The Indian Law Institute

5

COMPANY LAW

*Arya A Kumar**

1 INTRODUCTION

IN THE year 2010, the Supreme Court and various High Courts delivered many significant judgments covering important points in the arena of company law. Only selected important landmark cases, deviating from earlier views, have been discussed in this survey. The proposal for the establishment of the National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal (NCLAT) to look into various matters pertaining to companies had been a matter of controversy in *Union of India* v. *R. Gandhi, President, Madras Bar Association.*[1] In this case, decided by the constitution bench, the Supreme Court addressed important issues pertaining not only to company law but also to constitutional law.

II ESTABLISHMENT OF NCT & NCLAT

The creation of NCLT and NCLAT and vesting in them the powers and jurisdiction exercised by the High Courts in regard to company law matters was challenged in *Union of India* v. *R. Gandhi, President, Madras Bar Association* wherein the court held that the creation of such quasi-judicial bodies was constitutional. In this case, the constitutionality of the Companies (Second Amendment) Act, 2002 was challenged in the Madras High Court[2] on various grounds in which the court held that the establishment of NCLT and NCLAT and vesting in them the powers hitherto exercised by the High Courts and the Company Law Board (CLB) was not unconstitutional. The court also ruled that various provisions of parts 1B and 1C of the Act suffered from constitutional infirmities, which had to be sufficiently amended, to establish the NCLT and NCLAT. Considering the constitutional issues involved, the Supreme Court referred the matter to a constitution bench. The apex court had to resolve the following issues:

i) Whether the Parliament had the legislative competence to vest in any tribunal all the intrinsic judicial functions that were being performed by the High Courts.

* Assistant Research Professor, The Indian Law Institute, New Delhi, India.

1 [2010] 100 SCL 142.

2 2010 (3) CTC 517.

The Indian Law Institute

ii) Whether the creation and transfer of the entire company jurisdiction of the High Courts to the tribunals was violative of the doctrine of separation of powers and independence of the judiciary, particularly having regard to the proposed qualifications for the membership of the NCLT.

The court upheld the legislative competence of the Parliament to create the NCLT as this power could be exercised in respect of all matters in list I of the seventh schedule; articles 323-A and 323-B of the Constitution of India were not limiting provisions and the subject matters specifically listed in those articles were not exhaustive. Though the court upheld the competence of Parliament to establish NCLT, it did not uphold the actual establishment of the NCLT itself and directed the Parliament to modify the present law for the effective functioning of the tribunal. The court indicated certain qualifications for the members to be appointed and adhered to the principle that once competence was established, there could be no further test. The court observed:[3]

> If the Tribunals are intended to serve an area which requires specialized knowledge or expertise, no doubt there can be Technical Members in addition to Judicial Members. Where however jurisdiction to try certain category of cases are transferred from Courts to Tribunals only to expedite the hearing and disposal or relieve from the rigours of the Evidence Act and procedural laws, there is obviously no need to have any non-judicial Technical Member. In respect of such Tribunals, only members of the Judiciary should be the Presiding Officers/members of such Tribunals… Therefore, when transferring the jurisdiction exercised by Courts to Tribunals, which does not involve any specialized knowledge or expertise in any field and expediting the disposal and relaxing the procedure is the only object, a provision for technical members in addition to or in substitution of judicial members would clearly be a case of dilution of and encroachment upon the independence of the Judiciary and Rule of Law and would be unconstitutional.

While dealing with the issue of the qualification and appointment of members of the tribunals, the court laid down the following principles:

i) Only judges and advocates can be considered for appointment as judicial members. Furthermore, only the High Court's judges, or judges who have served in the rank of a district judge for at least five years, or a lawyer who has practised for at least ten years, can be considered for appointment as a judicial member.

3 *Id.*, para.35.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

ii) Persons who have held a group A or equivalent post under central or state governments with experience in the services such as the Indian company law service (legal branch) and Indian legal service (grade-1) cannot be considered for appointment as judicial members. Their expertise in these services can at best mean that they can be considered for appointment as technical members. In sum, a judicial member is like a High Court judge.

iii) Only officers holding the rank of secretary/additional secretary can be considered for appointment as technical members. A 'technical member' presupposes experience in the specific field to which the tribunal relates. A member of Indian company law service who has worked with accounts branch of that service, or officers in other departments who might have incidentally dealt with some aspect of company law, cannot be considered as 'expert' and cannot be considered as being qualified for appointment as a technical member.

iv) The selection committee must be headed by the Chief Justice of India or his nominee, who shall also have the casting vote. Besides, there is to be a senior judge of the High Court or the Supreme Court. The other two members can be the secretaries of some government department (such as finance & company affairs, and law & justice).

v) The term of office of three years shall be changed to a term of seven or five years subject to eligibility for appointment for one more term. This is because considerable time is required to achieve expertise in the concerned field. A term of three years is very short and by the time the members achieve the required knowledge, expertise and efficiency one term will be over. Further, the 'said term of three years with the retirement age of 65 years is perceived as having been tailor-made for persons who have retired or shortly to retire and encourages these tribunals to be treated as post-retirement havens. If these tribunals are to function effectively and efficiently they should be able to attract younger members who will have a reasonable period of service…'

vi) Two-member benches must have a judicial member. Whenever any larger bench or any special bench is constituted, the number of technical members cannot exceed the judicial members.

It was also clarified that the tribunal was an alternate judicial forum and requires least interference of the executive in its functioning. In this landmark judgment, the court upheld the legislative competence of the Parliament to set up the NCLT and directed the Parliament to modify the law relating to appointment of members to the tribunal. Company law matters are considered to be technical in nature and require expert knowledge to resolve it. Although the court gave green signal for the establishment of tribunals for handling

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

company law matters, the actual functioning of the tribunal would depend on the proposed amendments in the Act.

III MERGER

The Calcutta High Court in K. *Agri Genetics Ltd.* v.*Florence Alumina Ltd.*[4] dealt with the issue of merger. In this case, a scheme of arrangement and demerger (scheme) between JK Agri Genetics Ltd and Florence Alumina Ltd. had been filed in the Calcutta High Court for sanction pursuant to sections 391-394 of the Companies Act, 1956. The scheme was approved by the requisite majority of the equity shareholders of the two companies at their respective meetings held at Calcutta. An application was filed by the shareholder who had objected the sanction of a scheme of arrangement by demerger as it was unfair. Rejecting the application for sanction of scheme of arrangement and demerger, the court held that the procedure prescribed under sections 81(1A) and 391 of the Companies Act, 1956 ought to be followed for the conversion resulting in issuance of further shares to promoters and benefiting such class of shareholders.

The Madras High Court in *G.V. Films Ltd.* v. *Metage Special Emerging Market Fund Ltd*.[5] dealt with the question of the need for the consent of the bondholders in a scheme of arrangement, between the two companies for the demerger and to create two more companies. In this case, the petitioner company, G.V. Films Limited, proposed the demerger to form the offspring companies known as G.V. Studio City Limited and G.V. New Media Technologies Limited. The scheme of arrangement proposed by the appellant company was not sanctioned by the single judge as it was prejudicial to the interest of the shareholders.[6] The court held that the liability to pay either in the form of shares at the option of the bondholders or to repay the amount on maturity would be only on the company and, if the liability was transferred, it ought to have been done with the consent of the shareholders and creditors. The court observed:[7]

> On a overall consideration of the facts and circumstances of the case, for ascertaining the real purpose of the scheme, by piercing the veil of apparent corporate purpose underlying the scheme and also by scrutinizing the same judiciously in the light of the dictum laid down by the Hon'ble apex court, we are of the view that the approval sought for by the petitioner company for the demerger with its two offspring companies is prejudicial to the respondents 1 to 4 and the said scheme of arrangement is also violative of the provisions of Section 391 of the Companies Act, Sections 100 to 104 of the Act and

4 (2010) 157 Comp Cas 200 (Cal.).
5 (2010) 154 Comp Cas 252 (Mad.).
6 *G.V.Films Ltd., In re* [2009] 150 Comp Cas 415 (Mad.).
7 *Id*., para. 48.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

> Section 62 of the Indian Contract Act. Therefore, the rejection of approval of the scheme of arrangement by the learned Single Judge is in order, and we are unable to see anything to disturb the finding of the learned Single Judge.

In *Alchemist Ltd and Alchemist Foods Ltd., In re*,[8] a scheme related to demerger was challenged on the ground that incorporation of the resultant company after the appointed date could be a reason for rejecting sanction of the scheme. The court held that the appointed date was only to identify and the value of assets to be transferred to the resultant company and date was immaterial as the scheme would be effective only on the effective date.

IV MEMORANDUM OF UNDERSTANDING (MOU)

In *Reliance Natural Resources Ltd*. v. *Reliance Industries Ltd*.,[9] the main issue was related to the validity of the MoU entered into between the Ambani brothers, which were in the nature of a family arrangement between Chairman-cum-MD and the disputant. The court held that the MoU was not binding on Reliance Industries since it was entered into in a private capacity, and the Government of India pricing for gas would be binding as gas was a national asset owned by the government and ordered the parties to come with a new agreement within fourteen weeks. In this case, both the companies were supplying natural gas from the Krishna-Godavari basin, Bay of Bengal and took separate ownership of the companies following a demerger after the death of their father. A dispute arose between RIL and RNRL following the decision of the government to allow limited private sector participation in gas exploration. The MoU gave RNRL a specified entitlement of oil and gas at the price at which RIL had agreed to supply gas to NTPC. RNRL filed an application in the Bombay High Court praying the court to direct RIL to supply gas at the price agreed in the MoU. The single judge, having rejected jurisdictional objections, agreed with RNRL that the GSPA was in breach of the scheme, and directed the parties to comply with the "suitable arrangement" requirement in the scheme, in light of the MoU. Both parties appealed to the division bench, which held that the "suitable arrangement" in the scheme had to be formulated in light of the MoU.

Before the Supreme Court, the substantive part of the case turned on the main issue: Whether the MoU entered into between Ambani brothers was binding on the respective companies. The majority held that the MoU could not bind the companies because it was entered into by private persons in a private capacity and the doctrine of identification did not apply to large companies with millions of shareholders. The court held:[10]

8 (2010) 160 Comp Cas 469 (Del.).
9 (2010) 156 Comp Cas 455.
10 *Id*., para. 163.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

> [B]oth the learned Single Judge and the Division Bench committed a serious error in exercising jurisdiction in the manner they did under Section 392 of the Companies Act, 1956, for such interference has resulted in the provisions of a document (MoU) which was not before the shareholders supersede the Scheme of Arrangement. Such a document could not have been read into and incorporated in the Scheme propounded by the Board, approved by the shareholders and sanctioned by the Company Court; (ii) the courts below having rightly directed the parties to negotiate, and further having rightly refused to grant the prayers in the Company Application, however, fell into error directing the MoU to be binding and the basis for further negotiations between the parties. MoU is a private pact between the members of Ambani family which is not binding on RIL.

V SCHEME OF ARRANGEMENT OF A COMPANY

The Gujarat High Court in *Rajeev S. Mardia, In re*[11] dealt with the question of discharging the liabilities to statutory creditors in liquidation of the companies. In this case, the petitioners challenged the scheme introduced for transferring the assets of a company in favour of some relatives. The ex-promoters of the company in liquidation in order to revive the company sought sanction of the court for a composite scheme of arrangement in the nature of compromise with its creditors and reconstruction of its share capital as well as the transfer of assets and liabilities to its wholly-owned subsidiaries. The scheme was approved by requisite majority of creditors and equity shareholders. However, objection was raised by the official liquidator and the regional director that the scheme did not contain any provision for settlement or payment of statutory professional claims of government. Even the claims of workers and employees were yet to be invited by official liquidator and the provisions of the scheme would not bind ex-workers and employees in respect of their claims, the scheme appeared to be a ploy to dispose of the properties of the company in liquidation. In fact, the scheme was introduced for the sole purpose of transferring the assets only and not for the discharge of liabilities of the statutory creditors. Dismissing the petition, and rejecting the scheme, the court held that since the scheme did not contain any provisions for the re-employment of the workers in the company in liquidation and it was merely to transfer the assets of the company to some interested parties, the scheme cannot be accepted.

In *Thermopack Industries* v. *Ajay Electrical Industries Ltd.*,[12] the question related to a scheme for the revival of the company proposed by the ex-directors of the company in liquidation. By permitting the scheme, the court

11 (2010) 153 Comp Cas 306 (Guj).
12 (2010) 153 Comp Cas 470 (Del.).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

held that the scheme was for the entire revival of the company since it safeguards the interest of the workers and the payment of all dues of the company. In *Sasken Communication Technologies Ltd., In re*,[13] the petitioner company sought the sanction for a scheme of arrangement in which it was proposed to create developmental plans for the improvement of its business. Reiterating its earlier decisions, the court held that the scheme was not in violation of the accounting standards and not against the interest of the shareholders.

VI POWERS OF THE OFFICIAL LIQUIDATOR

Section 456 of the Companies Act deals with the powers and duties of the official liquidator in the case of winding up of a company. As per this section, an official liquidator is required to take into his custody all the properties of the company in winding up.

In *TCI Distribution Centers Ltd*. v. *Official Liquidator, High Court of Madras*,[14] the court set aside a sale confirmed in favour of the appellant and ordered the official liquidator to return the sale consideration to the appellant. In this case, the property of the company in liquidation was sold in an auction to the appellant who paid the entire amount of transaction. The auction-purchaser later found out that the properties were not exactly the same as described in the sale advertisement. The appellant filed a petition contending that the properties were found to be mis-described by the official liquidator. The court set aside the sale in exercise of its powers conferred under rule 9 of the Companies (Court) Rules, 1959. In this judgment, the court clarified that the role of an official liquidator was limited; he was like a 'trustee' of the property and the property remains with the company. By reiterating the judicial precedents, the court explained the liabilities of an official liquidator in case of deceit, negligence or mis-management made out with regard to sale of property.

VII OPPRESSION AND MISMANAGEMENT

The provisions of the Companies Act, 1956 dealing with the issue of providing relief to the minority shareholders against the acts of oppression and mismanagement in the company by the majority shareholders has been subjected to judicial interpretation in a number of cases. In many cases, the constitutional courts have clarified the principles that have to be followed in interpreting these statutory provisions.

In *Incable Net (Andhra) Limited* v. *AP Akash Broadband Ltd.*,[15] the Supreme Court held that no act of oppression or mismanagement within the meaning of sections 397, 398, 402 and 403 of the Companies Act had been made

13 (2010) 155 Comp Cas 463.
14 (2010) 153 Comp Cas 437.
15 (2010) 3 Comp LJ 1 (SC).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

out by the petitioners against the majority shareholders of the respondent company. The petitioners had contended that the respondents had, in this case, by a series of acts, mismanaged the affairs of the company and rendered the petitioners completely ineffective in spite of their investment, thereby attracting the provisions of sections 402 and 403 of the Act. The CLB and the High Court dismissed the petition whereupon the petitioners appealed to the Supreme Court. The court observed that the respondent company had committed a breach of contract in regard to supply of materials to the respondent company and such lapse would not constitute the ingredients of a complaint under sections 397, 398, 402 and 403 of the Act. By applying the decision in *V.S. Krishnan*,[16] the court observed:[17]

> [T]he expression "oppression" within the meaning of the Sections 398, 399 and 402 of the Companies Act had been interpreted to mean that the conduct of the majority shareholders towards the minority shareholders was harsh, burdensome and wrong and that such conduct was *mala fide* and was for a collateral purpose which would result in an advantage for some shareholders over others, although, the ultimate object might be in the interest of the Company. However, the facts disclosed in this case do not establish such conduct on the part of the Respondent. Until the conduct of the majority shareholders was found to be oppressive in terms of the above description, under Sections 397 and 398 of the Companies Act, 1956, the Company Law Board was not competent to invoke its jurisdiction under Section 402 of the said Act to set right, or put an end to such oppression.

In *S. Peer Mohamed* v. *S. M. Mohideen Ahmed Shaw*,[18] the applicant, the managing director of the company, filed a petition before the CLB alleging oppression and mismanagement under sections 399, 402 and 403 of the Act. The CLB held that the respondent had failed to produce any share certificate to prove his holdings in the company and there was no dispute regarding the genuineness of the annual return produced by the applicant who disclosed that the first respondent held less than 10 per cent of the paid-up capital of the company. Therefore, the burden of proof regarding the shareholding of the respondent fulfilling the minimum requirement as stipulated in section 399 of the Act had not been duly discharged by him. The court held that a person holding less than 10 per cent of the share capital of the company had no *locus standi* to file the petition under sections 397 and 398 of the Act.

16 *V.S. Krishnan* v. *Westfort Hi-Tech Hospital Ltd.* (2008) 3 SCC 363.
17 *Id*., para. 39.
18 (2010) 153 Comp Cas 24.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

VIII WINDING UP OF COMPANIES

Under section 433 of the Companies Act, it is the discretion of the court to pass an order to wind up a company in the circumstances mentioned in the section. Although power of the court to order for the winding up of the company is discretionary, it has to take into consideration "public interest" involved in such cases. In *HMT Ltd*. v. *N.T.Ramatulla Khan and Associates*,[19] a petition seeking winding up of a public sector undertaking was admitted by the single judge and publication was ordered. The company filed an appeal and contended that the court had passed the order without giving proper and adequate opportunity of hearing to it. The division bench held that the mere possibility of the fiction being employed to deem that the company was unable to pay its debt could not *ipso facto* lead to the inference that the company could not be ordered to be wound up. By allowing the appeal, the court remanded back the matter to the single judge directing the parties to present their versions before the court. In this case, the following observation made by the court is noteworthy:[20]

> It is the discretion of the court to pass an order to wind up a company in the mentioned in section 433 of the Companies Act, 1956. While the circumstances stipulated in any of the clauses of section 433 of the Act are present, still it is in the discretion of the court to pass an order to wind up a company. It is for the court to bestow its attention to protect public interest. Public interest was involved, as the company was a public sector undertaking with the government holding 99% of its shares. It was a matter of public concern as to whether such a company was to exist or was to be wound up irrespective of the ability of the company to pay its debts. The order of winding up passed without considering all aspects was vitiated and was to be set aside. Therefore the appellant company was to be given adequate opportunity to put up its defense before the petition for winding up was examined.

In *ICICI Bank Ltd.* v. *Saura Chemicals Ltd.*,[21] the court held that default in furnishing of specified information was purely a question of fact and winding up of such petitions could be resolved only by a civil court. In this case, as per the agreement between the petitioner and respondent company, the petitioner company lent large sums of money for the purpose of transacting derivatives. Later on, the petitioner company filed a petition for winding up as the respondent company had failed to make the outstanding payments.

19 (2010) 155 Comp Cas 169 (Kar.).
20 *Id*., para.13.
21 (2010) 153 Comp Cas 429 (P & H).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

In another case,[22] the petitioner filed a winding up petition when the respondent company failed to settle the debts, which had been given by the petitioner bank. The respondent company put forward the defense that the borrowing itself was without any authority and could not bind the company and that before the statutory notice, the petitioner bank had filed a suit before the High Court regarding the transactions referred in the statutory period. Allowing the petition, the court held that the defense of the company was not bona fide. The court further clarified that merely because the company had filed a suit before the statutory notice was issued, it did not make the dispute a *bonafide* one. The respondent company was directed to repay the debt upon failure of which the petition would be admitted.

In *E-City Media Pvt Ltd.* v. *Sadhrta Retail Ltd.*,[23] the petitioner filed a petition seeking an order for winding up of the respondent company for its failure to pay debt due. The court held that a claim could be transformed into a debt only through proper adjudication in a civil court and prior to that it will only be a claim for damages. Dismissing the petition, the Bombay High Court held that only through court proceedings and analysis of the evidential matters a claim can be transformed into a debt. In *Sound Fibre* v. *B.K.Duplex Ltd.*,[24] the petitioner filed a winding up petition through an agent on the ground of inability of the respondent company to pay the debt for the value of goods supplied to it. The court ordered winding up of the company holding that the profits shown in the balance sheet of a company was not sufficient proof of viability of the company to pay the debts. The question whether the power of attorney can file a winding up petition on behalf of the creditor was answered by the court affirmatively.

In *IBA Health (I) (P) Ltd*. v. *Info-Drive Systems Sdn.Bhd*,[25] the issue related to the winding up of a company on the ground of inability to pay debts. In this case, the respondent filed a petition for winding up of the company alleging that the appellant company had failed to discharge its liability to pay under the deed of settlement between them. The High Court ordered the publication of advertisement in the newspaper for the amicable settlement of the dispute between the parties. The court held that in order to invoke section 433(e) & (f), where there was a bonafide dispute as to liability on substantial grounds, petition for winding up shall not be entertained. In such circumstances, the party seeking winding up cannot be regarded as creditor of the company for the purpose of winding up and the court should act with circumspection in order to examine whether winding up petition was used as a ploy to pressurize company to pay substantially disputed debt. By setting aside the High Court's direction, the court held that the winding up petition implied insolvency and was likely to damage company's creditworthiness or

22 *ICICI Bank Ltd.* v. *Saura Chemicals Ltd*. (2010) 153 Comp Cas 424 (Bom.).
23 (2010) 153 Comp Cas 326.
24 (2010) 155 Comp Cas 308 (P & H).
25 (2010) 159 Comp Cas 369.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

its financial standing. The court further clarified that where dispute required investigation of facts and evidence and interpretation of the terms and conditions of agreement between parties, the court shall not proceed with winding up proceedings. The court held that in the present case, there was a bonfide dispute as to appellant's liability towards the respondent. The court observed:[26]

> If the debt is bonafide disputed, there cannot be "neglect to pay" within the meaning of section 433(1)(a) of the Companies Act, 1956. If there is no neglect, the deeming provision does not come into play and the winding up on the ground that the company is unable to pay its debts is not substantiated ad the non-payment of the amount of such a bonafide disputed debt cannot be termed as "neglect to pay" so as to incur the liability under section 433(e) read with section 434(1)(a) of the Companies act, 1956.

In *Sampat Trading and Co*. v. *Talayar Tea Co.Ltd.*,[27] the petitioner filed a winding up petition based on the ground that the respondent had to pay Rs.100 lacs to the petitioner. The petitioner further contended that the winding up petition was based on the information by the managing director that a sum of Rs.100 lacs was due to the petitioner and the respondent had paid Rs. 69 lacs out of it. The respondent company stated that there was no debt due to the petitioner, instead the petitioner owed Rs.37 lacs as per the statement of accounts of the company. The respondent had established by materials that there was a bonafide dispute about the debt and its defense was substantial in nature. The court held that the winding up order would cause unnecessary hardship and stigma to the respondent-company.

Similarly, in *TRS Forms and Services P. Ltd*. v. *Eduquity Technologies P.Ltd*.,[28] the court held that the machinery of winding up was to be allowed merely as a means for realizing debts due from a company. In the present case, the petitioner filed a petition under sections 433(e), (f) and 434 of the Companies Act for the winding up of the respondent-company which had failed to make payment despite performance of the contract by the petitioner. The respondent company defended contending that there were several defects in the works carried out by the petitioner on which the respondent company was not satisfied. The court held that the claim of the petitioner company that the respondent was insolvent to pay the debts was not supported with evidence and dismissed the petition.

In *Priyaraj Electronics Ltd*. v. *Motorola India P. Ltd.*,[29] the petitioner rendered some services to the company for which the company had paid the

26 *Id*., para. 23.
27 (2010) 153 Comp Cas 64 (Mad.).
28 (2010) 153 Comp Cas 321 (Kar.).
29 (2010) 153 Comp Cas 88 (P & H).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

due amount withholding part of the amount. The pertinent issue was whether the due amount becomes debt when part of the payment had been withheld. The petitioner filed a petition for winding up of the company due to the non-payment of the part amount. Dismissing the winding up petition, the court held that the petitioner was entitled only to get the balance amount when the company receives this amount from the third party, which had also been mentioned in the agreement. In *Kiptly Industries Ltd.* v. *California Pacific Trading Corporation*,[30] the appellant company was ordered to be wound up in a petition filed by the respondent on the basis of a decree obtained from a foreign court. The single judge refused to examine the legality of the foreign court's decree wherein the court had held that the single judge erred in not examining the foreign decree in due course of law. The matter was remitted back to the single judge for adjudication of the issue in accordance with law. In *R.P. Television(India) P. Ltd*. v. *Official Liquidator*,[31] a private financier filed two applications for permission to run the company by the employees under his guidance and for the sale of assets of the company in his favour. The single judge rejected both the applications on the ground that the private financier's interest in the company was susceptible and had to be investigated. An application for winding up a company was rejected in *Infrastructure Leasing and Financial Services Ltd.* v. *S.A.B. Industries*[32] as the appellant had effective alternative remedies like resorting to civil suit or arbitration clause rather than winding up of the company. In this case, the appellant was claiming a speculative amount on the basis of an agreement which could not be determined in summary proceedings. In a similar vein, the court held:[33]

> [I]t is held that no case for Company invoking the discretionary winding up provision against the respondent-Company is made out under the present set of circumstances, particularly, when the appellant-Company has effective alternative remedies to settle their dispute by way of arbitration or through the civil court. It is in this manner that the learned Company Judge has decided the matter and relegated the parties to the remedy of civil suit. Therefore, no ground for interference in the impugned judgment of the learned Company Judge is made out in the obtaining circumstances of the case. No other point, worth consideration, has either been urged or pressed by the learned counsel for the parties.

In *European Metal Recycling Ltd.* v. *Blue Engineering P. Ltd*.,[34] the court analyzed the scope of sections 433 and 434 of the Companies Act which deal with grounds for winding up of a company. In this case, the petitioner

30 (2010) 153 Comp Cas 345 (Gau.).
31 (2010) 155 Comp Cas 488.
32 (2010) 155 Comp Cas 159.
33 *Id*., para.11.
34 (2010) 154 Comp Cas 35.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

entered into various cost and freight contracts with the respondent company for sale and purchase of non-ferrous scrap. The petitioner purchased the contracted goods for the respondent and shipped them to India, but on arrival of the goods in India, the respondent failed to take possession and make payment. The main issue was whether the difference between the contracted price and the resale price of goods could be treated as a debt to initiate winding up proceedings against the defaulter company. Dismissing the petition for winding up, the court held that the amount claimed by the petitioner might be disputed, and thus did not amount to a 'debt' for the purposes of winding up proceedings. In *Tezpore Tea Co.Ltd.* v. *Bijoynagar Tea Co. Ltd.*,[35] the Calcutta High Court reiterated that no winding up shall be permissible if the debt alleged to be due was disputed one and the winding up was the extreme remedy which had to be resorted sparingly.

IX AMALGAMATION

The provisions relating to amalgamation is contained in sections 396A of the Companies Act, 1956 under which any proposal of amalgamation should begin with due diligence and, whenever a company approaches a court for the approval of the scheme, it should go with clean hands.

In *Nu-line India P. Ltd., In re*,[36] three petitions were filed seeking sanction of the court for a scheme of amalgamation of two transferor companies with the transferee company. Objections were raised by a promoter-director and another to the scheme that the objectors had been illegally removed from the post of directors, that the shareholding of the companies was likely to increase the shareholding of one group, that a petition before CLB was pending and that this information had been withheld from the court, shareholders and creditors. The court refused to give sanction to the scheme on the ground that the documents filed by the petitioners were contrary to each other and the petitioners had withheld material facts from the court and had filed documents to mislead the court. The court clarified that the scheme of amalgamation could not be approved till the matter was disposed by the CLB.

In *Anup Kumar Sheth* v. *Reliance Industries*,[37] it was held that in the absence of any material contradicting the conclusions of the experts applying the standard methods in valuation of shares in cases of schemes of amalgamations, the court would not go into technical aspects while considering the approval of the scheme of amalgamation. In this case, a scheme of amalgamation approved by the majority of the equity shares was sanctioned by the court in a petition by the transferee company. The Gujarat High Court in one case[38] held that in cases of companies whose amalgamation scheme

35 (2010) 158 Comp Cas 578.
36 (2010) 155 Comp Cas 186 (HP).
37 (2010)154 Comp Cas 278 (Bom.).
38 *Nirmay Properties (P) Ltd., In re* (2010) 97 SCL 207 (Guj.).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

had been sanctioned, the same would not absolve the petitioner-companies from any liability that may arise in future or would not affect the pending civil or criminal proceedings.

X LIABILITIES OF THE DIRECTORS

The Madras High Court in *R. Vasinathan* v. *Commercial Tax Officer (FAC), Ambattur Assessment Circle, Villiwakkam, Chennai*[39] was confronted with the question of a director's liability for the tax arrears of the company as they were its major share-holders. The respondent company in this case had to pay arrears of sales tax under the Tamil Nadu General Sales Tax Act, 1959 and Central Sales Tax Act, 1956. The petitioners were directed to pay the arrears as they were the major shareholders and directors of the company. The Madras High Court held that section 19 of the Tamil Nadu General Sales Tax Act was applicable to the firms and their partners and directors were exempted under this provision. Similarly, in another case[40] in which the issue related to the liability of a director who had resigned from the post in order to escape the liability, the court directed filing of the statement of affairs. In this case, a company was dissolved on a petition filed by the director (who had resigned from the company) for winding up of the same. An official liquidator was appointed to enquire into the matter wherein the director refused to file the statement of affairs. The court observed that the director of the company, who had filed the petition, had raised a frivolous claim to mislead the court regarding the assets of the company under liquidation as he had not properly communicated about his resignation to the officials concerned. The court held that he could not escape from the liability as a director of the company.

In *Gaurangbhai Bipinbhai* v. *Bank of Baroda*,[41] the petitioner, a director of a company, filed a writ petition under article 226 of the Constitution of India for recovery of the amount due upon the realization of the security over a hypothecation from a bank. The bank had retained the surplus amount due to the petitioner under the right of *lien* of the bank. The petitioner had taken a housing loan from the bank and, on default, proceedings were initiated under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. The court held that the petitioner was entitled to get the surplus amount from the bank and the bank cannot retain the amount under the right of lien.

In *Robin Paul* v. *State of West Bengal*,[42] petitions were filed against the directors of a company for the failure to deposit contribution to the provident fund. The court clarified that the term 'employer' under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 cannot cover the

39 (2010) 153 Comp Cas 174 (Mad.).
40 *Official Liquidator, High Court of Patna* v. *Mahindra Prasad* (2010) 153 Comp Cas 354 (Pat.).
41 (2010) 153 Comp Cas 359 (Gau.).
42 (2010) 153 Comp Cas 419.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

director when he was sought to be prosecuted for an offence under section 405 of the Indian Penal Code, 1860. Again, in another case,[43] the apex court settled down the principle of liability of the directors of the company for the offence of dishonor of cheques. The substantial question in this case related to the sustainability of the complaint under section 138 read with section 141 of the Negotiable Instruments Act, 1881 against the director of a company for dishonor of the cheque. Relying on the judicial precedents[44] and the statutory provisions[45] the court fixed liability upon the directors of the company under section 141 of the Act for prosecuting them under section 138 for return of the cheque un-paid by the banker which had been issued on behalf of a company. Upholding the quashing order of the High Court, the Supreme Court laid down the following principles to be followed in such cases:

* The primary responsibility is on the complainant to make specific averments as are required under the law in the complaint so as to make the accused vicariously liable. For fastening the criminal liability, there is no presumption that every director knows about the transaction.
* Section 141 does not make all the directors liable for the offence. The criminal liability can be fastened only on those who, at the time of the commission of the offence, were in charge of and were responsible for the conduct of the business of the company.
* Vicarious liability can be inferred against a company registered or incorporated under the Companies Act, 1956 only if the requisite statements, which are required to be averred in the complaint/petition, are made so as to make accused therein vicariously liable for offence committed by company along with averments in the petition containing that accused were in-charge of and responsible for the business of the company and by virtue of their position they are liable to be proceeded with.
* Vicarious liability on the part of a person must be pleaded and proved and not inferred.
* If accused is managing director or joint managing director, it is not necessary to make specific averment in the complaint and by virtue of their position they are liable to be proceeded with.
* If accused is a director or an officer of a company who signed the cheques on behalf of the company then also it is not necessary to make specific averment in complaint.

The person sought to be made liable should be in charge of, and responsible for, the conduct of the business of the company at the relevant

43 *National Small Industries Corp Ltd*. v. *Harmeet Singh Paintal* (2010) 154 Comp Cas 313.

44 *K.K. Ahuja* v. *V.K. Vora* (2009) 10 SCC 48.

45 S. 141 of the Negotiable Instruments Act, 1881, provides for the offences by companies in which the director may be held liable for the offences committed by companies.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

time. This has to be averred as a fact as there was no deemed liability of a director in such cases.[46]

In *V.S. Gupta* v. *Punjab National Bank*,[47] the Delhi High Court was confronted with the question of liability of a director for dishonor of the cheque given by the company. In this case, complaints under section 138 and 141 of Negotiable Instrument Act read with section 420, IPC were filed by the respondent, Punjab National Bank against the petitioner, director of Padmini Technologies Ltd., who were carrying on the management and day to day affairs of the company and were responsible for everything related to finances of the company. It was further alleged that he had availed credit facilities from the complainant bank and the cheques given by him and others were returned unpaid with remarks "funds insufficient".

The petitioner argued that since he had resigned as a director of the company prior to the issue of cheques in question, he was not vicariously liable for the offence committed by the company. Allowing the petition, the court held that criminal liability for the offence by a company under section 138 of the Negotiable Instruments Act was applied vicariously on the person referred to in section 141(1). Since the petitioner had resigned from the office as director and the nature of job was contractual, it was doubtful whether he would be covered under section 141(2) of the Act. The court held:[48]

> [N]o offence under Section 141 of Negotiable Instruments Act read with Section 138 thereof is made out against the petitioner on the basis of the complaints filed by the respondent. The proceedings initiated against the petitioner, therefore, cannot be allowed to continue. The complaints, subject matters of these petitions, to the extent they pertain to the petitioner are hereby quashed. It is made clear that quashing of complaint against the petitioner would not affect prosecution of other accused persons.

XI LIABILITY OF REGISTRAR OF COMPANIES

Sanjay Suri v. *State*[49] is a celebrated case in the area of company law. In this case, the registrar of companies ûled criminal complaints against the petitioner-company on the following grounds:

(i) that it had failed to attach with its own balance-sheet, the balance-sheet of the company in which it had acquired more than 90 per cent shareholding in contravention of section 212(1) of the Act ;

(ii) that the company had not made proper disclosure in the balance-

46 *Id*., para.25.
47 (2010) 154 Comp Cas 1.
48 *Id*., para. 26.
49 (2010) 157 Comp Cas 10.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

sheet regarding the collateral security attaching its bank account in accordance with the order of the court and the contingent liability; and

(iii) that the board of directors of the company had failed to give information relating to "activities relating to exports, initiative taken to increase exports, development of new export market for products and service and export plans".

The petitioner sought the quashing of the criminal complaints on the grounds that (i) the complaint was barred by limitation, (ii) that the registrar of companies could not be said to be a "person aggrieved by the offence" within the meaning of section 469(1)(b) of the Code of Criminal Procedure, 1973, (iii) that the offence could be said to have come to the knowledge of the registrar on the date of ûling the balance-sheet without scrutinising it, and (iv) that since the company had a managing director, other directors of the company were not liable to be prosecuted for the violations. The pertinent issues in the case were: the period of limitation for filing a complaint in respect of offences under the companies Act, 1956 and whether the registrar of companies is 'person aggrieved' in respect of offences under the Companies Act, 1956.

The court held that registrar of companies would be a person aggrieved of an offence under the Act as he has been assigned a statutory duty to ensure compliance with the provisions of the Act and also in view of the provisions contained in section 621(1) of the Act under which he is one of the persons on whose complaint the court can take cognizance under section 469, Cr PC. It was also held that since the complaints were filed within one year from the date of receipt of inspection report in the office of the registrar of companies and also of completion of inspection by the ofûcer, the complaints were not barred by limitation. Without a detailed examination of the account books of the company, the registrar or his ofûcial could not have known that there was an order of the court attaching its bank account and that the company had given collateral security pursuant to that order. Therefore, it could not be said that the offence committed could have come to the knowledge of the registrar merely from the scrutiny of the balance-sheet of the company.

XII TRANSFER/ALLOTTMENT OF SHARES

Section 111 of the Companies Act, 1956 provides for free transfer of debentures and shares of a company. Before its amendment in 1995, section 111 applied to private companies as well as public limited companies. This section has been amended by the Depositories Act, 1996 that inserted sub-section (14A), wherein the operation of the section has been confined to private companies only. The validity of this section was challenged in many cases and the courts have clarified that free transferability was the norm in the case of shares in a public company.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

In *Western Maharashtra Development Corporation Ltd.* v. *Bajaj Auto Ltd.*,[50] on an issue whether a public limited company can restrict the transfer of shares by a shareholder by way of providing pre-emptive right, the Bombay High Court ruled that preemptive rights with respect to transfer of shares was illegal for a public company. The court clarified that under section 111A of the Companies Act , no restriction can be imposed on the transferability of shares in a public company. The issue in this case centered on an arbitral award entered between the parties under section 34 of the Arbitration and Conciliation Act, 1996. Setting aside an arbitral award resolving a dispute over price for transfer of shares under a right of first refusal clause between the litigating parties, the court held that the arbitrator ought to have held that the pre-emptive right was completely contrary to law and, therefore, unenforceable and, consequently, the award deserved to be set aside.

The court ruled that any pre-emptive rights over shares in public limited companies were patently illegal in view of the principle of "free transferability" enshrined in section 111A of the Companies Act. This revives the debate on the enforceability of shareholder agreements and joint venture agreements governing public limited companies. The Bombay High Court had held that a pre-emptive right would impose a fetter on transferability of shares which was envisaged for private companies only and, in fact, prohibited for public companies, in the scheme of the Act and, therefore, "patently illegal". The court observed:[51]

> The principle of free transferability must be given a broad dimension in order to fulfill the object of the law. Imposing restrictions on the principle of free transferability is a legislative function, simply because the postulate of free transferability was enunciated as a matter of legislative policy when Parliament introduced Section 111A into the Companies' Act, 1956. That is a binding precept, which governs the discourse on transferability of shares. The word "transferable" is of the widest possible import and Parliament by using the expression "freely transferable", has reinforced the legislative intent of allowing transfers of shares of public companies in a free and efficient domain… .The effect of a clause of preemption is to impose a restriction on the free transferability of the shares by subjecting the norms of transferability laid down in Section 111A to a preemptive right created by the agreement between the parties. This is impermissible.

In *Morgan Ventures Ltd* v. *Blue Coast Hotels and Resorts Ltd.*,[52] the question was whether the allotment of shares by a public company could be challenged under section 111A of the Companies Act. The court held that there was no right of appeal provided by section 111A in relation to public

50 (2010) 154 Comp Cas 593 (Bom.).
51 *Id*., para. 53.
52 (2010) 3 Comp LJ 33 (Bom.).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

limited companies, which was contained in sub-section (4) of section 111 of the Act. By upholding the stand of the CLB in dismissing the application as proper on precedent, the court clarified that while enacting section 111A in relation to the public limited companies, the legislature restricted the right of appeal only in case of transfer of shares and the wider right of appeal which was provided by sub-section (4) was not enacted in section 111A.

Similarly, in *Gopal Krishna Baliga* v. *Poona Industrial Hotel Ltd.*,[53] the appellant challenged the resolution passed by the AGM of the company regarding the allotment of equity shares to the promoters of the company. In *Smt. Biva Pyne* v. *Pyne Properties P. Ltd.*,[54] the court held that the legal heir of the deceased joint shareholder was not legally or factually entitled to transmission of shares in her favour. In this case, the petitioner claimed 1800 equity shares that her late husband had left behind under a will on which she had obtained a probate in her favour. Dismissing her petition, the CLB had held that the petitioner could not claim any exclusive interest in the shares as the shares were not held jointly in her husband's name and, therefore, she could not seek transmission of these shares in her favour. The court clarified that since the provisions of the articles were binding on the company as well as every shareholder, only the survivors in respect of the shares would be entitled to the shares held jointly with the deceased. In one case,[55] the members of the board of directors had failed to protect the pre-emptive rights of the shareholders of the company in transferring the shares. The court held that no person could take advantage of his position to the detriment of a third party.

XIII DIVIDEND OF A COMPANY

In *Indowind Energy Ltd*. v. *ICICI Bank Ltd.*,[56] the company filed a petition for declaration of dividend and for the issuance of the bonus shares under section 397 of the Companies Act, 1956. Dismissing the petition, the CLB held that no-declaration of the dividend would not amount to oppression and cannot be adjudicated. The court observed that in cases where there was no arbitration agreement between the parties, no claim against any party or no dispute thereon can be the subject-matter of reference to an arbitrator and the power of the courts was to determine existence of an arbitration agreement and not to ascertain the rights and obligations between the parties to contract.

XIV CHANGE OF MANAGEMENT OF A COMPANY

In one case,[57] directions were issued to the BIFR to examine the proposal

53 (2010) 3 Comp LJ 44 (Bom.).
54 (2010) 153 Comp Cas 49.
55 *J.R. Srininivas* v. *Sri Gururaj Enterprises* (2010) 157 Comp Cas 46.
56 (2010) 153 Comp Cas 394.
57 *Raam Tyres Ltd.* v. *Appellate Authority for Industrial and Financial Reconstruction* (2010) 155 Comp Case 80 (Del.).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

of the existing management for infusion of funds through a strategic investor. The petitioner in a writ petition contended that the strategic investor was only infusing the funds and there was no transfer of the management. The Delhi High Court held that there was no participation by the strategic investor for transfer of shares and the change of management was only a wrong presumption.

XV COMPANY LAW BOARD

Under section 634 of the Companies Act, 1956, any order made by the CLB may be enforced by it in the same manner as a decree made by the court. In *A. Mylsamy* v. *Sri Gajendira Paper and Boards P. Ltd.*,[58] the registered office of the company was shifted without giving proper information to the applicant. Against this, the applicant applied to the CLB to direct the holding of the annual general meeting at the premises of the company instead of the registered office. The CLB held that the annual general meeting of a company has to be held at its registered office under section 166(2) of the Companies Act.

The power of the High Court to interfere with CLB's power was examined in *Shree Ram Urban Infrastructure Ltd*. v. *R.K. Dhall.*[59] In this case, the CLB had restrained the appellant company from implementing the decisions given by the board of directors for the issue of convertible warrants. The CLB passed an *interim* order granting permission to the appellant to file its objection to the petition. The appellant company challenged this in appeal. The court held that the CLB cannot grant *interim* reliefs pertaining to matters which were not a subject matter of a petition. Under regulation 44,[60] CLB did not have the power to extend time given by the High Court for granting of reliefs. Setting aside the order of the CLB, the court held that it had wrongly proceeded to grant such a relief.

In *C.N. Ramesh* v. *Mars Theraputics and Chemicals Ltd.*,[61] the CLB ordered enforcement of its previous order by which the respondents had been directed to transfer their shares in favour of the applicants and had further directed the applicants to pay the consideration in return. Again, in another case,[62] the CLB, in exercise of its powers under section 188(5), through an order, restrained the circulation of a statement on the ground that the words used in the statement may lower the image of the company. In *V.L. Sridharan* v. *Econo Valves P. Ltd.*,[63] deviating from Andhra Pradesh High Court's[64] view, the Madras High Court held that the Act empowers the CLB to decide

58 (2010) 153 Comp Cas 2.
59 (2010) 153 Comp Cas 150 (Bom.).
60 Regulation 44 of the Company Law Board Regulations, 1991.
61 (2010) 158 Comp Cas 8 (CLB).
62 (2010) 158 Comp Cas 16.
63 (2010) 158 Comp Cas 505.
64 *B. Subba Reddy* v. *S.S. Organics Ltd.* (2009) 151 Comp Cas 190.

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

about the competence of the person to file petition under section 397/398 of the Act.

XVI COMPANY MEETINGS

In *Ranbaxy Laboratarries Ltd*. v. *Dr. Jayaram Chigupati*,[65] the meeting called by a director for the appointment of two new directors was challenged on the ground that constituting a one-member quorum was not in accordance with sections 260 and 287(2) of the Companies Act, 1956. The CLB, while dismissing the application, held that the decision take by the single director for the appointment of two directors at the board's meeting was in accordance with section 260 of the Act, which was legal and valid in the eyes of law. In *Marble City Hospital and Research Centre P. Ltd.* v. *Sarabjeet Singh Mokha*,[66] the question was whether the notice of meeting sent by the certificate of post was sufficient for attracting section 283(1)(g). In this case, the Madhya Pradesh High Court held that the company had failed to discharge its onus regarding of service of notice since the mere filing of postal certificates would not corroborate service of notice. The court held that mere production of the certificate of posting issued by the postal authorities was not sufficient to prove that the meeting notice was served to the addressee.

XVII LIFTING OF CORPORATE VEIL

The court dealt with the issue of lifting of the corporate veils in *Atul Gupta (HUF)* v. *Trident Projects Ltd.*[67] by allowing an application for lifting the corporate veil by way of an amendment. The court held that the amendment was necessary to decide the real controversy between the parties. In this case, the plaintiff sought an amendment in the plaint for the inclusion of pleadings regarding the lifting of corporate veil for holding the defendants personally liable for the claim in a suit under the transaction made by them in the name of the defendant company.

XVIII *LOCUS STANDI* OF AN INTERVENER

In *Reliance Communications Ltd., In re*,[68] the intervention by a third person who raised an objection of the scheme of arrangement between RCL and RT which were the demerged company and the resulting company, respectively. The majority of the shareholders of the demerged company voted in favour of the scheme which was unanimously approved by the

65 (2010) 153 Comp Cas 162.
66 (2010) 155 Comp Cas 13 (MP).
67 (2010) 153 Comp Cas 74.
68 (2010) 153 Comp Cas 233 (Bom.).

www.ili.ac.in The Indian Law Institute

The Indian Law Institute

shareholders of the resulting company. A third person raised certain objections to the scheme. The court held that since the intervener was not related to the company in any capacity, either as a creditor or as a shareholder, he had no *locus standi* to object to the scheme.

XIX MISCELLENOUS

In *Securities Exchange Board of India* v. *Ajay Agrawal*,[69] the question was whether section 11B of the Securities and Exchange Board of India Act, 1992 could be invoked by the chairman of the Securities and Exchange Board of India (SEBI) in conjunction with sections 4(3) and 11 for restraining the respondent from associating with any corporate body in accessing the securities market and prohibiting him from buying, selling or dealing in securities. In the present case, a restraint was imposed upon the respondent under section 11B of the Securities and Exchange Board of Indian Act, 1992 on the ground that the respondent had committed an irregularity in the public issue of shares. The respondent put forward the plea that he was entitled to the benefit under article 20(1) of the Constitution of India as section 11B was an *ex post facto* law and had no retrospective operation. By upholding the restraint order passed by the SEBI, the Supreme Court held that immunity/ protection under article 20(1) was not available to the respondent. It observed:[70]

> The right of a person of not being convicted of any offence except for violation of a law in force at the time of the commission of the act charged as an offence and not to be subjected to a penalty greater than that which might have been inflicted under the law in force at the time of the commission of the offence, is a Fundamental Right guaranteed under our Constitution only in a case where a person is charged of having committed an "offence" and is subjected to a "penalty.

The court, by reiterating the *ratio* in *Union of India* v. *Sukumar Pyne*,[71] held that section 11B was procedural law and could be applied retrospectively.

In a question whether the civil courts had jurisdiction to decide the validity of the contracts entered into by the director and guarantor was decided by the court in *Pyramid Saimira Theatre Ltd.* v. *S. Murgan.*[72] Rejecting the contention that the jurisdiction of the civil court was ousted, the court held that for the proper administration of justice, the suits, which were pending before the other quasi-judicial bodies, could be entertained in civil courts.

69 (2010) 155 Comp Cas 1.
70 *Id*., para. 29.
71 AIR 1966 SC 1206.
72 (2010) 155 Comp Cas 42.

www.ili.ac.in The Indian Law Institute