Calcutta High Court
Hindusthan Commercial Bank Ltd. vs Hindusthan General Electrical ... on 11 August, 1959
Equivalent citations: AIR 1960 Cal 637, 64 CWN 458
Author: Bachawat
Bench: S Lahiri, R Bachawat
JUDGMENT Bachawat, J.

1. The appeal No. 129 of 1958 is from an order sanctioning a scheme of arrangement under Section 391 of the Indian Companies Act, 1956. The appeal Mo. 130 of 1958 is from an order confirming reduction of capital. Both these orders were passed by Bose, J. The two appeals have been heard together. This judgment is intended to cover both the appeals.

2. The respondent company is a public company limited by shares. It was incorporated in 1945 under the Indian Companies Act, 1913. The appellant holds 2000 preference shares in the share capital of the company. The authorised share capital of the company is Rs. 50,00,000/- divided into 3,75,000 ordinary shares of Rs. 10/- each, 10,000 5 per cent cumulative participating preference shares of Rs. 100/- each and 50,000 deferred shares of Rs. 5/- each. The memorandum of the company states that shares have the rights, privileges and conditions attached thereto as are provided by the regulations of the company for the time being with power to increase and reduce capital of the company and to attach thereto respectively such preferential, deferred, qualified or special rights or privileges or conditions as may be determined by or increased under the regulations of the company and to vary, modify or abrogate any such rights, privileges and conditions in such manner as may for the time being be provided by the regulations of the company. Article 74 authorises the company to reduce its capital by special resolution subject to confirmation by the Court. Article 8 contains a statement of the rights and privileges of the several classes of shares. The article is expressly subject to what is thereafter provided in other articles of the company. By Article 8 the preferential shareholders have the right to a fixed cumulative preferential dividend of five per cent per annum (income-tax tree) on the capital for the time being paid up, on the shares and to extra non-cumulative dividend in certain contingencies, the total dividend in any year not to exceed 7 per cent. In winding up all the preferential shares are to rank in priority both as regards the return of capital and the payment of arrears of the 5 per cent preferential dividend. The total paid up capital of the company is Rs. 29,20,300/-. The paid up capital consists of 1,89,985 ordinary shares of Rs. 10/- each, 8,452 preference shares of Rs. 100/-each and 35,050 deferred shares of Rs. 5/- each all fully paid up. The main business of the company is the manufacture of Radios and Radiograms and house-hold electrical accessories. The company had always the benefit of technical collaboration with well-known foreign firms of repute. The company was, however, never able to declare dividends. The 5 per cent preferential cumulative dividend on the preference shares was not paid for 12 years since 1945 upto 1957. The company sustained heavy losses. The total loss upto the 31st July, 1956 amounts to Rs. 36,00,000/-. In May, 1956 the company entered into an arrangement of technical collaboration with Messrs. Simplex Electric Company Ltd., a well-known company of Electrical equipment manufacturers of Birmingham. This arrangement was approved of by the Government of India. For the purpose of maintaining and increasing its production further finance is necessary and tor that purpose a presentable balance-sheet is essential. For the present Messrs. Simplex Electric Co., Ltd., has agreed to the arrangement only on a royalty basis. If the financial

condition of the company improves they will also partake in the capital of the company. The company had to incur various loans. A sum of Rs. 10,80,000/- is due to the Industrial Finance Corporation of India on account of loans advanced by the Corporation, The loan from Messrs. Karamchand Bros. Private Ltd., the Managing Agents of the company stands at over Rs. 75,00,000/-. The total dues of the Sundry creditors amount to Rs. 5,36,286/-.

3. In these circumstances, in January, 1957 the Board of Directors of the company proposed a scheme of arrangement between the several classes of Shareholders and as part of the scheme a reduction of the capital of the company. The proposal for the scheme of arrangement was accompanied by an explanatory circular. The scheme as originally proposed, provided for (a) cancellation of share capital in accordance with the arrangement detailed in the circular (b) for reduction of the share capital by cancellation of the paid up capital to the extent of Rs. 70/- for every preference share of Rs. 100/-each to the extent of Rs. 8/- for every ordinary share of Rs. 10/- each and to the extent of Rs. 4/- each for every deferred share of Rs. 5/- each (c) for consolidation of the shares and for issue of fully paid up ordinary shares of Rs. 10/- each in lieu of preference, ordinary and deferred shares and for allotment of 3 fully paid up ordinary shares of Rs. 10/- each in lieu of one preference share of Rs. 100/-

each including the arrears of dividend thereon (d)-

for reduction of the authorized capital of the company to Rs. 37,50,000/- divided into 3,75,000 ordinary shares of Rs. 10/- each (e) for further issue of Rs. 2,83,142/- ordinary shares of Rs. 10/- each subject to the sanction of the Controller of the Capital Issues out of which 1,20,000/- ordinary shares are to be allotted to the Managing Agents or their nominees in part satisfaction of their dues from the company to the extent of Rupees 12 lacs, 66, 858 ordinary shares are to be offered to the existing shareholders of the company and the remaining 96,284 ordinary shares are to be disposed of by the Directors in such manner as they deem fit. The-

explanatory circular pointed out that by the pro posed cancellation of capital a sum of Rs. 22,5l,720/-

would become available for wiping out the debit balance in the Profit and Loss Account and that on making such adjustment a sum of Rs. 13,48,280/-

would remain to the debit of the Profit and Loss Account. The circular states that the Managing Agents had subject to the acceptance of the scheme, agreed to forego Rs. 13 lacs out of their advance to the company and to convert Rs. 12 lacs out of the balance of the advance into ordinary shares of the company. The circular added that the Managing Agents had not charged any interest on their advance since August, 1951 and had thereby foregone interests amounting to over Rs. 10 1/2 lacs and had also fore-gone their monthly allowance amounting to Rs. 3,75,000/-.

4. As the scheme of arrangement involved reduction of capital the Directors convened separate class meetings of the preference, ordinary and deferred shareholders for passing special resolutions for reduction of capital and also an extraordinary general meeting of the three classes of shareholders

for approving the scheme of arrangement. Special resolutions for the reduction of capital were unanimously passed by the three classes of shareholders at their separate class meetings held on the 14th February, 1957. The scheme of arrangement as a whole including the reduction of capital was also approved at the extraordinary general meeting of the preference, ordinary and deferred shareholders held on the same day. At the extraordinary general meeting the scheme was opposed by the appellants, S.S. Puri who held 2000 preference shares and by one Mohamed Abdulla who held 100 preference shares. The other shareholders present at the meeting approved of the scheme.

5. On 12-9-1957 the appellant instituted in this Court a suit for declaration that the resolutions passed on 14-2-1957 were ultra vires and illegal and not binding upon the company and for consequential injunction. We are informed that the suit is still pending. Mr. Mitra did not contend that the pendency of the suit is a relevant matter to be taken into consideration by the Court in these appeals.

6. On or about the 25th September, 1957 the Company presented to this Court two separate petitions for reduction of capital and for sanctioning the scheme of arrangement. The two petitions were admitted by Mallick, J., who gave the necessary directions for the convening of the class meetings of the three classes of shareholders for approval of the scheme of arrangement. Pursuant to that order three separate class meetings were convened and held on 11-12-1957. The proposed scheme of arrangement with certain important modifications was approved by all the three separate meetings. The class meetings of ordinary and deferred share-holders unanimously approved of the modified scheme of arrangement. The meetings of the preference share-holders were attended by shareholders holding shares of the value of Rs. 4,42,700/-. Shareholders holding shares of the value of Rs. 4,42,700/- voted in favour of the resolution approving the modified scheme. No one voted against the resolution. The appellant holding preference shares of the value of Rs. 2 lacs was represented at the meeting by one V.G. Pai. The Chairman enquired of V.G. Pai whether he was voting against the resolution and if so, to raise his hands against it. V.G. Pai did not vote and informed the Chairman and the meeting that he was neutral and that he would not vote either for and against the resolution. The Chairman thereupon declared the resolution for approval of the modified scheme to be carried unanimously by the persons present and voting at the meeting. Subsequently by letter and in the affidavits tiled on its behalf the appellant attempted to contend that the minutes of the meeting did not accurately represent what transpired there and that V.G. Pai really intended to oppose the resolution. This contention was apparently not pressed before Bose, J. Before us Mr. Mitra expressly abandoned this contention. Before Bose, J., it was argued that the modified scheme was not approved by the requisite majority of prelerence shareholders. This contention was rejected by Bose, J. There is no substance in this contention. The records show clearly that the majority in number representing 3/4ths in value of preference shareholders present and voting at the meeting of preference shareholders approved of the modified scheme. Before us Mr. Mitra expressly conceded that the modified scheme was approved by the requisite majority of preference shareholders and other classes of shareholders in accordance with Section 391 of the Indian Companies Act, 1956.

7. The scheme which was approved at the separate class meetings was the scheme as originally proposed subject to certain important variations proposed and carried out at those meetings. In lieu

of the original proposal to cancel the preference shares and to allot ordinary shares in lieu of the preference shares the amended scheme provides tor re-organisation and sub-division of the reduced preference shares of Rs. 30/- each into preference shares of Rs. 10/- and for allotment of 3 preference shares of Rs. 10/- each in lieu of the reduced preference share of Rs. 30/- each including arrears of dividend on the preference share. The modified scheme attaches to the re-organised preference share of Rs. 10/- each the right to payment of a fixed cumulative preferential dividend at 7 per cent per annum and for certain extra dividend not exceeding in any year 5 per cent per annum. The modified scheme also provides for sub-division and re-organisation of the deferred shares in lieu of their cancellation as provided in the original scheme.

8. The two applications were heard and disposed of by Bose, J., by two separate judgments and orders on the 13th of June, 1958 (see AIR 1959 Cal 872 and 679). He allowed both applications. By one order he sanctioned the modified scheme of arrangement subject to the conditions that (a) within three months from the date of his order the managing agents of the company would pay off the claims of the unpaid Sundry creditors of the company (b) within one month from the date of the order the managing agents would acknowledge in writing that they forego Rs. 13 lacs of their claim against the company and (c) if the company does not or is unable to pay any dividend to the shareholders by 31-12-1961, this fact may be brought to the notice of the Court and the Court would be at liberty to give directions for changing the management of the company if it thinks fit to do so and to take such other steps as it appears to the Court to be proper. By a separate order he confirmed the proposed reduction of capital. These two appeals have been preferred from those orders. Pending the appeals the operation of the order of Bose, J., sanctioning the scheme of arrangement was stayed.

9. It is to be observed that the reduction of capital is an integral part of the scheme of arrangement. The scheme of arrangement being expressly conditional on the confirmation of the reduction of capital by the Court the scheme will not be sanctioned if the reduction of capital is not confirmed. On the other hand, if the Court for some reason refuses to sanction the scheme of arrangement, in the circumstances of the case, it will not be fair and equitable to confirm the reduction of capital alone.

10. Many of the matters which arise for consideration in the two appeals are common to them. In this judgment I will firstly deal with the contentions which are peculiar to one or the other appeal and will thereafter deal with contentions which are common to both of them.

11. Appeal No. 130 of 1958 is from the order confirming the reduction of capital. The share capital is sought to be reduced by cancelling the paid up share capital which has been lost and is un-represented by available assets. Mr. Mitra contended that the company has no power to reduce any share capital which is already lost. He relied on the decision of Jessel M.R. in In re Ebbw Vale Steel, Iron and Coal Co. (1877) 4 Ch. D. 827 in which Jesseli M. R. held that under Section 9 of the English Companies Act, 1867, he had no jurisdiction to sanction the reduction of the paid up share capital which had been partially lost. He relied upon the toiiowing observation of Jessel M. R. at page 831: "You do not "reduce" capital which has been already paid up and exhausted". It is curious that such an eminent Master of Law as the late Master of the Rolls came to a conclusion which

certainly did not represent the state of the law even at the time when that decision was given. This point is brought out clearly by Lord Macnaghten in British and American Trustee and Finance Corporation Limited and Reduced v. Couper (1894) AC 399 at p. 412. The Court had then and has now power to confirm a reduction of capital by cancellation of lost capital. The point is made clear by Section 100 of the Indian Companies Act, 1956, which provides that subject to confirmation by the Court, a company limited by shares may, if so authorised by its articles, by special resolution, reduce its share capital in any way: and in particular and without prejudice to the generality of this power, the company may cancel any paid up share capital which is lost or is unrepresented by available assets.

12. Mr. Mitra argued that where the whole of the paid up share capital has been lost, part of it cannot be cancelled. There is no substance in this contention. The company may reduce its share capital in any way. It may cancel any paid up share capital which is lost. It may cancel a part of the lost share capital. Where the whole of the capital is lost the company may cancel any part of it. The section does not place any fetter on the power of the company as is suggested by Mr. Mitra.

13. In appeal to No. 130 of 1958, Mr. Mitra further argued that the loss of capital has not been proved. In agreement with Bose, J., I am of the opinion that the loss of capital has been sufficiently proved. There is cogent evidence of the loss of capital on the record of this case. The balance-sheets tell then own tale. There is also the affidavit of a Director of the Company in support of the petition. Even prima facie evidence of the loss of capital is sufficient where the power of the Court under Section 100 of the Indian Companies Act is invoked. See Caldwell v. Caldwell and Co. Ltd., (1916) WN 70; Marwari Stores Ltd. v. Gourishankar Goenka .

14. In Appeal No. 129 of 1958, Mr. Mitra expressly abandoned the contention that the issue of fresh shares under the scheme of arrangement amounts to borrowing and as such is in violation of Section 293(d) of the Indian Companies Act, 1956. This contention was advanced before Bose J., and was rejected by him. It is plain that the raising of capital by the issue of shares cannot be the borrowing of monies within the meaning of Section 293(1)(d) of the Indian Companies Act, 1956.

15. In Appeal No. 129 of 1958, Mr. Mitra argued that Clauses 9 (a) and 9(c) of the scheme of Arrangement which authorises allotment of 120,000 ordinary shares to the Managing Agents and which further authorises the Directors to dispose of 96,284 ordinary shares in such manner as they deem fit is in contravention of Section 81 of the Indian Companies Act, 1956. It is true that by the scheme it is proposed to increase the subscribed capital of the company by the issue of new shares and such proposal is made at a time subsequent to the first allotment of shares in the company. In such a case, by Section 81, subject to any directions to the contrary which may be given by the company in general meeting, the new shares have to be offered to the persons who are then holders of the equity shares of the company in proportion to the capital then paid up on those shares. In the absence of statutory restrictions the directors had power to issue new shares up to the limit of the authorised capital in such manner as they think fit. The section is intended to fetter this power of the Directors where no direction is given on this matter by the company in the general meeting. The section preserves the power of the company in a general meeting to give directions to the contrary. In this case, the company in a general meeting has given clear directions to the contrary. Having

regard to those directions, the allotment of shares to the Managing Agents and the disposal of shares in such manner as the directors deem fit, can not be said to be in contravention of Section 81. I should have expected that a complaint of contravention of Section 81 should have come from the holder of an. equity share who is sought to be deprived of the benefit of Section 81. But the complaint in this case comes not from the holder of an equity share but from the holder of preference shares.

16. In Appeal No. 130 of 1958, Mr. Mitra contended that Clause 1 of the modified scheme of arrangement passed at the class meetings held on the 11th December, itself involves reduction of capital and as such the modified scheme ought not to be sanctioned because there is no special resolution for reduction of capital by the modified scheme and because the formalities required for the confirmation of such reduction have not been complied with. He relies on the decision of Simonds J., In re St. James Court Estate Ltd., (1944) 1 Ch. 6. In that case, Simonds J., refused to sanction a scheme of arrangement which provided for conversion of preference shares into redeemable preference shares. Such a conversion was in substance a surrender of the existing preference shares in exchange for the redeemable preference shares and amounted to a reduction and simultaneous increase of capital. Nothing of that kind took place by Clause (1) of the modified scheme. Clause (1) of the modified scheme provides for reorganisation and sub-division of preference shares of Rs. 30/- into preference shares of Rs. 10/- each and also for extinguishment and/or modification of the special rights, privileges and conditions attached to the existing preference shares. The preference shares as such were not extinguished. The existing shares with the reduced capital were sub-divided and re-organised and the rights attached thereto were modified.

17. I will now deal with the arguments which are common to both appeals. Mr. Mitra argued that the scheme of arrangement as a whole including the reduction of capital has modified special rights attached to preference shareholders.

18. Mr. Deb appearing on behalf of the respondent expressly conceded that the scheme has modified some of the special rights and privileges attached to the preference shares. This concession was made though Bose J. seems to have ruled that the scheme did not modify any of those special rights and privileges. I think that the concession was rightly made by Mr. Deb. Out of deference to Bose J., I must briefly state the reasons for this conclusion. By Article 8(e) of the Articles of Association the preference shares rank in priority both as regards return of capital and payment of arrears of the 5 per cent preferential dividend whether declared or not over all other shares for the time being in the capital of the company.

19. The scheme of arrangement wipes out the arrears of the 5 per cent cumulative preferential dividend for the last twelve years. In lieu of one preference share of Rs. 100/- and reduced to Rs. 30/-and all arrears of dividends thereon a preference shareholder would receive three preference shares of Rs. 10/- each. The preference shareholders have been allowed to retain 30 per cent of their paid up capital while the ordinary and deferred shareholders have been allowed to retain 20 per cent of their paid up capital. The provision for reduetion of capital forms part of one entire arrangement and it is impossible to say that extra 10 per cent capital is given to the preference shareholders in lieu of their right to arrears of dividend. Assuming that the extra 10 per cent capital represents

arrears of dividend the pSyment of the arrears of dividend is being made by the issue of shares. The market value of the shares is not known. The right to receive payment of the arrears of dividend in cash is taken away. Quite clearly the scheme of arrangement abrogates and/or modifies, commutes and affects the preferential right to payment of the arrears of the 5 per cent cumulative preferential dividend.

20. The scheme cancels 70 per cent of the paid up capital of the preference shares without cancelling the entire paid up capital of the ordinary and the deferred shareholders. The scheme, therefore, abrogates, modifies and affects the right of preference shareholders to preferential return of capital. The decision of Re Mackenzie and Co. Ltd., (1916) 2 Ch. 450 is distinguishable. In that case the share capital of the company was divided into ordinary and preference shares. The preference shares were entitled to a fixed cumulative preferential dividend on the nominal amount of the capital from time to lime paid up on them but they had no priority as to capital. Astbury, J., held that in the circumstances of the case a rateable reduction of capital of both preference and ordinary shares did not alter the eights attached to the preference shares. In the instant case the right of the preference share-holder to preferential return of capital on winding up is abrogated, modified and affected by the cancellation of part of the capital paid up on the preference shares before cancelling the entire capital paid up on the deferred and the ordinary shares.

21. Mr. Mitra then referred us to the provisions of Ss, 106 and 107 of the Indian Companies Act, 1956 and Article 77A of the articles of the company

22. By Section 106 of the Indian Companies Act, 1956 in the case of a company the share capital of which is divided into different classes of shares provision may be made by the memorandum or articles authorising the variation of the rights attached to any class of shares subject to the consent of the holders of not less than three-fourths of the issued shares of that class or the sanction or a resolution passed at a separate meeting of the holders of those shares and supported by the holders of not less than three-fourths of those shares. By Sub-section (2) of Section 106 any provision in the memorandum or articles in force immediately before the commencement of the Act which specifies for this purpose a proportion of less than three-fourths of the shareholders shall have effect as if a proportion of three-fourths had been specified therein instead. The variation of the rights attached to a class of shares in pursuance of such a provision is subject to the rights of dissentient shareholders given by Section 107 of the Indian Companies Act, 1956. Where an application on behalf of the holders of not less than ten per cent of the issued shares of that class is made to the court in accordance with the section to have the variation cancelled, the variation cannot take effect unless and until it is confirmed by the Court and the Court may disallow the variation if it is satisfied that the variation would unfairly prejudice the shareholders of the class represented by the applicant.

23. In this case rights have been attached to-separate class of shares by the articles and the articles also provide for variation of those rights. Article 77A provides that the rights and privileges attached to each class of shares may, subject to the provisions of Section 66A of the Indian Companies Act, 1913, corresponding to Section 106 of the Indian Companies Act, 1956 be modified, commuted, affected, abrogated or dealt with by agreement between the company and any person purporting to

contract on behalf of that class, provided such agreement is (a) ratified in writing by the holders of at least three fourths in nominal value of the issued shares of the class or is (b) confirmed by an extraordinary resolution passed at a separate general meeting of the holders of shares of that class. The last sentence of this article runs thus: "This Article is not to derogate from any power the company would have had if this article were omitted".

24. Mr. Mitra argued that the modification of the special rights attached to the preference shares could only be made with the sanction of the majority of the holders of three-fourths of the issued preference shares in accordance with Article 77A of the Articles of Association read with Section 106 of the Indian Companies Act, 1956, and as the sanction of the requisite majority was not obtained, the scheme of arrangement as a whole including the reduction of capital cannot be sanctioned by this Court.

25. Now rights may be attached to classes of shares either by the articles or by the memorandum. Where rights are attached to a class of shares by the Articles, in view of Section 31 of the Indian Companies Act, 1956, it is permissible for the company to alter those rights by special resolution. And where rights are attached to a class of shares by the memorandum, in view of Sections 13 and 16 of the Indian Companies Act, 1956, such a provision of the memorandum is not deemed to be one of its conditions and may therefore be altered in the same manner as the articles of the company. The Indian Companies Act, 1956. does not contain a provision similar to Section 23(2) of the English Companies Act, 1948, by which the power of the company to alter any condition in the memorandum which could lawfully have been contained in the articles does not extend to variation or abrogation of the special rights of any class of members. An alteration of the rights attached to a class of shares by special resolution is, however, open to challenge on the ground that it is an abuse of the power of the company to alter its articles and an oppressive device to benefit the majority at the expense of the class. For this reason the memorandum or the articles generally contains a provision authorising the variation of the rights attached to any class of shares with the sanction of the Holders of not less than three-fourths of the issued shares of that class. Such a provision is lawful and is sanctioned by Section 106 of the Indian Companies Act, 1956. Article 77A of the articles of association of the respondent company is such a provision. In form Article 77A is permissive. Article 77A explicitly states that it does not derogate from any other power which the company would have had if it had been omitted. Under these articles in strict law it is permissible for the company to alter the rights attached to a class of shares by the articles by passing a special resolution altering the articles. See Palmer's Company Precedents, 16th Edn., page 531. Still except in special circumstances and in the absence of a scheme of arrangement the Court should refuse to sanction a reduction of capital involving alteration of class rights where the special resolution for reduction has not obtained the approval of the requisite majority of the class in accordance with the variation of rights clause. Sometimes the provisions for variation of class rights in terms restrict the powers of the company to alter those rights. In re Old Silkstone Collieries Ltd., (1954) 1 Ch 169, Article 6 provided that the special rights attached to any class of shares may either with the consent in writing of holders of three-fourths shares of that class or with the sanction of an extraordinary resolution passed at a separate general meeting of such holders (but not otherwise) be modified and abrogated. Certain special rights had been attached to two classes of preference stock by two previous special resolutions for reduction of capital which had been confirmed by the Court. The

company passed a third resolution for reduction of capital which purported to extinguish those stocks. This resolution was not passed with the assent of separate meetings of those classes or with the consent of the holders of three fourths shares of those classes. The English Court of Appeal refused to confirm the reduction. The Court held that the reduction modified or abrogated the special rights of those classes. On this finding it was conceded (pp. 182, 185) that the total elimination of the preference capital was incompetent without the approval of those classes under Article 6. Evershed M.R. observed (p. 185) that the special rights could only be taken away under the articles by observing the restrictions of Article 6. Jenkins L.J. observed (pp. 195-6) that in order validly to carry out the reduction it was necessary to put the proposals to those two classes of stock in accordance with Article 6 and to procure the approval of those two classes to the proposals by the requisite majority. It should be noticed that Art, 6 provided that the special rights might foe modified or abrogated in the manner provided in that Article but not otherwise, that Article 6 had been neither deleted nor altered and that the company by special resolution in exercise of its power under the articles sought to abrogate and modify the special rights without observing the restrictions imposed by the article and in these circumstances the Court held that the special resolution had not been validly passed. The learned Editors of Buckley on the Companies Acts, 13th Edn. at page 158, foot note (r) notices the case of Fife Coal Co. Ltd., (1948) SC 505, where a Scottish Court in special circumstances confirmed a reduction of capital which involved repayment of part of the ordinary paid up share capital otherwise than in accordance with the rights of the preference shareholders without requiring the approval of a class meeting of such shareholders.

26. It should be noticed that there was no scheme of arrangement or compromise in the case of (1954) 1 Ch. 169. The special rights attached to a class of shares may lawfully be altered by the machinery of a scheme of arrangement and under Section 391 the Court may sanction a scheme Which involves alteration of class rights.

27. The word, 'arrangement', in Section 391 is of wide import. By Section 390, 'arrangement' includes reorganisation of the share capital of the company by the consolidation of shares of different classes or by the division of shares into shares of different classes or by both those methods. The Court has the power to sanction a scheme of arrangement though the scheme modifies the special rights attached to a class of shares. In re: Hoare and Co. Ltd. and Reduced, (1910) W. N. 87, Nevile J., sanctioned a scheme or arrangement which involved a reduction of capital and which modified the special rights attached to two classes of preference shares. The share capital was divided into preference shares of £ 10 each, A cumulative preference shares of £ 10 each and ordinary shares of £. 1 all fully paid up. The preference dividend was five per cent. The preference shares had priority in dividend and capital over the ordinary shares. The scheme provided for cancellation of the entire paid up capital of the ordinary shares and for extinction of those shares, for cancellation of the paid up capital of preference shares to the extent of £. 2 per share and for cancellation of the capital paid up on A preference shares of £. 10 each to the extent of £. 8-10s. per share and for consolidation and conversion of the reduced shares into shares of £. 10 each all ranking pari passu as regards dividends and capital. The reduction there, as in this case, was conditional on the scheme of arrangement being approved by the shareholders of the company and sanctioned by the Court. The scheme provided for the extinguishment of all arrears of dividend on the two classes of preference shares and for issue of participation certificates to the two classes of

shareholders. Palmer's Company Precedents, 16th Edition, pages 1103-1104, gives a form of an order sanctioning a scheme of arrangement and altering the rights of shareholders as fixed by the memorandum. The share capital of the company was divided into ordinary and deferred shares and the scheme varied the rights attached to ordinary shares by conferring on them a right to a preferential dividend at the rate of 7 1/2 per cent on their paid up capital in modification of Clause 5 of the memorandum. I am conscious that the majority required by Section 391(2) is the majority in number representing three-fourths in value of the class or members present and voting at the meeting whereas the majority required by the provision referred to in Section 106 is the majority of the three-fourths of the issued shares of the class. Considering that the majority required by Section 391(2) is less than the majority required by the provision referred to in Section 108. the Court is bound to scrutinise this scheme of arrangement with care. But the absence of approval of the scheme by the majority required by the provision referred to in Section 106 is no bar to the sanction of the scheme of arrangement under Section 391.

28. Mr. Mitra argued that the special formalities required by Article 77A or any other provision for variation of class rights such as is referred to in Section 106 must be followed and observed just as the special formalities required to be observed by Sections 100 to 105 on reduction of capital must be complied with in the case of a scheme of arrangement involving reduction of capital. There can be no doubt that where the scheme of arrangement involves reduction of capital, the special provisions relating to reduction of capital must be complied with. (See In Re Cooper, Cooper and Johnson Ltd., 1902 W. N, 199 ; In re Indian National Bank Ltd., 53 Cal WN 207 at p. 210 and Bengal Bank Ltd. v. Suresh Chakraverty . Sections 100 to 103 of the Indian Companies Act being special provisions relating to the power of the Court to confirm reduction of capital, they limit the generality of the power which is conferred on the Court by Section 391 to sanction a scheme of arrangement. Where the Court, called upon to sanction a scheme of arrangement, finds that it is also called upon to confirm a reduction of capital, the Court is bound to follow and observe the formalities which it ought to follow and observe in cases of confirmation of reduction of capital. A provision in the articles providing for variation of rights of a class does not, however, prescribe any formality or formalities to be observed by the Court, A provision of this type enables the company to alter the rights attached to a class without the sanction of the Court. Where the power of the Court to sanction a scheme of arrangement involving modification of the rights attached to a class is invoked such a provision can have no application.

29. Mr. Mitra next argued that in the exercise of its discretionary power, the Court should refuse to sanction the reduction of capital as also the scheme of arrangement. On this point, his argument was two-fold. He argued firstly that the reduction of capital and the scheme of arrangement are unfair and inequitable inasmuch as they cancel part of the capital paid up on the preference shares without cancelling the entire capital paid up on the deferred and the ordinary shares though, under the constitution of the company, the losses should fall in the first instance upon the ordinary and the deferred shareholders. He argued secondly that apart from this major consideration, having regard to all the circumstances of the case, the Court ought not to confirm the reduction of capital or sanction the scheme of arrangement.

30. In this case the statutory formalities with regard to the reduction of capital as also the scheme of arrangement have all been complied with. The creditors do not object and are not prejudiced. Still before confirming the reduction of capital the Court is under the duty of satisfying itself that the reduction is fair and equitable between the different classes of shareholders: per Lord Simonds in Scottish Insurance Corporation Ltd. v. Wilsons and Clyde Coal Co. Ltd. 1949 AC 462 (486). And before sanctioning the scheme of arrangement the Court is under the duty of satisfying itself that the scheme is such that an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve: per Maugham J. in Re: Dorman Long and Co. Ltd. (1934) 1 Ch. 635 at pp. 655, 657; whereas in this case the reduction of capital forms part of the scheme of arrangement these two considerations are interlinked with each other and the overall duty of the Court is to satisfy itself that the scheme of arrangement together with the reduction of capital is such that an intelligent and honest man, a member of the class concerned and acting in respect of his interest might reasonably approve and might reasonably consider to be fair and equitable.

31. I will now consider the first branch of Mr. Mitra's argument. Prima facie on general principles of fairness the burden of the loss upon reduction of lost capital ought to fall in the same manner as it would have fallen if the company were being wound up. But there may be special circumstances which may make it fair and equitable to throw the burden of the loss in some other manner. Thus where there is only one class of shares prima facie the loss should be borne rateably by all. But for good reasons the loss may be made to fall unequally on different sets of shares and the Court may sanction such a reduction: see 1894 AC 399, in Re Credit Assurance and Guarantee Corporation Ltd., (1902) 2 Ch. 601. And also where there are different classes of shares such as equity and preference shares and the preference shares are constituted without any preference as regards capital prima facie there should be an all-round reduction of capital and the loss should be borne rateably by all the shares. Bannatyne v. Direct Spanish Telegraph Co., (1886) 34 Ch. D. 287 at pp. 299-300. But where there are different classes of shares and one class has priority as regards return of capital in winding up prima facie the loss should be thrown first on the shares who have no such priority: see Re Floating Dock Co. of St. Thomas Ltd., (1895) 1 Ch. 691. But special circumstances may justify a departure from this prima facie rule. In the present case the preference shares have a right to preferential return of capital in winding up. Prima facie the whole of the capital paid up on the deferred and the ordinary shares should be cancelled before any part of the capital paid up on the preference shares is cancelled. This prima facie rule has not been observed. Only 80 per cent of the capital paid up on the ordinary and the deferred shares have been cancelled. Without cancelling the remaining 20 per cent of their paid up capital there has been cancellation of 70 per cent of the capital paid up on the preference shares. But I have come to the conclusion that we ought not to withhold our sanction to the scheme of reduction on the ground that the entire capital paid up on the ordinary and deferred shares should have been cancelled in the first instance for the following reasons:

32. This ground was not taken and was not argued before Bose, J. There is no reference to this ground in the two judgments delivered by him. Mr. Mitra conceded before us that he did not argue this point before the learned Judge and that this is a new point taken by him for the first time in appeal. The present contention appears to be contrary to the submissions made on behalf of the

appellant by one Bhagatatula Venkata Sanyasi Rao in his affidavit affirmed on the 11th January 1958. In paragraph 24 of his affidavit he submitted that the proposed reduction was in any event not equitable inasmuch as the proportion of reduction was not rateable and that the losses, if any, were not rateably borne by the different classes of shareholders and that the proposed reduction and/or scheme would work injustice on all the different classes of shareholders. Far from saying that the whole of the ordinary and deferred share capital should be wiped out before cancellation of the preference share capital, his contention there was that the losses should be rateably borne by all the different classes of shareholders. Quite distinct and separate considerations of fact arise with respect to the contentions advanced in paragraph 24 of that affidavit and to the contention advanced now. Considerations of fact which are germane to the present argument are not necessarily germane to the argument advanced in that paragraph. In view of the fact that this point was not taken before Bose, J., and in view of the fact that the contention there taken was contrary to and inconsistent with the present contention, we are not inclined to allow Mr. Mitra to raise this point for the first time in the appeal.

33. On the assumption that the appellant should be allowed now to raise this point I have examined the materials on the record and I have come to the conclusion that the Court ought not to withhold confirmation of the reduction of capital and the sanction of the scheme of arrangement on the ground now taken.

34. The whole of the paid up capital of the company has been lost. If the company were wound up today, not only the entire paid up capital of the ordinary and the deferred shares, but also the whole of the paid up preference share capital would be wiped out. In such winding up in spite of their preferential right to return of capital the preference share-holders would get nothing. If the scheme of arrangement is not sanctioned the company is bound to be wound up and all the shareholders will lose their entire capital. The retention of 20 p.c. of the capital of file ordinary and the deferred shares is not being made at the expense of the preference share-holders. The Managing Agents have foregone 13 lacs of their dues conditionally on the scheme of arrangement being sanctioned by the Court. If the scheme of arrangement is not sanctioned, the company will not get the benefit of this concession of Rs. 13 lacs. The total uncancelled paid up share capilal of the ordinary and deferred share-holders amounts of roughly about Rs. 415020/-. If the abstract claim of the preference share-holders is upheld, loss to the extent of Rs. 415020 should be further borne by the ordinary and the deferred share-holders but by the sanction of the scheme of arrangement the company is getting the additional benefit of Rs. 13 lacs. The preference share-holders are, therefore, not really made to bear an additional burden of the loss by reason of the retention of 20 p.c. of the paid up capital of the ordinary and the deferred shares to the extent of Rs. 415020/. In effect, what has been allowed to be retained by the ordinary and the deferred share-holders have come out of the concession of Rs. 13 lacs made by the Managing Agents.

35. The scheme was approved at the separate class meeting of preference share-holders. At that meeting no one voted against the resolution. The appellant was represented at the meeting but its representative chose to remain neutral. The appellant now accepts the position that the minutes of the meeting correctly represents what happened at that meeting. Having done that the appellant does not explain why the appellant did not then oppose the resolution.

36. In these circumstances, I have come to the conclusion that the reduction of capital and the scheme of arrangement cannot be pronounced to be unfair and inequitable on the first ground advanced by Mr. Mitra.

37. I will now deal with the second branch of Mr. Mitra's argument on this point. He suggested that the scheme of arrangement has been proposed in order to prevent investigation in winding up with regard to the huge loss. The affidavit filed on behalf of the appellant suggests that the company should be wound up. Yet I find, that the appellant has not chosen to present a petition to this Court for winding up of this company. Mr. Mitra suggested that the allotment of the block of ordinary shares of the value of Rs. 13 lacs will bring back the Managing Agents into power. The Managing Agents appear already to be in power. The managing agents have been with this company through all its lean times. They have advanced to it the huge sum of Rs. 75 lacs. The object of the allotment of the shares of about the value of Rs. 13 lacs is to reduce the indebtedness of the company to the managing agents. There is reasonable chance of the company making profits if the company is allowed to function and to raise further capital. The total loss amounts to Rs. 36 lacs. By the reduction of capital a sum of Rs. 22,51,720/- becomes available for partially wiping out this loss. A further sum of Rs. 13 lacs is being foregone by the managing agents. The effect of sanctioning the scheme of arrangement is that almost the entire loss is being wiped out. Bose, J., has by his order imposed the further safeguard that if the company does not or is unable to pay any dividend to the share-holders by December 31, 1961, that fact may be brought to the notice of the Court and the Court may give direction for changing the management of the company if it thinks fit to do so. Considering all the materials on the record, I have come to the conclusion that the scheme of arrangement is such that an independent and honest man, a member of the class concerned, namely, the class of preferential shareholders and acting in respect of his interest might reasonably approve and might reasonably consider to be fair and equitable.

38. The scheme of arrangement is in the interest of the Creditors. All the sundry creditors will be paid up by the managing agents. The other creditors do not object to the scheme of arrangement.

39. In these circumstances, I have come to the conclusion that the Court in the exercise of its discretionary power ought to confirm the reduction of capital and ought also to sanction the scheme of arrangement.

40. I have, therefore, come to the conclusion that the two orders passed by Bose, J., ought to be sustained and both these appeals should be dismissed.

41. In Appeal No. 129 of 1958, I propose that the following orders be passed.

The appeal be dismissed. Each party do pay and bear its own cost of the appeal. We direct that the time fixed by the order of Bose, J., by which the managing agents are to pay off the sundry creditors be extended upto three months from today. We further direct that the condition imposed by Bose, J., that if the appellant company does not or is unable to pay any dividend to its shareholders by December 31, 1961, the same may be brought to the notice of the Court and the Court will then be at liberty to give directions the modified and that the condition be read as a condition that if the

appellant company does not or is unable to pay any dividend to its shareholders by 28th February 1963, the same may be brought to the notice of the Court and the Court will then be at liberty to give directions.

42. In appeal No. 130 of 1958, I propose that the following order be passed.

The appeal be dismissed. Each party to pay and 'bear its own cost of the appeal.

Lahiri, J.

43. I agree.