CASE LAW ANALYSIS

Dr. K. R. Chandratre[1]

Can a legal representative of deceased member file a petition under section 241 ?

The word "member" in section 287(3) of the English Companies Act, 1948[2] was construed as extending to the legal personal representative of the deceased member[3]. In *Bayswater Trading Co. Ltd., In re* [1970] 40 Comp Cas 1196 (Ch D), it was held that having regard to the context in which the word "member" is found in section 353(6) of the English Companies Act, 1948[4], it ought to be so construed as to include a legal representative of the deceased member although not on the register of members, for it would not be unlikely that in the course of the 20 years allowed by the sub-section that his personal representative should not be a person entitled to ask the court to restore the name of the company to the register. Applying the ratio of the case cited above, Penmycuick J. held in *Jermyn Street Turkish Baths Ltd., In re* [1971] 41 Comp Cas 735 (Ch D) that personal representatives of a deceased member must be regarded as members of a company for the purposes of section 210 of the English Companies Act, 1948 (section 397 of the Companies Act, 1956). This ruling has been applied by the Supreme Court in *World Wide Agencies P. Ltd.* v. *Mrs. Margaret T. Desor* [1990] 67 Comp Cas 607 (SC) in which it has been held that legal representatives of a deceased member are entitled to petition under sections 397 and 398. If the term "member" under sections 397 and 398 is construed to exclude all persons who have parted with the beneficial interest in the shares, there will be a large number of members who would be deprived of the remedies provided by those sections (*Killick Nixon Ltd.* v. *Bank of India* [1985] 57 Comp Cas 831 (Bom)).

The legal representatives of the deceased member whose names are still not on the register of members are entitled to petition under section 241. It would be wrong to insist that legal representatives' names must be first put on the register before they can move an application under section 397/398. This would frustrate the very purpose of the necessity of action (*World Wide Agencies P. Ltd.* v. *Mrs. Margaret T. Desor* [1990] 67 Comp Cas 607 (SC)).

1. Practising Company Secretary, Past President, the Institute of Company Secretaries of India.
2. Section 494(3) of the Companies Act, 1956.
3. *Llewellyn* v. *Kasintoe Rubber Estates Ltd.* [1914] 2 Ch D 670 (CA).
4. Section 560(6) of the Companies Act, 1956.

But in *Arun Bhat* v. *Banana County Resort P. Ltd.* [2019] 215 Comp Cas 1 (NCLT), the National Company Law Tribunal has held that as legal heir of his father, the son could get the deceased father's estate, which included the shares held by his father, after applying for transmission in accordance with law and the company had to consider it. The son could not maintain the petition which was filed by his father making allegations of various acts of oppression and mismanagement. However, the son, after getting transmission of the shares of his father, could claim his rights based on such transmission, in accordance with law. The son was not involved in the affairs of the company by attending annual general meetings or board meetings as contended by the respondents. Therefore, he could not maintain the petition filed by his father, under sections 397 and 398 of the Act.

Dispensing with meetings of members or creditors for approval of scheme of compromise or arrangement : Law lacks clarity

Under section 391 of the Companies Act, 1956 while almost all High Courts used, in appropriate cases and subject certain conditions, to dispense with meetings of members and/or creditors in the case of a scheme of compromise or arrangement, the courts sometimes did decline to dispense with these meetings in exercise of their discretionary powers. There were, however, cases in which the courts had questioned the very existence of the power in this regard and emphasized the language of the statute and construed it so that the court has no discretion. In some cases, the courts had, while declining to dispense with meetings, questioned the propriety of the dispensation or rationale behind the requirement of holding a meeting.

Under the Companies Act, 2013 while section 230(1) requires meetings of members and creditors or their classes, to be held, sub-section (9) of that section provides that the Tribunal may dispense with calling of a meeting of the creditors or a class of creditors where such creditors or class of creditors, having at least ninety per cent. value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

There is no similar provision concerning meetings of members or classes of members. One would think that the holding of meetings of members is mandatory even if there are only two members (or even only one member of a class of shares).

In this confusing state of affairs, the National Company Law Appellate Tribunal's order in *MEL Windmills P. Ltd.* v. *Mineral Enterprises Ltd.* [2019] 215 Comp Cas 45 (NCLAT) will add confusion inasmuch as the Appellate Tribunal has held observed that "the Tribunal, while dealing with an application under section 230 of the Companies Act, 2013, on being satisfied that the compromise or arrangement had been proposed in connection with a scheme for the reconstruction of the company or companies involving merger or amalgamation of two or more companies and under the scheme property or liabilities of the transferor company are required to be transferred to the transferee company or divided among or transferred to two or more companies, is required to order meetings of the creditors or members, as the case may be, to be called. Sub-section (9) thereof empowers the Tribunal to dispense with calling a meeting of the creditors where such creditors, having at least 90 per cent. value agree to and confirm the scheme of compromise or arrangement. The creditors or *members* are required to file an affidavit stating that they agree to and confirm the scheme of compromise or arrangement. Where the creditors or *members* having at least 90 per cent. value signify their consent to the scheme of compromise or arrangement by filing affidavits, the Tribunal will have the discretion to dispense with calling the meeting of creditors or *members*". (emphasis[1] supplied)

A petitioner under section 241 must be a member of the company

Under section 241 a person who is a member alone can apply to the National Company Law Tribunal. The term "member" is defined in section 2(55) of the Companies Act, 2013 ("the Act").

Conditions of acquisition of membership

The definition of "member" in section 2(55) of the Companies Act, 2013, refers to three classes of members, namely :—

(i) persons who have subscribed to the company's memorandum of association ;

(ii) persons who have agreed to become members ; and

(iii) persons who hold shares and whose names are entered as beneficial owners in the records of a depository.

In order to be recorded as member of the company the person must agree in writing to be a member and his name should also find place in the register of members (*Bihar State Industrial Development Corporation Ltd.* v. *Company Law Board* [2010] 158 Comp Cas 561 (Patna)).

A member means a shareholder of a company whose name is entered in the register of members. A founder member is a person who signs the initial memorandum of association ; any person purchasing shares subsequently or possessing shares after the incorporation of the company whose

1. Here printed in italics.

name is entered in the register of members becomes a member. In the case of a subscriber to the memorandum, no agreement besides the memorandum is necessary in order that the subscriber is treated as a member. A person who is not a subscriber to the memorandum of the company may acquire membership in the manner specified in clause (ii), namely, by agreeing to become a member. Here too, entry in the register of members is vital, but that is the duty of the company. A person holding equity shares of a company and whose name is entered in the records of a depository as a beneficial owner of the shares is deemed to be a member of the company.

Generally, a person may become a member of a company in any of the following ways : (1) by subscribing to the memorandum of association before its registration ; (2) by agreeing with the company to take a share or shares and being placed in the register of members ; (3) by taking a transfer of a share or shares, and being placed in the register of members ; (4) by registration on succession to a deceased or bankrupt member ; and (5) by allowing his name to be in the register of members or otherwise holding himself out or allowing himself to be held out as a member (*Collector of Moradabad* v. *Equity Insurance Co. Ltd.* [1948] 18 Comp Cas 309 (Oudh)).

Two essential conditions have to be satisfied to constitute a person a member :

(1) an agreement in writing to become a member ; and

(2) an entry on the register.

If these two conditions are not satisfied, the person in question cannot claim the status of member (*Lalithamba Bai* v. *Harrisons Malayalam Ltd.* [1988] 63 Comp Cas 662 (Ker)). It is well-settled that a contract to purchase shares or debentures is concluded by allotment of shares (*N. Parthasarathy* v. *Controller of Capital Issues* [1991] 72 Comp Cas 651 (SC)). To constitute a binding contract to take shares in a company when such contract is based upon application and allotment, it is necessary that there should be an application by the intending shareholder, an allotment by the directors of the company of the shares applied for, and a communication by the directors to the applicant of the fact of such allotment having been made. The purchase of shares is governed by the same law as the purchase of goods (*Shiromani Sugar Mills Ltd.* v. *Debi Prasad* [1950] 20 Comp Cas 296 (All)). The application for shares and the letter of allotment constitute a valid and legally binding contract between the applicant and the company, "a contract the fruit of which is shares"[1].

1. *Collins* v. *Associated Greyhound Racecourses Ltd.* [1930] 1 Ch D 1 (CA) ; *Tillotson Ltd.* v. *IRC* [1933] 1 KB 134 and *Heaton's Steel and Iron Co., In re* [1876] 4 Ch D 140.

No person can be a shareholder until he is registered. A person who is not a shareholder by registration cannot claim that the share has been issued to him, but only that the company is bound by contract to issue a share to him. A person who has been allotted shares is in as good a position in equity as a person to whom shares have been issued but that does not mean that there is no distinction between allotment and issue ; an allotment creates an enforceable contract to issue and accept shares[1].

The Company Law Board has held that for any person to become a member, two conditions must be fulfilled : (a) that there is an agreement to become a member, and (b) that the name is entered on the register of members. It is, therefore, abundantly clear that no one can become a member unless he has agreed in writing to become a member of the company (*Kumar Malavalli* v. *CRCW Search Technologies P. Ltd.* [2004] 118 Comp Cas 618 (CLB)).

Allotment of shares means division, distribution or appropriation of shares in a company. It is a method of distributing previously unissued shares in a company having a share capital from out of the authorised share capital in exchange for a contribution of capital, in response to an application for such shares. The company accepts the application by allotting the shares in full or in part. Then it communicates to the allottee by dispatching a letter of allotment to the applicant stating how many shares he has been allotted ; he then has an unconditional right to be entered in the register of members in respect of those shares. If the number of shares applied for exceeds the number available (over-subscription), allotment is made by a random draw or by a proportional allocation. If an applicant has been allotted fewer shares than he has applied for, he receives a cheque or warrant for the refund of the application money in respect of the unallotted balance.

Allotment is the acceptance by the company of the offer to take shares by the applicant. That offer is accepted by the allotment either of the total number mentioned in the offer or a less number, to be taken by the person who made the offer. This constitutes a binding contract to make that number according to the offer and acceptance[2].

Under the Act, a company having a share capital is required to state in its memorandum of association the amount of the capital and the division thereof into shares of a fixed amount. This is what is called the authorised capital of the company. Then the company proceeds to issue the shares

1. *Collins* v. *Associated Greyhound Racecourses Ltd.* [1930] 1 Ch D 1 (CA) ; *Tillotson Ltd.* v. *IRC* [1933] 1 KB 134 and *Heaton's Steel and Iron Co., In re* [1876] 4 Ch D 140.
2. *Florence Land and Public Works Co., In re* [1885] LR 29 Ch D 421.

depending on the condition of the market. That only means inviting applications for these shares. When the applications are received, it accepts them and this is what is generally called allotment. Allotment means the appropriation out of the previously unappropriated capital of a company, of a certain number of shares to a person. Till such allotment, the shares do not exist as such. It is on allotment in this sense that the shares come into existence (*Sri Gopal Jalan and Co.* v. *Calcutta Stock Exchange Association Ltd.* [1963] 33 Comp Cas 862 (SC)).

Till the allotment shares do not exist ; it is only on allotment that shares come into existence and become movable goods. Shares come into existence on the evolution of a process, which begins with the creation of shares and ends with the allotment thereof. The intermediary step is that of issue of the shares. Creation, issue and allotment are the three stages towards the formation or coming into existence of new share capital (*Sri Gopal Jalan and Co.* v. *Calcutta Stock Exchange Association Ltd.* [1963] 33 Comp Cas 862 (SC)). Shares can never be called "goods", at the stage of application for shares. An applicant for shares before allotment is only a prospective investor in future goods. A fortiori, an application for allotment of shares cannot constitute goods (*Morgan Stanley Mutual Fund* v. *Kartick Das* [1994] 81 Comp Cas 318 (SC). See also *Consumer Education and Research Centre* v. *T. T. K. Pharma Ltd.* [1990] 68 Comp Cas 89 (MRTPC) [FB] and *Director-General of Investigation and Registration* v. *Deepak Fertilizers and Petrochemicals Corporation Ltd.* [1994] 81 Comp Cas 341 (MRTPC) [FB]).

A contract to purchase shares or debentures is concluded by allotment of shares[1]. To constitute a binding contract to take shares in a company when such contract is based upon application and allotment, it is necessary that there should be an application by the intending shareholder, an allotment by the directors of the company of the shares applied for, and a communication by the directors to the applicant of the fact of such allotment having been made. When a return of allotment is made the whole process gets completed in all respects. The purchase of shares is governed by the same law as the purchase of goods (*Shiromani Sugar Mills Ltd.* v. *Debi Prasad* [1950] 20 Comp Cas 296 (All)).

Allotment and transfer of a share are two different things. An allotment of shares is an act of the company by which the applicant for shares becomes the holder of unappropriated shares ; shares standing in the name of one person cannot be allotted to another person by the company even

1. *Larsen and Toubro Ltd.* v. *Haresh Jagtiani*, AIR 1991 SC 1420 ; [1991] 2 Comp LJ 1 (SC).

with the former's consent, though such shares may be transferred by the person in whose name they stand[1].

It should be noted that according to section 41(2) of the Companies Act, 1956 registration of a person's name on the register of members is a condition precedent to acquire the membership of a company. However, as held by the Supreme Court in *Shree Gopal Paper Mills Ltd.* v. *CIT* [1970] 77 ITR 543 (SC), a person becomes the owner of a share on allotment (and not on the registration of his name) notwithstanding that he may become entitled to exercise the right of members on the registration.

In the context of levy of income-tax, with regard to bonus shares issued by a company it was held by the Supreme Court that a shareholder became the owner of the bonus shares allotted to him from the date of the resolution passed at a general meeting approving the bonus issue, even without issue of share certificates to him and the shares allotted became the property of the shareholders on the date of passing of the resolution (*Shree Gopal Paper Mills Ltd.* v. *CIT* [1970] 77 ITR 543 (SC)). It was held that merely because in the resolution of the general meeting, the directors of the company were directed to issue bonus shares, the property in the bonus shares had not passed to the ordinary shareholders on the date of the resolution ; the words "allot" and "distribute" found in the resolution did not carry the matter further ; their meaning should be gathered from the context in which they were used ; the word "allotment" had not been defined in the Companies Act ; the meaning of the word "allot" or "allotment" would have to be gathered from the context in which those words were used.

In *Greenline Transit System P. Ltd.* v. *Airone Aviation P. Ltd.* [2019] 215 Comp Cas 116 (NCLT), the National Company Law Tribunal emphasized that a petitioner under section 241 must show that he is a member of the respondent-company.

The definition of a member of a company shows that there should be an application in writing and the name of the member should be entered in the register of members of the company. The provision requires as a condition precedent for membership that the name of the person in question is entered in the register. Secondly such a person may be regarded as a member if he has acquired the right of membership although his name is not in the register. One may become a shareholder in a company by subscribing to the memorandum as provided by section 41 of the Companies Act, 1956, by allotment apart from other modes. An effective allotment has to comply

1. *Mumtaz Bank Ltd.* v. *Syed Masud Ali Chisti* [1937] 7 Comp Cas 230 (Lahore). See also *Spitzel* v. *Chinese Corporation Ltd.* [1899] 80 LT 347.

with the requirements of the law of contracts relating to acceptance of an offer. An allotment is required to be made by the proper authority. The allotment is a duty primarily falling upon the directors. In the first place, an allotment must be made by a resolution of the board of directors and it cannot be delegated. The allotment is also required to be made within a reasonable period of time which is a question of fact in each case, say six months. On the expiry of reasonable time, section 6 of the Indian Contract Act, 1872, applies and the application must be deemed to have been revoked. An allotment must be absolute and in accordance with the terms and conditions of the application, if any. An allottee of a share is entitled to have a document, called share certificate, unless by precedent of the company shares are kept in its safe custody. Thus, every company making an allotment of shares is obliged to deliver to an allottee a certificate of shares within three months after the allotment.

Directors' liability for non-compliance with CSR provisions

Under section 134(3)(o), the Board's report of every company must disclose the details about the policy developed and implemented by the company on corporate social responsibility initiatives taken during the year. Failure to do so attracts penal consequences under sub-section (8) of that section which provides that, if a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

According to section 135(5), the Board of every company referred to in sub-section (1), shall ensure that the company spends, in every financial year, at least two per cent. of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its corporate social responsibility policy ; and according to the second proviso to section 135(5), if the company fails to spend an amount equal to two per cent. of its net profits of a financial year on CSR activities, the board shall, in its report made under clause (o) of sub-section (3) of section 134, specify the reasons for not spending the amount.

Section 135 does not provide for any penalty for non-compliance with any requirement of that section, but in such a case, section 450 will get attracted. This section lays down punishment where no specific penalty or punishment is provided, and states that if a company or any officer of a company or any other person contravenes any of the provisions of this Act or the rules made thereunder, or any condition, limitation or restriction subject to which any approval, sanction, consent, confirmation, recognition, direction or exemption in relation to any matter has been accorded, given or granted, and for which no penalty or punishment is provided elsewhere in this Act, the company and every officer of the company who is in default or such other person shall be punishable with fine which may extend to ten thousand rupees, and where the contravention is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the contravention continues.

In *Peregrine Guarding P. Ltd.* v. *Registrar of Companies* [2019] 215 Comp Cas 134 (NCLAT), the National Company Law Appellate Tribunal has held that the requirement under section 134(3)(o) read with section 135(2) of the Companies Act, 2013, to disclose in its director's report, the details of the corporate social responsibility policy developed and implemented during the year and to constitute a corporate social responsibility committee was not fulfilled by the appellant-company for the financial years 2014-15, 2015-16 and 2016-17. Finally, the board of directors of the company in its meeting held on April 16, 2018 cured the defects with effect from the year ending March 31, 2018. The company and its directors filed a petition under section 441 of the Act praying for compounding of the offence. The Tribunal on hearing the parties and taking into consideration the fact that the provision of law was newly introduced under 2013 Act and that the appellants had not much clarity on it and as the default had been subsequently made good, imposed a fine on the company and its directors for compounding the offence for three years, i. e., 2014-15, 2015-16 and 2016-17. The directors on whom fine was imposed had been party to default and had not taken steps to correct and bring the default to the notice of the board of directors. If nothing had been shown by the Registrar of Companies, it was a typographic error and mistake. The directors were liable for penal action under section 134(8) of the 2013 Act. The penal amount was less than 33 per cent. of the total maximum penal amount payable. Since the provisions of the 2013 Act were practically similar to the provisions in the 1956 Act, the lenient view taken by the Tribunal on the ground that the new Act had been introduced was not acceptable.

Net profit computation for the purpose of section 135

Sub-section (5) of section 135 provides that, a company which has a net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during the immediately preceding financial year shall spend at least two per cent.

of the average net profits of the company made during the three immediately preceding financial years.

Further, the *Explanation* to sub-section (5) provides that net profit shall not include such sums as may be prescribed, and shall be calculated in accordance with the provisions of section 198.

Therefore, to arrive at the average of net profits during the immediately three preceding financial years, a company shall calculate the net profits as specified in section 198 of the Act for each year.

Section 198 of the Act provides for computation of net profits, which is relevant for the purpose of section 135(5). According to sub-section (4) of section 198 enumerates the sums which shall be deducted in making the computation of profits under section 198, and one of the sums enumerated therein is "(l) the excess of expenditure over income, which had arisen in computing the net profits in accordance with this section in any year, in so far as such excess has not been deducted in any subsequent year preceding the year in respect of which the net profits have to be ascertained".

For example, if computation of net profits under section 198 shows that the total of net profits before tax for the three financial years 2015-16, 2016-17 and 2017-18, after deducting loss of the financial year 2015-16 is Rs. 23,22,91,012 and the average net profits before tax for these three financial years is Rs. 7,74,30,337, it is this amount of net profits which is relevant for the calculation of 2 per cent. being the CSR contribution to be made by the company in the financial year 2018-19. Two per cent. of this amount comes to Rs. 15,48,607. In my opinion, it was held in the case of *Shri Santosh Meenakshi Textiles P. Ltd.* v. *Registrar of Companies* [2019] 215 Comp Cas 154 (NCLAT) as follows :

> ". . . the appellant-company was liable to appropriate expenditure in respect of corporate social responsibility for the financial year 2014-15 taking into account only the net profit for the financial year 2013-14. The company was held liable to adhere to the other provisions of section 135 of the Companies Act, 2013. According to the company's own calculation the net profit was Rs. 5,68,70,023 for the financial year 2013-14 which was more than Rs. 5 crores, the threshold limited prescribed under section 135(1) of the Act. Therefore, the company was covered under section 135(1) of the Act. The company was liable to constitute a corporate social responsibility committee of the board in the year 2014-15. Section 135(5) of the Act stipulated that the board of every company which comes under section 135(1) of the Act should ensure that the company spends in every year at least 2 per cent. of the average net profit of the company made during the three

immediately preceding financial years in pursuance of the corporate social responsibility. The net profit would be calculated in terms of section 198 of the Act and that the profit before tax would be taken as 'net profit'. According to the calculation of the company the net profit of three years was negative. In that calculation the figures of financial year 2011-12 and 2012-13 had been deducted twice from the figures of 2013-14, and therefore, the figures had reached a negative level. In the chart Rs. 1,38,69,595 was the net profit of three years and dividing it by three the average net profit for three years had to be considered. From the net profit before tax of 2014, first the loss as reflected in 2012 and 2013 had to be deducted and the yield being still positive, would be the net profit of the three years. The method of calculation of the average net profit for the immediately preceding three years was applicable."

Voting right of preference shareholders

According to clause (a) of sub-section (1) of section 47, every member holding equity shares in a company has a right to vote on every resolution placed before the company ; and according to clause (b), the voting right of an equity shareholder, on a poll, shall be in proportion to his share in the paid-up equity share capital of the company.

Clause (b) of section 47(1) seeks to lay down the rule that every equity shareholder in one class of shares with equal voting rights has voting right on every share held by him in proportion to his share in the paid-up equity share capital of the company.

Section 47(2) of the Companies Act, 2013 (2013 Act) reads as follows :

"(2) Every member of a company limited by shares and holding any preference share capital therein shall, in respect of such capital, have a right to vote only on resolutions placed before the company which directly affect the rights attached to his preference shares and, any resolution for the winding up of the company or for the repayment or reduction of its equity or preference share capital and his voting right on a poll shall be in proportion to his share in the paid-up preference share capital of the company :

Provided that the proportion of the voting rights of equity shareholders to the voting rights of the preference shareholders shall be in the same proportion as the paid-up capital in respect of the equity shares bears to the paid-up capital in respect of the preference shares :

Provided further that where the dividend in respect of a class of preference shares has not been paid for a period of two years or more, such class of preference shareholders shall have a right to vote on all the resolutions placed before the company."

As against that, section 87(2) of the Companies Act, 1956 (1956 Act) reads as follows :

"(2)(a) . . . every member of a company limited by shares and holding any preference share capital therein shall, in respect of such capital, have a right to vote only on resolutions placed before the company which directly affect the rights attached to his preference shares.

Explanation.—Any resolution for winding up the company or for the repayment or reduction of its share capital shall be deemed directly to affect the rights attached to preference shares within the meaning of this clause.

(b) Subject as aforesaid, every member of a company limited by shares and holding any preference share capital therein shall, in respect of such capital, be entitled to vote on every resolution placed before the company at any meeting, if the dividend due on such capital or any part of such dividend has remained unpaid—

(i) in the case of cumulative preference shares, in respect of an aggregate period of not less than two years preceding the date of commencement of the meeting ; and

(ii) in the case of non-cumulative preference shares, either in respect of a period of not less than two years ending with the expiry of the financial year immediately preceding the commencement of the meeting or in respect of an aggregate period of not less than three years comprised in the six years ending with the expiry of the financial year aforesaid.

Explanation.—For the purposes of this clause, dividend shall be deemed to be due on preference shares in respect of any period, whether a dividend has been declared by the company on such shares for such period or not,—

(a) on the last day specified for the payment of such dividend for such period, in the articles or other instrument executed by the company in that behalf ; or

(b) in case no day is so specified, on the day immediately following such period ;

(c) where the holder of any preference share has a right to vote on any resolution in accordance with the provisions of this sub-section,

> his voting right on a poll, as the holder of such share, shall, subject to the provisions of section 89 and sub-section (2) of section 92, be in the same proportion as the capital paid-up in respect of the preference share bears to the total paid-up equity capital of the company."

Unlike equity shareholders, preference shareholders have a limited right of voting. A preference shareholder has a right to vote only on resolutions which directly affect any of the rights attached to his preference shares.

For this purpose, any resolution for winding up of the company or for the repayment or reduction of its share capital shall be deemed directly to affect the rights attached to preference shares.

Besides, resolutions for the following matters are some such resolutions :

- Change in the rate of dividend.
- Change in the period of redemption of capital.
- Compromise or arrangement, including amalgamation of the company.
- Change in the nature of the shares, such as cumulative to non-cumulative, redeemable to irredeemable.

A resolution for alteration of the memorandum to shift the registered office of the company is not a resolution which directly affects the rights of the preference shareholders (*Parikh Engineering and Body Building Co. Ltd., In re* [1975] 45 Comp Cas 157 (Patna)).

Issue of further ordinary shares carrying the usual voting rights does not affect the voting rights of preference shareholders, and, therefore, they cannot complain that their voting rights are affected[1].

In *John Smith's Tadcaster Brewery Co. Ltd., In re* [1953] 1 All ER 518 (CA) and *White* v. *Bristol Aeroplane Co. Ltd.* [1953] 1 All ER 40 (CA), the company's articles provided, inter alia, that the holders of preference stock shall not as such be entitled to receive notice of or to attend or vote at any general meeting of the company unless (A) the fixed cumulative preferential dividend on the preference stock is in arrears or unpaid for six months prior to the date of the meeting ; or (B) a resolution is proposed to be passed at such meeting for the sale of the company's undertaking, or for the winding up or reduction of the capital of the company, or for altering the regulations of the company so as directly to interfere with or affect the rights and privileges of the said holders. The directors of the company, of which the issued paid-up capital consisted of £ 1,740,000 five per cent, cumulative preference stock and one million nine hundred and twenty

1. *John Smith's Tadcaster Brewery Co. Ltd., In re* [1953] 1 All ER 518 (CA) and *White* v. *Bristol Aeroplane Co. Ltd.* [1953] 1 All ER 40 (CA).

thousand ordinary shares of £ 1 each, proposed to increase the capital of the company by the creation of two hundred and eighty thousand ordinary shares of £ 1 each, to capitalise an amount standing to the credit of the company's reserve account, and to apply the same in paying up the new ordinary shares which would then be distributed among ordinary shareholders credited as fully paid. The Court of Appeal held, following the decision in *White* v. *Bristol Aeroplane Co. Ltd.* [1953] 1 All ER 40 (CA), that notwithstanding that the position of the ordinary shareholders would be thereby strengthened as compared with the preference stockholders, the proposed transactions did not affect the rights of the preference stockholders.

Where preference shares were issued to a foreign party and the Reserve Bank had stipulated a condition that the foreign equity (including preference share with an option of conversion into equity shares) should not exceed 49 per cent. it was held that voting rights acquired in terms of section 87(2)(b)(ii) of the 1956 Act could not be exercised as that would have resulted in violation of the condition stipulated by the RBI which had overriding effect (*CDS Financial Services (Mauritius) Ltd.* v. *BPL Communications Ltd.* [2004] 121 Comp Cas 374 (Bom)).

The effect of the provision in section 87(2) was explained in a case as follows : From a reading of sub-section (2) of section 87, it is obvious that holders of preference share capital have a right to vote only on resolutions which directly affect the rights attached to their preference shares. Clause (b) of sub-section (2), however, gives the preference shareholder a right to vote on every resolution in case the dividend due on such capital has remained unpaid, in the case of cumulative preference shares in respect of a total period of not less than two years (*Parikh Engineering and Body Building Co. Ltd., In re* [1975] 45 Comp Cas 157 (Patna)).

In *Ram Parshotam Mittal* v. *Hillcrest Realty Sdn. Bhd.* [2009] 152 Comp Cas 477 (SC), it was submitted that since the company in question had not paid a dividend for more than two consecutive years, under section 87(2)(b)(i) of the Companies Act, the preference shareholder had become entitled on expiry of the two years from the date of allotment of the preference shares, to vote on every resolution placed before the company at any meeting, as provided under section 87(2)(b) of the said Act, and that even if the company had not made profits and no dividend had been declared for more than two years, dividend would be deemed to be due for the purpose of section 87(2)(b), as indicated in the *Explanation* thereto. It was urged that the aforesaid *Explanation* created a legal fiction that dividend would be deemed to be due for the purpose of clause (b) of section 87(2) of the Companies Act, whether a dividend is declared by the company on such shares or not. It was submitted that the rationale for the legal fiction was that if the company is managed in such a manner that no profits are being made and no dividend is, therefore, declared or paid to preference shareholders, such preference shareholders would then be entitled to have voting rights on every resolution for selecting a better management. The Supreme Court accepted the above submissions and held that the preference shareholder had acquired the voting rights under section 87(2)(b) of the 1956 Act which indicated the rights of a preference shareholder in *clear and unambiguous terms*. (emphasis[1] supplied)

Now, in *Ram Parshotam Mittal* v. *Hotel Queen Road P. Ltd.* [2019] 215 Comp Cas 163 (SC), partly affirming the decision of the Delhi High Court in *Hillcrest Realty Sdn. Bhd.* v. *Hotel Queen Road P. Ltd.* [2013] 179 Comp Cas 475 (Delhi), the Supreme Court once again dealt with the subject of voting rights of preference shareholders, and held that in terms of section 87 of the Companies Act, 1956, a notice of a general meeting had to be issued to the preference shareholders also for the meeting and they had a right to participate in the meeting, prima facie, when dividend had not been declared. Therefore, the preference shareholders had a right to vote in the meeting.

Compounding of offences

In the Case Law Analysis in Volume 214, a detailed discussion on compounding of offences is set out. Section 441 of the Companies Act, 2013 contains the provisions concerning compounding of offences under the Act. In the Companies Act, 1956, these provisions were contained in section 621A.

It is not mandatory for law-enforcing agency to agree to the compounding of an offence

According to section 441 of the Companies Act, 2013 any offence punishable under this Act (whether committed by a company or any officer thereof) not being an offence punishable with imprisonment only, or punishable with imprisonment and also with fine, may, either before or after the institution of any prosecution, be compounded by—

(a) the Tribunal ; or

(b) where the maximum amount of fine which may be imposed for such offence does not exceed twenty-five lakh rupees, by the Regional Director or any officer authorised by the Central Government, on payment or credit, by the company or, as the case may be, the officer, to the Central

1. Here printed in italics.

Government of such sum as that Tribunal or the Regional Director or any officer authorised by the Central Government, as the case may be, may specify.

The use of the words "may be compounded" indicate that it is a discretionary power of the Tribunal/Regional Director to compound an offence when an application is made by a company or its officer for the same.

Sub-section (3) of section 441 contain the following requirements as regards an application for compounding of offences :

> "(a) Every application for the compounding of an offence shall be made to the Registrar who shall forward the same, together with his comments thereon, to the Tribunal or the Regional Director or any officer authorised by the Central Government, as the case may be.
>
> (b) Where any offence is compounded under this section, whether before or after the institution of any prosecution, an intimation thereof shall be given by the company to the Registrar within seven days from the date on which the offence is so compounded.
>
> (c) Where any offence is compounded before the institution of any prosecution, no prosecution shall be instituted in relation to such offence, either by the Registrar or by any shareholder of the company or by any person authorised by the Central Government against the offender in relation to whom the offence is so compounded.
>
> (d) Where the compounding of any offence is made after the institution of any prosecution, such compounding shall be brought by the Registrar in writing, to the notice of the court in which the prosecution is pending and on such notice of the compounding of the offence being given, the company or its officer in relation to whom the offence is so compounded shall be discharged."

The question is whether compounding of an offence is a sort of compromise to settle a dispute. The question whether the Securities and Exchange Board of India can be compelled to agree to compounding of an offence, was considered by the Bombay High Court in *N. H. Securities Ltd.* v. *Securities and Exchange Board of India* [2019] 215 Comp Cas 251 (Bom).

In the High Court's view, the Securities and Exchange Board of India cannot be compelled to settle a dispute. Section 24A of the 1992 Act indeed stipulates that notwithstanding anything contained in the Code of Criminal Procedure, 1973 any offence punishable under the 1992 Act not being an offence punishable with imprisonment only or with imprisonment or also with fine may either before or after the institution of any proceedings be compounded by the Securities Appellate Tribunal or the court before which such proceedings are pending. The interpretation of the provision would not mean that whenever an application is preferred by the accused such offence has to be compounded or that the prosecution agency cannot oppose such an application. It would also not mean that the prosecuting agency, viz., the Board can be compelled to concede for allowing compounding application.

Compounding cannot be found fault with if it is done applying all parameters

In *Serious Fraud Investigation Office* v. *IL & FS Engineering and Construction Co. Ltd.* [2019] 215 Comp Cas 282 (T&AP), the Telangana and Andhra Pradesh High Court has held, in the context of section 621A of the Companies Act, 1956, that cases seeking compounding under the Companies Act, 1956, are required to be considered applying principles analogous for compounding of offences under section 320 of the Code of Criminal Procedure, 1973. The Serious Fraud Investigation Office, after completion of investigation assigned to it, had launched prosecution against the respondent-company and its directors. During the pendency of the prosecution, the company and its directors approached the Company Law Board admitting the violations and seeking to compound the contravention of the provisions of section 297 of the Companies Act, 1956. The Company Law Board compounded the offences, subject to payment of a fee. On an appeal by the Serious Fraud Investigation Office contending that the violations committed were of serious nature affecting public interest and the Company Law Board gravely erred in allowing compounding of offences in a casual manner, the court, dismissing the appeal, held that the offence alleged against the company and its directors of violation of the provisions of section 297 of the Act was compoundable in terms of section 621A of the Act. The Company Law Board had applied the necessary parameters for compounding the offences. The penalty imposed for compounding was substantially high and would serve as a deterrent in future to the respondents and similarly situated entities or persons. The decision of the Company Law Board was based on the material placed before it. No question of perversity of finding of fact having been raised, interference was not called for.

Elucidating the object of the provisions of section 621A, the High Court said :

> "Section 621A of the Companies Act, 1956 came to be introduced by the Companies (Amendment) Act, 1988. The objective of introducing the compounding provision in the Act was to reduce litigation

in the courts as the offences under the Act were generally of technical nature. The section was brought into existence following the recommendations of the Sachar Committee which had suggested providing for realisation of fines through court proceedings by a system of penalty as provided in the Income-tax Act, 1961, by conferring power on the Company Law Board. In the absence of any specific restriction, the Company Law Board is entitled to consider the facts in each case and, taking into consideration the nature of violation found, consequent damage that may be caused to the public interest at large, and the relative merits of allowing the criminal proceedings to proceed, and is empowered to take decision in a given case whether to compound or not."

Scheme devised to benefit four shareholders of transferor company and to avoid tax : Scheme unfair, unreasonable and not for benefit of shareholders of transferee company

There was no provision in the Companies Act, 1956 requiring notice of the proposed scheme to be given to the income-tax authorities, and it was held in some cases that no such notice was required to be given.

For instance, in *Vinay Metal Printers P. Ltd., In re* [1996] 87 Comp Cas 266 (AP), a scheme of amalgamation was approved by shareholders of both companies. Petitions for sanction were filed and notices published in newspapers as well as issued to official liquidator and Registrar of Companies. The official liquidator filed his report and stated that there was no objection to the proposed amalgamation. However, the Registrar of Companies sought issuance of notice to the Income-tax Department to find out whether there was a motive of tax evasion by the proposed amalgamation. It was held that when the official liquidator had not stated that the transferor company was going to avoid tax or reduce its tax liability by the proposed amalgamation, there was no necessity to give any separate notice to the tax Department as public notice had already been published in the newspapers and the law did not require issuance of a separate notice to the tax Department.

In *Gabs Investments P. Ltd* v. *Ajanta Pharma Ltd.* [2019] 215 Comp Cas 293 (NCLT), the National Company Law Tribunal has dealt with the issue as to whether a scheme which had the only intention of tax avoidance should be sanctioned under section 230 of the Companies Act. The National Company Law Tribunal held :

"According to the proposed scheme of amalgamations and arrangement shares of transferee company would be allotted only to

> the four shareholders of the transferor company who were promoters of the transferee company or common promoters of both transferor and transferee company. The proposed scheme was a deliberate measure to avoid tax and resulted directly and indirectly, in the misuse or abuse of the provisions of the Income-tax Act, 1961. No provision was also made with regard to open offer to be made by the promoters of transferor company. The common promoters of the petitioner-companies were prima facie required to comply with the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011. According to the report of the Income-tax Department, the proposed scheme would amount to transfer or sale of shares. In view of these infirmities, no benefit accrued to the thousands of shareholders of the transferee company especially the retail shareholders of the transferee company. Therefore, the scheme was unfair, unreasonable and not in the public interest and could not be sanctioned as proposed."

Whether a trust can be prosecuted for cheque bouncing

The Indian Trusts Act defines "trust" as an obligation annexed to the ownership of property, and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another, or of another and the owner. The person who reposes or declares the confidence is called the "author of the trust" ; the person who accepts the confidence is called the "trustee" ; the person for whose benefit the confidence is accepted is called the "beneficiary" ; the subject-matter of the trust is called "trust-property" or "trust-money" ; the "beneficial interest" or "interest" of the beneficiary is his right against the trustee as owner of the trust property ; and the instrument, if any, by which the trust is declared is called the "instrument of trust".

In India, a number of statutes contain the general penal provision (GPP) under the heading "Offences by Companies" an identically worded provision regarding corporate criminal liability vicarious liability of directors and other company officers for the company's offences. It appears under the title "Offences by Companies" and provides that where an offence under this Act has been committed by a company, every person who, at the time the offence was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

In the *Explanation* appended to this provision that it is stated, inter alia, that for the purposes of this section, "company" means any body corporate, and includes a firm or other association of individuals.

In *Pratibha Pratishan* v. *Manager, Canara Bank*, AIR 2017 SC 1303, it was held that a trust is not a "person" as defined in the Consumer Protection Act, 1986, which defined the term "person" as follows :

"'person' includes,—

(i) a firm whether registered or not ;

(ii) a Hindu undivided family ;

(iii) a co-operative society ;

(iv) every other association of persons whether registered under the Societies Registration Act, 1860 (21 of 1860) or not."

In *K. P. Shibu* v. *State of Kerala* [2019] 215 Comp Cas 327 (Ker), the Kerala High Court considered the question whether the trustees of a trust (the petitioners) could not prosecuted under section 141 of the Negotiable Instruments Act, 1881 (which contains the abovementioned provision under the title "Offences by companies") on the ground that the "trust" was not an "association of individuals".

Relying on the Supreme Court's decision in *Pratibha Pratishan* v. *Manager, Canara Bank*, AIR 2017 SC 1303, the High Court has held that the "trust" was not a "body corporate" or an "association of individuals" as provided in the *Explanation* to section 141 of the Act. Therefore, no prosecution against the trustees, invoking the provisions under section 141 of the Act could be maintained. According to the complaint, accused Nos. 2 and 6 alone had signed the cheque. Since the petitioners had not signed the cheque, no successful prosecution against the petitioners under section 138 could be sustained and consequently, no purpose would be served even if the prosecution against the petitioners was permitted to be continued. The complaint and further proceedings against the petitioners were to be quashed.

Withholding from, or not sharing with, co-directors material information may amount to oppressive conduct

The principles of fiduciary duty and good faith demand that a director of a company, especially those who are in control of the management of the company, shares with his co-directors, material information pertaining to the business and affairs of the company. While where a director entered into a clandestine negotiation with a competing business, his removal was held to be justified on the grounds that his attempts to conceal the existence of the negotiations was destructive of any remnants of trust between the four[1], such a conduct should be considered to be oppressive to other directors-shareholders. Likewise, where a director enters into negotiations or a contract with an outsider in connection with the sale of the company's business or purchase of it by the director's individual company or a partnership and keeps other directors/shareholder in the dark about it, it should be considered to be oppressive to other directors-shareholders.

Hiding or withholding such information might constitute oppression of the minority by the majority. In *Scottish Co-operative Wholesale Society Ltd.* v. *Meyer* [1959] 29 Comp Cas 1 (HL) three out five directors of a subsidiary company were nominees of the holding company and they did not share some material information (that the holding company had decided to liquidate the subsidiary) and Viscount Simonds said (page 7) :

> "At this time the three nominee directors of the company were aware (Taylor by his own confession) of the policy of the society. It is undeniable that persons so placed may find themselves in a difficulty. But in all the evidence I have not been able to find the least trace that they regarded themselves as owing any duty to the company of which they were directors. They were the nominees of the society and, if the society doomed the company to destruction, it was not for them to put out a saving hand. Rather, they were to join in that work, and, when a frank and prompt statement to their co-directors might have enabled them to retrieve its fortunes, they played their part by maintaining silence. That it how they conducted the affairs of the company, and it is impossible to suppose that that was not part of the deliberate policy of the society. As I have said, nominees of a parent company upon the board of a subsidiary company may be placed in a difficult and delicate position. It is, then, the more incumbent on the parent company to behave with scrupulous fairness to the minority shareholders and to avoid imposing upon their nominees the alternative of disregarding their instructions or betraying the interests of the minority."

And Lord Denning said (page 31) :

> "Thus, when the realignment of shareholding was under discussion, the duty of the three directors to the textile company was to get the best possible price for any new issue of its shares (see per Lord Wright in *Lowry* v. *Consolidated African Selection Trust Ltd.* [1940] AC 648 (HL)) whereas their duty to the co-operative society was to obtain the new shares at the lowest possible price at par, if they could.

1. *Grace* v. *Biagioli* [2006] BCC 73 (CA).

Again, when the co-operative society determined to set up its own rayon department, competing with the business of the textile company, the duty of the three directors to the textile company was to do their best to promote its business and to act with complete good faith towards it; and in consequence not to disclose their knowledge of its affairs to a competitor, and not even to work for a competitor when to do so might operate to the disadvantage of the textile company (see *HIVAC Ltd.* v. *Park Royal Scientific Instruments Ltd.* [1946] 18 Comp Cas 16 (CA)) whereas they were under the self-same duties to the co-operative society. It is plain that, in the circumstances, these three gentlemen could not do their duty by both companies, and not do so. They put their duty to the co-operative society above their duty to the textile company in this sense, at least, that they did nothing to defend the interests of the textile company against the conduct of the co-operative society. They probably thought that 'as nominees' of the co-operative society their first duty was to the co-operative society. In this they were wrong. By subordinating the interests of the textile company to those of the co-operative society, they conducted the affairs of the textile company in manner oppressive to the other shareholders."

In a case decided by the House of Lords under section 459 of the English Companies Act, 1985, payment of management charges by a quasi-partnership company having two shareholders with 70 per cent. and 30 per cent. shareholding, to a company which was under the control of the majority shareholder-director, without consulting the minority was held to be unfairly prejudicial conduct towards the minority shareholder as it was in breach of the fiduciary duty of the majority shareholder-director[1].

Stamp duty on High Court's/Tribunal's order sanctioning a scheme of amalgamation or demerger

In amalgamation the undertaking comprising property, assets and liabilities, of one (or more) company (amalgamating or transferor company) are absorbed by and transferred to an existing company or a new company (amalgamated or transferee company). The transferor company merges into or integrates with the transferee company. The former loses its entity and is dissolved (without winding up).

Section 232(3)(a) of the Companies Act, 2013 provides that the Tribunal, after satisfying itself that the procedure specified in sub-sections (1) and (2) has been complied with, may, by order, sanction the compromise or

1. *Wilson* v. *Jaymarke Estates Ltd.* [2007] BCC 883 (HL).

arrangement or by a subsequent order, make provision for the following matters, namely : (a) the transfer to the transferee company of the whole or any part of the undertaking, property or liabilities of the transferor company from a date to be determined by the parties unless the Tribunal, for reasons to be recorded by it in writing, decides otherwise.

The transfer and vesting of the transferor-company's property, assets, etc., into the transferee company takes place by virtue of the Tribunal's order. Thus, the vesting of the property occurs on the strength of the order of the High Court sanctioning the scheme of amalgamation, without any further document or deed. Property includes every kind of property, rights and powers of every description.

In most of the States, stamp duty is levied on an order of the High Court (now the National Company Law Tribunal) sanctioning a scheme of amalgamation or demerger.

For instance, in Maharashtra, article 25(da) of Schedule I to the Bombay Stamp Act states that in respect of a "conveyance" which relates to the order of the High Court in respect of the amalgamation or reconstruction of companies under section 394 of the Companies Act, 1956 or under the order of the Reserve Bank of India under section 44A of the Banking Regulation Act, 1949, stamp duty is payable in the following manner on the true market value of the property which is the subject-matter of the conveyance :

> "ten (10) per cent. of the aggregate of the market value of the shares issued or allotted in exchange or otherwise and the amount of consideration paid for such amalgamation, provided that the amount of duty chargeable under this clause shall not exceed an amount equal to 0.7 per cent. of the aggregate of the market value of the shares issued or allotted in exchange or otherwise and the amount of consideration paid, for such amalgamation, whichever is higher."

Explanation III to article 25 states, in relation to a company whose shares are not listed, that : "For the purposes of clause (da), the market value of the shares in relation to the transferee company, whose shares are not listed or listed but not quoted on a stock exchange, means the market value of the shares issued or allotted with reference to the market value of the shares of the transferor company or as determined by the Collector after giving the transferee company an opportunity of being heard".

Further, the Government of Maharashtra has issued a notification No. Mudrank 2002/875/CR-173/M1, dated May 6, 2002 (the "May 6, Notification"), pursuant to which the maximum stamp duty chargeable under clause (da) of article 25 of Schedule I to the Bombay Stamp Act has been limited to Rs. 25 crores with effect from May 1, 2002.

Under the Bombay Stamp Act, section 2(g)(iv), stamp duty is payable on, inter alia, "every order made by the High Court under section 394 of the Act in respect of amalgamation or reconstruction of companies by which property, whether movable or immovable, or any estate or interest in property to, or vested in, any other person, inter vivos, and which is not otherwise specifically provided for by Schedule I". When a scheme of amalgamation is sanctioned by the High Court, there is passed one single, composite order on which stamp duty is payable and, therefore, if in the present case a single order sanctioning the scheme of amalgamation of companies in the three phases, as proposed, is passed, there will be payable stamp duty in accordance with article 25(da) of Schedule I to that Act. In such a case, the limit of Rs. 25 crores also will apply. However, if the High Court requires three separate schemes to be presented, the stamp duty will be payable on three orders.

In a case of issue of shares, the stamp duty payable under the Bombay Stamp Act on the shares will be paid only by the transferee company and not by the transferor company. Such stamp duty is payable (if it is payable) on the market value of the shares issued and allotted in exchange for shares of the transferor company. Going by experience, the Stamp Superintendent would ask for a valuation certificate and determine the total value of the shares allotted according to the valuation of the shares as per valuation report/certificate of a chartered accountant for the purpose of share exchange ratio. For example, if the chartered accountant fixes Rs. 50 per share of Rs. 10 as the value of the shares of the transferee company, the Stamp Superintendent would take Rs. 50 per share as the value of each share and calculate the amount of duty taking into consideration the total number of shares allotted by the transferee company to the shareholders of the transferor company. Since the company issuing the shares (the transferee company) is not a listed company and hence the market value of its share is not available, the aforesaid basis is usually adopted to determine the amount of duty payable.

The number of shares issued or allotted in exchange or otherwise means the number of shares of the transferor company accounted as per exchange ratio as on the appointed date.

The constitutional validity of this levy was challenged by several companies. But by its common order, a Division Bench of the Bombay High Court in *Li Taka Pharmaceuticals Ltd.* v. *State of Maharashtra* [1998] 91 Comp Cas 871 (Bom) upheld its constitutional validity. An appeal against this order is pending in the Supreme Court. Meanwhile, however, the Supreme Court has held in *Hindustan Lever* v. *State of Maharashtra* [2003] 117 Comp Cas 758 (SC) that the amalgamation scheme sanctioned by the court would be an "instrument", within the meaning of section 2(i) of the Bombay Stamp Act, 1958, which transfers the properties from the transferor company to the transferee company and the State Legislature has the legislative competence to impose stamp duty on the order of amalgamation passed by a court. Further, it was held that the word "inter vivos" appearing in section 5 of the Bombay Stamp Act, in the context of section 394 of the Companies Act would include within its meaning a transfer between two "juristic persons" or a transfer in which a "juristic person" is one of the parties.

In *Gemini Silk Ltd.* v. *Gemini Overseas Ltd.* [2003] 114 Comp Cas 92 (Cal), the Calcutta High Court held that a court order sanctioning a scheme of reconstruction or amalgamation under section 391/394 is covered by the definition of the words "conveyances" and "instrument" under the Stamp Act and was, therefore liable to stamp duty. The Registrar of Companies was accordingly directed by the High Court not to take on record any order sanctioning a scheme until the order has been duly stamped. However, this case has been overruled by the Division Bench of Calcutta High Court in the case of *Madhu Intra Ltd.* v. *Registrar of Companies* [2006] 130 Comp Cas 510 (Cal) relying on *New Central Jute Mills Co. Ltd.* v. *River Steam Navigation Co. Ltd.* [1959] 29 Comp Cas 357 (Cal), where the learned judges have held that the transfer of assets and liabilities from the transferor company to the transferee company takes place by virtue of sub-section (2) of section 394 without any further act or deed.

Upholding the constitutional validity of the levy of stamp duty on orders under section 391/394, the Supreme Court has held in *Hindustan Lever* v. *State of Maharashtra* [2003] 117 Comp Cas 758 (SC) that an order passed by the court under section 394 of the Companies Act sanctioning a scheme of amalgamation of companies is based upon the compromise between two or more companies. It is an instrument which transfers properties and would fall within the definition of section 2(1) of the Bombay Stamp Act which includes every document by which any right or liability is transferred. The State Legislature would have the jurisdiction to levy stamp duty under entry 44, List III of the Seventh Schedule to the Constitution of India and prescribe rates of stamp duty under entry 63, List II.

In *Dalgreen Agro P. Ltd.* v. *State of West Bengal* [2019] 215 Comp Cas 452 (Cal), the stamp duty was payable in West Bengal under article 23A in Schedule I to the Indian Stamp Act, which is as follows (page 457) :

"*Description of investments*	*Proper stamp duty*
23A. Conveyance, in respect of amalgamation, merger, reconstruction, or demerger, of companies, other than amalgamation, merger, reconstruction or demerger, of two banking companies or a banking company with a non-banking financial company, executed on the basis of decree or final order of any civil court or every order made by the Tribunal under section 394 of the Companies Act, 1956 (1 of 1956), as defined by section 2(10), not being a transfer charged or exempted under No. 62, on the market value of the property which is the subject-matter of the conveyance, when the property of the transferor company located in the State of West Bengal is transferred to the transferee company by way of such amalgamation, merger, reconstruction, or demerger of companies under the decree of final order of any civil court or every order of the Tribunal under section 394 of the Companies Act, 1956 : Provided that on and after the constitution of the National Company Law Tribunal, the expression 'High Court' shall be read as 'Tribunal'.	The same duty as a Conveyance (No. 23) on the aggregate of the market value of the shares issued or allotted, in exchange or otherwise, and the amount of consideration paid— (a) by the transferee company, for such amalgamation or merger : Provided that the amount of such duty chargeable under this article shall not exceed— (i) an amount equal to two per centum of the true market value of the immovable property located within the State of West Bengal of the transferor company, or (ii) an amount equal to half per centum of the aggregate of the market value of the shares issued or allotted, in exchange or otherwise, and the amount of consideration paid by such transferor company, for such amalgamation, whichever is higher ; (b) by the resulting company, for such reconstruction or demerger : Provided that in case of reconstruction or demerger, the amount of such duty chargeable under this item shall not exceed— (i) an amount equal to two per centum of the true market value of the immovable property located within the State of West Bengal of the transferor company, or (ii) an amount equal to half per centum of the aggregate of the market value of the shares issued or allotted, to the resulting company and the amount of consideration paid for such demerger, whichever is higher ;"

A scheme of amalgamation between the transferor and the transferee companies was sanctioned and the authorities adjudicated the stamp duty payable in respect of the scheme of amalgamation, by the writing dated February 8, 2018 at Rs. 17,65,500. On a writ petition contending that since the transferee company was not the beneficiary of any immovable property being transferred to it by virtue of sanction granted to the scheme of amalgamation, the stamp duty for a conveyance of an immovable property was not payable by the transferee company and that article 23A prescribed half per centum of the value of the issued, paid-up and subscribed share capital of the transferee company as the stamp duty payable by the transferee company.

But the High Court held that the transferor company did not have any immovable property located within the State of West Bengal. The issued share capital of the transferee company was Rs. 13,75,00,000. The value paid by the transferee company was Rs. 2,94,25,000. Therefore, the amount of stamp duty payable would be half per cent. of Rs. 2,94,25,000. None of the situations prescribed in article 23 were attracted in the facts of the case. The authorities had arrived at a figure, after calculating the value paid by the transferee company to be at Rs. 2,94,25,000. The authorities had applied 6 per cent. rate on the sum of Rs. 2,94,25,000 to arrive at the figure of Rs. 17,65,500. The rate applicable would be half per cent. on the value paid by the transferee company. The writing dated February 8, 2018 was to be quashed. The registering authority had to allow the petitioner to present the document accompanied by stamp duty payable at the rate of half per cent. on Rs. 2,94,25,000.

Whether section 241 is applicable to producer companies

Section 465(1) of the Companies Act, 2013 provides that the Companies Act, 1956 and the Registration of Companies (Sikkim) Act, 1961 shall stand repealed ; and the first proviso states that the provisions of Part IXA of the Companies Act, 1956 (1 of 1956) shall be applicable mutatis mutandis to a producer company in a manner as if the Companies Act, 1956 had not been repealed until a special Act is enacted for producer companies.

In *Kozhikode Coconut Farmers Producer Co. Ltd.* v. *Moolath Mannil Sreenivasan* [2019] 215 Comp Cas 514 (NCLAT) the question before the National Company Law Tribunal was whether a petition filed under section 241 of the Companies Act, 2013 by a member of a producer company was maintainable. The National Company Law Tribunal was of the view that such a petition was maintainable. But reversing the National Company Law Tribunal's decision, the National Company Law Appellate Tribunal held that the provisions of Part IX-A of the Companies Act, 1956 shall be applicable mutatis mutandis to a producer company as if the Companies Act, 1956 had not been repealed until a special Act is enacted for producer companies.

In the National Company Law Appellate Tribunal's view, the provisions of sections 241 and 242 of the Companies Act, 2013 could not be invoked for settlement of disputes regarding oppression and mismanagement of a "producer company". Such disputes would continue to be resolved through conciliation or arbitration. The Tribunal had narrowed down the definition of "dispute" for purpose of section 581ZO by misinterpreting the *Explanation* which only sought to include certain types of disputes within the ambit of "dispute" as defined in the provision. The *Explanation* could not be read in a manner so as to restrict the meaning of "dispute" as contemplated under the section in the context of objects of the producer company and its being treated as a class apart. The Tribunal had proceeded to return a finding that the dispute alleged in the petition did not fall under the *Explanation* of "dispute" thereby usurping the jurisdiction vested in the "arbitrator" under section 581ZO(2) of the Act. The order could not be sustained and was liable to be set aside.

Whether a director named in the articles as permanent director can be removed

In a petition under section 241 of the Companies Act, 2013 before the National Company Law Tribunal in *Puttanarayanappa Nadikeraiah* v. *Bindu Labels P. Ltd.* [2019] 215 Comp Cas 524 (NCLT), the respondent-company was a closely held family company, in which respondent No. 2 held 70 per cent. shareholding of the company and the remaining 30 per cent. was held by all the petitioners together. The petitioners were also directors of the company. The petition was filed under sections 397 and 398 of the Companies Act, 1956, inter alia, to declare that the resignation filed by the petitioner was illegal, null and void, that the petitioners and the second respondent were first and permanent directors of the company and that therefore, they could not be removed and the alleged resignation of the first petitioner was also denied.

This issue often figures in petition under section 241 when removal of a director is challenged by a minority shareholder who also happens to be on the board of the company and who is removed by the majority by resorting to section 169 of the Companies Act, 2013 (corresponding to section 284 of the Companies Act, 1956).

Section 169 of the Act deals with "removal of directors". It empowers shareholders of a company to remove any director of their company. This is one of the most crucial powers conferred on the shareholders by the Act. This section enables the majority of the shareholders of a company to assert themselves against the directors, if need be so that the shareholders may remove them and as and when they decide to change directors, they can remove the existing ones and appoint in their place others by a resolution with simple majority of votes, i. e., an ordinary resolution.

This section corresponds with section 284 of the Companies Act, 1956 and 184 of the U. K. Companies Act of 1948 and section 303 of the Act of 1985. The U. K. provision gives this section an overriding effect vis-a-vis articles of a company by using a non obstante clause. The Indian provision does not contain any words suggesting overriding effect, but the Indian Act contains a provision in its section 9 that gives all its provisions an overriding effect as against the memorandum and articles of a company. Thus articles of no company can have a provision that contradicts section 284. This is true of private companies.

A person appointed as a life director or permanent director by the articles or by an agreement is nevertheless removable by the company in general meeting and has no security of tenure in office. While the shareholders have no power, apart from that given in the statute or the articles, to intervene in the management of the company's affairs, this section is designed to enable them to control the directors by their removal (*Tarlok Chand Khanna* v. *Raj Kumar Kapoor* [1983] 54 Comp Cas 12 (Delhi)).

In *Life Insurance Corporation of India* v. *Escorts Ltd.* [1986] 59 Comp Cas 548, 632 (SC), the Supreme Court said :

> ". . . the only effective way the members in general meeting can exercise their over the directorate in a democratic manner is to alter the articles so as to restrict the powers of the directors for the future or to dismiss the directorate and appoint others in their place. The holders of the majority of the stock of a corporation have the power to appoint, by election, directors of their choice and the power to regulate them by a resolution for their removal. And, an injunction cannot to restrain the holding of a general meeting to remove a director and appoint another."

Does section 284 give absolute right as to removal of director ? The answer to this question is in the negative. The statutory right given by section 284 is subject to the "just and equitable" principle and equitable considerations underlying section 433(f) and section 397. This has been so held in many cases. The following observations of Plowman J. in *Westbourne Galleries Ltd., In re* [1970] 3 All ER 374 (Ch D) ; [1971] 41 Comp Cas 754 (Ch D) (which the House of Lords confirmed in *Ebrahimi* v. *Westbourne Galleries Ltd.* [1972] 2 All ER 492 (HL) ; [1973] AC 360 (HL)) are apposite to answer the above question :

> "As I have already said, counsel for the respondents submitted that section 184 gives an absolute right to shareholders to remove directors, that a director removed under that power is lawfully removed and that the lawful removal of a director cannot be a ground for a

winding up order even in a quasi-partnership case. I cannot accept that argument. The fallacy in it, in my judgment, is that while no doubt the petitioner was lawfully removed, in the sense that he ceased in law to be a director, it does not follow that in removing him the respondents did not do him a wrong. In my judgment, they did do him a wrong, in the sense that it was an abuse of power and a breach of the good faith which partners owe to each other to exclude one of them from all participation in the business on which they have embarked on the basis that all should participate in its management. The main justification put forward for removing him was that he was perpetually complaining, but the faults were not all on one side and, in my judgment, this is not sufficient justification. For these reasons, in my judgment, the petitioner therefore has made out a case for a winding up order."

Statutory right is subject to equitable considerations

While it is the shareholders' legal or statutory right to remove directors according to section 284 and there is no impediment in removing a director by following the procedure laid down in that section, equitable considerations enter the arena when it comes to removal of a director of a private company which is a family company or a quasi-partnership type company and equitable considerations override the legal right. It, therefore, often happens that when challenged in proceedings under section 397, the removal faces the brunt of equitable considerations and can be set aside by the Company Law Board in proceedings under section 397. This is now well established in company law. In such a case, the principles applicable to the winding up of a company on just and equitable grounds under section 433(f) of the Act apply and it is very rarely that the removal is upheld by the Company Law Board.

Section 241 (corresponding to section 397 of the 1956 Act) has proved to be a powerful weapon for minority shareholders, particularly in the case of quasi-partnerships. In such companies, minorities who are excluded from management participation or who unfairly suffer loss as a result of wrongdoing by directors or majority shareholders may get relief under the section.

There cannot be any doubt whatsoever that the acts of omission and commission on the part of a member of a company should be qua the management of the company, but the just and equitable test, which is applicable in a case for winding up of a company, is not totally outside the purview of section 397 of the Act. The function of the Company Law Board in such matters is first to see how the interests of the company vis-a-vis shareholders can be safeguarded. The Company Law Board must also make an endeavour to find out whether an order of winding up will serve the interests of the company or subvert them. The Company Law Board may not shut its doors only on a sheer technicality even if it is found as of fact that unless the jurisdiction under section 402 of the Act is exercised, there will be a complete mismanagement in regard to the affairs of the company (*M. S. D. C. Radharamanan* v. *M. S. D. Chandrasekara Raja* [2008] 143 Comp Cas 97 (SC)).

In applying section 241, two factors are of considerable importance. The first is the terms of association of the company contained normally in the company's articles or perhaps collateral agreements between the shareholders. The second factor is the established rules of equity which subjected strict legal rights to equitable considerations. These equitable considerations can involve promises between the parties which are not necessarily independently enforceable (*Buckley on the Companies Acts*, 15th edition, Volume II, paragraph 459.23).

As has been held in a number of cases, section 397 being a protective or remedial provision (mainly) aimed at protecting minority shareholders against the majority power and adopting equitable considerations, has to be construed widely. Accordingly the Company Law Board is expected to apply equitable considerations copiously with a view to protecting the interests of the minority shareholder when some prejudice is caused to him as a result of use (or abuse) of the majority power, going beyond the legality or illegality of an action, the aim of the exercise underlying section 397 proceedings being to ascertain whether the action (of the majority) has resulted in prejudice as against infringement of legal rights of the minority.

A private company is considered to be a quasi-partnership and is nothing but a partnership in substance or in the guise of a private company if it satisfies the tests laid down by courts and the Company Law Board for a company to qualify as quasi-partnership, namely :

(a) a pre-existing partnership ;

(b) the company as a successor to the partnership ;

(c) all the partners becoming shareholders of the company ;

(d) all the shareholders were the subscribers to the memorandum of association ;

(e) all the shareholders were named as the first directors and still are directors of the company ; and

(f) all the shareholders have equal shareholding.

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