

(1953) 05 PAT CK 0016

In the Patna High Court

Case No : Letters Patent Appeal No. 2 of 1953

Nandkishore Bajoria and Another

APPELLANT

Vs

Gaya Sugar Mills Ltd. (In Liquidation)

RESPONDENT

Date of Decision : 13-05-1953

Acts Referred:

Companies Act, 1913 — Section 185
Trusts Act, 1882 — Section 3, 95

Citation : AIR 1953 Patna 390 : (1953) 1 BLJR 36

Hon'ble Judges : Sinha, J;S.K. Das, J

Bench : Division Bench

Advocate : A.K. Sen and N.L. Untwalia, for the Appellant; Sultan Ahmad, K.K. Varma, S.C. Mukherji and Akbar Imam and Official Liquidator, for the Respondent

Final Decision : Allowed

Judgement

Das, J.—This is a Letters Patent appeal from a decision of Imam J., dated 23-13-1952, on an application made by the Official Liquidator of the Gaya Sugar Mills, Limited (in liquidation) under the provisions of Section 185, Companies Act.

2. The material facts are the following. The Gaya Sugar Mills, Limited (hereinafter referred to as the company) was incorporated, in 1934 with an authorised capital of Rs. 7,00,000 divided into 7,000 shares of Rs. 100 each. For some years it was extremely successful; but in 1944 the company embarked on an ambitious scheme for the erection of a new factory at Warsaligunj, some fifty or sixty miles from Guraru where the original factory of the company is situate. In order to obtain the funds necessary for this very great expansion of the business, the authorised capital of the company was raised to 12 lacs in 1944, to 40 lacs in 1945 and to 1 crore in 1946. Out of this approximately 65 lacs were subscribed, and in order to obtain the balance, the directors in 1946 issued debentures of Rs. 1000 each to the value of about 25 lacs. The authorised capital of the company consisted of, amongst other shares, 2000 seven per cent, preference shares of Rs. 100 each fully paid up, and 28,000 five per cent. A-class

preference shares of Rs. 100 each fully paid, minus certain arrears, the total of the capital raised by these A-class preference shares being in the neighbourhood of about 27 lacs.

In or about 1947-48, a large block of machinery worth about four lacs which the company had ordered from the United Kingdom reached Calcutta: but the company had no funds and the machinery was shipped back to the United Kingdom; the manufacturers cancelled the contract and claimed damages of about eight lacs. By this time the company had got into serious trouble, and on 24-10-1949, one Sohanlal Jajodia, a director and debenture-trustee of the company, filed a suit against Gurusaran Lal, the then Managing Director of the company, and others for several reliefs in respect of the management of the company.

The suit was filed in the Calcutta High Court and was numbered 3803 of 1949. On 1-1-1950, an agreement was arrived at between Sohanlal Jajodia and Gurusaran Lal, the terms whereof will be found in annexure A appended to the affidavit made by one of the appellants, Mahadeo Lal Jhunjunwala. I shall advert to those terms in detail later in the course of this judgment. I may merely state here briefly that one of the terms was to pay off the preference shareholders in the following way: the company held some 42,200 shares of Ryam Sugar Company, Limited. These shares, it appears, were purchased in order to obtain a controlling interest in Ryam Sugar Company, Limited, and the reason why this controlling interest was sought was to enable the company to obtain the selling agency for the Ryam Sugar Company, Limited. This agency was obtained, but it was taken not in the name of the company but in the name of a firm which was the joint family business of Gurusaran Lal and his son Arjun Prasad. One of the terms of the agreement was that the shares of the Ryam Sugar Company, Limited, would be sold and the sale-proceeds would be utilised for paying off the preference share-holders; in addition to the payment of some amount in cash, the preference shareholders would get; five per cent, taxable debentures of the face value of ten lacs and five per cent, tax-free cumulative, redeemable preference shares of five lacs in full payment of their dues on account of capital and arrears of interest. The agreement recited that two persons, Messrs. Nandkishore Bajoria and Mahadeolal Jhunjunwala, who are the appellants before us and who, it appears, held about nine lacs of preference shares, were to be appointed as trustees for the purpose of carrying out the terms of the agreement. It further recited that steps should be taken for obtaining the sanction of the Court and of the shareholders in giving effect to the terms of the agreement. On 9-1-1950, a meeting of the board of directors was held in Calcutta, and the agreement referred to was accepted.

The minutes of the meeting stated:

"Pending the sanction of the Court and of the shareholders for reduction of capital and redemption of preference shares, it was decided that the shares in the Ryam Sugar Col., Ltd. be sold and the sale-proceeds thereof and the

Chakand and Gaya lands together with structures thereon be put in the possession of Messrs. Nand-kishoro Bajoria and Mahadeolal Jhunhunwala (hereinafter referred to as preference trustees) upon trust that they will sell the said lands with structures thereon and hold the sale-proceeds of Ryam Sugar Company Limited and Rs. 70,000 out of the sale-proceeds of the lands and structures for distribution among the preference shareholders in the event of the redemption of capital being sanctioned by the Court. The selling commission of Ryam Sugar and the last dividend of Ryam shares will also be paid to the preference trustees to be also held by them for similar distribution. If the commission, and dividend be less than Rs. 65,000 the deficiency will be made good out of other assets. 42,200 shares in Ryam Sugar Company, Limited, be sold to Messrs. Netherlands Trading Society at the rate of Rs. 27 per share nett ex-dividend already declared and the Bank of Baroda be instructed to deliver the shares to Messrs. Netherlands Trading Society against a cheque or draft in favour of Nand Kishore Bajoria and Mahadeo Lal Jhunhunwala."

Presumably in pursuance of the aforesaid resolution of the board of directors, 42,200 shares of Ryam Sugar Company, Limited were made over to the appellants who sold them, and the sale-proceeds are still being held by them. In the meantime, the Government of Bihar made an order under the Essential Supplies (Temporary Powers) Act, 1946, and appointed a Controller to take charge of the assets of the company. On 19-5-1951, the Controller asked the appellants to return the money which they had got by the sale of the shares of Ryam Sugar Company Limited. On 9-7-1951, an application was made under Article 226 of the Constitution of India in the Calcutta High Court, apparently for the purpose of restraining the Controller from acting under the Essential Supplies (Temporary Powers) Act, 1940. A rule was issued, but the application was subsequently withdrawn.

On 14-11-1951, Shearer J., who was then a Judge of this Court, passed an order for the winding up of the company. The Official Liquidator, who represents the company as respondent before us, was later appointed on 1-2-1952 to take charge of the assets of the company. On or about 3-3-1952, the Official Liquidator made a report to the Court that the appellants were holding a sum of Rs. 14,77,000 in trust for the preference shareholders. The Official Liquidator said that, in spite of notice to the appellants, they did not make over the money to him. He asked for an order, under the provisions of Section 135, Companies Act, that the appellants should be directed to make over the money forthwith to the Official Liquidator. On 9-4-1952, a notice was issued by this Court to the appellants to show cause why an order u/s 135, Companies Act, should not be made against them. The appellants showed cause, and after hearing the parties, Imam, J. made an order dated 23-12-1952, directing the appellants to pay to the Official liquidator a sum of Rs. 11,39,400 only. This sum was admitted by the appellants to be the amount for which 42,200 shares of Ryam Sugar Company, Limited were sold at the rate of Rs. 27 per share.

3. As I have already stated, the present appeal is from the aforesaid decision of Imam, J. The principal question which has been urged before us in support of the appeal is a question of jurisdiction. It is argued that the word "trustee" in Section 185, Companies Act, means an express trustee, and an order u/s 185 can be asked for only against the persons named therein, namely, contributories, trustees, receivers, bankers, agents or other officers of the company, and cannot be extended to other persons. The point taken before us is that the learned Judge, in passing the order complained of against the appellants, has exceeded the jurisdiction given to him under the provisions of Section 185, Companies Act.

4. The point is an important one and requires a very careful consideration.

5. Section 185, Companies Act, is in these terms:

"The Court may, at any time after making a winding up order, require any contributory for the time being settled on the list of contributories and any trustee, receiver, banker, agent, or officer of the company to pay, deliver, surrender or transfer forthwith, or within such time as the Court directs to the official liquidator any money, property or documents in his hands to which the company is "prima facie" entitled."

The section authorises the Court by a summary procedure, at any time after the making of a winding up order, to require the persons named in the section to transfer forthwith to the official liquidator any money or property or documents to which the company is "prima facie" entitled. The object of the section appears to be to prevent expensive litigation and to substitute therefore a summary procedure. It is also clear from the provisions of the Indian Companies Act that one of the primary duties of the liquidator is to collect the assets of the company. It very often happens that the properties of the company are retained or detained by persons to whom they are entrusted as trustees or agents, etc., and unless some expeditious procedure is provided for the recovery of such properties by the Official Liquidator, the latter would be forced to a suit in every case. Imam J. came to the conclusion that there was no doubt that the company was "prima facie" entitled to the sum of Rs. 11,39,400 which represented the sale-proceeds of 42,200 shares of Ryam Sugar Company, Limited. After hearing learned counsel for the parties, I am satisfied that there are no good grounds for not accepting the conclusion of Imam, J. that the company was "prima facie" entitled to the sum of Rs. 11,30,400; therefore, one of the essential requirements of Section 185 was undoubtedly fulfilled.

6. The controversy before us has, however, centred round the other essential requirement of Section 185, namely, if the appellants are trustees within the meaning of the expression "trustee" occurring in the section. I may state here at once that no argument was advanced before us to bring the appellants within the category of other persons named in the section, such as contributories, receivers, bankers, or officers of the company. There was some argument before us as to whether the appellants could be treated as agents of the company. I am

satisfied, however, that there was no relation of agency between the company and the appellants. The relation has been, thus described in Halsbury's Laws of England, Hailsham Edition (second), Volume I, para. 345 at page 194:

"In order to ascertain whether the relation of agency exists, the true nature of the agreement or the exact circumstances of the relationship between the alleged principal and agent will be regarded, and if it be found that such agreement in substance contemplates the alleged agent acting on his own behalf, and not on behalf of a principal, then though the alleged agent may be described as an agent in the agreement the relation of agency will not have arisen."

I have examined with care the terms of the memorandum of agreement dated 1-1-1950 and I am satisfied that those terms do not establish any relation of agency. Messrs. Nandkishore Bajoria and Mahadeo Lal Jhunjhunwala were appointed trustees for the purposes mentioned in the memorandum of agreement, one of the purposes being to sell the shares of Ryam Sugar Company, Limited, in order to pay off the preference shareholders. The so-called trustees were to act in their own right and not as agents of the company. Moreover, as has been rightly pointed out by learned counsel for the appellants, the latter could not act as agents of the company in respect of purposes which were unlawful & which the directors themselves could not lawfully give effect to. To this aspect of the case, I shall again return in dealing with the argument whether the appellants, were trustees of the company. It is sufficient to state here that the appellants were not agents of the company.

7. The critical question in this case is if the appellants are trustees of the company. Imam, J. proceeded on the footing that if a trust was created by the memorandum of agreement dated 1-1-1950, endorsed by the resolution of the board of directors dated 9-1-1950, its objects were not fulfilled before the winding up order and since the winding up order, the trust became incapable of execution; therefore, the appellants held the sale-proceeds for the benefit of the author of the trust namely, the company. Though the learned Judge has not referred to any of the provisions of the Indian Trusts Act, he was obviously applying the principle embodied in Section 83, Trusts Act.

Dr. Sultan Ahmad, who has argued the case on behalf of the respondent, has strongly relied on Section 83 and has contended that this was a case where a trust was created which became incapable of execution, therefore, the trust property was held by the appellants for the benefit of the author of the trust and the appellants were trustees within the meaning of Section 185, Companies Act. Mr. A.K. Sen has argued the case on behalf of the appellants and has contended that the purpose for which the so-called trust was created was an illegal purpose; because, in effect, it amounted to paying off the preference shareholders by trafficking in the shares of the company. He pointed out that such a purpose was against the Memorandum of Association which was the charter of the company. He referred us to Section 12, Companies Act, which allowed an alteration of the Memorandum only for certain special purposes which, in his

opinion, did not include the purpose for which the memorandum of agreement was entered into. Our attention was also drawn to Sections 50 and 55, Companies Act, which provided for alteration and reduction of the share capital of a company limited by shares if so authorised by its Articles.

The contention of Dr. Sultan Ahmad was that the purpose of the agreement, dated 1-1-1950 was not illegal inasmuch as the purpose really amounted to a reduction of the share capital and, as the agreement itself recited that the sanction of the Court and of the share-holders would be taken, the purpose of the agreement was in consonance with, and not in violation of, the provisions of the Indian Companies Act.

Mr. Sen also drew our attention to Section 105B, Companies Act, which permits a company, limited by shares to issue redeemable preference shares, if so authorised by its Articles; he drew our attention to proviso (a) of the section which says that no such shares shall be redeemed except out of the profits of the company. His contention was that the purpose of the agreement dated 1-1-1950 was to pay off the shares by diverting the capital of the company, which under the law, as also under the charter (of the) company, it was not open to the directors or to the share-holders to do.

8. Having given my best consideration to the arguments advanced by learned counsel for the parties, I have come to the conclusion that the purpose of the agreement dated 1-1-1950 was an illegal purpose and neither the directors nor the share-holders of the company could give effect to it either by an alteration in the charter of the company or the Articles of Association. It is, I think, well settled that a company has no power to purchase its own shares by diverting its capital, in order to reduce the share capital in the way sought to be done in the case before us: see --"Trevor v. Whitworth (1887) 12 AC 409 (A). If I may say so with great respect. Lord Watson put the matter very clearly when he said:

"Paid up capital may be diminished or lost in the course of the company's trading; that is a result which no legislation can prevent; but persons who deal with, and give credit to a limited company, naturally rely upon the fact that the company is trading with a certain amount of capital already paid, as well as upon the responsibility of its members for the capital remaining at call; and they are entitled to assume that no part of the capital which has been paid into the coffers of the company has been subsequently paid out, except in the legitimate course of its business."

If the purpose was illegal, then no trust was created by the memorandum of agreement or the resolution of the board of directors, and Section 83, Trusts Act, will have no application. In fairness to learned counsel for the appellants, I must also state that he contended that if any valid trust was created by the memorandum of agreement and the resolution of the board of directors, then the trust has not become incapable of execution; it can still be carried into effect that the appellants in that event, will be the trustees not of the company but of the

beneficiaries under the trust, namely, the preference share-holder. It is, however, unnecessary to consider this alternative argument of learned counsel for the appellants, as I am satisfied that no valid trust was at all created by either the memorandum of agreement or the resolution of the board of directors.

9. I have also considered Sections 84 94 and 95, Trusts Act. Learned counsel for the appellants has contended that neither Section 84 nor Section 94 applied in the present case. With regard to Section 84, his argument was that no transfer was made by the company as such, and the directors were not under the law entitled to make a transfer; he also drew a distinction between a transfer which is "sb initio" void and a transfer which is for an illegal purpose. With regard to Section 94, he said that as no part of the beneficial interest vested in the appellants who had the possession of the property, that section did not apply.

10. In my opinion, it is unnecessary to consider these arguments with regard to Sections 84 and 94, Trusts Act, though some of the arguments have an attractive subtlety. Sections 83, 84 and 95, all occur in Chapter 9 of the Indian Trusts Act, the heading of which is "Of certain obligations in the nature of trusts". Section 95 states:

"The person holding property in accordance with any of the preceding sections of this Chapter must, so far as may be, perform the same duties, and is subject, so far as may be to the same liabilities and disabilities, as if he were a trustee of the property for the person for whose benefit he holds it." (I have quoted only the relevant portion of the section).

I was at one time inclined to think that by reason of the provisions of Section 95, Trusts Act, a person who holds as a constructive trustee will also be subject to the liability created by Section 185, Companies Act; in other words, I was inclined to take the view that Section 185, Companies Act, was not confined to an express trustee. On further consideration, however, I find that both authority and the principles to be gathered from the provisions of the Indian Trusts Act, are against that view.

11. As to principle first: Section 95, when it talks of duties, liabilities and disabilities, refers to the earlier chapters in the Indian Trusts Act, Chapters dealing with the rights and powers of trustees, disabilities of trustees, and duties and liabilities of trustees. Section 95, Trusts Act, does not refer to liabilities under any other Act. More over, the section itself makes a distinction between a trustee as defined in Section 3, Trusts Act, and a person who holds property subject "to an obligation in the nature of a trust" (see Section 80). The words which I have underlined above (here in " ") bring out the distinction. If the obligations referred to in Chapter 9 of the Indian Trusts Act made the person holding property subject to those obligations, a trustee as defined in Section 3 of the Act, it would have been unnecessary to enact the provisions of Section 95. The very enactment of Section 95 shows that there is a distinction between an express trust and a constructive trust. Section 95 by itself will not make the appellants

trustees within the meaning of Section 185, Companies Act; on the contrary, Section 95 shows that the appellants are not trustees within the meaning of the word as defined in Section 3, Trusts Act.

12. Now as to authority, learned counsel for the appellants has relied on two English decisions which, in my opinion, show clearly enough that Section 185, Companies Act, is confined to an express trustee, and does not include the case of a constructive trustee. It is to be noted that the legislation in India relating to companies has followed the lines of legislation in England, and Section 185, Companies Act, is taken, almost word for word from similar provisions in the English Acts one of the earliest being Section 66, Joint Stock companies Winding up Act, 1848, (11 and 12 Vict., ch. 45). It is, therefore, permissible to enquire how similar provisions have been interpreted by the English Courts and to follow the principles laid down by them (see the observations in -- "Naresh Chandra v. Ramani Kanto AIR 1949 Cal 360 at p. 363 (B); -- Suresh Chandra Khasnabish Vs. The Bank of Calcutta Ltd.,).

The two English decisions on which learned counsel for the appellants has relied are -- "In the Matter of the Direct London and Exeter Railway Co. (1849) 64 E R 399 (D), the case being known as -- "Hollingsworth's Case (D)"; and -- "In re United English and Scottish Assurance Co (1868) 3 Ch A 787 (E).

In -- "Hollingsworth's Case (D)", Vice-Chancellor Knight Bruce dealt with an order made by the Master u/s 6S, Joint Stock Companies Winding Up Act, 1843. The appellants in that case, who practised as solicitors, were appointed solicitors to the company. They received certain moneys from the promoters of the company and the question was whether they should be asked to pay back part of the money which they had received. The Vice-Chancellor first dealt with the question whether the appellants were agents. After having found that they were not agents within the meaning of the section, he went on to discuss the question of trusteeship and said as follows:

"Then as to trusteeship. Express trusteeship is out of the case. It was argued that there was a constructive trusteeship, by reason that, as it was said, the money in dispute is a part of a sum which, as I understood to be contended, was paid to the appellants in breach of a trust upon which the persons who made the payment were said to have held it, and the appellants were alleged to have received it with notice, and so to have become themselves trustees of it-- trustees, the argument must have meant, for the company. If the evidence had appeared to me sufficient to support this contention, so far as mere matter of fact is concerned (which it has not done), I should still have thought that a trusteeship, so merely constructive, was not within the meaning of the section, for the appellants did not receive the money under any contract, or with any assent on their part to be trustees of it, or otherwise than as money on account of a debt which they claim to be due to them or to them and Mr. Columbine -- money to be retained by them for their own use, or for the use of themselves and Mr. Columbine, except so far (if at all) as it should on investigation appear to

exceed the debt due."

It is sufficiently clear that the decision proceeded on the footing that a mere constructive trusteeship was not within the meaning of Section 66 of the relevant Act.

In the second case, Lord Justice Page Wood was dealing with Section 100, Companies Act, 1862 (25 and 26 Vict. eb. 89), which section was in terms similar to Section 135, Indian Companies Act. His Lordship said:

"The case has been very well argued on both sides, but I entertain no doubt that the Court had no jurisdiction to make the order appealed from. Section 100 is as follows: (His Lordship read the section). The object of the enactment was to prevent the expense of the company bringing actions against the persons named, who are its own contributories & officers, & ought not to be extended to ether persons. I say this the mere confidently since the case (1849) 3 De G. & Sm-102 (D) and -- "Cox"s Case (1850-3 De G. & Sm-180 (F))."

Lord Justice Selwyn made even a clearer pronouncement. He said:

"I p.lso think that -- "Hollingsworth"s case (D)" and -- "Cox"s case (F)" are conclusive authorities that a constructive trust of this kind is not within Section 100, Companies Act, 1862.'"

In view of these two decisions, I would hold that the expression "trustee" in Section 385, Companies Act, means an express trustee and does not include the case of a constructive trustee. Therefore, the appellants are not trustees within the meaning of Section 135, Companies Act. and no order can be passed against them under that section.

13. Dr. sultan Ahmad has pointed out that the Courts have always liberally construed the powers given u/s 195 and have attempted to assist the liquidator by trying to bring within its compass any question properly cognisable by the Court. He has relied on the decisions -- "In. re Oakwell Collieries Co. (1879) W N 65 (G) and -- "Stringer"s case (1879) 4 Ch A 475 (H). It is true tliat in a case lying within the compass of Section 135 the Courts have liberally construed its provisions. Where, however, a person does not come wrtbin the categories of persons mentioned in Section 185. the question of liberally construing the provisions of that section does not arise. The question becomes one of jurisdiction, and this Court cannot enlarge the scope of the section: that would be legislating, and not interpreting what the Legislature has said in Section 185, Companies Act.

14. It is understandable why the Official Liquidator asks for the return of the money to which the company is "prima facie" entitled. The question before us is not whether the Official Liquidator is legally entitled to get the money back; he may be so entitled. But the question which we have to answer in this case is the much narrower question, namely, whether the Official Liquidator is entitled to an order for the return of the money by the summary procedure of Section 185,

Companies Act; in other words, the question is whether this Court has jurisdiction to pass an order against the appellants u/s 185, Companies Act. In my opinion, the answer to this question, both on principle and authority should be in the negative, however much we may regret that it should be so.

15. For the reasons given above, I would allow the appeal, and set aside the order against the appellants directing them to pay to the Official Liquidator the sum of Rs. 11,39,400. In the peculiar circumstances of this case, I would direct that the parties must bear their own costs of the proceeding u/s 185 and this appeal.

16. Before I conclude, I must say a few words about the cross-objection preferred by the respondent. In the cross-objection, the respondent has claimed the dividend on the Ryam shares and commission for the sale of the shares. This cross-objection must fail on my finding on the question, of jurisdiction. It must also fail on the "ground that the claim which has now been made does not appear to have been made before the learned Company Judge. The cross-objection must also be dismissed, but without any cost.

Sinha, J.

17. I agree.