

(2010) 02 AP CK 0002

In the Andhra Pradesh High Court

Case No : Letter Patent Appeal No. 313 of 2001

D. Ramakrishna Rao and Others

APPELLANT

Vs

LRR Hatcheries Pvt. Ltd. and Others

RESPONDENT

Date of Decision : 19-02-2010

Acts Referred:

Companies (Court) Rules, 1959 — Rule 9
Companies Act, 1956 — Section 394, 397, 398, 402
Constitution of India, 1950 — Article 136

Citation : (2010) 4 ALT 234

Hon'ble Judges : B. Chandra Kumar, J;A. Gopal Reddy, J

Bench : Division Bench

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

Final Decision : Allowed

Judgement

A. Gopal Reddy, J.—This intra-Court appeal under Clause 15 of the Letters Patent is directed against the orders of the learned Single Judge, dated 10.7.2001 dismissing the Company Appeal No. 3 of 1999.

2. Relevant facts shorn of details, which gave rise for filing this appeal are as under:

Appellants filed a petition u/s 397 and 398 of the Companies Act before the Company Law Board, Principal Bench, New Delhi alleging that themselves and the respondents 2 to 8 are the shareholders of first respondent - M/s. LLR Hatcheries Pvt. Limited, which was incorporated for carrying on business in hatcheries and related activities. The first appellant and the respondents 2 to 4 were signatories to the Memorandum of Articles of Association of Company each subscribing to 5 shares. Over a period of time, by issuing of further shares/transfers, the appellants' group happen to hold 6900 shares as against the respondents' holding of 5500 shares. The first appellant was a Director in-charge of Marketing while the third respondent had been the Chairman and Managing Director of the company. In the Board Meeting held on 11.5.1997, the Board

allotted 2600 shares to two respondent directors by which, the appellants' group was reduced from majority into minority. The said allotment, according to the appellants, was done with mala fide intention to reduce the appellants' group from majority to minority. Hence, they approached the Company Law Board by filing C.P. No. 96 of 1997 alleging that the allotment is in total disregard to the agreement as entered in the minutes book in the month of April, 1996, wherein it was agreed upon that in case, further shares were to be allotted, that would be done so only in pro-rata basis. The so called resolution of the Board meeting on 11.5.1997 by allotting 2600 shares to the respondents 2 and 3 is without notice to the appellants and this was done with a view to gain majority position in the company by the respondents' group and to oppress the appellants. The respondents filed a counter opposing the petition contending that the appellants approached the Bench with unclean hands and the first appellant was guilty of embezzlement of funds of the first respondent-Company, fabrication of accounts and illegal acquisition of shares by forging the signatures of transferors with a view to acquire majority stake in the company. With a view to wreak vengeance on the third respondent-Chairman and Managing Director of the Company, the appellants 1 and 2 even made an attempt on his life after filing the petition resulting in registering an F.I.R. against them. The first appellant with a view to gain controlling interest in the company used the money siphoned off from the company for purchase of the shares. The appellants' group was originally not in majority but by acquiring shares by transfer by adopting various illegal ways and registering such transfers without the approval of the Board, now claiming majority. The first appellant was removed from being in-charge of the Accounts and Administration in February, 1996 and was later removed from the directorship. In view of that, the appellants made various complaints to the Vigilance Commissioner and the Registrar of Companies and also the Bankers of the first respondent company making various motivated allegations, due to which, the bank initiated the proceedings before the Debts Recovery Tribunal. The conduct of the appellants in relation to the affairs of the first respondent-Company are detrimental to the interest of the Company and therefore, prayed for dismissal of the petition.

3. The Company Law Board by its order, dated 26.4.1999 observed that in the Board Meeting held on 8.4.1996 a decision was taken to the effect that the shares should be allotted pro rata basis, but in the Board Meeting held on 11.5.1997, the undistributed 2600 shares were allotted to respondents 2 and 3 at 1000 and 1600 shares respectively as against the decision taken on 8.4.1996. As per Article 5 of the Articles of Association, the Board has the power to allot shares to such persons and on such terms and conditions as the Board may think fit. Since no notice of the Board Meeting had been given to the first appellant even though at the relevant time he was a Director of the Company and that as the normal rule of law is that the decisions taken in a Board Meeting to which notices have not been sent to all directors are invalid, it has to be held that the decision taken in the meeting to allot the shares has to be declared as invalid.

Further the Company Law Board observed that the allotment made was not on account of any need for the funds of the Company as it transpired that the shares were allotted in adjustment of certain loans given by these respondents to the Company. After considering the minutes of the meeting relating to the matter, the Board came to the conclusion that the allotment of 2600 shares was made only with a view to gain majority position in the company by the respondents, may be on the ground that the appellants' group gained the majority by alleged unlawful means. But, if the reason for the allotment were to be what the respondents have alleged, then, the proper course of action for them should have been to initiate necessary proceedings to get the acquisition by the appellants invalid and not to allot shares to themselves as a counter action. Therefore, though the Board was of the view to declare the allotment of shares as invalid, but did not do so for the reason that there was no possibility for the parties to continue the business together, and that the appellants would gain majority control and as they had earlier issued a notice for convening an EOGM to remove the respondents as directors, they would be at liberty to do it again which would pave way for further litigation affecting the interests of the company. Since in a petition filed under Sections 397 and 398, the interest of the company should be paramount and considering the pendency of proceedings before the Debts Recovery Tribunal, the Board was of the view to protect the interest of the first respondent-Company by directing one of the groups to go out of the company by selling their shares to the other group. Pending the proceedings, though an agreement was reached between the parties in the presence of the Board, which was recorded by order, dated 22.1.1998, wherein the respondents agreed to go out of the Company by selling their shares to the appellants, the same could not be materialized due to the stand taken by the bank in releasing the personal guarantees given by the respondents. Therefore, the Board was of the view that the only way by which the parting of ways between the groups could be effected is that the appellants' group should sell their shares to the, respondents, who offered a sum of Rs. 325/- per share to the appellants. But, as the said rate was not acceptable to the appellants, the Board considered it appropriate to get the shares of the Company valued by an independent valuer so that there could be no dispute regarding the price payable by the respondents to the appellants. Since Article 13 of the Articles of Association of the Company provides for determination of fair value by the auditors of the company in case of transfer of shares, the Board was of the view that the provisions of the said Article should be applied in valuation of shares to decide the present dispute. In case, it was not acceptable to either of the parties that the auditors of the company should value the shares, the Board gave the option to the parties to suggest a valuer agreeable to both of them so that the Board could appoint him to value the shares, and observing so, the Board disposed of the company petition.

4. Feeling aggrieved by the said order, the appellants filed Company Appeal No. 3 of 1999 which was dismissed by a learned single Judge of this Court by order,

dated 10.7.2001 holding that:

...while deciding the issues arising u/s 397 and 398 of the Companies Act, the body entrusted with the responsibility of the resolution of the dispute, a Court or a body like the Company Law Board, is not only concerned with the immediate legal rights of the parties before it, but also the community at large. The Company Law Board being the body is entrusted with the responsibility for resolving the disputes falling within the scope of Sections 397 and 398 of the Companies Act. On an overall consideration of the facts and circumstances, it cannot totally be branded as "perverse", for the reason, that the company was being run for quite some time by the respondents herein successfully, which is evident from the fact that the shares of the company which are the face value of Rs. 100/- each are valued around Rs. 300/- though there is some variation between the assessment of variation in the views of the contesting parties and the independent valuer about the agreed valuation.

I, therefore, do not wish to substitute my wisdom for the wisdom of the Company Law Board in an appeal. The appeal is therefore, dismissed.

5. Sri S. Ravi, learned senior Counsel appearing for the appellants would contend that once the Company Law Board found the allotment of 2600 shares by respondent 2 and 3 for themselves as invalid which finding has become final in the absence of any cross-appeal being filed by the respondents, the Company Law Board ought to have allowed the company petition by setting aside the said allotment, which was done only to oppress the majority shareholders. If the appellants purchased the 1800 shares fraudulently by transfer, as rightly observed by the Board, the same could have been challenged before the appropriate forum and therefore, the respondents having not chosen to challenge the same, now cannot set up it as a defence for oppression and mismanagement. Had the respondents challenged the same, the appellants would have established that they acquired the shares in rightful manner. Among the groups of appellants and the respondents, for the purpose of selling/buying the shares, valuation of the shares is must and for the said proposition, he placed reliance on *Tea Brokers (P) Ltd. and Ors. v. Hemendra Prosad Barooah* (1998) 5 Comp LJ 463 (Cal). The respondents can fix the share value and give an option to the appellants for purchase. The appellants are offering Rs. 1600/- per share either for buying or selling their shares. Since the land to an extent of Ac.8.70 cents is owned and possessed by the first respondent-Company on the Guntur-Madras highway which is 19 k.ms. away from Guntur, the appellants are making the said offer for purchasing the shares.

6. Per contra, Sri V.S. Raju, learned Counsel appearing for the respondents would contend that the Company Petition was filed only on the allegation that the allotment of 2600 shares in favour of respondents 2 and 3 as illegal and contrary to the earlier Board resolution. In fact, the appellants were holding 5100 shares before 1999, whereas, the respondents were holding 5800 shares. But, 1800 shares were acquired by the appellants fraudulently by transfer and thereby

became majority shareholders. Once the Company Law Board considered the paramount interest of the Company in view of the pendency of Debt Recovery proceedings, and once the offer made by the respondents was not accepted to by the appellants, the Company Law Board passed an equitable order and the same has been confirmed in appeal and therefore, the same cannot be interfered in exercise of jurisdiction under Letters Patent. To support of the contentions, the learned Counsel placed strong reliance on S.D.N. Wadiyar v. Sri Venkateswara Real Estate P. Ltd. (1991) 72 Comp. Cas 211; P. Ramkumar v. T.V. Chandran and Ors. (1994) 1 Comp LJ 469 (Ker) ; and M.S.D.C. Radharamanan Vs. M.S.D. Chandrasekara Raja and Another,

7. In the light of the above submissions, the issue which cropped up for consideration in this appeal is, once the acquisition of 2600 shares by the respondents" group has been declared invalid, whether the Company Law Board is justified in directing the appellants to sell their shares to the respondents after valuation of shares by the valuer?

8. Indisputably, the Board of Directors in the meeting held on 8.4.1996 under the Chairmanship of third respondent, took a decision at the suggestion of the first appellant to the effect that undistributed shares would be kept till distributed equally among all the shareholders in proportion to the shares held by them. But, subsequently, contrary to the said decision and without notice to the first appellant, in the Board meeting held on 11.5.1997 the undistributed shares numbering 2600 were allotted to the respondents 2 and 3 at 1000 and 1600 shares respectively, by increasing the shareholding of the respondents" group from 5500 to 8100 as against 6900 shares held by the appellants" group. The appellants group was holding 5100 shares in 1999 and subsequently, their acquiring/purchasing of 1800 shares was taken note in the Board meeting held on 8.4.1996, but the respondents" group did not choose to challenge the said acquisition/purchase before the appropriate forum. The finding of the Company Law Board that the Board meeting held on 11.5.1997 without giving any notice to the first appellant though he was a Director; and that the decision taken in that meeting for allotting 2600 shares to respondents 2 and 3 has to be declared as invalid remained unchallenged. Further the Company Law Board disposed of the Company Petition on 26.4.1999 recording a finding that the respondents offered a sum of Rs. 325/- per share to the appellants, which was not acceptable to them and that the appellants should sell their shares to the respondents since the price offered by the respondents was not acceptable to them, and that the shares of the Company should be valued by an independent valuer so that there should be no dispute about the price paid by the appellants to the respondents as provided under Article 13 of Articles of Association of the Company and that if it is not acceptable to the parties for valuing the shares by the auditor of the company, the Company Law Board can appoint the valuer suggested by both the parties for valuing the shares. The Company Law Board reserved the right to issue an order for appointment of valuer and determining the price for the shares. By further order, dated 17.5.1999, the matter was adjourned at the

request of the counsel for appellants to consult his clients as to whether the price offered by the respondents at Rs. 325/- per share is acceptable so that the appointment of valuer, which is expensive and time consuming could be avoided. On 31.5.1999, the counsel informed the Board that the proposal for sale of the shares of the appellants to the respondents was not acceptable to them and prayed for passing necessary orders. Upon that, the Company Law Board passed an order on 6.8.1999 appointing Sri Shanti Lal Daga, Chartered Accountants & Co., Hyderabad to determine the value of the shares of the Company as on 31.3.1998, the proximate date of Petition and holding that the fair value to be determined by the valuer shall be final and binding on the parties. Pursuant to the same, the valuer submitted his report determining the value of the each share as Rs. 285.50 ps. as appropriate value under net asset method.

9. A Division Bench of Calcutta High Court in Tea Brokers (P) Ltd. and Ors. (1 supra) was called upon to decide an identical issue wherein the learned trial judge directed one group of the company to sell the shares to other group. The Division Bench at para 57 held:

...The order of the learned trial Judge directing Barooah and his group to sell the shares to Khaund and his group undoubtedly enables Khaund and Mitra to achieve their purpose. For achieving their purpose, the allotment of 1,000 shares to Khaund had become necessary and Khaund had to pay a sum of Rs. 1,00,000/- to the company. The learned trial Judge has rightly set aside the allotment of the said 1,000 shares to Khaund and has consequently, directed refund of the said sum of Rs. 1,00,000/- paid to the company by Khaund for the said 1,000 shares. By virtue of the said order of the learned trial Judge Khaund will, therefore, be entitled to a refund of the said one lakh of rupees. He will, however, succeed, by virtue of the further order made by the learned trial Judge directing Barooah and his group to sell their shares to Khaund and his group in ousting Barooah from the company and in getting the full control of the company for himself and his group by paying to Barooah and his group the value of the shares held by them and price that Khaund and his group will have to pay Barooah and his group for their shares will be a much smaller amount than the sum of Rs. 1,00,000/- which Khaund had to pay for the said 1,000 shares for seeking to gain control of the company. In consequence of the said order of the learned trial Judge directing Barooah and his group to sell their shares to Khaund and his group, Khaund and his group will succeed in achieving their purpose of completely ousting Barooah from the company by spending much smaller sum. Order of learned trial Judge directing Barooah and his group to sell their shares will, therefore, result in greater benefit for Khaund and Mitra who have found to be guilty of wrongful, improper and mala fide conduct, and said order will not redress the grievance of Barooah which has been found to be just and legitimate and will indeed have the effect of making him more aggrieved. The said order of learned trial Judge directing Barooah and his group to sell their shares to Khaund and his group cannot, in the facts and circumstances of the case, be considered to be a just order. The said order cannot, therefore, be upheld and must be set

aside and the cross-objection preferred by Barooah must succeed. I, therefore, set aside the order of the learned trial Judge directing Barooah and his group to sell their shares to Khaund and his group. In the facts of the instant case, I do not think it will be also just and proper to direct Khaund and Mitra to sell their shares to Barooah, as, in my opinion, Khaund and Mitra substantially contributed to the welfare and prosperity of the company. Khaund and Mitra have also existing agreements with the company. The prosperity can best be attained and maintained by Barooah, Khaund and Mitra acting together. All of them have been associated with the company for years and the position that the company has acquired is due to combined efforts of all of them. It is indeed unfortunate that they have fallen out and disputes have arisen between them. Khaund and Barooah have also been friend for years. I sincerely hope that they will all forget the past and sink their differences and will continue to work together to serve the best interest of the company. It is, however, indeed a matter for them. If, however, they are not in a position to compose their differences and work together, the members of the company have necessarily to decide as to how the affairs of the company are to be managed....

Observing so, the order of the trial judge setting aside the allotment of 1000 shares and also upholding the superceding of the Board of Directors appointing a Special Officer and directing him to appoint a competent valuer for valuing the shares of the Company and that after such valuation, Khaund and his group will have to be the option to purchase the shares of Barooah and his group at such valuation and in the event of Khaund and his group is not willing to buy the shares, Barooah and his group would have the option to purchase the shares has been set aside.

10. The Karnataka High Court in the decision rendered in *S.D.N. Wadiyar* (2 *supra*) while referring to a paragraph in the 5th edition of Pennington's Company Law in page 750:

A petition for relief from oppression under the original statutory provision would be dismissed if it was not presented in good faith solely in order to obtain such relief, and because of the equitable and therefore, discretionary character of the Court's jurisdiction under both the original and the present provision, the requirement of good faith on the part of the petitioner undoubtedly continues. Thus, even if the directors or majority shareholders have been guilty of improper or irregular conduct, so that there is a *prima facie* case for relief, it will be refused if the real purpose of the petitioner is to obtain payment of a debt owed by the company, or to force the directors to accept his , views as to the way in which the company's business should be managed; or if the petitioner has submitted to the conduct complained of without protest and has acquiesced in the improper management of the company affairs. Likewise, delay by the petitioner in initiating proceedings after he must have realized that he was the victim of a scheme of oppression or unfair treatment will induce the court to refuse relief, because this indicates that the petitioner has acquiesced in the

respondents" conduct and that his complaint is, therefore, not made in good faith.

held that "the Court should first make an order under Sections 394, 397 and 398 and, in that order, it has to provide for matters more particularly stipulated in Section 402 of the Act. This section read with Rule 9 of the Company (Court) Rules, 1959, which deals with the inherent powers of the court to give such direction to meet the ends of justice was the basis of the decision of the Supreme Court in Needle Industries" case (1981) 51 Comp Cas 743. In my view that power of the company court is wide enough on the facts and circumstances of these cases and, on the basis of the memos of compromise filed by the parties to make suitable provisions u/s 402 of the Act read with Rule 9 of the Companies (Court) Rules, 1959, to bring about an amicable settlement to the longstanding dispute between the parties."

11. A Division Bench of Kerala High Court in the case of P. Ramkumar (3 supra) considering the expressions "oppression" and "mismanagement" at para 19 observed as under:

19. The expressions "oppression" and "mismanagement" which are the core concepts in the section are left by the Legislature without defining them. When once it is left without definition, the task of the court is difficult and more responsible. Naturally, the court will always incline to wade through precedents to find out and to assign the correct meaning of these two words "oppression" and "mismanagement" in the context in which they are used. Certainly, the courts have to decide on the facts of each case as to whether there is a real cause of action u/s 397 or 398 of the Act.

Further the Division Bench after referring to the judgment of the Supreme Court in Shanti Prasad Jain Vs. Kalinga Tubes Ltd., held that isolated acts of the controlling shareholders cannot be used as a ground for taking action u/s 397 of the Act, and that one of the conditions essential for seeking relief u/s 397 of the Act is that there should be continued oppression over a period of time, and accordingly, allowed the appeal setting aside the judgment of the company court granting certain reliefs under Sections 397 and 398 of the Act.

12. The facts in the case of M.S.D.C. Radharamanan (4 supra) are that the Company Law Board directed the appellant therein to purchase 2,84,000 shares held by the first respondent at a value to be determined by the chartered valuer in an application filed under Sections 397 and 398 of the Companies Act, 1956. On appeal being filed, the High Court of Madras dismissed the same. On further appeal, the Supreme Court after referring to its earlier decision in Needle Industries (India) Ltd. and Others Vs. Needle Industries Newey (India) Holding Ltd. and Others, wherein it was held that:

Even though the company petition fails and the appeals succeed on the finding that the holding company has failed to make out case of oppression, 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 were held in accordance with law.

and after referring to the judgment of the Delhi High Court in Pearson Education Inc. (formerly Prentice Hall Inc.) Vs. Prentice Hall India (P) Ltd. and Others, dismissed the appeal holding that both the Company Law Board as well as the High Court have arrived at a concurrent finding that there was no mutual trust and confidence between the parties and, thus, it would be impossible for the company to run the same smoothly and the said findings do not call for interference in exercise of the discretionary jurisdiction under Article 136 of the Constitution of India.

13. A careful analysis of the above judgments clearly discloses that a group of shareholders who have gained majority by allotting the shares to themselves by illegal acts cannot be conferred benefit of their purchasing the shares of other group shareholders nor can compel the other group shareholders to sell their shares to achieve their purpose and when the parties are at loggerhead making it impossible for the Company to run the same smoothly, it is always open for the Company Law Board to pass equitable orders keeping in view of the interest of the company for sale of the shares by one group to the other group.

14. Coming to the facts of the case on hand, the Company Law Board was of the view that the only way by which the parting of ways between the groups could be effected is that the appellants' group should sell their shares to the respondents' group and if the price offered by the respondents' group is not acceptable to the appellants' group, the Board was of the view that the shares of the Company should be valued by an independent valuer so that there could be no dispute regarding the price payable by the respondents to the appellants and accordingly appointed Sri Shanti Lal Daga, Chartered Accounts & Company, Hyderabad to determine the value of the shares of the company as on 31.3.1998, the proximate date of petition with a further observation that the fair value to be determined by the valuer shall be final and binding on the parties. The Calcutta High Court in the case of Tea Brokers (P) Ltd. and Ors. (1 supra) held that directing the shareholders of a group to sell their shares to the other shareholders' group who were found to be guilty of wrongful, improper and mala fide conduct cannot be considered to be a just order and accordingly set aside the same. It was further ordered that:

The order of learned trial Judge directing the special officer to appoint a competent valuer for valuing the shares of the company and further order that after such valuation Khaund and his group will have the option to purchase the shares of Barooah and his group at such valuation and in the event of Khaund and his group not being able or willing to buy the shares, Barooah and his group will have the option to purchase the shares is hereby set aside. There will be no order or any direction on any of the parties to buy or sell the shares held by them.

15. In view of the fact that the specific finding of the Company Law Board that allotment of 2,600 shares by the respondents 2 and 3 for themselves as invalid has become final and no cross-appeal has been filed by the respondents against the said finding, we set aside the allotment of 2,600 shares by the respondents 2 and 3 for themselves. The finding of the Company Law Board that "the only way by which the parting of ways between the groups could be effected is that the appellants should sell their shares to the respondents" would also amount to conferring premium on the respondents and the same is accordingly set aside. Merely because the appellants are not agreeable to purchase the shares of the respondents at Rs. 325/- per share as offered by the respondents that itself cannot be a ground to direct them to sell their shares as valued by the independent valuer for the reason that the appellants have rightly not agreed to purchase the shares of the respondents' group at Rs. 325/- per share as offered by respondents, as they have to purchase not only 5800 shares held by the respondents' group but also 2600 shares which were got allotted by respondents 2 and 3 for themselves. Therefore, we remit the matter to the Company Law Board for passing appropriate orders by giving an opportunity to both the parties" with an option to purchase the shares of other group shareholders in the light of the share value fixed by the approved valuer at Rs. 285/- per share or as offered and agreed by each party.

16. The appeal is allowed accordingly. No order as to costs.