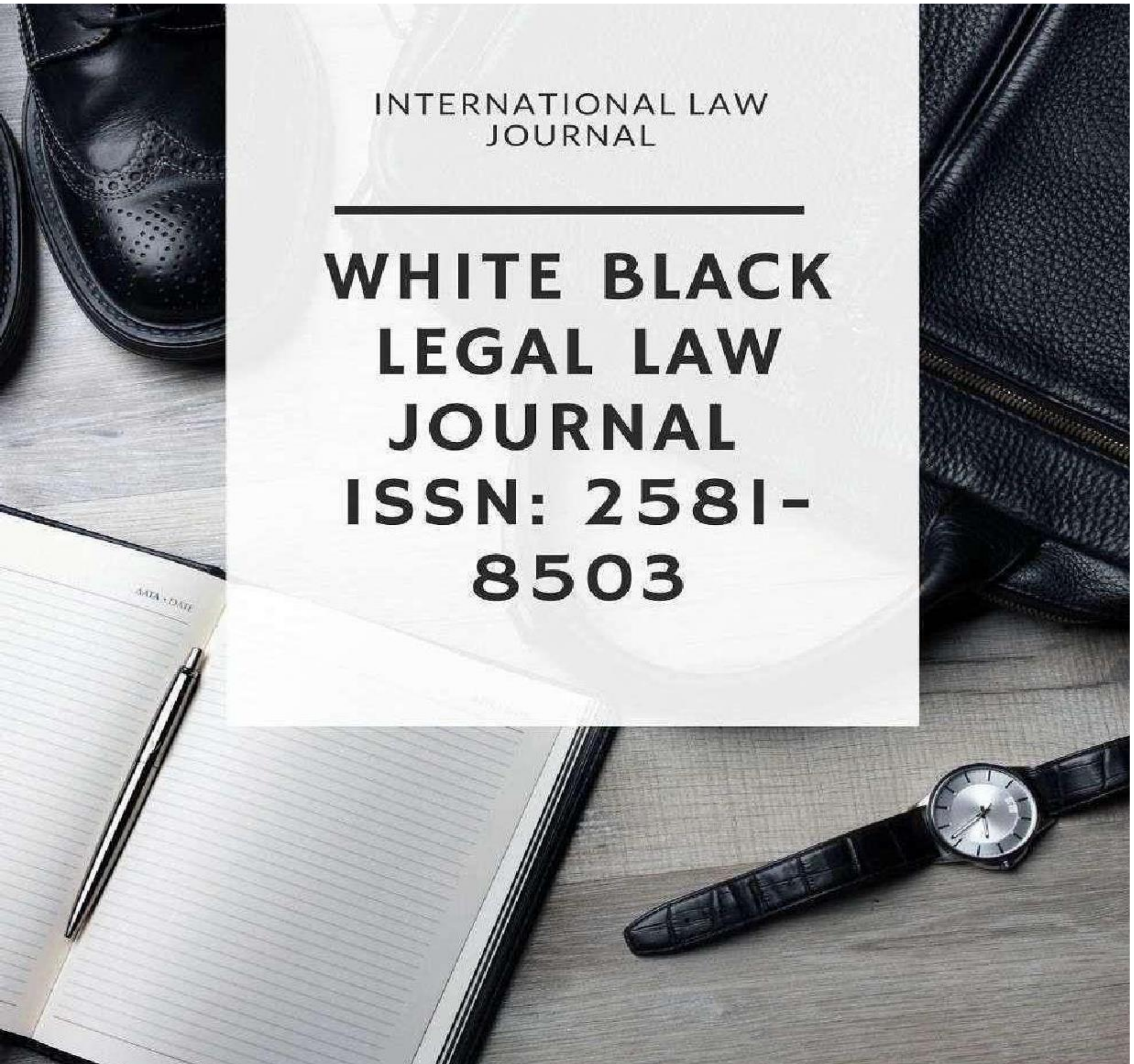

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THE LEGAL FRAMEWORK GOVERNING ONE PERSON COMPANIES (OPCs) IN INDIA

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Abstract

One of the greatest innovation came in the corporate legal framework of India in the Companies Act, 2013, that of the One Person Company (OPC). Until now, company law has been founded on the principle that a company is an association of two or more persons who pool their resources to achieve a common business goal. This traditional concept posed problems for the individual entrepreneur who wanted to enjoy the advantages of corporate personality, limited liability and perpetual succession, but without recruiting additional members simply for the sake of the law. Under the Companies Act, 2013, Entrepreneurship and Ease of doing business is recognized as an important factor and with this consideration, the concept of OPCs (Single Person Company) has been introduced and by it, the entrepreneur can establish and operate the company with limited liability and have a separate legal personality. Since its inception, the legal structure of OPCs has been significantly changed with various amendments and notifications to improve flexibility and foster startups and small businesses. The article critically analyzes the statutory provisions related to the establishment of OPCs in India, their incorporation, management, compliance, conversion, benefits, limitations and recent regulatory changes. The article also discusses the importance of OPCs to the economic development and the promotion of entrepreneurship, and points to the law enforcement difficulties encountered by OPCs. It concludes that OPCs have proved to be a promising legal structure for individual entrepreneurs, but there are some issues that need to be taken up.

Keywords: One Person Company, Companies Act 2013, Corporate Governance, Limited Liability, Entrepreneurship, Company Law, Sole Proprietorship, Corporate Personality.

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Introduction

Corporate law has been evolving in response to the economic realities and to adapt to the various types of business organizations. The company law was traditionally based on the presence of several members who would constitute an incorporated entity. A principle of limited liability was developed in the landmark case of Salomon v. A. Salomon & Co. Ltd.[1] that paved the way for modern company law, but the traditional corporate forms were not always suitable for the needs of the individual entrepreneur who wanted limited liability and corporate status without taking on additional members. The One Person Company (OPC) was introduced under the Companies Act, 2013 (the 'Companies Act') and it introduced a new idea that a company could have only one member.[2] The idea was taken from other jurisdictions where there was a recognition of companies having only one member as a viable form of business structure. The main reason for introducing OPCs was to promote entrepreneurship by giving individual business persons a simplified corporate structure which will afford them legal security and flexibility. With the rise of the startup ecosystem in India and the ease of doing business being a key agenda of the Government, the OPC framework has gained significance in this context. OPCs help bridge the gap between sole traders and private limited companies by allowing the owner(s) to enjoy the advantages of incorporation without giving up any control over business operations.

Historical Development of OPCs in India

Prior to the Companies Act, 2013, under Indian company law, it was not possible to incorporate a company with a single member. Due to the provisions of the Companies Act, 1956, the number of members required for a private company was set at two and for a public company, seven, so entrepreneurs would often add “nominal shareholders” simply to meet the minimum requirements imposed by the law.[3] In 2005, the Expert Committee on Company Law headed by Dr. J. J. Irani had recommended the formation of OPCs to meet the present day needs of business activities.[4] Legislature accepted the recommendation and made it a part of the Companies Act, 2013. The recognition of a One Person Company by the Companies Act, 2013, under Section 2(62) was game changing in Indian Company law and brought Indian Company law in tune with the international developments.

[1] *Salomon v. A. Salomon & Co. Ltd.*, [1897] AC 22 (HL).
[2] Companies Act, No. 18 of 2013, § 3, India Code.
[3] Companies Act, No. 1 of 1956, §§ 12–13, India Code.
[4] Ministry of Corporate Affairs, Report of the Expert Committee on Company Law (J.J. Irani Committee Report) (2005).

Concept and Legal Nature of One Person Companies

An OPC can be likened to a sole proprietorship and a private limited company. As in a sole proprietorship, ownership and management is centralized in one person. The OPC is also a separate legal entity from its member, like other incorporated entities.[5] The principle of separate legal personality is also applicable to the OPCs. This means that the company is able to own real estate, enter contracts, sue and be sued in its own name, and its sole member is only liable to the extent of the money invested in the company. The idea also helps to incorporate the principle of perpetual succession. While only one member is in place at any one time, the law stipulates that another member be nominated and the member be replaced by that other member upon the first member's death or incapacity.[6] This provides continuity of the corporate entity.

Incorporation of an OPC

Any natural person who is citizen of India and is residing in India can incorporate an OPC as per the provisions of the Companies Act, 2013 and the Companies (Incorporation) Rules, 2014. The incorporation process requires that a company reserves its name, obtains a Digital Signature Certificate, a Director Identification Number and prepare Memorandum of Association and Articles of Association before finally submitting the incorporation documents to the Registrar of Companies.[7] A distinctive feature of the incorporation of OPC is the need of a nominee. The nominee needs to provide his written consent and it needs to be filed with the Registrar, as per Section 3(1)(c) of the Companies Act. After a successful registration, the Registrar will issue a Certificate of Incorporation, granting the OPC corporate status.[8]

Management and Governance Structure

OPCs have a different governance structure to a regular private and public company. The number of procedural requirements that are applicable to multi-member companies have been streamlined, because there is only one member. The Companies Act contains a provision that if required, any business to be transacted at a general meeting is deemed to have been transacted if the resolution is signed by the sole member of the company and entered in writing.[9] If an

[5] Id. § 9.
[6] Companies Act, No. 18 of 2013, § 3(1)(c), India Code.
[7] Id.
[8] Id. § 7.
[9] Id. § 122.

OPC has only one director, a number of the board meeting requirements are significantly lessened.[10] These simplifications minimize administration and help to maintain critical governance requirements. Although these relaxations exist, directors still have fiduciary duties and statutory obligations under the Companies Act.[11] Directors have to exercise due care, good faith and promote the company's interests.

Compliance Requirements and Regulatory Obligations

OPCs have a number of exemptions, but are also required to comply with certain obligations. The company has to keep books of accounts, prepare financial statements and fulfill tax obligations.[12] Moreover, OPCs are not required to prepare cash flow statements in their financial statements in general.[13] The audit requirements remain in place, which is to ensure transparency and accountability. Each OPC is required to have a statutory auditor and to perform annual audit(s) of its financial statements. The Ministry of Corporate Affairs (MCA) has introduced various measures to facilitate the compliance of OPCs. These are efforts to achieve a balance between regulatory enforcement and ease of doing business.

Conversion of OPCs

There has been a lot of change in the legal structure for conversion of OPC. Former rules had set conversion thresholds that required mandatory conversions when paid-up capital or turnover reached a certain level.[14] The Companies (Incorporation) Second Amendment Rules, 2021, significantly relaxed the conversion regime, allowing OPCs to voluntarily convert to private or public companies at any time if all the procedures laid out are followed. This reform has improved flexibility and eliminated disincentives to growth. Now, as a result of this, entrepreneurs can expand their businesses without having to alter the structure of their business just because of financial growth.

Advantages of OPCs

Entrepreneurs can reap many benefits from the OPC structure. One of its greatest advantages is limited liability. The system limits risk liability to invested funds and promotes risk taking

[10] Id. § 149.
[11] Id. § 166.
[12] Id. §§ 128–129.
[13] Id. §§ 139–143.
[14] Companies (Incorporation) Rules, 2014, Rule 6 (prior to amendment).

and innovation.[15] Separate legal personality provides the company with the ability to hold assets on its own and contract certainty. The corporate form also helps to build credibility in commercial transactions and to gain better access to institutional financing. The compliance requirements are simplified, thus delivering administrative and operational cost savings. The ability to have full ownership and control is another attraction for solo entrepreneurs who want to maximize their independence in making decisions about their business. When it comes to the continuity of the company despite changes to its only member, the perpetual succession system works. This means that OPCs are more stable than sole proprietorships in terms of organizational structure.

Challenges and Limitations

OPCs have some drawbacks, although they have benefits. The requirement for only natural persons to be the owners of OPCs has narrowed the scope of possible ownership structures.[16] The capital raising process is also likely to be difficult, since shares can only be sold to more than one investor after OPCs have been converted into a different type of corporation. For this reason, the OPC structure might be limited to fast-growing businesses. Some of the compliance expenses of incorporation, auditing and filing could deter micro-enterprises from choosing the OPC model. Besides, banks and investors may view OPCs as less capable than traditional private businesses. Another factor may be that the ownership and management is concentrated in a single person, which can also increase the risk of operations and limit opportunities for collective decision-making.

Recent Regulatory Reforms

The government has made various changes to the OPC framework to enhance the framework. These changes in the Companies (Incorporation) Second Amendment Rules, 2021, broadened the parameters for incorporation and conversion, and also made the process easier.[17] The reforms lifted certain restrictions on paid-up capital and on the turnover threshold and allowed greater flexibility in the field of voluntary conversion. The changes were aimed at fostering start-ups, innovators and small businesses. The reforms follow other government measures to bring the country's business climate into line. The regulatory approach is a sign of the increasing awareness of the contribution of small businesses to economic development.

[15] Companies Act, No. 18 of 2013, § 3, India Code.
[16] Companies (Incorporation) Rules, 2014, Rule 3.
[17] Companies (Incorporation) Second Amendment Rules, 2021.

Comparative Perspective

Single member companies are recognized in many jurisdictions. The United Kingdom also allows single-member private companies to be established under the Companies Act 2006.[18] The European Union (EU) also has a policy to allow member states to provide for single-member companies. The OPC framework in India is similar to these frameworks, but it also has some unique characteristics, like the nomination of nominees. The comparative analysis reveals that India's strategy is designed to strike a balance between flexibilities for entrepreneurs and measures to protect the continuity and accountability of the business.

Conclusion

The enactment of the Companies Act, 2013 and the concept of One Person Companies is a historic achievement in the corporate law of India. OPCs have helped to bridge the gap between sole proprietorships and established corporations by allowing individual entrepreneurs to enjoy the advantages of incorporation, limited liability, and perpetual succession. The legal structure of OPCs shows that the government's goal is to encourage entrepreneurship while at the same time keeping some control over the OPC. Further reforms, notably those of 2021, have improved the attractiveness of the OPC model, from a procedural point of view.The OPC model has received additional procedural improvements, and in particular, has become more attractive since 2021. However, there remain limitations to the usefulness of OPCs in some contexts stemming from issues of capital investment, restrictions on ownership and related compliance costs. With the ongoing evolution of India's entrepreneurial landscape, the structure could be further improved to optimize its utility. Altogether, OPCs are a forward-looking and innovative legal tool, which makes a significant contribution to the economic development, formalisation of the business and entrepreneurial development of India.

[18] Companies Act 2006, c. 46, §§ 7–8 (UK).