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In the Bombay High Court

Case No : Company Appeal No. 6 of 1998 (Earlier Company Petition No. 287 of 1992)

Vasant Investment Corpn. Ltd. — APPELLANT

Vs

Company Law Board and others — RESPONDENT

Date of Decision : 16-12-1998

Acts Referred:
Civil Procedure Code, 1908 (CPC) — Section 100, 38
Companies Act, 1956 — Section 10, 108, 109, 110, 111
Evidence Act, 1872 — Section 101
Limitation Act, 1963 — Article 20, 40, 52, 5

Citation : AIR 1999 Bom 207 : (1999) 1 ALLMR 362 : (1999) 2 BomCR 254(1) : (1999) 1 BOMLR 916 : (2000) 102 CompCas 421

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

Bench : Single Bench

Advocate : N.H. Seervai and Pooniwala instructed by Fedral and Rashmikant, for the Appellant; Janak Dwarkadas and M.R. Sathe, instructed by y Kanga and Co., for the Respondent

Judgement

R.M. Lodha, J.—The legality and correctness of the order dated 22-5-1992 passed by the Company Law Board. Western Region Bench, Bombay is subject matter of challenge in this appeal filed u/s 10(f) of Companies Act, 1956. By the said order the Company Law Board disposed of two appeals namely Appeal Nos. 4 and 5(iii) CLB/WR of 1991 filed u/s 111 of Companies Act, 1956 wherein the order of the company refusing to register the shares lodged for transfer was impugned.

2. The present appellant M/s. Vasant Investment Corporation Limited (the Company) is incorporated under Companies Act, 1956. The issued, subscribed and paid up capital of the company is Rs. 36,97,435/- divided into 96,961 shares of Rs. 37/- each and 1500 equity shares of Rs. 74/-. The Company carries on business as dealer and consultant in securities and investment. The Company is not listed on any stock exchange. On 3-1-1989 Shri Kashi Deora, (respondent

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No. 4 - transferee) lodged to the company 14605 equity shares of the company for transfer of the said shares in his favour. Shri Suresh Deora (respondent No. 5 herein - transferee) lodged with the company 3270 equity shares for transfer of the said shares in his favour. Another application, for transfer of 1100 shares was made by Shri Prashad Deora on 3-1-1989 to the company for transfer of the said shares in his favour. The company on 1-3-1989 intimated the respondent Nos. 4 and 5 -transferees that the Board of Directors has refused to transfer the said shares in their favour on various grounds, namely, (a) that the application is not accompanied by transfer fees as prescribed by Article 40 of the Articles of Association; (b) that the application is incomplete in as much as full name of the transferor and transferee are not furnished; (c) that the intended acquisition is mala fide and for ulterior motives; (d) that the intended acquisition, if permitted, would be prejudicial to the interest of the company and general body of shareholders and (e) that the intended acquisition, if permitted, could bring out such a change in the composition of their Board of Directors resulting in placing the applicants in an advantageous position vis-a-vis the company resulting in total conflict of applicants personal interests and that of the company. On 6-11-1990 the respondent Nos. 4 and 5 herein - transferees reloaded applications for transfer of 14605 and 3270 equity shares along with transfer deeds for transfer of those equity shares in their favour. The company on 3-1-1991 intimated the respondent Nos. 4 and 5 herein that their applications for transfer had already been rejected and the reasons thereof were also intimated and in the absence of any change in the circumstances their applications stand rejected. The said rejection was challenged by the respondent Nos. 4 and 5 by filing two separate appeals on 18-2-1991 before the Company Law Board u/s 111 of the Companies Act. The company filed replies to the said appeals before the Company Law Board on 11-10-1991 and after hearing the learned Counsel for the parties, the Company Law Board disposed of both the appeals on 22-5-1992. The Company Law Board allowed both the appeals and directed the company to effect registration of the transfer of the said shares in favour of respondent Nos. 4 and 5 within 10 days of the receipt of the order. The said order of Company Law Board is under challenge in this appeal as aforestated.

3. I heard Mr. N.H. Seervai, the learned Counsel for the appellant company and Mr. Janak Dwarkadas, the learned Senior Counsel appearing for respondent Nos. 4 and 5 at quite some length and also perused the available material including the impugned order passed by the Company Law Board and the reasons given by the company in rejecting the applications for transfer of shares in favour of respondent Nos. 4 and 5.

4. Mr. Seervai, the learned Counsel appearing for the company strenuously urged that the appeals filed by the transferees applicants before the Company Law Board were barred by time u/s 111 of Companies Act. His contention is that section 111 of the Companies Act provides mandatory statutory period of limitation for filing appeal against rejection of the share transfer by the Company''s Board of Directors. He would urge that the applications made by the

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respondent Nos. 4 and 5 herein for share transfers were rejected by the company on 1-3-1989 but they did not challenge the said order of Board of Directors rejecting share transfers within time as provided u/s 111 of Companies Act and invented a fraudulent device by reloading shares for transfer in the year 1990 for getting out of difficulty of limitation and therefore the rejection of transfer of shares by the Board of Directors on 3-1-1991 cannot be said to have given fresh cause of action to the respondent Nos. 4 and 5 and these appeals were patently time barred.

5. Per contra, Mr. Dwarkadas, the learned Senior Counsel appearing for respondent Nos. 4 and 5 urged that earlier applications made by respondent Nos. 4 and 5 on 3-1-89 for transfer of equity shares were rejected on various grounds including non-compliance of the mandatory provisions by the applicants in as much as the applications were not accompanied by transfer fees and that the applications were incomplete in various respects and, therefore, there was no occasion for respondent Nos. 4 and 5 to challenge the said decision of Board of Directors rejecting the applications for transfer since even if they had challenged the said decision in appeal, no relief could have been granted to them since the applications for transfer were not in accordance with law.

6. Section 111 of the Companies Act deals with power to refuse registration of shares and appeal against such refusal. It reads thus :

"111. (1) If a company refused, whether in pursuance of any power of the company under its articles or otherwise, to register the transfer of, or the transmission by operation of law of the right to, any shares or interest of a member in, or debentures of, the company, it shall, within two months from the date on which the instrument of transfer, or the intimation of such transmission, as the case may be, was delivered to the company, send notice of the refusal to the transferee and the transferor or to the person giving intimation of such transmission, as the case may be, giving reasons for such refusal.

(2) The transferor or transferee, or the person who gave intimation of the transmission by operation of law, as the case may be, may appeal to the Company Law Board against any refusal of the company to register the transfer or transmission, or against any failure on its part within the period referred to in sub-section (1), either to register the transfer or transmission or to send notice of its refusal to register the same.

(3) An appeal under sub-section (2) shall be made within two months of the receipt of the notice of such refusal or, where no notice has been sent by the company, within four months from the date on which the instrument of transfer, or the intimation of transmission, as the case may be, was delivered to the company.

(4) If----

(a) the name of any person -

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(i) is, without sufficient cause, entered in the register of members of the company, or

(ii) after having been entered in the register, is, without sufficient cause, omitted therefrom; or

(b) default is made, or unnecessary delay takes place, in entering in the register the fact of any person having become, or ceased to be, a member [including a refusal under sub-section (1)],

the person aggrieved, or any member of the company, or the company, may apply to the Company Law Board for rectification of the register.

(5) The Company Law Board, while dealing with an appeal preferred under sub-section (2) or an application made under subsection (4) may, after hearing the parties, either dismiss the appeal or reject the application, or by order-

(a) direct that the transfer or transmission shall be registered by the company and the company shall comply with such order within ten days of the receipt of the order;

or

(b) direct rectification of the register and also direct the company to pay damages, if any, sustained by any party aggrieved.

(6) The Company Law Board, while acting under sub-section (5), may, at its discretion, make -

(a) such interim orders, including any orders as to injunction or stay, as it may deem fit and just;

(b) such orders as to costs as it think fit; and

(c) incidental or consequential orders regarding payment of dividend or the allotment of bonus or rights shares.

(7) On any application under this section, the Company Law Board -

(a) may decide any question relating to the title of any person who is a party to the application to have his name entered in, or omitted from, the register;

(b) generally, may decide any question which it is necessary or expedient to decide in connection with the application or rectification.

(8) The provisions of sub-sections (4) to (7) shall apply in relation to the rectification of the register of debenture holders as they apply in relation to the rectification of the register of members.

(9) If default is made in giving effect to the orders of the Company Law Board under this section, the company and every officer of the company who is in default shall be punishable with fine which may extend to one thousand rupees,

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and with a further fine which may extend to one hundred rupees for every day after the first day after which the default continues.

(10) Every appeal or application to the Company Law Board under sub-section (2) or sub-section (4) shall be made by a petition in writing and shall be accompanied by such fee as may be prescribed.

(11) In the case of a private company which is not a subsidiary of a public company, where the right to any shares or interest of a member in, or debentures of, the company is transmitted by a sale thereof held by a Court or other public authority, the provisions of sub-sections (4) to (7) shall apply as if the company were a public company:

Provided that the Company Law Board may, in lieu of an order under sub-section (5), pass an order directing the company to register the transmission of the right unless any member or members of the company specified in the order acquire the right aforesaid, within such time as may be allowed for the purpose by the order, on payment to the purchaser of the price paid by him therefore or such other sum as the Company Law Board may determine to be a reasonable compensation for the right in all the circumstances of the case.

(12) If default is made in complying with any of the provisions of this section, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to fifty rupees for every day during which the default continues.

(13) Nothing in this section and section 108, 109 or 110 shall prejudice any power of a private company under its articles to enforce the restrictions contained therein against the right to transfer the shares of such company.

(14) In this section "company" means a private company and includes a private company which had become a public company by virtue of section 43-A of this Act."

7. It would be seen from section 111 that if the company refuses to register the transfer of shares, it is required to send notice of refusal to the transferee and transferor within two months from the date on which the instrument of transfer was delivered to the company. Sub-section (2) of section 111 provides that the transferor or transferee as the case may be may appeal to the Company Law Board against a refusal of the company to register the transfer. Such appeal by aggrieved transferor or transferee has to be made within two months of the receipt of notice of such refusal and where no notice has been sent by the company within 4 months from the date on which the instrument of transfer was delivered to the company under subsection (3) of section 111. Sub-section (4) is not very relevant for the present purposes. Sub-sections (5) and (6) of section 111 deal with the power of the Company Law Board while dealing with an appeal under sub-section (2) of section 111 finally or at an ad-interim stage. Adverting to the facts now in the background of section 111, it would be seen that the

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respondent Nos. 4 and 5 herein made the applications on 3-1-1989 to the company for transfer of shares. The respondent No. 4 made the application for transfer of 14,506 equity shares while respondent No. 5 made the application for transfer of 3270 shares. Apparently, the said transfer applications were not in accordance with the Articles of Association and the provisions of law. The applications were not accompanied by transfer fees as prescribed by Article 40 of Articles of Association. The applications were incomplete in as much as full names of the transferees in all the applications were not furnished. Some of the annexures to the application were unsigned. Full name of the transferors in two applications in respect of the shares covered by register folio 2289 were not furnished. These infirmities weighed in the mind of the Board of Directors while deciding the transfer application coupled with other reasons in rejecting the said transfer applications made by respondent Nos. 4 and 5. On the face of such infirmities in the transfer applications made by respondent Nos. 4 and 5, even if the said respondents had filed appeal before the Company Law Board u/s 111(2) of Companies Act, no relief could have been granted to them assuming that the Company Law Board had not agreed with the view of the Board of Directors on other grounds rejecting the transfer of shares. It would, thus, be seen that the cause of action accrued to respondents No. 4 and 5 on rejection of their first transfer applications after relodgment in accordance with Articles of Association and law. The cause of action which accrued to the respondents No. 4 and 5 by fresh rejection on 3-1-1991 was entirely distinct and different and the appeals filed by respondent Nos. 4 and 5 on 18-2-91 could not be held as time barred. As already indicated above the transfer applications made by respondent Nos. 4 and 5 on 3-1-89 suffered from serious infirmities and on the face of such patent infirmities, the applications for transfer of shares were incompetent and if the respondent Nos. 4 and 5 were advised not to challenge the same in appeal unless fresh applications for transfer of shares were made in accordance with law, it cannot be inferred that respondent Nos. 4 and 5 invented fraudulent device to overcome limitation u/s 111 of the Companies Act. As a matter of law, the right and appropriate occasion for challenging the order of the company arose only after they reloaded their applications for transfer of shares in accordance and conformity with law and Articles of Association of the company on 6-11-90 and the said applications were rejected by the company on 3-1-91. There is no dispute that respondent Nos. 4 and 5 filed the appeals before the Company Law Board within two months of the rejection of their applications on 3-1-1991. The facts which have come on record and for the reasons which I have already stated above, I am not persuaded to accept the contention of the learned Counsel for the company that the appeals filed by respondent Nos. 4 and 5 before the Company Law Board were time barred.

7A. In view of my aforesaid finding, I do not feel it necessary to consider the contention raised by Mr. Seervai, the learned Counsel for the company that the Company Law Board is a Court within the meaning of Limitation Act and that the Company Law Board has power to condone the delay on sufficient cause being

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shown since section 5 of Limitation Act would be attracted and in the absence of any application for condonation of delay, the appeals were liable to be dismissed. As I have already held that the appeals preferred by respondent Nos. 4 and 5 before the Company Law Board challenging the decision of the company dated 3-1-91 were within time, there was no question of making any application for condonation of delay by respondent No. 4 and 5.

8. Mr. Seervai, the learned Counsel for the company then assailed the order of the Company Law Board on merits. He urged that the entire approach of the Company Law Board was against law in as much as the Company Law Board proceeded to examine the decision of the Board of Directors as if the burden lay on the Company to show that it acted bonafide, in good faith and not with corrupt motive. Mr. Seervai, vehemently contended that the presumption is that the Board of Directors acted bona fide and in good faith and the burden lay on the transferees-applicants while were challenging the order of the Board of Directors to show that the company acted mala fide, in bad faith, arbitrarily and with corrupt motive. The learned Counsel for the company also urged that the observations and findings recorded by the Company Law Board are perverse and not in accordance with the settled law. He, therefore, urged that the order of the Company Law Board being erroneous in law as well as on facts, is liable to be set aside.

9. On the other hand, Mr. Dwarkadas, the learned Senior Counsel appearing for respondent Nos. 4 and 5 would urge that there was total non-application of mind by the Board of Directors in rejecting the applications for transfer lodged by respondent Nos. 4 and 5 on 6-11-90. The learned Senior Counsel urged that when the decision was taken by the Board on 3-1-91, the circumstances and situation had changed in as much as the suit for eviction which was earlier pending between the Company and M/s. TIM. Pvt. Ltd., had been dismissed for default and was no more subjoined before the Court. He also urged that though earlier transfer applications related to 29.3% of equity shares, by the applications made on 6-11-90 the transfer of shares only related to about 18% of the shares. According to Mr. Dwarkadas, the Board of Directors did not advert to these aspects at all and by their predetermined decision rejected the applications for transfer made by respondent Nos. 4 and 5 and, therefore, the decision taken by the Board of Directors of the Company on 3-1-91 suffered from malice and actuated with ulterior motive and rightly set aside by Company Law Board

10. I feel appropriate at this stage to refer to the legal position concerning the power of the Board of Directors of the company in relation to transfer of shares. In Harinagar Sugar Mills Ltd. v. S.S. Jhunjhunwala, 1961 Vol. 31 Company Cases page 387, the Apex Court held with reference to the then section 155, that rectification of register can be granted only if it is established that the Directors had, in refusing to register the shares in the names of the transferee, acted oppressively, capriciously or corruptly, or in some way mala fide and not in the

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interest of the company. Such a plea, the Apex Court ruled, has to be expressly raised and affirmatively proved by evidence. The Apex Court held that normally, the Court would presume that where the Directors have refused to register the transfer of shares when they have been invested with absolute discretion to refuse registration, that the exercise of the power was bona fide. In other words, the Apex Court, ruled that discretionary power conferred by Articles of Association to refuse to register would be presumed to be properly exercised and it was for the aggrieved transferee to show affirmatively, that it had been exercised mala fide and not in the interest of the company.

11. In (Re. Bell Brothers Ltd. : Ex parte Hodgson) 1891(7) T.L.R. 689 : 65 L.T. 245 with reference to English Companies Act it has been held that power relating to rectification of register is presumed to have been exercised reasonably, bona fide and for the benefit of the company and a heavy onus lay on those challenging the resolution of the Directors to displace the presumption of bona fide exercise of power. It was emphasised in Bell Brothers Ltd, that the discretion to refuse to register transfers was not liable to be controlled unless the Directors "acted oppressively, capriciously or corruptly or in some way mala fide".

12. (In re, Melish, L.J. in Exparte Penney) observed "But in order to interfere it must be made out that the Directors have been acting from some improper motive, or arbitrarily and capriciously. That must be alleged and proved and the person who has a right to allege and prove it is the shareholder who seeks to be removed from the list of shareholders and to substitute another person for himself..... this Court could have jurisdiction to deal with it as a corrupt breach of trust; but if there is no such corrupt or arbitrary conduct as between the Directors and the person who is seeking to transfer his shares, it does not appear to me that this Court has any jurisdiction whatever to sit as a Court of appeal from the deliberate decision of the Board of Directors to whom by the constitution of the company the question of determining the eligibility or non-eligibility of new members is committed."

13. In Bajaj Auto Ltd., Poona v. N.K. Firodia and another etc., 1971 (Vol. 41) Company Cases page 1, the Apex Court laid down the legal position thus :

"In the present appeals, the reasons of the Directors have to be tested from three points of view. First, whether the Directors acted in the interest of the company; secondly, whether they acted on a wrong principle; and, thirdly, whether they acted with an oblique motive or for a collateral purpose. This Court in Harinagar Sugar Mills Ltd. v. Shyam Sunder Jhunjhunwala said that "the discretion of the Directors would be nullified if it were established that the Directors acted oppressively, capriciously or corruptly or in some other way mala fide". The decision in Harinagar Sugar Mills Ltd. related to a case under the Companies Act, 1956, prior to the introduction of section 111(5-A). That is why if the Directors under the articles were not to disclose reasons, it was said that the Court would presume, where the Directors refused to register the transfer of shares, that their power of absolute discretion was exercised bona fide unless

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corrupt or mala fide motives were affirmatively pleaded and proved. It would be for the aggrieved transferor to show that the refusal to register transfer was exercised mala fide and not in the interest of the company and thereby the presumption of bona fide would be displaced.

The words "bona fide and for the benefit of the company as a whole" have been considered in some English decisions. Reference may be made to the decision of Greenhalgh v. Arderne Cinimas Ltd., where Evershed M.R. said that if a resolution had the effect "to discriminate between the majority shareholders and the minority shareholders so as to give the former advantage of which the latter were deprived", the resolution could be attacked on grounds of elements of dishonesty or impropriety. The acts of the Directors would have to be scrutinised as to whether they were the honest opinion of the Directors acting for the company as a whole.

Mellish L.J., in Ex parte Penny: Gresham Life Assurance Society. In re 3, said that the Directors would have no right to force a particular shareholder to continue as a shareholder and not to allow him to transfer shares at all because that would be an abuse of their power Lord Cozens-Hardy M.R. in re Bede Steam Shipping Co. Ltd. said that the personal objections to a transferee were where the transferee would be quarrelsome person or he would be an unreasonable person or he would be acting in the interest of a rival company. The Directors there had power to refuse to register transfer of shares if "in their opinion it is contrary to the interest of the company that the proposed transferee should be a member thereof. In that case there were disputes between the elder brothers who were Directors. One of the elder brothers sold his two shares to a clerk of his and another share to his housekeeper. The other director said that the company was really a family concern and therefore the shares should not be transferred singly or in small lots to outside persons having no interest in, or knowledge of, shipping.

In In re Bede Steam Shipping Co. the power of the Directors was to refuse to register the transfer of share to any person of whom the Directors did not approve as transferee. The Directors in declining to register the transfer gave two reasons. First, that there would be increase in expenditure if the body of shareholders were numerically increased and, secondly, the individuals who were neither related to the founders'' family nor connected in business with the company would become members by the proposed transfer. Neither of these reasons was held to touch the fitness of the transferees. The real power of the Directors in refusing registration of transfer was on the ground of personal objections to the transferees. The apprehension on the part of the Directors in the increase in the number of shareholders was therefore found to be an abuse of power. It was found that the Directors in refusing registration to transfer thought of the proposed transferees as mere nominees who could adopt the attitude of the transferor who had disagreed with the Directors of the company. The Directors did not look at the relevant circumstances in which they were

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placed, namely, their status, their occupation, and, in particular, whether the transferees were interested in any private business competing with the company.

Reference may be made to an old decision in In re Bell Brothers Ltd. as an illustration of the power of the Directors to refuse registration of transfer. The relevant article in the case of Bell Brothers conferred discretionary power on the Directors to refuse registration of transfer of shares on the ground that the Directors did not approve of the transferee. Chitty, J., said in relation to the Directors'' power that the Directors must act in good faith and in the interest of the company and with due regard to the right of a shareholder to transfer his shares and they must fairly consider the question of the transferee''s fitness at a board meeting. The Directors in that case were not required to disclose reasons. Three propositions can be extracted from that case. First, where the Directors do not assign any reason because of the articles it is competent for those who seek to have the transfer registered to show affirmatively by proper evidence that the Directors had not duly exercised their power. Secondly, if reasons are given by the Directors and the reasons are legitimate the Court will not overrule the Directors'' decision merely because the Court itself would not have come to the same conclusion. Thirdly, if the reasons are not legitimate, the Court would hold that the power had not been duly exercised. An example would be where the Directors said that they rejected the transfer because the transferor''s object was to increase the voting power in respect of his shares by splitting them among his nominees.

In the case of Bell Brothers two Bell Brothers, John and Lowthian, and the members of their families were shareholders in Bell Brothers. John died leaving a Will and the beneficiaries under the Will were his widow and children. The Will provided for the widow and annuity. The Will contained a general trust for conversion. John''s shares were sold to provide a fund to meet the annuity. Hodgson purchased those shares. The Directors were Lowthian, his son, Hugh, and his son-in-law. Hugh was an executor trustee under the Will of John and as such was one of the transferors of the shares of John. The shares of the testator were in the names of Hugh, the nephew, and Charles, the son of the testator, as executor trustees. The shares being registered in two names, Hugh as the first on the register had the right to vote. Hugh had on the one hand expressed the opinion to sell the shares in the true interest of the beneficiaries and on the other hand as a director opposed the sale to Hodgson on the ground that the shares should be held by the members of the Bell family. The Directors did not allow registration either in the name of Hodgson or his nominees.

It has been well settled since the decision in Pender v. Lushington that the Directors are not entitled to look behind the register for any purpose. They do not take notice of trust. Similarly, they cannot say that the transferee is the nominee of some one whom they consider objectionable. The accent is always on personal objections to the transferee. The solicitors of the Directors in the case of Bell Brother''s gave the real reason for refusal of registration that Hodgson was

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holder of shares in a rival company. Chitty, J., said that the Directors carefully abstained from stating what their personal objection to Hodgson was and put forward their solicitors to assign the reason for it. The Directors who had an opportunity of exercising their power attempted to exercise it upon a wrong principle and therefore their power was gone. It is quite likely that if the Directors had given evidence of their real reason the Court might have accepted it as legitimate. The decision in the case of Bell Brothers illustrates that where the Directors have the power to refuse registration of the transfer of shares, their exercise of power on a wrong principle will vitiate the exercise of the power.

It follows that where the Directors have uncontrolled and absolute discretion in regard to declining registration of transfer of shares, the Court will consider if the reasons are legitimate if the Directors have acted on a wrong principle or from corrupt motive. If the Court found that the Directors gave reasons which were legitimate, the Court would not overrule that decision merely on the ground that the Court would not have come to the same conclusion. Reference may be made to the decision in Balwant Transport Co. Ltd, v. Y.H. Deshpande which is a Bench decision of the Nagpur High Court. Sapate was a shareholder in the company and owned shares. One of his shares was sold by public auction and was purchased by Deshpande. Deshpande applied for registration. The article in the Nagpur case conferred absolute and uncontrolled discretion on the Directors to refuse to register transfer where in the opinion of the Directors it was not in the interest of the company to admit the proposed transferee to membership. The evidence in that case was that Deshpande was the lawyer of Sapate. Sapate was quarrelling with the company. Sapate also joined a rival concern. The Directors'' decision in those surrounding circumstances was found to be a legitimate exercise of the power of the Directors in the interest of the company.

The decision in In re Smith & Fawcett Ltd. indicates the extent to which the Court upholds the exercise of absolute and uncontrolled discretion of the Directors to refuse to register any transfer of shares. In that case there were two Directors who held the shares in equal numbers. One died. The other director refused to register the transfer of shares in the names of the executors of the deceased Director except in respect of a part of the holding and upon the condition that the balance be transferred to the surviving Director. It was found to be a justifiable act of the director in the interest of the company.

In the old Bombay decision in Kaikhosro Muncherji Heeramaneck v. Coorla Spg. & Wvg. Co. the Board of Directors might decline to register any transfer of shares, unless the transferees were approved by the board. A shareholder became insolvent. His share vested in the official assignee. The official assignee sold the shares. The purchaser applied for registration. The Directors declined to approve of the transferees unless the transferees would pledge themselves not to oppose a certain change in the mode of remunerating the agents of the company, which the Directors desired to effect, and which they believed would be very advantageous to the company. It may be mentioned here that the

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purchaser of the shares required the official assignee to register transfer in the names of the two nominees who were already the holders of shares in the company. The company, however, did not take any objection to the nominees in their personal capacity. The Directors acted on wrong principle and in abuse of power in insisting on obtaining a pledge from the transferees not to oppose change in the remuneration of the managing agents.

A Bench decision of the Allahabad High Court in Muir Mills Co. Ltd. v. T.H. Condon related to the absolute power of the Directors to refuse registration of transfer of shares on personal objections to the transferee. The Muir Mills in that case disallowed the transfers on the ground that the transferees were subordinates of McRobert, the Managing Director of Cawnpore Mills. There was personal animosity between Johnson, the Managing Director of the Muir Mills, and McRobert. The Directors of the Muir Mills came to a conclusion that McRobert should not add to his voting power and "harass the management". It was found to be abuse of judiciary discretionary power of the Directors when they wanted to safeguard the Directors'' personal interest against McRobert."

14. The Apex Court thus emphasised that the decision of the Board of Directors has to be examined by applying the tests viz., (i) whether the Directors acted in the interest of the company, (ii) whether they acted on wrong a principle and (iii) whether the Board of Directors acted with an oblique motive for a collateral purpose. The Company Law Board in exercise of its power conferred under sub-section (2) of section 111 has to examine the decision of the Board of Directors in the light of these legal principles and not as an Appellate Court from the decision of the Court of the original jurisdiction.

15. Recently, the Apex Court in Bajaj Auto Ltd. Vs. Company Law Board and Others, considered the relevant provisions of the Companies Act including section 111 in the light of the Articles of Association of the company conferring absolute, uncontrolled and unbridled power of the Board of Directors to decline to register the transfer of shares and held thus :

"14. As we see if the power of the Board of Directors to refuse registration of transfer of shares must be in the interest of the company and the general body of shareholders. No doubt in the year, 1983, section 82 of the Act provided that the shares or other interest of any member in the company shall be movable property, transferable in the manner provided by the articles of the company. Article 52 sought to give absolute and uncontrolled discretion to the Board of Directors to decline to register or acknowledge any transfer of shares. Even then as already held in Bajaj Tempo Ltd''s case (supra), the Board has to act bona fide, and not arbitrarily and for the benefit of the company as a whole. In the case of a public Ltd. company which is listed with Stock Exchange, an important right of shareholder is to be able to sell his shares at a favourable price. It is seldom in the interest of the general body of shareholders that transfer of shares be refused because that will have an adverse impact on the market price of the shares. Free transferability of shares will not artificially deprive its market price.

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This does not mean that if there is a good reason then the Board has no power to refuse to register the transfer of shares. This Court while examining the action of the Board of Directors is not expected to exercise original appellate jurisdiction and sit in appeal on question of fact. The judicial review while hearing in appeal from the decision of the CLB would be limited to see whether there was a bona fide exercise of power by the Board of Directors while refusing to register the transfer of shares."

16. It would be relevant here to refer to a Division Bench judgment of the then Nagpur High Court in Balwant Transport Co. Ltd., v. Y.H. Deshpande AIR 1956 Nag 20 wherein the Division Bench was concerned with an appeal arising out of the order on the application for rectification of register. The Division Bench presided over by Hidayatullah, J., (as he then was), held that the onus was on the shareholder to prove that the action of Directors in refusing to register transfer of shares was mala fide. In the words of the Division Bench :

"(11) The learned Judge of the trial Court came to the conclusion that the exercise of discretion was arbitrary and, regard being had to what is stated above, we have to see whether the finding is proper or not. We cannot overlook the fact that under the proviso to section 38 this appeal is to be treated as equivalent to one filed u/s 100, C.P.C. A finding fairly reached on the evidence would, therefore, be binding.

In the present case, the learned Judge of the trial Court did not consider the question of onus at all. He felt that it was for the Board of Directors to justify their order, rather than for the applicant before him to show that there was lack of ''bona fides''. But it is well settled that the onus is on the shareholder to prove that the action of the Directors was ''mala fide'' :-- In re, Gresham Life Assurance Society; Ex Parte Penney 1872(8) Ch. A. 446(A), (In re Coalport China Co.) 1895(2) Ch. 404, (In re, Hannan''s King (Browning) Gold Mining Co., Ltd.) 1898(14) T.L.R. 314 (Sutherland (Duke) v. British Dominions Land Settlement Corporation Ltd.) 1926(I) Ch. 746. As in the present case the learned Judge reached his decision after placing the onus wrongly, the decision is open for further consideration even in an appeal u/s 100, Civil P.C. Peddi Reddi Jogi Reddi v. Chinnabbi Reddi AIR 1929 P.C. 13 and Jogeshchandra Roy v. Emdad Meah, AIR 1932 P.C. 28(F) .

"(12) In the resolution which the company passed and which is described at page 7 of the paper book, it merely stated that it was not in the interests of the company to admit the applicant to the membership of the company as a shareholder. Clause 9 of the Articles of Association says:

"Clauses 18 to 23 inclusive, of Table A, annexed to the Indian Companies Act, 1913, shall apply with the following modification :-

Clause 20 shall be modified so as to provide that the Directors may in their absolute and uncontrolled discretion refuse to register any transfer of share; whether fully paid or not, where in the opinion of the Directors it is not to the

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interest of the company to admit the proposed transferee to membership of (if he is already a member) to allow him to increase his holding. Save this change the other provisions of Clause 20 will remain intact".

"(13) Under this Clause the Directors enjoy very vast powers. Unless it can be shown that a power to vested in them was exercised ''mala fide" or for any collateral purpose, the Court cannot overrule the decision of the Directors and substitute its own judgment about the desirability of bringing the name of a person as a shareholder in the register.

"(14) .....

"The question, therefore, is simple whether, on the true construction of the particular article, the Directors are limited by anything except their ''bona fide'' view as to the interests of the company. In the present case the article is drafted in the widest possible terms, and I decide to write into that clear language any limitation other than a limitation, which is implicit by law, that a fiduciary power of this kind must be exercised ''bona fide'' in the interest of the company subject to that qualification, an article in this form appears to me to give the Directors what it says, namely, an absolute and uncontrolled discretion".

"(15) Judged from this test which, in our opinion, states the reasons of the law and the sense of matter, we cannot say that the learned Judge of the Court below reached a proper conclusion in all the circumstances of this case. He should have directed his attention to the question whether the action of the Directors in refusing to register Shri Deshpande disclosed a lack of ''bona fides'' or some oblique purpose not connected with the interests of the company or, lastly whether it was based on some wrong principle.

He did not approach the question that way. He considered the action of the Directors arbitrary. If the Directors of the company had not given any reasons, the burden on Shri Deshpande would have been all the heavier. Fortunately for Shri Deshpande, the Directors of the company in stating their reasons give certain clue to the working of their minds. We have, therefore, to examine the reasons given together with the evidence of the Managing Director and to see whether they are valid under the Articles or ''bona fide''.

"(17) The Directors'' decision has to be understood in the circumstances surrounding the purchase of the share by the respondent. The company was not paying dividends for four years. The transferee purchased but one share in the company. In fact, Shri Sapate managed to get one share sold in the Court auction, while retaining 30 still with him, and the purchaser was no other than his lawyer. The Directors probably considered that the lawyer, who was appearing for Sapate in some cases against the company, purchased just one share, though the company was not paying any dividend, probably only with a view to furthering the obstructionist policy of Shri Sapate.

Nothing has been shown that the Directors, in reaching the decision they did,

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were actuated by any considerations other than the interests of the company. It is not suggested that the decision of the Directors was motivated by mere considerations of group dominance as distinguished from, what they genuinely conceived to be, the interests of the company. Having regard to all the relevant circumstances, the objection to the transferee cannot be considered to be beyond the scope of their power under Art. 20.

In the absence of ''mala fide'', the Court cannot substitute its own discretion in place of that which is given to the Directors by the Articles to refuse to register the transfer."

17. The legal position that emerges from the aforesaid discussion is that despite the uncontrolled and unlimited power regarding rejection of the application for transfer of shares given to the Board of Directors in the Articles of Association such power has necessarily to be exercised apparently for the benefit of the company and the shareholders but the presumption is that the Board of Directors acted fairly, properly and bona fide and it is for the party challenging such decision to allege and prove that such decision was actuated with ulterior motive or was mala fide and not in the interest of the company or for the benefit of the shareholders. If the decision taken by the Board of Directors is supported by reasons, upon challenge to such decision in appeal, the Company Law Board is required to see the legitimacy of the reasons assigned. Again it is for the party challenging such order to show that the reasons assigned by the Board of Directors rejecting the application for transfer are not legitimate and in accordance with law. The burden always is on the party assailing the decision of the Board of Directors to demonstrate that such decision suffers from unsustainable reasons i.e. such reasons are not legitimate or that the decision is vitiated by ulterior motive or corrupt motive or arbitrary conduct or mala fides of the Board of Directors.

18. In the light of the aforesaid legal position, the impugned order of the Company Law Board setting aside the decision of the Board of Directors may now be examined.

19. The Board of Directors rejected the applications of respondent Nos. 4 and 5 because in the opinion of the Board of Directors, the intended acquisition of shares by respondent Nos. 4 and 5 was mala fide and for ulterior motives and if such acquisition was permitted it would be prejudicial to the interest of the company and the general body of shareholders. In the opinion of the Board of Directors the intended acquisition could bring about a change in the composition of the Board of Directors resulting in placing the respondent Nos. 4 and 5 in advantageous position in their dealings vis-a-vis the company resulting in a total conflict of personal interests of respondent Nos. 4 and 5 and that of the company. The basis of reaching such conclusion by the Board of Directors was that the respondents Nos. 4 and 5 together with other relative sought transfer of 28,875 shares which were equivalent to 29.78% of the total voting power. The respondent Nos. 4 and 5 and their relatives were in total management and

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control of the company, namely, M/s. Transformer Manufacturer of India Pvt. Ltd. The entire paid up equity share capital of the M/s. Transformer Manufacture of India Pvt. Ltd., (TMI) is held by respondent Nos. 4 and 5 and their relatives. TMI is tenant of premises owned by the company situated at Vile Parle. A suit for eviction was filed by the company against said TMI on various grounds in Small Causes Court and the said suit was pending. The company had submitted plans to the authorities for development of the said property part of which was in occupation and possession of TMI (company fully owned by respondent Nos. 4 and 5 and their relatives). Besides that the motive of respondent Nos. 4 and 5 was doubted because the company had not declared any dividends for the last several years. The Company Law Board while reversing the said decision observed that one of the reasons which prevailed and actively weighed in the decision making process of the Board was the pendency of the suit filed by the company against TMI but the fact was that the said suit was already dismissed for default and was no more pending. The Company Law Board though noted that an application for restoration of the suit was pending but observed that such application for restoration was time barred and has not been allowed so far. The Company Law Board also observed that it was not understood how the acquisition of shares by the respondent Nos. 4 and 5 herein to the extent of 18.43% shares would either change the composition of the Board of Directors or influence the eviction proceedings or they would be in an advantageous position in dealing with the company. The Company Law Board was not inclined to agree with the reasons of the Board of Directors as to the contention of the company that by acquisition of 18.43% shares it would be possible to change the composition of the Board of Directors. The Company Law Board was also influenced by the fact that though there is dispute between the TMI and the company but the shares of which transfer is sought by respondent Nos. 4 and 5 are 18.43% of the total holding of the company and the said acquisition is by respondent Nos. 4 and 5 in their individual capacity and not by TMI.

20. It may straightway be observed that so far as reason given by the Company Law Board relating to dismissal of the suit filed by the company against TMI is concerned, the said suit has admittedly been restored by the Small Causes Court and is pending trial before the Small Causes Court. Mr. Dwarkadas, the learned Senior Counsel appearing for respondent Nos. 4 and 5 urged that subsequent change of events in relation to the restoration of suit should not be taken into consideration because this Court is only required to see the legality and correctness of the Company Law Board on the facts which were obtaining on the date the decision was given by the Company Law Board and not the events that had taken place subsequently. If the impugned decision is required to be examined in the light of the facts and circumstances obtaining on the date such decision was given, which ordinarily is, then the Company Law Board was required to examine the correctness and legality of reasons given by the Board of Directors on the date such decision was taken. Admittedly, when the Board of Directors rejected the applications made by respondent Nos. 4 and 5 for transfer

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of shares, the suit for eviction filed by the company against TMI which is fully owned and held by respondents Nos. 4 and 5 was pending and the said suit had not come to an end. It was only during the pendency of the appeal before the Company Law Board that the said suit was dismissed for default. However, an application for restoration was made by the company and at the time the Company Law Board decided the matter, the application for restoration was pending and during the pendency of the present company appeal the said restoration application has been allowed and the suit for eviction filed by the company against TMI is pending. Therefore, the reason given by the Company Law Board for not agreeing with the Board of Directors concerning eviction suit no longer survives and needs to be examined afresh by the Company Law Board in the light of the pendency of the said suit now. Similarly, as regards the observation made by the Company Law Board that it is not understood as to how the acquisition of shares by the respondents Nos. 4 and 5 herein to the extent of 18.43% shares would either change the composition of the Board of Directors and influence the eviction proceedings or that they would be in an advantageous position in dealing with the company cannot hold good for want of relevant material before the Company Law Board about the composition of Board and the respective strength of the management. The respondent Nos. 4 and 5 herein challenged the order of the Board of Directors in appeal before the Company Law Board and it was for them to place sufficient material before the Company Law Board to show that acquisition of shares to the extent of 18.43% would not change the composition of the Board of Directors and would not put the said respondents in an advantageous position in dealing with the company. From the memorandum of appeal filed by respondent Nos. 4 and 5 nothing is discernible about the strength of the share holding of the management. It is true that when the earlier applications were made by the respondents Nos. 4 and 5 and some other transferees, the transfer of 29.78% of the total voting power was sought to be transferred and after rejection of the said applications, subsequently two applications for transfer of shares were made only in respect of 17875 equity shares (14605 + 3270) and the said transfer of shares were only to the extent of 18.43% shares but then the Company Law Board did not examine the likelihood of subsequent application/s for transfer of remaining shares which were earlier lodged for transfer which was likely to change the composition of the Board of Directors. The Company Law Board also did not advert to a very vital question about the motive of acquisition of these shares by respondent Nos. 4 and 5 in much as admittedly the company is not listed on any stock exchange nor the company has paid any dividends for the last many years. I do not intend to deal with these aspects at great length since in my view the order passed by the Company Law Board cannot be sustained as it stands and the matter needs to be re-examined and reconsidered in accordance with law by the Company Law Board in the light of the decisions of the Apex Court as noted and the reasons I have recorded.

21. Consequently, this company appeal is partly allowed. The order passed by

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the Company Law Board on 22-5-92 is quashed and set aside. The Company Law Board, Western Region, Bench Bombay is directed to hear and decide Appeal Nos. 4 and 5(111) CLB/WR of 1991 afresh in accordance with law after hearing the parties. Since the appeals are quite old, their expeditious disposal is expected preferably within three months from the date of the appearance of the parties. The parties are directed to appear before the Company Law Board on 18-1-1999.

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