East India Commercial Co. Private Ltd. vs Raymon Engineering Works Ltd. on 22 April, 1965

Equivalent citations: AIR1966CAL232, AIR 1966 CALCUTTA 232

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JUDGMENT

Sinha, J.

1. This is an application in an appeal against an order made by S.P. Mitra. J., dated 2nd February, 1965. The facts are briefly as follows: Raymon Engineering Works Ltd., the respondent company (hereinafter referred to as the 'company') is a private limited company incorporated in 1954 under the Indian Companies Act, 1913 with an authorised capital of Rupees 1,00,00,000/- divided into 8,00,000 ordinary shares of Rs. 10/- each and 20,000 redeemable preference shares of Rs. 100/- each. The appellant is a share-holder of the respondent company in respect of 125 equity shares By a resolution adopted at the company's annual general meeting held on 23rd September 1968 the capital was increased to Rs. 3,00,00,000/-. One of the reasons for this increase, as stated in the Explanatory Statement was that the company had undertaken a new project for the manufacture of spiral welded pipes in collaboration with an American/German group for which a manufacturing licence had been obtained and it was proposed to effect substantial expansion of the company's existing undertakings, for which negotiations were under way for a technical-cum-financial participation in the equity capital of the company with the same group. At the annual general meeting held on 23rd September, 1964 this increase was effected as follows: By an unanimous resolution the share capital of the company was reduced from Rs. 1,00,00,000/- to Rs. 84,83,000/-by the cancellation of 15170 unissued redeemable preference shares of Rs. 100/- each By a further resolution, also unanimously passed at the said meeting, the authorised share capital of the company was raised from Rs. 84 83,000/-to Rs. 3,00,00,000/- by creating 2151700 equity shares of Rs. 10/- each. The respondent company's authorised capital was thus divided into 29,51,700 equity shares of Rs. 10/- each and 4,830 redeemable preference shares of Rs. 100/-each. The company increased the number of equity shares to 29,61,700 and it was made clear in the explanatory statement that equity share capital would be issued to foreign collaborators and/or share-holders with a view to substantially expanding its business by undertaking a new project for the manufacture of spiral welded pipes in collaboration with American German groups. The respondent company thereafter issued a notice for an extraordinary general meeting of the shareholders to be held on the 30th September, 1964 According to the said notice, the company proposed to pass two special resolutions and one ordinary resolution. The first special resolution

proposed to be passed was as follows:

> "Resolved that subject to the sanction of the Controller of Capital Issues and approval of the Government of India to the foreign Financial participation in the Equity Capital, and Cooley Loan Arrangements and subject to repayment of outstanding loan to Industrial Finance Corporation of India, Equity Shares of nominal value of Rs. 10 each be issued to the following parties as set out against their names:
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> M/s. Garvey Grains Inc. Wichita, Kansas, U.S.A. 4,75,000 Equity Shares of Rs. 10/- each for cash.
>
> 29,700 Equity Shares of Rs.
>
> 10/- each for consideration other than cash.
>
> M/s. Phoenix-Rhein- rohar Dusseldorf, West Germany.
>
> 59,400 Equity Shares of Rs. 10/- each for cash.
>
> M/s. Handels Union AG. Dusseldorf, West Germany 59,400 Equity Shares of Rs. 10/- each for cash.
>
> without offering these shares to the existing shareholders, as provided in Section 81(1) of the Companies Act, 1956."

2. It is this special resolution which is the subject matter of this application The extraordinary general meeting has subsequently been held on the 30th January 1964 and this special resolution was passed by a majority of votes, the only dissenting party being the appellant who voted against it. It is, however, material to note here that notice was given of another special resolution by which it was proposed to alter and amend Article 1 and Article 89(B) of the Articles of Association as follows:

> "In Article 1: The word "Corporation" and definition thereof be deleted and the following be added at the end thereof : 'American Collaborators' means Messrs. Garvey Grains Inc., a corporation duly organised under the law of Kansas, U.S.A., with the principal office at 352 North Broadway, Wichita, Kansas, U.S.A. and their Assigns, 'German Collaborators' means Messrs. Handles Union AG. and Messrs. Phoenix Rheinrohar A. G. Corporations duly organised under the laws of the Federal Republic of Germany with principal offices at Koanigsalle 51 and in August Thyssen Stresse 1 respectively in Dusseldorf West Germany.
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> Article 89 (B) the and is hereby deleted, and the following new Article be inserted therefor bearing the same number. So long as the American and German collaborators hold between 47 to 25 per cent of the issued and paid up Equity Capital for the time being, they shall be entitled to appoint as Directors of the Company from

time to time, 3 persons on behalf of American collaborators and 1 person on behalf of the German collaborators. Such Director/Directors will hold office at the pleasure of the respective collaborators, who shall have full power to remove, the Director/Directors so appointed by them under this Article and appoint any other or others in his or their place as and when they shall deem it necessary. Such appointment or removal shall be by notice in writing to the company, provided however, if the share holding of the collaborators falls be-low 25 per cent then the number of Directors to he appointed by them shall be proportionately diminished."

3. The appellant did not object to these amendments which were unanimously passed. As is necessary under Section 178(2) of the Companies Act, 1956, an Explanatory Statement was annexed to the notice. The relevant Explanatory Statement so far as resolution No. 1 is concerned, runs as follows:

"You are aware that your company has undertaken a new project for the manufacture of spiral welded pipes, Crains and also pro-poses to effect substantial expansion of the existing units of the Company's factory at Santragachi, in Technical collaboration with Messrs. Rheinrohr AG and C. H. Jucho of West Germany. One of the conditions in the Industrial licence was that the cost of equipment to be imported was to be financed through foreign capital. Accordingly, the Foreign Exchange portion of the cost of this project is proposed to be financed by participation in cash in the Equity Capital of the Company by Messrs. Garvey Grains Inc. Kansas, U.S.A. to the extent of 1 Million or Rs. 47,50,000/- and by Messrs. Handels Union AG and Phoenix Rheinrohar AG of West Germany to the extent of $125.000 of Rs. 594,000 each. This participation in the Capital as also the Technical Collaboration Agreements have been approved by the Government of India in principle. Messrs. Germany Inc. who negotiated all the collaboration agreements and who will also negotiate the purchase of the equipment will he paid 5 p.c. of 1 1/4 Million Dollars for their services, in the form of fully paid up Equity shares of the Company. Necessary applications to the Controller of Capital issues as well as to the Reserve Bank of India have been made and their approval is awaited. In view of this, your Directors recommend that the resolution under reference may be passed and shares as indicated in the Notice be allotted in favour of the Financial participators, by waiving the rights of the members to be offered first the aforesaid shares.

The Financial participation Agreement is available for inspection in the Registered office of the Company during office hours (except on Saturdays). The material terms of financial participation agreements are as follows:

1. The American and German Participants will subscribe up to 47 p.c. of the issued and paid up Capital of the Company.

2. The American participators will be entitled to nominate on the Board of Directors three members and the German participators will be entitled to nominate one

member as long as the total holdings in the Equity capital of the Company of the Participators is 25 per cent or above. In case the holdings fall below 25 per cent the number of Directors so appointed by the participators will be diminished proportionately. These Directors will hold office at the pleasure of the participators (and will be subject to retirement by rotation.)

3. To finance the Rupee Capital expenditure in India a loan of Rs. 21.4 Million will have to be obtained from Cooley Amendment PL 480 Funds. Necessary applications have been made to the Government of India as also to the Agency for International Developments, Washington. While the approval of the Government of India is awaited, the sanction of the AID, Washington has been received. It is understood that the issue of Equity shares to the Foreign participators will only be made on sanction of Cooley loan by Government of India."

4. The notice and the Explanatory statement is dated 26th August, 1964 and the extraordinary general meeting of the shareholders was called on the 30th September, 1964. On or about the 28th September, 1964, the appellant filed a suit in this High Court being Suit No. 1930 of 1964 (Cal), East India Commercial Co. Private Ltd., v. Raymon Engineering Works Ltd, in which it was stated that the appellant received a notice on or about the 11th September, 1964. It is stated that upon receipt of the notice the petitioner for the first time came to know that the Company had been negotiating with American and German parties for foreign financial participation in the Equity capital and by the proposed special resolution was intending to issue large blocks of Equity shares to the said foreign parties out of the increased capital instead of offering the same to existing shareholders. The right of the Company to do the same was challenged and the petitioner in the said suit asked for an injunction restraining the Company, its Directors, officers and its servants from holding the extraordinary general meeting on 30th September, 1964; for a declaration that the manufacture of spiral welded pipes and cranes is ultra vires the object of the defendant company; for a declaration that the proposed callaboration and/or the financial participation agreements for the manufacture of spiral welded pipes and cranes were void, invalid and ineffective, and for other reliefs. It might be mentioned here that the suit has been framed as a representative suit, but no leave has been obtained under Order 1, Rule 6 of the Code of Civil Procedure. It can not therefore be treated as such. In the said suit, the appellant made an application, inter alia for an injunction restraining the respondent company from holding the extraordinary general meeting on 30th September, 1964. This application came up before S.P. Mitra, J., and the learned Judge has dismissed the application by his order dated 2nd February, 1965. It is against this order that the appeal is directed. In the appeal, an application has now been for an injunction pending the hearing of the appeal . We are now dealing with the said application. We might mention here that the judgment of S. P. Mitra, J., is very well-reasoned and we agree with both his reasoning and the conclusions arrived at. It will, therefore, only be necessary to set out our views briefly. The first point taken in the court below was that the notice dated 26th August, 1964 had been ante-dated and the appellant received the notice on the 11th September, 1964. Section 171 of the Companies Act, 1956, (hereinafter referred to as the 'said Act') provides inter alia that not less than 21 days, notice in writing must be given of a general meeting. Section 53 of the said Act provides that a document may be served by a company on any member thereof either personally, or by sending it by post to him to his registered address, and

where a document is sent by post, service thereof shall be deemed to be effected by properly addressing, prepaying and posting a letter containing the document. Such service shall be deemed to have been effected, in the case of a notice of a meeting, at the expiration of forty-eight hours after the letter containing the same has been posted. It is stated on behalf of the company that the notice and explanatory statement dated 26th August 1964 had been duly posted and duly received by the appellant, 21 clear days before the dale of the meeting. It was stated by the appellant in the court below that he had received the notice on the 11th September, 1964 and there was thus a delay of 3 days in the service of the notice. The learned Judge rightly pointed out that if the appellant intended to prove the date of the receipt of the notice as 11th September, 1964, a date which was disputed, or that the notice was not posted in due time, it could have produced the original notice and the envelope, with the postal marks, which would have clearly shown the date of posting and delivery. This was not done in the court below and the learned Judge rightly rejected the contention of the appellant that the notice had not been served in time. The position has not improved even now, and the original envelope has not been produced before us either. There is, therefore, no reason why we should interfere with the finding of the court below on this point. Upon the main point namely, the first-named special resolution mentioned above, relating to the allotment of Equity shares to foreign collaborators, two points were taken in the court below. They are as follows:

> (1) The manufacture of cranes and spiral welded pipes is outside the scope of the memorandum of the respondent company.
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> (2) The notice does not comply with the requirements of Sub-section (2) of Section 173 of the Companies Act, 1956.

5. With regard to point No. 1, the learned Judge has rightly pointed out that at this interlocutory stage it would not be right to come to a final conclusion in the matter, but having looked into the memorandum of association the learned Judge was of the opinion that the company had ample powers under Sub-clause (vi) of Clause (3). In our opinion, one or the other sub-clauses of Clause 3, mentioned below, are sufficient to authorise the passing of the special resolution :

> "(ii) To build, erect, equip, purchase or otherwise acquire, lay out, develop, maintain and work textile and other factories, saw mills, re-rolling mills, timber works, plywood works, refineries, kilns, plants and machinery of all kinds, bridges, wharves, steel and iron structures of all kinds and all conveniences and accessories thereof ;
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> (iv) To undertake and execute engineering contracts of all descriptions and generally to carry on business as Mechanical and structural Engineers;
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> (vi) To carry on business as general manufacturers, general agents, manufacturers, agents, representatives, carrying, forwarding, clearing and commission agents;"

6. A specimen of a spiral welded pipe was shown to the Court. It is used in modern mechinery as also in structures of all kinds, being particularly useful where pipes are required to be laid on a curved surface. In any event, when the company is entitled to carry on business as general

manufacturers, there seems to be no impediment in the way of manufacturing spiral welded pipes. So far as cranes are concerned, they directly come under Sub-clause (ii) read with sub-clause (vi). I now come to the point No. 2 which is really the point of substance which has been argued in the court below and also before us. It arises as follows :--

> Sub-section (2) of Section 173 of the said Act runs as follows :--
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> " (2). Where any items of business to be transacted at the meeting are deemed to be special as aforesaid, there shall be annexed to the notice of the meeting a statement setting out all material facts concerning each item of business, including in particular the nature of the concern or interest, if any, therein, of every director, the managing agent, if any, the secretaries and treasurers, if any, and the manager, if any. "

7. In the instant case, notice was given of a special resolution together with an Explanatory Statement, the relevant part of which has been set out above. The point to be decided is as to whether the Explanatory Statement is in accordance with law, that is to say, in accordance with Sub-section (2) of Section 173 of the said Act. According to that provision of law, it is necessary, in the explanatory statement, to set out "all material facts" concerning each item of business. The expression "material fact" has not been defined, but has been explained in decided cases. In Henderson v. Bank of Australasia, (1890) 41 Ch. D 330, Chitty, J., said that in cases of this kind it was settled law that the notice which specified the business to be done, or the object of the meeting, was to be a fair notice, intelligible to the minds of ordinary men the class of men who were shareholders in the company, and to whom it was addressed. The Court does not scrutinise these notices with a view to exercise criticism, or to find out defects, but it looks at them fairly. The learned Judge formulated the test as follows :--

> " I think the question may be put in this form: What is the meaning which this notice would fairly carry to ordinary minds ? That, I think, is a reasonable test." In the same case, Cotton, L.J., said in the Court of Appeal that he thought that the notice--"fairly and reasonably expressed to the shareholders what matters were going to be discussed at the meeting. "

8. A Division Bench judgment of this Court--Bimal Singh v. Muir Mills Co. Ltd. considered this point. In that case, notice was given of an extraordinary general meeting of the Muir Mills Co., Ltd., of Kanpur. It was intended to amend the Articles of Association in such a way as to make it almost a new and revised Articles of Association. The prime motive was to enable a group, who had acquired a majority of shares, to get the control of the company. No particulars were given of such amendments, but along with the notice there was a Circular in which it was, inter alia stated that copies of the proposed new Articles of Association and of the Managing Agency agreement were available for inspection at the registered office of the company at Kanpur. The plaintiff, a shareholder of the company, challenged the notice and special resolutions passed at the extraordinary General Meeting convened on the strength of the said notice. Banerjee. J. said as follows : --

> "It is quite possible to argue in this case that the notice in question was a 'tricky' notice, as was said in Kaye v. Croydon Tramways Co. (1898) 1 Ch. 358, and in Baillie's case, (1915) 1 Ch. 503. In this case there is no dispute that there was a partnership between defendant No. 5 and the two Nepalese gentlemen. There is no dispute further that they acquired a very large number of shares in the defendant company. There is no dispute that the partners have acquired and now control the majority of the shares in the two Companies, namely, the Indian Textile Syndicate Ltd., and the Cotton Textile Corporation Ltd., one of which companies has been appointed the Selling Agent of the defendant company. It is quite clear therefore, that the three partners through the said two Companies have acquired a preponderance of voting power in the defendant Company and is in a position to divide practically the entire profit of the Company amongst themselves. On these facts we are of opinion that it was necessary for the defendant company to disclose to the share holders the controlling interest of the partners in the two Companies. But that was not done. An argument is quite plausible that the notice deliberately withheld material facts from the knowledge of the shareholders including the plaintiffs and committed fraud on the plaintiffs. In this case it may be fairly argued that not only there has been a suppression of true facts, but also a false suggestion. Such an argument, we cannot say, would be unreasonable."

It is clear therefore, that the solution of the problem as to whether all material facts were disclosed in an explanatory statement, depends upon the facts of each case.

9. Let us now come to the facts of the instant case. In order to find out the complaint made on behalf of the appellant in connection with the Explanatory Statement, it is necessary to look at paragraph 5 of the plaint (paragraph 6 of the petition) where, particulars of the objections have been enunciated. It is stated therein that the Explanatory Statement annexed to the notice containing the proposed resolution is lacking in the following material particulars :--

> (1) Concerning the proposed foreign financial participation relating to the said "new project" of manufacturing spiral welded pipes and cranes, inasmuch as the three foreign parties belong to two different countries, namely, U.S.A., and West Germany and the nature and extent of their participation in the "new project" has not been disclosed.
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> (2) The technical collaboration agreements with the three foreign collaborators, though alleged to have been approved by the Government on principle, have not been disclosed to the shareholders including the appellant, who have been kept in the dark, and no inspection of such agreements has been offered as required by law.
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> (3) The shareholders have not been told as to whether when and how this new project will be set up in view of the already existing collaboration since 1959 with one Messrs Hoescht G m b H (West Germany) for Railway Coach building at its present factory at Santragachi.

(4) No materials have been given as to the success of the new project and what would be the effect in case of loss in the new project vis-a-vis the existing collaboration.

10. Before considering the question as to whether these complaints are justified, it is necessary to bear in mind the special resolution (No. 1) which was sought to be explained by the Explanatory Statement. It has been mentioned above that by an appropriate resolution passed at the annual general meeting held on the 23rd September, 1963 the authorised capital of the company had already been increased from Rs, 1,00,00,000 to Rs. 3,00,00,000 and new shares were to be issued. In the Explanatory Statement appended to the notice of that annual general meeing, it had been clearly stated that the company had undertaken a new project for the manufacture of spiral welded pipes in collaboration with an American/German group, (for which a manufacturing license had already been obtained) and also to effect substantial expansion of the existing undertakings. It was also stated that negotiations had been under way for a technical-cum-financial participation in the Equity capital of the company with the same group. It was stated therein that it was in view of these developments that the Directors of the Company considered it necessary to increase the authorised capital of the company to Rs. 3 crores by the creation of new Equity Shares, so that upon the finalisation of the collaboration arrangement and confirmation of all the formalities further Equity Share capital could be issued to the foreign collaborators and/or shareholders. It is clear therefore, that the shareholders were not in ignorance of the proposal for foreign collaboration and the allotment of shares to the foreign collaborators. In the Directors' Report, being the Annual Report annexed to the audited account for the year ending 31st March 1963, published in connection with the said annual general meeting, the following statement appears :--

> "Your Directors would also like to record that negotiations are proceeding satisfactorily with a well-known American/German Group for foreign financial participation with technical-cum-management know-How for the installation of a plant for the manufacture of Spirally Welded Pipes for oil, gas, water, sewages, etc., of larger diameter. Your Company has been granted a manufacturing licence for such a plant with an annual capacity of 45,000 tons. The plant is to be supplied by Messrs Hoesch Export GmbH., Dortmund (West Germany) Negotiations are also under way with the same group for substantial expansion of the units already set up. "

11. It is therefore quite clear that the shareholders had already agreed to an increase in the authorised capital and issue of further shares and had already been told that the primary object of increasing the capital and the number of shares, was to invite foreign collaboration from a certain American/German group by ensuring their financial participation and technical cum-management know-how. All that the impugned special resolution asked for is that a definite number of such shares should be allotted to certain American German collaborators mentioned therein. This is necessary because of the provisions of Section 81 of the said Act, which provides that where further share capital is issued they should be offered first to the existing shareholders, unless the company decides by a special resolution that the same may be offered to any other person. What then were the facts that were material to be stated for the purpose of passing such a resolution ? As I have already stated above, the shareholders had already been apprised of the fact of the foreign collaboration and indeed, the primary object with which the annual general meeting held on 23rd

September, 1963 authorised an increase in the capital was to effect foreign collaboration. This resolution was only giving a concrete shape to that intention. That the appellant was not unaware of the factum of foreign collaboration is apparent from the fact that it did not object to the passing of the third (special) resolution, particularly the amendments effected thereby in Article 1 and Article 89 (B) of the Articles of Association. In the relevant Explanatory Statement, we find that the reasons are given for inviting foreign collaboration. It is mentioned therein that the foreign collaborators would give financial help, as also furnish the technical know-how. It has been explained there that the Foreign Exchange portion of the cost of the project was proposed to be financed by participation in cash in the Equity capital by the foreign collaborators. In other words, it has been made clear that by allotting the shares to the foreign collaborators, the company would get the necessary foreign exchange needed for the expansion of the project It has been clearly mentioned as to what commission would be paid for such collaboration. All necessary particulars of the financial participation agreement have been set out and inspection has been offered of the original agreement at the registered office of the company In my opinion, all the material facts necessary for the purpose of the proposed special resolution has been given in the Explanatory Statement. It is not the function of an Explanatory Statement to travel beyond the proposed resolution. Material fads have to be given, but not detailed particulars. So far as the purely technical part of the collaboration is concerned that is a matter which is within the province of the Directors of the Company. It is the Directors who have been entrusted by the shareholders to carry on the administration of the Company. Therefore, the technical details of the Company's work and administration, including the question as to where certain projects were to be set up or how, are not matters which the Directors are bound to disclose to the shareholders in the Explanatory Statement, unless there are special reasons why they should do so. These are details concerning the general administration of the Company, and if the shareholders have lost confidence in the Directors they can always remove them by taking appropriate steps. As it Is, the Directors could not possibly give the details at this stage because the Scheme of foreign collaboration is only at an early stage and actual expansion of the company would require complicated steps like Government sanction, availability of requisite machinery etc. Those are not matters which were necessary to be set out in an Explanatory Statement in support of the impugned resolution. Ordinary shareholders are not to be treated as experts sitting upon judgment as to the technical aspects of manufacture, and such considerations are too farfetched in respect of the allotment of shares under Section 81 of the Companies Act, 1956. The learned Judge has rightly pointed out that the resolution which is challenged does not seek the shareholders' approval either to the technical collaboration agreements or the financial participation agreements, which had already been entered into. Article 124 of the Articles of Association vests in the Directors the entire control and management of the Company. In exercise of their powers under Article 124, the Directors have already entered into such agreements and if the shareholders were dissatisfied with the same, they could ask for the removal of the Directors under Section 284 and other provisions of the Companies Act, 1956. The learned Judge has also rightly pointed out that the plea of non-disclosure of the technical collaboration agreement is by no means bona fide. It is significant that the appellants did ask in their correspondence for inspection of the financial participation agreement but never of the technical collaboration agreements. It took inspection of the financial agreement.

12. Briefly speaking, the matter stands as follows : The shareholders have clearly been apprised of the fact that the company intended to extend its activities and inter alia proposed to manufacture spiral welded pipes. For this purpose they were seeking for foreign collaboration with an American/German group. A manufacturing license had been obtained. It was made clear at the time when the resolution at the annual general meeting dated 23rd September, 1963, was passed for the purpose of increasing the authorised share capital, that the increase was necessary because of the foreign collaboration and Equity shares would be allotted to foreign collaborators In the Explanatory Statement, the details were given, namely, the names of the foreign collaborators, the amounts involved in the financial agreement the commission to be paid to the foreign collaborators and what was expected of them. The resolution was carrying out the objects with which the authorised share capital had already been increased at the annual general meeting dated 23rd September, 1963 which has not been challenged in any court of law. In our opinion, all material facts have been disclosed in the relevant Explanatory Statement and this point accordingly fails.

13. We must however make it clear, as has been done by the learned Judge in the court, below, that our observations in this case must be taken to be observations made at an interlocutory stage and should not be treated as conclusive and binding upon the Court when finally disposing of the suit or the appeal. Subject to this, we consider that the application has no merits and should be dismissed. The cost will be cost in the appeal, certified for two counsel.

14. Interim orders, if any, are vacated.

A.K. Mukherjea, J.

15. I agree `