

(1992) 03 MP CK 0034

In the Madhya Pradesh High Court

Case No : Company Petition No's. 10, 11 and 12 of 1990

**In Re: Kriti Plastics Pvt. Ltd.;
 In Re: Purti Pipes and Processors Pvt. Ltd.**

Date of Decision : 31-03-1992

Acts Referred:

Companies Act, 1956 — Section 394

Citation : (1992) 37 MPLJ 671 : (1992) MPLJ 671

Hon'ble Judges : A.G. Qureshi, J

Bench : Single Bench

Advocate : Chapekar, for the Appellant;

Judgement

A.G. Qureshi, J.

This order shall govern the disposal of Company Petition No. 10 of 1990 (Kriti Plastics Pvt. Ltd.), Company Petition No. 11 of 1990 (Kasta Extrusions Pvt. Ltd.) and Company Petition No. 12 of 1990 (Purti Pipes and Processors Pvt. Ltd.). These three petitions have been filed by three different private limited companies duly incorporated under the Companies Act, 1956. The object of the petitions is to obtain sanction of this court to compromise or arrangement whereby Kasta Extrusions Pvt. Ltd., and Purti Pipes and Processors Pvt. Ltd. will amalgamate with another company, Kriti Plastics Pvt. Ltd. According to the scheme of amalgamation, the transferor-companies are Kasta Extrusions Pvt. Ltd., Indore and Purti Pipes and Processors Pvt. Ltd. also having its office at Indore and the transferee-company is Kriti Plastics Pvt. Ltd., which has also its office at Indore. The transferee-company, Kasta Extrusions Pvt. Ltd., is engaged in the business of manufacturing rigid PVC pipes and the transferor-company, Purli Pipes and Processors Pvt. Ltd., is also engaged in the business of manufacture of rigid PVC pipes. Both the transferor companies by resolution of the board of directors dated April 4, 1990, as well as the transferee-company by resolution of its board of directors dated April 4, 1990, unanimously resolved to amalgamate/merge the transferor-companies, Kasta Extrusions Pvt. Ltd. and Purti Pipes and Processors Pvt. Ltd., into transferee-company, Kriti Plastics Pvt. Ltd. subject to the approval

of members/shareholders in general meeting, court, the Central Government and other concerned authorities as may be required.

The three companies presented an application for making a request to the court for convening a meeting of the shareholders and appointing a chairman. Accordingly, the court appointed Smt. M. Chaphekar as chairman and Shri Uday Vadnerkar as alternate chairman and directed issuance of notices in accordance with rules. After the meeting, the chairman submitted her report and according to the report there was unanimous decision of all the shareholders present approving the resolution of the board of directors and all the members accorded their approval to the amalgamation and the scheme of amalgamation. The arrangement of the share ratio was also decided in that meeting.

After the report, a prayer was made to this court by the three companies to approve the amalgamation of the three companies in accordance with the scheme. The court thereupon sought a report from the official liquidator as required by the Act and a firm, T. Unni and Co., chartered accountants of Indore, was appointed to scrutinise the accounts and other records of the company to assist the official liquidator in submitting the report. The official liquidator has filed his report along with the report of the chartered accountant. According to the report of the official liquidator u/s 394(1) of the Companies Act, 1956, the amalgamation scheme is in violation of Section 393 of the Companies Act and the amalgamation is ultra vires the memorandum of association of the transferee-company and the business proposal does not appear to be viable. However, the main emphasis of the official liquidator is that the scheme of amalgamation is nothing but a device to avoid payment of capital gains tax and has been so arranged so as to help avoidance of wealth-tax by Chetak Builders Pvt. Ltd. The valuation of the assets is also defective and unfair. The modus operandi has been adopted in execution of a sub letting agreement of September 1, 1990, whereby an attempt to avoid payment of stamp duty and capital gains tax has been made. The provisions of the Import Trade Control Order, 1955, have also been violated. Clearance from the Pollution Control Board has not been sought for manufacture of organic fertiliser. As such the scheme of amalgamation is prejudicial to the public interest.

A reply was filed to the report of the official liquidator by the company, whereupon a rejoinder was again filed by the official liquidator. In the reply filed by the companies it has been stated that compliance with Section 393(1) is to be settled by the court. All the procedural formalities regarding the amalgamation were complied with. Necessary notices were issued with the permission of the court. Hundred per cent, share-holders were present in the meeting and they have approved the scheme of amalgamation as well as the share exchange ratio which is based on audited books of account. The creditors were given notices as per provisions of the Companies Act and the share exchange ratio was modified by all the shareholders and the creditors who were present in the respective meeting. The modification of the share exchange ratio is based on audited

balance-sheets.

As regards the objection regarding viability it has been stated that business success is the outcome of the entrepreneur's experience and organised effort. Therefore, it cannot be said that the project to manufacture the organic fertiliser by Kriti Plastics Pvt. Ltd. is only an experimental exercise. It had also been submitted that the business is a combination of management and resources and, therefore, it is not necessary for all the companies desiring amalgamation to provide substantial resources. Actually the three companies are privately and closely held by the family members and they propose to merge into a single company. The shares to be allotted by the Kriti Plastics Pvt. Ltd. on amalgamation will be in the same proportion to the shares held by the family members in Purti Pipes and Processors Pvt. Ltd. and Kasta Extrusions Pvt. Ltd. Therefore the question of transfer for purpose of avoiding capital gains does not arise. There is no device to transfer the assets of the transferor companies to a third party and new interest of another party is not being created. Therefore, there is no scheme for avoiding capital gains tax.

As regards the valuation of the company assets it has been stated that that was done by the chartered accountant and the valuers authorised by the Government of India in this behalf. The official liquidator could not make a grievance regarding the question of public interest in view of the admitted position that the basis of valuation adopted was one which is recognised in the Rules framed under the Wealth-tax Act for the purpose of the said Act. The grievance that the valuation was arbitrary and unreasonable cannot, therefore, be made. The revaluation of the assets was made by the company when they were advised to do so during the negotiation with bankers for financial assistance. The share capital of the company was increased on the advice of the State Bank of Indore, the bankers of the transferor-company. Therefore, the company has followed the necessary procedure for transfer of material on loan and, therefore, there is no violation of any law of the land. Clearance from the Pollution Board has also been received and, therefore, the scheme of the company deserves to be allowed. Some annexures have also been filed to show that Kriti Plastics Pvt. Ltd., the transferee-company, is already in the business of manufacturing organic fertilizer.

Learned counsel for the companies, Shri Chapekar, has strenuously argued that the scope of the report of the official liquidator is limited u/s 394(1) of the Companies Act. The court obtains the report of the official liquidator only for the purpose of knowing that the affairs of the company have not been conducted in a manner prejudicial to the interest of its members or the public interest. Therefore, the official liquidator could not go into the reports of the chartered accountant of the company and the official valuers of the assets and say that the valuation is bad or that the report of the chartered accountant is not in accordance with the law. Therefore, when all the members/share holders of the three companies have unanimously agreed for amalgamation it cannot be said that the affairs of the company have been conducted in a manner prejudicial to

the interest of its members or public interest.

On the other hand the official liquidator, Shri S. C. Gupta, maintains that the report is based on the inspection of the accounts of the three companies and, therefore, the report that the amalgamation scheme is not in the interest of the shareholders and the public interest is justified.

On perusal of the report of the official liquidator and the chartered accountant, I find that the official liquidator has taken great pains in going through all the aspects of the management of the company and the scheme of amalgamation.

The chartered accountant appointed by the court has also thoroughly checked the books of account of the company and I appreciate the labour put in by the official liquidator in submitting his report. The official liquidator is actually an agency of the court to satisfy itself that the affairs of the company to be dissolved have not been conducted in a manner prejudicial to the interest of its members and public interest. Therefore, the court has to ascertain that the schemes of amalgamation are sanctioned only after the court has the other side of the picture before it and the report filed by the official liquidator along with the scheme of amalgamation leads the court to arrive at a conclusion that in the amalgamation scheme the interests of the shareholders are not jeopardised in any way and the public interest is not being defeated. Therefore, the report of the official liquidator in all aspects of the matter can be taken into consideration by the court. Therefore, I find no force in the argument advanced by the learned counsel for the companies that the report of the official liquidator in respect of the affairs of the company cannot be looked into pertaining to its assets and the earlier transfers.

On examining the amalgamation scheme, I find that actually all the three companies, i.e., the two transferor-companies and one transferee-company, have their office at the same place, i.e., Mehta Chambers, Siyaganj, Indore. The shareholders of all the three companies are also practically common and this fact cannot be disputed that the shareholders of the three companies are all family members and closely knit. Therefore, I am of the opinion that in view of the unanimous resolution passed by the board of directors of the three companies and approved by all the shareholders unanimously and the creditors having no objection to the amalgamation, the scheme of amalgamation cannot be said to be a scheme against the members of the companies. Therefore, the scheme of amalgamation has to be approved on that ground.

The objection of the official liquidator, however, is that the scheme of amalgamation is a device to avoid capital gains tax and the payment of stamp duty and also to legalise the earlier illegal acts. In view of the aforesaid the court has to consider whether any safeguards have to be provided so that the amalgamation may not result in avoidance of capital gains tax or result in the illegal transfer of any property which otherwise may not be transferable under the law. Hon''ble Justice Shri D. A. Desai, a judge of the Gujarat High Court (as

he then was) in the case of Wood Polymer Limited, In re and Bengal Hotels Pvt. Ltd., In re [1977] 47 Comp Cas 597 (cal) has held that merely because it is shown to the court that the requisite formalities in relation to the proposed scheme of amalgamation have been carried out, the court is not bound to sanction the scheme. The court has a discretion in the matter either to sanction or refuse to sanction the scheme. In the same judgment it has also been emphasised that the report of the official liquidator has to be obtained before passing any order on the amalgamation scheme. If the court finds that the amalgamation scheme has been made solely to facilitate the transfer of building to the transferee-company of a transferor-company without attracting the liability to pay capital gains tax the court can refuse to sanction the scheme because if such a scheme is approved the scheme of amalgamation would result in the avoidance of payment of capital gains tax. If the court arrives at a conclusion that the purpose of amalgamation is to defeat tax by creating a paper company and transferring an asset to such company which can without consequence be amalgamated with another company to whom the capital asset was to be transferred so that on amalgamation it may pass on to the amalgamating company, it would distinctly appear that the provision for such a scheme of amalgamation was utilised for the avowed object of defeating tax. The court has emphasised that a company may arrange its affairs in such a way that under the law may be exempt from tax, but that is permissible only if it is done without the aid of the court. However if the indulgence of the court is sought, then the court cannot allow the avoidance of tax by approving the amalgamation scheme and public interest enjoins upon the court to find out why the transferee-company came into existence and can go into the details of the affairs of the transferor and transferee-companies. The machinery of judicial process cannot be pressed into service for defeating the public interest and the court would not lend its assistance for that purpose. In that case the scheme of amalgamation was refused by the court.

The case of McDowell and Co. Ltd. Vs. Commercial Tax Officer, was considered by the Supreme Court in respect of tax planning, wherein the Supreme Court has said that tax planning may be legitimate provided it is within the framework of the law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid payment of tax by dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuge. In the aforesaid judgment the Supreme Court has held that although planning of the accounts of the company in such a way that they may avoid certain taxes is permissible under the law, colourable devices cannot be part of the tax planning and the court should not allow avoidance of tax if it is planned in such way that by the order of the court the tax can be avoided.

In view of the above authorities, I am of the opinion that reading the scheme of amalgamation and the report of the official liquidator together, it cannot be said positively that the sole purpose of the whole exercise of amalgamation is

avoidance of tax. Therefore, the amalgamation scheme cannot be rejected on this ground. However, the court while passing the amalgamation order can always issue directions, which shall form part of the amalgamation scheme, so that the public interest is not adversely affected because of the scheme of amalgamation.

In the result in the circumstances placed before me I am of the opinion that the amalgamation scheme has to be approved, but subject to the following conditions :

(1) that the approval of this amalgamation scheme does not in any way dispense with the formality of execution of instrument of conveyance or other documents for effectively vesting of the property and rights of the transferor-companies in the transferee-company, nor does the approval of the scheme give any right to the properties which in law are not assignable or transferable to the transferee-company. If the transfer has to be effected it has to be effected in accordance with the law of the Transfer of Property Act and in those cases where the property is on a lease with restriction on the transfer or sub-letting of such property, the sanction of the relevant authority is sought before its transfer.

(2) If, as a result of the transfer of any assets or shares of the transferor-company to the transferee-company a liability to the capital gains tax may arise against any company or its shareholders, this order shall not absolve such company or the shareholders from payment of taxes which may be leviable under the existing taxing laws and as such the taxing authorities shall be free to proceed in the matter of tax, irrespective of the present order of amalgamation.

(3) The present order of amalgamation will not absolve any of the companies or its directors from the liability for breach of any law or control order which might have been committed before the order of amalgamation.

This amalgamation order is being passed strictly with a view that the three companies which have as its shareholders members of closely knit families have desired to form one company to launch their activities in the new field of organic fertilisers and as stated by learned counsel for the companies the amalgamation scheme is not a device to avoid any tax payment or to overcome any illegal act committed on behalf of the company. As such the aforesaid conditions imposed in the amalgamation order will sufficiently take care of the doubts expressed by the official liquidator on the basis of the inspection of the record and the accounts of the company.

With the aforesaid conditions the amalgamation scheme is approved on this 31st Day of March, 1992.