
(1996) 01 AP CK 0016

In the Andhra Pradesh High Court

Case No : Company Petition No. 27 of 1988

C.N. Shetty

APPELLANT

Vs

Hillock Hotels Pvt. Ltd. and Others

RESPONDENT

Date of Decision : 22-01-1996

Acts Referred:

Companies Act, 1956 — Section 210, 283(1), 397, 398, 400

Citation : (1996) 87 CompCas 1

Hon'ble Judges : S. Dasaradharama Reddy, J

Bench : Single Bench

Advocate : S. Ravi, for the Appellant; V.V.S. Rao, for the Respondent

Judgement

S. Dasaradha Rama Reddy, J.—This is a petition filed by one of the shareholders of the first respondent-company, Hillock Hotels Private Limited, Visakhapatnam, under sections 397 and 398 of the Companies Act, 1956, alleging oppression, exclusion and mismanagement by the managing director, the second respondent, and other director, respondent No. 3. Respondent No. 2 is the managing director of the company, while the third respondent, his wife, is a director and respondent No. 4, their daughter and respondents Nos. 5 and 6, their sons are shareholders.

2. The averments in the petition are as follows : The authorised share capital of the company formed on May 13, 1980, was Rs. 10,00,000, divided into 1,000 equity shares of Rs. 1,000 each. The issued, subscribed and paid-up share capital as on September 30, 1985, was Rs. 1,10,000 divided into 110 equity shares of Rs. 1,000 each. The main object of the company, as per exhibit A-1 memorandum of association, is to carry on the business of a hotel. Respondents Nos. 2 and 3 who originally subscribed five shares each at the time of formation of the company were appointed as directors under article 12 of the articles. By virtue of article 19, respondent No. 2 was appointed as the managing director. The petitioner was inducted as a director of the company in its first meeting on June 7, 1980, and five shares were allotted to him (exhibit A-2). Thereafter when the allotment of shares took place on March 9, 1981, he was allotted 45 shares

(exhibit A-3). The shareholding of the second and third respondents was 25 each. The company (not petitioner, which is evidently a typographical mistake) purchased a plot of land in Dasapalla Hills, Visakhapatnam, admeasuring 1,300 square yards by sale deed dated July 29, 1980, for Rs. 27,000. The value of the land has appreciated to more than Rs. 10,00,000. Even till 1987 construction of the hotel was not commenced. In the year 1987, the managing director had obtained permission of the municipal corporation of Visakhapatnam, for the construction of a multi-storeyed apartment on the plot of land. At this stage the second respondent entertained the idea of excluding the petitioner from the management of the company and stopped sending notices of the meetings of the board of directors and also of the general body to the petitioner. Respondents Nos. 2 and 3 allotted 150 additional shares, to themselves, their daughter and two sons, who were allotted 30 each. Consequently, the petitioner who, until then was holding shares at par with respondents Nos. 2 and 3, has been reduced to a miserable minority. No shares were offered to the petitioner in accordance with the proportional representation which is the accepted mode in joint ventures. The petitioner goes on to say that he apprehends that respondents Nos. 2 and 3 are entering into agreements with prospective buyers and large amounts of money may pass without being accounted for in the books of the company. The action of the respondents lacks probity and fair conduct and constitutes acts of oppression and mismanagement. As the initial shareholding of the petitioner on the one hand, and that of respondents Nos. 2 and 3 on the other hand were equal and the company is a private limited company, the nature of relationship as between the petitioner and respondents Nos. 2 and 3 must be regarded as that which obtains in a partnership, and, therefore, any breach of faith or trust must automatically entail the winding up of the company by applying the principles of dissolution of a partnership. But as the winding up of the company will be unfair and prejudicial to the interests of the petitioner, the petitioner seeks for the following reliefs :

That the additional issue of shares to respondents Nos. 2 to 6 purportedly effected on March 24, 1988, to the extent of 150 shares be set aside as illegal, null and void; that the second respondent be removed from the office of the managing director of the company; that the articles of association of the company be amended to have proportionate representation for the petitioner on the one hand and respondents Nos. 2 and 3 on the other hand, with casting vote for neither group; that the appointment of respondents Nos. 4 to 6 as directors, if any, be set aside; that the petitioner be allowed to purchase the shares of respondents Nos. 2 and 3 at the value to be fixed by this court and grant any relief.

3. The company petition was filed on April 18, 1988, and pursuant to the warrant of commission issued by this court, on April 29, 1988, Sri P. Venkateswarlu, advocate, who was appointed as the Commissioner, filed a report along with the inventory showing 16 items which consist of registers, the minutes books of the proceedings of the board of directors and the annual general meetings, etc.

Documents however were not directed to be seized.

4. The second respondent filed a counter stating that the company is not a joint venture of in the nature of a partnership. The extent of the land purchased is 1,361 square yards and not 1,300 square yards and the value under three sale deeds was Rs. 81,660. In accordance with the decision of the board to take up the construction of the residential complex, the second respondent applied for necessary permission to the municipal corporation of Visakhapatnam. The allegation that he has excluded the petitioner from the management of the company is false, motivated and misleading. On the other hand, the petitioner was never taking any interest in the management of the company and was not attending any meetings in spite of notices. As finances were required, additional shares were issued in accordance with the articles and it was always open to the petitioner who is a shareholder to offer to purchase any number of shares. There is absolutely no oppression or mismanagement or lack of probity or of fair conduct. The petition is nothing but an abuse of the process of law.

5. No separate counters were filed by respondents Nos. 3 to 6 and it is not clear whether this counter was filed on behalf of respondents Nos. 3 to 6 also. Notice was issued to the Central Government as contemplated u/s 400 of the Companies Act. On the pleadings, the following issues have been framed by this court on October 20, 1989 :

1. Whether the respondent-company is in the nature of a joint venture partnership between the petitioner and the third respondent?

2. Whether the issue of additional share capital in March, 1988, suffers from any illegality and has been done by the respondents for their exclusive benefit and is an act of oppression?

3. Whether the company has undertaken construction of residential flats and if so, is it within the scope and authority conferred by the memorandum of association?

4. Whether the affairs of the company are being conducted in a manner oppressive to the interests of the petitioner for the reasons mentioned in the petition?

5. What relief to be granted in this petition?

6. On behalf of the petitioner, the petitioner himself was examined as PW-1, while one P.V. Satyanarayana Murthy, manager of the first respondent-company, was examined on behalf of the respondents. Exhibits A-1 to A-4 were marked on behalf of the petitioner, while on behalf of the respondents, exhibits B-1 to B-36 were marked. It is significant to note that respondent No. 2 has not chosen to give evidence though he was cited as one of the witnesses in the memo filed by counsel for the respondents. It is only the manager who gave evidence and that too on behalf of the company.

7. Issue No. 1 : Whether the respondent-company is in the nature of a joint venture partnership between the petitioner and the third respondent?

8. The issue may be recast as follows :

Whether the respondent-company is in the nature of a joint venture partnership between the petitioner and respondent No. 2?

9. It is undisputed that at the time of incorporation of the company, respondent No. 2 and his wife held five shares each. On June 7, 1980, the petitioner was allotted five shares and co-opted as a director. On October 31, 1980, two outsiders, viz., Gupta and Raju, were allotted five shares each and co-opted as directors. On March 9, 1981, the petitioner was allotted 45 shares, while respondents Nos. 2 and 3 put together were allotted 40 shares. Thus out of the total of 110 shares, 50 shares were held by the petitioner, 50 shares by respondents Nos. 2 and 3 while 10 shares were held by Gupta and Raju. In other words, the shareholding of the petitioner and respondents Nos. 2 and 3 was nearly 45.5 per cent. each.

10. Mr. S. Ravi submits that though earlier there was no partnership firm, if the corporate veil is pierced, the company is in substance a partnership firm. He submits that in view of the equal shareholding between the petitioner and respondent No. 2 representing his family and the outside shareholders being an insignificant minority and in view of the fact that it is a private limited company, the company has to be treated in substance as a quasi-partnership.

11. The leading case on this subject is *Ebrahimi v. Westbourne Galleries Ltd.* [1972] 2 All ER 492 : [1973] AC 360, which has been noticed by the Supreme Court in *Hind Overseas Private Limited Vs. Raghunath Prasad Jhunjhunwalla and Another*, , where it is stated at page 104 as follows :

"When more than one family or several friends and relations together form a company and there is no right as such agreed upon for active participation of members who are sought to be excluded from management, the principles of dissolution of partnership cannot be liberally invoked. Besides it is only when shareholding is more or less equal and there is a case of complete deadlock in the company on account of lack of probity in the management of the company and there is no hope or possibility of smooth and efficient continuance of the company as a commercial concern, there may arise a case for winding up on the just and equitable ground. In a given case the principles of dissolution of partnership may apply squarely if the apparent structure of the company is not the real structure and on piercing the veil it is found that in reality it is a partnership."

12. These two decisions were summarised succinctly by Justice K.A. Swamy (as he then was) at page 897 of *Synchron Machine Tools P. Ltd. and others Vs. U.M. Suresh Rao*, , (though this decision was reversed by the Division Bench on other points in *Synchron Machine Tools P. Ltd. and others Vs. U.M. Suresh Rao*, on this

point, it was affirmed thus (p. 897) :

"In order to determine whether in reality the company is a partnership, the following norms are to be satisfied :

- (i) shareholdings should be more or less equal;
- (ii) the company must have been formed or continued on the basis of a personal relationship involving mutual confidence;
- (iii) an agreement or understanding that all or some of the shareholders shall participate in the conduct of the business;
- (iv) restriction on the transfer of shares so as to ensure the continuation of the element of mutual confidence between the shareholders"

13. The first test is satisfied in this case since the shareholding of the petitioner and respondent No. 2 was equal till 1987, seven years from the formation of the company. The second test is also satisfied since the company was formed on the basis of the personal relationship involving mutual confidence between the petitioner and respondent No. 2. As already seen outsiders hold an insignificant minority of shares of 9 per cent. The petitioner and respondent No. 2 being also directors were participating in the conduct of the business. Regarding the transfer of shares there are restrictions imposed in the article (exhibit A-1). Clauses 2A, 4, 5 and 6 of the articles read as follows :

"Clause 2A. - The right to transfer shares shall be restricted as hereinafter provided.

Clause 4. - The person proposing to transfer any share or shares hereinafter called the "proposing transferor" shall give notice in writing to the company that he desires to transfer the same. Such notice shall constitute the company as his agent for the sale of the share or shares to any member of the company or to any person empowered by the directors as provided hereinafter at the value agreed to the proposing transferor and the transferee or at the fair value to be determined as hereinafter provided. The transfer notice shall not be revocable except with the sanction of the directors.

Clause 5. - In case no sum be specified in the transfer notice as the fair value or in case the "proposing transferor" and the purchasing member, do not agree as to the fair value of a share, such fair value shall be determined by the board of directors in consultation with the auditors of the company.

Clause 6. - The directors may in their absolute and uncontrolled discretion refuse to register any transfer of shares to a transferee of whom they do not approve."

14. Thus all the four tests are satisfied in the instant case.

15. Mr. V.V.S. Rao relies on the very same decision in Hind Overseas Private Limited Vs. Raghunath Prasad Jhunjhunwalla and Another, for the proposition that the company cannot be treated in substance as a firm. As both counsel are

relying on the same decision, it is necessary to examine in detail the facts in that case. The company there was formed first with R.P. Jhunhunwalla (RPJ) and Anil Chandra Datta who was an employee of V.D. Jhunhunwalla (VDJ) who arranged the entire finance but remained in the background. Datta soon resigned and ultimately there were 19 shareholders, 9 headed by RPJ and 10 headed by VDJ - the RPJ group holding 1,875 shares and the VDJ group holding 3,125 shares. The stake of the VDJ group in the company was Rs. 63,00,000 as opposed to the stake of the RPJ group amounting to Rs. 1,87,000.

16. The High Court held that the company was in substance a partnership venture based on the following reasons (at page 108 of 46 Comp Cas) :

"1. The original idea was to start a partnership venture and that idea was given ultimately the shape of a private company.

2. The Sir Khata account shows that for starting on a partnership venture the parties set up a private company.

3. The shareholding shows division amongst two family groups.

4. There was no denial by the appellants of a specific averment of the respondents that the company was in substance a partnership.

5. The respondents were all along functioning as working partners and the respondent, VDJ, was the financial partner."

17. Reversing the decision, the Supreme Court held that the company cannot be treated in substance as a partnership firm and gave the following reasons :

With regard to the first reason, it was held that there was no active contemplation about the forming of a partnership before forming the company, and although there might have been discussion about the advantages and disadvantages of the partnership vis-a-vis a private limited company, no time was lost in deciding to form a company. Regarding the second reason regarding the Sir Khata account it was held that it only showed that the joint account was opened for the purpose of formation of the company and the same was closed after such formation and it does not indicate any understanding as to the management of the company by any group of shareholders. Regarding the reasoning about the division of shareholding amongst two family groups, the Supreme Court held that it cannot be the sole reason to hold that the company takes the image of a partnership and that the very fact that after the discussion the parties deliberately abandoned the idea of formation of a partnership would show that there was no intention to carry on the business as partners. It was also found that VDJ has categorically denied the allegation of RPJ that the company was in substance a partnership. With regard to the last reason, the Supreme Court held that the fact that RPJ and his associates were functioning as working partners and VDJ was a financial partner is a neutral factor. The Supreme Court did not lay down that in order to hold that a company in substance is a partnership, there should be earlier a partnership which must be

converted later into a company. In fact the following observations indicate to the contrary (at page 107 of 46 Comp Cas) :

"Is this company, in substance a partnership or in the image of a partnership as claimed? We may now address to this aspect strenuously emphasised Mr. Sen. If, as in Ebrahimi's case [1973] AC 360, there had been an earlier partnership and the partners later on formed into a company, the matter would have stood on a different footing. In the present case, however, we do not find any special features which would unquestionably lead to the conclusion that the company is in substance a partnership. On the other hand, the following aspects are noteworthy."

18. The Division Bench of the Karnataka High Court in Synchron Machine Tools P. Ltd. and others Vs. U.M. Suresh Rao, held that the principles of special relationship between the members of private limited company cannot be limited cases of partnership converted into partnership companies and gave certain instances. The Division Bench of the Karnataka High Court disagreed with the view of the Division Bench of the Madras High Court in V.M. Rao and Others Vs. Rajeswari Ramakrishnan and Others, in this regard. I respectfully agree with the view of the Karnataka High Court. The distinguishing features of the Supreme Court case are : That the company was formed by Anil Chandra Datta and RPJ. Subsequently, VDJ became director and Anil Chandra Datta resigned and, ultimately, there were two family groups RPJ group holding 1,875 shares and VDI group holding 3,125 shares. In the instant case though there was no partnership firm earlier and the company was formed by respondent No. 2 only along with his wife, within one month thereafter, the petitioner became a director along with respondents Nos. 2 and 3 holding five shares as against 10 held by respondents Nos. 2 and 3 and within one year thereafter the shareholding of the petitioner and respondents Nos. 2 and 3 became equal each holding 45.45 per cent. The balance insignificant 9.1 per cent. was held outsiders. Thus the company in substance is a partnership and this issue is held in favour of the petitioner.

19. Issue No. 2. - Whether the issue of additional share capital in March, 1988, suffers from any illegality and has been done by the respondents for their exclusive benefit and is an act of oppression?

20. It may be noted that the additional share capital was issued admittedly on December 2, 1987, and not in March, 1988. As seen earlier, originally the petitioner and respondent No. 2 (together with respondent No. 3) held 45.45 per cent. shareholding, i.e., 50 shares each. On December 2, 1987, respondents Nos. 2 and 3 were allotted 30 shares each while respondents Nos. 4, 5, and 6 who are their children were allotted 30 shares each. As a result of this the total shares became 260 and the petitioner's shareholding was 19.23 per cent. (50 shares), while the shareholding of respondents Nos. 2 to 6 put together was 76.92 per cent. (200 shares) and the balance of 3.85 per cent. (10 shares) belonged to outsiders. The petitioner says in his evidence that no offer was made to him to allot the additional shares and he was not invited to the board meeting where the

decision to issue the shares was taken. He further says that as no hotel construction was commenced, there was no necessity to raise funds by way of share capital. It is submitted by RW-1 that at the time of increase of capital in the year 1987, no shares were offered to the petitioner. It is admitted by RW-1 that there is a further increase of capital in the year 1992 after the filing of the company petition and the shareholding of respondents Nos. 2 to 6 has increased to 455 shares including the 5 shares transferred by A.S. Gupta, while the petitioners shareholding stood at 50 only. RW-1 has not said that any offer was given to the petitioner in the year 1992. Of course, he denied the suggestion that the non-offer was with a view to convert the petitioner into minority. Thus, there is sufficient evidence on record to show that the shareholding of respondents Nos. 2 to 6 has been abnormally increased and the petitioner has been denied the right of applying for the allotment of shares and that this has been done for the exclusive benefit of the family of respondent No. 2. There is also nothing stated in the counter filed by the respondents (assuming that the second respondent filed the counter on behalf of respondents Nos. 2 to 6) regarding the necessity to issue additional capital, though in the evidence of RW-1 this has been adverted to. Even the so-called reasons given in the evidence, namely, that money is required for construction is not valid since no effort has been made by the company to construct the hotel which is the main object of the company. On the other hand, the evidence is that the company started constructing a multi-storeyed residential complex. Mr. V.V.S. Rao, learned counsel for the respondents, contends that issuing additional shares per se reducing the petitioner to a minority is not necessarily an act of oppression and relies on the decisions of the Supreme Court in *Shanti Prasad Jain Vs. Kalinga Tubes Ltd.*, and *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.* [1981] 51 Comp Cas 743 SC.

21. In *Shanti Prasad Jain Vs. Kalinga Tubes Ltd.*, , new shares were allotted to outsiders and not to the existing shareholders, overruling the view of the minority shareholders that the new shares should be allotted to existing shareholders only. In those circumstances, the Supreme Court held that the fact that one of the groups might be able to get the support of the holders of the new shares did not necessarily mean oppression of one of the shareholders and that the allotment of shares to their friends was not also of any significance since in any case if the shares had to be issued privately they were bound to go to the friends of the directors. Thus this decision is of no assistance to the respondents since in the present case the allotment is not to outsiders and there was no need for raising money.

22. The next decision is *Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.* [1981] 51 Comp Cas 743 (SC) wherein it was held that every illegality may not be per se oppressive; that an isolated act which is contrary to law may not necessarily and by itself support the inference that the law was violated with a male fide intention or that such violation was burdensome, harsh and wrongful; but a series of illegal acts following upon one

another can, in the context, lead justifiably to the conclusion that they are a part of the same transaction, the object of which is to cause or commit the oppression of persons against whom those acts are directed; that the test is whether the issue of shares is simply or solely for the benefit of the directors; that if the shares are issued in the larger interests of the company, the decision to issue shares cannot be struck down on the ground that it incidentally benefited the directors in their capacity as shareholders. It was also held that the fact that by the issue of shares the directors succeed, also or incidentally, in maintaining their control over the company or in newly acquiring it, does not amount to an abuse of their fiduciary power; that what is considered objectionable is the use of such powers merely for an extraneous purpose like maintenance or acquisition of control over the affairs of the company. The Supreme Court further laid down that the additional shares can be issued not only when there is need to raise additional capital but also for creating sufficient number of shareholders to enable the company to exercise statutory powers or to enable it to comply with the legal requirements. On the facts of that case, it was found that the issue of rights shares to Indian shareholders only, that too at par, was made by the directors for the purpose of complying with the requirements of the Foreign Exchange Regulation Act and the directives issued by the Reserve Bank of India under the Act, that the fact that while discharging their duty they incidentally trespassed upon the interests of the majority, could not invalidate their action, that the conversion of the existing majority into a minority was a consequence of what the directors were obliged lawfully to do and that such conversion was not the motive force of their action.

23. This decision also does not help the respondents since in the instant case there is no necessity for issue of additional share capital since the company did not do anything towards construction of the hotel and on the other hand the additional share capital was issued to procure funds for construction of a multi-storeyed residential complex which is not one of the objects of the company. In C.A. No. 184 of 1990, respondent No. 2 filed copies of minutes of the meetings of the board of directors held on June 6, 1987, and September 3, 1987, attended by only respondent No. 2 and his wife. At the meeting held on June 6, 1987, it was resolved to issue further shares for raising necessary funds for the construction of a residential complex, while at the meeting held on September 3, 1987, the managing director was requested to receive applications for the issue of additional shares. It is significant to note here that as RW-1 has admitted, respondent No. 2 is a partner in three other firms, viz., Paramount Construction Company, Builders and Builders and Architects, engaged in construction of residential complexes and evidently he was interested in that line of business. No other purpose either statutory or otherwise is shown for the issue of additional capital. Thus, this issue is decided against the respondents.

24. Issue No. 3. - Whether the company has undertaken construction of residential flats and if so, is it within the scope and authority conferred by the memorandum of association?

25. As admitted by RW-1, permission of the Municipal Corporation of Visakhapatnam, for construction of residential flats was applied for in 1987 and the company began construction of a residential complex which is clear from the purchase bills of construction material exhibits B-27 to B-33, which according to RW-1, relate to construction of residential flats. It was only after this the court granted injunction in C.A. No. 82 of 1988, on June 27, 1988, that the construction was stopped. RW-1 made a feeble attempt to say that the injunction is against construction of hotel but when he was confronted with the copy of the order of the injunction he resiled, which he could not but do so. RW-1 categorically admits that increase in the capital was for the purpose of constructing residential flats and that the objects of the company do not permit flats, In fact, he said he was manager for construction of residential flats. At the meeting of the board of directors held on December 13, 1986, a copy of the minutes of which was filed by respondent No. 2 in C.A. No. 184 of 1990, it was resolved to apply for permission to the Municipal Corporation of Visakhapatnam for construction of a residential complex and at the meeting on March 3, 1987, the plans prepared for construction of the complex were found satisfactory. A feeble attempt has been made by Mr. V.V.S. Rao, learned counsel for the respondents, that there is no plea to this effect in the petition in which the word used is "apartment". There is no substance in this. The word "flats" and "apartments" are synonymous in commercial parlance. In fact in the counter there is no denial of the allegation made in this regard in para. 10 of the petition. Thus this issue is decided against the respondents.

26. Issue No. 4. - Whether the affairs of the company are being conducted in a manner oppressive to the interests of the petitioner for the reasons mentioned in the petition?

27. Learned counsel for the petitioner, Mr. Ravi, submits that the following factors cumulatively indicate that the affairs of the company are being conducted in the manner oppressive to the petitioner :

- (i) Issue of additional share capital though not necessary.
- (ii) Abnormal increase in allotment of shares to the respondents to the complete exclusion of the petitioner.
- (iii) Removal of the petitioner as director in the year 1992.
- (iv) Construction of flats which is not one of the objects of the company and non-construction of the hotel project and;
- (v) Lack of confidence in the majority shareholders who are acting without fairness and probity.

28. Regarding the complaint of removal of the petitioner as director, exhibit A-4 which is the office copy of the letter dated August 7, 1992, shows that the petitioner has been intimated by registered post with acknowledgment due, that he was deemed to have vacated the post of directorship u/s 283(1)(g) of the

Companies Act as he has not attended more than three consecutive meetings. Form 32 (exhibit B-34) sent to the Registrar of Companies shows that the petitioner is deemed to have vacated the office due to disqualification u/s 283(1) (g) of the Act. The complaint of the petitioner is that he has not been given notice of meetings by the board of directors. But he admits that he was always receiving intimation of meetings by telephone. The respondents say that in accordance with the usual practice, the petitioner was being informed about the meetings over the telephone and that the petitioner did not choose to attend. The question whether the petitioner was given due notice and whether the vacation of the office is valid or not cannot be decided in this proceeding as there is no adequate material.

29. Regarding lack of probity it has been observed by the Delhi High Court in *Bhaskar Stoneware Pipes P. Ltd. v. Rajinder Nath Bhasker* (1988] 63 Comp Cas 184 Delhi :

"The crux of the question seems to be not whether any group has been expelled or whether this was done lawfully or otherwise but whether there has been breach of a basic mutual understanding."

30. There, the court found that all along there was proportionate parity in shareholding which was sought to be disturbed and the breach of the implied understanding with a view to consolidate the power in one group was indicative of oppression as revealing lack of probity and fair dealing. Though that was the prima facie view of the court, this case is apposite to the facts of the present case. Mr. S. Ravi, learned counsel for the petitioner, submits that in view of ingredients (i), (ii), (iv) and (v) it has to be held that the affairs of the company are being conducted in a manner oppressive to the interests of the petitioner and relies on *Shanti Prasad Jain Vs. Kalinga Tubes Ltd.*, wherein at page 366, it was observed by the Supreme Court :

"As has already been indicated, it is not enough to show that there is just and equitable cause for winding up the company, though that must be shown as preliminary to the application of section 397. It must further be shown that the conduct of the majority shareholders was oppressive to the minority as members and this requires that events have to be considered not in isolation but as a part of a consecutive story. There must be continuous acts on the part of the majority shareholders, continuing up to the date of petition, showing that the affairs of the company were being conducted in a manner oppressive to some part of the members. The conduct must be burdensome, harsh and wrongful and mere lack of confidence between the majority shareholders and the minority shareholders would not be enough unless the lack of confidence springs from oppression of a minority by a majority in the management of the company's affairs, and such oppression must involve at least an element of lack of probity or fair dealing to a member in the matter of his proprietary rights as a shareholder. It is in the light of these principles that we have to consider the facts in this case with reference to section 397."

31. Mr. V.V.S. Rao contends that the construction of flats, even assuming that it is unauthorised and illegal, does not constitute an act of oppression and relies on the decisions in Suresh Kumar Sanghi Vs. Supreme Motors Ltd. and others, , Jaladhar Chakraborty and Others Vs. Power Tools and Appliances Co. Ltd. and Others, , Chander Krishan Gupta Vs. Pannalal Girdhari Lal Pvt. Ltd. and Others, , Palghat Exports Private Ltd. and P. Ramkumar Vs. T.V. Chandran and Others, , Nagavarapu Krishna Prasad and Another Vs. Andhra Bank Ltd., and Devaraj Dhanram Vs. Firebricks and Potteries Pvt. Ltd. and others, .

32. In Suresh Kumar Sanghi Vs. Supreme Motors Ltd. and others, , it was held mere violation of the provisions of the Act per se does not constitute oppression and that the remedy of the aggrieved party is elsewhere under the Act. The petition was rejected in that case as the petitioner had not proved that there have been continuous acts of oppression of the minority shareholders by the majority.

33. The next decision is Jaladhar Chakraborty and Others Vs. Power Tools and Appliances Co. Ltd. and Others, . In that case, the complaint of the minority shareholders that no dividend was declared by the company although the company made profits for a number of years by manipulating the accounts; that those who were in the management caused unauthorised constructions in the company's building and let them to various persons at a high premium which had not been shown in the accounts of the company; that various portions of the building had been let at low rents and that the respondents had misappropriated the premiums. It was held by the single judge of the Calcutta High Court that non-declaration of the dividend could not by itself amount to mismanagement, that there was sufficient reason given by the respondents for failure to give dividends that the manipulation of the accounts was not proved by the petitioners, that there was no material to prove that the premises in question could fetch a higher rent or the directors had profited thereby and that a single act of letting did not amount to oppression. It was further held that the acts of oppression or mismanagement must be continuing ones. The decisions in Chander Krishan Gupta Vs. Pannalal Girdhari Lal Pvt. Ltd. and Others, and Palghat Exports Private Ltd. and P. Ramkumar Vs. T.V. Chandran and Others, are to the same effect, namely, that isolated illegal past acts do not amount to oppression.

34. In Nagavarapu Krishna Prasad and Another Vs. Andhra Bank Ltd., , a Division Bench of this court held that a mere apprehension that the minority shareholders will be oppressed in the conduct of a company, that is to be formed in the future, cannot be a sufficient ground for invoking section 397. The Division Bench was dealing with the case of Andhra Bank Ltd., which prior to the nationalisation of banks was carrying on the business of banking. In view of the nationalisation of private banks, the Division Bench held that the substratum of the company has disappeared and that it was a fit case for winding up, on just and equitable grounds. Having ordered winding up it was not necessary for the Division Bench

to consider the section 397 petition. However, their Lordships after noticing this, considered the petition as elaborate arguments have been addressed on this aspect. The section 397 petition was dismissed in view of the petitioner's own case that the winding up of the company will be more advantageous and will not unfairly prejudice them. Further even on the merits, the Division Bench held that there was no act of oppression. This decision is not relevant to the point in issue.

35. In *Devaraj Dhanram Vs. Firebricks and Potteries Pvt. Ltd. and others*, , the Karnataka High Court held that what the court has to see in a petition under sections 397 and 398 of the Companies Act, 1956, is not whether the respondents intended to harm the petitioner, but whether by reasonable standards, the consequences of the conduct complained of would be regarded as having unfairly prejudiced the petitioner's interest. In that case the allegations were that the petitioner who was joint managing director of the company was prevented by the respondents from discharging his functions as joint managing director; that the respondents sold some machinery and land and that 85 per cent. of the shares were proposed to be sold to third parties. Dismissing the petition, the court held that the petitioner could not prove any of the allegations and also found that as the petitioner has refused to avail of the pre-emptive offer made to him, purchase of shares of the respondents, transfer of shares to third parties is not hit by article 37 of the articles of association which does not imply absolute bar on transfer to third parties. All the above decisions lay down that there must be continuous acts of oppression up to the date of filing the petition u/s 397 and that isolated past acts or future apprehended acts are not enough. There is no dispute about this proposition which has been authoritatively laid down by the Supreme Court in *Shanti Prasad Jain Vs. Kalinga Tubes Ltd.*, . Whether the particular acts constitute oppression depend on the facts of each case and in the above cases on the facts it was held that there was no oppression.

36. In the instant case, the construction of flats, as already seen, is beyond the objects of the company which is to construct a hotel. It is clear that when once the residential complex is constructed the question of construction of a hotel will not arise and that the company will not be able to achieve its object. The factor coupled with the fact that the second respondent is a builder and is a partner in three other construction firms shows that respondent No. 2 wanted to make use of the land for the purpose of constructing the residential flats after converting the petitioner into an insignificant minority shareholder. Issuing additional shares to the respondents to the complete exclusion of the petitioner, the unfair conduct of the respondents and the construction of flats which means that the construction of the hotel project was abandoned cumulatively show that there is oppression of the petitioner by the group of respondent No. 2. Thus, this issue is also decided in favour of the petitioner.

37. Issue No. 5. - What relief to be granted in this petition?

38. From the findings on the above issue, it follows that the complaint of the

petitioner that the affairs of the company are being conducted by the majority shareholders in a manner oppressive to the interests of the petitioner is justified and that there are sufficient grounds to wind up the company. But as the winding up of the company will unfairly prejudice the petitioner, the petitioner seeks relief u/s 402(b) of the Act, which enables the court to make an order providing for the purchase of the shares or interests of any members of the company by other members thereof or by the company. It is well-settled that there is no limitation upon the powers of the court to pass appropriate orders u/s 402 of the Act to suit the circumstances of the case and that the only limitation upon the powers of the court is that the order should not be violative of the provisions of the Act. In fact, in *Needle Industries (India) Ltd. v. Needle Industries Newly (India) Holding Ltd.* [1981] 51 Comp Cas 743 (SC), the Supreme Court, while dismissing the petition filed for relief against oppression, observed that the court is not powerless to do substantial justice between the parties and place them as nearly as it may in the same position in which they would have been if the meeting of May 2, 1977 (where the impugned resolution of allotting entire rights shares to Indian shareholders was passed) was held in accordance with law.

39. Interpreting section 210 of the English Companies Act, which is analogous to sections 397 and 402 of the Act, Lord Denning in *Scottish Co-operative Wholesale Society Ltd. v. Meyer* [1959] 29 Comp Cas 1 (HL) observed as under :

"One of the most useful orders mentioned in the section - which will enable the court to do justice to the injured shareholders - is to order the oppressor to buy their shares at a fair price : and a fair price would be, I think, the value which the shares would have had at the date of the petition, if there had been no oppression. Once the oppressor has bought the shares, the company can survive. It can continue to operate. That is a matter for him. It is, no doubt, true that an order of this kind gives to the oppressed shareholders what is in effect money compensation for the injury done to them : but I see no objection to this. The section gives a large discretion to the court and it is well exercised in making an oppressor make compensation to those who have suffered at his hands.

True it is that in this, as in other respects, your Lordships are giving a liberal interpretation to section 210. But it is a new section designed to suppress an acknowledged mischief."

40. So, the normal rule is that the oppressor has to buy the shares of the oppressed shareholders, though in exceptional cases as in *C.P. No. 8 of 1981*, dated June 10, 1988, decided by His Lordship B.P. Jeevan Reddy (as he then was), the oppressed shareholders were directed to buy the shares of the oppressor.

41. Then the next question is, at what rate have the shares to be purchased by respondents Nos. 2 to 6. In *Bird Precision Bellows Ltd.'s case* [1985] 3 All ER 523, which was also a case of quasi-partnership, it was held that the price has to be fixed on the basis of the market value of the petitioner's shares pro rata

according to the value of the company's shares as a whole but without any discount to reflect the fact that the petitioner's shares constituted a minority shareholding. In similar circumstances a Division Bench of the Karnataka High Court in Synchron Machine Tools P. Ltd. and others Vs. U.M. Suresh Rao, directed the oppressor shareholder to buy the shares of the minority shareholders at the market value to be fixed by the chartered accountant to be appointed by the court. The share value has to be fixed as on the date immediately before the issue of additional share capital. As the additional share capital was issued on December 2, 1987, the cut-off date can be taken as December 1, 1987.

42. PW-1 in his evidence stated that the value of the land can be computed at Rs. 3,000 per square yard, but that was as on the date of his deposition, i.e., September 16, 1993. RW-1 stated that the company purchased another piece of land of 1,016 square yards from one Smt. Bagawanth Mankani, for a total consideration of Rs. 8,00,000 in March, 1992. According to him this site is on the rear side of the land in question and access, separate road, which is, however, not the main road and yet it does not make any difference in so far as the value of the land is concerned. The relevant balance-sheet nearest to the date December 1, 1987, is the balance-sheet as on September 30, 1987, exhibit B-17, as per which there were no reserves, evidently, because there was no business or profits for the earlier years and practically the land is the principal asset. There were no substantial liabilities except to a small amount of Rs. 3,500 due to the chartered accountant. The amount of Rs. 91,193 is the book value of the land but for fixing the market value of the share, the market value of the land has to be taken. In the normal course I would have directed the valuation to be fixed by a chartered accountant but as the matter is very old, to avoid further delay I proceed to fix the value of the share in this proceeding itself instead of referring to a chartered accountant.

43. According to the counter of the respondents, the value of 1,361 square yards as on July 29, 1980 (financial year 1980-81), is Rs. 81,660, i.e., at the rate of about Rs. 60 per square yard. According to RW-1, the adjacent land which was purchased in the financial year 1991-92 was at the rate of Rs. 787 per square yard. The Central Government has notified the cost inflation index by Notification No. S.O. 600(E), dated August 19, 1994, published in Agew Steel Manufacturers Pvt. Ltd. Vs. Commissioner of Income Tax, , for the purpose of computation of capital gains u/s 48 of the Income Tax Act, 1961. The Table is as follows :

-----										Sl. Financial year			
Cost					inflation					index			
-----										(1)	(2)	(3)	
-----										1.	1981-82	100	
2.	1982-83	109	3.	1983-84	116	4.	1984-85	125	5.	1985-86	133	6.	1986-87
140	7.	1987-88	150	8.	1988-89	161	9.	1989-90	172	10.	1990-91	182	11.
1991-92	199	12.	1992-93	223	13.	1993-94	244	14.	1994-95	259			

44. According to this table if the cost of an asset is taken as Rs. 100 in the financial year 1981-82, the cost will be Rs. 150 in the financial year 1987-88 and Rs. 199 in the year 1991-92. The table commences from the financial year 1981-82. As the land purchased in the instant case was in 1980-81 and also in view of the period being longer (7 years), if computed with reference to 1980-81, as compared to four years, if taken with reference to 1991-92, the cost index for 1991-92 may be taken and the cost in 1987-88 correspondingly determined by applying the ratio. Thus, the value in 1987-88 can be taken as $150/200 \times 787$, or roughly $150/200 \times 787 = 590.25 = \text{Rs. } 590$. The total value of 1,361 square yards land will be Rs. 8,02,990. Dividing by 110, the value of the share will be Rs. 7,299. So, the value of 50 shares will be Rs. 3,64,950. But this can be taken only as maximum. In the deposition PW-1 stated that after filing the company petition Mr. Manga Raju, told him that respondent No. 2 was willing to pay Rs. 2,00,000 to him and retain the entire property for himself and that if he withdraw the company petition, he would pay about Rs. 2,00,000 to him; that he did not accept the proposal and that he would withdraw the company petition if the respondents pay half of the value of the land. But the value of the land was not mentioned in the deposition as on December 1, 1987. Mr. V.V.S. Rao, learned counsel submits that Rs. 2,00,000 will be reasonable amount of the value of the petitioner's shareholding. In view of this, I think it is just and reasonable that respondents Nos. 2 to 6 are directed to pay Rs. 2,00,000 (rupees two lakhs only), to the petitioner and acquire his shares, within three months from today. In default, it is open to the petitioner to move this court for an appropriate direction regarding the purchase of shares of respondents Nos. 2 to 6 by him as on today at a price to be fixed by the court.

45. The company petition is allowed no costs.

ON BEING MENTIONED

46. On being mentioned, Mr. V.V.S. Rao says that the company petition, C.P. No. 27 of 1988, may be treated as disposed of and not as allowed.

47. Accordingly, for the word "allowed" in the last para, substitute "disposed of".