
(1951) 01 MAD CK 0004
In the Madras High Court
Case No : O.S. Appeal No. 36 of 1950

R. Lakshmi Narasa Reddi	Vs	APPELLANT
The Official Receiver, Sree Films Ltd.		RESPONDENT

Date of Decision : 23-01-1951

Acts Referred:

Companies Act, 1913 — Section 101, 101(1), 101(2), 101(3), 101(4)

Citation : AIR 1951 Mad 890 : (1951) 21 CompCas 201 : (1952) ILR (Mad) 108 : (1951) 64 LW 683 : (1951) 1 MLJ 488

Hon'ble Judges : Rajamannar, C.J; Panchapakesa Ayyar, J

Bench : Division Bench

Advocate : V. Ramaswami Iyer, K. Srinivasan and S. Krishnaswami, for the Appellant; P. Satyanarayana Raju and V.V. Raghavan, for the Respondent

Final Decision : Dismissed

Judgement

1. This is an appeal against the judgment & decree of Mack J. in Appln. No. 4621 of 1949 in O. P. No. 94 of 1949 dismissing the appln. of the

applt. Lakshmi Narasa Reddi for excluding his name from the list of contributories settled by the Official Receiver in Sri Films Ltd. in liquidation.

The relevant facts are briefly these. Sri Films Ltd. went into liquidation by an order of this Ct. on the original side on 4-7-1949. It seems to have

been started as a private co., limited, in an informal kind of way, in December 1945; for, the minutes show that it was in existence on 26-12 1945.

One Lakshminarayana, one of the patnrs. of Lakahmi & Co, the managing agents of Sri Films Ltd., was the moving spirit, getting subscribers &

share-holders. Under the Articles of Assocn., the directors were the normal persons to allot shares. But there is also an article giving wide powers,

including, obviously, the power to allot shares, to the managing agents. This

Lakshminarayana is alleged by the applt. to have been his class-mate & intimate friend. The minutes book show a meeting of the Board of Directors on 23-2-1946, though it is not clear when these directors were elected. The next meeting of the Board of Directors recorded in the minutes book is on 6-4-1946 when the applt. was elected as the chairman of the Board of Directors & the fact said to have been intimated to him, though he denied it. It is admitted that the applt. signed an appln., Ex. R. 1, on 31-3-1946, applying for five shares of Rs. 1000 each in Sri Films Ltd. But, according to him he did so nominally & without any intention at all of taking any share in this company & aimply because Lakshminarayana who was his friend & class-mate, assured him that the appln. was only intended to lend prestige to the co., as the applt. was then the Chairman of Nellore municipality, in the public eye, as the inclusion of his name in the list of share-holders would induce other people to subscribe & pay for shares, though he need not pay himself a pie towards the five shares applied for by him. The applt. admitted that he was receiving notices, informing him from time to time of the directors' meetings & also of the general body meetings & that the co. was dealing with him as a director. "" He denied that he had received the originals of Exs. R. 3 & Rule 4 though his learned counsel before us did not want to argue against the finding of Mack J. to the contrary, regarding this. He urged that even if he had received Exs. Rule 3 & Rule 4, they would not bind him as there was no valid appln. by him, remitting Bs. 1000 per share, as shown in the form of appln., or Rs. 250 per share as demanded later on from him, or 5 per cent. of the share money as required by Section 101, Companies Act. He admitted that on 10-4-1946 the managing agent required him to send his consent to be chairman of the Board of Directors but added that he did not reply to that letter for obvious reasons, namely, to avoid any obligation to pay for the shares. But, in spite of ½ this, the managing agent drew a bill against him, for Rs. 5000 the value of the five shares, & sent it through his bankers, the Andhra Bank Ltd., Nellore, for collection. The applt. then instructed his bankers orally to dishonour that bill which was accordingly dishonoured. According to the applt. he met Lakshminarayana later on & protested to him that it was unfair to worry him for payment when he had repeatedly told him that he was not interested in the concern & had merely lent his

name to inveigle other share-holders, as requested by Lakshminarayana, & asked Lakshminarayana to take early steps to remove his name from the Register of members. The applt. went on to say that the co. issued a notice on 22-5-1947, calling for a general body meeting of the co. to be held on 15-6-1947, the agenda for the meeting including an item to consider the forfeiture of shares of the share-holders who were in arrears, that the meeting was held on 15-6-1947, & that the applt. understood that a resolution was passed then giving the defaulting share-holders a month's time to pay the balance, failing which the defaulters were to forfeit their shares as a matter of course, & that the applt.'s name was removed that day from the list of directors as he was a defaulting share-holder. The applt. went on to say that he consid. that his shares stood forfeited automatically, as he did not pay any money within the time fixed & that he therefore kept quiet without taking any action to remove his name from the register of shareholders under the bona fide impression that nothing further need be done by him. But to his surprise, when the co. went into liquidation by an order of this Ct. on the original side on 4-7-1949, a notice was sent to him by the Official Receiver on 4-8-1949, to show cause why his name should not be included in the list of contributories regarding the said sum of Rs. 5000 due in respect of his five shares. He went and showed cause before the Official Receiver, protesting that he had never intended to be a real shareholder of the co., for the reasons mentioned already & that, even if he had become a shareholder, he had ceased to be one after the resolution of the co. dated 15-6-1947 and that he was therefore not liable to be included in the list of contributories, or bound to contribute anything. The Official Receiver, nevertheless, included him in the list of contributories for Rs. 5000 in respect of his five shares. So, he filed the petn. which was dismissed by Mack J. who rejected his contention that there was no valid acceptance by the co. of his appln. for five shares as there was no resolution by the co. or the directors allotting the shares to him. Mack J. went on to say:

Even assuming his intention at the time he signed Ex. R. 1 to be true & that he never intended to pay for shares himself, he was not acting honourably as Chairman of the Municipality in lending his signature to a document to induce other people to become shareholders on the mistaken

impression that he had himself become one to the tune of Rs. 5000. It is regrettable that in this matter a liability has been sought to be evaded on grounds such as these.

2. We have perused the entire records & heard the arguments of Mr. V. Ramaswami Aiyar, for the applt. & of Mr. P. Satyanarayana Raju for the

Official Receiver. Mr. V. Ramaswami Aiyar raised many contentions. He did not rely on the pleas of the applt. before Mack J, namely, that he had

lent his name nominally as shareholder for five shares in order to inveigle other shareholders to subscribe & pay up & was therefore not liable, or

that he had not received Exs. R. 3 & Rule 4, but only raised grounds of law said to make the applt. not legally liable to be included as a

contributory & urged that mere dishonourable conduct, like the applt.'s. nominally applying for shares in order to inveigle other real shareholders

into subscribing for shares in this co., would not be a bar to considering the legal objections urged by him. Of course, we agree that mere

dishonourable conduct will be no bar to considering legal objections. There is "a considerable distinction between law and morality. Thus, a man

may subscribe nominally & bogusly a big sum for a charitable purpose, like leprosy relief fund, Tuberculosis fund, Maternity & Child Welfare fund

etc. with a clear understanding with the persons who went to him for subscription, that not a pie should be demanded from him & that his

subscription was only intended to make other men act on it as if it were real & pay up real amounts, though of smaller figures & yet he may not be

liable to pay a pie if he sets up & proves the above dishonourable understanding; But it is obvious that any such dishonourable conduct or

understanding will not also relieve him from legal liability where it exists otherwise.

3. V. Ramaswami Aiyar for the applt. contended vigorously that there was no valid appln. for shares by the applt. & so, no offer capable of being

acted on & followed by allotment, as the applt. had not sent at least 5 per cent. of the share money with his appln. as required u/s 101(3),

Companies Act, Section 101 (6) expressly making it impossible to waive this condition imposed by Section 101 (3). This contention took Mr. P.

Satyanarayana Eaju by surprise, as it had not been urged before Mack J. the only legal argument put forward before Mack J. being that there was

no resolution allotting the shares to the applt. But Mr. Satyanarayana Eaju soon recovered from the surprise & discovered that this argument had

not been urged before Mack J. for an excellent reason, namely, that this co. was a private co., to which Section 101, which is applicable only to

public cos., would not apply. The Articles of Assocn. produced by Mr. Satyanarayana. Eaju, clearly showed that this was only a private co. & the

order dated 4-7-1949 also showed this.

4. Then it was urged, somewhat feebly by Mr. Ramaswami Aiyar's junior that Section 101 (1) to (6) will apply to private companies also, since

Section 101 (8) says that Sub-section (7) shall not apply to a private co. implying thereby that Sub-section Sections (1) to (6) would apply to

private cos. also. We are satisfied that there is no substance in this contention. Section 101 (1) expressly shows that the entire Section 101, with all

its sub-sections, applies only to public cos. Section 101(8) is only intended to clear a possible ambiguity caused by the phrasing of Section 101(7).

So, this contention fails.

5. The next contention of Mr. Ramaswami Aiyar was that there was no valid acceptance of the applt.'s appln. for shares & no valid allotment of

the shares to him by a resolution of the co. or the directors or even the managing agent. He reld. on the rulings in *In re Homer District Consolidated*

Gold Mines; Ex parte Smith, (1888) 29 Ch. 546, *In re Sly Spink & Co* . 1911 2 ch. 430, *Pusarla Sanyasi v. Guntur Cotton Jute d Paper Mills*

Co., Ltd., 26 I. C. 349, *Bank of Peshawar Ltd. v Madhoram*, 51 I. c. 812, *Sukdevodas Bamprasad v. Govindoss Chathurbhujadas & Co* , 54

M. L. J. 130, *Bellary Electric Supply Co. Ltd. v. Kanniram Rowoothmal*, 64 M. L. J 130, *Indian States Bank Ltd. Official Liquidator Vs. Kunwar*

Sardar Singh and Others, , Mutual Bank of India v. Sohan Singh, A. I. R. (33) 1936 Lah. 790, *Ramlalsao v. M. E. B. Malak*, A. I. R. 1939 Nag.

225 & *Shiromani Sugar Mills Ltd. Vs. Debi Prasad*, , for the position that, in circumstances like these, where there was no satisfactory proof of

allotment by the directors, or by the managing agent where he had power under the Articles of Assocn. to allot shares, there was no valid allotment

or binding contract & that the mere entry of five shares, share Nos. 91 to 95 in his name in the register of shareholders of this eo. on 31-3.1946

itself would be no proof of any valid allotment in the absence of proof of a valid

order of allotment, & that the failure to deliver the share certificate to him would also show that the co. itself was aware of the bogus nature of the entry of the five shares in his name in the register of shareholders. It was also urged that Ex. E. 3 dated 16-4-1946 intimating to him the allotment of these five shares, mentioned the date of his appln. as 5-4 1946 instead of the correct date of 31-3-1946 found in the appln. itself, & did not mention the date of the allotment & that Ex. E. 4 dated 25-11-1946, asking him to pay the Rs. 5000 in pursuance of his promise to Lakshminarayana to do so after his return from Hyderabad, did not also mention the date of the allotment, & that there could have been no real allotment as the allotment, according to the date shown in the register of the shareholders, was made on 31-3-1946 itself with no visible interval for the co. or the directors to pass a resolution allotting the shares to him. This argument is of doubtful validity. If the managing agent, Lakshminarayana had the right to allot shares, aa the Articles of the Assocn. show, he could have allotted them immediately to the applt. & there was sufficient time for such allotment. It is not necessary to produce the order of allotment to prove the validity of an entry in the register of shareholders, though it is desirable to do so. As held by a Bench of the Bombay H. C. in Mahomed Akbar Abdulla Fazalbhoj Vs. The Official Liquidator, the liability of a member of a co. to be included in the list of contributories u/s 156, Companies Act, is not ex contractu but ex lege, & arises by reason of the fact that the name of the person appears on the register of members of the co. & it is, therefore, no answer for the contributory against the claim of the co. to say that, although his name appears on the register, he is not liable, because the allotment to him was void, or because he has sold his shares to another, &, in the absence of rectification of the register by an appln. by him u/s 38 soon after he comes to know that his name is entered in the register of members fraudulently or without sufficient cause, his liability becomes absolute u/s 156 of the Act, all the more so when winding up also has supervened; as here. We may add that in the cases reld. on by Mr. V. Ramaswami Aiyar the shareholders whose names appeared in the register of members were not proved to have knowledge of their names having been entered in that register, unlike here, where from the very beginning the applt. had such knowledge & continued to have it for

more than three years & took no action till he received the notice dated 4-8-1949 from the Official Receiver after the winding up. The failure to deliver the share certificate to the applt. is, of course, of no consequence, & was not seriously pressed by Mr. V. Ramaswami Aiyar for proving the applt.'s non-liability to be a contributory. The applt. could claim the delivery of the share certificate only after he had paid Rs. 5000, or whatever amount was due on the shares by that time &, admittedly, he had paid not a pie & was not entitled to the delivery.

6. Even assuming that there was no valid allotment of the five shares to the applt. & that the allotment was even void, we have no doubt whatever that the order of Mack J. dismissing the applt.'s appln. was correct on the "doctrine of holding out." This doctrine has been stated in Palmer's

Company law, Edn. 19, by Topham K. C. at p. 105, as follows :

The result of this doctrine of holding out is that if a person's name is on the register with his consent, & he claims a right to have it removed on

some ground or other, he must exercise the right promptly, otherwise, he forfeits it (see *Re Scottish Petroleum Co.*, (1883) 23 Ch. D. 413 . Even

where a name is, pursuant to a void contract, placed on the register delay after knowledge may be fatal (see *Re Railway Time Tables Publishing*

Co., (1890) 42 Ch. D. 98." Mr. K. M. Ghosh says at p. 347 of his *Indian Co. Law*, Edn. 8 as follows:

Before a co. goes into liquidation, the liability to contribute is measured by the contractual obligation arising from membership; but, after

liquidation, this section (Section 156) imposes new liabilities on the shareholders in respect of unpaid calls made before or after winding up; & such

calls can be recovered, though barred by limitation before the order of winding up was made. The liability of a member under this section in

respect of the shares is absolute & flows from the fact of his being on the register of members in respect of those shares. The original contract may

supply the reason for his name having been placed there, but, after the winding up, his liability arises *ex lege* not *ex contractu*.

Mr. Sen Gupta, in his *Indian Company Manual* Edn. 4 holds the same view.

7. The above view of the text book writers is amply borne out of (by?) authoritative rulings. The P. C. has held in *Hansraj Gupta v. Asthanna*, 63

M. L. J. 859 at p. 866 as follows:

Whatever may have been the rights & liabilities of the testator before the winding up intervened, the position was altered by the happening of that

event. At the commencement of the winding up, he was & had for over three years been, entered on the register of shareholders as the holder of

the shares now in question, with his full knowledge & assent. On the winding up. Section 156 of the Indian Cos. Act came into play. His liability

under that section in respect of the shares was absolute & flowed from the fact of his being on the register in respect of those shares. The original

contract may supply the reason for his name having been placed on the register in respect of the shares, but after the winding up, his liability in

respect of the shares arose *ex lege* & not *ex contractu*.

These observations apply, almost completely, to the facts of this case. Even though, after the Independence of India & the severance of its ties with

the King of England & the P. C., the ruling of the P. C. is not absolutely binding on us, it is entitled to very great respect, as held by the P.C. & the

S. C. in several recent cases, & we have not the slightest hesitation in accepting the observations of the P.C. quoted above as representing the

correct position regarding the liability of a shareholder, like the applt. for contribution u/s 156, Companies Act. In *The Garland Petroleum Co.*

(Madras), In re, 1939 2 M.L.J. 122, Gentle J. has held:

If any person whose name is included in the register of shareholders of a co. becomes aware that circumstances are such that, if proceedings are

brought against the company, he would succeed in having his name removed & the register rectified he must do so promptly. He must not stand by

& wait & then, at a later stage, with knowledge that he has been held out to the public as a shareholder of the co. seek to have his name removed.

In the cases which I have quoted, the grounds were that the contract, under which the shares were obtained could be set aside as void.

The case cited by Gentle J. included *Re Scottish Petroleum Co.*, (1883) 23 Ch. D. 413, *Sewell's case*, In re, *New Zealand Banking Corporation*,

(1868) 3 Ch. A. 131, *Lawrence Case*, In re, *Cacharo Co.*, 2 Ch. Ap. 412 & *Central Rly. Co.*, of *Venezuela v. Kisch*, (1867) L. R. 2 H. L. 99.

Even a delay of a fortnight has been held to be fatal, & here, the delay is more than three years, & the circumstances set up shaky. We have no

hesitation in agreeing with the conclusion of Gentle J. in that case. The same

views, as held by the P. G. & Gentle J. were expressed by a Bench of the Bombay H. C. in Mahomed Akbar Abdulla Fazalbhoys Vs. The Official Liquidator, & by a Bench of the Allahabad H. C. in Shiromani Sugar

Mills Ltd. Vs. Debi Prasad, . So, this contention must fail especially as winding up has also supervened, adding to the other ground of delay.

8. The last contention urged on behalf of the applt. was that the applt's. shares should have been forfeited & his name removed from the register of

the members as per the resolution of the co. dated 15-6-1947. This argument too is untenable. It was admitted that the applt's share were not

fortified as a matter of fact as per that resolution & that the co. continued to treat the applt. as a shareholder. So, as per the ruling of Gentle J. in

Gurusami v. Indo Carnattc Bank Ltd., A.I R. 1940 Mad. 873 with which we fully agree, the applt cannot object to being included in the list of

contributories.

9. In the result, this appeal fails & is dismissed with costs.