
(1929) 10 BOM CK 0002

In the Bombay High Court

Case No : Civil Revision Application No. 378 of 1928

The Bhagirath Spinning and Weaving and C. Co. Ltd.

APPELLANT

Vs

Balaji Bhavani Powar

RESPONDENT

Date of Decision : 14-10-1929

Acts Referred:

Citation : AIR 1930 Bom 267 : (1930) 32 BOMLR 87 : (1930) ILR (Bom) 178

Hon'ble Judges : Madgavkar, J;Allison, J

Bench : Division Bench

Judgement

Madgavkar, J.—These applications raise an important question as to the right of a company to revoke a resolution of forfeiture and to call for the amount due on the shares.

2. The plaintiff petitioner in all the applications is the Bhagirath Spinning, Weaving and Manufacturing Company Limited, Jalgaon, East Khandesh. The defendants-opponents are various persons, who applied for shares and to whom shares were allotted. In one case a defence of misrepresentation was set up resting on the alleged failure of the company to supply the defendants with a prospectus after application and allotment. That ground has been negatived in the trial Court and need not, therefore, be considered.

3. The facts common to all the applications are as follows: In April 1925, the defendants-opponents applied for shares along with the application money and were allotted these shares. In August and November 1925 and in March 1926, the directors passed three resolutions for calls. Calls were issued accordingly and were not met. On October 10, 1926, the directors passed a resolution forfeiting all the shares under Rule 34 of the memorandum of association. In a suit (Appeal No.252 of 1926 of the District Court, Jalgaon) filed by the company against certain other shareholders, not parties to the present suit and applications, on the calls prior to the resolution of forfeiture, the Court held that the calls were not validly made as the resolutions of the directors making the calls did not stipulate the amount, time, or place of payment, as required by Rule 26. On

February 14, 1927, the directors passed a resolution rescinding the previous resolution of forfeiture. On February 23, 1927, the defendants were informed of this resolution and on March 10, 1927, the directors by a resolution properly made issued a fresh call of Rs. 25 per share. This last call was not paid by the present defendants. Hence the present suits claiming in respect of each share Rs. 20 on allotment and Rs. 25 on the last call of March 10, 1927.

4. The Subordinate Courts held, relying on Larkworthy's Case [1903] 1 Ch. 711 that the defendants-opponents were liable for the amount of allotment but not for the amount of the last call, and decreed accordingly.

5. The pleading and the evidence are defective, and in one suit (Small Cause No. 2713 of 1927) it is not easy to reconcile the finding of the learned Subordinate Judge (Mr. Munim) that the revocation of the resolution of forfeiture was valid with the conclusion that the defendants were nevertheless not liable for the last call. The judgment not inter parties in which the Court held that the first three calls were not valid is not upon the record. But the three resolutions of the calls prior to the resolution of forfeiture, Exhibits 47, 48 and 49, show that the directors merely resolved in respect of certain shares including the shares now in suit "to make the first call", "to make the second call", "to make the third call" without specifying the amount of the call, or the time or place for payment. These were supplied by the secretary in the notice. The trial Courts have held that these calls were invalid. Nor does it appear that the defendants took any steps, whether of accepting or of repudiating the forfeiture. In one case referred to above the defendants had sent a letter asking for the prospectus and informed the company that they did not require the shares. That letter, however, was prior to the resolution of forfeiture and has no bearing on the question in the present suits.

6. The argument for the petitioner above covers a large ground and is shortly as follows:-Forfeiture of shares is in fact a reduction of capital, and therefore it can only be carried out under the conditions expressly laid down in the memorandum and the articles of association. Any defect in procedure renders such forfeiture illegal and void and estoppel inapplicable. The first three calls were invalid and therefore the resolution of forfeiture was void. The company has a right even without an express revocation to issue the call now in question. It is not open to the opponents to treat the first three calls as invalid for the purpose of payment yet to treat them as valid for the purpose of forfeiture. The company cannot be bound by any laches on the part of the directors in regard to the first three calls. Larkworthy's Case is distinguishable on two grounds, firstly, the calls there were admittedly valid, and, secondly, the contributory accepted the forfeiture, complied with the conditions, and informed the company to that effect.

7. It is argued for the opponents that the resolution of forfeiture is not void but only voidable at the option of the contributories opponents. It is possible that in one case at least forfeiture might have been induced because the directors thought the contributories contentious and cantankerous in insisting on the

prospectus. It is not open to the company to revoke forfeiture and issue a fresh call.

8. On the larger ground taken for the petitioners to strengthen their argument it is not, in my opinion, necessary to enter. It may be conceded that the three parties concerned are, the shareholders with their individual liability limited under the Indian Companies Act, the company registered under that Act, and the public in general and the creditors in particular. The rights and liabilities of all three must be decided upon the Act and the limitations whether of business or of exercising the power necessary towards that particular business as limited by the memorandum and the articles of association. I am unable to agree that forfeiture, because it may result in a certain reduction of capital, therefore necessarily stands in law on the same footing. Nor is it necessary to consider the question of the power of purchase and sale by a company of its own shares or of surrender. Such a power of sale was held illegal as tantamount to reduction of capital without the necessary resolution of the shareholders and the sanction of the Court: *Trevor v. Whitworth* (1887) 12 App. Cas. 409. Similarly, a surrender stands on its own merits but it can hardly be legalised unless it is within the limits of forfeiture : *Bellerby v. Rowland & Marwood's Steamship Company, Limited* [1902] 2 Ch. 14. Forfeiture of shares is permitted by law and in the present case is expressly within the powers of the directors under Rule 34 of the memorandum. There is also as in *Lard macworthy's Case* the power of annulment under Rule 37 as follows :- "

The directors may at any time before any share so forfeited shall have been sold, re-allotted, or otherwise disposed of annul the forfeiture thereof upon such conditions as they think fit.

9. Ordinarily in law the power of forfeiture is purely a lien upon the unpaid calls at the option of the company to enforce in case of default. The present is not an instance of the rule giving the company a power to forfeit for general debts due from a member as distinguished from the amount due from him as a contributory. Such a power would be illegal: *Hopkinson v. Mortimer, Harley & Co., Limited* [1917] 1 Ch. 646. The question in this particular case to my mind is whether the first three calls and the resolution of forfeiture are invalid; if so, are they illegal and therefore void, or are they voidable at the option of the company or are they voidable only at the option of the opponents ? On the other hand, can the opponent be allowed to say that the calls are defective for the purpose of payment and yet not defective for the resolution of forfeiture ? It is desirable, in my opinion, to avoid the use of vague words such as illegal, and I prefer therefore to use words such as, ultra vires, void, voidable, or irrevocable, with a more definite legal meaning.

10. The law on the point as summarised in *Halsbury's Laws of England*, Vol. V, page 201, para. 331, is as follows:-

As against the company the shareholder can insist that conditions precedent to

forfeiture must have been strictly complied with ; but he may rely on a forfeiture as against the company although some formalities have not been complied with. Laches on the part of the shareholder may bar the right to relief, even when the forfeiture is irregular, but not when it is wholly void A forfeiture is not made invalid by the fact that no notice is sent, even where the articles provide that notice of forfeiture shall be given to the shareholder.

11. As regards the first three calls, the resolutions of the directors have been stated above. They omit mention of the amount and the time and place of payment as is necessary under Rules 26, 27, 28 and 29. Apart from the judgment not inter pares and not before us, these calls, in my opinion, were clearly invalid as against the contributories and on such invalid calls there could be no legal default. I may refer to the judgment of Tara-porowala J. in *Pioneer Alkali Works v. Amiruddin* (1925) 28 Bom. L.R. 411 in which English cases such as *In re Cawley & Co.* (1889) 42 Ch. D. 209 and *Johnson v. Lyttle's Iron Agency* (1877) 5 Ch. D. 687 are cited. Johnson's case is also an authority for the rule that " no forfeiture of property can be made unless every condition has been literally and strictly complied with, and very little inaccuracy is as bad as the greatest." An irregular forfeiture of shares without proper notice will not debar a past shareholder from proving for damages as a creditor even though re-allotment might make it impossible for him to be placed on the register as a contributory : *In re New Chile Gold Mining Company* (1890) 45 Ch. D. 598.

12. In the present case the bona fides of the directors is not challenged and they thought that they were acting in the interest of the company. These two elements did not exist in cases such as *Bellerby v. Rowland & Marwood's Steamship Company, Limited* [1902] 2 Ch. 14. At the same time it has been held that the conditions precedent for forfeiture must exist to make it valid and irrevocable. The directors, for instance, must be properly appointed: *Garden Gully United Quartz Mining Company v. Mc Lister* (1875) 1 App. Cas. 39. On the other hand mere laches on the part of directors or irregularities such as that the forfeiture is not formally registered or that there is no formal resolution of the directors cannot give the directors power to revoke a forfeiture otherwise valid: *Lyster's Case* (1867) L.R. 4 Eq. 233; *Knight's Case* (1867) L.R. 2 Ch. 321 and *Painter* In the present case under the Act and under the memorandum the first three calls by the directors were both in law and according to the opponents' own case invalid so that there was no default and they were not bound to pay these calls. If so, forfeiture was completely ultra vires of the directors. Without default of payment of calls the directors had no power to forfeit. That forfeiture is not shown to have been accepted by the opponents or registered in the company, much less the shares sold or re-allotted. Under these circumstances, as the directors acted ultra vires, the company is not, in my opinion, estopped from relying on the ultra vires nature of the act, and showing they had no power to do what they purported to do : *Home and Foreign Investment and Agency Company, Limited, In re* [1912] 1 Ch. 72 ; *Great North-West Central Ilailivay v. Charlebois* [1890] Sec 114; and *Chapleo v. Brunswick Building Society* (1881) 6

Q.B.D. 696. A compromise by directors of unpaid calls under guise of forfeiture was held even after twelve years to be ultra vires and invalid and it was observed that "members of a company are not bound by acts ultra vires of their directors though beneficial to the company unless such acts have been expressly ratified by all the shareholders or unless all, with knowledge or notice, have acquiesced in what has been done. Time alone without knowledge or notice will not grow into proof of acquiescence." *Spademan v. Evans* (1868) 37 L.J. Ch. 752. Where the memorandum of association gave the directors no power to forfeit shares, such forfeiture cannot be set aside : *In re The National Patent "Steam Fuel Co.: Barton's Case* (1859) 4 Drew. 535 and *Stanhope's Case* (1863) L.R. 1 Ch. 161.

13. Nor is it open, in my opinion, to the opponents to contend in these suits that the first three calls were valid as regarded forfeiture so as to make the latter irrevocable without their consent and at the same time to contend that those calls were invalid in so far that there was no liability on the defendants to meet them. But the contentions of the parties apart, in law, the first three calls were, in my opinion, invalid, there was no default, the directors had no power of forfeiture and on realising their mistake it was not only open but it was incumbent upon them to withdraw the forfeiture on which neither party had so far acted and it was open to them to make the new call after such revocation. The laches of the directors in respect of the former resolutions of the first three calls make those calls and the resolution of forfeiture invalid but do not estop the company from revoking the resolution of forfeiture and treating it as invalid and the new call as valid.

14. All the cases in which the forfeiture has been upheld are cases in which the calls have been valid. *Larkworthy's Case* is no exception. A valid call and default are conditions precedent to and necessary for a valid forfeiture. Where the calls have been valid and there has been default and the power of forfeiture has once been exercised by the directors, it is not open to the directors or to the company to rely upon the irregularity in their own procedure and without the consent of the contributory whose shares have been forfeited to revoke the forfeiture and replace him on the register as contributory : *Re The Phosphate of Lime Company (Limited)* : (*Austin's Case* (1871) 24 L.T.N.S. 932. All the cases as far as I know including *Larkworthy's Case* go no further than this. There is no case in which a call has been ab initio invalid and yet forfeiture upheld.

15. For these reasons I am of opinion that the decrees of the lower Courts are wrong in law. The applications are allowed and each defendant should be held further liable for the call in respect of Rs. 25 per share issued on and after March 10, 1927,

16. As the directors are entirely responsible for this litigation, each party will pay its own costs throughout.

Allison, J.

17. The material facts have already been stated.

18. The principal defence in the lower Court in Small Cause Civil Suit 2718 of 1927 was that the defendants had been induced by misrepresentation to subscribe for shares in the company, and that therefore they were not liable to pay anything in respect of these shares. The lower Court has returned a definite finding of fact on this issue, which cannot be re-opened in this Court.

19. Though this defence failed, the lower Court dismissed that suit with the other suits now in question relying on the judgment in Larhworthy's case [1903] 1 Ch. 711 in which it was held that a shareholder was not liable to pay any calls made after his shares had been forfeited unless he consented to be restored to his position as a shareholder. That case, however, is to be clearly distinguished from these, because while there the validity of the forfeiture was never questioned, in the present case it is common ground that the shares were forfeited, by a resolution of the directors, for non-payment of calls, which in fact were made without due notice and not in accordance with other provisions of the articles of association.

20. The lower Court framed an issue, whether the annulment of the previous forfeiture of defendants' shares was valid, and decided it in the affirmative ; but did not sufficiently explain the reasons for this finding, probably because it regarded the authority of Larkworthy's Case as sufficient to dispose completely of the suits.

21. These applications must be decided on the footing that the calls first made were not made, in material particulars, in accordance with the articles of association : and for their decision two questions must be answered, first, were the forfeitures based on the failure to pay calls thus improperly made, invalid, so that the former relations between the company and defendants remained unchanged; and, secondly, whether the plaintiffs, i. e., the company, can assert that against the defendants in these suits.

22. The general principle of law founded on principles of public policy and rigidly enforced by the Courts is that no action resulting in the reduction of the capital of a company with limited liability should be permitted unless the reduction is effected under statutory authority or by forfeiture in strict accordance with the procedure, if any, laid down in that behalf in the articles of association. Any reduction of capital contrary to this principle is illegal and ultra vires : *Hopkinson v. Mortimer, Harley & Co., Limited* [1917] 1 Ch. 646 see also the leading case of *Trevor v. Whitworth* (1887) 12 App. Cas. 409.

23. In the case of *Johnson v. Lyttle's Iron Agency* (1877) 5 Ch. 687 the facts were very similar to the present case. There shares were forfeited for non-payment of calls which had not been made with proper notice. That forfeiture was held to be invalid.

24. Decision in this and similar cases has proceeded on the principle already referred to that there is no liability on a shareholder in respect of any call not made in strict accordance with the articles of association. The principle has been

restored in the Pioneer Alkali Works v. Amiruddin (1925) 28 Bom. L.R. 411.

25. A forfeiture based as in the present cases on a call thus irregularly made is ultra vires of the directors and is invalid.

26. With regard to the second question, directors of a company with limited liability can only bind the shareholders by acts coming within the authority given them by the articles of association, Any act which results in the release of shareholders from liability is not within their power except as authorised by and strictly for the purposes contemplated by the articles of association : Stanhope's Case (1865) L.R. 1 Ch. 161. The suits are brought not by the directors, but by the company, and there is therefore nothing to prevent the company as representing the shareholders from pleading the invalidity of this forfeiture. The same, result follows from the accepted principle that a corporate body cannot be estopped by deed or otherwise from showing that it has no power to do what it purported to do: Home and Foreign Investment and Agency Company, Limited, In re [1912] 1 Ch. 72.

27. Both these questions then must be decided in favour of the petitioners.

I agree to the order proposed. Rule made absolute.