

(2012) 12 GUJ CK 0119

In the Gujarat High Court

Case No : CP No. 228 of 2012 in CA No. 307 of 2012 and CP No. 231 of 2012 in CA No. 310 of 2012

In Re: Prayas Engineering Ltd.

Date of Decision : 21-12-2012

Acts Referred:

Companies Act, 1956 — Section 100, 101, 102, 103, 205

Citation : (2013) 115 CLA 117

Hon'ble Judges : R.M. Chhaya, J

Bench : Single Bench

Advocate : Swati Soparkar and Y.V. Vaghela, for the Appellant;

Judgement

R.M. Chhaya, J.—These are the petitions filed by four group companies, viz., Prayas Engineering Ltd., EMTICI Engineering Ltd., Elecon Engineering Co. Ltd. and Elecon EPC Projects Ltd., for the purpose of obtaining the sanction of this court to a scheme of arrangement in the nature of de-merger and transfer of different undertakings between these four companies, proposed under sections 391 and 394 read with sections 100 to 103 of the Companies Act, 1956 ("the Act"). It has been submitted that all the companies under the present scheme belong to the same group of management. All these companies are engaged in manufacturing and/or marketing of specialised engineering products used in several segments of industries. Their activities are similar and interconnected in a complex manner. Most of the companies are engaged in variety of activities. They are profit making and dividend paying companies. It has been realised by the management of these companies that with the increasing competition, changing technologies and several other factors, it is necessary that each company concentrate in a given sphere of activities. It is, therefore, proposed that the activities of the companies be segregated on the basis of the product lines, viz., MHE Division and Gears Division and under the present scheme of restructure by means of de-merger and transfer as well as slump sale, the specific activities be undertaken by specific companies instead of all the companies. It is envisaged that the proposed scheme and realignment of activities between these companies shall enable the companies to achieve

operational and managerial efficiency; and increase in the ability to raise funds. It is envisaged that this will be beneficial to the respective companies, its shareholders, employees as well as creditors. The petitions give in detail the commercial advantages that would flow by virtue of the proposed de-merger.

2. (i) It has been submitted that vide order dated 11th September, 2012 passed in Co. Appl. No. 307 and 308 of 2012, filed by Prayas Engineering Ltd. and EMTICI Engineering Ltd., being the two de-merged companies, and being closely held limited companies, the meetings of the equity shareholders were dispensed with in view of the written consent letters from all its shareholders, approving the proposed scheme, being placed on record; whereas separate meetings of the secured creditors and unsecured creditors of these companies were directed to be/convened for the purpose of seeking the approval from all the concerned parties to the proposed scheme. Pursuant to the directions, issued with regard to the meetings, after the due notices to the concerned parties as well as the public notice, the said meetings were duly convened respectively on 22nd and 23rd October, 2012. The proposed scheme was duly approved unanimously at all the respective meetings of the secured and unsecured creditors, i.e., 100 per cent in number and 100 per cent in value by the creditors present and voting at the respective meetings. The chairmans reports for all these meetings are placed on record confirming the result of these meetings.

(ii) Vide the order dated 11th September, 2012, passed in Company Application No. 309 of 2012, filed by Elecon Engineering Co. Ltd., the First Resulting Co. and the transferor-company, being the listed public limited company, separate meetings of equity shareholders, secured creditors and unsecured creditors were directed to be convened for the purpose of seeking the approval from all the concerned parties to the proposed scheme. Pursuant to the directions, issued with regard to the meetings, after the due notices to the concerned parties as well as the public notice, the same were duly convened, respectively on 22nd and 23rd October, 2012. The proposed scheme was duly approved unanimously at the respective meetings of the secured creditors and unsecured creditors, i.e., 100 per cent in number and 100 per cent in value by the creditors present and voting at the respective meetings. In case of the meeting of the equity shareholders, the scheme was approved by requisite statutory majority of 97.24 per cent in number and 81.6 per cent in value. The chairmans reports for all these meetings are placed on record confirming the result of these meetings.

(iii) Vide the order dated 11th September, 2012, passed in Company Application No. 310 of 2012, filed by Elecon EPC Project Ltd., the second resulting company, being the wholly owned subsidiary of Elecon Engineering Co. Ltd., the meeting of the equity shareholders of the company was dispensed with in view of the written consent letters from all its shareholders, approving the proposed scheme, being placed on record.

3. The substantive petitions for the sanction of the scheme were filed by all these companies which were admitted on 7th November, 2012. The notice for the

hearing of the petitions were duly advertised in the newspapers being Indian Express English daily and Sandesh Gujarati daily both Ahmedabad edns. of 13th November, 2012 and the publication in the Government Gazette was dispensed with as directed in the said orders. Pursuant to the said publication in the newspapers, no objections were received by the petitioner or its advocate.

4. Notice of the petition have been served upon the Central Government, and Shri Y.V. Vaghela, learned Central Government counsel appears for the Central Government. An affidavit dated 5th December, 2012 has been filed by Mr. Kashmir Lal Kamboj, the Regional Director, North-Western Region, Ministry of Corporate Affairs, whereby some observations are made. The same pertain to- (a) the details of the assets and liabilities of the de-merged undertakings, and (b) the accounting treatment as proposed under the scheme.

5. The attention of this court is drawn to the Additional Affidavit dated 18th December, 2012, filed by Mr. Paresh M. Shukla on behalf of the petitioner-companies, whereby all the above issues have been dealt with. I have further heard submissions made by the learned advocate appearing for the Central Government, and Mrs. Swati Soparkar, learned advocate appearing for the petitioners as follows:

(a) It has been pointed out on behalf of the petitioners that the petitioner companies have submitted the broad picture of the assets and liabilities of all the de-merged undertakings as on 31st March, 2012 to the Regional Director. It has been further submitted that since all the undertakings have running business, these details are bound to undergo change even in normal course of business. Upon sanction of the scheme, the petitioner company is required to furnish the schedule of fixed assets only as on the date of the sanction of the scheme by the hon'ble court, along with the drawn up order in accordance with the applicable Form as provided in Company Court Rules. The company has undertaken to comply with the said requirement.

(b) With regard to the issue of accounting treatment proposed under the scheme to treat the reserves arising under the scheme as general reserve and to treat the same as free reserves, it has been submitted on behalf of the petitioner-companies that the contention of the Regional Director that the said proposal is contradictory to the provisions of section 205 of the Act is ill founded. It has been submitted that the petitioner companies are authorised to provide for the specific treatment to its reserves under the scheme. Further, the concerned parties, viz., shareholders, secured creditors and unsecured creditors of all these companies have approved the scheme without raising any objection to the said clause. Even the concerned stock exchanges have approved the scheme with the said clause without any objection. It has been further pointed out that the said issue is settled vide series of judgments given by different High Courts and the Apex Court. Reliance is placed upon the following judgments: Bhagwati Developers Vs. Peerless General Finance and Investment Co. and Others, , Highland Distilleries Ltd. and Others Vs. Shaw Wallace Distilleries Ltd., ; In Re:

Sutlej Industries Ltd., . It has also been pointed out that recently, the Division Bench of Gujarat High Court has also taken the same view in the matter of In Re: Adishree Tradelinks P. Ltd., ; being OJ Appeal No. 31 to 34 of 2012, after considering all above judgments; and held that the company is entitled to provide for the accounting treatment for such reserve arising out of the excess of net assets over the share capital issued by the resulting company as general reserve and the same can be treated as free reserves for all purposes.

6. In view of the explanation given by the petitioner and considering the ratio laid down by this court in OJ Appeal No. 31 of 2012 and allied matters the objection raised by Regional Director deserves to be negated.

7. It is pertinent to note that the Division Bench of this court in the case of Adishree Tradelinks (P.) Ltd., being OJ Appeal No. 31 to 34 of 2012 has considered the identical observation as raised by the Regional Director in this case and has observed, thus:

7.1 In this behalf reference is required to be made to a decision of the hon''ble Apex Court in the case of Bhagwati Developers Vs. Peerless General Finance and Investment Co. and Others, . In the said case, the Supreme Court has considered the aspect of utilisation of reserve arising out of revaluation of assets for the purpose of issuing fully paid-up bonus shares, therein, it was found that article 182 authorised the company to issue bonus shares out of reserve, arising from revaluation of capital assets. Therefore, in the said case, it was held that the company was entitled to issue bonus shares out of revaluation reserve.

7.2 The learned counsel for the appellants has next relied on a decision of the learned Single Judge of this court rendered in Company Petition Nos. 59 & 60 of 2009, dated 8th May, 2009. In the aforesaid case, the learned Single Judge held that any profit arising out of capital transaction, such merger or demerger, which can be treated as capital profit, and hence, the same can be transferred to capital reserve and not to general reserve. In the aforesaid case, the learned Single Judge has considered the provision of section 205 of the Companies Act and the aspect of issuing bonus shares out of credit standing in the reserve account. Relying upon the observations made in the case of Bhagwati Developers (supra), the learned Single Judge, in para 12 thereof, has held as under:

12. The court further derives support from the decision of hon''ble Supreme Court in the case of Bhagwati Developers Vs. Peerless General Finance and Investment Co. and Others, , wherein the court was concerned with the question of bonus shares issued out of revaluation reserves. In this context, it was observed that section 205 of the Companies Act, 1956 provides that dividend could only be paid out of profits. The proviso to sub-section (3) of section 205 permits capitalisation of profits on reserve of a company for the purpose of issuing fully paid-up shares or paying up any money for the time being unpaid on any shares held by the members of the company. Thus, the Companies Act clearly and specifically permits utilisation of reserve arising out of revaluation of

assets for purpose of issuing fully paid-up bonus shares.

7.3 Learned counsel for the appellants has also relied upon another decision of the learned Single Judge of this court reported in *In Re: Paramount Centrispun Castings P. Ltd.*, wherein in para 19, it is held as under:

19. With regard to the Accounting Standard-14 as discussed above, the legal position is also very clear. The Allahabad High Court in the case of *In Re: Jagran TV (P.) Ltd.*, has taken the view that with regard to Accounting Standard-14, a Statement was given in Delhi High Court that since the transferor-company will merge into the transferee-company, the Accounting Standard-14 will be followed. The court further derived support from the decision of the hon'ble Supreme Court in the case of *Bhagwati Developers Vs. Peerless General Finance and Investment Co. and Others*, wherein the court was concerned with the question of bonus shares issued out of revaluation reserves. In this context it was observed that section 205 of the Companies Act, 1956 provides that dividend can be only paid out of the profits. Proviso to sub-section (3) of section 205 permits capitalisation of profit of reserve of a company for the purpose of issuing fully paid up shares or paying up any money for the time being unpaid on any shares held by the members of the company. Thus, the Companies Act clearly and specifically permits utilisation of reserve arising out of revaluation of assets for the purpose of issuing fully paid up bonus shares.

7.4 The learned counsel for the appellants, then, relied on a decision of the High Court of Rajasthan in *In Re: Sutlej Industries Ltd.*, wherein the Rajasthan High Court has observed that the creditors and shareholders of both the companies approved the proposed scheme, which was objected to by the Regional Director in regard to a clause laying down that in case any amalgamation/arrangement reserve arose, it would be treated as free reserve for distribution to shareholders and since, utilisation of arrangement/amalgamation reserve for distribution to shareholders was not objected to by the shareholders and the scheme was approved unanimously in the meeting of the shareholders, there was no reason to exclude that clause from the proposed scheme. It was, therefore, held that since proposed scheme appeared to be fair, reasonable and in the interest of shareholders, scheme was to be sanctioned.

7.5 The learned counsel for the appellant, next, relied upon a decision of the Punjab & Haryana High Court in *Motorola India (P.) Ltd.*, *In re.* [2006] 71 SCL 444,

31. The objection that the surplus arising out of the scheme of amalgamation, i.e., "amalgamation reserves" is of capital nature and cannot be considered as general reserve as the general reserve, is free for distribution to the shareholders of a company in the form of dividends, bonus shares, whereas amalgamation reserve cannot be utilised for distribution to the shareholders. In respect of the said objection of the Regional Director, it is pointed out that the accounting standard issued by the Council of Institute of Chartered Accountants of India

specifically provides for a treatment in respect of such amalgamation reserves in terms of clause 23 of the Accounting Standard-14, therefore, in terms of the scheme, it is deemed to specify the user of amalgamation reserve.

7.6 Considering the various case laws, it is clear that the reserve can be utilised for the purpose of declaring dividends. Since, aforesaid aspect was not pointed out to the learned counsel for the appellant, either at the time of hearing of the petition or when the matter was kept for dictating the order, in our view, there was no justification in imposing such a condition, while sanctioning the scheme in connection with non-utilisation of amalgamation reserve for the purpose of declaring dividend. Here, it is required to be noted that no objection was taken by the Regional Director to the said clause and even the shareholders have unanimously approved the scheme with the original clause 10.5. Considering the same, it cannot be said that incorporation of the said clause is in violation of public policy and as held by various courts, such amalgamation reserve can be utilised for the purpose of declaring dividends. Even, the learned Single judge of this court has, earlier, taken the similar view. In view of the same, the direction given by the learned Single Judge that such amalgamated reserve shall not be used, in any manner, for declaring dividend, requires to be set aside and the scheme is held to have been sanctioned as a whole, including the original clause 10.5 of the scheme.

8. Considering all the facts and circumstances and taking into account all the contentions raised by the affidavits and reply affidavits, considering the decisions of other High Courts, Supreme Court and the Division Bench of this High Court on the issues raised by the Regional Director and the submissions during the course of hearing, I am satisfied that the observations made by the Regional Director, Ministry of Corporate Affairs, do not survive. I have come to the conclusion that the present scheme of arrangement is in the interest of its shareholders and creditors as well as in the public interest and the same deserves to be sanctioned.

9. The proposed scheme of arrangement is hereby sanctioned. Prayers in terms of paragraph 22(a) of the CP Nos. 228, 229 and 230 of 2012 and prayers made in paragraph 15(a) of the CP No. 231 of 2012 are hereby granted. The petitions are disposed of accordingly. So far as the costs to be paid to the Central Government standing counsel is concerned, I quantify the same at Rs. 7,500 per petition. The same may be paid to Mr. Y.V. Vaghela, the learned standing counsel appearing for the Central Government.