
(1974) 03 CAL CK 0035

In the Calcutta High Court

Case No : A.F.O. No. 89 of 1973 (G.P.No. 18 of 1972)

Mcleod and Co. and Others

APPELLANT

Vs

S.K. Ganguly and Others

RESPONDENT

Date of Decision : 12-03-1974

Acts Referred:

Companies Act, 1956 — Section 100, 101, 102, 391, 391(1)

Citation : (1975) 45 CompCas 563 : 79 CWN 132

Hon'ble Judges : Ghose, J;B.C. Mitra, J

Bench : Division Bench

Advocate : Nag, for the Appellant; S.B. Mookherjee, for the Respondent

Final Decision : Allowed

Judgement

B.C. Mitra, J.—The Craig Jute Mills Ltd. (hereinafter referred to as " the company ") was incorporated in 1918 under the Indian Companies Act, 1913. The authorised share capital of the company was originally Rs. 60,00,000 divided into 50,000 preference shares of Rs. 100 each and 3,00,000 ordinary shares of Rs. 10 each. Subsequently, in 1928, the ordinary share capital of the company was reduced to Rs. 7,50,000 divided into 3,00,000 ordinary shares of Rs. 2-8-0. The company's capital was further reduced in 1940 by reducing the face value of the preference shares from Rs. 100 each to Rs. 50 each and by further reducing the face value of the ordinary shares from Rs. 2-8-0 to annas 8 each.

2. The object for which the company was formed was to carry on the business of spinners, weavers, manufacturers, bailers and pressers of jute, jute cuttings, jute rejections, hemp, cotton, etc. After incorporation, the company commenced its business of manufacturing jute goods and also dealt in raw jute and jute goods of various kinds and carried on such business till March, 1943. In that year the company's mills were requisitioned by the Government of India. The company at that time had a mill known as Craig Jute Mills situated at Jagatdal, Barrackpore, in the District of 24 Parganas. The company was a lessee under different landlords in respect of the lands on which the mill was situated and

other adjoining lands of a total area of 72.09 acres of land.

3. At all material times Mcleod & Co. Ltd. (appellant No. 1) was the managing agent of the company and also the managing agent of another jute company known as Alliance Jute Mills Co. Ltd., which was in occupation of adjoining lands comprising an area of 72.09 acres.

4. By notifications dated December 19, 1946, and March 23, 1947, the Government of India acquired under the Defence of India Rules, 1939, the lands of the company together with all its buildings and machinery at the factory at Jagatdal, as also the land and factory of Alliance Jute Mills Co. Ltd. The Central Government retained some of the machinery and motors belonging to the jute mills, but most of the plant and machinery remained with the company to be removed from the said requisitioned premises.

5. A sum of Rs. 46,21,447 was paid as compensation for requisition and acquisition of the property of the said two companies. Out of this sum Rs. 30,00,000 was made over to the first appellant as the managing agent of the two companies and the balance was made over by the Central Government to the liquidators of the company, who were partners of Lovelock and Lewes, auditors of the company.

6. On March 15, 1949, a special resolution was passed at a meeting of the company for voluntary winding up of the company and the partners of Lovelock and Lewes, the auditors of the company, were appointed liquidators. The first appellant who were the managing agents of the company handed over all assets, books, papers and documents including the compensation money to the liquidators. It is claimed on behalf of the appellants, and indeed it is not disputed, that the debenture-holders of the company have been paid in full. The holders of preference shares of the company of Rs. 50 each have been similarly paid in full in 1949. The holders of ordinary shares of the company of annas 8 each have been paid twice, the total amount paid for each share being Rs. 13. According to the appellants, there are no other creditors of the company and no other claims against the company are outstanding.

7. It is claimed on behalf of the Central Government that a sum of about Rs. 1.47 lakhs have been paid in excess. The appellants claim that from the last available accounts of the liquidators for the period from March 15, 1968, to March 14, 1969, a sum of Rs. 10,45,384.68 is lying in their hands as the funds of the company as on March 14, 1969, It is claimed that on December 11, 1971, when a meeting of the company was held u/s 391 of the Companies Act, 1956 (hereinafter referred to as "the Act"), the sum of money held by the liquidators had increased to Rs. 11.18 lakhs. It is in these circumstances that the scheme was prepared between the company and holders of ordinary shares with a view to revive the company. On July 16, 1971, a meeting of the equity shareholders of the company was directed to be convened for the purpose of considering, and if thought fit, approving the scheme of arrangement. After extensions granted by

the court the meeting was ultimately held on December 11, 1971, and the scheme proposed was approved by the ordinary shareholders of the company. Thereafter, an application for sanction of the scheme by the court was moved and by a judgment and order dated November 21, 1972, this application was dismissed with costs. Aggrieved by this order of dismissal the appellants have preferred this appeal.

8. Appearing on behalf of the appellants, Mr. Nag contended that there has been an improvement in the situation for the manufacture of jute goods and also for trade in jute and jute goods, and the prospects of business in manufacture of jute and jute goods are very bright. He also contended that the majority of holders of equity shares of the company were desirous of reviving the company and resuming its business according to the memorandum of association of the company. The company, it was contended, was and still is a solvent concern and had substantial assets and even after providing for the claim for excess payment by the Central Government, substantial assets would be left with the company to carry on business. It was argued that under the memorandum and articles of the company the preference shareholders who have received the full amount of their investment have no claim to participate in the surplus assets and have no say in the proposed scheme.

9. In order to appreciate this contention it is necessary to refer first of all to Clause 5 of the memorandum of association which says that preference shares shall confer the right to a fixed cumulative preferential dividend at 7% per annum on the capital for the time being paid up thereon, and shall rank as regards return of capital in priority to the ordinary shares but shall not confer the right to any further participation in profits or assets. The amended Clause 4-A of the articles of association of the company also provides that the preference shareholders shall be entitled to a fixed cumulative preferential dividend at Rs. 5% per annum. Sub-clause (c) of Article 4-A provides that in a winding-up the preference shareholders shall have the right to payment of capital in priority to the ordinary shares but they will have no right in a winding-up to any further participation in profits or assets.

10. Relying on the provisions in the memorandum and the articles mentioned above, Mr. Nag contended that the preference shareholders were in no way affected by the scheme proposed between the company and the ordinary shareholders, as they have been paid back their investment and under the memorandum and articles of the company, which is in liquidation they have no further right to the profits and assets. It was also argued that it is the ordinary shareholders alone who have the right to participate in the surplus assets now in the hands of the liquidators, and since they have decided to revive the company on the terms of the proposed scheme, the preference shareholders cannot be allowed to have any say in the matter of this scheme. In support of this contention reliance was placed by counsel for the appellants on Palmer's Company Law, 21st edition, page 293, for the proposition that the provision in

the memorandum and articles dealing with the rights of preference shareholders, the accumulation and participation in dividend was, *prima facie*, exhaustive and no further rights could be implied unless the articles gave further rights to such shareholders. Reliance was also placed on page 704 for the proposition that the scheme must be such as a man of business would reasonably approve and that in exercising its discretion whether or not to sanction a scheme the court treats it as cardinal that its function does not extend to usurping the views of the members or creditors. The court's duty, according to the learned author, is to see that the scheme is a reasonable one and if the court is of opinion that there is such objection that any reasonable man might say that he would not approve it, the court might refuse to confirm the scheme.

11. Reliance was placed by Mr. Nag on a decision of the House of Lords in *Scottish Insurance Corporation Ltd. v. Wilsons and Clyde Coal Co. Ltd.* In that case, under a Nationalisation Act, the colliery assets of the company were transferred to the National Coal Board with the result that the company could no longer pursue the objects for which it was incorporated. At an extraordinary general meeting of the company a resolution was passed for reduction of capital by returning the whole of the paid up capital of the preference stock-holders and also for extinguishing such preference shares. The preference stock-holders objected to the reduction on the ground that it deprived them prematurely of a 7% investment and also it deprived them of the right to participate along with the ordinary shareholders in the surplus assets. After referring to the relevant articles, Viscount Maugham observed that it was clear that subject to payment to preference shareholders of their capital and preferential dividends the whole of the reserve funds and other assets of the company were appropriated to the ordinary shareholders and belonged to them to the exclusion of preference shareholders. It was also held that profits which have been appropriated to the ordinary shareholders to the exclusion of preference shareholders must, in the absence of some other considerations, remain property of the former in a winding-up. Reliance was next placed by Mr. Nag on a decision of the English Court of Appeal in *In re Isle of Thane Electric Supply Co. Ltd.* In that case a company adopted new articles and under these articles the preference shareholders were given the right to a fixed cumulative preferential dividend at 6% per annum in priority to ordinary shares and the right to participate *pari passu* with the ordinary shares in the surplus profits which in respect of any year it shall be determined to distribute after paying the preferential dividend. The company went into voluntary liquidation. The question that was raised was whether the preference shareholders were entitled to the surplus assets and it was held that the onus lay on the preference shareholders to show that they were entitled to participate therein. Reliance was next placed by counsel for the appellants on *In re Tea Corporation Ltd.* In that case an application for a scheme of arrangement with creditors and contributories of a company in liquidation came up for consideration. At the meeting of the contributories the majority of preference shareholders voted in support of the proposed scheme but the

ordinary shareholders did not vote in favour of it. It was held that since the ordinary shareholders had no interest in the asset their dissent was immaterial. Vaughan Williams L.J. observed at page 23 of the report :

"..... if you have the assent to the scheme of all those classes who have an interest in the matter, you ought not to consider the votes of those classes who have really no interest at all. It would be very unfortunate if a different view had to be taken, for if there were ordinary shareholders who had really no interest in the company's assets and a scheme had been approved by the creditors and all those who were really interested in the assets, the ordinary shareholders would be able to say that it should not be carried into effect unless some terms were made with them. "

12. Our attention was also drawn to a passage in Gore-Browne on Companies, new edition, pages 873-874, for the proposition that it was upon the applicant for sanction of the scheme to determine what class of members and creditors are to be summoned to any meeting as constituting a class and also that in sanctioning a scheme the court might ignore the fact that a class had not consented if it be proved that upon an immediate distribution of the assets none would be available for that class.

13. Mr. S.B. Mookherjee, appearing for the respondents, contended that under the provisions of Section 391(2) of the Act the court's jurisdiction to sanction a scheme was conditional upon approval of the scheme by the members of the company of all different classes being obtained in accordance with the statutory prescribed majority. He argued that the jurisdiction of the court u/s 391 of the Act could not be invoked unless a meeting of the preference shareholders of the company was called and held, and in the absence of any such meeting the condition precedent could not be said to have been fulfilled and, therefore, the court had no jurisdiction to sanction the scheme. It was submitted that even assuming that the preference shareholders have been repaid money invested by them in the capital of the company, they still continued to be on the register of members of the company and, as such, their existence could not be ignored. It was argued that they have as much right to express their views with regard to the scheme, because even though they were not entitled to participate in the surplus assets in a winding-up they had a right to express their views since the winding-up was proposed to be stayed and the company was sought to be revived. In support of this contention reliance was placed by Mr. Mookherjee on Bucktey, 13th edition, for the proposition that if a company's assets are insufficient for payment of debts the paid up shareholders have no interest and if it presents a petition he must allege and prove that there are assets of such amount as that in winding-up he will have a tangible interest. Reliance was also placed by counsel for the respondents on Palmer, 21st edition, page 702, for the proposition that at a meeting of members held for considering a scheme the court must see that the resolutions are passed by the statutory majority in value and number in accordance with the scheme at a meeting duly convened and held

and upon this jurisdiction of the court to confirm the scheme depended.

14. Attractive though the argument of Mr. Mookherjee appears to be, we are not impressed by it. It must be noticed that Section 391 of the Act contemplates a scheme between a company and its creditors or any class of them or between a company and its members or any class of them. The scheme which is now before us in this appeal is a scheme between the company and its ordinary shareholders. It does not concern or involve in any way the preference shareholders of the company. The statute expressly authorises the company to frame a scheme with any class of its members and it cannot be said that in a proposed scheme between a company and one class of its members, a meeting of all the different classes of members must be held and their approval obtained to the scheme. Such a proposition cannot be upheld having regard to the clear language in Section 391(1) of the Act. The rights of the preference shareholders of the company, such as they are, remain where they are and are not intended to be interfered with. Keeping in mind the provisions of the memorandum of association of the company and its amended articles, it must be held that the preference shareholders have no right to the surplus assets of the company in the hands of the liquidators, and if with these funds the ordinary shareholders of the company wish to revive the company without in any way curbing the rights of preference shareholders, whatever they are, it cannot in our view be said that the court had no jurisdiction to sanction the scheme, merely because a meeting of the preference shareholders was not called and held, and their views on the scheme were not ascertained.

15. The next contention of counsel for the respondents was that the scheme involved a reduction of share capital, inasmuch as the capital structure of the company would be the investment to be made by holders of ordinary shares only, leaving out the capital that the preference shareholders had contributed. It was argued that the investment of the preference shareholders was paid back to them and the proposed scheme was a scheme between the company and its ordinary shareholders. The scheme as framed, it was submitted, involved a reduction in the share capital of the company". Originally, the authorised share capital of the company was Rs. 60,00,000. In 1928, the ordinary share capital of the company was reduced to Rs. 7,50,000 comprising 3,00,000 ordinary shares each and this was effected by reducing the face value of ordinary shares from Rs. 10 each to Rs. 2-8-0 each. The capital was further reduced in 1940 by reducing the face value of preference shares from Rs. 100 each to Rs. 50 each and by further reducing the face value of ordinary shares of Rs. 2-8-0 each to annas 8 each. As on the date of voluntary liquidation of the company, the authorised capital was Rs. 1.6,50,000 and the subscribed and paid up capital was Rs. 6,50,000, It is to be remembered that the company had repaid the capital invested both by the preference and the ordinary shareholders. If instead of paying the preference shareholders in full as has been done, the company had paid them only in part or had repaid the capital of only one class of shareholders, namely, the preference shareholders or the ordinary shareholders and the

proposal in the scheme was to carry on business with the existing shareholders, there would certainly have been a reduction of share capital of the company. But, as it is, the proposal in the scheme is that the share capital of the company shall be Rs. 9,00,000 divided into 3,00,000 ordinary shares of Rs. 3 each. No shares of the company proposed under the scheme have been subscribed yet, as indeed it cannot be subscribed, until the scheme has been sanctioned by the court and has come into force. Under the scheme the company does not propose to carry on its business with the share capital subscribed by the shareholders but with the surplus now in the hands of the liquidators after repayment of the capital invested by the shareholders. In our view, therefore, it is not a case of reduction of the share capital as contemplated by Sections 100, 101 and 102 of the Act. But the existing provisions in the memorandum of association and articles of association of the company do not reflect the proposed capital structure of the company under the scheme. There should, therefore, be appropriate alteration and amendment of the memorandum and articles of association of the company, to indicate the new capital structure of the company proposed in the scheme.

16. Our attention was drawn by Mr. Mookerjee to a Bench decision of this court in *Hindustan Commercial Bank Ltd. v. Hindusthan General Electric Corporation*. In that case it was held that, where the court called upon to sanction a scheme of arrangement found that it was called upon also to confirm a reduction of capital, the court was bound to follow and observe the formalities which it ought to follow and observe in the case of confirmation of reduction of capital. This decision, in our view, is of no assistance to Mr. Mookerjee as there is no reduction of share capital as such of the company. But, what has happened is that the company has repaid the capital of both the preference and ordinary shareholders of the company, and is proposing to carry on business under the scheme with the surplus now in the hands of the liquidators. The amount now in the hands of the liquidators, which would ultimately go to the company if the scheme is sanctioned, is not the share capital of the company but the surplus assets in the hands of the liquidators. If this amount represented part of the share capital subscribed by the shareholders of either class, and the company proposed to carry on business with this share capital, but at the same time declared that the capital structure would be Rs. 9,00,000 only, the question of reduction of share capital would have arisen. But that is not the case here. There is no reduction in the share capital as such and, therefore, the scheme cannot be rejected on the ground that there is a reduction in the share capital of the company without complying with the provisions in the Act for such reduction.

17. In our view, however, there is good deal of force in the contention of Mr. Mookherjee that provision should be made to secure the claim of the Central Government for excess payment of compensation. It was argued that the Central Government has claimed Rs. 1,47,605 on account of excess payment to the company. Mr. Mookherjee drew our attention to the letter of the liquidators to the company dated November 19, 1969, from which it appeared that the State Government had claimed this amount to have been paid in excess on account of

the claim of the other parties in the compensation paid to the company. It seems to us that this claim of the Central Government ought to be sufficiently secured, so that in the event of it being ultimately found that the amount has in fact been paid in excess, there may be no difficulty with regard to the recovery of the sum received in excess by the company.

18. It was further argued by Mr. Mookherjee that nearly 50% of the ordinary shareholders of the company cannot be traced as they might either be dead or might have migrated to Pakistan. He argued that under Clause 5 of the proposed scheme, the company would offer shares to the existing holders of ordinary shares and upon acceptance of the offer necessary share certificates would be issued by the company, but if no intimation was received within a fortnight from the date of despatch of the notice, the directors of the company would be at liberty to deal with the shares as they might in their absolute discretion think fit and proper. Mr. Mookherjee contended that this arbitrary power ought not to be given to the directors of the company as the directors would be put in a position to control the entire surplus assets of nearly Rs. 11,00,000 without issuing 50% of the ordinary shares of the company. In repelling this contention of counsel for the respondents, Mr. Nag drew our attention to paragraph 9(b) of the affidavit affirmed on behalf of the company by Alien Cook Fotheringham on March 29, 1972. It has been proposed on behalf of the company that, if intimation of acceptance is not received as contemplated by Clause 5 of the scheme, the balance of the ordinary shares not issued shall not be dealt with by the directors in exercise of the powers conferred by Clause 5 of the scheme, without leave and direction of this court. In our view, the directors of the company ought not to be allowed to deal with, the balance of the ordinary shares without an order of court obtained for that purpose.

19. There is one other matter, however, which must be taken note of in dealing with the scheme. It is obvious that the memorandum of association and the articles of association of the company remain as they were at the time of commencement of the voluntary liquidation. The memorandum and the articles, as they stand, contemplate two classes of shareholders, namely, preference shareholders and ordinary shareholders. But, under the scheme, there will be only one class of shareholders, namely, ordinary shareholders, and the price of ordinary shares will be Rs. 3 for each share. It is obvious that both the memorandum of association and the articles of association must be altered so as to correctly reflect the capital structure of the company under the scheme. In our view, therefore, steps must be taken by the company to alter its memorandum of association and amend the articles of association to correctly reflect the capital structure of the company under the scheme.

20. The scheme proposed by the company, therefore, ought to be and is accordingly sanctioned subject to the following conditions :

(1) A sum of Rs. 1,48,000 to be deposited by the company in a fixed deposit account for a term of 5 years with the State Bank of India. Upon adjudication of

the claim of the Government of India on account of excess payment made in respect of compensation money paid to the company, such claim should be satisfied out of the amount then lying in the fixed deposit account.

(2) The residue of the ordinary shares, after allotment of shares to such of the ordinary shareholders as apply for the same, should not be issued or dealt with by the directors of the company, without obtaining an order of court for that purpose, and upon such terms as the court may impose.

(3) The memorandum of association and the articles of association of the company should be altered and amended, in accordance with the provisions in the Companies Act, 1956, so as to correctly reflect the capital structure of the company under the scheme.

21. Subject to the conditions mentioned above, the scheme proposed by the company is sanctioned. There will also be an order for stay of winding up of the company and an order directing the respondents to hand over all books, papers, documents and assets including the bank balances and fixed deposits of the company, to its directors and to execute necessary letter of authority in favour of the directors of the company.

22. In the result, the appeal is allowed. The judgment and order under appeal are set aside. Each party to pay its own costs.

Ghose, J.

22. I agree.