

**(1991) 11 MAD CK 0039**  
**In the Madras High Court**

D.A. Swamy and Others

APPELLANT

Vs

India Meters limited

RESPONDENT

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**Date of Decision :** 26-11-1991

**Acts Referred:**

Companies Act, 1956 — Section 391, 391(1)

**Citation :** (1992) 1 LW 332 : (1992) 1 MLJ 523

**Hon'ble Judges :** Mishra, J

**Bench :** Division Bench

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**Judgement**

Mishra, J.—This appeal has to be disposed of mainly on the ground whether unsecured creditors were legally classified as one group and thus there has been compliance with the requirements of Section 391 of the Companies Act in accepting the compromise for the revival of the company.

2. It is not in dispute before us that in C.P.No.59 of 1982, a petition was filed in the fond hope of reviving the company and the court appointed in the course of the said proceeding, one Mr. T.P. Nagarajan, who happened to be one of the directors of the company to be the Chairman to conduct the meeting of unsecured creditors., He submitted a report to this Court stating inter alia that such a meeting was held on 15.9.1982 at 11 a.m. at Palmgrove, 5, Kodambakkam High Road, Madras and that the meeting was attended either in person or by proxy by 363 members of unsecured creditors, the value of their debt amounting to Rs. 36,85,539.09 as per the company"s books of account as on 31.3.1981.

3. The resolution put to vote at the said meeting was as follows:

Resolved that the compromise or arrangement proposed by M/s. India Meters Limited, Madras-600 006 vide Company Application No. 370 of 1982 on the file of the High Court of, Judicature, Tamil Nadu and placed before the meeting and initialled for identification by the Chairman be and is hereby approved.

4. Some of the creditors sought clarification as to why the same scheme of

compromise or arrangement proposed by the company vide Company Application No. 242 of 1982 on the file of this Court was presented once again to the unsecured creditors without any modification whatsoever. According to the Chairman, it was explained to them that the scheme of compromise presented earlier was approved by the equity and preference share-holders and secured creditors at the meeting held on 19.6.1982. The unsecured creditors by value accepted the scheme. Since the required number of unsecured creditors did not accept, the requirement of the Act was not satisfied, the company moved an application in C.A.No.370 of 1982 giving another opportunity to unsecured creditors to consider the scheme having regard to the fact that the number of persons present at the end of the meeting was far less than the persons present at the commencement of the meeting. Shanmukham, J. ordered on 30.7.1982 that the meeting of the unsecured creditors be convened to consider the scheme again.

5. The report further states how certain amendments were proposed and they were turned down as none of them secured the requisite majority at the meeting and thereafter when the resolution was put to vote,

193 unsecured creditors valuing Rs. 23,77,612.81 voted for the resolution while 73 persons valuing Rs. 6,18,057.67 voted against the resolution. The final resolution obtained 72.55% majority in number and 78.66% majority in value.

The number of creditors present in the meeting as shown however in the report was as follows:

6. Four unsecured creditors, however, filed their objections stating inter alia that the very classification of the creditors into two broad categories, secured and unsecured, is not correct and in so far as unsecured creditors are concerned, fixed deposit holders were differently treated from loan receipt holders and others, foreign creditors completely placed on a different footing from that of the local creditors and yet all the unsecured creditors, were together asked to examine the proposal and vote either for or against the scheme proposed by the company. Besides this general objection, there has been some specific objections saying, the creditors for whom better proposals were given would naturally defeat the other lawful claims of less fortunate creditors. To illustrate this I may be permitted to mention the treatment given to Osaki Electric Company Ltd., Japan, an unsecured creditor. The entire debt due to the said firm has to be paid in full, both principal and interest under the scheme and no sacrifice is proposed at all.

They also objected to the manner in which the meeting was conducted and alleged inter alia.

Right from 11.00 a.m. the meeting went on till 9.15 p.m. After 5 p.m. representations were made to me Chairman asking him to adjourn it and he refused to do the same. Number of unsecured creditors present till 5.00 p.m. who were aged and or ill went away without exercising their valuable right to

vete...the company employees by name Visweswaran, Devanathan and Sundararaman went to the residence of several number of unsecured creditors and threatened them that if they did not give proxy in their name, they would not be able to see any money at all from the company. They canvassed for proxies and used all sorts of undue influence and coerced some people to give proxies in their name. I believe they obtained blank proxies also and used the same at the meeting to suit to their convenience. Mrs. K. Saroja, Dr. K. Rajaram, Mrs. K. Savithiri and myself brought this fact to the notice of the Chairman by writing. The Chairman had not even felt bad about it and went on conducting the meeting as if nothing had ever happened.

According to these unsecured creditors, proximate made havoc and played a role adverse to the interest of those who gave these proxies and listed as follows:

The following illustrations will clearly explain this aspect of the matter. Amendment No. 1 brought forward by one of the unsecured creditor was for the benefit of loan receipt holders. That amendment was to provide equal treatment to the loan receipt holders along with the Fixed Deposit holders. It would have been natural that all the loan receipt holders who were present either in person or proxy, voted for this amendment since it provided better treatment and more advantageous. But this was defeated by the very same loan receipt holders. It appears that 43 loan receipt holders valuing Rs. 1,48,000 voted against this amendment. Number two brought forward by no less a person than the Financial Adviser and Chief Controller of Accounts of Tansi. This amendment was certainly for the benefit of sundry creditors for goods supplied and services rendered. As per the amendment the debt due to those unsecured creditors who had supplied goods and rendered service to the company should be paid in full. If this amendment also was voted against by other type of creditors one can understand the class fight. But it was voted against by the very same sundry creditors which can be seen from the report filed by the Chairman.

They made a specific allegation against the Chairman Mr. T.P. Nagarajan saying that as per the Companies Act, the Directors or the Managing Director should not have any interest in the scheme, and in fact it was also stated in the notice sent by the company that the Directors were not at all interested in the scheme, but,

Mr. T.P. Nagarajan, I.A.S., who is also one of the Directors of the company and he was the Chairman of the meeting. I am told that he obtained two proxies in his favour from two creditors valuing Rs. 10.77 lakhs and Rs. 2.30 lakhs.

These two according to the objectors were from sundry creditors for the goods supplied and services-rendered to the company. These proxies were(used in defeating all the amendments including the amendment which was beneficial to those who issued proxies. The Chairman himself voted for the scheme though in the beginning of the meeting, he said that he would be neutral. Another Director Mr. Chakrapahi, Financial Adviser to BHEL also exercised several proxies and used all of them to vote for the scheme.

7. On the basis of the above, they alleged that the decision at the meeting was not valid and that holding of a third meeting of different classes of unsecured creditors alone would be in accordance with law. The unsecured creditors are:

1. Foreign collaborator whose debt has to be paid in full.
2. Fixed Deposit holders.
3. Loan Receipt holders and Hundi creditors.
4. Sundry creditors for goods supplied and services rendered.

8. The scheme that has been approved is a long document it has something for this secured creditors, as well as employees besides unsecured creditors. So far as the secured creditors are concerned, it says,

1. That the full amount of interest due on secured creditors upto the effective date and all claims thereto be cancelled.

2. That upon the scheme being sanctioned by the court, the loans will be treated as follows from the effective date.

(a) That loan of Rs. 10.65 lakhs from Tamil Nadu Industrial Investment Corporation limited will be retained as fresh loan which will carry interest at 8.5%. The loan amount will be paid in three annual instalments.

(b) The loan of Rs. 4.80 lakhs from Industrial Finance Corporation of India will carry interest at 8.5% and the loan amount will be paid in three annual instalments.

In the category of unsecured creditors, fixed deposit holders are given as follows:

1. That the full amount of interest due on fixed deposits upto the effective date and all claims thereto be cancelled and extinguished .

2. That upon the scheme being sanctioned, out of the principal amounts outstanding, payment in respect of fixed deposits aggregating to Rs. 15.45 lakhs, will be made as follows:

(a) Each deposit of less than Rs. 5,000 will be paid 80% of the principal amount due,

(b) Such deposit of Rs. 5,000 to Rs. 10,000 will be paid Rs. 4,000 plus 40% of the amount exceeding Rs. 5,000.

(c) Each deposit Rs. 10,001 and above will be paid Rs. 6,000 plus 20% on the amount exceeding Rs. 10,000. The total sacrifice to be made by the deposit holders is Rs. 4.65 lakhs. The total amount to be paid is Rs. 10.80 lakhs.

3. That the amount to be paid of Rs. 10.80 lakhs will not carry any interest and will be paid in two annual instalments commencing within one year from the effective date.

Other unsecured creditors are:

(a) Other loans and short term loans.

1. That the full amount of interest due on the loans and hundies upto the effective date and all claims thereto be cancelled and extinguished.
2. That upon the scheme being sanctioned, out of the principal amounts outstanding payment due in respect of loans and hundies aggregating to Rs. 29.71 lakhs, 80% thereof, and all claims thereto be cancelled and extinguished.
3. That the balance 20% of such amounts to be paid to the holders thereof without any interest, in two annual instalments commencing within one year from the effective date.

(b) Sundry creditors for goods supplied:

1. That upon the scheme being sanctioned, out of the amounts of outstanding due payments to all creditors for goods supplied aggregating to Rs. 29.93 lakhs 80% thereof and all claims thereto be cancelled and extinguished.
2. That the balance 20% of the such amounts to be paid to the concerned creditors without any interest in two annual instalments commencing within one year from the effective date.

(c) Sundry creditors for expenses:

1. That upon the scheme being sanctioned, out of the amounts outstanding payment to all the creditors for expenses except the Government, Employees and Foreign Collaborators, aggregating to Rs. 2.55 lakhs, 80% thereof and all claims thereto be cancelled and extinguished.
2. That the balance of 20% of such amounts to be paid to concerned creditors, without any interest, in two annual instalments commencing within one year from the effective date.

9. Dealing with the objections, learned Shanmukham, J. has said,

As regards unsecured creditors, in first meeting held on 17.6.1982 under the Presidentship of Mr. T.P. Nagarajan, I.A.S., two amendments were prepared but were lost because neither of them secured 75% of voting value of shares. Further the resolution as such though secured the approval of the prescribed majority in value of the unsecured creditors, it failed to secure the required majority in the number of the unsecured creditors. Therefore, the company was necessitated to come forward with C. A.No.370 of 1982 for holding a fresh meeting of the secured creditors and the same was held on 15.9.1982 presided by Mr. T.P. Nagarajan. The meeting was attended either in person or by proxy by 363 unsecured creditors whose value of debt amounted to Rs. 36,85,539.09. Three amendments were moved, but were lost as none secured the required majority.

Except few unsecured creditors who stoutly oppose this proceeding, there is no protest from any other quarters, inclusive of the Central Government. On 8.7.1983, Mr. Asokan representing Mr. R. Shanmugham, learned Counsel for the Central Government stated that the Central Government has no objection to sanction the permission as prayed for in the petition. The ground of objection are the classification of the unsecured creditors is quite arbitrary in that the fixed depositors are treated differentially from other creditors who have lent on hundies and other instruments, particularly foreign collaborators treating them as one class. According to Mr. Rajamanickam, such clubbing of the unsecured creditors namely fixed depositors, and other unsecured creditors as a class is quite improper....Though there is force in the argument relating to the classification, in reality I find it would not remain as a valid fetter to accord sanction. Let me analyse the scope of the defence and its ineffectiveness....

In the classification of unsecured creditors in this case, a differential treatment is meted out to the fixed depositors on the one hand and the other unsecured creditors on the other. For the concession extended to fixed depositors is quite different from the other unsecured creditors. Nevertheless, I propose to make the same approach as done by the learned Judge in *Manickchowk v. Ahmedabad Mfg. Co* (1970) 2 C.L.J. 300. As a matter of fact, one of the arguments which was seriously pressed into service by Rajamanickam is that this court shall direct a fresh meeting of the unsecured creditors, excluding the fixed depositors, I find that the facts in this case are stronger than those in the reported case. Now if we examine the strength of voting in severality among the unsecured creditors, as seen from the report of the Chairman, the following are the particulars.

The actual voting in favour of the resolution is 193 of the value of Rs. 23,77,612.89. It is thus seen that the numerical strength as also valuation of other creditors outnumber the fixed depositors. The other creditors, if they wanted to defeat the resolution, could have done so very easily. But that is not the case here. On the other hand, as set out above, the actual voting is 193 carrying the value of Rs. 23,77,612.89. The other important factor which will go a long way to reject the objection is that if the company were to be wound up, none of the unsecured creditors will get a paisa. Indeed, I asked the learned Counsel for the objectors to prepare a working-sheet and to point out that the unsecured creditors will stand in a better footing in case of winding up than in the event of putting through the compromise. He had not done so. But the learned Counsel for the petitioner had pointed out that in case of winding-up, even the secured creditors could not be paid in full. Above all, the secured creditors are foregoing their claims for interest. It has to be pointed out at this stage that the company could not get any further benefit under the Tamil Nadu Relief Undertaking Special Provisions Act, 1969 for the company had the maximum term that is guaranteed under the Act, namely, ten years. It is common ground that it is going to expire by 21.9.1983. Above all, the secured creditors are foregoing their claims for interest, as shown in paragraph 3 of the petition. This apart, the interest of as many as 600 employees should as far as

possible be safeguarded. The most vital factor is the benefit of the collaboration with a Japanese firm should not be allowed to be lost to the public at large to the extent possible. I have pointed out at the earliest that the opposition is not based on behalf of the whole body of unsecured creditors, save the fixed depositors. Their sacrifice is very negligible compared to the sacrifice made by the other unsecured and secured creditors. Finally, their interest can be sacrificed for, the well-being of the company, serving the public interest, securing the sustenance of the employees and their dependants. Besides there is the reasonable chance of restitution of what is now being sacrificed if the Company were to be revised.

10. Coming to the other objections, learned Judge has summarily, almost dismissively said:

The other objections, in the circumstances of the case, carry no merit. After all proxies carry out the instructions of the respective shareholders. That is the sole function of the proxy. He has no right to substitute his own opinion in the place of the definite instructions given to him. Likewise, if the Chairman is authorized to be a proxy by the Collaborator and if he had exercised such a right, it is not his personal reaction that is reflected in such exercise of proxy. On the other hand, it represents the reaction of the collaborator through such proxy,, namely the Chairman. Therefore, I find that there is no substance in the objection that there had been an improper and illegal exercise of proxy and also that the exercise of proxy by the Chairman itself is illegal.

Regarding the undue length of the meeting pressed into service by the learned Counsel for the objectors, I do not find any force. There is nothing stated by the objectors nor do I see in the report filed by the Chairman that there was any protest by any of the creditors for undue ""delay in concluding the meeting. That would mean that the meeting was unavoidably extended till 9.15 p.m. if that is beyond the control of the Chairman, the objectors cannot take advantage of that. As a matter of fact, it is seen from the report filed by the Chairman that the meeting commenced at 10.30 a.m. and lasted till 6.30 p.m.

11. It will be difficult to find any exception to the concern shown by the learned Judge that survival of the industry alone was likely to ensure continuance of employment of a large number of employees and that if it functioned, it would benefit all and would cause injury to none. Any concern for the employees of the company and others however must always weigh favourably with the interest of the unsecured creditors amongst whom are fixed Depositors, who are not members of the Company, but have invested their small savings to earn small interest thereon to augment their income in future. If they lose and others also lose equitably, there may not be anything wrong. But then if they lose more and others lose less, will it not cause discrimination? Section 391 of the Companies Act has got a purpose. It says,

(1) Where a compromise or arrangement is proposed:

(a) between a company and its creditors or any class of them; or

(b) between a company and its members of any class of them; the court may, on the application of the company or of any creditor or member of the company or in the case of a company which is being wound up, of the liquidator, order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the court directs.

(2) If a majority in number representing three-fourths in value of the creditors, or class of creditors or members, or class of members, as the case may be present and voting either in person or, where proxies are allowed under the rule made u/s 643, by proxy, at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the court, be binding on all the creditors, all the creditors of the class, all the members, or all the members of the class, as the case may be, and also on the company, or, in the case of a company which is being wound up, on the liquidator and contributories of the company; Provided that no order sanctioning any compromise or arrangement shall be made by the court unless the court is satisfied that the company or any other person by whom an application has been made under Sub-section (1) has disclosed to the court, by affidavit or otherwise, all material facts relating to the company, such as the latest financial position of the company, the latest auditor's report on the accounts of the company, the pendency of any investigation proceedings in relation to the company under Sections 235 to 251, and the like.

(3) An order made by the court under Sub-Section (2) shall have no effect until a certified copy of the order has been filed with the Registrar.

(4) A copy of every such order shall be annexed to every copy of the memorandum of the company issued after the certified copy of the order has been filed as aforesaid or in the case of a company not having a memorandum, to every copy so issued of the instrument constituting or defining the constitution of the company.

(5) If default is made in complying with Sub-Section (4), the company, and every officer of the company who is in default, shall be punishable with fine which may extend to ten rupees for each copy in respect of which default is made.

(6) The court may, at any time after an application has been made to it under this section, stay the commencement or continuation of any suit or proceeding against the company on such terms as the court thinks fit, until the application is finally disposed of.

(7) An appeal shall lie from any order made by a court exercising original jurisdiction until this section to the court empowered to hear appeals from the decisions of that court, or if more than one court is so empowered, to the court of inferior jurisdiction.

The provisions of Sub-Sections (3) to (6) shall apply in relation to the appellate order and the appeal as they apply in relation to the original order and the application.

12. Shanmukham, J. had the advantage of the judgment in *Manickchowk v. Ahmedabad Mfg. Co.* (1970) 2 C. L.J. 300. It states,

it is always a moot question what constitutes a class. Buckley on the Companies Acts, 13th edition, page 406, has observed that it is a formidable difficulty to say what constitutes a "class" of creditors. The creditors composing the different classes must have different interest. When one finds a different state of fact existing among different creditors which may differently affect their minds and their judgment, they must be divided into different classes, "class" must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest (vide *Sovereign Life Assurance Co. v. Dodd* (1892) 2 Q.R 573 ,. Speaking very generally, in order to constitute a class, members belonging to the class must form a homogeneous group with commonality of interest. If people with heterogeneous interests are combined in a class, naturally the majority having common interest may ride rough shod over the minority representing a distinct interest. One test that can be applied with reasonable certainty is as to the nature of compromise offered to different groups or classes. The company will ordinarily be expected to offer an identical compromise to persons belonging to one class, otherwise it may be discriminatory. At any rate, those who are offered substantially different compromises each will form a different class. Even if there are different groups within a class the interests of which are different from the rest of the class or who are to be treated differently in the scheme, such groups must be treated as separate classes for the purpose of the scheme. Broadly speaking, a group of persons would constitute one class when it is shown that they have conveyed all interest and their claims are capable of being ascertained by any common system of valuation. The group styled as a class should ordinarily be homogeneous and must have commonality of interest and the compromise offered to them must be identical. This will provide a rational indicia for determining the peripheral boundaries of classification. The test as stated earlier would be that a class must be confined to those persons whose rights are not so similar as to make it impossible for them to consult together with a view to their common interest.

13. As against the force of the aforequoted observations, Shanmukham, J. has thus taken notice of a different observation in the said judgment which is as follows:

The defects as far as the meeting of unsecured creditors is concerned, appears to be that the preferential and other unsecured creditors have been grouped together. The workers are preferential creditors in winding up but not otherwise would form a separate class. Instead of remitting the scheme to separate meetings of unsecured and preferential creditors in my opinion, there is ample

material in the report of the Chairman from which the votes in number and value representing the preferential creditors can be separated from the votes and value of the votes representing the other unsecured creditors.

As this is quite possible and which would be worked out while considering the ground of attack that the scheme is not approved by a statutory majority in each class, it is not necessary to direct a separate meeting of preferential creditors and other unsecured creditors.

14. It seems that the learned Judge was not informed that there were objections to the clubbing of the Fixed Deposit Holders with the sundry creditors for the goods supplied or Sundry creditors for expenses as well as other loans and short term loan. Interest of Fixed Deposit holders in retaining their investment in deposit is not similar to a person who advanced loans on hundies or otherwise advanced money to the company for earning profits. Sundry creditors for goods supplied or for expenses, the quotation above will show, have been divided into two groups, one group of Government employees and foreign collaborators and the other creditors in this category. Their separate number is nowhere available. While the Government employees and foreign collaborators are not affected, sundry creditors for expenses have been made to lose 80% of their claims. The court while resolving the voting pattern has overlooked a serious allegation that proxies were utilised to neutralize the majority of objectors and in any case, the classification had been artificial in the sense that all unsecured creditors could not form one and the same class. We have given our anxious consideration to the figures worked out in the impugned judgment. It is necessary to notice that except the number of votes" shown in the report of the Chairman, it is nowhere available as to who of the fixed deposit holders were present either in person or through proxy. Similarly it is not known who amongst those who were suppliers or advanced loans and how their figure or number was worked out. The Chairman was no longer impartial for he too was a proxy not for one but for more than one. In the absence of any independent evidence, it is not passable to accept the figures of those who voted for or against the resolution except that amongst the unsecured creditors, 363 voted, 193 for the resolution and the rest either voted against or abstained. If the number is carefully calculated, one may not find it surprising that besides the Fixed Deposit holders, the exact number of other creditors present was 194-193 are said to have voted for the resolution. We do not think it is a case to ignore the artificial classification of unsecured creditors as one group. How they have been differently treated and how they stand separately is evidence in the scheme. It will be proper that the scheme if at all has to be voted and consent obtained should be adopted by identifying the class of the unsecured creditors in the light of the observations that are available in the case of *Manickchowk v. Ahmedabad Mfg. Co.* (1970) 2 C. L.J. 300. It is unnecessary to repeat that to constitute a class, members belonging to the class must form a homogeneous group with commonality of interest and those who have such common interest, thus must be found to constitute one class, whereas those whose interests are in conflict with the interests of such a group have to be

treated as a separate class. In the instant case, the requirements of Section 391(1) of the Act, in our opinion, have not been fulfilled. The impugned judgment for the said reason is fit to beset aside and it is accordingly set aside. The case is remitted to the trial court for a re-hearing and if necessary a further direction for holding of the meeting of different classes of unsecured creditors and their consent in accordance with law.

15. In the result, the appeal is allowed. The impugned judgment is set aside. On the facts and circumstances of the case, however, there shall be no order as to costs.