns form (Form MR-1) within 60 days from the appointment of a managing director, manager, or another key managerial posting.
- When the company has 20 or exceeding employees, employees would be mandated to be members of the Employees' Provident Fund Organization (EPFO) i.e. company is required to take registration under EPF Act, 1952.

(Mandatory = Employees who draw less than Rs. 15000/- per month.

Optional = Employees if draws more than Rs. 15000 per month with permission of Assistant PF Commissioner).

- Provident fund returns should be furnished through all the entities securing PF registration every month. On the 25th of every month, PF returns would be due. Moreover, a final PF return would be due dated 25th April for the year finished on 31st March.
- For the case when the company secures 10 or more employees and the monthly wage shall not be more than Rs 21,000, the company would be obligated to opt for enrollment under Employee's State Insurance (ESI) Act, 1948.

- ESI returns should require to get filed by the employer on monthly grounds, and the last date would indeed be fixed: The 15th of the subsequent month would be the last date for ESI return filing.

Features of a Section 8 company CA provides for various conditions as well as relaxations for a Section 8 company considering the fact that it has been formed to attain its foundational purpose for and without enrichment of its settlers. Some of these features are discussed below: Relaxation to use the words ‘Limited” or “Private Limited” A company registered under this section is not required to use the word “limited” or “private limited” in its name. Instead, the name ends with words such as foundation, forum, association, federation, chambers, confederation, council, etc. Prohibition to declare dividend Clause (c) of sub-section (1) of section 8 expressly prohibits a company registered under this section from paying any dividends to its members. Profits and other income to be used for the objects for which the company has been formed A limited company registered under section 8 of CA must have in its objects, the promotion of commerce, art, science, sports, education, research, social welfare, religion, charity, protection of environment or any such other object. Moreover, it has to apply its profits or any other income solely in promoting its objects. In B. Ramachandra Adityan vs Educational Trustee Co. (P.) Ltd.; 2003 113 CompCas 334 Mad, the Madras High Court held that where a company formed under section 25 of the Companies Act, 1956 exists solely for getting personal advantage to any party and not in the public interest, the company is liable to be wound up. Restriction on payment of managerial remuneration in certain cases The license issued to a Section 8 company imposes restriction on payment of remuneration or other benefit in money or money’s worth by the company to any of its members except payment of out-of-pocket expenses, reasonable and proper interest on money lent, or reasonable and proper rent on premises let to the company. However, that should not completely restrict the company to pay reasonable remuneration in good faith for any services actually rendered to the company by any person other than its member, unless otherwise stated in the charter documents. Restriction on issue of bonus shares Similar to the prohibition on payment of dividend, the Companies (Incorporation) Rules, 2014 specifically prohibits a Section 8 company to issue bonus shares to its members as the same will tantamount to routing the company’s accumulated earnings back to its shareholders which contradicts the intention with which these companies are set up. Amalgamation with another Section 8 company with similar objectives The profits earned and assets acquired by a Section 8 company throughout its lifetime enjoys various government subsidy and tax exemption benefits. To rule out the possibility of either transferring the said accumulated profits to a non-Section 8 company or passing on the benefit to the shareholders in such company, the Companies (Incorporation) Rules, 2014 provides that a Section 8 company can only amalgamate with another Section 8 company having similar objectives. Section 8 Company as a Defunct Company The term ‘defunct company’ is not defined under the CA, however, to understand its meaning, one needs to take reference from section 248 of the CA which describes the features of a company eligible to be struck off the Register of Companies. It is important to note that there are two ways under section 248 through which the name of such companies can be struck off. The first way is by receiving a notice by the Registrar who has a reason to believe that the company has not commenced its business within one year of its incorporation or has not carried on its business for a period of two preceding financial years. Whereas the other way is when such a company after extinguishing all its liabilities makes an application to the Registrar for removing its name from the Register. It is important to note that the section explicitly prohibits a section 8 company to make an application for removing its name as mentioned under sub-section (2) of the CA. This restriction on a section 8 company makes it evident that its funds cannot be used for meeting its liabilities per se but can only be used for furtherance of its objects. While meeting liabilities arising in the course of business is no doubt an act done for the furtherance of its objects, however, meeting liabilities so as to exhaust the assets and apply for striking off is definitely not an act for meeting the objects of a section 8 company. Section 8 Company as a Dormant Company While the provisions of section 455 cover application by any company registered under the CA to become a dormant company, however, if we look at the meaning of a Section 8 company, we understand that it is made for pursuing a specific object, therefore it may be a uncommon situation for a Section 8 company to apply for a dormant status. Having said since there is no express bar on a Section 8 company to apply for the dormant status, we find that in reality there are section 8 companies which have applied for dormant status and have been admitted so by the Registrar. The Ministry of Corporate Affairs (MCA) has the list of companies which have applied for becoming a dormant company and if we go through the long list, we find that certain companies are in the nature of Section 8 companies since they have the word 'Foundation' etc, in their name without the words 'Limited' or 'Private Limited'

Understanding the fetters on utilization of accumulated profits by a Section 8 company I. Issue of Redeemable Preference Shares The Preference Shares of a company are termed so because they have preference over the equity shareholders in regards to payment of dividends, and return of surplus in the event of winding up. As discussed above, section 8 of the CA prohibits a company registered under this section to pay dividend to its members. Moreover, it also prohibits returning the surplus assets of such a company to its members in the event of winding up. Therefore, the entire reasoning behind issue of redeemable preference shares becomes futlie and therefore, section 8 companies cannot issue such securities. II. Issue of Bonus Shares Rule 22 (4) of the Companies (Incorporation) Rules, 2014 requires a declaration from the Board of directors that no portion of the income or property of the company has been or shall be paid or transferred directly or indirectly by way of dividend or bonus or otherwise to persons who are or have been members of the company or to any one or more of them or to any person claiming through any one or more of them. As we discussed earlier, given the objective principles of a Section 8 company, any profit or gain earned by it is to be used for and in furtherance of its objects. Accordingly, since issuing bonus shares is a means of distributing the profits by capitalizing the same, the issuance of bonus shares to the members of a Section 8 company has been expressly prohibited by the law. III. Buy-back of shares Buy-back of shares by a Section 8 company has not been expressly prohibited under CA. However, buyback is only a mode of releasing the value accumulated in the company to its shareholders. If release of profits by a section 8 company is not allowed, it becomes easy to understand that even a buyback will not be allowed