(2013) 07 CAL CK 0107

In the Calcutta High Court

Case No : C.P. No. 67 of 2013 and C.A. No. 745 of 2012

In Re: Heritage Housing Finance Ltd. and Others

Date of Decision : 08-07-2013

Acts Referred:

Citation : (2014) 118 CLA 429 : (2014) 182 CompCas 247 : (2014) 124 SCL 319

Hon'ble Judges : Harish Tandon, J

Bench : Single Bench

Advocate : Manju Bhuteria, for the Appellant;Arindam Sen and Biswajit Sarkar for Union of India, for the Respondent

Judgement

Harish Tandon, J.—The only question raised in this application is whether the Central Government can object to the sanctioning of the arrangement and/or scheme because of the discrepancy in the share exchange ratio when in a shareholders'' meeting the entire scheme has been approved unanimously. At the time of moving of the application u/s 391 of the Companies Act, 1956, which provides where a compromise or arrangement is proposed between a company and its creditors or class of them or between a company and its members or class of them the court may order meeting of the creditors or class of creditors or members or class of members to be held and continued in the manner as may be directed. The court ordered the holding of the meeting of the shareholders and appointed the chairperson. Pursuant to the said order the meeting was convened and the chairperson submitted the report as well.

2. In an application u/s 394 of the said Act containing the report of the chairperson the court directed the service of the copy of the said application upon the Central Government.

3. At the time of promulgation of the Companies Act, 1956, section 394A was not incorporated therein which subsequently came to be incorporated and/or inserted by Act XXXI of 1965 with effect from October 15, 1964. The said provision contemplates the notice to be given to the Central Government for the purpose of ascertaining the objection which may be raised before passing any order either u/s 391 or section 394 of the said Act. The aforesaid provision was introduced

with the specific object, intent and purpose so that the court who is not supposed to put a mere rubber seal to the sanction of the arrangement and/or scheme proposed u/s 391 of the said Act. It is obviously for the definite object and purpose that the aforesaid arrangement/or scheme is fair, reasonable and is not oppressive to the members or the public.

4. The Central Government in the affidavit have taken the only objection that the share exchange ratio as proposed in the said scheme and/or arrangement is not fair and reasonable. The affidavit filed by the Regional Director on behalf of the Central Government have annexed a report of the chartered accountant relied on by the petitioners wherein the various aspects relating to the determination of the share exchange ratio for one equity share of Rs. 10 each in the transferor company to be credited as fully paid up as every 20 equity shares of Rs. 10 each fully paid-up and held by the shareholders in Heritage Housing Finance Ltd., and in likewise manner the share exchange ratio should also be adhered to in case of Mangalam Services Ltd., is indicated.

5. This court before sanctioning the scheme invited the petitioners to address this court whether they are agreeable to the modification of the scheme in the manner as suggested in the affidavit filed by the Regional Director.

6. The learned advocate appearing for the petitioners, however, submits that the Central Government is denuded of its power to raise any question relating to the share exchange ratio as the same should be left to the commercial wisdom of the shareholders.

7. In support of the aforesaid contention reliance is placed upon a judgment of the Chancery Division rendered in Sussex Brick Co. Ltd., In re [1960] 1 All ER 772 (Ch D). By placing reliance on a judgment of the apex court in the case of Miheer H. Mafatlal Vs. Mafatlal Industries Ltd., it is further contended that when the majority shareholders have consented to the ratio of exchange of shares who are likely to be affected by the said arrangement, the Central Government should not raise any objection in relation thereto and therefore, the aforesaid objection of the Central Government should not be looked into.

8. It is audaciously contended that the valuation is a matter within the realm of the experts unless it shockingly appears to be unfair and/or unreasonable, the court should not sit as an appellate court over the decision of the majority shareholders and placed reliance upon a Division Bench judgment of this court in the case of Bengal Tea Industries Ltd. and Others Vs. Union of India and Another,

9. It is further contended that relating to the share exchange ratio a report of a chartered accountant is annexed, who in his wisdom, has determined such exchange value and unless the method adopted by the chartered accountant can be proved to be unreasonable or tainted with malice, the court should not refuse to sanction the scheme on the basis of an objection raised by the Central Government and placed reliance upon the co-ordinate Bench judgment in the case of In Re: Joonktollee Enterprises Ltd. and Others,

10. Lastly, it is contended that the valuation of share should be left to the shareholders who may ultimately be interested in the scheme and/or arrangement and therefore, the Central Government could not have raised dispute relating to the share exchange ratio and relied upon the judgment of the apex court in the Hindustan Lever Employees'' Union Vs. Hindustan Lever Limited and others,

11. The learned advocate appearing for the Central Government, however, submits that section 394A of the said Act does not prohibit the Central Government to bring before the court the unreasonableness and/or unfairness in the share exchange ratio and the powers so conferred under the said provision should not be restricted as sought to be pleaded by the petitioners.

12. Upon hearing the respective submissions, as indicated earlier, the pivotal objections raised by the Central Government for sanctioning the proposed scheme is the share exchange ratio as suggested in the said scheme. The plain reading of the provision contained u/s 394A does not postulate the nature of the objection required to be raised by the Central Government but what it provides is that the court before passing any order either u/s 391 or 394 the court must take into consideration the representations and/or objections raised by the Central Government. The court is not required to put a mere rubber seal to a proposed arrangement and/or scheme unless it is specified that the proposed arrangement and/or scheme is not only fair and reasonable to the creditors or class of creditors or members of class of creditors but also in conformity with public policy and/or interest.

13. Before proceeding further, this court must take note of the observations made by the apex court in the Hindustan Lever Employees'' Union Vs. Hindustan Lever Limited and others, wherein in paragraph 13 thereof the apex court specifically observed that even if the shareholders have consented to the valuation of the shares to be reasonable and fair that is done in their commercial wisdom but the court is certainly not bound by such decision. The relevant portion of the said judgment is extracted hereinbelow (page 44 of 83 Comp Cas):

Transfer of shares to a foreign company on undervaluation is of course a matter of concern. It is true that the transfer of shares by one company to another company is primarily to be determined by the shareholders and, therefore, if 99 per cent, are of the view that the valuation of the shares was reasonable and fair then the court should be slow to interfere with it. But what is necessary to be emphasised is that a shareholder may not be interested in the ultimate effect of allotting shares to a multinational on a low price valuation, but the court certainly is. For instance, if the value of the share which has been determined at Rs. 105 for allotment to HLL is hypothetically determined, say at Rs. 210, then the result would be that UI, will have to pay more in lieu of getting the shares and that could definitely bring more foreign exchange to the national stream. It is just one illustration to demonstrate how low pricing of shares affects the public interest. That the valuation was low-priced was found even by the High Court. Therefore, it is not open to the respondents to argue that the valuation of Rs. 105 having been accepted by majority of almost all the shareholders, no public interest is involved in it. No further need be said as allotment of shares to UL at Rs. 105 is not approved by the Reserve Bank of India. It has been challenged before the High Court and is pending adjudication.

(emphasis here printed in italics supplied)

14. In the case of Miheer H. Mafatlal Vs. Mafatlal Industries Ltd., the apex court was considering the matter relating to sanction of the scheme on the basis of an objection raised by the minority director. The apex court formulated five points where fifth point relates to share exchange ratio of the equity shares of the transferor and transferee companies. In the said judgment, the apex court took note of the observations made by Sahai J. while concurring the judgment rendered in the case of Hindustan Lever Employees'' Union Vs. Hindustan Lever Limited and others, that the jurisdiction of the court in sanctioning a claim of merger is not to be ascertained in mathematical accuracy as the company court does not exercise the appellate jurisdiction, but the court proceeded to observe that section 394 cast obligation on the court whether the scheme or arrangement is contrary to public interest or unfair and unconscionable.

15. In paragraph 40 of the said judgment the apex court observed that the valuation of share is a technical and complex problem which can be appropriately left to the consideration of the experts in the field of accountancy. The apex court in the said judgment, however, refused to interfere with the scheme as the objection to the share exchange ratio was raised by one of the directors who himself was present in a meeting and dissented. The court have further proceeded as no contrary expert opinion regarding the valuation of the assets of the transferor company was placed before the court such object is not tenable. The relevant portion of the said judgment is extracted hereinbelow (page 836 of 87 Comp Cas):

Not only that, even before the court he did not submit any contrary expert opinion regarding the valuation of shares of the transferor and transferee companies for supporting his ipse dixit that the correct ratio would be 6:1 so far as the transferor and transferee companies were concerned. Shri Shanti Bhushan, learned senior counsel for the appellant, having realised this difficulty submitted that at least these proceedings are continuation of proceedings before the High Court, therefore, this court may now in order to satisfy itself send for the opinion of an expert. It is difficult to agree.

16. What could be culled out from the aforesaid judgment is that an objection to share exchange ratio was raised by one of the directors and not by the Central Government.

17. This court can lend support from some of the observations made by the apex court in the said judgment where the apex court have in unequivocal terms held that the question of valuation of the share for the purpose of share exchange

ratio is within the realm of an expert which could be deducible from the above observations (page 836 of 87 Comp Cas):

For all these years neither before the learned single judge nor before the High Court in appeal the appellant thought it fit to request the court to either call for the report of any other expert on valuation of shares nor did he himself get such report for placing for consideration of the court in support of his supposed better ratio.

18. The Division Bench in the case of Bengal Tea Industries Ltd. and Others Vs. Union of India and Another, oes not laid down that even if the share exchange ratio is unconscionably unfair or have been done without following the proper method, still the court should allow as the shareholders have uniformly accepted and/or vetted in favour of the proposed scheme. The Division Bench observed that the ratio of share exchange to be determined on the valuation made by an expert. In paragraph 60 of the said judgment the Division Bench has proceeded that in the event any objection is raised by any of the shareholder, the matter would have taken a different complexion as it would require a further probe into the question of ratio of share exchange. The aforesaid judgment, in my considered view, runs contrary to the ratio laid down in the case of Miheer H. Mafatlal Vs. Mafatlal Industries Ltd., where the court overruled the objections raised by one of the shareholder-director on the finding that the same should be left to the domain of an expert.

19. As an alternative submission, the petitioners tried to impress upon the court that fairness opinion is obtained from one Karn Merchant Bankers Ltd., relating to the report of the chartered accountant who determined the share exchange ratio as the company is listed in the Calcutta Stock Exchange.

20. According to the petitioner, the said report contemplates that the share exchange ratio is fair as determined by the said chartered accountant and, therefore, the objection of the Central Government should be overlooked and the scheme should be sanctioned by the court.

21. Before dealing with the same, this court must determine the basic point as raised by the petitioner that it is not within the competence of the Central Government to raise any objection to the share exchange ratio after approval of the majority shareholders.

22. The apex court in the case of Miheer H. Mafatlal Vs. Mafatlal Industries Ltd., and Hindustan Lever Employees'' Union Vs. Hindustan Lever Limited and others, as relied by the petitioner, ever suggested that the Central Government is denuded of any power to raise objection as to the share exchange ratio.

23. The company court has to act as a check post and should not allow the arrangement and/or scheme to percolate through its machinery, merely because the majority shareholders have consented and/or agreed the proposed arrangement and/or scheme. If the contention as raised by the petitioner is

accepted, the provisions contained u/s 394A would render otiose and/or nugatory and/or meaningless. The Central Government is certainly within their competence to raise the objection as they are required to see that no unfairness and/or unreasonableness to be shown either to the creditors or the class of creditors and/or members or the class of members and public interest, which certainly imbibes itself with the power to question the said share exchange ratio.

24. This court, therefore, does not find any force in the submission of the petitioner that the Central Government cannot raise objection to the share exchange ratio.

25. As indicated above, it is tried to be contended at the instance of the petitioner that there are other experts'' opinions before the company court and the same should be looked into for the purpose of adjudicating and/or determining the objection by the Regional Director. The Regional Director in the said affidavit indicated that the fair value of the inter holdings of shares between the transferor companies have not been taken into consideration for valuation of shares for the purpose of calculation of the exchange ratio and, therefore, the said exchange ratio is not reasonable and fair.

26. The fairness opinion was sought before convening the meeting and the same was placed before the shareholders and after considering the same the shareholders have unanimously approved the proposed scheme and/or arrangement.

27. Although a fairness opinion has been obtained, which suggests that the exchange ratio has been valued in line with the past practices and cannot be said to be unfair or improper. The said fairness opinion is based upon the economic regulatory monetary market and other conditions as on the date of September 12, 2012 and endorse the manner in which the valuation has been made by the said chartered accountant.

28. This court, therefore, finds that in order to dispel all the clouds raised because of the conflicting opinions of the expert, an independent chartered accountant from the panel of the official liquidator should be appointed for the purpose of verifying the share exchange ratio as indicated in the proposed scheme.

29. This court, therefore, directs the official liquidator to engage a chartered accountant from its panel, who shall submit the report before this court within three weeks'' from the date relating to the fairness and/or reasonableness of the share exchange ratio, and the cost for such purpose shall be borne by the petitioner. The petitioner is directed to hand over all the relevant documents to the said chartered accountant required for the said purpose within three days from date. Let a copy of this order be communicated to the official liquidator forthwith. Let the matter appear on July 29, 2013.

