



## 4

# COMPANY LAW

*M Ishaque Qureshi\**

### I INTRODUCTION

THE SURVEY reflects the important contributions made by the Supreme Court, High Courts and the Company Law Board (CLB) in company law during the year 2009. It is, however, relevant to note that significant development at the national and international economic environment have taken place since the enactment of the Companies Act, 1956. A need has, therefore, been felt to provide a new legal framework that would respond to the needs of the hour. In order to meet the situation in company law, a revised statutory framework in the form of a “New Companies Bill, 2009” has been submitted to the secretary general, *Lok Sabha* for introduction and consideration by Parliament. In the following pages, an attempt has been made to present judicial pronouncements highlighting briefly their salient features.

### II PROMOTERS

The functions of promoters and their duties and liabilities play an important role in the formation and establishments of a company. The Calcutta High Court in *Kailash Kumar Kanoria v. Shiv Shankar Pasari*,<sup>1</sup> held that the new promoter is liable as per the scheme of rehabilitation to the debt of outgoing promoter and he should implead himself in the banks’ proceedings before the debts recovery tribunal.

### III OFFENCES AND PROSECUTIONS

#### **Liability for non-disclosure of material facts in prospectus**

One of the most important advantages of promoting a public company is that necessary capital for business can be raised from the general public by means of public issue. For the protection of investors, section 63(1) of

\* Professor, National Law Institute University, Bhopal; formerly Chairman and Dean, Faculty of Law, Aligarh Muslim University, Aligarh; Professor, University of Maiduguri, Maiduguri, Borno State (Nigeria), Assistant Professor, International Islamic University, Malaysia, (Selangore, Malaysia).

1 (2009) 147 Comp Cas 231 (Cal).



the Companies Act, 1956 prescribes criminal liability for misstatement in the prospectus, subject to certain exceptions given under sub-section (2).

In *B.B. Bajaj v. State of Maharashtra*,<sup>2</sup> the petitioners contended that they (i) were officers of the state undertaking, (ii) were only nominal directors and (iii) did not participate in the day-do-day management of the accused company and, therefore, they were not responsible for non-disclosure of the material facts. The court considered their plea and held that suppression of material facts in the complaint was substantially against the other accused and not against the petitioners. Therefore, the interim relief as prayed by them was granted. The court, however, directed that the trial in respect to complaint against other accused persons including the company would continue during the pendency of the petition.

**Failure to file annual returns**

In *Union of India v. Suman Distributor*,<sup>3</sup> upon failure to file annual returns, a complaint was lodged against the respondents under section 159 read with section 162 of the Companies Act. The trial judge acquitted the respondents on the ground that (i) the statement of the prosecution witness did not clarify the contents of the complaint and (ii) the ingredients of the offence were not proved. In an appeal against the acquittal, the Rajasthan High Court held that the powers of the High Court, against an order of acquittal, to re-assess evidence and to reach its own conclusion were extensive as in an appeal against an order of conviction. Yet, as a rule of prudence, it should always give proper weightage and consideration to the views of the trial judge as to the credibility of the witnesses, the presumption of innocence in favour of the accused and the rights of the accused to the benefit of any doubt and thus, it should not ordinarily disturb an order of acquittal.

**Failure to file Balance Sheets, etc.**

In *B.N. Kaushik v. Registrar of Companies*,<sup>4</sup> the registrar of companies lodged complaints on failure of the company to file balance sheets, etc. The petitioner was, therefore, convicted, although he had resigned as an honorary secretary of the company. The violations were made for the period after his resignation. In view of this, the court set aside the order of conviction and sentence.

The Madras High Court in *T.G. Krishnamurthy v. Assistant Registrar of Companies*,<sup>5</sup> however, neither considered the plea of period of limitation nor the plea that the company suspended its business after BIFR had passed an order of winding up of the company and, therefore, there was no question of filing the balance sheets and profit and loss account for the

2 (2009) 148 Comp Cas 636 (Bom).

3 (2009) 149 Comp Cas 338 (Raj).

4 (2009) 150 Comp Cas 97 (Del).

5 (2009) 148 Comp Cas 226 (Mad).



concerned period. But, the court dismissed the petition and upheld the punishment for the failure of the company to file with the registrar of the companies copies of balance sheets. *etc.* as required under the Companies Act.

**Failure to file statement of affairs**

The official liquidator can demand a statement of affairs from the officers of the company in liquidation proceedings as mentioned in clauses (a) to (d) of sub-section (2) of section 454 of the Companies Act only by getting orders from the court. However, the Kerala High Court in *K.R. Subramaniam v. Official Liquidator, High Court of Kerala*,<sup>6</sup> was of the view that by mere not filing a statement of affairs of the company as required under the Act, it cannot be deemed that it was not filed without any reasonable excuse.

#### IV COMPANY LAW BOARD

The CLB has wide powers under section 402 of the Companies Act which are without prejudice to the generality of its powers under sections 397 and 398 of the Act. In *Amrik Singh Hayer v. Hayer Estate P. Ltd.*,<sup>7</sup> the petitioner challenged the transfer of possession of the properties of the companies, increase of share holdings, allotment of fresh shares, closure of bank accounts and removal of the petitioner and his son as directors of the company under sections 397 and 398 of the Act. The respondents opposed that petition on several grounds including that the directors were not eligible to file petitions under these sections and the petitioner had no control over the business and had no right to participate in the management of the company. The CLB allowed the petition and observed that though it does not sit in judgment over the commercial wisdom of the share holders as reflected in the memorandum of understanding, it was the non-compliance with the terms of memorandum of understanding which had caused oppression to the shareholders and resulted in prejudice to the interest of the companies whose affairs had been mismanaged by the respondents. It could, with its extraordinary powers under section 402 of the Act, decide and provide reliefs which were just and equitable.

The power to regulate the affairs of the company were also discussed by the CLB in a petition by the central government. In *Union of India v. Satyam Computer Services Ltd.*,<sup>8</sup> the CLB suspended the board of directors of the company and authorized the central government to constitute a fresh board with its nominees.<sup>9</sup> The central government appointed six eminent

6 (2009) 147 Comp Cas 213 (Ker).

7 (2009) 147 Comp Cas 761 (CLB).

8 *Union of India v. Satyam Computer Services Ltd.*, (No.2), (2009) 148 Comp Cas 629 (CLB).

9 See also (2009) 148 Comp Cas 252 (CLB).



persons as directors for the time being. The provident fund authorities threatened to initiate action against these directors. On an application by the company, the CLB held that these authorities had ignored the larger public interest of reviving the troubled company and were to be restrained from initiating any action against them without leave of the board especially in respect of the omission, commission and default on the part of the suspended board of directors.

The power of the CLB was also discussed by CLB in *S.N. Harish v. PODS Biotech P. Ltd.*<sup>10</sup> A question arose whether the CLB could exercise its powers under section 10E(5) of the Act to send the documents to the forensic science department. The CLB held that the board had adequate jurisdiction and powers to enquire into the allegations of mismanagement including allegations of *mala fides* and grant reliefs. Sending documents to the forensic science department was also part of enquiry while dealing with the matters under sections 397 and 398 of the Act.

In *Bhadravathi Balaji Oil Palms Ltd. v. Balaji Oil Industries P. Ltd.*,<sup>11</sup> the powers of the CLB were again examined in a petition for restoration of change in register of charges and investigation into the affairs of a company. Allowing the petition, the CLB held that the manner in which the affairs of the company had been conducted had shaken the confidence of the public in the company. It observed that there was a need to create confidence in the minds of all those connected with the company and also to assure that the regulatory or the judicial mechanism in India was alive and active to take immediate and positive steps.

## V MEMORANDUM OF ASSOCIATION

In *Kawality Ice Creams (India) P. Ltd., In re*,<sup>12</sup> in a petition, the company under section 17 of the Companies Act, sought confirmation of alteration to the situation clause in the memorandum of association for shifting the registered office of the company from one state to another state as approved by the special resolution in accordance with section 189 of the Act. The ex-employees of the company raised objections on the ground that they would be prejudicially affected by such transfer as the court proceedings initiated by them against the company were pending. The CLB held that a special resolution had been passed unanimously by the members of the company at the annual general meeting and the registrar of companies had no objection to the proposed alteration. There was no restraint order from any court against the proposed alteration of situation nor was the board restrained from proceeding with the petition filed under section 17 of the

10 (2009) 148 Comp Cas 804 (CLB).

11 (2009) 148 Comp Cas 9 (CLB).

12 (2009) 148 Comp Cas 631 (CLB).



Act. Having regard to the rights and interests of the members of the company as well as of the creditors, it was held to be just and proper to allow the petition subject to the condition that the interest of none of the employees at the registered office be prejudiced by retrenchment or otherwise.

In *Forbes Finance Ltd., In re.*,<sup>13</sup> the CLB held that a procedural lapse or mere technicalities were not to defeat the legal rights of the company especially when there was a substantial compliance with the requirement of section 18(1)(b) of the Companies Act. Ignoring the procedural lapse, the CLB allowed the application.

## VI MEETINGS

The institution of meeting is very important in the life of a company. However, the right to file an application for directions to convene an annual general meeting of a company would accrue only when there is a default in complying with the provision of section 166 of the Act, which stipulates that not more than 15 months shall elapse between the date of one annual general meeting of a company and that of the next. In *Jogin De Alias Jogindra Nath De v. Eastern India Motion Picture Association*,<sup>14</sup> the order passed by the CLB for conducting of annual general meeting was recalled as the same was not legally valid in terms of section 167 of the Act. In *Asia Stone S.L. v. B&G Impex P. Ltd.*,<sup>15</sup> the CLB was of the view that a single member present in person or by proxy should be deemed to constitute valid quorum for extraordinary meeting.

The Calcutta High Court in *Jaideep Halwasiya v. Rasai Ltd (I)*,<sup>16</sup> held that when no undue hardship or prejudice was caused to the minority shareholders, the court would not sit in judgment over the business decisions approved by the majority shareholders, since the acts complained of were all *intra-vires* the company's authority. When the company was in need of money, further issue was not detrimental to the company. However, the court in an interim order directed the promoters not to exercise any rights in respect of allotted shares pending further order. Subsequently, the applications were dismissed and it was held that there appeared nothing misleading in the explanatory statement and there was no concealment of material fact.

The above decision by a single judge of Calcutta High Court was set aside in *Jaideep Halwasiya v. Rasai Ltd (II)*.<sup>17</sup> Allowing the appeal, the court held that the conduct of the chairman in postponing the poll to the

13 (2009) 149 Comp Cas 16 (CLB).

14 (2009) 148 Comp Cas 15 (CLB).

15 (2009) 149 Comp Cas 269 (CLB).

16 (2009) 150 Comp Cas 269 (Cal).

17 (2009) 150 Comp Cas 20 (Cal).



following day did not meet the test of fairness and reasonableness. Therefore, the *ad-interim* order passed by the single judge directing the promoters not to exercise any right in respect of allotted shares pending further orders was to continue till the disposal of the suit.

## VII LIABILITY OF DIRECTORS

In *Tamil Nadu Electricity Board v. Rasipuram Textile P. Ltd.*,<sup>18</sup> criminal prosecution was lodged against the respondent company, its managing director and other directors for the theft of electrical energy. The trial judge convicted the accused persons holding them responsible for the administration of the company. The additional district and session judge set aside the conviction holding that the prosecution had not alleged that the directors were participating in the day-to-day affairs of the mill. The High Court confirmed the order. On appeal, the Supreme Court held that in a criminal proceeding against the directors of a company, it should have been alleged that the directors were in charge of, and responsible to, the company for the conduct of the business of the company and the records of the investigation must have shown that they were participating in the day-to-day affairs of the mill. The mere fact that the accused persons were the directors would not be sufficient to fasten criminal liability on them.

In *Amit Suresh Bhatnagar v. Income Tax Officer*,<sup>19</sup> the Gujarat High Court held:<sup>20</sup>

[B]efore action under section 179 of the Act, 1961 can be initiated against the director or directors of a private company, the Revenue has to first of all show that such a director or directors were responsible for the conduct of the business during the previous year in relation to which the liability exists.

The condition precedent for the exercise of power by court under section 633 of the Companies Act is that the officer in question is, in fact, in default having failed to perform the statutory obligations which are mandated on him.

The Madras High Court in *S. Pattabhiraman v. Registrar of Companies*,<sup>21</sup> held that in exercise powers under section 633 of the Act, it was not necessary that the continuing offence must come to an end but the officer in question must be in default. When the documents relating to the company were with other directors, the petitioner ought to be excused in

18 (2009) 147 Comp Cas 315 (SC).

19 (2009) 147 Comp Cas 576 (Guj).

20 *Id.* at 578.

21 (2009) 148 Comp Cas 705 (Mad).



respect of the statutory obligations relating to the filing of annual returns and balance sheets. However, where the petitioner and his wife jointly held 50 per cent of shares and no step was taken for the purpose of convening the annual general meeting, the non-availability of the documents did not, in any way, prevent him from approaching the appropriate authority under section 167 of the Act or to convene an extraordinary general meeting by requisition in accordance with section 169 of the Act. In relation to this duty to convene the annual general meeting, the petitioner could not be held to have acted honestly and reasonably to be excused and relieved of his responsibility.

The issue of liability of directors in the event of failure to file statement of affairs was considered by the Gujarat High Court in *O.L. of Jupiter Industries Ltd. v. Mansukhbhai Raghavji Joshi*.<sup>22</sup> The court was of the view that the accused persons who took part in the management of the company despite their resignation before the date of winding up order, were technically not liable to file statement of affairs. However, those who were responsible for not handing over the books of account or those found participating in the conduct of the business of the company even after their resignation would be liable for non-filing of statement of affairs even though they had tendered their resignation before the date of winding up order.

The Delhi High Court, in *Ashok Mittal v. Ram Parshottam Mittal*,<sup>23</sup> while dealing with the matter of injunction to restrain the appointment of director, held that if a *prima facie* case was not made out against a director in respect of his duties in another company, no injunction regarding the appointment may be granted.

## VIII SHARES

### Transfer of shares

The CLB in *Akhil Pandey v. Karvy Consultants Ltd.*<sup>24</sup> considered the case of transfer of shares under sections 113(3) and 111 A of the Companies Act when the petitioner came before it. It held that when forgery was found in the transfer form, the transfer of shares should be treated to be a nullity. The petitioner must produce the material to prove the actual loss suffered while claiming punitive damages against the company for causing mental agony and harassment to the petitioner for seven years and for deliberate negligence of the company which perpetuated forgery and fraud. The company opposed the claim of the petitioner on the grounds that neither the High Court nor the CLB granted any relief towards the bonus

22 (2009) 148 Comp Cas 727 (Guj).

23 (2009) 149 Comp Cas 737 (Del).

24 (2009) 147 Comp Cas 481 (CLB).



shares, unpaid dividend and punitive damages. The CLB, however, directed the company to pay an amount of Rs. 25,000/- by way of damages on the basis of materials produced before it to prove actual loss suffered during the course of non-transferring of shares in favour of the petitioner.

In *Padmavathy Srinivasan v. Maples E & M Technologies P. Ltd.*,<sup>25</sup> the petitioner sold equity share to the respondent. The respondent made part payment against the delivery of share certificate for the entire shares. The entire shares were transferred and duly registered in the name of respondent under section 111(4) of the Act. The petitioner sought rectification of register of members in respect of shares, the payment of which was not made and substituting her name in place of the respondent. The CLB dismissed the petition and held that the transfer of shares in favour of the respondent satisfied the mandatory requirement of section 108(1) and it was applauded by the board of directors of the company. It observed that it could not be said that the name of the respondent had been substituted without sufficient cause so as to invoke section 111(4) of the Companies Act.

#### Rights issue

The Calcutta High Court reiterated the principle in *Hanuman Prasad Baghi v. Bagren Cereals P. Ltd.*<sup>26</sup> that the civil court should not sit in judgment over the commercial wisdom of the corporators. Since the appellants did not show that the decision to issue further shares was *ultra-vires* the powers of the directors under the articles of association of the company, in the absence of any apparent illegality, the propriety of the issue hinged on the collective wisdom of the board against the assertion of the appellants.

#### Reduction of share capital

In the matter of reduction of share capital, the Bombay High Court in *India Value Fund Advisors P. Ltd., In re*<sup>27</sup> demanded certification from qualified auditors/chartered accountants, *etc.* in order to ensure the interest of the creditors and also to facilitate the court in taking an informed decision.

In another case, however, the court held that the report of the auditor should be treated as an aid to the court and not mandatory in every case. Thus, the Bombay High Court in *Tata Realty and Infra Structure Ltd, In re*.<sup>28</sup> allowed the petition and held that sections 78 and 100-105 of the Companies Act did not make a recourse to such a procedure mandatory.<sup>29</sup>

25 (2009) 148 Comp Cas 240 (CLB).

26 (2009) 148 Comp Cas 353 (Cal).

27 (2009) 149 Comp Cas 115 (Bom).

28 (2009) 149 Comp Cas 117 (Bom).

29 *Ibid.*





## IX OPPRESSION AND MISMANAGEMENT

The Companies Act contains special provisions under sections 397, 398 and 402 for prevention of oppression and mismanagement in the affairs of a company. The aim of these provisions is to safeguard the interest of investors and to protect the public interest.

In a matter of oppression and mismanagement, the petitioners appealed to the High Court against an order passed by the CLB in the petition filed under sections 397, 398 and 402. The High Court in *Vijay Kumar Chopra v. Smt. Sudarshan Chopra*,<sup>30</sup> recorded the settlement between the parties. The parties were relegated to the CLB for implementation of the settlement. It gave certain directions for division of assets and properties of the company. Against this order, both parties filed separate appeals before the High Court. The court held that the order passed by it was in the nature of an agreement to divide the assets and properties of the company among the groups and for which the actual division was to be effected by the CLB. The function of the CLB was only to execute the order of the High Court in accordance with the conditions contained in the proposal without altering its terms.

The power of the CLB was acknowledged by the Delhi High Court in *Ajay Kirti Kumar Dalmia v. Company Law Board*<sup>31</sup> in the matter of oppression and mismanagement in exercising its discretion under article 226 of the Constitution. The court observed that in the absence of such illegality, the High Court could invoke its powers to quash decisions of statutory tribunals such as the CLB. The High Court can have recourse where the tribunal was shown to have acted upon beyond the bounds of its powers or acted in manifest illegality.

The Supreme Court considered the issue of oppression and mismanagement in *Girdhar Gopal Gupta v. AAR GEE Board Mills P. Ltd.*<sup>32</sup> The appellants' group filed an application under sections 397 and 398 before the CLB alleging illegal allotment of shares and many other irregularities. The CLB held the allotment partially illegal and partially legal. Both the groups appealed against this order of the CLB. From the facts of the case, the High Court inferred that the appellants group had information about the allotment of shares and, therefore, the court did not interfere with the decision of CLB. The appellant appealed to the Supreme Court which was of the view that the appellants' representing the company before various authorities clearly ruled out the possibility of the appellants being unaware of the situation and the Supreme Court refused to interfere with the decision of the High Court.

30 (2009) 147 Comp Cas 267 (P&H).

31 (2009) 148 Comp Cas 742 (Del).

32 (2009) 149 Comp Cas 119 (SC).



The increase of share capital and the removal and appointment of directors were found to be oppressive by Punjab and Haryana High Court in *Zora Singh v. Amrik Singh Hayer*.<sup>33</sup> The effect of non-service of notice of the meeting to the petitioner was that the decision to appoint additional directors and increase of share capital constituted oppression and mismanagement.

In *Suryakant Gupta v. Rajaram Corn Products (Punjab) Ltd.*,<sup>34</sup> the court held that complete lack of transparency and systematic disposal of assets of the company involving shareholders in the decision making constituted oppression and mismanagement.

The Punjab and Haryana High Court in a petition filed under sections 397 and 398 in *S. Sukhdeep Singh Jhim Ka v. S. Ajit Singh Deogan*,<sup>35</sup> stated that the legal heirs of the deceased shareholders as holders of the shares can maintain a petition under sections 397 and 398. However, there is no duty for issuance of notice to the legal representatives of the deceased shareholders if no action was taken by them to have the share of the deceased shareholders transmitted in their respective names. The court was also of the opinion that by mere increase in shares by additional allotment would not by itself constitute an act of oppression and mismanagement except in a case where the action was *malafide* and reduced the majority of members into minority without adequate opportunity being given to them for taking additional shares.

The Supreme Court in *Ram Bahadur Thakur Ltd v. Manish Mohan Sharma*<sup>36</sup> opined that when the CLB had passed an order on remand by it and the same was confirmed by the High Court, it was in pursuance of the order passed by the High Court and the CLB pursuant to the order passed by the apex court on the earlier appeal, and therefore, no interference was called for.

The petition filed by the appellant under sections 397 and 398, was dismissed by the CLB on the ground that the appellant did not qualify to file the petition under section 399, as he held less than one tenth of the issued share capital.<sup>37</sup>

An appeal under section 10F of the Companies Act was maintainable only on a question of law and not on a question of fact. In *E. Shanmugam v. APS Cam-O- Matec P. Ltd.*,<sup>38</sup> it was also observed that an allegation which was not examined or raised before the CLB cannot be raised before the High Court in an appeal under section 10F of the Act.

33 (2009) 149 Comp Cas 328 (P&H).

34 (2009) 150 Comp Cas 77 (P&H).

35 (2009) 150 Comp Cas 182 (P&H).

36 (2009) 148 Comp Cas 182 (SC).

37 *Ibid.* See also (2007) 140 Comp Cas 300 (CLB).

38 (2009) 148 Comp Cas 701 (Del).



In a petition for winding up, the Bombay High Court considered the power of CLB to implead additional respondents to an application under sections 397 or 398. In *Rani Ram Kiran Agarawal v. Mool Chand Shah*,<sup>39</sup> it is stated that under section 405, if the managing director or manager of a company or any other person had not been impleaded and such person applies to be added as respondent, CLB was empowered to pass an order adding him as respondent, if sufficient cause for doing so, was established to its satisfaction.

## X MISCELLANEOUS MATTERS

### Register of members

The power of the registrar to strike off the company's name after issuing notice under section 560(1) and (2) for failure to file balance sheets and returns was considered by the Patna High Court in *Aakancha Securities Services and Co. P. Ltd. v. Union of India*.<sup>40</sup> In the petition for restoration of the name of the company, the court allowed the petition and stated that notice sent under section 560(2) of the Act was time barred and notice under section 560(3) had been issued and the petitioner had filed the returns electronically with additional fees. In view of the above facts, the *gazette* notification in respect of the company was set aside and the company was directed to be in operation and carrying on its operation since its inception.

In *P.V. Prem Nath v. T.V.S. Motors Co. Ltd.*,<sup>41</sup> the CLB held that a party cannot execute a decree obtained against another under the guise of rectification of register of members since no cause of action arises against the company.

The CLB considered the matter of rectification of register on the loss of share certificate during the course of transit in *Prem Kabra and Co. v. Mangalore Rejimoney and Petrochemical Ltd.*<sup>42</sup> Allowing the petition, it held that as the respondent had not denied the *bona fides* of the petitioner and due procedure for issuance of duplicate certificate had been complied with, the petitioner was entitled to get duplicate share certificate and rectify the register of members. In *Mrs. Sapra Gupta v. Jagran Publication Ltd.*,<sup>43</sup> however, CLB refused rectification on the ground that deletion of name was likely to result in the collapse of substratum of the company.

### Registrar of companies

The role of the registrar in a matter between the company and its director was discussed by CLB in *Mrs. G. Yasodha v. Jai Hanuman*

<sup>39</sup> (2009) 157 Comp Cas 637 (Bom).

<sup>40</sup> (2009) 148 Comp Cas 430 (Patna).

<sup>41</sup> (2009) 148 Comp Cas 774 (CLB).

<sup>42</sup> (2009) 148 Comp Cas 56 (CLB).

<sup>43</sup> (2009) 148 Comp Cas 154 (CLB).



*Barepat Ltd.*<sup>44</sup> under section 614 of the Companies Act. The petitioner sought directions to the respondent company to file form 32 with registrar of companies regarding her resignation as a director with effect from 20.11.2004. The company denied the receipt of legal notice. However, the company accepted that it came to the knowledge of company only on receiving legal notice dated 17.9.2007. The plea of the company was rejected by the CLB. It held 20.11.2004 as the date of resignation and directed the registrar to file form 32 with effect from 20.11.2004 and not from 26.9.2007 when she had not been re-elected as director.

#### Registration of charges

In a matter relating to registration of charges, the Bombay High Court in *Bank of Baroda v. Official Liquidator Finance Ltd.*<sup>45</sup> stated the effect of section 126 of the Act. The court observed that a purchaser was bound to make all reasonable enquiries as to the title of his vendor. Once the title was vested in a company, any prudent purchaser must enquire whether the company had created a mortgage in respect of the property in favour of third party and such mortgage or charge was registered under section 125 of the Companies Act. It added that the effect of section 126 of the Act would operate even on subsequent purchasers.

#### Investigation

Incorporated enterprise is a method of allocating and channeling limited capital resources. A performance that will ensure adequate return on capital is ultimately the best protection to those who provide capital. Hence, the need and importance of investigation cannot be ruled out. The power of investigation is divided into two parts, namely mandatory and permissive.

A division bench of the Madras High Court in *Harish Chand v. C.G. Granites*<sup>46</sup> confirmed the decision of a single judge of the same court in a matter of investigation. The court held that the person complaining, must have had some interest on the day the offending transaction took place. When the appellant purchased the shares of the company knowing that the company had been delisted, as a well informed person from the open market showed that the purchase was meant only to maintain a petition under section 237 of the Act to harass the respondent company, the lack of *bona fide* intention on the part of the appellant disentitled him to seek a ny remedy against the company.

## XI SCHEME OF MERGER AND AMALGAMATION

Is a company entitled to distribute its assets to shareholders under a scheme sanctioned? This issue was discussed in *Nestle India Ltd., In re*<sup>47</sup>

44 (2009) 148 Comp Cas 493 (CLB).

45 (2009) 149 Comp Cas 1 (Bom).

46 (2009) 148 Comp Cas 170 (Mad).

47 (2009) 147 Comp Cas 712 (Del).



by the Delhi High Court. The court noted that the scheme had been approved by the shareholders under various sections of the Act, by an overwhelming majority of the members, and the secured creditors had given their consent. Since no objections were raised by any unsecured creditor despite notice, the scheme was to be sanctioned.

The Bombay High Court in *Delta Distilleries Ltd v. Shaw Wallacne and Co. Ltd.*,<sup>48</sup> in a matter of scheme of amalgamation, considered the issue of devolution of interest of transferor on transferee. The concept of abatement is not attached to a situation where, as a result of a scheme of amalgamation, the transferor company ceased to exist and there was devolution of interest upon the transferee the transferee was entitled to be impleaded in the proceedings.

The Rajasthan High Court in *Modern Syntex Ltd, In re*,<sup>49</sup> acknowledged the board of industrial and financial reconstruction (BIFR) as an expert body to deal with rehabilitation of the sick company. The court held that it cannot interfere if the BIFR had not given any green signal for the revival of the sick unit. It also held that the jurisdiction of the company court in this matter was not appellate, but restricted to that of overseeing that the meetings were properly held and the voting was properly exercised.

In *Modern Denim Ltd, In re*,<sup>50</sup> the court held that a scheme of amalgamation or compromise or merger was a commercial document and once a finding was arrived at that, the legal requirements had been complied with, the company court had no jurisdiction to sit in appeal over the commercial wisdom of the class of persons who had approved the same.<sup>51</sup>

The Karnataka High Court in *Mysore Cements Ltd, In re*,<sup>52</sup> in an application under section 391 of the Act, allowed the applicants to convene a meeting of its equity shareholders to consider a scheme to amalgamate the transferor companies with the applicant and for dispensation of the meeting of the preference shareholders and creditors.

In *Webneuron Services Ltd., In re*<sup>53</sup> the equity shareholders had already given their consent to the proposed scheme. The official liquidator and the regional director had not opposed the scheme. The scheme of amalgamation was, therefore, sanctioned

The Bombay High Court in *Reliance Natural Resources Ltd. v. Reliance Industries Ltd.*,<sup>54</sup> examined the jurisdiction of the company court. It held that the company court had jurisdiction to pass appropriate orders or directions to modify a scheme only in the given facts and circumstances under sections 391 and 394 of the Act.

48 (2009) 148 Comp Cas 809 (Bom).

49 (2009) 148 Comp Cas 843 (Raj).

50 (2009) 148 Comp Cas 873 (Raj).

51 *Modern Denim Ltd., In re* (2009) 148 Comp Cas 884 (Raj).

52 (2009) 149 Comp Cas 50 (Karn).

53 (2009) 149 Comp Cas 61 (Del).

54 (2009) 149 Comp Cas 129 (Bom).



In *Surabhi Chemicals and Investments Ltd., In re*<sup>55</sup> the court sanctioned the scheme of amalgamation when it found that the scheme was in the interest of the companies, their members and creditors. However, where the scheme was found against their interests, the court declined to give its approval.

## XII WINDING UP

Winding up of a company is the process whereby its life is ended and its property is administered for the benefit of its creditors and members. The applicant company was ordered to be wound up by the Punjab and Haryana High Court in *Shivalik Savings and General Investment Ltd v. C.J. Singh*.<sup>56</sup> The official liquidator filed a petition under section 478 of the Companies Act, for public examination of the erstwhile directors. On the examination, the directors were found to have committed various acts of malfeasance, misfeasance and breach of trust and were, therefore, held liable for criminal prosecution under sections 542 (3) and 543(1) of the Act.

During the course of winding up, the protection of interest of all concerned and the protection of property of the company is the main concern of the court. In *Rasik Lal S. Mardia v. OL of Mardia Chemicals Ltd.*,<sup>57</sup> the court applied the principles of natural justice. Although, powers and authority are vested in the official liquidator to represent the company in liquidation, the Act does not debar the promoters, shareholders or guarantors from rendering proper and effective assistance to the official liquidator. Preventing persons from assisting official liquidator would be violative of the principles of natural justice.

The Andhra Pradesh High Court in *Smt. P. Srideni v. Chirishma Housing P. Ltd.*,<sup>58</sup> was of the view that it was only when the other available remedy was not efficacious that the discretionary jurisdiction of the court under section 433(f) can be invoked. However, when there was a complete deadlock in the ownership and management of the company and it appeared incapable of resolution, initiation of winding up proceedings was approved by the court after observing that the winding up was not a happy device for the solution of company's problem.

In *R. Vijay Kumar v. M. Ravindran*,<sup>59</sup> the appellant sought to set aside the sale of land of the company in liquidation which was dismissed. Challenging the order of dismissal, the appellant contended that as the sale deeds were not registered, there was no sale in favour of the company and

55 (2009) 149 Comp Cas 278 (Guj).

56 (2009) 147 Comp Cas 22 (P&H).

57 (2009) 147 Comp Cas 31 (Guj).

58 (2004) 147 Comp Cas 130 (AP).

59 (2009) 147 Comp Cas 223 (Mad).



the third party's property would not be sold in liquidation. The court held that since the order of sale directing the official liquidator to auction the property had not been challenged, the matter could not be re-opened. The appeal was dismissed for suppression of material facts by the original owner.

In *Shraddha Armotics P. Ltd v. Official Liquidator*,<sup>60</sup> the Gujarat High Court considered the interest of secured creditors and the workers in recalling the order of sale of properties of the company, after the sale was confirmed. The court observed that the first consideration was inadequate and the sale in favour of the subsequent higher bidder would fetch maximum price and adequate consideration. However, the sale consideration deposited by the earliest bidder should be returned with interest. The Gujarat High Court in *Sarvariya Exports Ltd. v. Official Liquidator of Urmi Oil Ltd.*,<sup>61</sup> held that a subsequent higher offer would not constitute valid ground for refusing confirmation of sale, once the court comes to the conclusion that the price offered is adequate.

The Madras High Court in *Yehuda Silherberg Ltd v. Premier Poly Weaves P. Ltd*<sup>62</sup> stated that the decree of the court of a non-reciprocal state did not have binding effect. In this case, the petitioner sought winding up of the respondent company on the basis of a decree obtained from a court of Israel and upon failure of the respondent to satisfy its claim after service of notice. The respondent countered the claim and said that Israel was not a reciprocal state and her decree did not have a binding effect of a foreign decree and, therefore, not a "debt." The court held that there was no justification to order winding up as the balance sheets revealed that the company was a going concern.

Under an agreement, the vendor of property to the company was allowed to repurchase under certain circumstances. This contractual right in the nature of pre-emption was sought to be exercised in *Tilagarh Papers Ltd. v. Official Liquidator*.<sup>63</sup> The court held that the right of repurchase could be exercised. The applicant was, therefore, allowed to purchase the property without out-bidding the highest bidder in a sale by auction conducted by the court under the scheme of compromise and arrangement.

The Gujarat High Court in *Ambala G. Doshi v. Bharat Traders*<sup>64</sup> discussed two principles relating to the company in liquidation, namely, (i) if a suit was filed against the company in liquidation, a notice should be given to the official liquidator; and (ii) if the suit was filed after the company had gone in liquidation, the suit would not be maintainable if the

60 (2009) 147 Comp Cas 322 (Guj).

61 (2009) 147 Comp Cas 336 (Guj)

62 (2009) 147 Comp Cas 360 (Mad).

63 (2009) 147 Comp Cas 366 (Cal).

64 (2009) 147 Comp Cas 465 (Guj).



permission of the company court had not been obtained under section 440(2) of the Act.

The Delhi High Court in *ST & Enterprises Ltd. v. Shin Satellite Public Co. Ltd.*<sup>65</sup> directed that the order of winding up, on request, may be vacated in the event of payment to the petitioner/creditor within two weeks from the date of its orders. In appeal, the company sought extension for payment which was opposed by the respondent. The court held that the appellant company was needy and willing to pay the balance amount. However, it clarified that the extension granted would cease to be effective and the order passed by a single judge would be operative with immediate effect no sooner there was a default in making payment as per schedule.

In *Saraf Paper Mills Ltd. (In liquidation), In re*,<sup>66</sup> the Delhi High Court held that it was not sufficient in an auction sale pertaining to the property of the company in liquidation that the price offered by a bidder was the highest in competition with others bidding before the court. It was essential that the highest bid price was commensurate with the prevalent market price. Thus, for the protection of the interest of creditors and contributories of the company in liquidation, the court cancelled the auction sale when it found that the highest bid was below the market price and that there existed several other irregularities in the holding of the auction sale.

The Supreme Court in *Al Champdany Industries Ltd v. Official Liquidator*<sup>67</sup> applied the principle laid down in *Isma Marbals v. Bihar State Electricity Board*.<sup>68</sup> When the company went into liquidation, it had already given due publicity. But the respondent municipality did not file its claim before the official liquidator. The municipality was, therefore, an unsecured creditor and could not stand on a higher footing than an ordinary unsecured creditor for the purpose of realization of dues from the sale proceeds.

In *DCM Dae Wood Motors Ltd. v. Official Liquidator*,<sup>69</sup> the Bombay High Court observed that in case of a hire purchase, the title to the plant and machinery had not passed in to the company and continued to remain with the financier (the bank). Therefore, the application filed by the commissioner of central excise was not sustainable. The official liquidator had to deal with the claim and pass orders.

In *India Capacitors Ltd. Employees Union v. Official Liquidator*,<sup>70</sup> after the sale of assets by auction and its confirmation in a winding up process, the court dismissed the appeal and observed that if such a process

<sup>65</sup> (2009) 148 Comp Cas 210 (Del).

<sup>66</sup> (2009) 14 Comp Cas 381 (Del).

<sup>67</sup> (2009) 148 Comp Cas 641 (SC).

<sup>68</sup> (1995) 2 SCC 648.

<sup>69</sup> (2009) 148 Comp Cas 665 (Bom).

<sup>70</sup> (2009) 148 Comp Cas 768 (Del).





was allowed, there could never be any end to a transaction of this nature. The clock could never be setback.

In *Bhagudeo Flour Mills P. Ltd. v. O.L. of Disha Agro Industries Ltd.*,<sup>71</sup> it was held that in the proceedings of winding up in order to set aside a transaction under section 531 of the Act, fraud must be clearly alleged, proved and established. Mere general allegations, using statutory words or language but lacking material particulars, would not suffice.

The Madhya Pradesh High Court in *Laxmichand Daya Bhavi Exports Co. v. Prestige Foods Ltd.*<sup>72</sup> stated that it was the duty rather than legal obligation of the BIFR to ensure expeditious disposal of the reference (registered one way or the other at an early date) so that both the creditors and the company should know their fate to recover the outstanding dues in accordance with law in the event of winding up of the company.

It has rightly been observed in *Ratna Commercial Enterprises P. Ltd v. Vasu Tech. Ltd.*<sup>73</sup> that winding up was not a mode of recovery of debt or amount payable by the company. It was the discretion of the court to order winding up which should be the last resort.

71 (2009) 148 Comp Cas 828 (Guj).

72 (2009) 149 Comp Cas 235 (MP).

73 (2009) 149 Comp Cas 477 (P&H).

