I

COMMENTARY ON COMPANY LAW

HISTORY

1.1 The company law in this country has its roots in the company legislations of the Indian sub-continent which in turn followed English concepts and English Companies Acts. To have a fair idea of the company law of Bangladesh, one must delve into English principles and appreciate the background of English legislations, their applications in the sub-continent and Bangladesh. The Bangladesh courts freely apply the English law and closely follow the decisions of other courts of the sub-continent.

1.2 In England, the principal medieval associations were the Guilds of Merchants corresponding roughly to the present day trade protection associations. These guilds mostly operated after obtaining charters from the Crown in order to maintain a monopoly over a particular trade. Trading on joint account was either something similar to the present day partnership or a system known as "commenda" a combination of a partnership and business loan advanced on condition of sharing profits.

The nomenclature of "company" was generally applied to English merchants trading abroad. These operated on royal charters and there are instances of royal charters being distributed as early as the fourteenth century. It was not until the sixteenth century when English mercantile activity exploded with foreign adventures, mainly intent on bringing wealth back to England by whatever means, that the royal charters were used frequently to grant monopoly to a particular company to trade in a particular area. This was probably to avoid fighting among the English traders themselves. These companies were loose associations and the members were free to indulge in private trading as well as trading on a joint account.

The most famous of these companies doing business after obtaining royal charter was the East India Company which obtained charter on the last day of 1600 having a monopoly of trade with the Indies. A member could trade privately and also share in the joint account business. It was not until 1692 that private trading was forbidden among members, but trading in India was so profitable that members continued to trade privately and the Board of Directors of the Company turned a blind eye as they were quite happy with the phenomenal profits they were making. The East India Company represented a company formed for a particular purpose where members traded on a joint account.

1.3 It was not until the end of the seventeenth century that the difference between the unincorporated partnerships and incorporated companies became clear. Since choses in action were not assignable in English common law so the legality of transfer of shares in a partnership was always in doubt. A corporation formed on incorporation had this advantage as well as having the benefit of being able to exist in perpetuity, to sue outsiders and its own members and possess a common seal. The greatest advantage of a company – limited liability – was not, however, freely available and was mainly relevant only so that the company could escape members' separate debts rather than members themselves escaping liability for the company's debts.

1.4 The Crown's prerogative to grant monopolies by charter was gradually discontinued after the Revolution of 1688 and it was limited to the right to grant a charter of incorporation. The eighteenth century saw a decline in the growth of foreign companies but there was a surge of domestic companies, and share dealings and stock-broking were common. There was however no separate company law, and only individual pieces of legislation dealt with particular problems. There was a tremendous boom of forming companies with strange objects and one of these was the South Sea Company which entered upon a scheme to acquire virtually the whole of the national debt by buying out the holders in exchange of the company's stock. The idea was that possession of control of all national loans would enable the company to raise vast sums to expand its trade.

It had to pay dearly to outbid the Bank of England for such a bid and, when there was some panic selling because of collapse of some other companies, the shares of this company plummeted in value (from 1000% to 125% in a period of six months). Parliament had to step in with the passage of the Bubble Act in 1720. The result was an erosion of public confidence and a sharp decline in private investments which continued throughout the eighteenth century. However, confidence was gradually restored and the years 1824-25 saw a boom comparable to that seen a century earlier. This boom was followed by a slump and various court cases did little to clarify the law.

1.5 The Joint Stock Companies Act of 1844 passed after the report of Gladstone who headed the Parliamentary Committee on Joint Stock Companies introduced the three basic principles of modern company law. It provided for the registration of all new companies with more than 25 members or with shares transferable without the consent of all members. Secondly, companies could be incorporated by mere registration as opposed to a special Act, and lastly, it provided for an extensive disclosure requirement which still is the cornerstone of all company laws in the world. Limited liability was not mentioned. This concept was introduced by the Act of 1855 later to be repealed and incorporated in the Joint Stock Companies Act, 1856. It was not however until the Salomon's case[1] that the principle was clearly vindicated and any doubt that remained as to the liability of members of a closely held company for the company's debts was removed.

1.6 In the sub-continent company legislation started in 1850. Act No 43 of 1850 was based on the English Companies Act of 1844 which made it possible, for the first time, to incorporate and register a company without obtaining a royal charter. Under the Indian Act of 1850 the Supreme Courts in the Presidency towns of Calcutta, Bombay and Madras were authorised to order registration of unincorporated companies of partners associated under a deed containing a provision that the shares were transferable. The privilege of limited liability was not conferred by this Act, although a company was permitted to sue and be sued in its registered name.

1.7 In India, in 1857, an Act for 'the incorporation and regulation of Joint Stock Companies and other Associations either with or without limited liability of the members thereof' was passed; but under this Act the privilege of limited liability was not extended to a company formed for the purpose of banking or insurance.

1.8 This disability was removed by Act VII of 1860 based on the English Companies Act of 1857. Then following the English Companies Act of 1862, a comprehensive Act was passed in India in 1866 for consolidating and amending the laws relating to the incorporation, regulation and winding up of 'Trading Companies and other Associations'. Between 1866 and 1913,various amendments in the Indian law were made following similar changes in England.

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1 Salomon-vs-Salomon [1897] A.C. 22

1.9 The whole law relating to companies was re-enacted in a comprehensive form by the Companies Act of 1913. This Act was principally based on the English Companies (Consolidation) Act of 1908. Between 1908 and 1936 small amendments were made in the Act of 1913. The Indian Companies (Amendment) Act, 1936, introduced important provisions in the Act of 1913 in the light of the English Companies Act, 1929. This Amendment Act of 1936 also recognised for the first time the system of managing agency in the sub-continent.

1.10 After the partition of the subcontinent, India passed a new comprehensive Act in 1956 which was primarily based on the English Companies Act, 1948 and the suggestions made by the Bhava Company Law Committee Report. This Act was amended in India a number of times (15) between 1960 and 1988.

1.11 During Pakistan time, a Company Law commission was set up and it did suggest amendments in 1962 in the light of the English and Indian amendments. However no law was passed although small amendments were made. The Securities and Exchange Ordinance 1969 was the most important piece of legislation touching our corporate activities during this period. It supplemented the Capital Issues (Continuance of Control) Act of 1947 which gave extensive powers to the Controller of Capital Issues.

1.12 After the emergence of Bangladesh, a Company Law Reforms Committee was set up in 1979 comprising leading government servants, chartered accountants and lawyers. The Ishtiaq Committee made extensive recommendations for changes in our company law but not until 1994 was a new comprehensive Act passed by the Parliament. The Securities and Exchange Commission Act of 1993 has created the Securities and Exchange Commission which oversees issue of capital, and has as its primary purpose the protection of the public in corporate investments. It has been given extensive powers to make rules and regulations. Its responsibilities include those of the Controller of Capital Issues under the Acts of 1947 and 1969.

1.13 Section 17(2) of the Companies Act 1994 in its original form makes certain Schedule 1 articles compulsory but while mentioning these articles, the draftsmen have blindly copied the numbers from section 17 of the Act of 1913 although the serial numbers of Table A Regulations in the Act of 1913 are different from the serial numbers of Schedule 1 regulations in the Act of 1994. The numbers of the Articles mentioned in section 17(2) should have been chronologically one number more (regulation 56 should have been regulation 57 and so on). The regulations mentioned in section 17(2) of the Act of 1994 are not at all the same mentioned in the Act of 1913.

DEFINITIONS

2.1.1 **Articles of Association** – The definition of "articles of association" in section 2 of the Companies Act, 1994 is similar to the one given in the Act of 1913. For a greater elucidation see sections 17-22 of the Act and section 6 below.

2.1.2 **Banking Company** – The definition of a "bank company" is new. Under section 5(9) of the Bank Companies Act of 1991 a bank company has been defined as a company working under the directions of the Bangladesh Bank including new and special banks but excluding companies which being mainly in the business of production of goods and commerce, accept deposits from the public.

2.1.3 **Company** – The definition of a "company" is the same as in the previous Act. The Supreme Court of India has observed that a company is in some respects, an institution like a State functioning under its basic constitution consisting of the Companies Act and the memorandum of association. [1]

2.1.4 **Court** – The definition given of a "Court "is substantially the same as provided in the earlier law. Wherever the Act mentions the word 'Court' the High Court Division of the Supreme Court will have the jurisdiction to entertain the case. The relevant case law will be elaborately discussed in the annotation of section 3 (supra).

2.1.5 **Debenture** – The definition of a "debenture" follows the definition given in the Act of 1913 and clarifies that a document will be a debenture whether it does or does not create a charge and includes debenture stock, bond and other securities. This definition corresponds to the definition of a debenture given in the Indian Act-section 2(12) which in turn was based on the Report of the Bhava Company Law Committee citing the English Companies Act of 1948. There is no precise definition of a debenture in the Act and one has to examine what the different authors of different countries have commented on this. Professor Gower summarises the essential feature of a debenture as being a type of transferable security (resembling shares) whereby a company can raise finance in form of loan capital instead of share capital.[2] He however apprehends that problems may arise, for in recent years, developments in banking and commercial circle have led to the invention of remarkable array of new and highly sophisticated types of "securitised" loan investment as a result of which finance, which would formerly have been raised by a straightforward bank loan (for most purposes not a debenture) may be obtained through the issue of instruments, some of which for most purposes unquestionably are debentures and others of which may or may not be.[3] At common law a company issues a debenture when it delivers its acknowledgment in writing of a debt it owes, whether existing or newly created but negotiable instruments such as bill of exchange and

1 Life Insurance Corporation of India vs Escorts Ltd [1986] 59 Comp. Cas. 548
2 Growers Principles of Modern Company Law 6th Ed. p. 323
3 ibid.

promissory notes as well as deeds of covenant are excluded.[1] When a public company raises loan finance from the investing public the company may, instead of creating a series of debentures, raise a single fund of debenture stock from which the company can issue to such subscriber a certificate declaring that the holder is entitled to be a creditor for a definite sum of money, being part of the stock. That would allow holders of debenture stock to transfer any fraction of the monetary sum represented by their holdings, something which cannot be done by a holder of a debenture.[2]

2.1.6 **Director** – The definition of a "director" is the same as given in the Act of 1913. It is the function and not the name that matters.[3] The articles of association of a company may designate its directors as governors but so far as the law is concerned they are directors.[4] Previously when joint stock companies were mostly unincorporated, their validity depended on a deed of settlement vesting the property of the company in trustees. The concept that the directors are trustees persisted even after companies became incorporated as the courts of equity in England tend to apply the label "trustee" to anyone in a fiduciary position. In truth, today, directors are agents of the company standing in a fiduciary relationship to the company, their principal.[5] Directors are trustees of the monies of the company.[6]

2.1.7 **District Court** – The definition of a "district court" is the same as that given in the preceding law.

2.1.8 **Existing Company** – The definition of an "existing company" is substantially the same as given in the previous law and all companies existing on the date of coming into effect of this Act are covered by this definition.

2.1.9 **Financial Year** – The definition of a "financial year" has been taken from the Indian Companies Act-section 2(17). The term body corporate has not been defined in our law and the definition given in the Indian Companies Act will be relevant as including a company incorporated outside the country. The definition of a financial year is relevant for the sections relating to balance sheet and audit.

2.1.10 **Insurance Company** – An "insurance company" under this Act remains the same as before.

2.1.11 **Manager** – The definition of a "manager" covers all who may be acting as a manager whether or not he is acting on the basis of a contract of employment and by whatever name called. Note the similarity of the position of a manager with that of a managing director except that a manager need not be a member of the Board whereas the managing director must be a director.

2.1.12 **Managing Agent** – The "managing agent" is the product of English colonial business in this country. The merchants in the East India Company used to do business individually but because they could not be present here full time so they used to appoint a managing agent to look after their business for a hefty commission and a share of the profits. The merchants were quite happy with whatever they used to get as they were reluctant to stay here full time or go and stay in the remote mine fields and tea estates of the sub-continent. The western Indian businessmen were quick to avail of this system and very soon managing agency houses mushroomed in the big commercial centres of India where it became an accepted

1 Handevel Pty Ltd vs Comptroller of Stamps (Vic) [1985]157 CLR 177; 62 ALR 204
2 Ford and Austi's Principles of Corporations Law 7th Ed. section 19.060.
3 In re Forest of Dean Coal Mining Co.[1879] 10 Ch.D. 450.
4 Pennington's Company Law 5th Ed 609.
5 Gower's Principles of Modern Company Law 6th Ed. 598.
6 Md. Yameen and another Vs. K A. Bashar and ors (1986) BLD(AD) 305.

norm to set up companies through managing agency houses and have these companies sign managing agency agreements with those houses and then go to the public for share subscription. It was not until 1936 that the legislature first took notice of the rampant practice of managing agency and put a curb on their profit taking by inserting limitations on the profits they could make. By definition a managing agent is entitled to manage the whole of the affairs of the company or the bulk of the affairs to the exclusion of the board of directors. In Bangladesh the system of managing agency is going out of fashion now.

2.1.13 **Managing Director** – The definition of a "managing director" is new in our Act and follows the definition given in section 2(26) of the Indian Act of 1956. There is some anomaly in this definition. The managing director must be a director and the definition goes on to say that whoever is occupying the position of a managing director, whether that be an individual, firm or a company, shall be included in this definition. It is submitted that it is irrelevant that a managing director may be a firm or a company as the definition prescribes that a managing director must be a director and if so then under section 90(3) of the Act must be a natural person. The Indian Act does not mention that a managing director may be a firm or company.

The second proviso that a managing director shall exercise his powers subject to the superintendence, control and direction of the board of directors will remove a controversy that has sometimes arisen when the promoters of a company sought to perpetuate their control over the affairs of the company by inserting a provision in the articles giving substantially all powers to the managing director and naming their nominee the managing director in the articles. In *Holdsworth and Co. vs Caddies*[1] it was held that the managing director of a parent company could be directed to look after the business of its subsidiaries only.

It is doubtful that the term of office of a managing director is protected if it is contained in the articles for if the articles are changed then the managing director loses all protection. Further, if he ceases to be director then he automatically loses his position as a managing director and his contract will be deemed to be terminated without that being a breach of contract.[2] Professor Gower comments that accordingly it would seem that the company in such circumstances can sack a managing director without breaking the contract by dismissing him as a director and that he can resign his directorship and then walk out without any period of notice. In any case this difficulty can be dealt with by the Director entering into a fixed term service contract with the company, as is commonly done in large public companies.[3]

If the managing director holds office simply by reference to the articles without any separate service contract, the relationship between the company and the managing director may be modified by the company's alteration of the articles governing employment and the company will not be in breach of the contract.[4] If however the managing director is employed under a contract which is clearly outside and independent of the articles, any interference by the company with the director's contractual rights will not be excusable merely because the prejudice arose from the company using its powers to alter its articles.[5] The courts have sometimes found an implied term in the service contract to the effect that the company will not exercise the power of alteration to put an end to the contract[6].

2.1.14 **Memorandum of Association** – The definition of "memorandum of association" corresponds to the definition given in section 2(10) of the Act of 1913. For further details see sections 5-12 and 22 of the Act and section 5 below.

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1 [1955] 1 W.L.R. 352 H.L.
2 Read vs Astoria Garage Ltd [1952] Ch 637 C.A.
3 Gower- 6th Ed. P. 192
4 Shuttleworth vs Cox Brothers and Co Ltd [1927] 2 K.B.9.
5 Allen vs Gold Reefs of West Africa [1900] 1 Ch 656.
6 Southern Foundries Ltd vs Shirlaw [1940] A.C.701

2.1.15 **Officer** – This definition is new and corresponds to the definition of an "officer" in section 2(30) of the Indian Companies Act except that the insertion in the Indian Companies Act in 1965 in this definition of a person in accordance with whose directions or instructions the Board of Directors or any director is accustomed to act is not present in our law. Our law also does not mention the treasurer as an officer of the company but the definition is wide enough to include a treasurer. The definition of an officer is relevant to determine the responsibility and the consequent liability of persons in running the company and complying with the statutory requirements of filing returns etc. An 'officer' in company law is different from an officer in Labour Law. Any persons who are regularly employed as part of their business or occupation in conducting the affairs of the company may be "officers" of the company.[1] The secretary, accountant and cashier are officers of the company.[2] It includes assistant secretaries, branch managers and a marketing manager.[3] It may include an agent employed by a company.[4] The English Court of Appeal has held that the definition of an officer does not exclude subordinate officers in lower ranks discharging managerial functions[5] but does not *include the 'receiver and manager' appointed by or on behalf of the debenture holders.*[6] An auditor is an officer of the company within the meaning of the sub-section for the purpose of prosecution for any misdeed etc. Although the Act mentions that an auditor is an officer only for the purpose of sections 331-333 yet because of the wide language used in the sections an auditor will be liable for any breach of confidence while discharging his duty.

2.1.16 **Prescribed** – The definition of "prescribed" is not new and follows the definition given in the Act of 1913 and the Indian Companies Act.

2.1.17 **Public and Private** – The definitions of a "public" and "private" company are similar to those given in the Act of 1913. The articles of associations of a private company must contain all the three conditions mentioned in the law, i.e., restriction of the right to transfer its shares, limiting the number of members to fifty excluding employees and prohibition of any invitation to the public to subscribe for the shares or debentures of the company. A private company may therefore offer privately its shares or debentures for subscriptions.

2.1.18 **Registrar** – The definition of a "Registrar" is the same as given in the Act of 1913.It has been held by the High Court Division that the Registrar has no authority to accept or reject annual filings by a company.[7] It has however become a practice at the Registrar's office to accept or reject a return filed by a company as if the validity of an action by the company or its shareholders are decided by his office and not the Court. It is submitted that in view of this decision ,the Registrar, in the absence of an apparent fraud or forgery, has no jurisdiction to pronounce on the validity of a transaction of which a return is filed in his office. The practice of scrutinising or accepting or rejecting all returns in the absence of a complaint of fraud or forgery is not known in other countries having a parallel company law.

2.1.19 **Schedule** – The definition of a "schedule" is new.

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1 Halsbury's Laws of England (4th Edn.Vol7 para 540).
2 Official Liquidator, Golcha Properties P. Ltd vs P.C.Dhadda [1980] 50 Comp Cas,175.
3 Suryanarayana vs Vijaya Commercial Bank Ltd [1959] 29 Comp Cas 114; AIR 1958 A.P.756; In re Hanuman Bank Ltd.[1964] 34 Comp Cas 640. Ravindra Kumar Sangal vs Auto Lamps Ltd [1984] 55 Comp. Cas. 742.
4 Nandlal More vs Mirchandani [1968] 38 Comp. Cas 39.
5 Re A. Company [1980] 1 All E.R. 284
6 In re Johnson & Co (Builders) Ltd [1955] Ch 634; [1955] 2 All E.R. 775.
7 BCIC vs Registrar 39 DLR(H.C.)1

2.1.20 **Secretary** – The definition of a "secretary" is new in the Act. The definition of a secretary in the corresponding Indian law is far more exhaustive probably because in India there has been a rampant practice of administering a company through appointment of secretaries in order to avoid the stringent restrictions on managing agencies. A secretary's duties are administrative in nature. He has no power to negotiate contracts or borrow money. He cannot register a transfer of shares if such transfer is to be sanctioned by the Board even if there be no board.[1] He cannot file a suit on behalf of the company unless so authorised;[2] or alter the register of members without the Board's authority[3] or summon a meeting without the Board's authority. *In re State of Wyoming Syndicate Ltd.*[4] The English Court of Appeal has however in recent times sought to give the secretary a more important role in the corporate world.[5] A secretary was entitled to hire cars. Lord Denning said that a company secretary had usual authority to sign contracts connected with the administrative side of a company's affairs, such as employing staff and ordering cars.Salmon L.J. referred to the secretary as the chief administrative officer of the company.[6]

2.1.21 **Share** – The definition of a " share" given in the Act of 1994 is the same as in the Act of 1913. Professor Gower comments that the definition of a share which is perhaps the most widely quoted is that of Farwell J. in *Borland's Trustee vs Steel*[7] that 'a share is the interest of a shareholder in the company measured by a sum of money, for the purpose of liability in the first place, and of interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders inter se in accordance with (section 22).[8] A share as a chose in action is an indivisible set of rights. As an item of property it differs from physical subjects of ownership such as land in that its characteristics are fixed, not by nature but by whatever is put into the contract between company and shareholder.[9] The Indian Supreme Court has observed that 'by a share in a company is meant not any sum of money but an interest measured by a sum of money and made up of diverse rights conferred on its holder by the articles of the company, which constitute a contract between him and the company.[10]

2.1.22 **Subsidiary** – The definition of a "subsidiary" company has been expanded and follows the definition given in section 4 of the Indian Companies Act, 1956 as originally framed but the amendments in India in 1960 and 1969 do not find place in our law. The definition intends to capture the spirit of the relationship between a company and another, i.e, if a company does control the other then the latter will be a subsidiary company. The concept of holding and subsidiary companies is a legacy of English law which requires the preparation and publication of a set of group accounts. Section 186 of the Act of 1994 requires a holding company to file certain documents relating to the subsidiary company. The Courts in other countries have viewed the group as a "single economic unit".[11]

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1 Re Zinotty Properties Ltd [1984] 3 All E.R.754

2 Turner Morrison & Co vs. Hungerford Investment Trust Ltd [1972] 42 Comp.Cas. 512 SC; also Daimler Co Ltd vs Continental Tyre and Rubber Co (G.B.) Ltd [1916] AC 307 HL.

3 In re Steam Navigation Co Ltd. [1917] 2 Ch. 100

4 In re State of Wyoming Syndicate Ltd. [1901] 2 Ch 431

5 Panorama Developments(Guildford) Ltd vs Fidelis Furishing Fabrics Ltd. [1971] 2 Q.B.711

6 See also Donato vs Legion Cabs (Trading) Co-operative Society Ltd [1966] 2 NSWR 583

7 [1901] 1 Ch 279

8 Principles of Modern Company Law 6th Ed. p. 300

9 Ford and Austin's Principles of Corporations Law 7th Ed.17.140.

10 CIT vs. Standard Vacuum Oil Company AIR 1966 SC 1393.

11 The Roberta (1937) 58 Ll.L.R. 159 (bills of lading issued by subsidiary company binding on the parent company); Holdsworth & Co vs Caddies [1955] 1 W.L.R. 352, H.L. (managing director of a parent company confined to duties in a subsidiary company); Scottish Co-operative Wholesale Society Ltd. vs Meyer [1959] A.C. 324H.L. (parent company held to be acting oppressively as it acted through a subsidiary which it had formed).

In *D.H.N. Food Distributors Ltd vs. Tower Hamlets L.B.C.*[1] the Court of Appeal held that D.H.N. was entitled to a proper compensation for compulsory sale of land of one of its subsidiaries because according to Lord Denning, M.R. the group was virtually the same as a partnership. However, the Scottish House of Lords expressed doubts on the proper application of the principle by which corporate personality was pierced.[2] In European Community law Articles 85 and 86 of the Treaty, while referring to "companies" mentioned "undertakings", a much wider and looser concept. If a company established outside the Community carried on business from a branch office within the E.C. it would be amenable to the jurisdiction of the E.C. Commission and Court.[3]

3.1 **Jurisdiction** – The High Court Division exercises special statutory jurisdiction to try matters under the Companies Act. In accordance with the provisions of section 3 of the Companies Act, an application relating to a company having its registered office in mofussil should be made in the original side of the High Court.[4] Sub-section 3 of section 3 will have no application where the objection to jurisdiction is taken at the very commencement of the proceeding or at proper time.

Murshed C.J. and A.S.Chowdhury J. held in *Dacca Jute Mills Ltd and ors vs Satish Chandra Banik and others*[5] that matters decided under the Companies Act in the High Court by a Single Bench are not disposed of in exercise of its ordinary original civil jurisdiction which has not yet exercised such jurisdiction. The Court does not exercise any ordinary original civil jurisdiction, although it has powers to do so, after necessary formalities have been complied with. Cases under the Companies Act are decided by way of a special statutory jurisdiction conferred upon the Court by the Act itself. It would be a misnomer to describe such jurisdiction as ordinary original civil jurisdiction.[6] Question arose in that case whether an appeal would lie against an order of a single judge passed under section 79(3) of the Companies Act 1913. Arguments were raised at the Bar that such an appeal would lie under the Letters Patent although no appeal was provided in the Companies Act. Repelling the argument Murshed C.J. held that the jurisdiction of the High Court to try matters relating to the Companies Act is derived under section 3 of the Act and not the Letters Patent. The law which must govern the situation is the Companies Act itself.[7]

This case was followed in *Uttara Jute Fibres Industries vs Ashraf Jute Mills Ltd.*[8] and Md. Ismailuddin Sarker J. observed that " the Court" means the Court having jurisdiction under this Act and according to section 3 the Court having jurisdiction under this Act shall be the High Court Division. The matters are decided under a special statutory jurisdiction conferred upon the High Court Division by the Companies Act itself[9]. In the case of *Md. Shamsuzzaman Khan vs M.S.Islam and others*[10] it was held that section 3 of the Companies Act only gives certain jurisdiction to the High Court for resolution of the disputes under the Companies Act. If the nature of the dispute which is being litigated upon is entirely a civil dispute then it can only be decided by a competent civil court. When the Registrar fails to exercise his duty, this section does not bar the writ jurisdiction of the High court to interfere.[11] A similar writ lay when the Registrar failed in his duties to accept the returns filed by the Company.[12]

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1 [1976] 1 W.L.R. 852
2 Woolfson vs Strathclyde Regional Council [1978] S.L.T. 159 H.L
3 Advice of Advocate General Warner in Instituto Chemioterapico Sp A and Commercial Solvents Corpn.vs. The Commission (Cases 6 and 7/73) [1974] E.C.R.223.
4 Al Haj Md Islam Khan vs Al Haj Abdur Rahim Choudhury and others 8 P.L.R. Dac 639.
5 19 D.L.R. Dac 735
6 ibid.
7 ibid. at page 742.
8 44 D.L.R. H.C.452
9 Also see Abdul Muhit and ors. vs Social Investment Bank Limited (SIBL) and others 54 DLR 306
10 28 D.L.R.101
11 Md. Idrish vs East Pakistan Timber Merchants Group 20 DLR(S.C.) 354; PLD (1968) SC 412
12 BCIC vs Registrar 39 DLR(H.C.) 1.

CONSTITUTION AND INCORPORATION

4.1 Section 4 of the Act of 1994 follows section 4 of the Act of 1913 with small modifications. It prohibits partnerships exceeding certain numbers. The section is intended to prevent the mischief arising from large trading undertakings being carried on by large fluctuating bodies, so that persons dealing with them would not know with whom they are contracting and so might be put to great difficulty and expense. This was a public mischief to be redressed.[1] One difficulty relating to unincorporated bodies was regarding the power to sue or be sued. The second and most important disadvantage of the absence of incorporation was that members could not limit their liability. Of course they could make a virtue of necessity, as did the Phoenix Assurance who emphasised the advantages to the public of the full responsibility of its members.[2] In fact however unlimited liability was a snare as the creditor did not know who were the latest members of such large trading bodies. The State intervened to put an end to such state of affairs and trading by large unincorporated bodies was forbidden. Nowadays it is becoming more and more uncommon for trading to be done by large unincorporated bodies and the application of this section to prosecute people is rare.

The word "person" is not defined in the Act and although the General Clauses Act includes a company or other association within the definition of a person, the Privy Council has held in *Senaji Kapurchand vs. Pannaji Devichand*[3] that it means only individuals.

An illegal company cannot sue to recover any debt or other property[4] nor can it be sued to recover money lent to it to carry out its illegal object.[5] But any person who is in possession of money or property received on behalf of an illegal company may be sued to render an account.[6] Offence under sub-section (5) is non cognizable offence.

Memorandum of Association

5.1 The Memorandum of Association is the basic constitution of the company. The "one man company" is legal.[7] The shares may be of the smallest nominal amount, and one share is enough to constitute membership. There is nothing in the Act requiring that the subscribers shall be independent or unconnected, or have a substantial interest, or have a mind and will of their own, or that there shall be anything like a balance of power in the constitution of the company. If there are seven, or, in the case of a private company, two members, this section is complied with.[8] The word "person" includes a body corporate and a company may become a member in another company.[9] Foreigners may now become shareholders subject to

1 Smith vs. Anderson (1880) 15 Ch.D. 247 at 273
2 Gower citing DuBois in Principles of Modern Company Law 6th ed. p.31
3 AIR 1930 P.C. 300
4 Jennings vs Hammond (1882) 9 QBD 225
5 Re Padstow Assocn. [1882] 20 Ch.D. 137
6 Greenberg vs Cooperstein [1926] 1 Ch 657
7 Salomon vs. Salomon [1897] A.C. 22, 45
8 ibid
9 See Section 2(39) of the General Clauses Act, 1897

conditions laid down by the Bangladesh Bank and the Board of Investment. There is at present almost no restriction on foreigners becoming shareholders although the Securities and Exchange Commission (SEC) may lay down conditions about the sale of their shares if they buy quoted shares of primary issue. The latest regulations laid down by the Authorities should be checked before foreigners are invited to float companies here.

5.2 Section 6 lays down the clauses a Memorandum of Association must contain. The name of the company must bear the word "limited" after its name so as to warn potential dealers with the company that the liability of the members of the company is limited. In modern days however very few people bother that the liability of the members is limited and banks have been known to be foolish enough to loan money to such companies without third party security only to rue the deed when the borrower fails to pay. Section 78 requires a company to publish its name in front of its office, on its seal and on its bills. Section 79 provides penalty for not doing so and any officer responsible for not including the name on its seal etc., will be personally liable for any debt contracted on those documents if the company does not meet its obligations. Memorandum of Association and Articles of Association of a company needs be signed by its promoter shareholders as a mandatory requirement of law.[1]

5.3 Section 6 further requires the Memorandum to mention the objects for which the company is formed. A company's activities are circumscribed by the objects clause and the company has no authority to act or contract beyond objects mentioned therein. The *ultra vires* doctrine was formulated by the House of Lords in the early case of *Ashbury Railway Carriage and Iron Co vs Riche*.[2] The Memorandum of Association of the company is its charter and defines the limitation of its powers.[3] Lord Selbourne gave the background of this doctrine by saying that a statutory corporation created by Act of Parliament for a particular purpose is limited as to all its powers by the purposes of its incorporation as defined by that Act. The memorandum of association is under this and earlier Companies Acts the fundamental and (except in certain specifies particulars) the unalterable law of companies incorporated by virtue of such Acts.[4]

5.4 **The Ultra Vire Doctrine** – The doctrine that any act not authorised by the memorandum is ultra vires is to be applied reasonably. Anything fairly incidental to the company's objects as defined is not to be held to be ultra vires.[5] The question is not, however, whether the act or business not expressly authorised by the memorandum can conveniently or advantageously be done or carried on in conjunction with acts or businesses which are so authorised, but whether it is reasonably incidental or accessory thereto. Thus it is ultra vires for a company formed to work tramways to carry on either the business of an omnibus company or a general parcels collection and delivery business, however conveniently or advantageously such business can be combined with the tramways business.[6] There are certain powers which are implied in the case of every company by reason of its being a corporation, e.g., a power to appoint and act by agents.[7] A trading company has also an implied power to borrow and give security for the purpose of its business.[8] A contract made by the directors upon a matter not authorised by the memorandum is ultra vires the company and therefore the directors. It is not binding on the company, and cannot

1 SSA Bangladesh Ltd and another vs Engineer Mahmudul Islam and o[illegible] 7 MLR (AD) 8

2 (1875) L.R. 7 H.L. 653

3 per Cairns L.C at page 668, ibid

4 ibid at page 692

5 A.G. vs. Great Eastern Rail Co [1879] 11 Ch.D. 449, 480; affirmed [1880] 5 App. Cas 473; London and North Western Rail Co vs. Price [1883] 11 Q.B.D. 485; Foster vs. London, Chatham and Dover Rail Co [1895] 1 Q.B. 711; A.G. vs. London County Council [1901] 1 Ch 781; on appeal [1902] A.C. 165; A.G. vs North Eastern R[illegible] Co [1906] 2 Ch 675; A.G.vs Liverpool Corpn [1922] 1 Ch 211;Deuchar vs Gas Light and Coke Co [1925] A.C. 691; Armour vs Liverpool Corpn. [1939] 1 All E.R. 363.

6 London County Council vs A.G.[19021 A.C. 165

7 Ferguson vs Wilson [1866] 2 Ch App 77, 89.

8 General Auction Estate and Monetary Co vs Smith [1891] 3 Ch 432.

be rendered binding even by the assent of every individual shareholder.[1] Not only the shareholders for the time being in the company, but also those who may become hereafter shareholders, and the outside public, and in particular those who are or may be the company's creditors are to be protected.[2] It is otherwise with acts which are within the memorandum but which are forbidden by or have not been done in manner directed by the articles.[3] The ultra vires doctrine was a pitfall for an outsider dealing in good faith with a company, whether as a creditor, a disponee of property or otherwise. It was inconvenient for companies seeking finance and wanting to do business.[4] This doctrine was not popular with the business world which with the aid of its advisers sought means of circumventing it. This was done by ensuring that the objects clauses of Memoranda of Association specified a profusion of all the objects and powers that the ingenuity of their advisers could dream up. The courts sought to narrow the scope of the resulting vires by distinguishing between 'objects' and 'powers' and applying the *ejusdem generis* rule of construction, ruling that the powers could be used only in relation to the objects. But that too was circumvented by the device of ending the "objects" clause by stating that each of the specified objects or powers should be treated as independent and in no way ancillary or subordinate one to another.

The House of Lords in *Cotman vs. Brougham*[5] felt reluctantly compelled to uphold the validity of such a provision, with the result that it was held to be intra vires for a rubber company to underwrite an issue of shares of an oil company by virtue of an independent general power to underwrite securities. The case of *Introductions Ltd. vs National Provincial Bank*[6] concerned a company with the object of providing foreign visitors with accommodation and entertainment but which later devoted itself to pig-breeding, an activity not contemplated by those who drafted its Memorandum, and granted its bank a debenture to secure the substantial overdraft which built up prior to its insolvent liquidation. It was held to have acted ultra vires so that the bank could not enforce the debenture or claim in the liquidation. It has now become a fashion to insert in the objects clause a power to carry on any other trade or business whatsoever, which can, in the opinion of the Board of Directors, be advantageously carried on by the company in connection with or as ancillary to any of the above businesses or the general business of the Company. The result of these devices is to destroy any value that the ultra vires doctrine might have had as a protection for members or creditors.

The doctrine however remains as a nuisance to the company. In *Parke vs. Daily News*[7] it was held that to use the proceeds of sale of the defunct NEWS CHRONICLE and STAR newspapers to compensate employees who lost their jobs was ultra vires since the company's business had ended. Under the rule of constructive notice, anyone dealing with a registered company will be deemed to have notice of its "public documents". In *Re Jon Beauforte (London) Ltd.*[8] where the insolvent company's stated objects were to manufacture dresses but it had for sometime instead been making veneered panels a combination of actual knowledge of the business being carried on by the company and of constructive notice of its stated objects resulted in most of its creditors' claims being ultra vires. Even the claim of the supplier of heating oil, who argued that this would have been needed whatever the company's business, was met by the answer that he had actual knowledge of the present nature of the business, since the fuel had been ordered on the company's notepaper which described it as "veneered panel manufacturers".

5.5 In the U.K. section 9(1) of the European Communities Act of 1972, later re enacted as section 35 of the Companies Act of 1985 attempted to dispose of all the problems by

1 Ashbury Railway Carriage and Iron Co vs Riche, supra 653.
2 Ashbury Railway Carriage and Iron Co. Case supra at p.667 .
3 Buckley on the Companies Acts 13th Ed p.24
4 Ford and Austin's Principles of Corporations Law 7th Ed. p.484.
5 [1918] A.C. 514
6 [1970] Ch 199, C.A.
7 [1962] Ch 927
8 [1953] Ch 131

providing that, in favour of a person dealing with a company in good faith, any transaction decided on by the directors should be deemed to be within the capacity of the company and free from any limitations under the memorandum and articles on the directors' powers and that the other party was not obliged to inquire about those matters. In Australia, the first major reforms of the ultra vires doctrine in its application to companies was made in the Uniform Companies Acts of 1961 and 1962. Section 21 provided that no act of a company was to be invalid by reason only that the company was without capacity to do the act. However if the company began to act beyond its capacity, a member or holder of debenture secured by floating charge, could seek an injunction to restrain the company from acting. Under amendments which operated from 1 January 1984 a company can decide whether it wants to state objects. For most companies there is no legal reason for doing so and an objects clause no longer goes to the root of corporate capacity.[1] In Bangladesh, however, the antiquated doctrine of ultra vires still applies and the draftsmen of memorandum of associations of companies make voluminous documents creating clauses and powers which only a very fond promoter would dream of regarding his company.

5.6. The Memorandum binds the company and its members to the same extent as if they had been signed and sealed by each member to observe all the provisions of the memorandum. (Section 22 of the Companies Act of 1994.) One consequence of this is that any member has a personal right to seek an injunction to prevent the commission of any act which is outside the objects clause, i. e., the investor is entitled to see that the objects for which he invested are adhered to.[2]

5.7 Section 11 provides for change of name of company. It was held by the Supreme Court of Pakistan sitting on an appeal from the judgment of the then High Court of East Pakistan that change of name of a company is possible only under section 11 of the Act after following the prescribed procedure for the purpose which requires such change to be made by a special resolution after obtaining the required approval. The change of name becomes complete under sub-section (5) (at present sub-section (7)) only after a certificate of incorporation in the altered name has been issued by the Registrar.[3] This case has been followed in a recent case where Mainur Reza Chowdhury J. refused to condone the delay in filing the return of allotment of shares on the ground that the company had not altered its name after the emergence of Bangladesh by substituting the word "Bangladesh" instead of "Pakistan" but continuing to carry on the business as a Bangladesh company and allotting shares as such. The Court seemed to have held that the identity of the Bangladesh Tank Terminal Ltd. was different from East Pakistan Tank Terminal Ltd. because the change of name was not done according to law although this obviously was not the case.[4]

5.8 Any change of the objects clause has to be sanctioned by the Court which will invariably give the creditors of the company a hearing on whether they want to oppose the amendment. This is a good chance for a creditor of a company who can prove his claim on documents or has a prima facie case to claim either that the company pay its debts or it give security therefore. The reason is that the sanctity of the objects clause is to be maintained for the security of the creditors. As to what entitles a particular company to be treated as a person interested in the assets of another company so as to receive notice when the other company applies for alteration of its memorandum of association.[5] The respondent company amended its objects and applied to the High Court for confirmation of the amendment. The appellant company opposed the amendments contending that it was an organisation entitled to become the beneficiary of the respondent company in the event of the latter not being recognised by

1 Ford and Austin's Principles of Corporations Law, 7th Ed. p.486
2 Parke vs Daily News, supra.
3 M/S M.M. Ispahani Ltd vs S.A.Rahman and Co 20 DLR (S.C.) 173.
4 In re Bangladesh Tank Terminals Ltd. Company Matter 30 of 1995 decided on 24 August 1995.
5 Chittagong Chamber of Commerce and Industry Chittagong vs. C.S. Ltd. 22 DLR (S.C.) 231.

the Government under the Trade Organisations Ordinance 1961 and as such entitled to notice under section 12. Clause (7) of the memorandum of association of the respondent company provided that upon winding up of the Association there remained property, the same should be given to other institutions having similar objects to be determined by the members of the Association. It was held, that the property of the respondent Association would not devolve automatically upon the appellant in case of winding up or dissolution of the respondent Association but only if it is so decided by the members of the Association. The appellant therefore had no present right to get the property of the Association and therefore could not oppose any alteration of the memorandum of association. Only if the appellant had an existing right which was sought to be taken away by the special resolution then it could resist the confirmation of the resolution.[1]

5.9 **Filing at the Registrar's Office** – The altered memorandum of association approved by the High Court is to be filed with the Registrar of Joint Stock Companies within the time mentioned in section 15. Extension of time for filing such application may be granted under section 15 by the Court or after its expiry by the Court under section 16 if an application is made within 30 days of the expiry of the time for filing the documents. When none of this has been done any alteration of the Memorandum of Association approved by the High Court becomes void.[2]

Articles of Association

6.1 The permanence of the general constitution of the company is secured by the memorandum which the articles cannot, save as provided by the Act, modify or alter. Neither can the articles authorise the company to do anything which is expressly or impliedly forbidden by the Act e.g., to pay dividends out of the capital, nor take away from the company or its members any rights conferred by the Act, e.g., the right of a member to petition to wind up the company.[3] Subject to these limitations the articles may contain such regulations for the management of the company as the original incorporators think fit.[4] The Articles constitute a network of rules regulating the affairs of the company. Each article is a rule for the regulation of the relations between the company and its shareholders and relations between the shareholders and the management. The Articles may explain the memorandum in case of ambiguity.[5]

6.2 In construing any article all relevant articles may be taken into account and if the words used are ambiguous attempt should be made to reconcile them and adopt such construction of the words as would avoid conflict between them. This principle of construction does not apply where the words are clear and unambiguous.[6] The Articles of Association of a company should be regarded as a business document and should be construed so as to give them reasonable business efficacy where a construction tending to that result is admissible on the language of the articles in preference to a result which would or might prove unworkable.[7] In *Fertilizers Corporation of India vs Their Workmen*[8] the Indian Supreme Court held that where the articles of association gave powers to the President of India to give directions regarding the working of the company, the exercise of the powers of the board of directors was, apart from other restrictions, subject to the directions issued by the President from time to time.

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1 ibid at p.234.
2 In the matter of Union Bank Ltd 21 DLR (Dac) 135.
3 Re Peveril Gold Mines[1898]1Ch 122
4 Buckley on the Companies Acts 13th Ed p.35.
5 London Financial Association vs Kelk (1884) 26 Ch.D. 107; Angostura Bitters Ltd vs Kerr [1933] A.C. 550.
6 Shiv Omkar Maheswari vs Bansidhar Jagannath AIR 1956 Bom 459.
7 per Jenkins L.J. in Holmes vs Keyes [1958] 2 All E.R. 129.
8 AIR 1970 S.C. 867 at 873

6.3 While drafting the Articles, the draftsman will require not only to know the nominal capital and the denomination of the shares but whether the shares are of one class and if not what special rights are to be attached to each class. The capital of a public company will have to be not less than the authorised minimum. The draftsman will have to take care in the matters that deviate from the Schedule 1 Regulations. The most likely matters are quorums, and the minimum and maximum number of directors. The main question for consideration is the extent to which Schedule 1 Regulations are to be adopted. When the incorporation is a private company what may be wanted is an absolute discretion to reject transfers and probably, provisions requiring the shares to be offered to the existing shareholders if a member wishes to sell. A common formula is to adopt a formula as "Table A (in the present Act Schedule 1) shall apply except in so far as it is varied by or inconsistent with the following provisions" – a formula which may lead to trouble if the draftsman is not careful while giving the variations from the statutory but optional regulations.

6.4 Section 17 states that a company limited by shares need not have any article and in any case shall be deemed to contain certain regulations identical with a number of Schedule 1 regulations. While enumerating these compulsory articles the draftsman has committed a serious error. He has obviously taken the number of compulsory articles from the previous Act of 1913 but forgot that the serial number of the Schedule 1 regulations vary from the Table A articles in the previous Act by one number. The articles cited in section 17(2) of the present Act should have been one number less. Perhaps this mistake will be noticed and corrected in the next amendment to company law.

6.5 The Articles of Association must be printed, set down chronologically in paragraphs and must be signed by the subscribers with the signatures of two witnesses. These may be filed at the office of the Registrar of Joint Stock Companies with certain forms filled up. Forms 1, 6, 9, 10 and 12 obtained from the Registrar's office in the case of a private company and in the case of a public company another two forms i.e., 11 and 14 must also be filled up. In other countries it is possible to form what is known as "shelf companies ", i.e., dummy companies so that promoters may readily buy these companies without waiting for the time consuming stage of registration formalities but in our country the Registrar's office insists on documents to prove that the registered office of the company is situate in a place where the directors have a title either by ownership or as tenant. This almost makes it impossible to form "shelf companies", a practice which hampers free trading in the long run. If in other countries one need not file proof of ownership of the registered address of the company why should we need these when the Companies Act does not need the promoters to file these at the time of registration ? Dummy companies are not necessarily illegal and a person may form many such companies but the over zealous authorities at the Registrar's office insist that these are not permissible.

6.6 It is not permissible however to register companies with illegal objects. In *R. vs Registrar of Companies ex.p. H.M.'s Attorney General*[1] where a prostitute had succeeded in incorporating her business under the name of "Lindi St. Claire (Personal Services) Ltd," the Registrar having rejected her first preference of "Prostitutes Ltd." or "Hookers Ltd." and shown no enthusiasm for "Lindi St Claire (French Lessons) Ltd." and with great clarity, specified its primary object as to carry on the business of prostitution, the Court on judicial review at the instance of the Attorney General, quashed the registration as contrary to public policy.[2]

6.7 Sections 22-27 of the Companies Act of 1994 deals with the effect of Memorandum and Articles of Association etc. Section 22 corresponds to section 21 of the previous Act and

1 [1991] BCLC 476.

2 Gower's Principles of Modern Company Law 6th Ed p. 112.

section 14 of the English Companies Act. The memorandum and articles constitute a contract between the company and each member. This fact has given rise to a large number of conflicting decisions which were reviewed by Ashubury J. in *Hickman vs. Kent or Romney Marsh Sheep-Breeders Association.*[1] The articles provided for the reference of differences between the company and any of its members to arbitration. H, a shareholder, brought an action against the company in connection with a dispute as to his expulsion from the company, i.e., a dispute between the company and him in his capacity as a member. Held, the company was entitled to have the action stayed, as the articles constituted a contract between the company and its members in respect of their ordinary rights as members. There was an observation however that "an outsider to whom rights purport to be given by the articles in his capacity as such outsider, whether he is, or subsequently becomes a member, cannot sue on those articles, treating them as contract between himself and the company, to enforce those rights ".[2]

But in the case of *Beatty vs Beatty Ltd.*[3] where there was a similar provision, the Court of Appeal, relying on the dictum in Hickman case, held that a dispute between a company and a director who was a member was not subject to the provision because the dispute was admittedly in relation to the director qua director. In the later case of *Rayfield vs Hands,*[4] the articles of a private company provided that a member intending to transfer his shares should give notice to the directors "who will take the said shares equally between them at a fair value." A member gave notice but the directors refused to buy. Vaisey J. felt able to hold that the provision was concerned with the relationship between the members and the directors as members and ordered them to buy.

6.8 Section 22 may provide an exception to the *Rule in Foss vs Harbottle.*[5] This Rule means that if the irregularity complained of is a wrong done to the company, the company acting, through its directors, is the proper plaintiff and an individual member may only file a "derivative" action suing on behalf of himself and the other members and joining the company as a defendant. None of this applies, however, if his personal rights have been infringed. In an article[6] Lord Wedderburn pointed out that in the case of *Quin & Axtens Ltd. v Salmon*[7] the House of Lords allowed a managing director, suing as a member, to obtain an injunction restraining the company from completing transactions entered into in breach of the company's articles which required consent of two managing directors for such transactions. This, in effect showed that a member had a personal right to require the company to act in accordance with its articles, which right could be enforced by the member even though the result was indirectly to protect a right which he had in another capacity. This decision seems to run contrary to an earlier decision where the articles provided that E. should be the solicitor to the company. Subsequently the company ceased to employ him. Held, E. was not entitled to damages for breach of contract against the company.[8] It is submitted that the view expressed in *Beatty vs. Beatty*[9] is to be preferred and the purpose of the article is to define the rights of a member as a member and that the articles do not constitute a contract between the company and a member in respect of rights and liabilities which he has in a capacity other than that of a member. But where such rights and liabilities are the subject of a written agreement, the articles will not be imported unless they are referred to.[10] Mr. Justice A. B. M. Khairul Haque observed in Dr. Manjurul Islam vs Al Rajhi Hospital that the articles of association will be applicable unless it is inconsistent with any of the provisions of the Act.[11]

1 [1915]1 Ch 881
2 ibid at p.897.
3 [1938] Ch.738.
4 [1960] Ch.1
5 (1843) 2 Hare 461.
6 Shareholders Rights and the Rule in Foss vs Harbottle (1957) Camb. L.J.193
7 (1909) AC 442 HL.
8 Eley vs Positive Life Assurance Co Ltd. (1876) 1 Ex. D. 88(C.A.)
9 supra.
10 Halsbury's Laws of England 4th Ed. para 118.
11. 1 Law Guardian (HCD) 46.

6.9 Section 23 mentions the documents to be filed with the Registrar. As stated above, Forms 1, 6, 9, 10, 12 in the case of private companies and Forms 1, 6, 9, 10, 11, 12 and 14 in the case of public companies need to be filed with the Registrar along with three copies of the memorandum and the articles. The Registrar's office inspects these and are generally quick in granting certificates after its objections are met. Recently the office insists on the father's name of the promoters to be mentioned in the memorandum of association on the reasoning that people cannot be identified otherwise, a requirement which is unknown in the Companies Act 1994 or in any other country, causing some eyebrows to be raised when foreigners are involved. The days when people used to give their address coming from villages are no longer there as company promoters have specified address but the promoters do not want to waste time arguing over the names of the fathers and inevitably give the names of their fathers, the foreigners accepting this as a third world whim. Similarly, the filing of proof that the proposed address of the company belongs to any of the promoters either by ownership or tenancy defies understanding. When queried, the Registrar's office says that this is required so that spurious companies are not formed for the purpose of raising loans from the banks. The over enthusiasm to control bank loans disbursed by some unfortunate banks, the Registrar's office thinks, is their domain. Again no body argues for fear of being held up or rejected and thus suffering hardship for fighting on principle. In such a case a writ would lie by an aggrieved person to remedy the Registrar's lapses.[1]

6.10 Once the fees are paid and objections to the drafts are met, the company is registered and a certificate of incorporation is issued and the subscribers to the memorandum form an incorporated body capable of performing all its functions. They are also saddled with the liability to contribute to the assets of the company in case it is wound up according to the Act. To give a sense of finality to the incorporation section 25 provides that the certificate of incorporation shall be conclusive evidence that all the requirements of the Act in respect of registration and of matters precedent and incidental thereto have been complied with.

6.11 The Memorandum and Articles of Association form the constitution of the company and section 26 prescribes that every member of the company is entitled to a copy of these documents on payment of a small fee. So that a member is not misled, the law further requires that any alteration of the memorandum and articles of association should be incorporated in those documents. The High Court Division has held that there is no provision in the Companies Act to correct clerical errors in the memorandum or articles of association and these may be amended by altering with Court's approval where needed.[2]

6.12 **Consequences of Incorporation** – An incorporated company has an artificial personality distinct from its members. Corporate personality became an attribute of the normal joint stock company at a comparatively late stage and it was not until the celebrated case of *Salomon vs. Salomon and Co*[3] that its implications were fully grasped. The facts are given below.

6.13 Aron Salomon, an established leather merchant and boot manufacturer, together with six other persons (wife and five children) registered a limited company. They were the only shareholders. Salomon sold his business to the company for 'a sum which represented the sanguine expectations of a fond owner rather than anything that can be called a businesslike or reasonable estimate of value'. The price was satisfied partly by debentures conferring a charge over all the company's assets, partly in fully paid shares and partly by cash. The result was that Salomon held 20,001 of the 20,007 shares issued and each of the remaining shares were held by a member of his family. The company failed with debts owing to outsiders. In the winding up of the company its assets were insufficient to meet both the secured debt and

1 Md. Idrish vs. East Pakistan Timber Merchants Group, Registrar 20 DLR (S.C.) 354.
2 Tropical Homes Ltd. vs Registrar 48 (1996) DLR 76.
3 [1897] A. C. 622

the unsecured creditors in full. The liquidator tried to have the secured debt postponed to the claims of unsecured creditors. Vaughan Williams J. at the first instance held for the liquidator holding that the company was the agent of Salomon who was bound to indemnify the agent who had a lien on the principal's assets. On appeal this argument was discarded because the property had in fact been sold to the company but the Court of Appeal held that the company was acting as a trustee for Salomon and that the Companies Act did not allow a sole trader to get limited liability by forming a company in which such shares as were not held by him were held by nominees on trust for him.

However, on further appeal the House of Lords unanimously held against the liquidator. It held that the company had conducted the business in its own right for itself beneficially and neither as agent nor as trustee; it was not just an alias for Salomon. The seven persons required for the formation of a company did not have to be independent of each other. Salomon was not liable to indemnify the company. Hence the debt for which security had been given to Salomon could rank before unsecured debts in the distribution of the company's assets. Lord Halsbury argued thus :

> Either the limited company was a legal entity or not. If it was, the business belonged to it and not to Mr. Salomon. If it was not, there was no person and no thing to be an agent at all; and it is impossible to say at the same time that there is a company and there is not.

Lord Macnaghten supported this by saying :

> The company is at law a different person altogether from the subscribers....and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits. The company is not in law the agent of the subscribers or trustee for them. Nor are the subscribers, as members, liable in any shape or form, except to the extent and in the manner provided by the Act.

6.14 The far sightedness of the English House of Lords in holding that a group of persons could form a company and do business behind its facade with limited liability without being termed its agent opened a new vista in the commercial world and enabled the small investor with small savings to put their mite in a joint pool so that a vast capital could be formed to undertake business at a far greater level than would if the investors were threatened by the possibility that they might be equated with the company and be held for its dues. Of course this decision also held that it was possible for a trader not merely to limit his liability to the money which he put into the enterprise but even to avoid any serious risk to the major part of it by subscribing for debentures rather than shares. Although a search at the Registrar's office would reveal the company's accounts and any charge on its property, quite often the records at the Registrar are backdated as not all charges are entered on the charge register immediately nor do many investors have the time and knowledge needed to search the file. Although inroads have been made into the doctrine, the Courts have, on the whole affirmed it. In *Lee vs. Lee's Air Farming Ltd*[1]. Mr. Lee beneficially owned all the shares in and was the sole "governing Director". He was also the chief pilot. The Privy Council, reversing the decision of the Court of Appeal of New Zealand, held that his widow was entitled to compensation under the Workmen's Compensation Act when he died in an accident although he was both the master and the servant.

6.15 **Advantages and Disadvantages of Incorporation:** Since the Salomon case, the complete separation of the company and its members has never been doubted. There are cases where the legislature, to a small extent, and the Courts have lifted the veil of incorporation but the general rule prevails that a company is a legal entity distinct from its members. It may have some unfortunate consequences e.g., if a trader transfers his business to a company owned by him he will cease to have interest in the property of the company and if he has forgotten to assign the insurance policy the company remains without any insurance.[2] Similarly the parent company may not have any insurable interest in the properties of its subsidiaries. If the company is limited by shares the liability of the members

1 [1961] A.C. 12, P.C.

2 Macura v Northern Assurance Co. [1985] AC 619.

are limited to the unpaid nominal value of their shares and in practice their shares are likely to be fully paid up so that they will be under no further liability. Herein lies the greatest advantage of a limited liability company over that of a partnership whose partners are liable for the entire debts of the partnership.

A limited liability company can sue and be sued in its name, and has perpetual succession. Its shares can be made transferable without disturbing its personality, something which may be difficult in the case of a proprietorship or a partnership. There is this fundamental difference: in a partnership transferability depends on express agreement and is subject to legal and practical limitations, whereas in a company it exists to the fullest extent in the absence of express restriction. The partnership relationship is essentially personal; and in practice this is maintained in the case of a private company which in economic reality is often a partnership though in law an incorporated company. In recent years the courts have shown a welcome tendency to recognise the economic reality in applying the legal rules to such incorporated partnerships.[1] On the other hand, the relationship between members of a public company is essentially impersonal and financial and hence there is usually no reason to restrict changes in membership.

Another advantage which the incorporated company has over unincorporated partnerships is that of borrowing. Though in theory, a sole trader should have more credit-worthiness yet in practice the ingenuity of the equity lawyers has innovated a system known as floating charge which allows the company to create a charge on its present and future properties and enable it to transfer its assets freely and thus raise capital with relative ease. The incorporated company also has a different tax base which is a flat rate whereas an individual has a different rate. The company's profits may be reduced by paying the salaries of the directors and buying cars etc. in the name of the company. These advantages are to some extent offset by the formalities and expenses needed to form an incorporated company and the requirement to have its accounts audited as per the company law at some expense and the botherations of holding meetings and filing returns at the office of the Registrar of Joint Stock companies.

6.16 The Salomon case was followed in the U.K. in numerous cases and one of the latest of these is the case of *J.H. Rayner (Mincing Lane) Ltd. vs. Department of Trade and Industry.*[2] The case arose out of the collapse of the International Tin Council in 1985 which left it owing millions of pounds to a number of metal traders and banks. The Council had been formed by several states and the Council's creditors sought to recover its debts from those member states. The House of Lords first decided that the Council was a corporate body with its own separate legal personality distinct from its members and held that only the Council and not its members could be liable for the debts. The creditors were left to the repeated exhortations in the various judgments to the member Governments to meet their moral obligations. In the later case of *Arab Monetary Fund vs. Hashim*[3] the House of Lords held that the Arab Monetary Fund had been established by an agreement between some twenty Arab states which agreement provided that the Fund should have "independent" juridical personality – and in particular the right to own, contract and litigate – and which required the member states to ratify it. This the United Arab Emirates did and this had the effect of creating the Fund as a body corporate and accordingly it could sue in the English courts.

6.17 The Indian Supreme Court has observed in *Bacha F. Guzdar vs. CIT*[4] that a shareholder has got no interest in the property of the company though he has undoubtedly a right to participate in the profits if and when the company decide to divide them...the company is a juristic person and is distinct from the shareholders. The dividend is a share in the profits declared by the company as liable to be distributed among the shareholders. There is nothing in the Indian law to warrant the assumption that a shareholder who buys shares,

1 Ebrahimi vs Westbourne Galleries Ltd. (1973) A.C. 360 H.L.
2 [1989] 3 WLR 969.
3 [1991] 2 A. C. 114
4 AIR 1955 SC 74

buys any interest in the property of the company which is juristic person entirely distinct from the shareholders. A member of a company has no locus standi to challenge any decree passed against the company unless his rights as such shareholder are affected.[1] A company is distinct from its board of directors. They cannot enforce a right in their individual capacity which belongs to the company.[2]

The Supreme Court of Bangladesh (Appellate Division) has observed in *Punjab Ali vs Mokarram Hossain*[3] that a company is entirely different from its members whose interests are confined to their shares. A company is an artificial person and must act through some natural agent. The Board of Directors are created for the management of the company. An individual shareholder has no proprietory interest in the property of the company's property and his interest in the shareholding is not directly affected by the sale of the property of the company and cannot bring an action for setting aside a sale under Order 21 rule 90 C.P.C. Our Appellate Division has held in the case of *A.S.A. Nur vs. Registrar, Joint Stock Companies*[4] that a company continues to have its separate existence even when the number of members of the company is reduced below the legal minimum. Citing English decisions, B.H. Chowdhury J. held that Jamuna Oil Company Ltd. whose shares were held by Petro Bangla and A.S.A. Nur must hold general meetings as required by law although it was a wholly owned subsidiary of Petro Bangla.

7.1 **Lifting the Veil of Incorporation :** Although the Salomon case laid down a salutory principle that a separate legal entity may be formed with one man being in sole control of the company yet it was criticised as opening the way for fraud etc. The Courts have since then shown a readiness to have a crack at the corporate shell without the aid of a legislative sledgehammer. In the cases where the veil is lifted, the law either goes behind the corporate personality to the individual members, or ignores the separate personality of each company in favour of the economic entity constituted by a group of associated companies. There is a greater willingness to lift the veil in the case of associated companies and look into the economic reality. One must remember however that the legislature has always required that a corporate personality should reveal its affairs to the public gaze and that these should be accompanied by wide publicity. A third party may know who a company's members are, what shares they hold and what is its constitution as well as what its capital is and how it has been obtained. They also have access to a company's accounts at the office of the Registrar. However, a third party will have no right to resort to against its members. Both the legislature and the courts have lifted the veil of incorporation and we discuss this below.

7.2 **Statutory Exceptions :** Section 222 of the current Act provides that if at any time the number of members falls below the prescribed minimum and the company carries on the business with that reduced shareholding for more than six months then the remaining members who know that this is the state of affairs , will be personally liable for all the debts the company contracts after the said period of six months. In other words, the members are personally liable for the debts of the company .The company remains a legal entity even though there is one member only.[5] The liability attaches only to a member and not to a director unless he is also a member.

Section 78 of the Act of 1994 requires a company to display in front of its office its name and registered address and also show its name on its seal, bill heads, notice and advertisements etc. Section 79 provides that if a company which defaults in complying with the provisions of section 78 then every officer who has knowingly and willingly approved of the default will be liable to penalty and personally responsible for any debt of the company contracted on the bill heads etc.

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1 Vivek Kumar vs. Pearl Cycle Industries Ltd (1983) 54 Company Case. 77 (Del).
2 Tata etc. Co Ltd. vs. State of Bihar AIR 1965 S.C. 40.
3 29 DLR(S.C.)185
4 (1981) BLD(AD) 202.
5 A.S.A. Nur vs. Registrar supra .

Section 75 of the Act provides that in a limited company the liability of the directors or of any director may, if so provided by the memorandum be unlimited. If a director holds any office then his liability may also be unlimited as an officer of the company if he is a director whose liability is unlimited Even if the memorandum does not provide for the liability of a director to be unlimited, a limited company if so authorised by its articles may , by special resolution, alter its memorandum so as to render unlimited the liability of its directors.

Section 186 of the Act requires a holding company to attach with its balance sheet the auditors report, profit and loss account and certain other informations of its subsidiaries. The statute thus seeks to publish a broad picture of the entire group and ignore the separate legal entity of the subsidiaries.

7.3 **Lifting the Veil under Case Law** – Ever since the Salomon case held that a "one man company" is possible to exist without being a mere alias of, or agent for , the principal shareholder, attempts have been made in various cases to make inroads into the doctrine.

The Courts have been inclined to observe that the judicial power will be exercised to pierce the corporate veil if it is necessary to achieve justice irrespective of the legal efficacy of the corporate structure.[1] However the English Court of Appeal in the case of *Adams vs. Cape Industries plc.*[2] gave a classic judgment and examined the issue exhaustively ; several arguments were raised and discussed.

The facts concerned the recognition and enforceability of judgments obtained in the United States in England. This depended on whether the company had established and maintained at its own expense a fixed place of business there for more than a minimal time or whether its representative had for more than a minimal time been carrying on its business there. The plaintiff raised three arguments:

i) the single "economic unit argument ";
ii) the corporate veil is a mere facade;
iii) the agency argument.

7.4 **The "Single Economic Unit" Argument** – The courts sometimes ignore the distinction between different companies in the same group. In the *Roberta*[3] a subsidiary company had signed the bills of lading but the parent company conceded that it was responsible for the bills. The parent company had owned all the shares and supplied two out of three directors and was a separate company in name only and probably for the purpose of taxation. In *Holdsworth and Co vs. Caddies,*[4] Caddies had been appointed the managing director of the parent company but was assigned to look after the affairs of a subsidiary company. He argued that the parent and subsidiaries were different legal entities under the control of their own board of directors. This argument was rejected as being too technical and should be construed in the light of the facts and realities of the situation. However, our Appellate Division has held that permanent transfer of an employee of Petro Bangla to one of its subsidiary companies is illegal as the service rules required consent of the employee who would have lost his status as a Corporation officer and become employee of a registered company.[5] In *Scottish Co-operative Wholesale Society Ltd. vs. Meyer*[6] it was complained that oppression of minority shareholders was done not by the parent company but by the subsidiary company which the parent company had formed. The House of Lords rejected this difference between the parent and subsidiary company because "every step taken by the subsidiary was determined by the parent company " and that the Courts should look into the business realities of the situation.

1 Re A Company (1985) cited in Gower's Principles of Modern Company Law 5th Ed p.125 .
2 [1990]Ch.433 and [1990] 2 WLR 657 (H.L.); [1991] 1 AllER 929
3 (1937) 58 LI.L.R.159
4 [1955] 1 WLR 352,H.L.
5 Chairman Petro Bangla & ors vs A.K.M. Fazlul Karim (1995) BLD (AD) 114.
6 [1959]A.C.324

In *Amalgamated Investment and Property Co vs. Texas Commercial Bank*[1] a guarantee of repayment of loans made by a bank was interpreted as covering those made by a wholly owned subsidiary set up by the bank as its channel for making the loans. The English Court of Appeal , in the case of *D.H.N. Food Distributors Ltd. vs. Tower Hamlets L.B.C,*[2] was concerned with compensation to be paid to the parent company when land belonging to a subsidiary was compulsorily acquired. Lord Denning, M.R. considered the economic entity of the group by saying that the group was virtually the same as a partnership in which all the three companies were partners and should not be treated separately so as to be defeated on a technical point and deprived of the compensation which should justly be payable.(at page 860). The Court of Appeal in the *Cape case,*[3] regarded the judgment in the D.H.N. case as decisions on the relevant provisions for compensation. In Revlon Inc. vs. Cripp and Lee Ltd.[4] the question arose as to whether goods were "connected in the course of trade with the proprietor of the trade mark" within the meaning of the Trade mark Act. The proprietor of the trade mark was not Revlon Inc(Revlon) but Revlon Suisse S.A.(Suisse). In holding that the goods traded by Revlon were connected with Suisse, Buckley J. said that" since...all the relevant companies are wholly owned subsidiaries of Revlon, it is undoubted that the mark is, albeit remotely, an asset of Revlon and its exploitation is for the ultimate benefit of no one but Revlon...."[5]

7.5 **The Corporate Veil Point** – The English Court of Appeal accepted in the *Cape case*[6] that quite apart from the cases where statute or contract permits a broad interpretation to be given to references to members of a group of companies there is one well recognised exception to the rule prohibiting the piercing of the "corporate veil." Such piercing of the corporate veil is done when the corporate structure is a "mere facade concealing the true facts" and have been variously described as a 'device', 'sham', 'creature', 'stratagem' etc. In *Jones vs. Lipman,*[7] a vendor of land wanted to avoid a contract to sell land , formed a company and conveyed the land to it. Russell J. made an order for specific performance against both the vendor and the company . The case shows that where a facade is alleged the motives of the architect of the facade may be relevant. In the *Cape case*[8] the Court held that one of Cape's wholly owned subsidiaries incorporated in Liechtenstein was a facade in the relevant sense. The reason seemed to be not only that it was a wholly owned subsidiary of Cape but also because its corporate name was used by Cape or its subsidiaries on invoices. On facts it was held however that this particular subsidiary did not do any business in the United States. What mattered in relation to establishing that Cape was present in the United States was whether another company, C.P.C. incorporated and carrying on business in the United States, was a facade. Although Cape probably paid for the expenses of C. P. C. at the time of its incorporation and was a party to the same arrangement as the other subsidiary, that did not in itself make it a mere facade. The Court was satisfied that it was an independent corporation and declared that

> as a matter of law the Court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group, merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law .[9]

1 [1982] Q.B. 84
2 [1976]1 WLR 852
3 ibid at page 536.
4 [1980] FSR 85 Cited in Gower's Principles of Modern Company Law.
5 Gower's Principles of Modern company Law 5th Ed p.128.
6 ibid at p.539
7 [1962] 1 W.L.R. 832
8 ibid.
9 ibid at P.544.

The English Courts therefore recognised that a corporate structure could be built on a pyramid scale but also cautioned that the Courts may lift the corporate veil. In this case the Salomon principle was applied and Cape was found not to be carrying on business in the United States.

In has been held by our High Court Division that a shareholder of the company holding shares in B Company has no locuastandi to petition for winding up of B company because he cannot derive advantage or disadvantage.[1] A division bench of the High Court Division agreed to lift the veil of incorporation to hold that BRAC a society registered under the Societies Registration Act could not hold controlling shares in a Bank and the entities of the two – Shareholder and the company – would be treated as one.[2]

7.6 **The Agency Principle** : A company having power to act as an agent may do so as agent for its parent company and the parent company will be bound by the activities of its agent. However, the agency may be difficult to establish as illustrated in the *Cape case*[3] A company registered in England is an alien company if its agents or the persons in de facto control of its affairs are alien enemies, and in determining whether alien enemies have such control, the number of alien enemy shareholders and the value of their holdings are material.[4] In *Smith, Stone & Knight Ltd. vs. Birmingham Corporation*[5] a subsidiary company which was carrying on the business of the parent company was held to be the agent of the parent company. The Court laid down a few principles to determine such agency but these principles do not seem to be followed in the subsequent English decisions. Conversely, in *Cory(Wm) & Son Ltd. vs. Dorman Long and Co Ltd.*[6] the parent company was held to be the agent of the subsidiary. This principle was followed in the *D.H.N. Food case*[7] but was doubted by the House of Lords in *Woolfson vs. Strathclyde Regional Council*[8] which wondered whether it was a correct application of the general principle that the veil should only be pierced where special circumstances existed indicating that it was a mere facade concealing the true facts. This approach has been applied in *National Dock Labour Board vs. Pin and Wheeler Ltd* (1989) and the *Cape Case* (1990).[9]

7.7 **Fraud** : Lord Denning M.R. was prepared to lift the veil in *Wallersteiner vs. Moir*[10] where the company of which the plaintiff was a director made a loan to another company which was his puppet so that the loan should be treated as made to him. In *Gilford Motor Co Ltd. vs. Horne*[11] the Court did not allow a company to be used as a device to mask the carrying on of a business by a former employee of another person and to enable the former employee to break a valid covenant in restraint of trade contained in the contract under which he was formerly employed. In that case the employee covenanted that after the termination of the employment he would not solicit his employer's customers. Soon after the termination of his employment he formed a company of which the two directors and shareholders were his wife and another person and which sent out circulars to customers of his former employer.

1 Mazharul Hoque vs Bulk Management (BD) Ltd. and another (1996) BLD (H.C.) 575, 48 DLR (1996) HC 453.
2 Prof. Muzaffar Ahmed vs. Bangladesh Bank and others 20 BLD (HC) 235 ; the case is under appeal before the Appellate Division.
3 supra.
4 Daimler Co Ltd. vs. Continental Tyre etc Ltd [1916] 2 A.C. 307.
5 [1939] 4 All.E.R. 116.
6 [1936] 2 All E.R. 386.
7 supra
8 [1978] S.L.T. 159 H.L.
9 Charlesworth and Morse: Company Law 14th Ed.p.31.
10 [1974] 1 W.L.R. 991.
11 [1933] Ch.935.

An injunction was granted. The case of *Jones vs. Lipman*[1] referred to above was a similar case where the Court lifted the veil of incorporation to avoid the perpetration of a fraud.

7.8 Where the subsidiary, being under capitalised, is operating only some portions of the business of the holding company there is no reason why it is not to be treated, so far as the liabilities incurred by it are concerned, as an agent of the parent company. The American Courts are more liberal in lifting the veil of incorporation and follow the famous observation of Sanborn J. of the Supreme Court of the U.S.A. in *United States vs Milwaukee Refrigerator Transit Co*[2]: "Where the notion of legal entity is used to defeat public convenience, justify wrong , protect fraud or defend crime, the law will disregard the corporate entity and treat it as an association of persons."

The Supreme Court of India, in *Workmen of Associated Rubber Industry Ltd. vs Associated Rubber Industry Ltd.*[3] lifted the veil of incorporation when a parent company promoted a subsidiary company and transferred to it some of its investments for the purpose of splitting the profits and reduce the amount of bonus to be paid. C. Reddy J. held that the avoidance of welfare legislation was as common as avoidance of taxation and the approach to the problems should be similar. The facts revealed that the new company did not have any asset other than the money transferred by the parent company and no business or income of its own.

7.9 **Conclusiveness of the Certificate of Incorporation** – Section 25 provides that a certificate of incorporation given by the Registrar in respect of any association shall be conclusive evidence that all the requirements of the Act in respect of registration and of matters precedent and incidental thereto have been complied with. This does not mean that all the objects of the company, as set out in the memorandum are legal. If a company with illegal objects happens to be registered the company may be forbidden to carry on its business in furtherance of its illegal objects.[4]

7.10 The Supreme Court of Pakistan in an appeal from the then East Pakistan has held that under section 24 (now section 25) of the Companies Act a certificate of incorporation granted by the Registrar is conclusive evidence of the fact that the requirements of the Act in respect of registration and matters precedent and incidental thereto have been complied with and that the association is company authorised to register under the Act. But this does not mean that even a certificate obtained fraudulently cannot be cancelled or set aside. The conclusiveness attaches only to a validly obtained certificate and not to any and every kind of certificate granted by the Registrar. In that suit a declaration was sought that the reconstitution of Messrs. A. Jabbar and Co. Ltd. and its change of name to Messrs. Chalna Fibre Co. Ltd. was illegal and inoperative. Held that there was no provision in the Companies Act whereby the reliefs could be claimed. Sections 10,11,12 and 20 of the Companies Act 1913 provided for changes in the name of the company, its memorandum and articles of association. If the procedure prescribed therein was not followed, the change could be challenged as being illegal, but there was no provision in the Companies Act for obtaining this relief. This relief could, therefore, be only obtained by way of suit.[5] The same Court held that when parties were challenging each other's rights in various litigations, the Registrar ought not to have taken any step in favour of either the one or the other group pending the decision of the disputes or done anything which might prejudice the claims of the rival parties in those

1 [1962] 1 WLR 832.

2 1905 142 Fed 247.

3 (1986) 59 Comp Case 134(SC)

4 Bowman vs. Secular Society[1917]A.C.406; see also Cotman vs. Brougham (1918)A.C.514;Performing Right Society Ltd. vs. London Theatre of Varieties [1922] 2 K.B. 433;Peel'sCase(1867)2 Ch.App.674;Official Receiver and Liquidator of Jubilee Cotton Mills Ltd. vs. Lewis[1924] A.C.958; and T.V. Krishna vs. Andhra Prabha Ltd. AIR 1960 A. P. 123

5 Chalna Fibre Co Ltd. vs. Abdul Jabbar 20 DLR(S.C.) 335.

litigations. If a certificate of incorporation is illegally granted it can always be challenged in an appropriate proceeding, in this case, a writ in the High court, as there was no remedy provided in the Companies Act for making the Registrar discharge his duties properly.[1]

7.11 **Associations not for Profit** – Section 28 provides that a company may be incorporated without the use of the word "limited" if it is incorporated to improve commerce, arts, science, religion, charity, or any other useful object and applies its income in promoting its objects and prohibits payment of dividend. A licence is required from the government for this purpose .

7.12 **Company Limited by Guarantee** – Section 29 permits a company to be incorporated with the liability of shareholders limited by guarantee. The feature that distinguishes a company limited by guarantee from a company limited by shares is that a member is not required to pay for any capital before the company commences to wind up. When a guarantee company is wound up without adequate funds to discharge its liabilities each person who is a member at the commencement of the winding up is primarily liable to pay an amount prescribed in the memorandum of association. If it appears to the Court that members are unable to meet the company's liabilities, persons who have been members within a year before the commencement of the winding up are liable to honour their guarantees. But those past members are liable to contribute only towards payment of the company's debts incurred before they cease to be members. The company is a limited company because a member's liability to contribute is limited to the amount of the guarantee.

Because members are not liable to pay any capital before the commencement of the winding up, any funds needed for the company's operations will have to be raised in some other way. For example, the initial capital required for such things as the purchase of the premises may be raised by loans from members and its current expenses can be met by subscriptions and fees. If it can give security it will be able to borrow from outsiders. The collapse in 1989 of the National Safety Council of Australia, Victoria Division showed that a non-commercial company was able to borrow on a scale equal to that of commercial companies. The amount of the guarantee is fixed at the time of the company's formation. There is no legal bar to a company limited by guarantee earning and distributing profits.[2] But because of its inflexible capital structure it is not usually suitable for trading activities. On occasion it has been used for trading purposes in tax minimisation schemes.[3]

1 Mohd. Idrish vs. E.P.Timber Merchants 20 DLR (S.C.) 355,363.
2 See Re NFU Development Trust Ltd. [1972] 1 WLR 1548.
3 e.g., FCT vs. Slater Holdings Ltd. [1984] 156 CLR 447;56 A.L.R. 306.

SHARES

8.1 Sections 30-76 of the Companies Act 1994 deal with shares, transfer of shares and rights of shareholders. Sections 152-156 deal with issue of shares at a discount, redeemable preference shares and issue of further shares.

8.1.1 A share is a movable property transferable as per provisions of the articles. There is no exhaustive definition of a share in the Act.[1] A share is the interest of a shareholder in the company measured by a sum of money, for the purpose of liability in the first place, and of interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders *inter se* in accordance with section 22.[2] A share is a type of contractual claim against a company. It is an example of intangible property called a ' chose in action' or 'thing in action'.[3] Professor R Pennington in (1989) 10 Company Lawyer 140 discusses the difficulty of defining shares and concludes that *they are a species of intangible movable property which comprise a collection of rights and obligations relating to an interest in a company of an economic and proprietory character, but not constituting a debt.*

A Legal Chose in Action. In English law there are two kinds of chose in action ; legal choses in action (being claims enforceable at common law) and equitable choses in action (being claims enforceable in equity). Because a share is a creature of statute, it is a legal rather than an equitable chose in action.[4] In that respect it differs from a share in a partnership, which is an equitable chose in action because, historically, the interest of a partner has been enforceable in equity and not at law.[5] A share in a company also differs from a share in a partnership in terms of transferability of membership. In companies listed on the Stock Exchange a share can be freely sold and transferred. In unlisted companies there can be restrictions on transfer. The transferee becomes a member of the company in substitution of the transferor. A person who buys the share of a partner, however, acquires an interest but does not become a partner; the vendor becomes a trustee for him of the interest agreed to be sold.[6]

A transfer of a share as a legal chose in action differs from transfer of a debt as a legal chose in action. A creditor can transfer the legal ownership of a debt by a two sided written assignment between a transferor and transferee with written notice to the debtor, but without needing his consent. Of course, the debtor cannot transfer the liability without the consent of the creditor. But to transfer the legal ownership of a share a change in the company's share register is needed. That means there is a three sided novation rather than a two sided assignment. Hence, liability attached to a partly paid up share can be transferred although the transferor can remain liable if the company commences to wind up within one year from the transfer.

1 See para 2.1.21 ante.
2 Farwell J. in Borland's Trustee vs. Steel [1901] 1 Ch. 279.
3 Archibald Howie Pty Ltd vs Commissioner of Stamp Duties [1948] 77 CLR 143 at 156.
4 Colonial Bank vs. Whinney (1886) 11 App. Cas 426.
5 Federal Commissioner of Taxation vs.Everett [1980] 143 CLR 440 at 447; 28 A.L.R. 179,182.
6 ibid at p.448 and p.183.

The rights making up a share are not separate pieces of property.[1] If a share had carried only financial rights it might have been considered divisible; but a share carries rights of membership and the whole scheme of the company law does not admit of membership referable to a fraction of a share. Hence, a company cannot allot fractional shares. Nor can a shareholder divide an allotted share so as to assign only some of the set of rights, such as the right to be paid dividends. If a member wishes to dispose of only part of the benefits of a share, that can be done behind the screen of a trust. The member could create a trust of the share so that the trustee would be bound to account to one beneficiary for, say, dividends only and to account to another beneficiary for other benefits.[2]

A share as an item of property differs from physical subjects of ownership such as land in that its characteristics are fixed, not by nature, but by whatever is put into the contract between company and shareholder. In a company, the rights attached to shares may be so framed that the shareholder is restricted (for example, as to transfer of the shares) and those restrictions will apply to anybody who becomes owner of the shares. In other words, in a share the restrictions can go to defining the property itself instead of being something external that is imposed in respect of a pre-existing item of property.[3]

8.1.2 **Share Capital** – The word "capital" used in connection with a company has several different meanings. It may mean the nominal or authorised share capital, the issued share capital, or the paid up share capital of the company.

The nominal or authorised capital is merely the amount of share capital which the company is authorised to issue. In the case of a limited company the amount of potential share capital with which it proposes to be registered, and the division thereof into shares of a fixed amount, must be set out in the memorandum of association.[4] This as well as the paid up amount may be increased or reduced.[5] The amount of the company's nominal capital depends on its business requirements , actual or potential. At the time of registration of the company the promoters will have to pay fees and stamp based on the amount of the nominal capital.

The issued or allotted capital is that part of the company's nominal capital which has been issued to the shareholders. The company is not bound to issue all its capital at once. Further issues of capital are made as they are needed. See section 155 of the Act.

The paid up capital is that part of the issued capital which has been paid up by the shareholders. The company may, for example, have a nominal capital of Tk 500,000 divided into 500,000 shares of Tk One each , of which Tk 400,000 is issued, i.e.,400,000 of the shares have been issued and only Tk 100,000 is paid up, i.e., the company has so far required only 25p. to be paid up on each share. The uncalled capital is the remainder of the issued capital and can be called up at any time by the company from the shareholders in accordance with the provisions of the articles. The paid up capital of the company includes the value of the shares paid up and any premium on such shares although the share premium will be shown as share Permian account in the balance sheet. The Securities and Exchange Commission has to be satisfied before shares can be issued at a premium as to the justification for it.

8.1.3 **Shares Issued at Discount etc.** – The issued share capital of a company is the fund to which creditors of the company can look for payment of their debts, and so, to protect the creditors , shares can be treated as paid up only to the extent of the amount actually received by the company. Section 152 and 153 of the Act impose restrictions on issue of shares and debentures at a commission or discount . A commission may be paid only if its payment and rate are approved by the articles and is mentioned in the prospectus where such a prospectus is issued and in a statement in lieu of prospectus where such a prospectus is not issued.

1 Re Alex Russell [1968] Victorian Reports 285 at 299.
2 Ford and Austin's Principles of Corporations Law 7th Ed.17.140.
3 *ibid.*
4 See Section 6 of the Companies Act.
5 See Sections 53 and 58 of the Act.

Shares may be issued at a discount if such issue is authorised by resolution of the company in general meeting and sanctioned by the Court. The resolution must specify the maximum rate of discount not exceeding ten percent at which shares are to be issued and not less than one year has elapsed since the date on which the company was entitled to commence business and the shares to be issued at discount are done so within six months after the date on which the company was entitled to commence business. Every prospectus and balance sheet issued after the share discount must contain particulars of the discount allowed on the issue of shares.

8.1.4 **Redeemable Preference Shares** – Redeemable Preference Shares can be issued if so authorised by the articles. Section 154 of the Companies Act however provides that no such share shall be redeemed except out of profits of the company which would be otherwise available for dividend or out of the proceeds of a fresh issue of shares made for the purposes of the redemption or out of sale proceeds of any of the profits of the company . No such share shall be redeemed unless they are fully paid up and where any such shares are redeemed otherwise than out of the proceeds of a fresh issue, there shall out of profits which would otherwise have been available for dividend, be transferred to a reserve fund to be called the capital reserve fund , a sum equal to the amount applied in redeeming the shares, and the provisions of the Act relating to the reduction of the share capital of a company shall apply as if the capital redemption reserve fund were paid up share capital of the company. Where any such shares are redeemed out of the fresh issue, the premium, if any, payable on redemption must have been provided for out of the profits of the company before the shares are redeemed. There shall be included in every balance sheet of a company which has issued redeemable preference shares a statement specifying what part of the issued capital of the company consists of such shares and the date when the shares are liable to be redeemed and where no such date is fixed the period of notice that is to be given for redemption.

8.1.5 **Further Issue** – Section 155 of the Act requires that where the directors decide to increase the capital of the company by the issue of further shares such shares shall be offered to the members in proportion to the existing shares held by each member irrespective of class. Such offer shall be made by notice specifying the number of shares to which the member is entitled and limiting the time, not less than fifteen days, within which the offer, if not accepted, will be deemed to be declined. After the expiration of such time or on receipt of an intimation from the member to which such notice is given that he declines to accept the shares offered, the directors may dispose of the same in such manner as they think most beneficial to the company. In the case of *Rowshan Ara Begum and others vs Doctor's Chemical Works Ltd. and others*[1] Mr. Justice M.M.Hoque relying on a decision of the Indian Supreme Court[2] held that this section was intended to cover a case where the directors decided to increase the capital by issuing further shares within the authorised limit. This power was not available to a general meeting of the company. On the exercise of powers by the directors bonafide, the Court also relied on the decisions of the Indian Courts[3] and observed thus :

> ...a power to issue shares in a limited company given to directors for the purpose of enabling them to raise capital when required for the purpose of the company is a fiduciary power to be exercised by them bona fide for the general advantage of the company, and when the company is in no need of further capital, directors are not entitled to use their power of issuing shares merely for the purpose of maintaining their control or the control of themselves and their friends, over the affairs of the company, or merely for the purpose of defeating the wishes of the existing majority of shareholders.[4]

1 44 DLR(1992) 371.
2 AIR 1950 S.C. 172.
3 AIR 1949 Bom. 56 and(1920) 1 Ch.D. 77.
4 ibid at p.378, also see the discussion on the fiduciary nature of directors

8.1.6 Where a company has paid any sums by way of commission in respect of any shares or debentures or allowed any sums by way of discount in respect of any debentures, the total amount so paid or allowed or so much of it as has not been written off , shall be stated in every balance sheet of the company as they think most beneficial to the company. See Section 156 of the Act.

8.2.1 **Preference Shares** – There is no comprehensive definition of a preference share in our Companies Act. Section 85 of the Indian Companies Act summarises the principles of preference shares enunciated in the western countries. Preference shares carry a preferred right to a certain minimum dividend in a year and the ordinary shares take the rest. The preference shareholder's prior right to dividend is expressed as a specified percentage of the par value of the shares or sometimes, the amount paid up on the share. There may, unusually, be provision for a supplementary dividend at a fixed rate if the rate of dividend on ordinary shares reaches a certain level. A share can still be called a preference share even if it gave no preference as to dividend but gave a preference in a winding up in the form of a right to be repaid capital in priority to holders of other classes of shares.[1] A narrower view is taken by Pennington[2] who sees the distinguishing feature as being entitlement to a dividend of a fixed amount, usually expressed as a percentage of the nominal or paid up value of the share, before any dividend is paid on the ordinary shares. This is similar to the view expressed earlier by Lopes L.J. in *Re Brighton and Dyke Railway:*[3] *"What I understand to be the definition of a preference share is this – a right conferred upon the holder to receive interest in priority to the ordinary shareholders."*

8.2.2 If a company wishes to raise money by issuing a security carrying the right to a fixed return, to be paid in priority to ordinary shares and with a right to return of only the capital advanced, it has the choice of issuing preference shares or borrowing money. Although preference shares carry the advantage that no dividend is payable unless profits are earned most companies will prefer to raise fixed interest capital by borrowing because interest is an allowable deduction against the company's assessable income for taxation whereas dividends are not.

8.2.3 **Participating Preference Shares** – If the preferred shares carry a right not only to a fixed percentage dividend but also to a further share of profits by way of dividend in the same year either equally with ordinary shareholders or after the ordinary shareholders have enjoyed a specified rate of dividend, which further share is not limited to any fixed rate, the preferred shares are called 'participating preference shares'. The name may also be given to a preference share which participates in a winding up in any surplus after return of capital even if, while the company is a going concern, the dividend is only on a fixed amount.[4]

8.3.1 The rights of preference shareholders depend on the provisions of the memorandum and articles of association and the terms of issue of the preference shares. The English Courts did, for some time give what seemed to be conflicting decisions and only recently a reasonably clear finale appears to have been reached. Professor Gower summarises the canons of construction thus:[5]

1. Prima facie all shares rank equally unless there are terms to the contrary in the terms of issue.
2. If, however, the shares are expressly divided into separate classes it is a question of construction in each case what the rights of each class are.[6]

1 Halsbury's Laws of England 4th Ed vol 7(1) para 176.
2 Company Law 5th Ed.p.226,
3 (1890)44 Ch.D. 28,at 38
4 Ford and Austin's Principles of Corpn Law 7th Ed. p.646.
5 Prof. Gower 5th ed. 371.
6 Re Isle of Thanet Electric Supply Co [1950] Ch.161 CA.

3. If nothing is expressly said about the rights of one class in respect of either (a) dividends, (b) return of capital, or (c) attendance at meetings or voting, then prima facie that class has the same rights in that respect as the residuary ordinary shares. Hence a preference as to dividend will not imply a preference as to capital(or vice versa). Nor will an exclusion of participation in dividends beyond a fixed preferential rate necessarily imply an exclusion of participation in capital or vice versa.
4. Where shares are entitled to participate in surplus capital on a winding up, prima facie they participate in all surplus assets and not merely in that part which does not represent undistributed profits that might have been distributed as dividend to another class.[1]
5. If, however, any rights in respect of any of these matters are expressly stated, that statement is presumed to be exhaustive so far as that matter is concerned. Hence if shares are given a preferential dividend they are presumed to be non-participating as regards further dividends,[2] and if they are given a preferential right to return of capital they are presumed to be non-participating in surplus assets.[3]
6. The onus of rebutting the presumption in para 5 above is not lightly discharged and the fact that shares are expressly made participating as regards either dividends or capital is no indication that they are participating as regards the other.
7. If a preference dividend is provided for, it is presumed to be cumulative.[4] This presumption can be rebutted by any words indicating that the preferential dividend for a year is to be payable only out of the profits of that year.[5]
8. It is presumed that even preferential dividends are payable only if declared.[6] Hence arrears even of cumulative dividend are prima facie not payable in a winding up unless previously declared.[7] But this presumption may be rebutted by the slightest indication to the contrary.[8]

When the arrears are payable , the presumption is that they are to be paid provided there are surplus assets available, whether or not these represent accumulated profits which might have been distributed by way of dividend.[9]

8.4.1 As a result, therefore, the position of the preference shareholders have undergone a change in the last hundred years or so, mostly to their detriment. Unless preference shareholders are expressly granted participating rights they are unlikely to be entitled to share in any way in the "equity" or to have voting rights except in narrowly prescribed circumstances. Yet they enjoy none of the advantages of debenture holders; they receive a return on their money only if profits are earned; they rank after creditors on a winding up and they have less effective remedies against the company. Suspended midway between true creditors and true members they get the worst of both worlds.[10]

8.5.1 **Deferred Shares** – Deferred shares, which are sometimes called founders or management shares, are usually of small nominal amount with a right to take the whole or a

1 Dimbula ValleyTea Co Ltd. vs Laurie [1961] Ch 353.
2 Will vs United Lankat Plantations Co [1914] A.C.11,H.L.
3 Scottish Insurance vs Wilson & Clyde Coal Co[1949] A.C. 462.
4 Webb vs Earle (1875) L.R. 20 Equity 556.
5 Staples vs Eastman Photographic Materials Co. [1896] 2 Ch. 303.
6 Burland vs Earle [1902] A.C. 83 P.C.; Re Buenos Ayres Gt.Southern Rly.[1947] Ch. 384;Godfrey Phillips Ltd. vs Investment Trust Ltd [1953] 1 W.L.R. 41; Re Foster & Son [1942] 1 All E.R.314;Re Catalina's Warehouses and Mole Co. Ltd., Re [1947] 1 All.E.R. 51.
7 Re Crichton's Oil Co. [1902] 2 Ch. 86,C.A.;Re Roberts & Cooper [1929] 2 Ch 383; Re Wood, Skinner & Co.Ltd[1944] Ch 323.
8 Re Walters Symons Ltd[1934] Ch 308; Re F.D. Jong & Co Ltd[1946] Ch 211, C.A., Re E.W. Savory Ltd.[1951] 2 All E.R. 1036; Re Wharfedale Brewery Co [1952] Ch 913.
9 Re New Chinese Antimony Co Ltd [1916] 2 Ch 115; Re Springbok Agricultural Estates Ltd [1920] 1 Ch. 563 and Re Wharfedale Brewery Co. above; Gower's Principles of Modern Company Law 5th Ed 371-3.
10 *Gower, ibid.*

proportion of the profits after a fixed dividend has been paid on the ordinary shares. Their rights depend on the articles or the terms of the issue. Deferred shares are rarely used now.

8.5.2 **Non Voting Ordinary Shares** – If a company wants to raise money and at the same time wishes that the control is retained by the majority, it may issue non- voting ordinary shares. The SEC will want to be satisfied of the reasons for such issue.

8.5.3 **No Par Value Shares** – No par value shares are found in the U.S.A. and New Zealand but not in our country, the U.K. or Australia. This means that shares may be allotted with no fixed value. Different law reform committees in the U.K. and Australia recommended the introduction of this type of shares but upto now these countries have not accepted this idea. Such shares would not give rise to the misleading impression which is often created by the nominal or par value of shares. A par value obscures the reality that a share is no more than a proportionate interest in the net worth of a business. The existence of a par value of a share differing from its market value can be confusing for new investors. Without par value there would be no concept of a premium in an issue price higher than par. Company financial statements would be less complex if there were no such premium. Such were the recommendations of the Australian Companies and Securities Review Committee. New Zealand has accepted this formula and perhaps our SEC and others should consider shares of no par value.

8.5.4 **Employees' Shares** – Some companies issue special shares to employees. In companies which were nationalised after liberation and then denationalised after the government decided to withdraw its investment and sell 51 % shares to outsiders invariably it followed a formula by which it would first sell 34% shares to the members of the public and 15% shares to the employees and then at a later stage sell the balance 51% shares to the highest bidder . This has given rise to some litigations when the employees resisted in conjunction with 34% public shareholders the amendment of articles permitting the government or the corporation looking after the company on behalf of the government to part with its shares. As a result, a new amendment to the Nationalisation Laws had to be passed permitting such amendment without requiring a special resolution to be passed.

8.6.1 **Variation of Shareholders Rights and their Protection** – Section 71 of the Companies Act protects the rights of holders of special classes of shares by requiring that to change their rights there should be a provision to that extent in the memorandum or articles of association and that these should be sanctioned by a specified majority of shareholders of that class. Any number of dissenting members holding at least ten percent of the issued shares of that class may within fourteen days of the resolution apply to the Court for cancellation of the resolution and such resolution shall not be effective until it is then confirmed by the Court. The consideration before the Court will then be whether the variation will unfairly prejudice the shareholders of the class.

8.7.1 **Sponsors Shares and Public Shares** – There is an unprecedented practice that has grown up in Bangladesh whereby a company requiring big capital, e.g., banks and insurance companies, issue shares divided into three different classes of shares, viz., Group A or Sponsors Shares, Group B or Government or Institution shares and Public shares known as Group C shares. Generally Group B shares do not exceed 5% of the shares and the holders of Group A shares retain the majority being 51% shares. Invariably the articles provide that Group A shares will nominate their own directors who generally comprise the majority in the Board. The Group B shareholders have one nominee in the Board, generally an officer of the relevant Ministry who is mainly interested in his allowance unless the interests of the government are involved. The Group C shareholders generally elect two or three directors from amongst themselves in the annual general meeting after long speeches are made by holders of small amount of shares. A practice has grown by which the shareholders attending

the meeting are feted with gifts and nourishments. Sometimes we find sharebrokers or their representatives gathering enough votes to be elected in such meetings to the board and everybody congratulates them without bothering to think that this may lead to the highest form of insider trading.

In order that the public may come to the board the SEC requires such companies to limit the amount of qualification shares to be held by a director not to exceed Tk 10,000 in value. Why a person investing only Tk 10,000 should be allowed to sit in the board of a company doing business of hundreds of millions of Taka is not understood. It is not that these people have specialised knowledge and the rationale behind the requirement that a director should have qualification shares so that he has a reasonable stake in the company is negatived by the forced introduction of people with negligible investment and who did not bother to spend their time or energy at the time the company was formed. It is only when the company has been a going concern that these small investors have come in and got into the board. To encourage small investments by the public is one thing and to introduce them into the management of the company is another.

The SEC requires public companies with more than a specified amount of capital to be listed in the stock exchange and thereby open its doors to the public. That is good but to require directly or indirectly that a shareholder having Tk ten thousand investment may be elected to the Board is something not heard of in countries with a history of successful investments. Similarly, the sooner the government sells or does away with Group B shares the better. In these days of free enterprise why the government should be involved with private investments is not known. This unnecessarily involves different government organisations like, for example, the Bureau of Anti Corruption, which leads sometimes to unnecessary interference and the resultant inhibition the Board may feel while doing business.

This division of shares in different classes is still in the nascent stage in this country and probably some sponsors will be bold enough to do away with this division and pursuade the SEC to amend its unnecessary benevolent attitude towards small investors at the cost of the interest of the company. After all, the small shareholders will be protected if there is enough disclosure about the financial and business affairs of the company so that a small investor knows where he is going and not allowing insider trading by some brokers.

9.1.1 Share Certificates – Section 158 of the Companies Act provides that every company shall within ninety days of the allotment or registration of transfer of any shares, debentures or debenture stock complete and keep ready for delivery a certificate regarding those securities. A failure to do so may attract a penalty of Tk 500 for each day the default continues to be imposed on the company and every officer who is knowingly and willingly a party to the default. It is enough that a company prepares and keeps ready the certificates and the law does not require that the company should also distribute them.

A Division Bench of the Dhaka High Court has held that all that the section requires is that the company keeps the certificates ready and that a complaint that the certificates were not ready for delivery to the complainant would not be an offence within the meaning of this section.[1] Following the case of *Asiatic Oxygen Ltd*[2] the Court held that this section does not impose upon the company to deliver the said share certificates and that the complainant who had already obtained a decree with respect to the non- delivery of share certificates should enforce the decree. The issue of a share certificate may give rise to an estoppel against the company. The company cannot deny the truth of the certificate against a person who has relied on the certificate and in consequence has changed his position.[3] There is no estoppel in favour of a person who procures the granting of a certificate on a forged transfer,[4] or forged power of attorney.[5] The company may be estopped from denying the title to shares of the

1 Muhammadullah vs Makbul Ahmed 44 DLR (1992)H.C. 107.
2 AIR 1972 (Cal) 50
3 Re Bahia and San Francisco Rlwy Co (1868) L.R. 3 Q.B 584.
4 Sheffield Corporation vs Barclay [1905] A.C. 392.
5 Sharkey vs Bank of England [1903] A.C. 114.

person to whom it has issued a share certificate.[1] The company may be estopped from denying the amount stated to be paid up on the shares.[2] There is no estoppel in favour of a person who knows the untruth of statements in a share certificate.[3] In England, if the shares had been transferred to a purchaser without notice that they were not fully paid up he could give a good title to a purchaser from him with or without notice.[4] The company is not estopped where a certificate is a forgery.[5]

9.1.2 Section 32 provides that the subscribers to the memorandum of association and every other person who agrees to become a member and whose name is entered in the share register shall be a member of the company. The register of members must, in addition to showing the names and address of every member and the date on which he was registered as a member, in the case of a company with a share capital, state the number of shares held by him and the amount paid up on each share.[6] The register and the index of members will have to be kept at the registered office of the company and shall be open for inspection by members during business hours without charge and by any other person on payment of a small fee and a copy of it or any part of it has to be supplied to anyone on payment of a modest charge.[7] Professor Gower comments that this is a legitimate help to any member who wishes to communicate with any of his fellow members and to a take over bidder. But unfortunately it also enables traders who wish to attempt to sell their wares by junk-mail or telephone calls to obtain, more cheaply than in any other way, a "sucker-list" of potential victims by buying a copy of the membership register.[8] The company may close the share register by notice of seven days for a period not exceeding 45 days a year but not exceeding thirty days at a time.[9]

9.1.3. **Share Register as Prima Facie Evidence** – Section 36 of the new Act corresponds to section 32 of the Act of 1913. This section requires every company having a share capital to file a return to the Registrar in a form as mentioned in Schedule 10 to the Act within eighteen months of its incorporation and at least once thereafter each year mentioning the list of persons who are members of the company on the date of the annual general meeting and of all persons who have ceased to be members since the last annual general meeting. Subsection (2) gives details of the particulars to be filed. The Form in Schedule 10 to the Act differs in certain respects from the requirements to be inserted according to sub-section (2). The Return has to be prepared and filed within twenty days of the annual general meeting.

9.1.4 The annual return to be filed should reflect the names entered in the register of members to be maintained under section 45 of the Act. This section provides that the share register shall be the prima facie evidence of any matters by this Act directed or authorised to be inserted therein. A share holder who has no direct access to the share register, may get a copy of the returns filed annually with the Registrar and know not only whether his name is still in the share register or not and whether anybody else has been allotted shares without giving them pre-emptive rights. This should alert them so that they may seek redress in the Courts.

Mustafa Kamal J. has held in *Shamsul Huda vs. Alauddin Taiwa*[10] that the register of members shall be prima facie evidence on any matters by the Companies Act directed or authorised to be inserted therein.

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1 Balkis Consolidated Co Ltd. vs Tomkinson [1893] A.C. 396; Dixon vs Kennaway & Co [1900] 1 Ch 833.
2 Bloomenthal vs Ford [1897] A.C. 156.
3 Crickmer's Case (1875) L.R. 10 Ch. App 614.
4 Barrow's Case (1880) 14 Ch.D. 432,C.A. and Charlesworth and Morse: Company Law 14 Ed. p.275.
5 Balkis Consolidated Co Ltd vs. Tomkinson, ante Supra.
6 Section 34.
7 Section 41.
8 Gower's Principles of Modern Company Law, 5th Ed. p.386.
9 Section 42.
10 36 DLR(H.C.) 316.

9.1.5 **Share Register Rectification** – Section 43 of the Act corresponds to section 38 of the Act of 1913. The new section differs from the old section in that it does not contemplate rectification of share register if a member's name has been fraudulently entered in or omitted from the share register. This section also does not contain a provision for filing an appeal in case a question of law has arisen as an issue and tried. Invariably an appeal was filed from a decision given by the company bench of the High Court Division to a division bench of the High Court Division although no such issue of law was raised and tried. Only recently a ground was taken before an appeal before the Appellate Division that such an appeal before the division bench of the High Court Division was incompetent.

In this case the division bench reversed the decision of the single bench and objection was raised before the Appellate Division that the entertaining of the appeal by the division bench was incompetent. No appeal lies against an interim order.[1] In *Jabed Ali Sarkar vs. Sultan Ahmed*[2] the Court held that if a question of law was decided an appeal would lie. In *ET Mills Ltd. vs. Abdul Awal*[3] Justice Badrul Haider Chowdhury discussed the provisions for filing an appeal against an order under section 38 of the Companies Act of 1913 and commented that " this means right of appeal is limited as it is for second appeal to a point of law...Calcutta High Court Rules, 1939 repealed the Rules in Chapter XXXI and the form prescribed in Appendix K of the Original Side Rules 1,14 and now the entire procedure is regulated by the Rules framed by the High Court. These Rules were framed under the power conferred under section 246 of the Companies Act the practice and procedure is regulated by these rules. Rule 5 prescribed for the register of companies matters and an application under section 38 is to be entered and numbered and then rule 15 provides the procedure for rectification of the share register. Before 1939 Rules an appeal from the judgment of a court of first instance at the original side lay to the division bench by virtue of clause 37 under Letters Patent of 1865 which conferred upon the High Court the Rule making power. Since its repeal the matter is regulated by 1939 Rules. These Rules had been adopted by this Court."

It is not understood why the learned judge went on discussing the rules in that case as the moot point involved was whether pending winding up an application under section 38 of the Act of 1913 for rectification of the share register would lie before the company judge. However, this is an excellent exposition of the law and rules relating to the procedure adopted in an application for share register. A division bench of the High Court Division while dismissing an appeal from a decision of the company judge made a passing reference to the provision for appeal and said that one of the reasons for dismissing the appeal was that they were not convinced that some law points were involved.[4] The issue was settled in *Moqbul Ahmed and another vs Ahmed Impex (Pvt) Ltd and another*[5] where Justice Mustafa Kamal delivering the judgment of the Appellate Division held that no appeal lay from a decision under section 38 of the Companies Act 1913 to a division bench of the High Court and a judgment of the division bench in that case would be non est having been passed completely without jurisdiction, a classic example of coram non judice. This is because the Original Side Rules are not in existence and more so after the repeal of the Letters Patent.

The application of this judgment is far reaching although under the new section 43 of the Act of 1994 there is no appeal provided for in the Act of 1994. If a division bench of the High Court Division cannot hear an appeal from a single judge of the High Court Division because the Letters Patent and the Original Side Rules are not in existence then the provisions for appeals in other sections of the Companies Act 1994 have in fact become redundant as in every case an appeal has to be filed with leave of the Appellate Division under Article 103 of the Constitution.

1 People's Tobacco vs. Md Nurul Huda (1969) 21 DLR 186.
2 (1974) 26 DLR 196.
3 38 DLR (AD) 26.
4 United Chemicals vs Niranjan Dey (1995) DLR (HCD) 423,430.
5 48 D.L.R.(A.D.) 82.

9.1.6 Section 43 provides that the Court may order a rectification of the share register if the name of any person is without sufficient cause entered in or omitted from the register of members of a company or neglect is made or unnecessary delay takes in entering on the register the fact of any person becomjng or ceased to be a member. The application for rectification may be made by the company, any of its members or by an aggrieved person. The Court may either refuse the application or may order rectification of the register and payment by the company of any damages sustained by any party aggrieved, and make such order as to costs as it in its discretion thinks fit. Sub-section (3) provides that on any application under this section the Court may decide any question that may arise between a member or alleged member or between themselves and the company and generally may decide any question necessary or expedient to be decided including a question of law for rectification of the register.

In *Shamsul Huda vs Alauddin Taiwa,*[1] Mustafa Kamal J. held that an application for rectification of share register is governed by the procedure prescribed for suits in accordance with section 141 of the Code of Civil Procedure. The Court however, refused to grant an injunction on the holding of a meeting because a shareholder's locus standi as a shareholder was disputed on the ground that he had already exercised his rights before.

There have been a number of cases in the High Court Division on the scope of the power of the High Court under section 43 of the Act. These cases have followed the principles in the Indian Courts and the English jurisdiction. As the case law in this regard is sufficient, the position as enunciated in our Court is discussed below in some details. Quite often the Court was required to examine whether an alleged transfer or allotment of shares was done validly. This would require the Court to examine whether the transfer or allotment was done after complying with the legal formalities and /or fraudulently. Though the present Act does away with fraud as one of the reasons for ordering share register rectification, the fact that a share register may be rectified if the name of any person is entered in or omitted without any sufficient cause will enable the Court to interfere if there is a fraudulent transaction . Also it is difficult to think of a transaction legally done if it is fraudulent. It does not matter what the intention of the Board of Directors are if they acted legally and complying with the provisions of the Act. Court exercises summary jurisdiction but of very wide amplitude.[2]

9.2.1 Primarily the following questions arose before the Court in an application for share register rectification:

a. Is there any time limit in an application for rectification of the share register?

b. Are the requirements for transfer of shares complied with, and what are those requirements ?

c. What is the extent of jurisdiction of the company bench to interfere in such an application?

9.2.2 After some amount of controversy that arose with the Edruc case (unreported) the Appellate Division finally held that the Limitation Act does not apply in a case for rectification of share register.[3] This case also settled other important relevant question, namely, that a share register is the prima facie evidence of any matter to be inserted therein but where both parties have led evidence the question of initial presumption loses its importance and that when the facts involved are not complicated calling for a detailed investigation in a separate forum, applications for corrections of share registers are maintainable.

On the question of limitation the Court held that when the Limitation Act is silent the Appellate Division would be reluctant to travel beyond the fixed path to lay down a law bringing an application for rectification of the share register within the application of the residuary Article 181. In this case one of the shareholders complained that his shares were

1 36 D.L.R.(H.C.) 332.

2 Dr. Manjurul Islam vs Al Rajhi Hospital. 1 Law Guardian (HCD) 46

3 Tamizul Haque vs Shamsul Haque 43 DLR (AD) 34.

transferred unauthorised and in a fraudulent manner. He learned about the transfers after making enquiries at the office of the Registrar . He filed a complaint to the Registrar and had a salish organised to settle the dispute with the other shareholders and having failed there he filed the applications for rectification of the share register. Evidence was given before the Company Bench and it was apparent that there was some sort of arrangement that the shares would be transferred and retransferred. The Appellate Division agreed with a suggestion made at the bar that if there had been a transfer of the shares , mere non-payment of the consideration would not stand in the way of the transfer becoming valid, but found that there had been no such transfer.[1] The returns filed at the office of the Registrar showed that there were interpolations and the explanation of the appellant that these were bonafide corrections made before filing of the Returns were rejected by all the Courts. It was also contended at the Bar that the application was filed after inordinate delay and was barred by limitation. The Court found that the petitioner was taking steps and never gave up his rights nor did he acquiesce in the acts done by his brother, the respondent in this case.

The lawyer for the transferees, contended that even if the limitation starts from the date of his knowledge about the transfer, that is April 1977, when he was prevented from entering the company's office and filed his complaint before the Registrar, still the period of 3 years , as laid down in Art.181 expired before he filed the applications in August 1982. The lawyer for the petitioner on the other hand contended that no period of limitation had been prescribed in law and consequently such an application would be governed by the general principle of reasonable time. Chief Justice Shahabuddin Ahmed delivering the judgment noted the arguments on both sides and commented thus (paragraphs 25 and 26):

> 25. Mr. Rafiqul Huq has referred to a decision of the Indian Supreme Court in the case of *Sha Mul Chand & Co. vs Jawahar Mills Ltd,*[2] in which it was indicated that an application under section 38 of the Companies Act might be governed by Art. 181 of the Limitation Act. Dr Rafiqur Rahman has also relied upon this decision in order to press his contention that in fact Article 181 was not held to be applicable to an application under section 38. The Supreme Court gave this decision in an appeal from a judgment of the High Court reported in;[3] Dr. Rahman has placed reliance on that judgment also. Article 181 prescribes a period of three years for an application for which no period of limitation is provided elsewhere in the First Schedule or by sec. 48 of the Civil PC. It has been observed by the Supreme Court that Art. 181, has, in a long series of decisions of most, if not all, of the High Courts, been held to govern only applications under the Code of Civil Procedure. It may be that there may be divergence of opinion even within the same High Court but the prepondering view undoubtedly is that the Article applies only to applications under the Code'.... The question raised in that appeal was, however, decided by the Supreme Court on the merit of the case and it was held that even if Art.181 did apply to the application, it would still be within time of the period of limitation of three years started from the time when the right to apply accrued.
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> " 26. The law of limitation is intended to put an end to litigation. It requires that persons must come to Court and take recourse to legal remedies with due diligence. The Limitation Act guillotines cases which seek reliefs at a point of time which is beyond the period specified thereunder. This is what has been exactly propounded in Para 309, Halsbury's Laws of England(4) as to an application to rectify a share register which must be made promptly. In this connection I have considered Articles 48,49,120,158,178 of the Limitation Act. Last mentioned two Articles govern appeals and applications respectively under the Arbitration Act. Analogy to these Articles does not provide any indication that applications under Art.181, which provide for residuary matters, also include an application under any other law than the Civil Procedure Code. Moreover, when the statute has remained silent, I do not think this Court should travel beyond its fixed path to lay down a law bringing an application under section 38, Companies Act, within the ambit of the residuary Art. 181. *I am , therefore, of the view that applications under the Civil Procedure Code and that the application for rectification of a share register under section 38 is left to be governed by the general principle that it shall be filed within a reasonable time and not after inordinate delay. What is a*

1 para 12,page 39,ibid.
2 AIR 1953 S.C.98
3 AIR 1957 Mad 572.

reasonable time or an inordinate delay is left to be determined by the Court on consideration of the facts and circumstances of a particular case. Two decisions of the High Court Division given by two different Benches, have been cited before us. In one decision a period of six years, and in the other a period of ten years were considered to be reasonable time within which an application for rectification of share register should be filed.

"The position, therefore, is that an application for rectification of the share register must be made within reasonable time of the knowledge that the cause of action has arisen."

9.2.3 The considered opinion of the High Court Division is that the procedure under section 38(3) of the present Act (section 34 of the Act of 1913) must be complied with before the Courts will uphold the validity of a transfer of shares. Sub-section (3) of section 38 lays down that it shall not be lawful for the company to register a transfer of shares in or debentures of the company unless the proper instrument of transfer duly stamped and executed by the transferor and the transferee has been delivered to the company along with the scrip. The directors may however, register the transfer if they are satisfied that the instrument of transfer has been lost. There should therefore be:

a) An instrument of transfer signed by both the transferor and the transferee;

b) The instrument of transfer should be properly stamped; in fact the consideration of revenue seems to the foremost in the mind of the legislature;

c) The share scrip must be delivered along with the instrument of transfer for registration of the transfer of shares.

This was held by *Fazle Munim J. in Jabed Ali vs Dr. Sultan Ahmed.*[1] This was a case where two transferees were contending for registration of their names as shareholders. The appellants applied to have his name registered and asked the company to collect the share scrip from the State Bank; before the company did anything the respondent delivered the share scrip and asked for registration of his name. The Court held that the title of the appellant who was an unregistered transferee is of a kind which has been described by expressions such as "incomplete","hidden" and "inchoate". This title is not, therefore available against the claim to title by the respondent No.1 who had both documents of transfer and the share certificates at the time of considering the appellant's claim for registration. This case was distinguished in *Sher Ali Amir Ali Virjee vs Eastern Industries Ltd*[2] *and ors.* where the Court held that it was not necessary to produce the script (original share certificate) before the managing director for transfer of the shares because he knew about the shares and in the facts of the case , non-production of scrip would not debar the transferee from getting his name registered in the company as its shareholder. Mr Justice M.M.Hoque interpreted the above case as saying that " their lordships view was that if there was no dispute or doubt , then the production of script was not necessary and without production of scripts, in such a case, the name of the transferee might be registered."

The Court held that the respondent's title must be preferred to the title of the appellant who claimed priority on the basis of an instrument of transfer which, when produced to the company, was not accompanied by the share certificates. The title of the appellant who was an unregistered transferee is of a kind which has been described as incomplete etc. The title is not, therefore, available against the claim to title by the respondent No. 1 who had both documents of transfer and the share certificates at the time of considering the appellant's claim for registration. The Court supported this by quoting from *Pennington's Company Law*,[3]:

the purpose of registering the transfer is to notify the company of it so that the transferee may compel the company to pay him future dividends and allow him to vote at shareholders' meetings. By registering the transferee acquires legal rights against the company, but it does not follow that the legal title to the shares has not already passed from his transferor to him by

1 26 DLR (1974) 303,312. Also see Ahsan Karim Jinnah vs Meghna Insurance Company Limited & ors. 52 DLR 160 = 20 BLD (HCD) 114 = 6 MLR (HCD) 149.

2 43 DLR 54.

3 (1967) Second Ed.page 289,

virtue of the executed share transfer and the transferor's share certificate being delivered to him, so making his right to the share effective against all interested persons except the company.

The learned judge cited the case of *Maneckji Pestonji Bharncha vs Wadilal Sarabhai & Co*[1] where it has been held by the Judicial Committee that the property in shares passes as soon an instrument of transfer along with the share certificates are delivered to the transferee and held that as soon as the State Bank delivered the share certificates to the Respondent No 1, such delivery effected the change of ownership of the shares in question and title to the same vested with the Respondent No 1. This of course does not mean that the respondent would become a shareholder inasmuch as until the company enters his name on the share register he would not be a member.

The Court discussed the provisions of section 34(3) of the Act of 1913 equivalent to section 38 of the present Act, and observed that the company was not merely required to perform a ministerial act on the presentation of an application for registration of the transferee's name. No transfer can be registered without a proper instrument of transfer and share certificates and the company will be perfectly justified to refuse registration of the appellant's name on the ground of non-production of share certificates particularly when the company was unable to waive their production. Had the share certificates been lost the company might have waived their production under the power to do so under the articles. The Court observed thus:

> ...A claim for registration on the basis of a transfer which was not accompanied by share certificates or whose absence was not duly accounted for to the satisfaction of the company cannot give the transferee 'a present, absolute, unconditional right to have the transfer registered' and more so when "the company was informed of a better title.' In saying so we are supported by the case of The *Societe Generale De Baris and G. Colladon vs Janet Walker and others reported* in [1885] A.C. 20. Here the position of a transferee of shares in a company whose claim for registration was met by the opposing claim of another transferee who had the share certificates in his possession was considered by the Court. In saying that such a transferee had before registration merely an inchoate title in the shares which was not equivalent to a legal estate in the shares, Earl of Selborne observed:
>
> Such a transfer might, indeed, give a legal right of action against the company if they, without just cause, refused to register it; it might also be a good foundation for an application to a competent court to rectify the register. But it could not, under the 26th article of association of the Tramways Company confer (while unregistered) a legal title to the shares themselves; nor do I think that the fact of its execution and of a claim having been made to register it before the company had notice of the prior equitable title would necessarily make it the duty of the company, after receiving such notice, to register it, or of a court to compel them to do so, and thereby to effectuate a fraud, till then incomplete.
>
> He, then, went on to observe :
>
> If, indeed, all necessary conditions had been fulfilled to give the transferee, as between himself and the company, a present, absolute, unconditional right to have the transfer registered, before the company was informed of the existence of a better title, the case might be different.
>
> In the circumstances, the appellant's claim for registration of his name in the share register of the company could not succeed and prevail over that of the respondent No 1.

On the question of determining the priority of purported transfers of the same shares to different people, the English courts have relied on two traditional principles of English property law : i.e., (1) that as between two competing holders of equitable interests, if their equities are equal the first in time prevails and (2) that a bonafide purchaser for value of a legal interest takes free of earlier equitable interests of which he has no notice at the time of purchase. In applying these principles to competing share transfers, a transferee prior to registration is treated as having an equitable interest only but registration converts his interest into a legal one.[2]

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1 30 CWN (PC) 890.

2 Gower's Principles of Modern Company Law 5th Ed page 400

In *Shoaib (Md) vs Uttara Bank Ltd and another*[1] Justice M.M.Hoque refused to apply the above case on the ground that the facts of the case before him did not attract the principle laid down in the earlier case. The petitioner claimed that he had purchased the shares of Eastern Banking Corporation but the Uttara Bank refused his claim to be recognised as a shareholder. When sued in the Company Court the Bank took up the position that as the instruments of transfer of shares had not been duly stamped and approved by the company's board of directors and as the name of the petitioner did not find place in the register of members of the company the petitioner was not entitled to get the share of the company. The petitioner argued that at the relevant time the petitioner was not required under law to affix stamp duties on the instruments of transfer as this was exempted by the government in the case of public companies. The Court found force in this argument and held that his application could not be turned down for the alleged non-fixation of stamp duty on the instruments of transfer. As the petitioner approached the Bank at a much later date the Bank argued that the instruments of transfer of shares should have been lodged with the company duly stamped after the actual transfer. The case of Jabed Ali Sarker vs Dr Sultan Ahmed,[2] was cited at the bar but the Court held that the observations made in that case did not fit in the case before him. Justice M.M.Hoque commented thus :

> 18. From the provisions of law it appears that there is no time limit or any other consequential obligation if stamp is not affixed with the instrument of transfer. There is no penal provision either. Since it is a requirement of law, it must be complied with, but I find that as there is no penal provision, it may be paid even after submission of the instrument of transfer to the company. In the present case the affixing of stamp with the instruments of transfer does not arise in view of the fact that the respondent Bank in its first letter dated 15.4.84 refused to consider the case of the petitioner as he is not the registered shareholder of the erstwhile Eastern Banking Corporation.

On the issue of the discretion of the directors to refuse to register a transfer of shares, the learned judge observed thus :

> 25. It is provided in the Articles of Association and the prospectus that directors have got discretion either to refuse or to accept the transfer of shares. It is true that the directors have got discretion, but it must be a reasonable and judicial discretion. Such a discretion should not be an arbitrary one at any rate. In my view, the discretion exercised by the directors in the present case is absolutely arbitrary without having any legal basis.... Moreover the three reasons for not considering the case of the petitioner have already been answered above. In my view, those reasons are not at all tenable in law and as such the submissions of Mr. Nurullah has no substance. Considering facts and circumstances of the case and the provisions of law as discussed above I am of the view that the petitioner is entitled to get relief prayed for in this application.

It is not clear whether the Bank argued that a person does not become a member of a company (Eastern Banking Corporation Ltd) until his name is entered in the share register of members although this seems to be one of the reasons the Bank refused to recognise the petitioner as a shareholder. This argument would have been relevant because the background of the case was that the petitioner was claiming pre emption rights in shares of Uttara Bank Ltd as a former shareholder of Eastern banking Corporation Ltd. His lordship M.M.Hoque was undoubtedly right in holding that there is no time limit for affixing stamps on instruments of transfer since the only consequential result of not affixing stamps would be that the company would be entitled to refuse to register the transfer and the transferee may wait for indefinite time to affix the stamp but he would not be entitled to have the transfer registered unless the instrument properly stamped was lodged with the company. The petitioner would certainly have a right to have his name entered on the share register but as long as his name was not actually entered in the register of members of the Eastern Banking Corporation could he claim that he was in fact a member of that bank? This question remains unanswered as from the judgment this argument does not seem to have been raised at the Bar.

An observation was made in *Sonali Bank vs United Commercial Bank Ltd and others*[3] that section 34 of the Companies Act 1913 (section 38 of the current Act) contemplates two

1 43 DLR(1991) 329

2 ibid.

3 (1992) 12 BLD(AD) 256.

kinds of transfer of shares, namely, under an instrument of transfer duly stamped and executed by the transferor and the transferee and the transmission by operation of law. This was an obiter as the question in issue was whether some share certificates could be attached in execution proceedings of an admiralty suit when the same were deposited with another bank for sale and adjustment of the judgment-debtor's dues to the bank.

Professor Gower comments[1] that notwithstanding a suggestion by Lord Selbourne in the case of *Societe Generale vs Walker*[2] that "a present *absolute right* to have the transfer registered" might suffice, it seems that nothing less than actual registration will do." In *Ireland vs Hart*[3] the transfer had been lodged for registration and the directors had no power to refuse but it was held that the legal interest had not passed. In Life Insurance Corporation of *India Ltd vs Escorts Ltd*[4] the Supreme Court of India held that

> a transfer effective between transferor and transferee is not effective as against the company and any person without notice of the transfer until the transfer is registered in the company's register.

In this case the Court made an obiter observation that it was true that the directors had got a discretion either to refuse or to accept the transfer of shares but it must be a reasonable and judicial discretion and should not be an arbitrary one at any rate.[5] Board's discretion to refuse registration of transfer must be exercised after just and proper consideration.[6]

Justice Latifur Rahman delivering a judgment of a Division Bench of the High Court Division commented thus:

> 14. From the judgment of the Company Judge, we find that the Company Judge on the facts of the present case found that there might be an arrangement between the brothers having no legal sanction. In this regard we may refer to section 34(3) of the Companies Act which says that the transfer of shares shall not be lawful without any instrument of transfer. Though transfer may be voluntary act of parties but until an instrument is executed as contemplated under section 34(3) of the Companies Act, the legal title remains with the transferor.[7]

Instrument of Transfer is mandatory for registering a transfer of shares.[8] The share certificate must be shown to have been handed over to the Company or the transferee.[9]

In *Sudhangshu Shekhar vs Anath Bandhu,*[10] Justice S.M.Hossain made an obiter that the obligation under section 34(3) of the Companies Act of 1913(section 38(3) of the present Act) is "an obligation of the company which the company must discharge. But this obligation of the company is not obligatory on the Court while administering the provision of section 38 (43 of the present Act) of the Companies Act. Sub-section (2) of section 38 provides that the Court may either refuse the application or may order rectification of the share register. The power of the Court under section 38 is wider than the obligation of the company under section 38. Under section 34, the company is obliged to see whether the instrument of transfer of share has been duly stamped or not. Under section 38, the Court is obliged to see whether there has been a valid transfer of the share or not. Accordingly, the aforesaid objection with regard to the validity of the instrument of transfer of the share has no substance." The objection raised in this case was that the instrument of transfer of share was not duly stamped and cancelled according to the Stamp Act.

Notice whether to take shares under a pre emption clause not sent by registered post is not valid and the consequent transfer of shares was not valid.[11]

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1 5th Ed. ibid.page 400.
2 [1885]11 A.C. 20,H.L.
3 [1902] 1 Ch.521.
4 [1986] 59 Comp. Cas 548,618.
5 ibid at para 25.
6 Giasuddin Ahmed vs Green Delta Insurance Co. Ltd. and another. 52 DLR 41. This decision was set aside by the Appellate Division on a finding of fact that the discretion was used improperly in a publicly traded company. Giasuddin Ahmed vs Green Delta Insurance Co. Ltd. and another 9 MLR (AD) 1 = 56 DLR (AD) 31; Also see Dr. Manjurul Islam vs Al Rajhi Hospital 1 Law Guardian (HCD) 46.
7 Haque Brothers vs Shamsul Haque (1987) 39 DLR 290, 299
8 Nur Mohammad vs Agrani Flour Mills Ltd. (1995) 47 DLR 462 (HC).
9 Abu Taher vs Nur Muhammed & ors. 53 DLR (AD) 88 = 21 BLD (AD) 60 = 7 BLC (AD) 38.
10 28 DLR(1976) 315
11 United Chemicals and Pharmaceuticals Ltd. ñvs- Niranjan Dëy and ors. MLR (1996) AD 420.

9.2.4 In India the language is "shall not transfer" instead of "it shall not be lawful" in Bangladesh. The Indians have watered down the forceful effect of the requirements for registration of a transfer and yet the Supreme Court in interpreting the expression "shall not register" has pointed out that, where the language used is in the negative form, it 'emphasises the insistence of compliance' with the provisions concerned and is intended as a legislative device to make a statutory provision imperative.[1] An injunction may issue against a company restraining it from effecting a transfer where the requirements of the section are not complied with.[2]

9.2.5 **Blank Transfer** – In a blank transfer the buyer's name or signature or the date of sale may not be given. The seller signs and the transfer form may change hands and the first transferor will be treated as the transferor even if the registration takes place after his death. Blank transfers are common also when securities are mortgaged to raise money. The advantage is that it saves the trouble of complying with the formalities of transfer every time a security changes hands. A transfer in blank, when accompanied by the share certificate or scrip conveys both the legal and equitable right in the shares and also the right to call upon the company to register the transfer. Lord Watson said more than a century ago that "the person to whom it *i.e.*, the blank transfer along with the certificate is delivered, can effectually transfer his interest by handing his certificate to another, and the document may thus pass from hand to hand until it comes into the possession of the holder who thinks fit to insert his own name as transferee, and to present the document to the company for the purpose of having his name entered in the register of shareholders and obtaining a new certificate in his own favour."[3] Only a bonafide holder will have the right to fill in his name or the name of a person for whom he is acting under an authority and apply for registration of the transfer.[4] In *Howrah Trading Co Ltd vs C.I.T.*[5] the Supreme Court of India upheld the validity of "blank transfers" where the name of the transferor is entered and he signs the transfer with the share scrip annexed, and hands it over to the transferee who may complete the transfer and hand it over to the company for registration of his name." The company is not bound to conduct an enquiry as to whether the transferee is alive on the date the transfer is accepted by the company or whether he is capable of entering into a valid contract on that date.[6] In *Bengal Silk Mills Ltd*[7] the Court held that a blank transfer instrument can be completed even after the death of the transferor. Of course, the share certificate will have to accompany the transfer form. Same rule applies if the blank transfer forms are signed as a gift to the transferee.[8]

A transfer when accepted, relates back to the date of execution of the instrument.[9] A forged transfer can pass no title as it is a void document.[10] If there are no restrictions in the articles or the debenture, a registered holder of security may transfer it by way of gift. The donee's acquisition of legal ownership occurs on registration of the transfer. On a gratuitous transfer of shares or a debenture for which there is a share certificate the mere signing of the instrument of transfer without delivery of the transfer and share certificate to the transferee will not pass any interest to the transferee.[11] According to the weight of authority if the donor has done everything which it is necessary for the donor to have done to effect a transfer of

1 Mannalal Khetan vs Kedar Nath Khetan [1977] 47 Comp Cas 185.
2 Somani vs Somani [1986] 59 Comp Cas 910(All).
3 Colonial Bank vs Cady [1890] 15 App. Cas 267,277.
4 Colonial Bank vs Hepworth[1887]36 Ch.D.36.
5 AIR 1959 S.C. 775.
6 ibid.
7 AIR 1942 Cal 461.
8 Ramchandra Shelat vs Pranlal Jaymand Thakar AIR 1974 SC 1728; Sheila Devi Chamria vs Tara Chand Saraogi [1986] 60Comp Cas 735.
9 Killick Nixon Ltd vs Dhanraj Mills Pvt Ltd. [1983] 54 Comp Cas 432.
10 Sheffield Corporation vs Barclay[1905] A.C. 392(HL).
11 Poliwka vs Heven Holdings Pty Ltd[1992] 7 Auatralian Corporations and Securities Reports, 85.

the legal title, the intended donee becomes owner in equity. That will require delivery to the transferee of a registrable instrument of transfer and the relevant security certificate.[1] The transferee although not registered holds the beneficial interest and is competent to require the transferor to vote according to his wish as well as to transfer the dividend to him.[2]

9.2.6 The statement by courts that shares are prima facie transferable[3] suggests that the right of transfer can be taken away entirely. There would seem to be no reason why a provision in the articles that shares shall be transferable only with the consent of all members should be held invalid.[4] In some companies the articles may limit the persons to whom members can transfer shares. A usual pre-emption provision is that any member who is desirous of disposing of shares shall first offer them to other members by a prescribed notice. Under some provisions the other members may be obliged to take the shares. Under others they may be free to refuse to buy, in which case the shares can then be offered to non-members. There will be a provision for determination of the price at which others members are to buy. Sometimes the sale price is to be determined by the company's auditor. The articles may also provide for the notice to constitute the board of directors to be the agent of the selling member for the sale of the shares and for the board to ascertain from other members the number of shares each wishes to buy. Where articles create a right of pre-emption in the members, each of them has an individual membership right sufficient to give standing to sue the company to restrain shares being transferred in breach of the articles, or if the shares have been transferred, to have the register rectified.[5] If articles oblige remaining shareholders to buy the shares of a member that member may enforce the article directly against those other members.[6] In a case from Chittagong a group of shareholders complained in the Company Court that other shareholders had transferred their shares to outsiders although the articles required them to offer the shares first to all shareholders including the petitioners. The Court held that no such offer was made and that a notice sent by a certificate of posting was not enough presumption that the notice had in fact been sent. The result was upheld in appeal before a division bench of the High Court Division and the Appellate Division.[7]

9.3.1 The Court is to decide the domicile of the company for ascertaining its own jurisdiction to deal with the matter under the section.[8] An Indian purchased shares of a Pakistani company; subsequently he became a Pakistani- his name could be enrolled.[9] In *Monzurur Rahman vs Rema Tea Co. Ltd*[10] Justice S.M.Hossain held that a proceeding for rectification of the share register is a special proceeding before the original side of the High Court Division and this proceeding is not in the nature of a suit as contemplated under section 9 of the Code of Civil Procedure. The forum for the adjudication of any dispute under section 38(43 of the present Act) exclusively vests with the original side of the High Court Division in view of the clear provisions of sub-section(1) of section 3 of the Companies Act. The Court held that shares in a company held jointly by more than one person could only be split up specifically between the individual shareholders either amicably between them or at the instance of any shareholder by the company under section 34(38 of the present Act) or at the instance of any shareholder by the Court under section 38(43 of the present Act) of the Companies Act. In whatever manner such division of shares might be effected either mutually between the parties or by an act of the company or by an order of the Court, it must be done within the four corners of the Companies Act and not under any other law. In such

1 Ford and Austin's Principles of Corporations Law (7th Ed) p.789
2 R.Mathalone vs. Bombay Life Assurance Co. Ltd. AIR 1953 S.C. 385; Chunilal Khasaldas Patel vs. H.K. Adyaru AIR 1956 S.C. 655; Howrah Trading Co. vs I.T. Commissioner AIR 1959 S.C. 775.
3 Greenhalgh vs Mallard[1943] 2 All E.R. 234.
4 Philips vs Manufacturers' Securities Ltd[1917] 86 LJ Ch 305.
5 Grant vs John Grant & Sons Pty Ltd[1950] 82 CLR 129.
6 Rayfield vs Hands(1960) Ch 1.
7 Company Matter No 8 of 1993 Niranjan Dey vs United Chemical Works Ltd. (1995) DLR (HCD) 423.
8 Sakhawat Hossain vs Chittaranjan Cotton Mills Ltd(1962) 14 DLR (Dac)407.
9 Sirajuddin A. Kader vs Chittaranjan Cotton Mills (1968) 20 DLR 196.
10 33 DLR(1981) 49.

circumstances when the parties disagreed amongst them to divide their joint shares and when the company failed to effect such division, the only remedy left with the parties in question to divide such shares is by way of an order of the Court to rectify the share registers of the company under section 38(43) of the Companies Act.

In A.Ahad vs S.M.Anwaruddin and others[1] it was held that a company or corporation was to be sued not in the name of its directors but in the name of the company or the corporation but where allegation in the plaint affected such executive members in their personal 'capacity it could not be said that they had been wrongly impleaded as this would give them a chance to rebut allegations behind their back.

9.3.2 **Jurisdiction of the Company Court to Rectify Share Register** – Both the civil court and the High Court Division exercising its jurisdiction under the Companies Act (section 43) may rectify a share register. When the dispute involves complicated questions of fact, the Company Court may refuse to exercise its jurisdiction. This however depends upon the judge concerned and if the applicant can show a strong prima facie case and has the sympathy of the Court the chances are that the judge will interfere even if it means taking evidence by deposition in Court. The position that emerges after a number of decisions on this point is that where the Company Court exercises jurisdiction the Court feels that it has a wide range of power. Section 38 of the Companies Act of 1913 (corresponding to section 43 of the current Act of 1994) gives the Court a wide discretion to scrutinize any fraud, error or undue influence or misrepresentation in the matter of transfer of any share and grant relief commensurating with the appropriate possible relief.[2]

The question of jurisdiction came up as early as 1956. In *Re Anath Bandhu Guha and Sons Ltd*[3] a division bench of the High Court held that the provisions of section 38 of the Companies Act, 1913, relating to the rectification of a register of members are very wide and give the judge wide discretion in the matter. The wide terms of sub-section (3) of that section are not to be limited by the terms of sub-sections (1) and (2) thereof; and the court grants appropriate relief to prevent harassment to parties in any case, irrespective of any finding of fraud, error, mistake or default on the part of the company. Amin Ahmed C.J. delivering the judgment discussed exhaustively the decisions of the Indian sub-continent and the U.K. and quoted the observations of Mookerjee and Fletcher JJ. in *Ramesh Chandra Mitter vs Jogini Mohan Chatterji*[4] as follows:

> ... It is now well settled that although persons are not entitled to an order ex debito justitae, the jurisdiction under section 38 is unlimited, with a discretion in the Court in the circumstances of each case. In support of this proposition, reference may be made to the decisions.[5] In a simple case where an immediate rectification is essential, it may be desirable to apply under the section, but if the case is at all complicated, an action should be brought. The respondent has, however, argued that section 38 does not authorise the Court to consider a dispute between a member and a stranger....We are of the opinion that we should not adopt this narrow interpretation of the section. The Legislature obviously intended that the Court should have the widest possible power to determine, in its discretion, question which may appear to it to be necessary or expedient for decision before an order for rectification is made or refused.
>
> ... we have no doubt that the provisions of section 38 of the Companies Act are very wide, and in appropriate cases give a judge dealing with Company matters a very wide discretion in granting speedy relief to the holder of shares, as it has been held in *ExParte A.R. Shaw's case,*[6] and also in a number of cases. It is not necessary for the Court to find that there has been actual default on the part of the Company, and even in cases other than that of default of the Company under section 38 the Court has ample scope and power to grant relief, and save the parties from being harassed, and unnecessarily relegated to protracted litigation in a simple

1 18 DLR(1966) 109.

2 Ahmed Impex (Private) Ltd. vs. Moqbul Ahmed 56 DLR (AD) 92.

3 7 PLR (Dac) 159.

4 I.L.R. 47 Cal 901

5 In Re Kimberley North Block Diamond Company(1888) 59 L.T. 579, In re Ruby Consolidated Mining Company (1874) 43 L.J. Ch 633,In re Sussex Brick Company [1904] 1 Ch. 598, and In re Gresham Life Assurance Society (1872) 42 L.J. Ch 183.

6 (1877) 2 Q.B.D. 463.

> case. It has even been held that the jurisdiction given to the Court under section 38 of the Companies Act, is not limited to the cases mentioned in this section.....Buckley on the Companies Acts, 12th Edition at page 261 says : When there is no dispute as to a person being, or having ceased to be, a member, the summary jurisdiction under this section (i.e.,the corresponding section in the English Companies Act) to compel the Company to perform the ministerial duty of entering the fact on the register is clear...As between alleged shareholders and the Company, there are numerous cases in which this section has been used for determining the equities, although, if the case be one of difficulty and complication, the Court may refuse the motion without prejudice to an action being brought. As between the applicant and the Company, the court will' enforce the ministerial duty if the applicant shews a clear right, and will not readily refuse to proceed and leave an action to be brought.

This case has been cited in numerous cases of the High Court mostly when the Court wanted to intervene but sometimes also when the Court did not want to intervene. If the Court does not consider the matter as a simple one, then it is a matter of the Court's discretion.[1] In *Monzurur Rahman vs Rema Tea Co Ltd,*[2] the Court held that a proceeding under section 38(3) of the Companies Act is a special proceeding before the High Court Division of the Supreme Court and this proceeding is not in the nature of a suit as contemplated under section 9 of the Code of Civil Procedure. The forum for the adjudication of any dispute under section 38 of the Companies Act exclusively vests with the Original Side of the High Court Division of the Supreme Court in view of the clear provisions of sub-section (1) of section 3 of the Companies Act. The Court proceeded to exercise its jurisdiction to give effect to a division of the shares held jointly when the company failed to effect such division. In *Shoaib vs Uttara Bank Ltd,*[3] the learned company judge cited the decisions given in *United Planters case*[4] *and Anath Bandhu's case*[5] and agreed with the submissions of the lawyer for the petitioner that the jurisdiction of the Company Court was sufficiently wide for him to intervene in a case where the company did not recognise the purchase of shares and gave three reasons for such refusal. The same judge referred to the same decisions cited above in the case of *Sher Ali Amir Ali Virjee vs Eastern Industries (Bangladesh) Ltd*[6] and held that if a dispute could not be resolved without resorting to any other means excepting the papers and documents filed before the Court, the question might arise whether such an application would be maintainable or not. In the case before him he intervened to give relief to an applicant 'who produced only the instrument of transfer and not the share scrip. The learned judge continued his exposition of the law relating to section 38 of the Act of 1913 in the case of *Mohiuddin Ahmed vs Lutfur Rahman.*[7] He held that he could intervene to rectify the share register of a company as per the terms of an agreement although the company was not a party to the agreement. He said :

> ... In the case of Sirish Chandra Das vs SriSri Chatteswari Debi Bigraha,[8] it is held that the consenting parties have got right to challenge the document if it is otherwise illegal. In the present case since the petitioner Nos 2-5 are consenting parties and since they have been aggrieved for non-fulfillment of the terms of the agreements by the respondent No 1 they are also considered as aggrieved persons to come before this Court under section 38 of the Companies Act... In every case the facts will be disputed as one party will allege and the other party will deny. But from the materials available on record and on the basis of the facts which in fact cannot be disputed, this Court can decide the matter under section 38 of the Act. No doubt it is a summary proceeding under section 38 of the Act but it is a discretion of the Court to see whether the point at issue can be disposed of and resolved on the basis of the materials on record. If the case is complicated and very doubtful and if it appears that without resorting to some other procedure a case cannot be disposed of, this Court should not interfere with

1 United Planters Traders Ltd. vs Md Mosharraf Hossain Khan (1982) 34 DLR 345.
2 33 DLR (1981) 49.
3 43 DLR(1991) 329
4 34 DLR 345.
5 7 PLR (Dac) 159
6 43 DLR 55.
7 44 DLR(1992) 48.
8 38 DLR(AD)283.

such a matter. But if it is apparent on the face of the records that legal rights of the parties are clear and the same can be settled on the basis of the materials on record, then this Court can interfere with the matter under section 38 of the Act....

His Lordship cited with approval the case of *AR Shaw vs The Diamond Rock Boring Co Ltd*[1] where the English Lords thought that the legislature intended to give the Court jurisdiction to make an order so as to decide questions of title, trusting to the discretion of the Court not to decide in this summary manner any intricate or difficult question of title; but that, if the Court thinks fit, they have jurisdiction to make the order in all cases.

The Court also discussed the case of *Anath Bandhu Guha and Sons Ltd*[2] to hold that he could exercise jurisdiction although there were denials by one party to the allegations of another.

The same judge held in the case of *Rowshan Ara Begum and others vs Doctor's Chemical Works Ltd*[3] that when papers and documents filed by the parties were sufficient to settle their rights and interests, the jurisdiction of the Company Court was sufficiently wide to resolve the question of rectification of shares.

Although section 43 gives the High Court Division a wide jurisdiction to settle disputes between the claimants it is well settled that a suit in the civil court is not barred thereby, especially when detailed evidence is to be taken to settle issue of fact.[4] The Court has power to decide any question relating to the title of any person who is a party to the application. When the company cannot produce an instrument of transfer, and the share scrip is with the shareholder the company did not discharge the burden of proof of transfer.[5]

In the case of *Investment Corporation of Bangladesh vs Bata Shoe Company*[6] the Court held that it was not correct to say that shares could be transferred only to an individual and not to any juristic person, because the latter was not a citizen. The petitioner Investment Corporation of Bangladesh being a legal and juristic person was competent to purchase the shares in question on renunciation and there would be no bar for its authorised officer to fill up the form, a registration application, on behalf of the juristic person. The form had no legal effect and could be written according to the requirement for executing the document of transfer as necessary.

9.3.3 Rectification of shares cannot be granted when petitioner makes a case for winding up the company.[7] In that case the Court held that this was a fit case for winding up on the principle of partnership when fraud was practised and as such no benefit would be had if an application for rectification of the share register was made. In *Ellal Textile Mills vs Md. Abdul Awal*[8] the Appellate Division upheld the same principle. Two prayers, one for winding up of the company under section 162 and another for rectification of the share register in the same application made before the company judge, cannot be entertained. This section gives unlimited jurisdiction to the Court as to rectification of the register though there is a discretion as to whether it ought to be exercised under the circumstances of a particular case; it is well settled that where winding up order had intervened whereby rights of creditors were made paramount, application for rectification must be refused.[9] In Ibrahim Cotton Mills Ltd. and others vs The Chittagong Chamber of Commerce and Industry and others[10] an application to rectify share register of a trade organizations association under section 43 of the Companies Act was refused because there was a provision in the Articles to refer the matter to Arbitration Tribunal. Further when there is no legal right to freely transfer shares to outsiders rectification of share register may be rejected.[11]

1 [1877] 2 Q.B.D. 463.
2 7 PLR(Dac) 159.
3 44 DLR(H.C.D.)371.
4 Afruj Miah vs Al-Haj Md. Siraj Miah 43 DLR(AD)89.
5 Industrial Development Company Ltd. –vs–Sukendu Shekhar Mukherjee (1997) BLD (AD) 171 = 2 BLC (AD) 117.
6 43 DLR(1991) 487.
7 Md Ismail Siddique vs M/S Crescent Apparels. 43 DLR 99.
8 38 DLR (AD) 26=(1985) BLD (AD) 230.
9 ibid. at para 14 and 19.
10 19 BLD (HCD) 372
11 Golam Kibria vs Bangladesh Commerce Bank Ltd. and others 6 BLC (HCD) 747

9.3.4 There is no clear case law in this country whether section 43 providing for rectification of the share register contemplates an application for rectification of the share register by way of specific performance of contract. *Mohiuddin Ahmed vs Lutfur Rahman*[1] was a case where the petitioners prayed for rectification of the share register on the ground that they transferred their shares to the respondents on the basis of an agreement which the respondents failed to perform. The Court found as a finding of fact that the respondents failed to perform the agreement and exercised jurisdiction to entertain the matter. In paragraph 30 of the judgment the Court observed thus:

> Mr. Ishtiaq Ahmed further submits that the shares were duly transferred to the respondent No 1 by the petitioners under section 34 of the Companies Act. So it is a transaction passed and closed and it cannot be reopened. I am unable to accept the above submission of Mr. Ishtiaq Ahmed inasmuch as the above transfer of shares by the petitioners was subject to the terms and conditions of the agreements.

The question remains as to what happens if the petitioner prays for a rectification of the share register on the ground that the respondent had agreed to transfer the shares to the petitioner for a consideration but is now refusing to do so although the petitioner is ready and willing to perform his part of the contract.

The English commentators and judges do not find anything wrong with the idea of a contract to sell shares which may be specifically enforced. In fact, that the agreement is subject to fulfillment of a condition beyond the control of the parties will not prevent it from being specifically enforceable, notwithstanding that the condition has not been fulfilled, if the party for whose benefit the condition was inserted is prepared to waive it.[2] In *Wood Preservation Ltd vs Price,*[3] where the condition was for the benefit of the buyer, the Court was prepared to hold that the seller ceased to be "the beneficial owner" on the date of the contract notwithstanding that the buyer did not become the beneficial owner until he later waived the condition. While it is not lawful for the company to register a transfer of shares unless the instrument of transfer duly stamped and signed by the transferor and transferee is lodged with the company along with the share scrip the power of the Court under section 43 is wider.[4]

9.3.5 The transferee does not become a shareholder until and unless his name is entered in the share register. The transaction involves three stages : (1) an agreement, (2) delivery of the signed transfer and the certificate by the seller and payment of the consideration by the buyer and (3) lodgment of the transfer for registration by the company. Even if the transfer is not lodged for registration or registration is refused, the beneficial interest in the shares will, it seems, pass from the seller to the buyer at the latest at stage (2) and, indeed will do so at the stage (1) if the agreement is one which the Courts would order to be specifically enforced.[5] The seller then becomes a trustee for the buyer and must account to him for the buyer and must account to him for any dividends he receives and vote in accordance with his instructions or appoint him as his proxy. If however, the payment for the shares is to be done in instalments then the Court will refuse to register the transfer until full payment is made for the shares. Although an equitable interest will pass to the buyer the Courts will protect the seller's lien and he will be entitled to vote as he thinks will best protect his interest.[6] Transferor holds shares in trust for transferee and dividends paid to transferor and the right to vote belongs to the transferee who may direct transferor to vote.[7]

The next question that arises is what happens when there is a right of pre emption under the articles by which shares must first be offered to other shareholders. The House of Lords observed in *Hunter vs Hunter*[8] that as this transaction is in contravention of the implied

1 44 DLR 48.
2 Gower's Principles of Modern Company Law 5th Ed p.399.
3 [1969] 1 W.L.R. 1077,C.A.
4 Sudhangsu Shekhar vs Anath Bandhu 28 DLR(1976) 315, section 9.2.3 ante.
5 Gower ibid.
6 Musselwhite vs Musselwhite & Sons Ltd [1962] Ch. 964.
7 AIR 1953 SC 385; AIR 1956 SC 655; AIR 1959 SC 775.
8 [1936] A.C.222

contract with the company under the articles so it is void. However, in later cases[1] the Courts have refused to follow this line of thinking and Professor Gower comments[2] that it must surely be right, at any rate if the price has been paid, that the buyer obtains such rights as the seller had, although this may not be of much help to him if all the shares sold are subject to pre emption.[3]

When the transaction is not a sale but a gift there need be no agreement. If the donor has chosen to make the gift by handing to the donee a signed transfer and the share certificate, rather than by a formal declaration of trust in favour of the donee, the gift would not be effective unless and until the transfer is registered. In two English cases of the same name, i.e., *Re Rose*[4] it has been held that so long as the donor has done all he needs to do, the beneficial interest passes from him to the donee.

9.3.5.1 **Damages** – Section 43(3) gives Court the power to award damages while rectifying the share register. However, if a party does not seek damages while filing a petition for rectification of share register and gets an order of rectification he may file a fresh civil suit for realisation of damages and this claim for damages will not be barred under Order 2 rule 2 of the Code of Civil Procedure because an application for rectification of share register is not a suit.[5]

9.3.6 **Share Warrants** – Section 46 provides that if a company, if so authorised by its articles, may issue with respect to any fully paid shares a warrant stating that the bearer of the warrant is entitled to the shares specified in it: If similarly authorised, it may provide, by coupons attached to the warrant or otherwise, for the payment of future dividends. Title to the shares specified then passes by manual delivery of the warrant which is a negotiable instrument.[6] On their issue, the company removes from its register of members the name of the former registered holder and merely states the fact and date of issue of the warrant and the number of shares or amount of stock to which it relates.[7] The bearer of the warrant from time to time is a shareholder but to what extent if at all, he is a member of the company depends on a provision to that effect in the articles.[8] Hence shareholding and membership are not necessarily co-terminous if share warrants are issued. However, again subject to the articles , the bearer of the warrant is entitled, on surrendering it for cancellation, to have his name and shareholding re-entered on the register and the company shall be responsible for any loss incurred by any person by reason of the company entering in its register the name of a bearer of a share warrant in respect of the shares or stock therein specified without the warrant being surrendered and cancelled.[9] In Australia under the Corporations Law[10] companies are prohibited from issuing share warrants, mainly to look after the interests of the State governments to raise revenue by stamp duty on transfers of shares. In Bangladesh although the law allows the issue of share warrants if the articles so provide, in practice it is rare to find the use of share warrants.

9.3.7 **Reduction of Share Capital** – Sections 58 to 70 of the Companies Act 1994 provide for reduction of share capital. The law proceeds on three assumptions :

a) A company cannot buy or finance the purchase of its own shares (Section 58);

b) The articles must provide for such reduction; if the articles do not do so these will have to be amended to insert such a provision; the resolution sanctioning the reduction must be passed by a special resolution (section 59);

c) The Court must sanction the reduction; while doing so the Court will look to safeguard the interests of the creditors.

1 Hawks vs MacArthur [1951] 1 All E.R. 22.
2 5th Ed. P. 399.
3 See also Niranjan Dey and others vs Dey Chemical Works Ltd (1994) Company Matter No 8 of 1993 affirmed by the division bench at (1995) DLR 423.
4 [1949] Ch.78 and [1952] Ch 499 C.A.
5 Dhaka Stock Exchange and others vs Motiur Rahman, 7 BLC (HCD) 150. Note: In the law report the reference to Order 2 rule 2 CPC has been wrongly reported as Order XI rule 2.
6 section 47.
7 section 50.
8 section 49.
9 section 48.
10 section 189.

9.3.8 The Courts have always been anxious to keep the capital of the company intact for "the creditor gives credit to that capital; gives credit to the company on the faith of the representation that the capital shall be applied only for the purpose of the business and, therefore, has a right to say that the corporation shall keep its capital and not return it to the shareholders."[1] The House of Lords held that the company could not purchase its own shares, even though there was a provision to that effect in the memorandum of association since this would result in a reduction of share capital.[2] This was a much more strict principle than followed in some common law countries like the U.S.A. and Canada. Even in England the objection did not apply if, for example, the shares were given to the company and held by a nominee for it.[3] In *Kirby vs Wilkins*[4] four partners sold their business to a company and the purchase price was satisfied by the company allotting them 16,000 shares fully-paid to one pound each. Later it was found that the value of stock in trade in the business had been over-stated and that the company had paid 3000 punds too much. Wanting to put the matter right, the vendors transferred 3000 shares to the chairman of the company to be held on trust for the company. This was regarded as a voluntary act on the basis that the company had no cause of action to recover that money from the vendors. There was argument that the trust was invalid as offending the principle in *Trevor vs Whitworth.*[5] However Romer J. held that as no consideration moved from the company for the acquisition of the company's equitable interest as beneficiary, the case was outside the prohibition on purchasing. The company could not call on the trustee for a transfer of the legal title to the shares since the company could not become a member of itself. It was not illegal for the company to direct the chairman as to how votes attached to the shares should be cast. In Australia a company may acquire an interest other than a legal interest in fully paid shares in the company where no consideration is provided by the company, or by any related corporation, for the acquisition.[6]

Section 58 of our Companies Act provides that no company limited by shares shall have power to buy its own shares or the shares of a public company of which it is a subsidiary company unless the consequent reduction of capital is effected and sanctioned in the manner provided by sections 59 to 70. No company limited by shares other than a private company, not being a subsidiary company of a public company, shall give, whether directly or indirectly, and whether by means of a loan, guarantee, the provision of security or otherwise any financial assistance for the purpose of or in connection with a purchase made or to be made by any person of any shares in the company. Nothing in the section shall affect the rights of a company to redeem any shares issued under section 155. Presumably the forfeiture of shares under the articles for non-payment of call money will also be outside the restriction of the law.

9.3.9. Section 59 provides that subject to confirmation by the Court, a company limited by shares if so authorised by its articles, may by special resolution reduce its share capital in any way, and in particular without prejudice to the generality of the foregoing power may –

a) extinguish or reduce the liability on any of its shares in respect of share capital not paid up ; or

b) either with or without extinguishing or reducing liability on any of its shares, cancel any paid up share capital which is lost or unrepresented by available assets; or

c) either with or without extinguishing or reducing liability on any of its shares, pay off any paid up share capital which is in excess of the wants of the company, and may if and so far as is necessary, alter its memorandum by reducing the amount of its share capital and of its shares accordingly.

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1 Jessel M.R. in Flitcroft's Case (1882) 21 Ch.D. 519.
2 Trevor vs Whitworth (1887) 12 App. Cas 409.
3 Re Castiglione's Will Trust [1958] Ch 549.
4 [1929] 2 Ch 444.
5 (1887) 12 App Cas 409.
6 Section 205(8)(e) of the Corporations Law of Australia.

Where shares issued to Shilpa Bank were redeemed on payment of the loan a reduction of share capital took place.[1]

Sections 60-63 of the Act provide for application to the Court and the power of the Court to safeguard the interests of the creditors. A company will have to use the words "and reduced" after its name but the Court may dispense with the addition of the words 'and reduced' after the name of the company where the reduction involves either the diminution of any liability in respect of unpaid share capital or the payment to the shareholder of any paid up share capital. Where the creditors object, the Court shall settle a list of creditors so entitled to object, and for that purpose shall ascertain, as far as possible without requiring an application from any creditor, the names of those creditors and the nature and amount of their debts or claims and may publish notices fixing a day within which creditors not in the list are to claim to be entered in the list of objectors.[1A] Where the creditor whose name is in the list of the creditors objects to the reduction of share capital the Court may dispense with the objection on the company providing security for the creditor.[2] The Court, if satisfied that every creditor has either given his consent or his credit has been secured or his debt has been discharged, may make an order confirming the reduction on such terms and conditions as it thinks fit.[3] While considering the application for sanction of the reduction of share capital the Court may require the company to publish the reasons for reduction with a view to give proper information to the public.[4] The Registrar, on production of the order of the Court and of a minute approved by the Court, showing with respect to the share capital of the company as altered by the order, the amount of the share capital, the number of shares into which it is divided and the amount of each share and the amount, if any, at the date of the registration deemed to be paid up on each share, shall register the order and minute. On such registration the resolution for reducing the share capital shall take effect.[5] Such minute shall form part of the memorandum and the shareholders will have reduced liability to that extent.[6] There is a penalty of imprisonment which may extend upto two years or with fine or both, for any officer of the company who willingly conceals the name of a creditor.[7]

9.3.10 The prescribed majority of the shareholders are entitled to determine whether there should be a reduction of capital and if so in what manner and to what extent it should be carried into effect.[8] The Court may sanction a reduction of capital without insisting on proof of loss of capital but where the petition is based on this ground, the Court will insist on at least a prima facie proof of loss of capital.[9] Capital is not lost unless it is permanently lost.[10] Subject to the confirmation of the Court which is required for safeguarding the interests of creditors and minority shareholders and seeing that it is fair and reasonable, the question of reducing the capital is a domestic affair to be decided by the majority, and the Act leaves the company to decide for itself the extent, mode etc of the reduction and the application of the monies released thereby.[11] Lord Simond said in *Scottish Insurance Corporation vs Wilson & Clyde Coal Co Ltd*[12] that 'important though its task is to see that the procedure, by which a

1 Uttara Himghar Limited 6 BLC (HCD) 173 = 8 BLT (HCD) 331. 1A. Section 62 of the Act.
2 Section 63 of the Act.
3 Section 64 of the Act.
4 Section 69 of the Act.
5 Section 65 of the Act.
6 Sections 66 and 67 of the Act.
7 Section 68 of the Act.
8 British & American Trustee and Finance Corporation vs Couper [1894] A.C. 399;Poole vs National Bank of China [1907] A.C. 229;Caldwell and Co vs Caldwell [1916] SC(HL) 120;Re De La Rue(Thomas) & Co Ltd,[1911] 2 Ch.361 and Lord Normand in Westburn Sugar Refineries Ltd [1951] 1 All E.R. 881(HL).
9 Caldwell vs Caldwell and Co [1916] WN 70(HL); followed in Marwari Stores Ltd. vs Gouri Shankar Goenka (1935) 40 CWN 661.
10 Barrow Haematite Steel Co, In re [1901] 2 Ch 746; Welsbach Incandescent Gas Light Co Ltd, In re [1904] 1 Ch 87.
11 Hindustan Commercial Bank Ltd vs Hindustan General Electric Corporation AIR 1960 Cal 637.
12 [1949] 1 All E.R. 1068 HL.

resolution is carried through, is formally correct and that creditors are not prejudiced; it has the further duty of satisfying itself that the scheme is fair and equitable between the different classes of shareholders'. An injunction may be sought against the directors if they illegally proceed to effect a reduction of capital.[1] There may be a reduction for paying off one class of shareholders, e.g. preference shareholders.[2] The Court will see whether the reduction is fair and equitable, though it will not be concerned with the motive for the reduction such as the intention to avoid the effects of a threatened nationalisation, or avoid or diminish tax liability or estate duty.[3] The Court can sanction a reduction even if it amounts to a variation of class rights if the regulations are complied with and those voting believed that they were acting bonafide in the interests of the general body of that class.[4] The court cannot sanction a scheme which can be effected under some other provisions of the Companies Act.[5]

1 Holmes vs Newcastle -upon-Tyne Free-hold Abatror Co [1875] 1 Ch.D 682; Hope vs International Financial Society [1876] 4 ChD 327.

2 Scottish Insurance Corporation Ltd vs Wilsons and Clyde Coal Co Ltd [1949] 1 All E.R. 1068(HL);Re Chatterley-Whitefield Collieries Co Ltd [1948] 2 All E R 593 CA and [1949] 1 All E R 1094(HL), or for paying off one set of shareholders like foreign share holders; British and American Trustee and Finance Corporation vs Couper [1894] A.C. 399.

3 Exparte Westburn Sugar Refineries Ltd[1951] 1 All ER 881 (HL) and Re Panruti Industrial Co. AIR 1960 Mad 537.

4 In re Holders Investment Trust Ltd. [1971] 2 All E R 289.

5 Pennington's Company Law 5th Ed 1985 page 586.

MANAGEMENT AND ADMINISTRATION

10.1 **Registered Office of the Companies** – Section 77 of the Companies Act 1994 requires all companies to maintain a registered office within twenty eight days from the date of its incorporation to which all communications and notices may be addresed. Notice of the situation of the registered office and of any change therein shall be given within twenty days after the date of the incorporation of the company or of the change, as the case may be to the Registrar, who shall record the same. For this purpose, the inclusion in the annual return of the company of the statement as to the address of the registered office shall not be taken to satisfy the statutory obligation . The penalty is a continuing fine of upto two hundred taka for every day the company carries on business without complying with the legal requirements.[1]

The situation of the registered office of a company determines its domicile for all purposes.[2] The Companies Act does not provide for the transfer of a registered office of a company from one country to another. All that the Act permits is the movement of the registered office of the company within the same sovereign state from one province to another and from one district to another. If the removal of the registered office is from the jurisdiction of one High Court to another within the same country, the company has to obtain permission from the High Court within whose jurisdiction the registered office was situate.[3] That same case also decided that change of the registered office of the company was not permissible without the sanction of the High Court and notice of any change could not be effected by collateral document.

10.1.1 **General Meetings** – Sections 81-89 of the Companies Act 1994 deal with meetings and proceedings of the company. The provisions are broadly similar to those in the Act of 1913 but some changes have been introduced in the light of the recommendations of the Report of the Company Law Reforms Committee, 1979, and the experience of other countries.

Section 81 provides that every company must hold a general meeting called the annual general meeting every year but so that not more than fifteen months elapse between the meetings. A company must hold the first annual general meeting within eighteen months of its incorporation. The Registrar has been given the power to extend the time for holding such meetings if an application is made within one month from the date of expiry of the period specified for holding such meetings but no such extension shall exceed the 31st day of December of the year in which the meeting was scheduled to be held. This provision is new and is meant to give relief to parties who do not want to go to the Court if they have bonafide missed holding such meetings. Section 81 further provides that the Court may, on the

1 Section 77(4) of the Act.

2 Daimler Co Ltd. vs Continental Tyre and Rubber Co Ltd [1916] 2 A.C. 307.Gasque vs I.R.C. [1940] 2 K.B. 80.

3 Shakhawat Hossain vs Chittaranjan Cotton Mills Ltd (1962) 14 DLR 407.

application of any member of the company, call or direct the calling of a general meeting of the company and give such ancillary or consequential direction as the Court thinks expedient in relation to the calling , holding and conducting of the meeting. Section 82 provides for a fine not exceeding take ten thousand and a continuing fine which may extend upto two hundred fifty taka for every day that the default continues.

10.1.2 The power of the Court to call or direct the calling of a general meeting should be read with the power of the Court given under section 85(3) of the Act. If for any reason it is impracticable to call a meeting of the company in the manner in which meetings of that company may be called or conducted in the manner prescribed by the articles or the Act the Court may, either on its own motion or on the application of any director or member who would be entitled to vote at the meeting, order a meeting of the company to be called, conducted and held in such a manner as the Court thinks fit, and may give such ancillary or consequential directions as it thinks expedient, and any meeting held and conducted in accordance with any such order shall for all purposes be deemed to be a meeting of the company duly called, held and conducted. There has been some extensive case law in this country touching disputes among shareholders for control of the company. These will be discussed below (section 10.1.4).

10.1.3 The Act requires a public company to hold a statutory meeting within a period of not less than one month nor more than six months from the date at which the company is entitled to commence business . A report known as a statutory report shall have to be sent twenty one days before the meeting with the Registrar. The statutory report shall state certain basic facts about the company like the number of shares allotted, total amount of cash received showing the heads they are so received , the names , address and occupations of the directors, managing agents, managers and secretaries , the particulars of any contract which should be submitted to the company for approval, the extent to which underwriting contract if any has not been carried out, the arrears if any due on calls from every director, managing agent etc, and the particulars of any commission , brokerage etc paid or to be paid in connection with the issue or sale of shares or debentures to any director and managing agent. The statutory report has to be certified by at least two directors including the managing director. The report shall have to be certified by the auditors of the company so far as shares allotted by the company and the cash received by the company are concerned. The report shall have to be filed with the Registrar of Joint Stock Companies. The directors shall cause a list showing the names, addresses and occupation of the members of the company and the number of shares held by them respectively. A company may be wound up if default is made in holding the statutory meeting or in filing the statutory report,[1] but the Court, on a petition made to it, may instead of directing that the company be wound up give directions for the statutory report to be filed.[2]

Section 84 requires the directors to call an extraordinary general meeting on the requisition of holders of not less than one tenth of the issued share capital of the company upon which all calls have been made. The requisition must state the objects of the meeting and must be signed and deposited at the registered office of the company by the requisitionists. If the directors do not, within twenty one days from the date of deposit of the requisition, proceed to call a meeting on a day not later than forty five days from the date of the requisition , then the requisitionists or a majority of them in value, may themselves call the meeting but any meeting shall not be held after the expiration of three months from the date of the requisition.

1 (Section 241).
2 Section 83(10).

10.1.4 Complaint for not holding annual general meetings cannot be made directly to the High Court. The application made direct to the High Court for taking penal action was untenable and misconceived. The High Court would have jurisdiction to try the accused if the case is committed to the High Court under section 194(1) Cr. P.C. or if the proceedings are started on an application of the Attorney General under section 195(2) Cr. P.C. or are transferred to it under section 526 Cr.P.C.[1] The Dhaka High Court has held that the High Court Division can in exercise of its powers to call a meeting under section 79(3) of the Act of 1913 (equivalent to section 85(3) of the present Act) allow annual general meeting of the company to be held within fifteen months from the date of the previous annual general meeting and that sections 76 and 79(3) of the Act of 1913 corresponding to sections 81 and 85 of the Act of 1994, are supplementary to each other.[2] The legislature recognises that there may be circumstances in which the holding of the annual general meeting cannot be held within time. The legislature has therefore bestowed on the Court the power to direct that such a meeting of the company be called held, and conducted in such a manner as the Court thinks fit. In this, the Court can act not only on an application of any director of the company or of a member of the company but also suo moto.. In directing the holding of such a meeting the Court is to "look to the general interest of the public and not to any individual consideration."[3] The Court while deciding on an application under section 85(3) of the Act is not required to adjudicate on an allegation about the misdoings of the President.[4] A member of a company which has separate legal entity is entitled to apply to the court under section 85(3) of the Act for calling an annual general meeting.[5] Where meeting could not be held in compliance with the manner prescribed by the Articles, the court ordered that delay in holding the first general meeting be condoned.[6] In exercising the powers under section 85(3) the Court will look at the facts from a reasonable commonsense point of view and as a prudent person of business to decide whether it has become impracticable to call a general meeting and in normal circumstances should not supersede the rights of shareholders.[7]

10.1.5 A division bench of the High Court Division observed in *BCIC vs Registrar of Joint Stock Companies*[8] that the words "not more than 15 months after holding of the last preceding general meeting" can be interpreted in two different ways. When a company does not hold its annual general meeting within eighteen months of incorporation and thereafter fails to hold its successive annual general meetings the company is in perennial default and its statutory legal obligation commences from the date when the last general meeting ought to have been held in accordance with the statutory provision. If no meeting was actually held time would run from the date when the meeting fell due, in terms of the statute. But when the company has actually held its last preceding annual general meeting within the time extended by the High Court Division, the legal obligation to hold the next general meeting will start from the date when the meeting was actually held. The petitioner Bangladesh Chemical Industries Corporation controlled the Sylhet Pulp and Paper Mills Ltd. which failed to hold its annual general meeting within the prescribed time .The company approached the High Court Division and obtained extension of time to hold the meeting. The company held the meeting within the time extended by the Court but when it held the next annual general meeting the Registrar's office verbally told that the return would not be accepted because that meeting was not held within fifteen months of the time the previous meeting ought to have been held. The Registrar's office counted the time from the day the meeting ought to have been held before its extension by the High Court. According to Mr. Justice Mustafa Kamal delivering the judgment of the Court the words " after the holding of the last preceding general meeting" clearly postulate the actual holding of a meeting. The condonation of delay

1 Muhammad Azhar Hossain vs District Cricket Assocn (1969) 21 DLR(WP) 204.
2 Manipur Tea Company Ltd. vs Ahmedur Rahman (1975) 27 DLR 490.
3 Ahmed Hossain vs Syedur Rahman (1966) 18 DLR 506.
4 ibid.
5 A.S.A.Nur vs Registrar of Joint Stock Company (1981) 33 DLR (AD) 315.
6 In the matter of Bangthai Electrical Industries Ltd 1984 BCR (HCD) 72.
7 Jahangir Alam Khan vs. Registrar of Joint Stock Companies and others. 55 DLR 495 = 7 BLC (HCD) 458 = 23 BLD (HCD) 449.
8 (1987) DLR (HC) 1

has the effect of wiping out the fixed schedules of the annual general meetings. A new schedule starts along with the actual holding of the annual general meeting in accordance with the directions of the High Court Division.

This case is however better known for the discussion that the Court laid down on the powers of the Registrar to withhold acceptance of an annual return. Mr. Justice Mustafa Kamal in his usual forthright manner discussed and held as under :

> Dr M. Zahir however has raised a fundamental objection with regard to the power and authority of the Registrar of Joint Companies to withhold acceptance of an annual return. He submits that in the Companies Act there is no provision whatsoever authorising or empowering the Registrar of Joint Stock Companies to withhold, delay or refuse acceptance of any filing or return. The Registrar has no authority to arrogate to himself the power of judging the validity of a return....Indeed we find no authority for the proposition that the Registrar can withhold acceptance of an annual return submitted by a company under section 32 of the Companies Act until it satisfies the Registrar that its annual general meeting was held within the scheduled period. Under section 131 of the Companies Act the directors of every company have a legal obligation to lay before the company in general meeting a balance sheet and profit and loss account once at least in every calendar year. The Registrar has the power to extend the period by a maximum of 3 (three) months for any special reason, but section 131 has to be read with section 76 and once the High Court Division condones the delay in holding annual general meetings, the submission of balance sheet and profit and loss account will also follow the altered schedule. Those will be submitted as and when the next annual general meeting will be due. Even section 131 does not authorise the Registrar to withhold acceptance of any return. We are of the opinion that the Registrar has no option but to accept the filing made by the petitioner . The law does not authorise him to act as mini-Court to impose his own judgment as to when a general meeting is due. It is his function to operate as a filing house and if he is of the opinion that any company has violated the provision of section 76(1) of the Companies Act, he is certainly within his powers to initiate appropriate legal proceedings against it and its directors/ managers under section 76(2) of the Companies Act. The annual return filed by the company will itself be a piece of evidence against it and its directors/ managers. He cannot, however, withhold acceptance of any filing.

This decision was followed in *Fazal Mahmud vs Pioneer Printing Press.*[1] A single bench of the High Court Division felt bound by the above judgment when an argument was raised at the bar that the Registrar had jurisdiction in the manner to examine the question of the validity of holding annual general meetings .The single bench agreed with the advocate for the respondents that the condonation of delay had the effect of wiping out of the schedule for the annual general meeting provided for in section 76(1) of the Companies Act and a new schedule would start with the actual holding of the annual general meeting in accordance with the direction of the High Court Division. The period of 15 months, therefore, should be counted from that date of holding the last annual general meeting.

Justice Hamoodur Rahman in the case of *Muhammad Idrish vs East Pakistan Timber Merchants Group*[2] however commented that section 137 of the Act of 1913 (corresponding to section 193 of the current Act) empowered the Registrar to call on the person submitting his document to furnish information or explanation and that this did not indicate that he was a mere automation and had no duty to discharge in relation to those matters. The Companies Act provided special procedures for the change of name of a company, alteration of the memorandum and articles of association , special resolutions, annual general meetings, notices etc, which have of necessity to be followed to make an act of a company valid and it was incumbent upon the Registrar to see that the provisions were complied with. These provisions cast a duty upon the Registrar of Joint Stock Companies also to see that the requirements of the Companies Act were complied with. There was nothing in the Companies Act which prohibited the Registrar from refusing to file such information.

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1 41 DLR 529. Also see The City Bank Limited vs The Registrar, Joint Stock Companies and others 21 BLD (HCD) 495 = 6 BLC (HCD) 479

2 PLD (1968) SC 412.

Similar comments were made by a division bench of the Dacca High Court in *The East Pakistan Timber Merchants Group, Chittagong vs The Registrar*[1] when it observed, following the decision in *Abdur Rab Choudhury vs Registrar*[2] that on a reference to section 137 of the Companies Act (Act of 1913) equivalent to section 193 of the present Act it was apparent that the Registrar fulfilled a quasi-judicial function and he was authorised to make such investigations as might be found necessary for a proper discharge of his duties.[3]

With all respect to Justice Hamoodur Rahman and the other judges of the East Pakistan High Court it is submitted that the language of section 88 of the current Act clearly enjoins upon the Registrar a duty to record the filing of a copy of a special or extraordinary resolution. The Registrar must allow the same to be filed. He certainly has the option to call for further documents but only when information or explanation is necessary in order that such document may afford full particulars of the matter to which the filing purports to relate. Once the company has filed the documents these should be in the office of the Registrar. If the Registrar finds that further information is necessary then only he will ask for documents or explanation. Until that is done or a representation is made to him that the business of a company are being carried on in fraud of its members the Registrar's office should have no concern with the filings. The current practice of certifying that the documents filed are "Under Scrutiny" has no meaning because in any event the Registrar has no power to declare on the validity of a document filed. He may ask for an explanation etc, but must refer the matter to the Government for investigation. He cannot act as a mini Court as held rightly by the division bench. When authorised, he may do so. He may thus refuse to register a name because the Act empowers him to scrutinise the name and reject these in certain circumstances.

In Bangladesh the pioneering case on the law relating to annual general meetings was Satish Chandra Banik and others vs Dacca Jute Mills Ltd and others.[4] Some shareholders challenged the validity of the annual general meeting of Dacca Jute Mills Ltd. alleging that the provisions of the articles of association were not observed and that the person who presided at the meeting was not qualified to do so having already been due to retire and not being re elected. They prayed for a fresh meeting of the company to be held under the supervision of the Court under section 76(3) and 79(3) of the Companies Act of 1913. No poll was held although demanded by the petitioners and 15 persons were elected as directors who were unknown to the petitioners. The petitioners were the majority, holding 57% of the share capital.

The Court noted that the Chairman of the meeting being the oldest member of the Board should have retired and also that he was an ex-officio director of the company representing the EPIDC but found that only the managing agent of the company (not EPIDC in this case) could appoint ex-officio directors under the articles of the company which required the longest serving director to retire at the annual general meeting. A director representing EPIDC could be a director without having the qualification shares since EPIDC had the qualification shares but under the articles only the managing agent could appoint an ex-officio director. Mr. Hafizullah who presided over the meeting might have been a de facto director but the immunity continued only till it was challenged. The Chairman of the meeting not being a director could not have presided at the annual general meeting and the entire proceedings were struck down as being a nullity. The annual general meeting also suffered from the illegality in that it did not include an agenda for approval of the new management. (With all respect to the learned judge, this is not an agenda that must be decided at the annual general meeting!). The Court then dealt with the effect of not holding the meeting. Relying

1 PLD(1968) Dac 211.
2 PLD(1960) Dac 541.
3 Also see Mousel & Co vs Registrar PLD(1957) Dac 209 and section 10.1.7 below.
4 PLD(1968) Dac 610.

on the decision of the Allahabad High Court in *Bal Krishna Maheswari vs Uma Shankar Mehrotra*[1] it held that the statute required the holding of a valid meeting and mere holding of a meeting was not enough and in such a case there would be a default in holding the annual general meeting. Since there was keen rivalry between the two groups of shareholders the Court thought fit to exercise its jurisdiction to call a meeting under sections 76(3) and 79(3) of the Act of 1913 and commented that there was a dispute as to who would act as chairman of the meeting and that it would make it almost impossible for the shareholders to participate normally in an annual general meeting and ordered that a fresh meeting be held under the chairmanship of a practising Barrister at the registered office of the company. Mr. Justice Abdullah held thus :

> In my opinion the two sub-sections must be read in their own context. Section 76 provides for the first statutory (!) meeting and the Annual General Meeting. Subsection 3 gives the Court the power to enlarge the time for holding such a meeting and presupposes that a valid meeting can be called in accordance with the Articles of Association. Section 79 on the other hand provides the general procedure to be followed in case of all meetings including the Annual General Meeting. Section 76 is a special provision regarding the statutory(!) meeting and Annual General Meeting whereas section 79 is the general provision. Where there had been a default in the holding of an Annual General Meeting primarily the powers under section 76(3) of the Companies Act 1913 of the Court can be invoked. But in exercising the powers under section 76, subsection (3) the Court will also have the powers conferred on it by section 79, sub-section (3). If due to inadvertence the Annual General Meeting of the Company could not be held within the period prescribed by the statute then the Court has power under section 76(3) to direct the calling of such an Annual General Meeting beyond the prescribed period provided that the meeting can otherwise be validly held but if a default has been made and it is impracticable in the circumstances to hold the meeting in accordance with the provisions of the Articles of Association the Court can exercise its powers under section 79(3) of the Act. In my opinion section 76 subsection (3) and section 79 subsection (3) of the Act are not exclusive but supplementary to each other....[2]

Similar Orders were passed in the event of rivalry between two groups of shareholders in the case of Jahangir Alam Khan vs Registrar, Joint Stock Companies and others.[3]

A division bench of the Dacca High Court held in *The East Pakistan Timber Merchants Group, Chittagong vs The Registrar*[4] that meeting of a company at a place other than mentioned in the memorandum and articles of association could not take place legally unless relevant article was amended. A single bench of the Karachi High Court held in *Capt.John Johnston vs G.B.Potts & Co Ltd*[5] that where articles required meetings to be called by directors and the two directors were at loggerheads, the Court, in circumstances, was justified to call extra ordinary general meeting and also could modify or supplement articles of association and thus prescribe the mode in which proxies could be used.

The law relating to Court's power in calling a general meeting was discussed by the Appellate Division in Ghyasuddin Ahmed vs Faruque.[6] Their lordships referred to a number of decisions and seemed to hold that the Court could interfere in a proper case but cautioned against interference in internal management. The respondents complained that the annual general meeting purportedly held by the managing director was invalid because it did not consider the accounts prepared by S.F. Ahmed & Co, Auditors who were nominated by the majority of the board of directors and the audit report prepared by another auditor was not sent to the respondents prior to the annual general meeting. The annual general meeting thus was not properly held. It was argued by the appellants that once annual general meeting was held, the Court should not interfere. As observations of the Appellate Division are binding on all courts in the country, the relevant portion of the judgment are given below:[7]

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1 AIR 1947 All 361.

2 The exclamation signs are by the author as the Act provides for statutory meetings elsewhere.

3 7 BLC (HCD) 458; 56 DLR (AD) 76; Also see Jalaluddin Jaffar Ali Husein vs Tahmid Ahmed 6 MLR (HCD) 53 = 52 DLR 141.

4 PLD (1968) Dac 211.

5 PLD(1967) Kar. 496.

6 38 DLR(AD) 296.

7 ibid. at pp 301-303.

...The learned Counsels then cited decisions of various Courts of this sub-continent in support of their respective contentions as to the proper extent and scope of the powers conferred upon the Company Court to order such meeting.

Referring to a number of decisions cited by counsel for appellant[1] and also by counsel for respondent[2] the Court continued :

16. On going through the affidavits and after hearing the submissions made by the parties' learned Counsels , both on facts and law, it appears that the essence of the controversy appears to be whether the Annual General Meeting of the Company ordered by the Company Judge imposing certain conditions as mentioned above is permissible. There is no dispute that powers conferred under sections 79(3) read with section 76(3) of the Companies Act to call such a meeting, are exercisable by the Court in the circumstances stated therein.

17. Decisions cited by the learned Counsels have considered a few principles as to the extent of such powers which may be referred to. In exercising such powers the Court has to regard what is provided in the Articles of the Company. The other constraint on the exercise of powers under the aforesaid provisions of law is that the Court should not ordinarily interfere with internal management of the Company. The provisions contained in the aforesaid sections are not mutually exclusive, but supplement each other. It is only when the Court in the particular circumstances of the case is of the view that it is impracticable to call a meeting, it could intervene and order such meeting to be held. Reasons why the powers so conferred should be used sparingly and with caution are that the court's neutrality may be seen to have become involved in the process and trying to participate in the management of the internal affairs of the company either as a shareholder or director of the Company. If necessary, the Court may, in exercise of the powers conferred by section 79(3), appoint an independent person to preside over such meeting. This may not be viewed as interference with the internal management of the Company. Impracticability of calling a meeting may not be equated with impossibility of calling such a meeting.

18. Having regard to the powers conferred under section 79(3), the Court may order a meeting of the Company in any of the circumstances mentioned therein, namely,

A) if for any reason it is impracticable to call a meeting of the company;

B) if for any reason it is impracticable to hold a meeting;

C) if for any reason it is impracticable to conduct the meeting.

19. On the happening of any or all of the circumstances as above the Court may order such meeting. Above all, before exercising powers conferred under section 79(3), the Court must be satisfied that it has been impracticable to call a meeting in the manner in which such a meeting is to be called.

20. in view of these principles enunciated in the decisions cited by the learned Counsels of the appellant and respondents, there remains no doubt about the powers of the Court to call a meeting of the Company when invoked by a shareholder or director of the Company under section 79(3) of the Act.

The Appellate Division in the above case ordered another general meeting of the company to be held to consider the balance sheet etc and to ratify the appointment of S.F.Ahmed & Co if so needed.[3]

Delay in holding Annual General Meeting was condoned as balance sheet and profit and loss account were not received.[4]

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1 Bengal and Assam Investors Ltd vs J.K.Eastern Industries Private Ltd. AIR 1956 Cal 658 at para 7 and 17; In re Ruttonjee & Co Ltd AIR (1969) Cal 550 at para 2 and 85; R.Rangachari vs S.Suppaiah, AIR 1976 SC 73 at para 6; Pasari Flour Mills. In the matter of AIR 1961
Madhya Pradesh 340; Satish Chandra Banik vs Dacca Jute Mills Ltd PLD(1968) Dac 610.

2 Mrs A Ananthalakshmi Ammal vs Tijin's Barytes, Asbestos and Paints Limited AIR 1952 Mad 60 at para 3;The Indian Spinning Mills Ltd vs His Excellency General Madan Shamsher Jang Bahadur Rana AIR 1953 Cal 335 at para 21;Bal Krishna Maheshwari vs Uma Shanker Mehrotra AIR 1947 All 361; Bengal and Assam Investors Ltd vs J.K. Eastern Industries Private Ltd AIR1956 Cal 658; Re El Sombrero Ltd. [1958] 3 All E.R. p.1;Captain John Johnston vs G.B.Potts & Co Ltd. PLD(1967) Kar 496;Satish Chandra Banik vs Dacca Jute Mills Ltd. PLD (1968) Dac 610 at p.641.

3 Similar comments were made in United Commercial Bank Ltd. vs Jahangir Alam Khan & ors. 9 MLR (AD) 172.

4 Bengal Steel Works Ltd. vs Registrar 48 (1996) DLR (HC) 101.

In *Social Marketing Co. vs Mr Mahbubuzzaman*[1] Mr Justice Mahmudur Rahman, sitting in a case where the company inadvertently held the annual general meeting beyond the statutory period , held that the High Court is empowered to condone the delay in holding the annual general meeting of the company where it could not be held within the statutory period. The meeting held already was not a valid meeting as the same was held after the statutory period. The Court however ordered that the meeting be held under the chairmanship of a learned advocate.[2]

10.1.6 **Business of Annual General Meeting** – The Act does not precisely say what business must be transacted at the annual general meeting. But the presentation of the accounts and reports and the appointment of auditors must normally be undertaken at regular intervals, and the company's articles will almost certainly provide for other matters of an annually recurring nature. Schedule 1 to the Companies Act indicates that the agenda of sanctioning a dividend, the consideration of the accounts, balance sheets and directors' reports, auditors, the election of directors and other officers in the place of those retiring by rotation, and the fixing of the remuneration of auditors are matters that are usually taken up at the annual general meeting. That meeting may take up any other matter with prior notice that may be discussed at a general meeting. (Regulations 50 and 51 of Schedule 1).

The AGM is the one occasion when members can have an opportunity of meeting the directors and of questioning them on the accounts, on their report, and on the company's financial position and prospects. It is at this meeting that the members may exercise their power of not electing the existing directors when they retire. Most of the powers of the shareholders at the annual general meeting may also be exercised by them in other general meetings but the AGM is a convenient time to exercise the powers of shareholders. Small shareholders may not be able to master enough votes to requisition an extra ordinary general meeting. Professor Gower comments that' the AGM is a general meeting, and anything that can be done at a general meeting can be undertaken at the AGM. There is, for example, no reason why a special resolution or an extra ordinary resolution should not be considered.[3] In practice however the shareholders of big public companies come in at a gala function arranged by the directors and take home token presents and make speeches trying to find fault of the directors but in the end get tired and approve the balance sheet and the directors' report. If the company declares a good dividend the shareholders are naturally pleased but if they do not, then there will be a rough time for the management at the meeting. In the case of non-exempt public companies, the company must file with the Securities and Exchange Commission a copy of audited financial statements, annual report and minutes of the annual general meeting within fourteen days of the completion of the audit or, as the case may be, holding of the annual general meeting.[4]

10.1.7 **Notice of Meetings** – Section 85 provides for the rules pertaining to calling and holding of general meetings. An annual general meeting may be called by notice of fourteen days in writing and a meeting other than an annual general meeting or a meeting for the passing of a special resolution may be called by twenty one days notice in writing , provided that a meeting may be called by shorter notice than aforesaid if it is so agreed in writing in the case of an annual general meeting by all the members entitled to attend and vote thereat and in the case of any other meeting , by the members of the company holding not less than 95% of the paid up share capital and having a right to vote at the meeting. Notice of the meeting must be served on every member in the manner provided in Schedule 1 to the Act. It is not understood why a shorter notice is needed for an annual general meeting which covers

1 (1993) 13 BLD(HCD) 569

2 Also see Sultan Siddique Raisal Jalil Chowdhury vs. Spectra Net Limited & ors 4 BLC(1999) H.C. 348 on this point.

3 'Principles of Modern Company Law 5th Ed p.502.

4 Condition imposed by SEC Order No.SEC/CFD/2001/Admin/02-03 dated 4.10.2001.

important issues like the balance sheet and the directors' report than needed in an extraordinary general meeting. Moreover, the method of sending notice as provided for in the Schedule 1 seriously hampers the directors as they are required to follow the ancient method of sending notice personally or by registered post. The modern methods of communicating by e-mail or fax etc. are totally forgotten. This is important as more and more foreign investors are coming into the country. Sending notice to them by registered post involves loss of valuable time. It was held in *Azad Publications vs Md. Qamrul Anam Khan*[1] that notice of an AGM must be sent by registered post. Section 85 also provides that five persons present in person or by proxy or member or members holding not less than one tenth of the issued capital which carries voting rights may demand a poll, provided that in the case of a private company, if not more than seven members are personally present, one member, and if more than seven members are personally present, two members shall be entitled to demand a poll. An instrument of proxy, if in the form set out in Schedule 1, shall suffice irrespective of any special requirements in the article. A shareholder enjoys the same rights as other shareholders of the same class. If the articles do not make any special provision then votes may be given either personally or by proxy. In the case of a private company if the number of members does not exceed six then two members and if the number exceeds six then three members shall form a quorum. In the case of a public company five members personally present shall be a quorum. In the absence of a contrary provision in the articles, a proxy need not be a member of the company. In the case of a company limited by guarantee the appointment of a proxy is not allowed.

Extraordinary resolutions must be passed by a majority of not less than three fourths of members entitled to vote at a general meeting of which notice specifying the intention to propose the resolution as an extraordinary resolution has been given. A special resolution must be passed by an identical majority of voters as required for an extraordinary resolution in a meeting of which twenty one days notice has been given specifying the intention to propose the resolution as a special resolution.[2] If all members entitled to attend and vote agree then such resolutions may be passed on shorter notice. The company is required to send a copy of the extraordinary or special resolution to the Registrar within fifteen days from the passing thereof. If articles have been registered then a copy of every special resolution for the time being in force shall be embodied in or annexed to every copy of the articles issued after the date of the resolution.[3] Proceedings of general meetings and directors should be maintained in books kept for that purpose and any such minute, if purporting to be signed by the chairman of the meeting shall be evidence of the proceedings and a member is entitled to get a copy for a nominal fee within seven days of the minutes.[4] The English courts hold that "days' mean "clear days.[5]

10.1.8 It was observed *in Mousel & Co Ltd vs The Registrar*[6] that the Registrar had a quasi judicial function and a certain discretion in the matter of recording resolutions. In this case the Registrar kept the return of a resolution passed in another country removing a director of a company and sought legal advise from the Legal Remembrancer. The Court discharged the Writ holding that the Registrar had not refused to register but observed extensively from Indian and English decisions.[7] On the discretion and duty of the Registrar also see above.[8]

It was held in Moyejuddin vs State[9] that applications for copies of the proceedings of meetings by a shareholder must be made at the Head Office of the Company at Dacca and not

1 (1981) BLD (AD) 426.
2 Section 87.
3 Section 88.
4 Section 89.
5 Re Hector Whaling [1936] Ch 208.
6 8 DLR(1956) 202
7 In re Radiant Chemical Co Ltd. Monghyr AIR 1943 Pat. 278 ; Pioneer Mutual Benefit etc vs Asstt Registrar AIR 1933 Mad 129; The King vs The Registrar [1912] 3 K.B. 23.
8 Section 10.1.5.
9 28 DLR (1976) 46.

at Pabna. In a proceeding for quashing criminal cases, a division bench of the Dacca High Court held that proceedings of all meetings of the company should be kept at the registered office of the company at Dacca. Under the law it is the registered office of a limited company where all documents, books and registers should be kept. It was therefore obvious that if any copy of a document was required, it would be furnished only from the registered office. Where the application for copies were not submitted at the registered office, the applicant was not entitled to get them within the periods mentioned in the Act and the officers of the company were not "in default" in sending the copies as a mere failure to furnish the copy was not an offence. In the case of *Shamsul Huda and others vs Alauddin & Taiwa Textile Mills Ltd.*[1] Mr. Justice Mustafa Kamal pointed out that under section 40 of the Companies Act, 1913 (corresponding to section 45 of the Act of 1994) the register of members was the prima facie evidence on any matters by the Companies Act directed or authorised to be inserted therein. The Court further commented on the legal effect of the minutes of proceedings of meetings of shareholders and directors. His Lordship commented as follows :

> 33. When a company produces the minutes of proceedings of its annual general meeting or of its Board of Directors signed by the Chairman of the meeting at which the meetings were held or by the Chairman of the next succeeding meeting the minutes shall be evidence of the proceeding, under section 83(2) of the Companies Act. (Corresponding to section 89(2) of the Act of 1994). Under section 83(3) of the Companies Act (corresponding to section 89(3) of the Act of 1994), until the contrary is proved, every general meeting of the company or meeting of the Board of Directors in respect of the proceedings whereof minutes have been so made shall be deemed to have been duly called and held, and all proceedings had thereat to have duly had. The onus is on the petitioners to show that the minutes of proceedings are not correct and until the petitioners so prove this Court shall take the minutes of proceedings to be evidence of the same...
>
> "48. Under section 83(3) of the Companies Act every meeting of the directors in respect of the proceedings whereof minutes have been so made shall be deemed to have been duly called and held and all proceedings had thereat to have been duly had until the contrary is proved. The burden of proof is upon the said respondents. Until the said burden is discharged the said respondents cannot be heard to say that the minutes of the proceedings of the Board of Directors were wrong. Prima facie they were parties to the decision to sell the shares...and they cannot be given credence at this stage....

10.1.9 **Notice** – If having sent the notices the company finds it necessary to change the venue of the meeting it will have to notify members of the change before the expiration of the minimum period of notice prescribed by the Act or the articles. The members are entitled to that length of notice in order to make arrangements to attend if they want to.[2] The notice must fairly indicate the object of the meeting so as to enable a shareholder to decide whether he should attend the meeting or not. In the case of an AGM the "ordinary business" will denote consideration of the balance sheet, directors report, auditor's appointment, election of directors etc. If however, resolutions on other matters are to be proposed as special, extraordinary, elective or ordinary resolutions then it is customary to set out the resolutions verbatim.[3]

10.1.10 Under Schedule 1 Regulations to the Act, proxies must be deposited at least 48 hours before the meeting. In the U.S.A. where there is no such practice, the meeting may be deliberately prolonged in order to obtain more proxy votes to be obtained by high pressure solicitation. It is quite an universal practice now for the board to send out proxy forms in their own favour with the notice of the meeting and for these to be stamped and addressed at the company's expense. The directors thus have a significant advantage in securing the votes.

1 (1984) 36 DLR (HC) 316.

2 Byng vs London Life Association Ltd [1990] Ch.170, C.A.

3 See Re Moorgate Mercantile Holdings Ltd [1980] 1 W.L.R. 227 at 242;Choppington Collieries Ltd vs Johnson [1944] 1 All E.R. 762; Batchellor and Sons Ltd vs Batchellor [1945] Ch 169.

Directors

11.1 Sections 90 -110 of the Companies Act deal with directors.

Section 90 makes it obligatory for every public company and all private companies that are subsidiaries of a public company, to have a minimum of three directors. This section has improved upon the previous section 83A of the Act of 1913. It requires a private company to have at least two directors, and provides that only an individual may be appointed a director. This removes the shortcoming in the previous law which did not mention whether a private company is required to have any director or not. Also following the Indian Act , the law now requires that only an individual can now be appointed a director. This removes the complaint that the appointment of bodies corporate as directors was undesirable.

11.1.1 Section 91 provides that the subscribers to the memorandum of association shall be deemed to be the directors of the company until the first directors are appointed. Other directors are to be elected by the members in general meeting or in the case of a casual vacancy to be appointed by the board but so that the new appointee retires at the meeting in which the outgoing director was to retire. At least one third of the directors must be such that they are required to retire by rotation at any time. Section 83(2) of the Act of 1913 required two third of the number of directors to retire by rotation and it is not understood why the new Act deviated from the time tested formula of requiring that at least two third of the board should be persons facing periodical elections at the general meeting. This is important because apart from the three types of directors mentioned above there is another category of directors, namely, those who are appointed by outsiders under a contract, e.g., directors appointed by loan giving agencies. Previously the law required that permanent directors could not exceed one-third of the total number of directors but now it seems that upto two thirds of the total number of directors of a public company can be appointed under contract or on a permanent basis even under the articles.

11.1.2 The Act however leaves the determination of the number of directors to the company's discretion. Not infrequently, articles provide for a maximum and minimum number of directors. If there is any inconsistency between the articles, only a question of construction arises. Thus, where one of the articles of association (article 109) of a company prescribed a maximum and minimum number of directors without any qualifying words, and another article (article 126) authorised the company in general meeting to increase or reduce the number of directors, subject to provisions of section 83 A of the Act of 1913 (section 91 of the current Act) , to alter their qualification and change the order of rotation of the increased or reduced number, it was held that this was a case of inconsistency of the articles. As to whether the power of the company by ordinary resolution to ' increase or reduce ' the number of directors conferred by article 126 was only exercisable within the limits set by the maximum and minimum prescribed by article 109, and whether a special resolution altering article 109 was required to increase the number of directors beyond the prescribed maximum, it was held by the Privy Council, reversing the decision of the Calcutta High Court, that the company had power to increase the number of directors beyond the maximum prescribed by article 109, by an ordinary resolution and consequently a special resolution altering article 109 for the purpose was not required. The power to "increase or reduce the number of directors", according to the natural meaning of the words, includes power to increase the maximum without necessarily making specific appointments, and subject to law, to reduce the minimum, for otherwise, an ordinary resolution at a general meeting would suffice without the necessity of having a special article for that purpose.[1]

11.1.3 **Restrictions on Appointments and Disqualifications** – Sections 92 and 93 of the Act relate to restrictions on appointment of directors. A person shall not be capable of being appointed a director of a company by the articles, and shall not be named as a director in any

1 Ramkissendas vs Satya Charan Law AIR 1950 P.C. 81.

prospectus issued by or on behalf of the company unless before the registration of the articles or the publication of the prospectus, he has signed and filed with the Registrar a consent in writing to act as such director and a contract in writing to take from the company and pay for his qualification shares if he has not already taken and paid for the shares and filed an affidavit to the effect that shares not less than qualification shares are registered in his name.[1] On an application for registration of the memorandum and articles of a company, the applicant shall file with the Registrar a list of the persons who have consented to become directors of the company. Section 93 requires that every person proposed as a candidate for the office of a director shall sign and file with the company his consent in writing to act as a director, if appointed, and shall not act as a director of the company unless he has, within thirty days of his appointment, signed and filed with the Registrar his consent in writing to act as a director. Section 94 provides for disqualifications of directors. A person shall not be capable of being appointed a director of a company if he is found to be of unsound mind by a court of competent jurisdiction, is an undischarged insolvent or has applied to be so adjudicated or has not paid the call money on his shares for six months or is a minor. A company may by articles provide for additional grounds for disqualification. This section is new and should be read with section 108 which provides that the office of a director shall be vacated in certain circumstances. Thus, a person will cease to be a director if he has failed to obtain his share qualifications within the time prescribed in section 97(1), or is found to be of unsound mind by a Court of competent jurisdiction, or is adjudged an insolvent , or fails to pay for his shares within six months of the call to pay such money, or he or any firm of which he is a partner or any private company of which he is a director without the sanction of the company in general meeting accepts or holds any office of profit under the company other than that of a managing director or manager or a legal or technical adviser or a banker, or absents himself from three consecutive meetings of directors or from all meetings of directors for a continuous period of three months whichever is longer without the leave of the Board, or accepts a loan or guarantee from the company in contravention of section 103, or acts in contravention of section 105 of the Act. A company by its articles may provide that the office of a director shall be vacated on additional grounds.

Sections 93 and 94 are new in our law. It was long felt that while the Act of 1913 provided for filing of consent to act as director if named so in the articles or the prospectus it did not require that all directors should give their consent to act so. Further, while a director would vacate his seat under certain circumstances, there was no provision for disqualifications of directors at the time of appointment. Three of the disqualifications, namely, being of unsound mind, undischarged insolvent or not paying for shares within six months of the call to do so, are common in both sections 94 and 108.

Section 98 provides that the acts of a director shall be valid notwithstanding any defect that may afterwards be discovered in his appointment or qualification, provided that nothing in this section shall be deemed to give validity to acts done by a director after the appointment of such a director has shown to be invalid.

11.1.4 **Election of Directors** – Provided he is not otherwise disqualified, any person can get himself elected to the board of directors if he can get the support of the majority of the directors. In *Gujrat-Punjab Bus Ltd. vs Muhammad Ashraf*[2] Shafi J. held that the words 'votes-majority' meant majority of shares of shareholders present at a meeting convened for the purpose of electing the office holders. Regulation 57 of the Schedule 1 Regulations to the Act of 1994 provides that at any general meeting a resolution put to the vote of the meeting shall be decided on a show of hands, unless a poll is demanded before or at the declaration of the result of the show of hands according to the provisions of section 85 of the Act. It is clear that any resolution, including a resolution for the election of directors, has, in the first instance, got to be put to the vote of the meeting, which must decide it on a show of hands. If

1 Section 92.
2 PLD (1960) Lah 609.

the show of hands shows that a certain person has majority, then the chairman will declare him as having been so elected even though he may not have the support of the majority of the shares in his favour. In such a case, every person present has one vote, but if a poll is demanded then on a poll every member has one vote in respect of each share held by him. When no poll is demanded, the question of vote in respect of each share does not arise.

Acts to be valid – The acts of a director will be valid notwithstanding any defect that may afterwards be discovered in his appointment or qualification, but nothing can give validity to acts done by a director after his appointment has been shown to be invalid.[1] This law protects innocent outsiders in their transactions with invalidly appointed directors. However a person will not be allowed to take advantage of this section , if he has notice of some probable defect or if he knows that the regularity of the appointment has been challenged and takes no steps to ascertain the facts.[2] Also, this section does not justify the claims of a person against a company for services as liquidator where, because he had not been validly appointed, he never had authority from the company to act as liquidator.[3]

11.1.5 **Qualification Shares** – Section 97 requires a director to hold qualification shares within sixty days of his appointment. Regulation 71 of the First Schedule Regulations require a director to have at least one share. It has been held that when the petitioner had transferred all his shares in a company he had ceased to be a director and chairman of the company.[4] A company's articles of association frequently require its directors to hold a certain number of shares in the company to ensure that they have a material stake in its success and will consequently devote their best endeavours to its service.[5] The amount of the share qualification is often specified in the articles, but if the company is governed by Schedule 1 Regulations, it is enough to hold a single share in the company.[6] Unless the company's articles so require, a director need not obtain his qualification shares before he is appointed, nor need he obtain them by allotment from the company, but unless he obtains them within two months after his appointment or such shorter time as is fixed by the articles, he ceases to be a director.[7]

There is nothing in the policy of the Companies Act or in its language which prohibits the inclusion in articles of additional or different qualifications for directorships. Thus, a special resolution passed at the extraordinary meeting of a bank providing for a holding of a fixed deposit of Rs.1000/- as an additional qualification for a director is intra vires and legal.[8] In *Zamir Ahmad vs D.R.Banaji*[9] the directors appointed did not acquire qualification shares but the company went into liquidation within two months of the appointment of the directors. On an application by the liquidator to put the names of the directors on the list of contributories, it was held that no contract to take shares had come into existence and that the names of the directors not being on the register could not be included in the list. Mere appointment as a director does not mean that a contract has taken place to take the shares. The directors must specifically apply for allotment of shares from the company, for they are not bound to take up the unpaid shares directly from the company. It is open to the director concerned to choose the manner of acquiring shares.[10] Before it was enacted that the failure of a director to obtain his qualification shares would cause him to vacate office, it was held in England that a director impliedly authorised the company to allot to him his qualification shares, if he did not obtain them elsewhere within the time fixed by the articles or, if no time

1 Section 98.
2 Morris vs Kanssen [1946] A.C. 459.
3 Re Allison, Johnson and Foster Ltd [1904] 2 K.B. 327,329 per Kennedy J.
4 A.U. Ahmed vs Bangladesh (1996) BLC 337 (HC).
5 Re North Australian Territory Co [1892] 1 Ch. 322 at 337.
6 Regulation 71.
7 Section 108(1)(a).
8 Saraswathi Vilasan Ltd vs V.S.D.Mudalair (1951) 1 M.L.J.18.
9 [1957] Comp. Cas 634.
10 Re Metropolitan Public Carriage and Repository Company.Browns Case [1873] L.R. 9 Ch.App.102.

was fixed, within a reasonable time after his allotment, which has been interpreted to mean before he first acted as a director.[1]

Now that the legislature requires the directors to obtain share qualifications within two months or in default, lose their directorships, it would seem that the company cannot allot shares to him so as to make him a shareholder and qualify him as a director. This is because the company's authority to allot only arises at the expiration of the fixed time and at the moment when it arises the director has vacated office under statutory provisions, thus revoking the authority. The qualification shares must be registered in the director's name especially where the articles require that they must be so qualified.[2] Similarly, if the articles require shares to be held in the director's own right, then if one holds shares in a company as liquidator of another company (which held shares in the former), one is not entitled to treat them as qualification shares.[3]

It is enough if the director holds shares as a trustee but not beneficially.[4] But see Cooper vs Griffin[5] for a contrary view. In this case Lord Coleridge C.J. discussed the *Pullbrook case* and said that in that case the qualification clause required a director to hold the qualification shares as a registered member in his own right and Jessel J., while holding that registered ownership was sufficient under that clause to confer the qualification, founded his judgment upon the words 'as registered member'. In *Bainbridge vs Smith*[6] Cotton L.J. said that in his opinion although the judgment in the *Pullbrook case* was right, the dictum was not well founded and that the meaning of 'a shareholder holding shares in his own right', is that he must not only have the legal right to deal with them but must have the beneficial ownership of them, although he may still be the beneficial owner, if he has mortgaged his shares. A still later case, Sutton vs English and Colonial Produce Co.,[7] while confirming that holding qualification shares as a trustee without beneficial ownership is sufficient (if the articles require holding shares 'in his own right'), held that it was not so, if he held them in a representative character. It was further held that, in such a case, it was not necessary that a director should hold the shares as a beneficial owner, but, to comply with the articles, he must hold them in such a way that the company might safely deal with them, whatever his interest in them might be. *Sutton's case* appears to take a middle lane between the two extremes in the *Pullbrook case* and the *Cooper's Case* in holding that the company must be able to deal with the shares safely, although beneficial ownership is not necessary.

Modern day company practice however does not require that a director should be the beneficial owner.[8] Directors who accept and hold their qualification shares in trust for and at the will of the promoter, to whom they hand blank transfers, are guilty of misfeasance, and the measure of damages is the highest value of shares during their holding. It is not only improper but it is misfeasance to qualify by taking shares in trust for the promoter to fill up at his pleasure. Directors so qualified hold office at the will of the promoter and as long as they fulfill his wishes. But as soon as they act contrary to the promoter's wishes, he can fill up and lodge the transfers and disqualify them.[9]

The Court has jurisdiction to relieve a person who has acted as a director without having obtained qualification shares within the prescribed period from penalties under section 97(2).[10] There the Court assumed jurisdiction under section 372(1) of the Companies Act 1929, which provided that the Court might excuse a director for negligence, if he had acted honestly and reasonably. The corresponding section in our Companies Act is section 396. As to what constitutes acting reasonably is a question of fact. Where a person had been given shares to qualify him, if he had held himself out as a shareholder, then he would be estopped

1 Re Portuguese Consolidated Copper Mines Ltd. Inchiquins Case [1891] 3 Ch.D. 28.
2 Spencer vs Kennedy [1926] Ch.125.
3 Boschoek Proprietory Co. Ltd vs Fuke [1906] 1 Ch.148.
4 Palmer's Company Law 20th Ed.p.529 and Pullbrook vs Richmond Mining Co [1889] 9 Ch.D. 610.
5 [1892] 1 Q.B.740.
6 [1889] 41 Ch.D.462.
7 [1902] 2 Ch.502.
8 Venture Acceptance Corp Ltd.vs Kirton [1985] 9 ACLR 390.
9 Swinfen Eady J. in In re London and South Western Canal Ltd. [1911] 1 Ch.346.
10 In re Barry and Staines Linoleum Ltd[1934] 1 Ch 227.

from denying it.[1] The Lahore High Court also held a few years earlier in regard to the affairs of the same company that there was nothing in the Companies Act making it obligatory for any director to hold shares and if in the articles of association it had been provided that a director should hold a certain number of shares, the Articles could be amended so as to make persons who were not shareholders eligible for directorships.[2] If directors are required to take their qualification shares within a specified time after election, the period will run from the date on which the result of the poll is declared, and not from the date on which the taking of the poll is completed.[3] The SEC requires that public companies listed in the stock exchange should not require a director to have shares worth more than Tk 10,000, the obvious reason being that a small investor may then contest to be a director.

11.1.6 **Re-appointment and Replacement of Directors** – Section 91 does not make it clear whether the appointment of directors in general meeting can be done by an ordinary resolution. But section 106 provides that the company may appoint a director in place of another by ordinary resolution, although the removal of his predecessor must be done by an extra-ordinary resolution. If the articles prescribe the maximum number of directors who may be appointed, appointments in excess of the maximum are void. Usually however, the members are empowered to increase or reduce the maximum number of directors by an ordinary resolution. Article 84 of the Schedule 1 regulations provide that subject to the provisions of sections 90 and 91 of the Companies Act, the company may from time to time in general meeting increase or reduce the number of directors and may also determine in what rotation the increased or reduced number is to go out of office. The Appellate Division has confirmed a High Court decision in a split judgement that where articles provide that an outsider can seek election at the AGM only if the candidate submits nomination seven days before and is recommended by the board any appointment in contravention of this Article is invalid.[4] The Court observed that the word "recommended" means power of the Board to point out defects, if any, in the candidature of a person for the office of a director in the annual general meeting to avoid complication in such meeting and not the power to reject any candidature on the ground of any defect.

11.1.7 **Casual Vacancy** – Regulation 85 of the Schedule 1 Regulations provide that any casual vacancy occurring on the board of directors may be filled up by the directors but the person so chosen shall be subject to retirement at the same time as if he had become a director on the day on which the director in whose place he is appointed was last elected a director. This article does not contain the additional provision in section 91 (c) of the Act that the person so appointed shall be a person qualified to be elected a director. This is consistent with the requirements of section 97 which requires a director to obtain qualification shares. A co-optee director should therefore obtain qualification shares within two months after his appointment. Article 86 empowers the directors, from time to time, to appoint a person as an additional director who shall retire from office at the next following ordinary general meeting (the annual general meeting) but shall be eligible for election by the company at that meeting as an additional director. Section 97 requires such a director to obtain qualification shares within two months after his appointment.

A casual vacancy on the board of directors is one which occurs otherwise than by a director's term of office expiring.[5] and so there will be a casual vacancy if a director dies or resigns or is removed or becomes disqualified from holding office. Article 87 in the First Schedule applies to remove any director before the expiration of his period of office, and the Act provides that the company may by extraordinary resolution remove a director and may by an ordinary resolution appoint another person in his stead; the person appointed shall be subject to retirement at the same time as if he had become a director on the day on which the director in whose place he is

1 Mulk Raj Bhalla vs People's Bank of Northern India Ltd. AIR 1936 Lah 480.
2 In re People's Bank of Northern India Ltd AIR 1933 Lah 51.
3 Holmes vs Keys [1958] WLR 772.
4 ASF Rahman and another vs A.M. Agha Yusuf and others 52 DLR (AD) 127.
5 Munster vs Cammell Co (1882) 21 Ch. D. 183,187.

appointed was last elected a director. This article differs from section 106 in that it applies to all directors while section 106 which deals with the removal of directors speaks only of removal of shareholder directors by an extraordinary resolution. It is obvious that the draftsmen , while drafting the new Act, omitted to make corresponding changes in the Schedule I Regulations. Neither the article nor the section refers to the filling up of a casual vacancy.

It is not clear however whether this means that the members in general meeting can appoint an additional director whether or not that has the effect of filling up a casual vacancy. Section 91 (1) (b) is clear in its terms that the members may elect a director from among themselves in a general meeting. There is divergence of opinion by the English courts on the construction of this sort of articles. In *Blair Open Furnace Co vs Reigert*[1] one article provided that until otherwise determined by a general meeting, the number of directors shall not be less than two or more than seven. Another article provided that any casual vacancy in the board may be filled up at all times by the board. The directors were also given power to appoint additional directors but so that the total does not exceed seven. It was held by Eve J. on a construction of the above articles that the power of the company to appoint additional directors had been wholly delegated by the company to the board of directors to the exclusion of the company. This case was distinguished in *Worcester Corsetry Ltd. vs Witting*[2] where by another article the company might from time to time in general meeting increase or reduce the number of directors and the rotation in which the increased or reduced number is to go out of office. On the construction of the last words of this article, it was held that the power of appointing additional directors which was vested in the general body of shareholders, was not wholly taken away by the articles from the general meeting. The Court relied on the case of *Isle of Wight vs Tahourdin*[3] where the Court refused an application by the directors of a statutory company for an injunction to restrain the holding of a general meeting. Where articles provide that 'until otherwise determined by the company in general meeting, the number of directors shall be not less than five and not more than nine', the Courts have held that this means that the general meeting can increase the number of directors beyond the maximum fixed and also appoint directors to fill up the extra seats.[4]

There is nothing in the Companies Act which requires that Articles of Association must be rigid and may not in themselves provide for varying sets of circumstances. There was a second contention in the Sind case that the power to appoint additional directors vested in the directors and not in the company under an article which provided that the directors should have power at any time and from time to time, to appoint any other qualified person to be a director, either to fill a vacancy or an addition to the board. It was held that, until divested of its powers, the company in general meeting could appoint directors and that this principle was set out in the statute.[5] In Vishwanathan vs Tiffin S B.A. and P. Company,[6] six new directors were appointed in a general meeting of a company. The appointment was attacked on the ground inter alia, that , under the articles the general power of appointing directors was vested in the board, that the general body had power to appoint directors only in place of those retiring and that, as only one director had retired at the meeting, the appointment of at least five new directors was invalid.'It was held, following *Witting's case*[7] that the meeting had full right and power to appoint directors.

The weight of authorities therefore support the view that unless specifically provided against, the general meeting has concurrent powers with the board to appoint additional directors or to fill a casual vacancy.

1 [1913] 108 L.T. 665.
2 [1936] 1 Ch 640.
3 [1884] 25 Ch.D. 320.
4 Guru Prasad vs Rameshwar AIR 1933 All 344 and Topandas vs Yeotmal Electric Supply Company AIR 1940 Sind 89.
5 Section 91 .
6 AIR 1953 Mad 520.
7 supra

11.1.8 **Appointment by Non-Members** – An outsider may, by virtue of a special contract with the company, appoint directors and the articles of association may expressly empower an outsider to appoint directors and in that case the outsider's right to appoint a director will be further strengthened. In *British Murac Syndicate vs Appleton Rubber Co.*[1] by an agreement made between the plaintiff syndicate and the defendant company, the plaintiff syndicate agreed to sell and the defendant company agreed to buy certain patent rights and the goodwill of a business in consideration of cash and shares in the defendant company. By a clause in the agreement it was provided that, so long as the plaintiff held at least 5000 shares in the capital of the defendant company, the plaintiff syndicate should have the right to nominate two directors on the board of the defendant company. This provision in the agreement was also entrenched in the articles of association. The patent rights having been assigned to the defendant company, and the purchase price paid and satisfied, two directors were nominated by the plaintiff, but the defendant company refused to accept their nomination.

It was held that, as the agreement had been carried out by the assignment of the patent rights, it was a mere question of carrying out a subsisting obligation and as soon as the plaintiff syndicate nominated the two persons as directors, they became directors there and then and nothing remained to be done by the defendant company to perfect their appointment. So there being no objection of a personal nature as against one of the nominees, an injunction was granted to compel the acceptance of the said person as director of the company. It is to be noted that the articles constitute a contract between the members and the company only so that they do not confer rights or obligations on a member otherwise than in his capacity as a member.[2] In the instant case, the articles were only relevant to the question whether the agreement had been executed (and on facts it was found that it had), for as Eve J. said at about the same time this case was decided, *(Plantations Trust Ltd. vs Bila Rubber Lands*[3]*)* as a general rule the Court will not grant an injunction to enforce specific performance of an executory agreement between a company and an outside body to elect as director a nominee of such outside body.

The courts are, however, reluctant to impose on a company as director a person unfit to act or one in whom the members generally have no confidence. Thus in the *British Murac Syndicate case* the Court adjourned the matter till the general meeting of the company had expressed its views as to whether it had any personal objection against the appointment of the other nominee, whose business was in competition with the company. It was commented in the course of the judgment[4] *that although an outside body like the plaintiff syndicate may have the power of nominating two directors on the board, the Court would not by an injunction force the company to accept on its board persons who were unfit or thoroughly unacceptable as members of the board of directors.* Under the managing agency system, managing agents often had a right to appoint directors on the board, but not exceeding one-third (at present two-thirds) of the total number of directors.

11.1.9 **Summary** – Directors may therefore be appointed under an authority in the memorandum or articles, it being possible to give that authority to one or more members or to someone who is not a member, or appointed by the board while filling up a casual vacancy or appointed by the company in general meeting. The term of office is normally fixed by the memorandum or articles. This may provide for the appointment of named individuals with provision to cover the eventuality of the appointee's death or onset of legal incapacity occurring while in office. Directors have to file written consent for acting as such. Subsequent directors can be appointed by the company in general meeting in the exercise of their inherent power to direct the control of the company,[5] unless that power is excluded by the contract embodied in the articles, either expressly or by clear implication.[6] Typically, however, the articles make provision for the appointment of directors. Articles commonly provide for the power to

1 [1915] 2 Ch. 186.
2 Eley vs Positive Government Security Life Assoc.(1876) 1 Ex.D. 88.
3 1916 85 L.J. Ch.804.
4 ibid at page 196.
5 Witting case [1936] Ch. 640 at 650 supra.
6 Integrated Medical Technologies Ltd. vs Macel Nominees Pty Ltd (1988) 13 ACLR 110.

appoint directors to be exercised by the general meeting (Schedule 1 Regulations 82, 84, 87). An article empowering the directors to appoint additional directors does not necessarily deprive the general meeting of its inherent power to appoint additional directors upto the maximum number prescribed by the articles,[1] sometimes with the qualification that the board may make appointments to fill casual vacancies, or as appointments of additional directors upto the maximum allowed by the articles.[2]

While the adoption of such provisions has become common, there are few limits to the kinds of arrangements which the incorporators may choose to make for the appointment of directors. In a small company it is not unusual for the holders of a majority of shares to have the power to appoint directors. In a joint venture company formed by several companies to carry out a project each venturer will typically have power to nominate a number of directors proportionate to the value of the venturer's contribution. Where a company is being administered under a shareholder's agreement the terms of appointment of directors may be laid down in the agreement. To avoid the possibility of a meeting electing a person as a director without proper notice to members, articles sometimes require notice of intention to propose a person for election, other than a retiring director, to be given to the company some days before the meeting as a condition of eligibility for election of the person proposed. Such a provision also protects incumbent directors against surprise nominations.

The powers given to directors to fill casual vacancies and to appoint additional directors must, like other powers given to the board, be exercised for the benefit of the company as a whole. In exercising their powers the directors should consider whether the person nominating replacement directors appears to have the necessary voting powers to prevail in a general meeting.[3] The directors are entitled to take into account the possible disruption and expense that could be caused by a contested election which develops into a proxy fight. If they decide to resist the nominations made by a person who claims to have attained control, they are entitled to reasonable use of the company's resources to inform shareholders about candidates for election but they are not to campaign in a partisan way for particular candidates.[4]

11.1.10 **Failure to Appoint Directors** – Articles may provide that, in case there is no election of directors at a meeting then the retiring directors, if willing, will be deemed to have been re-elected. Alternatively, the meeting may be considered to be adjourned, and if at the adjourned meeting the places of the vacating directors are not filled up, the latter may be deemed to be re-elected. In *Re Great Northern Salt etc Co.*,[5] an article provided that, if the vacating director's place is not filled up at the adjourned meeting, he is to continue in office. At the first ordinary meeting (of the seven subscribers to the Memorandum) four directors who were due to retire did not retire from office as provided by the articles but a resolution was passed at the meeting authorising them to continue to act as directors. It was held that the article was directory only and the meaning of that article was that if, for any reason, either the first meeting or the adjourned meeting, at which the election of the directors ought to take place, does not proceed validly to fill up the places of the vacating directors, they are to continue in office. Hence the four directors were validly in office. In *Re Consolidated Nickel Mines,*[6] one article provided that the directors must summon a general meeting of the company once a year; another provided that in 1906 all the directors must retire at the ordinary meeting. No meeting was held in 1906 and 1907. It was held that the contention of the liquidator that the directors deemed to have retired on 31 Dec. 1906, was well founded. In *Spencer vs Kennedy*,[7] a director was due to retire at the general meeting of the company and

1 Integrated Case.
2 Schedule 1 Regulations 85,86.
3 Ford and Austin's Principles of Corporations Law 7th Ed. para 7.170.
4 Ford and Austin; ibid and Advance Bank of Australia Ltd. vs.FAI Insurances Australia Ltd. (1987) 12 ACLR 118.
5 [1890] 44 Ch.D. 472
6 [1914] 1 Ch 883.
7 [1926] 1 Ch 125.

notice had been given to elect a new director in his place. At the meeting, the re-election of the retiring director was proposed but no decision was reached in either that meeting or the three which followed. At the last meeting his re-election was put to vote, lost and another person was re-elected. It was held by Astbury J. that the proceedings were in order and the articles providing for automatic re-election had no application. In *Holt vs Catterall*[1] one of the items of business at a general meeting was the election of a director, Mr. Holt, retiring by rotation. He was proposed for re-election, but the motion was lost. It was held that the relevant articles (roughly corresponding to articles 79 and 83 of the Schedule 1 regulations) could not be cut down so as to apply only in cases of complete inadvertence. As the articles provided that, in the absence of a fresh appointment, the retiring director would be deemed to be re-appointed, Mr. Holt must be deemed to have been re-elected; there was therefore, no vacancy and no occasion arose to appoint additional directors as the company had purported to do. In this case no one else was re-appointed. However, in *Robert Batchellor and Sons Ltd. vs Batchellor*,[2] the retiring directors having been proposed for re-election, lost and two other persons were elected in their place by the meeting wrongly, as was found, on technical grounds. The retiring directors thereupon, claimed to be re-elected. It was held that, in the circumstances, to hold that the majority must nevertheless be deemed to have exercised their voting power in a directly contrary sense to that in which in fact it did exercise it, was a conclusion so extraordinary that it was repugnant to common sense and much clear language would be required before the Court could be driven to it.[3]

In Kailash Chandra vs Jogesh Chandra[4] the directors of a company were elected in 1921. According to the articles, the directors were to be elected annually. A general meeting was convened in 1922 at which election of new directors was proposed. Before the election of directors was completed, the meeting came to an end, and there was no subsequent meeting for the election of directors. The old directors continued to act. In a suit brought to declare that the directors elected in 1921 were no longer the directors of the company, it was held that no general meeting having been held at which directors were elected, the directors elected at the last general meeting would continue in office. In another of the Calcutta cases, *Sati Nath Mukherjee vs Suresh Chandra Roy*[5] the board of directors, at a meeting held prior to the annual meeting, co-opted six of the defendants as directors. At the annual meeting only two directors were elected and no adjourned meeting was held. The defendants contended that they were deemed to have been re-elected under the articles of association of the company.[6] Subsequently the two elected directors co-opted six other persons, including the plaintiff as directors.

The plaintiff sued for declarations that the proceedings at the annual meeting were valid, that he was a director and that the appointments of the defendants as directors were invalid and asked for their removal. It was held that in so far as it related to a declaration that the plaintiff was a director, the suit was properly constituted, but it was incompetent, if it sought to challenge the appointment of the other directors or ask for their removal. In *M.K.Srinivasan and others vs Watrap S.Ayyar and other*[7] the general meeting did not fill up the vacancies and the adjourned meeting which was supposed to fill up the vacancies of the retiring directors by poll, the board having co-opted certain directors as shareholder-directors, the Court held that the words "if at an ordinary general meeting at which an election of directors ought to take place" in the article imply that it must be possible for the poll to be

1 [1931] 47 Times Law Reports 332.
2 [1945] 1 Ch.169.
3 For more cases on this topic, see also Kanssen vs Rialto [1944] Ch 346; Morris vs Kanssen [1946]A.C. 459,Ammal vs Indian Trades and Investment Ltd [1952] 22 Comp. Cas 324, Lalchand Mengraj vs Shreeram Mills Ltd [1968] 38 Comp Cas 606 ,In re Hindustan Co-operative Insurance Ltd [1961] 65 C.W.N. 68.
4 AIR 1928 Cal 868.
5 I.L.R.(1940) Cal 560.
6 Corresponding to articles 83 and 85 of Schedule 1 Regulations.
7 AIR 1932 Mad 100

taken at the appointed time and place. There must at least be a reasonable opportunity to the voters and to the candidates of having the poll taken. This not being done, the shareholders had a right to bring an action and that a fresh poll be taken as the co-option was illegal.

11.1.11 **Retirement by Rotation** – Regulations 79 to 82 of the Schedule 1 Regulations deal with retirement of directors by rotation.

These provisions are applicable to public companies and require a fraction of directors (one- third) to retire each year by rotation and empower the members to fill the vacancies at the annual general meeting. At the first annual general meeting all directors must retire. Regulation 80 of the First Schedule provides that the directors to retire every year shall be those who have been the longest in office but as between persons who became directors on the same day, those to retire shall, unless they agree among themselves, be determined by lot. In *Eyre vs Milton Proprietary Ltd*[1] the articles stated that they should be chosen by ballot. The Court held that this meant by lot. Regulation 81 in the First Schedule provides that a retiring director shall be eligible for re-election. The next Regulation provides that the company at the general meeting at which a director retires may fill up the vacancy by electing a person in his place. Regulation 83 provides for the re-appointment of vacating directors if the vacancies are not filled up at the annual general meeting or at any adjournment thereof. Regulations 79 to 82 are compulsorily applicable in the case of public companies and private companies which are subsidiaries of a public company by virtue of section 17 of the Act of 1994 but due to a printing error the section numbers the compulsory regulations as one number less.

In *Maqbool Elahi vs Khan Abdul Rahman*[2] the board of directors passed a resolution that the seats of three directors had been automatically vacated under section 86I of the Companies Act 1913, for an alleged contravention of section 86F of the same Act in that the defaulters did not obtain prior consent of the Board while purchasing steel sheets from the company. The Supreme Court of Pakistan held on an appeal from a writ petition(!) filed in the High Court of West Pakistan that on the facts of the case there was no contravention of section 86F and no consent was necessary. It further held that in such a case the argument that since by efflux of time and by the rule of rotation of directors under the relevant instruments, the three ousted directors would in any event cease to be directors by the time the case had been decided, was not tenable. Mr. Justice Cornelius said at page 285 of the judgment :

> ... It is evident that the smooth working of the company under the law and the Articles has been interrupted with the ousting of these three directors, and has not been restored to the present day. This condition rendered operation of the rule of rotation completely impossible. The purpose of the order which we propose to make is , as stated earlier, to place in position those who were entitled in law to act as the directors immediately before the 16th. September,1957.

It has been held In *Ananthalaxmi vs Indian Trader and Investment Limited*[3] that, where in any calendar year an annual general meeting is not held as required by the articles, the directors who would have been required to retire if such a meeting was held, would be held to have vacated office on the last day of the year. The Indian author A.Ramaiya , on the basis of this and some other judgments, holds the view that a director who would have retired at the annual general meeting will automatically vacate his seat at the end of the year even if the meeting was not held at all.[4] This proposition, it is submitted, is against the language of the Schedule A Regulations and although supported by the theory that the defaulting directors cannot get advantage of their own lapse in calling the annual general meeting, runs contrary to the legal position which will be if the Court condones the delay and orders a fresh annual general meeting to be held as the meetings would then be held according to the new schedule.[5]

1 [1936] Ch 244.
2 PLD (1960) S.C. 266.
3 (1953) 1 Mad L.J. 275.
4 Guide to the Companies Act 11th Ed. p.779.
5 BCIC vs Registrar (1987)D.L.R.(H.C.)1.

Moreover the language of Regulation is clear – the directors will retire at the annual general meeting. If a person is aggrieved he may approach the High Court for calling the annual general meeting.

Please note that Regulation 79 of Schedule 1 Regulations to the Act requires that every year one-third of the directors for the time being shall retire and may seek re-election whereas section 91(2) permits two-thirds of the directors to be persons not liable to retire by rotation. In the previous Act of 1913, the requirement was that at least two-thirds of the total number of directors should be liable to retire by rotation.(Section 83B(2)).

11.1.12 **Vacation of Office** – If a director becomes disqualified by law or by the articles from continuing to be a director, he automatically vacates office. Section 108 lays down the circumstances under which a director will automatically vacate his office. Sub-section (2) provides that nothing in this section shall preclude a company from providing by its articles that the office of a director shall be vacated on grounds additional to those specified in the section. Regulation 78 of Schedule 1 Regulations lays down, apart from repeating most of the circumstances contained in section 104, that the office of a director shall be vacated if he is concerned with or participates in the profits of any contract with the company or is punished with imprisonment for a term exceeding six months provided that no director shall vacate his office by reason of being a member of any company which has entered into any contract with the company of which he is a director.

It was held in *Sureshchandra vs Jivanlal*[1] that just as the grounds on which the office of a director is vacated are specified in section 86 I of the Act of 1913, so additional grounds for vacation of such office must also be specifically stated in the articles in the case of a private company. Regulation 77, Table A (of the Act of 1913) therefore, if incorporated into the articles of association of a private company, not being a subsidiary to a public company, will give more scope than the section itself. Similarly, Article 78 of Schedule 1 differs from section 108(h) (acting in contravention of section 105) and section 105, in that it does not save the director (if he participates in or is concerned with the profits of any contract with the company) even if he does so with the consent of other directors.

Section 108 (f) provides that a director shall vacate his office if he absents from three consecutive meetings of the directors or from all meetings of directors for a continuous period of three months whichever is longer without leave of absence from the board of directors. It has been held in England that the absence must be voluntary and not due to illness, unless the illness obliges the director to go abroad.[2] The period of absence does not begin to run until a meeting is held at which the director ought to have attended.[3]

There is a difference of opinion whether the office of a director falls automatically vacant. In an English case it was held that the director should be given an opportunity to explain himself.[4] But an Indian Court has held that no such hearing was required and that the vacation of office was automatic.[5] The provision applies to all kinds of directors but a director may show that he did not receive notice of meetings and the company has to produce postal certificates to prove service.[6] A director need not resign if he ceases to be a director by operation of law.[6A]

A director may resign his office and the ordinary rules regarding resignation will follow.[7] A notice of resignation sent not to the company but to an outsider is not effective.[8]

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1 [1956]Comp Cas.148.

2 Mark's Claim [1900] W.N. 114.

3 MacConnel's Claim [1901] 1 Ch. 728.

4 Richardson vs Methley School Board [1893] 3 Ch 510.

5 Shekhar Mehra vs Kilpest P. Ltd. [1986] 3 Comp. L.J. 234. See A.Ramaiya : Guide ,11th Ed p.835.

6 A.Ramaiya. ibid. 6A. Tanveerul Haque vs Unistar Shipping Ltd. and others 52 DLR 215.

7 Glossop vs Glossop [1907] 2 Ch 370,Latchford Premier Cinema Ltd vs Ennion [1931)]2 Ch 409,State vs Sitaram AIR 1967 Patna 433, Mohan Chandra vs Institute of Chartered Accountants AIR 1972 Delhi 91,T.Murari vs State [1976] 46 Comp. Cas. 613.

8 Registrar vs Orissa Paper Products Ltd.[1988] 63 Comp. Cas 460.

Also, once a director becomes subject to a disqualification, it cannot be waived or condoned by the Board.[1] Where the articles disqualified a director automatically if he acquired any interest in a contract with the company not disclosed to the Board, the disqualification continues only so long as such interest lasts. If on the cessation of such interest he is again re-elected, such re-election is not invalid.[2] In *F.P.S. Albuquerque vs Catholic Bank Ltd*[3] dealing with an article of a company, which declared that the office of a director " shall be vacated" if he resigned or for any other reason became incapable of acting as a director, it was held that the article contemplated resignation or some incapacity such as illness or any other capacity. His indebtedness to a bank could not be regarded as incapacity within the meaning of the article.

11.1.13 **Removal of a Director** – Section 106 of the Act provides that the company may by extraordinary resolution, remove any shareholder before the expiration of his period of office and may by ordinary resolution appoint another person in his stead. The person so appointed shall be subject to retirement at the same time as if he had become a director on the day on which the director in whose place he is appointed was last elected director. A director so removed shall not be re-appointed a director by the Board. Article 87 of the Schedule 1 Regulations are to the same effect . It is not clear why the shareholders will have to pass an extraordinary resolution to remove a director when they can appoint one by an ordinary resolution and both in India and the U.K. the shareholders may remove by an ordinary resolution. This section establishes one of the most important principles of company law - that though normally shareholders have no power to interfere with the day-to-day management of the affairs of the company by the directors yet they retain the ultimate control.

Director of a banking company can be removed under this section.[4]

11.1.14 The right of removal being absolute, the Court will not interfere with the shareholders' decision properly arrived at even if articles require reasonable cause for dismissal.[5] Section 106 empowers the shareholders to remove a director whose period of office is liable to determination by rotation. Read with section 91(2) this means that articles may provide that the shareholders of a public company can remove upto one third of the whole number of directors. Section 106 therefore, does not apply to contractual appointees, including those nominated by managing agents, banks under a loan agreement etc., so long as the latter do not exceed two-thirds of the Board and are not subject to the compulsory rule of retirement by rotation. An outsider's contractual rights to be represented on the Board will, however, be undermined if the company takes on its board of directors, other such appointees, so that the total number of such appointees exceed two-thirds of the Board. Can an outsider claim that a company should do nothing of its own accord to jeopardise his nominee's position on the Board? It depends on the terms of the contract and the proximity to the act of the company to the damage done to the plaintiff. In *Shindler vs Northern Raincoat Co. Ltd*[6] it was held that a company should do nothing of its own motion to put an end to the circumstances which enabled the plaintiff to continue as managing director. It is submitted, however, that unless there is an explicit term in the contract, binding the company not to exceed the number of contractual appointees on the board, it will not be possible to restrain the company to do so. A director who has been dismissed wrongly can sue the company for damages. In *Read vs Astoria Garage*[7] a private company's articles of association empowered the directors to appoint one of their body as managing director for such term and at such remuneration as they think fit, his appointment being subject to determination automatically if the company in general meeting resolved that his tenure of the office of managing director be determined.

1 In re Bodega Ltd [1904] 2 Ch.276 and Glossop vs Glossop [1907] supra.
2 ibid.
3 AIR 1942 Mad 737
4 Kh. Mahtabuddin Ahmed vs B. Bank and ors 14 BLD (1994) HC 365.
5 Re Gresham Life (1872) L.R. Ch.App. 446,449.
6 [1960] 1 W.L.R. 1038.
7 [1952] Ch. 637.

After a few years, the plaintiff was removed from his post of managing director. The plaintiff having brought proceedings claiming damages for wrongful dismissal without notice, it was held that his tenancy of the office of managing director could, under the articles, be determined ipso facto by a resolution of the company in general meeting without notice. In Pullbrook vs Richmond Mining Co.[1] it was held that a director of a company can, if qualified, sustain an action in his own name against the other directors, on the ground of individual injury to himself, for an injunction to restrain them from wrongfully excluding him from acting as a director. Further, a director-shareholder has sufficient proprietary interest to sustain a suit complaining that he has been wrongfully excluded by the other directors.[2] In this case the directors were entitled to remuneration under an article (Article 26) as the company in general meeting might decide. Following the decision in the Pullbrook Case that this is an individual wrong and that a director has a right by the constitution of the company to take part in its management, Wynn-Parry J. said in the course of delivering the judgment :

> ...It (Article 26) gives a director a right , if the company decides to pay the directors in any year for their services, to share in that remuneration, and that seems to me to be more than....*spas successionis*. It is ...a sufficient proprietary interest....[3]

If the removal of the director is a breach of his contract of employment, whether it is a breach of an express contract or a contract which incorporates the terms of the articles, he may sue the company for damages. If, however, a director is removed under a power in the articles, he may only sue for damages for wrongful dismissal if he has an express contract of employment, which does not empower the company to dismiss him in that way. If the articles are altered so as to introduce a new ground on which directors must vacate office, the new ground will apply to directors who are already in office, and may operate to terminate their directorships immediately. If his contract of employment incorporates the terms of the articles, however, either by expressly providing that he shall be employed on those terms or because the contract has arisen simply by the director serving as a director and the company accepting his services, it is implied that the contract shall embody the terms of the articles as they stand from time to time, so that if the articles are altered to introduce a new ground for vacating office, the director will vacate office on that ground, in accordance with, and not in breach of, his contract of employment and he will have no redress against the company in damages.[4] Similarly, a company cannot contract to employ a director on terms which conflict with its articles at the time when he is appointed.[5] If a director's service contract fails to provide that he shall vacate office on the grounds set out in the articles when the contract is entered into, the director cannot sue the company for damages. In *British Murac Syndicate vs Alperton Rubber Co Ltd*[6] it was held that a company had no power to alter its articles for the purpose of committing a breach of contract and that an injunction ought to be granted to restrain the holding of a meeting of the company called for that purpose. As to the argument that the company cannot contract itself out of its inherent statutory power to alter its articles, Sargent J. followed the argument given by Lindley M.R. in *Allen vs Gold Reefs of West Africa,*[7] that, although the regulations contained in a company's articles are revocable by special resolution , a special contract may be made with the company in the terms of one or more of the articles, and the question will then arise whether an alteration of the articles so embodied is consistent or not with the real bargain between the parties.[8] A company cannot break its contracts by altering its articles but when dealing with contracts referring to revocable articles, and especially with contracts between a member of the company and the

1 (1878) 9 Ch. D.610.
2 Hayes vs Bristol Paint Hire Ltd.[1957] 1 W.L.R. 499.
3 ibid. at p.504.
4 Shuttleworth vs Cox Brothers and Co. Ltd [1927] 2 K.B.9.
5 Bluett vs Stutchbury's Ltd. [1908] 24 T.L.R. 469.
6 [1915] 2 Ch.186.
7 [1900] 1 Ch. 656,673
8 ibid.at p.193.

company respecting its shares, care must be taken not to assume that the contract involves, as one of its terms, an article which is not to be altered. On the facts of this case, the contract between the plaintiff syndicate and the defendant company clearly involved, as one of its terms, that such an article was not to be altered.

If, however, no such term to keep the articles intact can be inferred, the company cannot be stopped from altering its articles.[1] Lord Porter remarked in this case that a company cannot be precluded from altering its articles of association, thereby giving itself power to act upon the provisions of the altered articles, but so to act may nevertheless, be actionable if it is contrary to a stipulation in a contract validly made before the alteration. The articles may give them a power to dismiss, but the power to dismiss is different from a right to dismiss. If the articles of association of a company contain no power to remove directors before the expiration of that period of office, but authorise the shareholders by special resolution to alter any of the articles, there must be a separate special resolution altering the articles, so as to give power to remove directors, before a resolution can be passed to remove any of them.[2] In *Re T.N. Farrer Ltd.*[3] the articles of a private company provided that one of the signatories of the memorandum of association was to be the governing director of the company for life or until he should resign or be removed by a special resolution. Subsequently, an extraordinary resolution of the company resolved that the company should be wound up voluntarily. The liquidators neither employed nor remunerated the governing director. In a claim for damages for an alleged breach of the governing director's contract of service, it was held, that his employment was conditional upon the continued existence of the company and there was no breach of contract. Further, that, as the governing director was employed on terms under which it was competent for the company at any time to dismiss him, he could not recover damages even if there had been a breach of contract of service. Simonds J. pointed out :[4]

> ...It is, in my opinion, necessary to distinguish between a case like the present one, in which the contract is constituted by the articles, and the governing director has assumed office in accordance with them, and a case where, apart altogether from the articles, the company and the director have entered into an independent agreement...No case have been brought to my notice where a director, having no agreement with the company outside the articles, has claimed, much less been held entitled to receive, damages because his period of office has been brought to a premature end by the winding up of the company....

Similar opinion was made in the *Cambrian Newspaper case*[5] where the articles protected the rights of members. Scott J.expressed the view that a company cannot by contract deprive its members of their rights to alter the articles by a special resolution even though so to act may involve it in a breach of contract. The Court cited the dictum by Lord Porter in the *Southern Foundries case*[6] to this effect.

In a Lahore case it was held that where in pursuance of certain articles acted upon by the company, a shareholder was appointed managing director and acted as such for eleven years and was remunerated in accordance with the terms set out in the articles, the articles constituted an implied contract between the company and the shareholder so as to entitle him to the declaration that he was the managing director of the company.[7]

The power of the company to remove a director may however be frustrated by a system of weighted voting. Thus, in *Bushell vs Faith*[8] articles provided that in the event of a resolution being proposed at a general meeting for the removal from office of a director, any shares held by that director would on a poll in respect of such resolution carry the right to three votes per share. Despite the fact that the articles had no significance independent of any

1 Southern Foundries Ltd vs Shirlaw. [1940] App. Case 701.
2 Imperial Hydropathic Hotel Co. vs Hampson (1882) 23 Ch.D.1.
3 [1937] 2 All E.R. 505
4 ibid. at p.508.
5 [1987]Ch.1.
6 supra.
7 Sardar Gulab Singh vs Punjab Zamindar Bank Ltd AIR 1942 Lah 47.
8 [1970] A.C. 1099.

attempt to remove a director, a majority of the House of Lords held the article effective. Lord Morris of Borth-y-gest, the sole dissentient, thought that such an article was equivalent to a provision that a director could not be removed against his will and as such was contrary to the equivalent of section 106 of our Act. The majority thought the statute had to be read in a context of company law which had for a long time permitted the giving of special voting rights or denying of voting rights to any class of shares.

In India, the corresponding section 284 of the Act of 1956 as amended, provide that any removal of director under the statutory powers does not take away the rights of a director to receive compensation and that he has a right of representation against such removal and therefore a prior notice of such resolution intending to remove him. *This right is also contained in the English and Australian law but there is nothing like this in our company law.*

Compensation can be claimed not only for the termination of the office, but also for any other office which will terminate along with that office.[1]

11.1.15 **Appointment of a Receiver** – The appointment of a receiver in a debenture-holder's action operates as a dismissal of the company's directors, because the management of the company's business is taken over by an outsider, and the consequences are the same as if the company had closed down its business.[2] It may be inferred therefrom that the appointment of a receiver out of Court has the same effect for the same reasons. It has been said in *Measures Brothers Ltd vs Measures*[3] that, if a company is ordered to be wound up by the Court, its directors are thereby dismissed, apparently for the same reasons as in the case of a receivership. Where a solvent company was wound up voluntarily for the purposes of amalgamation, the company's officers were not dismissed by the passing of the winding-up resolution.[4] It is not certain, however, whether directors are dismissed by the company passing a resolution to wind up voluntarily if the company is insolvent.[5] But whether directors are dismissed by a winding up resolution or not, the liquidator may dismiss them by excluding them from the management of the company's affairs.[6] If a director is dismissed in consequence of the company being wound up, and he was employed under contract which incorporated the terms of the articles, he cannot sue the company for damages for wrongful dismissal because it was an implied term of his contract of employment that it should terminate on the company being wound up but if he has an express contract of employment for a fixed period, no such condition can be implied and he will be entitled to damages for wrongful dismissal.[7]

11.2 **Powers of Directors and Board and General Meeting** – The board of directors and the members of a company in general meeting between them exercise all the company's powers. Subject to the provisions of the Companies Act which require certain powers to be exercised by the members in general meeting, the division of powers between the board and the members is left entirely to the discretion of those who frame the articles of association, but the distribution can, of course, be varied from time to time by an alteration of the articles. In American law, certain powers are considered to be managerial and therefore inalienable by the board; but there is no such provision here. The board's powers can be as broad or as narrow as is desired, but the tendency in modern articles of association is to follow the pattern of Schedule 1 regulations. Regulation 72 of that Schedule provides that the business of the company shall be managed by the directors who may pay all expenses incurred in

1 As to the amount of compensation, see British Transport Commission vs Gourley [1955] 3 All E.R. 796(HL); Beach vs Reed Corrugated Cases Ltd [1956] 2 All E.R 652;Phipps vs Orthodox Unit Trusts Ltd [1957] 3 All E.R.305.

2 Reid vs Explosives Co (1887) 19 Q.B.D. 264.

3 [1910] 2 Ch. 248,261.

4 Midland Counties District Bank Ltd vs Attwood [1905] 1 Ch. 357.

5 Obiter per Greer L.J. in Fowler vs Commercial Timber Company Ltd [1930] 2 K.B. 1,6.

6 ibid.

7 Re T.N. Farrer Ltd [1937] 2 All E.R. 505.

promoting and registering the company, and may exercise all such powers of the company as are not, by the Act, or any statutory modification thereof for the time being in force or by the articles, required to be exercised by the company in general meeting, subject nevertheless to any regulation in the articles, to the provisions of the Act and subject also to such regulations not being inconsistent with the aforesaid regulations or provisions, prescribed by the company in general meeting. No regulation made by the company in general meeting shall invalidate any prior act of the directors, which would have been valid, if that regulation had not been made. This regulation should have been made a compulsory article as it was in the Act of 1913 under section 17 of the Act but due to an error, it seems, the number of regulations given in section 17 of the Act of 1994 are serially one number less and as a result the old serial number "71" stays in the language of section 17 whereas it should be "72". It is, however, a standard article almost universally adopted by the draftsmen of articles of association. As will be explained later the language of this article is a synthesis of the development in the English case law and has been taken from the corresponding articles in the schedule to the English Companies Acts.

11.2.2 The statute itself denudes the directors of certain powers and places restrictions on the company's making loans to directors (section 103), on the director's holding an office of profit (section 104), or on contracts between the company and the director or the firm of which he is a partner or any partner of such firm or the private company of which he is a member or director (section 105). Section 100 prohibits any assignment of the office of a director. Section 107 provides that the directors of a public company or of a subsidiary of a public company shall not, except with the consent of the company in general meeting, sell or dispose of the undertaking of the company or remit any debt due by a director.

Regulations 72 to 76 in the Schedule 1 regulations to the Act of 1994 deal with the powers and duties of directors. Regulation 73 empowers the directors from time to time to appoint one or more of their body to the office of managing director or manager for such term and at such remuneration whether by way of remuneration by salary or commission or participation in profits or partly in one way and partly in another as they may think fit and a director so appointed shall not while holding that office, be obliged to retire by rotation or to be taken into account in determining the rotation of retirement by directors, but his appointment shall be subject to determination *ipso facto,* if he ceases from any cause to be a director or if the company in general meeting resolve that his tenure of the office of managing director or manager be determined.[1] Also, this regulation will now be read as subject to the provisions of section 109 of the Act which requires the consent of the company in general meeting for appointment of a managing director.

Regulation 74 further restricts the power of the board vis-a vis the general meeting. It provides that the amount for the time being undischarged of monies borrowed or raised by the directors for the purposes of the company (otherwise than by the issue of share capital) shall not at any time exceed the issued share capital of the company without the sanction of the company in general meeting. In *T.R. Pratt vs M.T. Ltd*[2] the Judicial Committee of the Privy Council has held that where monies borrowed in excess of the authority of the directors have been utilised in meeting the legitimate expenses of the company, objection cannot be raised in later stages that the company is not bound to pay interests on the sum borrowed in excess of that authority or to repay the whole sum advanced. Regulation 75 requires the directors to keep a register of directors, to comply with the provisions of the Act in regard to the registration of the particulars of mortgages and charges affecting the property of the company or created by it and to send to the Registrar an annual list of members, and a summary of particulars relating thereto and notice of any consolidation or increase of share capital or conversion of shares into stock and copies of special resolutions and a copy of the register of directors and notifications of any changes therein.

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1 As to the effect of such termination see section 11.1.14 above.

2 AIR 1938 P.C. 159.

Regulation 76 requires the directors to cause minutes to be made in books provided for the purpose of all appointments of officers made by the directors, of the names of the directors present at each meeting of the directors and of any committee of the directors, and of all resolutions and proceedings of all meetings of the company, of the directors and of committee of directors; and every director present at any meeting of directors or committee of directors shall sign his name in a book kept for that purpose.

11.2.3 As is pointed out in *Palmer's Company Law,*[1] the powers of the directors are limited in two ways : first, being agents of the company, the directors can do nothing which the company itself, their principal, cannot do under its memorandum of association and any purported act by them which is ultra vires the company will be invalid and of no effect and secondly, when acting within the powers of the company, the directors are limited to the powers which the company has delegated to them. If they act ultra vires their own powers, but intra vires the company's, the latter may ratify their acts in a general meeting. If, however, acts by directors in excess of their authority are not ratified by the company, they may be liable to those with whom they deal on the footing that they are taken to warrant their authority.[2]

The division of powers between the directors of the company and the company as a corporate body often raises question of some difficulty as regards the exact line of division. Articles generally give a certain number of specific powers to the directors and further add general provision that the directors may exercise all powers of the company, not required by the articles or the Act to be exercised by the company in general meeting. As Palmer points out,[3] where such a general residuary clause exists it is not necessary further to have a special article conferring specific powers on the directors to do or not to do certain acts. In fact such an article creates confusion and is often a fruitful source of controversy as to its exact meaning. Here again, English cases provide illuminating examples.

Thus, in *In re Gresham Life Assurance Society*[4] where the directors refused to register a transfer of shares, it was held that they were not bound to disclose their reasons for rejecting a transferee, provided they had fairly considered the question at a meeting of the board, and that, in the absence of evidence to the contrary, the Court would take for granted that they acted reasonably and bona fide. But, if there is evidence to show that directors who have such a power, have exercised it capriciously or unfairly then the Court has jurisdiction to interfere.

As Professor L.C.B. Gower puts it, until the end of the nineteenth century it seems to have been generally assumed that the principle remained intact that the general meeting was the supreme organ of the company and that the board of directors was merely an agent of the company subject to the control of the company in general meeting.[5] The case of *Isle of Wight Railway vs Tahourdin*[6] is then cited. Here the Court refused an application by the directors of a statutory company for an injunction to restrain the holding of a general meeting. Cotton L.J. said :[7]

> ... It is very strong thing indeed to prevent shareholders from holding a meeting of the company, when such a meeting is the only way in which they can interfere, if the majority of them think that the course taken by the directors, in a matter *intra vires* of the directors, is not for the benefit of the company....

With the turn of the century twentieth however, a different principle was introduced in the case of *Automatic Self-Cleansing Filter Syndicate Co. vs Cunninghame.*[8] Here, the

1 20th Ed.p.519
2 Starkey vs Bank of England [1903] A.C. 114.
3 supra.at p.520
4 (1872) L.R. 8 Ch.App 446.
5 Principles of Modern Company Law 5th. Ed. pp.147-148.
6 (1883) 25 Ch.D.320.
7 ibid. at page 329.
8 [1906] 2 Ch 34.

company had power under its memorandum of association to sell its undertaking to another company having similar objects, and by its articles of association the general management and control of the company were vested in the directors, subject to such regulations as might from time to time be made by extra ordinary resolution and the directors were empowered to sell or otherwise deal with any property of the company on such terms as they might think fit. At a general meeting of the company a resolution was passed by a simple majority of the shareholders for the sale of the company's assets . The directors being of the opinion that a sale on those terms was not for the benefit of the company declined to carry the sale into effect. It was held upon construction of the articles that they were not bound to do so. Collins M.R said at page 43 of the judgment :

> It is by the consensus of all the individuals in the company that these directors became agents and hold their rights as agents. It is not fair to say that a majority at a meeting is for the purposes of this case the principal so as to alter the mandate of the agent....

The apparent basis of this case was that the articles constituted a contract between the corporators by which the members had agreed that the directors and the directors alone shall manage.

The language of Regulation 72 of Schedule 1 Regulations to the Act is however clear that the delegation of powers to the Board is nevertheless, 'subject to such regulations being not inconsistent with (the Articles or the Act) as may be prescribed by the company in general meeting'. How then is the paramountcy of the company in general meeting cut down? Also, if the company in general meeting can, by passing a special resolution amend the articles and force the directors to obey a resolution of the general meeting then why they cannot do it by an ordinary resolution ?

In *Gramophone and Typewriter Ltd vs Stanley,*[1] an English company, owning all the shares of a German company, was not liable to pay income tax in England, for shareholders do not automatically run the company. Buckley L.J. commented that " the directors are not servants to obey directions given by the shareholders as individuals; they are not agents appointed by and bound to serve the shareholders as their principals."

In *Marshall's Valve Gear Co. vs Manning, Wardle and Company*[2] the Court held that it was for the members in general meeting to decide whether an action should be brought and that the directors could not restrain the company from acting on their decision. In the following year, however, the trend reversed again when the Court of Appeal followed the Cunninghame's case (supra) in *Salmon vs Quin and Axtens*[3] and were upheld by the House of Lords.

In *Shaw and Sons (Salford) Ltd vs Shaw*[4] it was held that a resolution of the members disapproving the commencement of an action was a nullity. Greer L.J. enunciated the modern doctrine as follows :[5]

> ...A company is an entity distinct alike from its shareholders and its directors. Some of its powers may, according to its articles, be exercised by directors, certain other powers may be reserved for the shareholders in general meeting. If powers of management are vested in the directors, they and they alone can exercise these powers. The only way in which the general body of shareholders can control the exercise of the powers vested by the articles in the directors is by altering their articles, or, if opportunity arises under the articles, by refusing to re-elect the directors of whose actions they disapprove. They cannot themselves usurp the powers which by the articles are vested in the directors any more than the directors can usurp the powers vested by the articles in the general body of shareholders....

In *Scott vs Scott*[6] it was held on the same grounds, that resolutions of a general meeting, which might be interpreted either as directions to pay an interim dividend or as instructions to make loans were nullities.

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1 [1908] 2 K.B.89.
2 [1909] 1 Ch 267
3 [1909] 1 Ch 311
4 [1935] 2 K.B. 113.
5 ibid. at p. 134
6 [1943] 1 All E.R. 582.

The modern rule, at least in England therefore, is that under an article in terms of Schedule 1 the members in general meeting cannot give directions on how the company's affairs are to be managed, nor can they over-rule any decision come to by the directors in the conduct of its business. Also, as Buckley thinks[1] and Greer L.J.[2] and Prof. Gower support it before the recent amendments in the Table A Articles of the English Company Law,[3] this rule applies even as regards matters not expressly reserved to a general meeting by the Act or the articles. It seems that both the general meeting and the board may be the company according to whether they are acting under the reserved powers or an express or general delegation respectively.[4]

But where the articles give the board of directors the power of appointing an additional director and owing to the differences between the directors , no board meeting can be held for the purpose, the company retains power to appoint additional directors in general meeting.[5] Similar rule will apply if the number of directors has fallen below the minimum number required for a quorum or if a company has no directors.[6]

It was held in *Indian I. and S. Co vs Dalhousie Holdings Ltd.*[7] that where an article of association of a company expressly vested both the control of the company and its business in the directors, the transfer of shares which are company's properties comes within the meaning of the term " business of the company " and its control and hence the directors can transfer company's shares.[8]

11.2.4 **Delegation of Powers by Board of Directors** – It has been pointed out in Lahore that whether there has been a valid delegation by the directors of their powers under the articles to a committee of directors or any one or more of themselves, is always a question of fact, and the determination of the question may involve incidentally the question whether the directors delegating were properly qualified or were otherwise acting within their powers of delegation.[9]

The powers delegated by the articles to the directors must be exercised by them collectively, for the company is entitled to the benefit of their combined wisdom and experience. So , unless power to do so is contained in the articles, directors are not entitled to delegate their authority to others, either to one or more of their number or to outsiders, for the general rule of law is *delegatus non potest delegare*. It is usual, however, for articles of association to contain clauses empowering the directors to delegate their duties. Regulation 73 of Schedule 1 to the Act of 1994 gives power to the directors to appoint from time to time one or more of their body to the office of managing directors or manager for such term and at such remuneration as they may think fit and a director so appointed shall not, while holding that office, be subject to retirement by rotation or taken into account in determining such rotation, but his appointment shall be subject to determination ipso facto if he ceases from any cause to be a director or if the company in general meeting resolve that his tenure of the office of the managing director or manager be determined. Regulation 92 of Schedule1 Regulations provides :

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1 Companies Act, 12th Ed.p.859.

2 [1935] 2 K.B. p.154

3 Modern Company Law, 2nd.Ed. p.123

4 For other cases on the subject. see Blair Open Hearth Furnace Co. vs Reigert [1913] 108 L.T. 665,Worcester Corsetry Ltd vs Witting [1936] 1 Ch. 640, Thomas Logan Ltd vs David [1911] 104 L.T. 914,Foster vs Foster [1916] 1 Ch. 532. Northern Counties vs. jackson and Steeple (1974) 1 WLR 1133 at 1143.

5 Barron vs Potter [1914] 1 Ch.D. 895.

6 Lord Hailsham in Alexander Ward & Co. Ltd. vs Samyang Navigation Co. Ltd [1975] Scottish Cases (H.L.) 26 at p. 47; [1975] 2 All ER 424.

7 AIR 1957 Cal 293

8 On this subject, also see Topandas vs Yeotmal Electric Supply Co.AIR 1940 Sind 89, Prasanna Venkatess Rao vs Trichinopoly District Co-operative Central Bank Ltd.(1940) 2 Mad L.J. 488.

9 Bank of Peshawar Ltd.vs Madho Ram AIR 1917 Lah 351.

The directors may delegate any of their powers to committees consisting of such member or members of their body as they think fit; any committee so formed shall, in exercise of the powers so delegated, conform to any regulations that may be imposed on them by the directors.

Where Schedule 1 articles apply, the board may delegate any of its powers to a committee of directors or to a managing director.

Where powers are delegated to a committee they may be general, including all the powers of the board, or limited to a particular matter, e.g., negotiating a contract, or to a particular function, as examining and passing transfers for registration and sealing share certificates. It is also possible to have a committee without any actual delegation of responsibility, as when it is not empowered to take a decision and put such decision into force, but merely ascertains facts with a view to recommending to the board what action should be taken. Under such provisions the board may appoint a committee merely to make recommendations to it, so that it may take the final decision itself, or it may empower a committee or attorney to exercise any of its powers and to bind the company without further reference to it. But, in the absence of a provision in the articles or a valid article to the contrary, it has been held in England that all delegations of power may be revoked either expressly or by the board exercising the delegated powers itself.[1] Furthermore, appointments to committees are revocable by the board, even though the member of the committee was appointed for a fixed period.[2] It is therefore impossible for the board to divide its powers permanently between itself and its committees in the same way as the articles divide the powers of the company between the members and the board.[3]

11.2.5 **Managing Directors** – The power that a managing director has, is delegated to him by the board of directors. Where there is an article in terms of Article 73 of Schedule 1 Regulations pursuant to which a managing director is appointed and a service agreement is entered into between him and the company, care is necessary in the drafting of the agreement so as to ensure that it sets out exactly what is intended by the parties. In modern company practice, a managing director, in the great majority of cases, combines the position of director and of employee and the validity of his appointment and the scope of his duties have to be gathered from the provisions of the articles and the terms of his contract with the company.[4]

In Harold Holdsworth and Co. vs Caddies,[5] Mr. Caddies was appointed managing director of a company for a period of five years by an agreement which provided that he should be appointed a managing director of the company and as such managing director he would perform the duties and exercise the powers in relation to the business of the company and its subsidiaries which might from time to time be assigned to or vested in him by the board of directors of the company. The agreement further provided that he should devote his whole time to his duties and should obey the orders and directions of the board. Differences having arisen, the board resolved, while his five year period was still running that he should confine his attention to one of the company's subsidiaries only. Mr. Caddies claimed that this deprivation of his powers of managing director of the parent company, was a repudiation of his agreement and he brought an action for damages for breach of contract. The House of Lords held that no breach had in fact occurred ,since his appointment as managing director did not limit the powers of the board and it was within the powers of the board to confine his duties to a subsidiary company. The agreement stated that Mr. Caddies should perform his duties which were assigned to him by the board in relation to the business of the company and its subsidiaries; it was successfully argued on behalf of the company that a direction to

1 Huth vs Clarke (1890) 25 Q.B.D.391.

2 Manton vs Brighton Corporation [1951] 2 All E.R. 101.

3 Horn vs H.Foulder and Co. [1908] 99 Law Times 524. See also the cases of Re County Paladine Loan and Discount Co.(1874) 9 Ch.App.691, U Ba Din vs Janki Devi AIR 1938 Rang.447(an extreme example of the principle that the board having been delegated the power it enjoys, it cannot delegate another to do its job).

4 Palmer's Company Law 20th Ed. p.551.

5 [1955] 1 W.L.R. 352

confine his attention to one of the subsidiaries was entirely consistent with that provision. The position of a managing director was elaborately discussed in the light of English and Scottish decisions in the Scottish case of *Anderson vs James Sutherland Ltd,*[1] in which it was held that a managing director performs two sets of functions and acts in two capacities. Apart from being a director, he is a party to a contract of employment with the company.

A managing director may have implied power to enter into certain agreements on behalf of the company even though there has been no express delegation of the power to him by the board. On the other hand the implied authority of a managing director is not limitless. He has no such implied power to act contrary to the articles and resolutions of the company and/or the board or to use the company's money to bribe someone for the benefit of the company.[2] A managing director has the *locus standi* to ask for custody and records of the company.[3] A managing director cannot assign a bond in favour of company after his resignation has been accepted.[4] Where a company's managing director, who had the powers of all the directors, was elected to the board of two other companies to represent and protect the interests of the first company, it was held that it was his duty to communicate to the first company any material fact which came to his knowledge as director of either of those companies, and notice of such fact could be imputed to the first company.[5] A pronote signed by a managing director can bind the company.[6]

The power to appoint a managing director rests with the company and unless special provision is made in the articles, the power cannot be delegated. Where power was given by the articles to the company to appoint and remove directors and by another article the board was given power to appoint a managing director, it was held by the Bombay High Court that on a proper construction of the articles, the right to appoint a managing director having been delegated to the board, the board had also implied power to remove a managing director.[7] The Court also held that a managing director who was not a shareholder, had neither such legal status nor legal character as would entitle him in law to file a declaratory suit for a declaration that he continued to be the managing director and therefore entitled to act and to exercise his rights as such. Even assuming that he was entitled to file such a suit, the Court would not decree specific performance in his favour, because it was open to the company in general meeting to put an end to such status or legal character. But the Lahore High Court has held that a suit by a managing director for a declaration that he has been unlawfully removed from his office is maintainable although a contract to appoint a person as managing director cannot be specifically enforced,[8] because the contract is a contract of service and no injunction can be granted in such a case restraining a company from removing a managing director. It would be contrary to public policy to impose on an unwilling principal an agent whom he did not wish to employ, especially as there was nothing to prevent an agent, whose contract of agency had been wrongfully terminated, from bringing an action for damages.[9]

Where a managing director is appointed under an article like Regulation 73 of Schedule 1 to the Act of 1994 (corresponding to Regulation 84 of the English Act) his appointment may be prematurely determined by his removal from his directorship,[10] but the company will be liable in damages if this is in breach of his service.[11] In the Australian case the articles empowered the company to remove a director, subject to the provisions of an agreement. The

1 [1941] Scottish Cases 203.
2 See Charlesworth and Morse: Company Law 14th Ed. p.391.
3 In re Chandigarh Tourist Syndicate Ltd [1978] 48 Comp. Cas.267.
4 Varkey Souriar vs Keraleeya Banking Co. Ltd. [1957] 27 Comp. Cas. 591.
5 T.R.Pratt Ltd vs E.D.Sassoon & Co Ltd [1936] 6 Comp. Cas 90.
6 K.K.Rohatgi vs State Bank of India [1980] 50 Comp. Cas 722.
7 Major Shanta Shamsher Jang Rana vs Kamani Bros. (1958) Bom. L.R. 1024.
8 Gulab Singh vs Punjab Zamindar Bank AIR 1942 Lah 47
9 Also see Joginder Singh Palta vs Time Travels Ltd [1984] 56 Comp. Cas 103 Cal.
10 Southern Foundries Ltd vs Shirlaw [1940] A.C.701.
11 Nelson vs James Nelson and Sons Ltd [1914] 2 K.B. 770 and Carrier Australasia Ltd. vs Hunt [1939] 61 Commonwealth Law Reports 534.

articles were altered so as to delete the words" subject to...any agreement" and then the managing director was removed from his directorship. He was held to be entitled to damages.[1] However, if the managing director has no independent contract of service, and is entirely dependant on the articles for his protection then if his service is terminated according to the articles he has no cause of action for damages.[2] Where directors have a discretionary power to dismiss a managing director, this power must be exercised in good faith in the interests of the company and not for some other purpose such as appropriation of the managing director's shares.[3] The same authors also comment that if, where the appointment of a managing director is in fact void, he performs services which are accepted by the company, it has been held that he is entitled to remuneration.[4] But see the case of *Guinness Plc vs Saunders*[5] where the House of Lords refused a quantum merit claim by a director, but in rather different circumstances, when there was no doubt as to the validity of the appointment.

A managing director may have a dual capacity. He may both be a director as well as an employee. In the capacity of a managing director he may be regarded as having not only the capacity as person of a director but also has the persona of an employee, or an agent depending upon the nature of his work and terms of his employment.

The nature of his employment may be determined by the articles of association of the company and/or the agreement, if any, under which a contractual relationship between the director and the company has been brought about.[6] Also see *Lee vs Lee's Air Farming Ltd*[7] where the designation was "governing director" but held to be an employee by the Privy Council. Managing directors and whole time or non-rotational and ordinary directors are entirely separate officers. Where term of managing director expires he ceases to be managing director and cannot continue as managing director.[8]

Restriction on Appointment of Managing Director – Section 2(m) of the Act of 1994 defines a managing director as a director who, by virtue of an agreement with the company or of a resolution passed by the company in general meeting or by its directors or by virtue of its memorandum or articles of association, is entrusted with substantial powers of management which would not otherwise be exercisable by him, and includes a director occupying the position of a managing director, by whatever name called. A power to do acts of a routine nature, i.e., to affix common seal of the company to any document or to draw and endorse any check etc or to sign any certificate of share or to direct registration of transfer of shares shall not be deemed to be substantial powers of management. A managing director shall exercise his powers subject to the superintendence, control and direction of the directors.

The definition given in the Act reflects the case law on the modes of appointment and the nature of duties of a managing director given above.

Section 109 of the Act of 1994 imposes restrictions on appointment of managing directors. No public company and no private company which is a subsidiary of a public company shall appoint any person as managing director if he is managing director or manager of another company. This condition is in line with similar provisions in India.[9] Our Act however, imposes a second condition, namely that no appointment shall be made without the consent of the company in general meeting. The Government may, by order, permit any person to be appointed as a managing director of more than two companies if the Government is satisfied that it is necessary that the companies should, for their proper working, function as a single unit and have a common managing director.

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1 Also see Shindler vs Northern Raincoat Co. Ltd [1960] 1 WLR 1038.
2 Read vs Astoria Garage (1952) Ch 637.
3 Charelesworth and Morse : Company Law 14th Ed. p. 392.
4 Craven-Ellis vs Canons Ltd [1936] 2 K.B. 403.
5 [1990] 1 All E.R. 652.
6 Ram Prashad vs CIT [1972] 42 Comp. Cas.544 (S.C.).
7 [1961] A.C. 12 P.C.
8 Shishu Ranjan Dutta vs Bhola Nath Paper House Ltd [1983] 53 Comp. Cas. 883. Cal.
9 Section 316.

Section 110 restricts the term of office of managing director to five years at a time. He may be reappointed for terms not exceeding five years on each occasion. This is similar to section 317 of the Indian Companies Act.

Other than in this country, nowhere else in the major commercial centers of the world the appointment of a managing director is required to be sanctioned in a general meeting. In India this has to be approved unanimously by the members present in a board meeting of which notice has been given to all the directors. The requirement that a managing director must be approved by the members in general meeting denudes the board of its very vital powers to conduct management of the company and subjects the managing director to harassment at such general meetings. He has to appease every shareholder whose interest may be selfish and not conforming to the interest of the company.

11.2.6 **Proceedings of the Board of Directors** – Directors generally exercise their powers and carry on the business of a company by means of resolutions passed at board meetings. Proceedings at meetings of directors are governed by the company's articles. More often than not, the articles empower the directors to conduct their proceedings as they think fit. Regulation 88 of Schedule 1 to the Act empowers the directors to 'meet together for the despatch of business, adjourn and otherwise regulate their meetings as they think fit'. The article continues to say that questions arising at any meeting shall be decided by a majority of votes. In case of an equality of votes, the chairman shall have a casting or second vote. A director may, and the secretary on the requisition of a director shall, at any time summon a meeting of the directors. These are standard provisions having their origin in the English company law. There is no statutory provision to guide a meeting of the directors and the relevant rules are contained in Regulations 88 to 94 in the First Schedule to the Act. They can, therefore be modified by any company, but unless expressly excluded, they will apply. If so, then the quorum necessary for the transaction of the business of the directors may be fixed by them and , unless so fixed, the number will be three, when the number of directors exceeds three.[1] Under Regulation 90, continuing directors may act notwithstanding any vacancy in their body, but, if their number is reduced below the number fixed as the quorum, they may act only for the purpose of increasing the number of directors to that number or of summoning a general meeting of the company. Under the subsequent articles, the directors may elect a chairman at their meetings and are given power to delegate their authority to a committee.

It is a cardinal rule of corporation law that, prima facie, a majority of its members is entitled to exercise the powers of the corporation and where no special provision is made, the whole are bound not only by the majority of members, but by the majority of those present at a regular corporate meeting, whether the number present be a majority of the total membership or not. This rule is equally applicable when a power of the corporation is delegated to a smaller body. Therefore, unless a construction of the articles of association of a company leads to the conclusion that there was an intention to supersede the ordinary rule, it must be held that where no quorum is fixed, the acts of a major part of the directors for the time being are valid.[2] Where two out of three directors resigned, the question arose how the accounts would be approved. The Court held that a general meeting could be called by the shareholders, the director or the Court to pass the accounts.[3] If there were an article like Regulation 90 of Schedule 1 Regulations then this problem would not arise as then the single director could co-opt others to the board or summon a general meeting. Unless he did so, he could not carry on the management of the company, for it has been held that, where rules lay down a quorum, a lesser number cannot transact any binding business by circulation, even though the rules permitting despatch of business by circulation do not stipulate the number to

1 Regulation 89.
2 Ganesh Flour Mills Co. vs Jag Mohan Saran AIR 1942 Lah 61.
3 Sorabji vs Scind Punjab Co. (1906) 8 Bom. L.R. 478.

whom the papers ought to be circulated.[1] Directors interested in a resolution cannot vote[2] and so cannot be counted as constituting the quorum.[3]

If the requisite quorum is not present, the meeting is irregular, and cannot transact business.[4] An irregular meeting can, however, be regularised by a subsequent regular meeting.[5]

11.2.7 **Notice of Board Meetings** – Section 95 of the Act provides that notice of every meeting of the Board of Directors of a company shall be given in writing to every director for the time being in Bangladesh and at his address in Bangladesh otherwise the Board Meeting is invalid.[6] This section is new and puts at rest the problems that used to arise when problematic directors were by-passed when important meetings were held. However, would this mean that if the articles or the directors decide that meetings may be held at fixed times; e.g., the first Saturday of every month, then also notice of every meeting must be given? Previously it has been held that in these cases no specific notice need be given.[7] The Lahore High Court has held before the introduction of this section in the Act that such a general notice may not suffice in certain circumstances.[8] and the articles are not a substitute for a general notice. The Supreme Court of India has held in *Parmeshwari Prasad Gupta vs Union of India*[9] that failure to send notice of board meetings will render the resolutions passed at the meeting null and void. Notice of adjournment of a meeting need not be given unless otherwise provided in the articles.[10] If notice of board meeting not given but all directors attend it and do not object to the absence of notice, meeting will be deemed to be validly held.[11] But see *Bharat Fire and General Insurance Co. Ltd vs Parameswari Prasad Guptam.*[12] The onus is, however, on those who allege that notice was not given. Just because an entry has been made in the register of directors that a particular director has ceased to hold office, it does not follow necessarily that no notice was given to him. [13] This case also held that sometimes by an accidental omission to give the notice to a director, a meeting of directors is rendered irregular, but the directors, nevertheless, transact business on behalf of the company and in such a case the rule in *Royal British Bank vs Turquand*[14] applies, and outsiders will not, as a general rule, be prejudiced by such irregularities. If there is an apparent breach of the provisions of section 95 then an injunction can be given to restrain the company from acting on the basis of the impugned meeting.[15] The High Court Division had earlier held that a written notice must be given to all the directors.[16] No fresh notice is needed for an adjourned meeting of the Board for transactions of unfinished business. Also no notice is needed if a director refuses to attend the adjourned meeting.[17]

Section 96 of the Act requires that board meetings of every company shall be held at least once in every three months and at least four such meetings shall be held in every year. This provision is new and unless the management of small companies are alert, will be

1 In re Mirza Ahmad Namazi AIR 1924 Mad 703.
2 section 131 of the Companies Act.
3 Pandalai vs South Indian General Assurance Co AIR 1942 Mad.95.
4 In the Matter of Karnal Distillery Co PLD(1956) Lah 731.
5 Re State of Wyoming Synd. [1901] 1 Ch.431.
6 Jalaluddin Jaffar Ali Husein vs Tahmid Ahmed 6 MLR (HCD) 53 = 52 DLR 141
7 Arunachalam vs Kaleeshawar Mills [1956] Comp. Cas.431 and Palmer's Company Law 20th Ed.P.544.
8 In the Matter of Karnal Distillery Co PLD(1956) Lah 731.
9 [1974] 44 Comp. Cas.1m 1 (SC)
10 Promod Kumar Mittal vs Southern Steel Ltd [1980] 50 Comp Cas. 555 (Cal).
11 Guide to the Companies Act, 11th Ed p.845 by A.Ramaiya.
12 AIR 1968 Delhi 68 and [1974] 44 Comp. Cas.1.
13 In re Peninsular Life Assurance Co. AIR 1936 Bom.24.
14 (1856) E.and B.327
15 Md. Mohibul Ahsan vs Ittefaq Group of Publications Ltd. (1998) BLD (AD) 207.
16 Ittafaq Group Publications Ltd. ñvs- Arab Bangladesh Bank Ltd. and others 50 DLR (1998) 597.
17 S I Khan vs Integrated Services Ltd. and others 7 MLR (HC) 56.

caught unawares. Private companies should have been excluded from the purview of this section as most of these are family concerns and meet only to record attendance. The section however does not say what will be the effect of non-compliance of this provision.

Section 98 of the Act provides that the acts of a director shall be valid notwithstanding any defect that may afterwards be discovered in his appointment or qualification. The section does not cover cases where there is a total absence of appointment or mere usurpation of authority.[1] The section will protect only bonafide acts and not where they are done with notice that they were done wrongfully or illegally. Knowingly acting after termination of office, and acting with knowledge of defect or disqualifications are not protected.[2] As to the protection given by-law to the outsiders if the board was not properly constituted, also see the discussion on the *Turquand Rule* in section 11.3.1 below.

11.2.8 **Ratification by the Company** – Unlike a transaction which is ultra vires the company, an act which is only beyond the authority vested in the board may be ratified by the shareholders in general meeting in accordance with the rule of agency law that the unauthorised act of an agent may be ratified by his principal. If the act is within the powers of the company, consent of all the shareholders, even if given irregularly, will validate it. For example, the law insists that only a resolution duly passed at a meeting of the company can be regarded as an act of the company itself. In a number of cases, however, the question has arisen whether something less formal than a resolution passed at a duly convened meeting will suffice. In other words, can the veil of incorporation be lifted so as to equate a decision of the members with a decision of the company itself? English case law on this point may be illumunating.

In the early case of *Re George Newman Ltd.*[3] it was held that individual assents given separately may preclude those who have given them from complaining of what they have sanctioned, but for the purpose of binding a company in its corporate capacity individual assents given separately are not equivalent to the assent of a meeting. Lindley L.J. observed[4]:

> ...Directors have no right to be paid for their services and cannot pay themselves or each other or make presents to themselves out of the company's assets unless authorised so to do by the instruments which regulate the company or by the shareholders at a properly convened meeting....

Later on, however, there was a shift towards a more liberal application in favour of lifting the veil of incorporation and a later Court of Appeal held in *Re Express Engineering Works Ltd*[5] that a resolution passed at a meeting of directors, at which all the shareholders were present, could not be impugned, notwithstanding that it was beyond the powers of the directors as such. In this case all the shareholders met and sanctioned a contract to sell the company a property and issue debentures to secure its price. They described themselves as directors. It was held that there being no suggestion of fraud, the company was bound in a matter intra vires the company by the unanimous agreement of its members. Warrington L.J. said at page 470 of the judgment :

> ...It happened that these five directors were the only shareholders of the company, and it is admitted that the five, acting together as shareholders, could have issued these debentures. As directors they could not, but as shareholders acting together they could have made the agreement in question. It was competent to waive all formalities as regards notice of meetings etc., and to resolve themselves into a meeting of shareholders and unanimously pass the resolution in question.....

Similarly, in *Re Oxted Motor Co.*[6] it was held that all the members might waive the normal length of notice, a provision which is now found in the Act.[7] The English Courts

1 Morris vs Kanssen [1946] 1 AllE.R. 586(HL).
2 Albert Judah vs Ramapada Gupta AIR 1959 Cal 715.
3 [1895] 1 Ch. 674,686.
4 ibid.
5 [1920] 1 Ch. 466
6 [1921] 3 K.B. 32.
7 Section 85(1)

again held that a company was bound in a matter intra vires the company by the unanimous agreement of all its incorporators.[1] If all the corporators in fact, assent to a transaction that is intra vires the company, though ultra vires the board, it is not necessary that they should hold a meeting in one room or one place to express that assent simultaneously. In this case there had been no meeting at all; the members had merely informally ratified a debenture granted by the directors acting beyond their powers.[2] In *Re Barry Artist Ltd*[3] the judge confirmed a special resolution to reduce the share capital which in fact was a unanimous written resolution but not passed in a meeting called for the purpose but did so after lot of hesitation and warning.

But as Professor Gower points out,[4] it is not clear whether in any circumstances, something less than an agreement of all members entitled to vote can be treated as equivalent to a resolution passed at a general meeting. In the case of *E.B.M. Bank vs Dominion Bank*[5] the holders of two shares in the company had omitted to ratify the debentures and the Privy Council held that as the company, acting through its directors, and not by its shareholders in general meeting, had purported to apply its property for the benefit of those directors, the transaction was not enforceable and the Court would not enquire whether the company had derived any benefit from it. The Privy Council, in an appeal from India held that to render valid an act of the directors of a company which was ultra vires, the acquiescence of the shareholders must be of the same extent as the consent which would have given validity from the first – the acquiescence of each and every shareholder of the company.[6] Of course, the acquiescence cannot be presumed unless knowledge of the transaction can be brought home to every one of the shareholders. By knowledge of the transaction, Lord Chelmsford, who was delivering the opinion of the Council, clearly meant knowledge of the invalidity of the transaction. There can be in truth no ratification without an intention to ratify without knowledge of the illegality. The Judicial Committee had followed the decision in *Irvine vs Union Bank of Australia*[7] in this case. The Privy Council also held in *Ho Tung vs Man On Insurance,*[8] that a mere tacit acquiescence over a long period may regularise the absence of a resolution. In *Re Bailey Hay and Co Ltd*[9] three out of five shareholders did not attend a meeting notice of which was given one day short. The meeting was to wind up a company. Later on the absenting members objected to the liquidation but the liquidator was not told that the validity of his appointment was disputed until three years later. The doctrine of laches was applied and the judge held that it would be " practically unjust" to the creditors and the liquidator of the company to declare certain payments made by the company as void.

To sum up, the position regarding ratification of corporate acts is :

1) The constitution of the company remains the basic source from which the respective powers of the board of directors and the shareholders in general meeting are derived ;
2) the board of directors cannot exceed their powers and bind the company by entering into a transaction (unless it falls within the Turquand Rule, discussed below) even if the matter is intra vires the company, if it is otherwise outside the powers given to the Board by the articles, and not ratified by the company in general meeting;
3) the company is bound by the transaction, if all the shareholders ratify it, even if it is done in a meeting not duly convened;

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1 Parker and Cooper Ltd vs Reading [1926] Ch 975.

2 For other cases on this point see Re Pearce Duff & Co Ltd [1960] 1 WLR 1014;Re Duomatic Ltd.[1969] 2 Ch. 365;Re Bailey Hay & Co Ltd [1971] 1 WLR 1357;Re Gee & Co(Woolwich) Ltd [1975] Ch. 52;Cane vs Jones [1980] 1 WLR 1451; Re Moorgate Mercantile Holdings Ltd. [1980] 1 WLR 227,242;G Multinational Gas Co. vs Multinational Gas Services [1983] 1 Ch. 258,289.

3 [1985] 1 WLR 1305.

4 Principles of Modern Company Law, 5th Ed. page 136.

5 [1937] 3 All E.R. 555.

6 Pramilla Devi vs People's Bank of Northern India [1938] 43 C.W.N. 205.

7 (1877) 12 App.Cas 366.

8 [1902] A.C. 232.

9 [1971] 1 WLR 1357.

4) ratification may be by way of tacit acquiescence over a long period.

11.3.1 **The Turquand Rule** – This rule was enunciated by the courts to mitigate the effects of the constructive doctrine notice. Every company is required to file with the office of the Registrar copies of the memorandum and articles of association so that anyone who deals with a company has constructive notice of the same. As that doctrine has now been abolished in England the *Turquand Rule* is of less significance now in England and is confined to where the third party's dealings have been with some other officer or agent other than the board. The position in Bangladesh is however, similar to the situation prevailing in England before the recent amendments there and the text books and case law prior to those amendments are of relevance here.

Persons dealing with directors will be presumed to have notice of the instruments conferring authority on them such as the memorandum and the articles of the company. These documents are required by section 23 of the Act of 1994 to be registered with the Registrar. In this respect the memorandum and the articles are public documents. Persons dealing with companies are therefore, bound to enquire into (and if they fail to enquire, will be fixed with notice of) the contents of the articles and the memorandum. Any action of a director of a company which is contrary to the provisions of the memorandum and articles of the company will not therefore be generally binding on the company, even though the outsider dealing with the company is unaware of the same. Outsiders are not, however, bound to enquire and will not, therefore, be presumed to know whether all the regulations of the company relating to its internal management and the conduct of its business, have been duly and properly complied with or not. In other words, they will not be fixed with notice of matters regarding the indoor management of the company and they will not be affected by any irregularities that may take place or have taken place therein. The law on this point was first formulated in the famous English case of *Royal British Bank vs Turquand*[1]. A string of cases have since then developed the law and the rights of third parties *vis a vis* the company when the directors enter into a contract regarding which the internal management was not in proper order.

The rule , which is based on a general presumption of law, is eminently practical, for business could not be carried on if a person dealing with the ostensible agents of a company was compelled to call for evidence that all internal regulations have been duly observed. Thus, where the articles give power to borrow with the sanction of an ordinary resolution passed at a general meeting, a lender who relies on this power need not enquire whether such sanction had in fact been obtained. He may assume that it has, and if he is acting bona fide he will, even though the sanction has not been obtained.

The legal reason for this rule, as Mr. Pennington points out, is that such a person has no right to insist on proof by the directors that the provisions of its memorandum and articles of association have been complied with, and he cannot, therefore, be deemed to have constructive notice of any failure to comply with which he has no means of discovering[2]. Of course if he knows that there has been some failure to comply,[3] or knows facts which would lead a reasonable man to enquire further and thus discover the failure,[4] he will not be able to rely on the rule and the company may refuse to be bound by the transaction.

In *Royal British Bank vs Turquand*[5], the board of directors were authorised to borrow on bond such sums as should from time to time be authorised by a general resolution of the company. Under the deed of settlement, which was the forerunner of the modern memorandum and articles, the directors' authority to borrow was expressly made subject to the consent of the company in general meeting. The board borrowed money from the bank on

1 (1856) 6 E.& B. 327.

2 Principles of Company Law 1st. Ed p.82. and County of Gloucester Bank vs R.M.Steam and House Colliery [1895] 1 Ch. 629,636.

3 Howard vs Patent Ivory Manufacturing Co. [1888] 38 Ch.D. 156.

4 Morris vs Kanssen [1946] 1 All E.R. 586

5 Supra

a bond bearing the company's seal. It was held, that, even if no resolution had in fact been passed by the company in general meeting, the company was nevertheless bound. Since under the deed, the directors might have had authority, the bank was entitled to assume that in fact they had obtained it. The law as it stood before the amendments in the English company law abolishing the doctrine of constructive notice, was summarised by Professor Gower in the form of six rules in the second edition of his book Modern Company Law pp.144-159 as follows:

i) Anyone dealing with a company is deemed to have notice of its public documents. Hence any act which is contrary to these documents will not bind the company, unless subsequently ratified by the company acting through its appropriate organ.

ii) But provided that everything appears to be regular so far as this can be checked from the public documents, an outsider dealing with the company is entitled to assume that all internal regulations of the company have been complied with, unless he has knowledge to the contrary or there are suspicious circumstances putting him on enquiry.

iii) Hence an outsider dealing with a company through its officials , purporting to exercise an authority which that sort of official would usually have, is entitled to hold the company liable for the official's acts, even though the official is in fact exceeding his actual authority unless,

   a) he knows that the official has no actual authority;

   b) the circumstances are such as to put him on enquiry;

   c) or the public documents make it clear that the official has no actual authority, or could not have authority unless a resolution had been passed which should be filed as a public document and no such document has been filed.

iv) If, however, the official is purporting to exercise an authority which that sort of official would not usually have, the outsider will not be protected if the official exceeds his actual authority, unless the company has held him out as having authority to act in the matter and the outsider has relied thereon, that is unless the company is estopped. But a provision in the memorandum and the articles or other public documents cannot create an estoppel unless the outsider knows of the provision and has actually relied on it, and for this purpose the registration at the Registrar's office does not constitute notice.

v) An outsider who can bring himself within the protection of rule (iii) or (iv) above will not necessarily lose his protection because the ostensible official with whom he deals has never been validly appointed. On the other hand, the official must at least have been held out in some way as an authorised official of the company by one of the regularly appointed organs of the company.

vi) If a document purported to be sealed by or signed on behalf of the company is proved to be a forgery it does not bind the company. But the company may be estopped from disclaiming the document as a forgery, if it has been put forward as genuine by an official acting within his actual, usual or apparent authority, and if a transaction is binding on the company under the foregoing rules the company will be liable notwithstanding that the official has acted fraudulently or committed forgery.

The above conclusions of Professor Gower in the earlier editions of his book are true in the case of Bangladesh which has no law abolishing the doctrine of constructive notice of the documents filed at the Registrar's office and has scant case law on the subject. The *Turquand case*[1], was followed by the case of *Mahony vs East Holyford Mining Co*[2]. where it was held that bankers who have funds of a company in their hands, may, acting bona fide, lawfully honour the cheques of the directors of the company signed according to a form sent by them to the bank, without being bound, previously, to enquire whether the persons pretending to sign as directors have been duly appointed to office, in conformity with the provisions of the memorandum and articles of association.

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1 ibid,

2 (1875) L.R. 7 H.L. 869.

Directors are, however, clearly insiders and cannot claim to be protected by this rule, at any rate if they themselves acted for the company in the transaction concerned[1]. As the object of the rule is to protect innocent outsider, he cannot claim that the director who entered into the transaction with him was clothed with apparent authority if he was put on enquiry. Indeed herein less the rationale of this rule. The company is not estopped from denying the actual authority of the directors in case of negligence by the other party to safeguard his own interest.[2]

If the person acting for the company is its chief executive or managing director, then, unless there are suspicious circumstances, or the transaction is of such magnitude as to imply the need for board approval, he may safely be assumed to be authorised. Even if he does not have the actual authority but has ostensible authority then his acts will bind the company.[3] In this case the Court of Appeal in a mammoth judgment of more than one hundred pages reviewed the entire case law of the last one hundred years and came to the conclusion that if the person dealing on behalf of the company has apparent or ostensible authority and the company has allowed him to act as such then the company is bound by the transactions entered into by him on behalf of the company. The cases which went against the Turquand Rule were discussed and distinguished. Willmer L.J. pointed out :[4]

> ...Houghton's Case, Schenker's case and Rama case are cases of unusual ransactions in none of which were the plaintiffs in a position to allege that the person with whom they contracted was acting within the scope of such authority as one in his position would be expected to possess. Those decisions are no more than illustrations of the well-established principle that a party, who seeks to set up an estoppel, must show that he in fact relied on the representation that he alleges....

Diplock L.J. pointed out[5] that where the principal is a fictitious person , two factors arising out of the legal characteristics of a corporation have to be borne in mind. The first is that the capacity of a corporation is limited by its constitution, that is, in the case of a company incorporated under the Companies Act by its memorandum and articles of association; the second is that a corporation cannot do any act, and that includes making a representation, except through its agent:

> ...The commonest form of representation by a principal creating an 'apparent' authority of an agent is by conduct, namely, by permitting the agent to act in the management or conduct of the principal's business. Thus, if in the case of a company the board of directors who have 'actual' authority under the Memorandum and Articles of Association to manage the company's business permit the agent to act in the management or conduct of the company's business, they thereby represent to all persons dealing with such agent that he has authority to enter on behalf of the corporation into contracts of a kind which an agent authorised to acts of the kind which he is in fact permitted to do usually enters into in the ordinary course of business....[6]

In *Mercantile Bank of India vs Chartered Bank of India*[7] the board of directors caused the company to appoint agents under powers of attorney which authorised them to borrow on the security of charges on the company's property. The directors imposed limits on the extent to which these agents could borrow but these limitations did not appear in the powers of attorney. A charge to secure a borrowing in excess of the limitations was held to bind the

1 Howard vs Patent Ivory Co. [1888] 38 Ch.D. 156;Morris vs Kanssen [1946] A.C. 459.

2 A.L.Underwood Ltd. vs Bank of Liverpool [1924]1 K.B. 775.

3 Freeman & Lockyar vs Buckhurst Park Properties Ltd.[1964] 2 Q.B.480.

4 at page 494-5 of the judgment

5 at page 504-506.

6 For other cases on the Turquand Rule see British Thomson-Houston Co vs Federated European Bank Ltd [1932] 2 K.B. 176, Houghton and Co. vs Nothard, Lowe and Wills [1927] 1 K.B. 246, Kreditbank Cassel G.M.B.H. vs Schenkers [1927] 1 K.B. 826,Rama Corporation Ltd vs Proved Tin and General Investments Ltd [1952] 2 Q.B. 147,Biggerstaff vs Rowatt's Wharf Ltd [1896] 2 Ch. 93, Clay Hill Brick Co. vs Rawlings [1938] 4 All E.R. 100. S.London Greyhound Racecourses vs Wake [1931] 1 Ch.496.

7 [1937] 1 All E.R. 231

company in favour of a lender who had relied on the powers of attorney. An officer or agent cannot confer ostensible authority on himself by representing that he has actual authority.[1]

A company is not, however, estopped from denying liability under a contract if the document seeking to bind it is in fact a forgery. This is, of course, if the directors have never said or done anything to represent or lead to the belief that the document belonged to the company. Without such a representation there can be no estoppel.[2] In *Rolled Steel Produts (Holdings) Ltd vs B.S.C.*,[3] Slade L.J. stated that the directors had no actual authority to exercise any express or implied power of the company other than for the purposes of the company as set out in the memorandum. As to actual authority, as Lord Denning M.R. pointed out in *Hely-Hutchinson vs Brayhead Ltd*,[4] a board of directors may pass a resolution authorising two of their number to sign cheques. But a person with actual authority to obtain quotations of prices has no implied authority to communicate acceptance of such quotes where no decision to purchase has been made by his principal – at most such a person may have apparent authority[5] but a company is also bound by the acts of an agent acting within his apparent authority, e.g. where the secretary had apparent authority to hire cars on behalf of the company.[6]

The Turquand Rule has been followed in Australia and Mason C.J. giving the opinion of the High Court in *Northside Developments Pty. Ltd vs Registrar General*[7] dwelt on the merits of the Rule as follows:

> the precise formulation and application of the rule call for a fine balance between competing interests. On the one hand, the rule has been developed to protect and promote business convenience which would be at hazard if persons dealing with companies were under the necessity of investigating their internal proceedings in order to satisfy themselves about the actual authority of officers and the validity of instruments. On the other hand, an over-extensive application of the rule may facilitate the commission of fraud and unjustly favour those who deal with companies at the expense of innocent creditors and shareholders who are the victims of unscrupulous persons acting or purporting to act on behalf of companies....

The Court agreed with the formulation of the rule as stated in the Halsbury's Laws of England that ' persons contracting with a company and dealing in good faith may assume that acts within its constitution and powers have been properly and duly performed, and are not bound to inquire whether acts of internal management have been regular '.[8]

In *Padumji and Co. vs N.H.Moosa*[9] the managing director had given a power of attorney to another director to act as managing director. One of his acts being impugned as not binding on the company, it was held that persons dealing with a company are not bound to inquire whether a de facto director was a de jure director as that was a matter of indoor management of the company. In *Shivlal Motilal vs Tricumdas Mills*[10] the Court applied the Turquand rule and went on to say at p. 591 that 'this doctrine appears to have been followed in an earlier case , where the question was not one of mere irregularity but one of active fraud on the part of the agent of a company' and that ' the plaintiff and his legal advisers assumed , as they had a perfect right to assume that what was being done was rightly and legitimately done, and that all the requirements for the execution of the document, which was executed by the managing director and another director of the defendant-company and countersigned by the firm of its secretaries, treasurers and agents and bore the company's seal, had been duly complied with, previous to the execution of the document...'.

1 Armagas Ltd vs Mundogas S.A. [1986] A.C. 717 H.L.
2 Ruben vs Great Fingall Consolidated and others [1906] A.C. 439 and Banks L.J. in Kreditbank Cassel etc vs Schenkers [1927] 1 K.B. 826,835.
3 [1986] Ch.246.
4 [1968] 1 Q.B. 549.
5 Crabtree -Vickers Pty. Ltd vs Australia Direct Mail Advertising Co. Pty. Ltd [1976] 50 A.L.J.R. 203.
6 Panorama Developments Guilford Ltd vs Fidelis Furnishing Fabrics Ltd [1971] 2 Q.B. 711.
7 [1990] 170 CLR 146,164.
8 ibid at pp.154-5,171,207.
9 AIR 1926 Bom.28.
10 (1912) ILR 36 Bom 564.

Having agreed with the argument of Mr. M.A.Jinnah, counsel for the plaintiff, that equity takes that as done that ought to have been done, the court then had no hesitation in holding that a valid, legal and binding further charge was created in favour of the plaintiff against the mortgaged property of the defendant company.[1]

Justice Hamoodur Rahman said in P.K.Basak and Co. Ltd vs Gossen and Co. Ltd[2] :-

> ...All persons who are strangers to the company dealing with a company, are fixed with the knowledge of the contents of the Articles of Association; but they are not concerned with what has been said to be the internal management of the company, for they are entitled to assume the regularity of all the internal acts of the company. It is therefore, not correct to say that in each case persons dealing with a company must further satisfy themselves that even 'if clearly the power could have been given by the Articles of Association of the company to do that thing, that in fact such power was properly given'. There is abundant authority for the proposition that persons dealing with directors or managing director of a company are not called upon to enquire whether the directors have been validly appointed or whether there is a specific resolution authorising them to do a particular act, if it is clear from the articles of association of the company that they could have been authorised to do the said act....

In this case the managing director of a company was held to have had the authority to enter into a contract although there was no board resolution authorising him to do so.

The Lahore High Court held in *Ghulam Nabi Corporation Ltd. vs Khan Iftekhar Hossain Khan*[3] that before a stranger, who enters into any agreement with a director of a company, can enforce that agreement, he has to show that he acted bona fide, that he knew that the power which the director purports to have exercised, could be delegated to him, and that such power was normally delegated to the directors.

Thus it seems that the rule laid down in the *Royal British Bank vs Turquand*[4] has been followed in the sub-continent in that a company cannot take advantage against an innocent third party of any breach of its own internal regulations if the officer purporting to enter into the contract on behalf of the company had ostensible authority to do so. The company, in such a case, will be bound by the deeds of a director, and indeed, of an officer acting in excess of his powers to an innocent third party if that director or officer had apparent and ostensible authority to do the act and the company allowed him to act so.

11.4.1 **Duties of a Director** – The Act of 1994 does not lay down what the duties of a director are. Formerly, compulsory regulation 71 in the First Schedule Table A to the Act of 1913 provided that 'the business of the company shall be managed by the directors' but now that the draftsman of the Act of 1994 added one number to the articles in the First Schedule but did not make the necessary amendments in numbering the regulations referred to in section 17 of the Act the provisions of Regulation 72 in the First Schedule to the Act which provides that the business of the company shall be managed by the directors is no longer a compulsory provision in the articles. However, the articles of association of a company here invariably provide a similar provision in their articles of association and in that case the basic powers of management rests with the board of directors.

11.4.2 **Statutory Provisions on Duties of Directors** – The Companies Act however contains provisions aimed at checking reckless abandonment of duties by directors or their liabilities. Section 96 requires that board meetings be held every three months; section 97 obliges a director to hold qualification shares; section 99 prohibits a bankrupt to act as a director; section 102 provides that save as provided in this section, any provision, whether contained

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1 For other cases on the subject see Charles Joseph vs Hyantage Grant Co Ltd AIR 1935 Rang.76, P.C. Mitra vs Road Oils (India) Ltd. AIR 1930 Cal.782, Ram Buran Singh vs Mofussil Bank Ltd AIR 1925 All.206, P.V. Damodara Reddi vs Indian National Agencies Ltd AIR 1946 Mad 35, Dehra Dun Electric Tram Co. vs Jagmandar AIR 1932 All. 141, B.Anand Bejari Lal vs Dinshaw and Co. AIR 1942 Oudh) 417.

2 PLD(1957) Dac. 233,238.

3 PLD(1962) W.P.Lah 370.

4 Supra

in the articles of a company or any contract or otherwise, for exempting any director... from or indemnifying him against any liability which by virtue of any rule of law would otherwise attach to him in respect of any negligence, default, breach of duty or breach of trust of which he may be guilty in relation to the company shall be void, provided that a company may, in pursuance of any such provision as aforesaid, indemnify any such director against any liability incurred by him in defending any proceedings against him in which judgment has been given in his favour. Section 103 prohibits a company from making any loans to a director; section 104 prohibits a director from holding any office of profit under the company except that of a managing director, manager, or a legal or technical adviser or banker; section 105 provides that except with the consent of the directors, a director of a company, or the firm of which he is a partner or any partner of such firm or the private company of which he is a director or member, shall not enter into any contract for the sale, purchase or supply of goods and materials of the company. Section 107 imposes restrictions on the powers of a public company or the subsidiary of a public company to sell or dispose of the undertaking of the company or remit any debt due by the director except with the consent of the members in general meeting. Section 108 provides that the office of a director shall be vacated in certain circumstances most of which happen if the director acts in contravention of the statutory control mentioned earlier.

Section 109 provides restrictions on the appointment of managing directors . No public company or the subsidiary of a public company shall appoint a person as a managing director if he is the managing director of more than one other company. Further, the appointment of a managing director should be sanctioned in a general meeting of the company. The government may relax the restrictions in this section . Please note that the restriction on the number of managing directorships a person may hold is not applicable in the case of a private company so that if there is a group of private companies then the same person may be the managing director of all the companies.

Section 110 provides that the appointment of a managing director shall not be for a term exceeding five years. He can not be re- appointed or his term extended for a period exceeding five years on each occasion. This will be applicable in case of all companies.

Sections 111 restricts payment of compensation for loss of office except to managing directors or directors who are managers. No payment shall be made to any other director. In any case no payment shall be made to a managing or other director where the director being in whole time employment of the company resigns his office in view of the reconstruction of the company or amalgamation of the company with any other body corporate and is appointed as any officer, including managing director or managing agent of that other company, or where the director resigns his office, or where the office of the director is vacated by virtue of any provision of the Act, or where the company is being wound up due to the negligence or default of the director or where the director has been guilty of fraud or breach of trust in relation to, or of gross negligence in, or gross mismanagement of, the conduct of the affairs of the company or any subsidiary or holding company thereof or where the director has instigated or has taken part directly or indirectly in bringing about the termination of his office. Any payment made to a director for loss of office should not exceed the payment due for the unexpired period of his service or for three years whichever is shorter.

Section 112 provides that no director of a company shall, in connection with the transfer of the whole or any part of the undertaking or property of the company, receive any payment , by way of compensation for loss of office, or as consideration for retirement from office, or in connection with such loss or retirement from such company or from the transferee of such undertaking or property or from any other person unless particulars with respect to the payment have been disclosed to the members of the company and approved by them in general meeting.

Section 113 provides that no director shall receive any payment by way of compensation for loss of office in connection with the transfer to any person of all or any of the shares in a company, being a transfer resulting from an offer made to the general body of shareholders,

or an offer made by a body corporate with a view to the company becoming a subsidiary to such body corporate, or an offer made by or on behalf of an individual with a view to obtaining the right to exercise , or control the exercise of , not less than one- third of the total voting power at any general meeting of the company. A director may have payment from the transferee but he is required to take reasonable steps to secure that particulars with respect to the payment proposed to be made by the transferees etc. be sent with the notice of the offer made for the shares. If it is not done then any payment received by him shall be in trust for any person who have sold their shares as a result of the offer made.

Section 114 makes provision so that the director concerned may not take the money indirectly in contravention of sections 111-113.

Section 115 requires every company to maintain a register of directors , managers and managing directors.

Section 130 provides that every director who is directly or indirectly concerned or interested in any contract or arrangement entered into by or on behalf of the company shall disclose the nature of his interest at the meeting of the directors at which the contract or arrangement is determined on, if his interest then exists, or in any other case at the first meeting of the directors after the acquisition of his interest etc. A general notice that a director is a director of any specified company or member of any specified firm and is regarded to be interested in any subsequent transaction with such firm or company will be regarded as a sufficient notice for the purpose of the section.

Section 131 prohibits a director from voting on any contract or arrangement in which he is directly or indirectly concerned or interested. His presence in such a meeting shall not be counted for the purpose of a quorum nor shall his vote be counted in the proceedings.

The above provisions in the Act relating to the activities of a director and restrictions thereon have been inserted so that a director does not act improperly in dealing with other people's money. In the next sub-section we shall deal with the position and duties of a director.

11.5.1 **Position of a Director** - The company itself cannot act in its own person; it can only act through its directors, merely the ordinary case of principal and agent.[1] Directors occupy a pivotal position in the structure of a joint stock company. In the early days of joint stock enterprise, when business was comparatively simple and markets well defined and easy of access, companies were actually managed by the directors. They met frequently, discussed and conducted the day to day regular business. They had, no doubt, to appoint technical and administrative officers, but the management of the undertaking remained more or less in their hands. Now, with the details of supervision and execution left to the junior staff, they are still responsible for the company's business as a whole and are hence sometimes termed its trustees. In their function as agents they stand in a fiduciary relationship to their principal, the company. To quote the famous words of Romer J. in *Re City Equitable Fire Insurance Co.*[2]:-

> ...It has sometimes been said that directors are trustees. If this means no more than that directors in the performance of their duties stand in a fiduciary relationship to the company the statement is true enough. But if the statement is meant to be an indication by way of analogy of what those duties are, it appears to me to be wholly misleading. I can see but little resemblance between the duties of a director and the duties of a trustee of a will or of a marriage settlement...

The duties of a director are somewhat akin to those of a trustee but as Professor Gower points out,[3] it is when we turn to the duties of care and skill that the trustee analogy breaks down. The duty of a trustee of a will or settlement is to be cautious and to avoid risks to the trust fund. The managers of a business fund must, perforce, take risks in an attempt to earn profits for the company and its members. They thus have fiduciary duties of loyalty and good faith and duties of care and skill.

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1 Per Cairns L.J. in Ferguson vs Wilson(1866) L.R. Ch.89; (1866) 2 Ch. App. 77.

2 [1925] Ch. 407,426.

3 Gower's Principles of Modern Company Law 5th.ed. p.550.

11.5.2 The fiduciary duties are owed to the company and not to the members.[1] This is a case where the directors purchased shares from their members without revealing that negotiations were in progress for a sale of the undertaking at a favourable price. When the seller of the shares discovered that the directors knew at the time of the contract that negotiations were on foot for the purchase by an outsider of all the shares in the company at a high figure, he found it impossible to impeach the contract. A later case shows that this rule must not be pushed too far; directors may by their conduct place themselves in a fiduciary position towards shareholders in the course of negotiating terms with the bidders.[2] To day in England this sort of action by the directors will be hit by the injunction against insider trading. The SEC in Bangladesh is supposed to protect shareholders and investors against insider trading but there is no set standard as yet in Bangladesh on the duties of a director or who they owe these to. The English principles will apply although the company law of Bangladesh does not contain the various restrictions the law in England, U.S.A. or Australia imposes upon the directors.

The English courts have described directors as 'persons invested with strictly defined powers of management under the Articles of Association of a statutory corporation...'.[3] A director may obtain an injunction against his fellow directors if he has a proprietary interest in the company, such as holding shares in it, or a right to be paid remunerations for his services.[4] However, the House of Lords has held that such an interest need not be shown in an action for re-instatement.[5]

The Supreme Court of Pakistan has held in *Maqbool Elahi vs Khan A. Rahman*[6] that the admission of a duly qualified director to the board of directors of a public company is within the scope of a writ of mandamus. With all respect, this is not a correct decision as the writ of mandamus will not issue unless the respondents are persons performing functions in connections with the affairs of a local body or the government or a statutory authority. The other observations of the Court however on the right of a director to sit on the board are indicative of how important the Court thought the position of a director of a public company was; the judges justified the issuance of the writ by holding that a duly qualified director has a legal right to sit on the board of directors and that this is a right which is of the greatest importance to the public interest in the field of the operation of public joint stock companies under company law. In this case Mr. H.S.Suhrawardy argued unsuccessfully that according to the principle established in *Pakistan vs Mirajuddin*[7] a writ would not lie. Justice Cornelius, delivering the decision of the Court relied on an old English case *Government Stock Investment Co. Ltd vs the Queen*[8] where mandamus was issued to admit to the directorship of a registered company the candidate elected by a show of hands. In England the High Court has got both the power to issue a prerogative writ and also hand out a decision regarding company directors.

The Lahore High Court had declared in *Gulab Singh vs Punjab Zamindar Bank*[9] that a director or a managing director is in no way a servant of the company for carrying on its business. Following the agency principle, it has been held in India that a personal liability to pay taxes due by a company cannot be imposed upon a director or even the managing director of the company. It is the corporate body itself and its assets which alone are so liable.[10] A director of the company is a trustee of the company and a trustee for the creditors

1 Percival vs Wright [1902] 2 Ch. 421.
2 Allen vs Hyatt AIR 1914 P.C. 246.
3 Bowen L.J. in Imperial Hydropathic Hotel Co. vs Hampson [1882] 23 Ch.d. 1,13.
4 Hayes vs Bristol Plant Hire Ltd. [1957] 1 All E.R. 685.
5 Bonsor vs Musician's Union [1956] A.C. 104.
6 PLD(1960) S.C. 266
7 PLD(1959) S.C. 147.
8 (1878) 3 Q.B. 442.
9 AIR 1942 Lah 77.
10 Re Venkata Krishna Sharma [1954] 2 M.L.J. 184.

of the company to the extent that he is bound to apply all the assets of the company for benefit of all the creditors of the company so far as they will extend.[1] However, the provisions of the Limitation Act 1908 dealing with express trustees do not apply to directors.[2]

The true position seems to be, as pointed out in Palmer's Company Law[3] that directors occupy a fiduciary position and all the powers entrusted to them are exercisable in their fiduciary capacity. One result is that, like all agents, they cannot contract in their personal capacity with themselves in their capacity as directors of the company. The fiduciary relationship does not extend to directors in their capacity as shareholders of the company. As such, a director may vote in a general meeting upon any matter in which he is personally interested,[4] and his vote cannot be challenged, unless it is being exercised in a manner oppressive to a minority of the shareholders.[5]

11.6.1 **Contracts with the Company** – The standard by which a director's duties in this country is evaluated, is the same as in England and other commonwealth countries. Directors are fiduciaries and must, therefore display the utmost good faith towards the company in their dealings with it or on its behalf. They must act bona fide, in what they believe to be the best interests of the company.[6] They must exercise their powers for the particular purpose for which they were conferred and not for some extraneous purpose, even though they honestly believe that to be in the best interest of the company. But the most important feature of the fiduciary nature of their duties is that they must not fetter their discretion to exercise their powers from time to time in accordance with the foregoing rules. Also they must not, without the consent of the company, place themselves in a position in which there is a conflict between their duties and personal interests. Good faith must not only be done but must manifestly be seen to be done, and the law will not allow a person acting in a fiduciary capacity to place himself in a situation in which his judgment is likely to be biased.

Professor Gower, however, comments that 'notwithstanding that it is for the directors and not the court to consider what is in the interests of the company, they may breach that duty notwithstanding that they have not acted with conscious dishonesty but have failed to direct their minds to the question whether a transaction was in fact in the interests of the company'.[7] Professor Gower cites by way of illustration the case of *Re W. & M. Roith Ltd.*[8] The controlling shareholder and director entered into a service agreement with the company whereby on his death his widow would get pension for life. Since no thought had been given to the question whether the arrangement was for the benefit of the company and that, indeed, the sole object was to make provision for the widow, the court held that the transaction was not binding on the company. But one should consider the case of *Charterbridge Corpn. vs Lloyds Bank*[9] where the directors of a company forming part of a group had considered the benefit of the group as a whole without giving separate consideration to that of the company alone. It was held that 'the proper test...in the absence of actual separate consideration must be whether an intelligent and honest man in the position of a director of the company concerned could...have reasonably believed that the transactions were for the benefit of the company...'[10] Professor Gower notes further that despite the separate personality of the company it is clear that directors are not expected to act on the basis of what is for the economic advantage of the corporate entity, disregarding the interests of the members. For

1 Mohamed Ishmail vs Sachidananda [1936] 40 CWN 769.
2 Kathiawad Trading Co. vs Veerchand Deepchand (1894) ILR 18 Bom.119.
3 20th. Ed.p.518.
4 North -West Transportation Co. vs Beattie. (1887) 12 App. Cas 589
5 Cook vs Deeks [1916] 1 A.C. 554; Menier vs Hooper Telegraphic Works (1874) 9 Ch.App.350.
6 per Lord Greene M.R. in Re Smith & Fawcett Ltd (1942) Ch. 304,306.
7 Principles of Modern Company Law 5th ed. 553.
8 [1967] 1 W.L.R. 432.
9 [1970] Ch. 62.
10 at p.74.

example, they can recommend the payment of dividends at the expense of the company if these are out of profits of the company. If, as will normally be the case, the directors themselves are shareholders, they are entitled to have some regard to their own interests as shareholders and not to think only of the others.[1] In *Mills vs Mills*,[2] Latham C.J. of the Australian High Court commenting on the duties of directors said that they were ' not required by the law to live in an unreal region of detached altruism and to act in a vague mood of ideal abstraction from obvious facts which must be present to the mind of any honest and intelligent man when he exercises his powers as a director'.

In England, section 309 of the Act of 1980 required directors to have regard to the interests of the company's employees in general, as well as the interests of its members. However, Lord Diplock commented in *Lonrho Ltd vs Shell Petroleum*[3] that 'it is the duty of the board to consider ...the best interests of the company. These are not exclusively those of its shareholders but may include those of its creditors'.[4]

In Bangladesh the company law is silent on the duties of the directors towards employees and the law reformers would do well to insert a provision requiring directors to look after the interests of the workers as well.

11.6.2 The trustee-like position of directors vitiates any contract which the board enters into on behalf of the company with one of their number. The Act of 1994, following the previous law of 1913 imposes particular restrictions on contracts between the company and the directors. Section 105 requires a director to have the consent of other directors before entering into a contract for the sale , purchase, or supply of any goods and materials with the company. Section 130 obliges a director to disclose his interest in a contract or arrangement entered into on behalf of the company at the meeting of the board in which such contract or arrangement is determined. Section 131 prohibits voting by such interested director in such meeting. In the absence of a specific provision, a director does not lose his position if he is interested in contracts with the company.[5] In this case the director of one company, who was managing director of another company and remunerated only by salary was held not to be disqualified on the ground that he was interested in contracts with that other company. A breach of the statutory provisions however automatically brings the basic equitable principle into operation and the contract is voidable by the company and the profits made by the interested director are recoverable.[6] This case concerned breach of provisions for disclosure contained in the Articles and the consequence of a failure to observe a statutory provision can hardly be less extensive.

Section 108(e) and Regulation 78 of the First Schedule to the Act of 1994 provide that the office of a director shall be vacated if among other things, the director accepts or holds any office of profit under the company other than that of a managing director or manager or legal or technical adviser or a banker without the sanction of the company in general meeting.

There is no corresponding section in the English Act to section 105 of our Act. The basic rule of English law that in the absence of an express provision in the company's Articles, the only effective step is to make full disclosure to the members of the company and to have the contract entered into or ratified by the company in general meeting is therefore not applicable in Bangladesh in case of such contracts because it is sufficient for the director to have such contract ratified by the board. The Privy Council has set out the law regarding conflict between duty and interest of a director in the Commonwealth when Lord Radcliffe commented in an appeal from Canada :

1 Gower,ibid.
2 [1938] 60 CLR 150,164.
3 [1980] 1 WLR 627,634.
4 See also for similar comments : Walker vs Wimborne [1976] 50 A.L.J.R. 446(Aust.H.C.).
5 Wilson vs L.N.W. Railway [1940] Ch. 169.
6 Imperial Mercantile Credit Association vs Coleman (1873) L.R. 6 H.L. 189.

> ...It is beyond dispute that there are certain obligations cast upon a director who places himself in the position of contracting with his company. The general principle is that such a contract is not binding on the company, for a director is not entitled to place himself in a position in which his interest is in conflict with his duty. The company, it has been said , has a right to the service of its directors as an entire board. Even if the contract is not avoided, whether because the company elects to affirm it or because circumstances have rendered it incapable of recission, the director is accountable to the company for any profit that he may have realised by the deal... If a trustee has placed himself in a position in which his interest conflicts with his duty and has not discharged himself from responsibility to account for the profits that his interest has secured for him , it is neither here nor there to speculate whether, if he had done his duty, he would not have been left with the same amount of profit. It has been said that a trustee, who is accountable, is not the less accountable if he shows that the transaction impugned is both reasonable and fair....[1]

Our Appellate Division has commented and held that directors are trustees of the fund of the company and can be proceeded against for misappropriation.[2]

If a director acts in contravention of section 105 then he vacates his office under section 108(1)(h). Before these two sections are made applicable , however, it must be clearly proved that the condition requisite for the application of the penalty are satisfied. The Supreme Court of Pakistan has held that the expression ' contract for sale' in section 105 must be consonant with the definitions in the Contract Act, 1872 and the Sale of Goods Act, 1930.[3]

Once, however, it is shown that a director has contravened the provisions of the Act regarding his duty, he cannot escape with impunity. While interpreting section 86F of the Act of 1913, which was the forerunner of section 105 of the current Act, Chagla C.J. of the Bombay High Court held that the word 'consent' in that section does not contemplate general consent but refers to particular or specific contracts.[4] The Court commented at page 286 of the judgment as follows:

> ...It is clear that, in enacting this provision , which is a novel provision and finds no place in the English Companies Act, the legislature wanted to suppress a particular mischief and had a particular object in mind. A director of a company occupies a responsible position and that the legislature wanted that , while occupying that position , he should not be placed in a situation where there would be a conflict between his interest and his duty. His duty would be to his company, of which he is director. His interest would be to enter into a profitable contract with the company, and in order to suppress that mischief and to achieve the object which the lesgislature had in mind, section 86F was enacted. It is a well settled canon of construction that , when we are considering a remedial measure, we must give to the provision of law as wide an interpretation as possible....

In the Bombay case, the director concerned had given general notice that he should be considered interested in any subsequent transactions with the companies and firms mentioned and although he never applied for any consent to any contract under section 86F of the Act of 1913, corresponding to section 105 of the current Act, yet a board meeting purported to have consent of various directors, including the relevant director, entering into contracts for sale, purchase or supply of goods and materials with the company. The notice and the consent given was valid under section 91A of the previous Act, corresponding to section 130 of the current Act, but the Court distinguished the two sections and held that the director would lose his seat although the relevant contract was for purchase of only one tin of ghee! A similar interpretation was given by the Lahore High Court in *Maqbool Elahi vs Khan Abdul Rahman Khan*.[5]

The judgment was set aside on appeal by the Supreme Court on a different point but the Court did not interfere with this particular finding. The Court held that the consent of the directors referred to in section 86F of the Act of 1913 does not mean a general consent,

1 James Joseph Gray vs N.A.P. Mines Ltd PLD (1952) P.C. 79 at p. 89,91.
2 Md. Yameen and another vs K.A. Baskar and others (1986) BLD (AD) 305.
3 Maqbool Elahi vs Khan Abdul Rahman Khan PLD(1960) S.C. 266 at 278,282.
4 Walchandnagar Industries Ltd vs Ratanchand AIR 1953 Bom 285.
5 PLD(1959) Lah 721.

because a general consent would defeat the object of the section, which was to require the directors in each individual case to examine the nature and implications of a contract and decide whether it was beneficial to the company.

Section 105 does not make it clear when and how the consent of the directors is to be obtained. In *Mohanlal vs Grain Chambers*[1] this section was held not to require the consent of directors to be either express or by means of a resolution of the board at a meeting or otherwise. Therefore, if each and every individual constituting the board, had entered since the inception of the company, into transactions with the company, and if no steps had been taken by the general body of shareholders at any time thereafter to alter their articles so as to provide otherwise, the requisite consent of the directors under the section would be deemed to have been impliedly given to such transactions of business with the company. Where every single director is a party to the consent, the exercise of the power must be done by the directors. Regulation 88 of the First Schedule Regulations provides that the directors may meet together for the despatch of business, adjourn and otherwise regulate their meetings as they think fit. Had it been intended that all work to be done by directors must be done at a meeting of the board of directors, the legislature would have used the word "shall" instead of the word "may".[2] In the same year , the Calcutta High Court, while reiterating that it was not imperative to have a formal resolution recording the consent of the other directors as required under the section, held further, that the language of the section did not indicate that such a contract entered into by a director without the consent of the other directors was void ab initio. The Court held as follows :

> ...In the first place, the language of the section does not indicate that such a contract effected by a director without the consent of other directors is illegal. The prohibition is against the director and there is a penalty for any violation of the provisions of the section. This does not mean that the contract is void.... [3]

What the section does is to prohibit a director from doing certain acts without the sanction of the board and the penalty imposed on the defaulting director is that he would lose his seat, but, unless it is shown that the director himself retained the profit indirectly, he cannot be asked to make good the loss.

Directors being trustees and acting as fiduciaries must apply the property of the company for the specified purposes of the company and a misapplication of it was a breach of the fiduciary duty.[4] Where a person has improperly profited from his fiduciary position the Court has equitable jurisdiction to award interest on the judgment for damages for misfeasance or breach of duty as a director.[5] Directors must not put themselves in a position where their duties and interests conflict.[6]

11.7.1 **Fiduciary Agents** – Directors of a company are fiduciary agents, and a power conferred upon them cannot be exercised in order to obtain some private advantage or for any purpose foreign to the power.[7] Like other agents, directors incur no personal liability on contracts made by them on behalf of the company, within the scope of their authority. If, however, directors exceed the powers given to them by the memorandum and articles they will be liable for breach of warranty or authority. Their actions may be ratified by the company in general meeting even if they have acted contrary to the company's constitution.[8] If shareholders appoint directors agents for sale of their shares and there is fraud then the shareholders are liable for fraud.[9] In *Dawson International plc vs Coats Patons plc*[10] it was

1 AIR 1959 All.276.
2 ibid at p.293.
3 Albert Judah vs Ramapada Gupta AIR 1959 Cal.715.
4 Selangor United Rubber Estates Ltd. vs. Craddock. [1968] 1 WLR 1555.
5 Wallersteiner vs Moir (No.2) [1975] Q.B. 373.
6 Piercy vs S. Mills and Co. Ltd [1920] 1 Ch. 77.
7 Per Dixon J. in Mills vs Mills [1938] 60 CLR 150,186.
8 Charlesworth and Morse: Company Law 14th Ed. p.397.
9 Briess vs Wolley [1954] A.C. 333.
10 [1988] 4 BCC 305.

held that if the directors chose to give shareholders advice about a take over bid they must act in good faith and not fraudulently but this was a fiduciary duty that was owed to the company and not current members as vendors of their shares. Directors' duties to the company override any undertakings they may have given to a third party.[1] Charlesworth and Morse cite two other decisions on the duties of directors.[2] In *Nicholson vs Permakraft Ltd.*[3] it was suggested that a director's fiduciary duty could, in certain circumstances, be owed to the company's creditors as well as the members. A payment made to the prejudice of current or continuing creditors, when a likelihood of loss to them ought to have been known, could amount to misfeasance to the company. On the other hand in Re Welfab Engineers Ltd,[4] directors were held not to be in breach of their duty to the company in selling the business of the company as a going concern for a lower price than could have been obtained for the premises alone. The directors were held not to be required to act as liquidators.

The directors are to exereise their powers for the purposes for which they were conferred and bona fide for the company as a whole.[5] Directors are not to put themselves in a position in which their duties to the company and personal interests may conflict.[6] Directors' discretionary power to refuse to register a transfer of shares is a fiduciary power. *Re Smith and Fawcett Ltd*[7] and per Lawson L.J. in *Heron International Ltd vs Lord Grade.*[8] Further, an issue of shares has traditionally been held to be invalid if the directors are motivated by self-interest, e.g., a desire to preserve their control of the company.[9]

In the *Hogg case* above the directors had issued unissued shares in the company to trustees to be held for the benefit of employees, the shares being paid for by the trustees out of an interest free loan from the company , in order to forestall a takeover bid. This issue was held to be in excess of the directors' fiduciary power.

The Canadian Courts refused to follow the reasoning in this case that issue of shares otherwise than to raise capital was a breach of duty. The test is whether the directors honestly believed that they were acting in the best interests of the company, and whether there were reasonable grounds for that belief.[10] The Privy Council considered the issue in *Howard Smith Ltd. vs Ampol Petroleum Ltd*[11] where the facts were similar to the *Hogg case* and held that once no self-interest is discovered there can be no breach of duty, and that the court must examine the substantial purpose for which the power was exercised and whether that purpose was proper or not. The court must respect the directors' opinion on questions of management but in other cases it is a question to be decided on the facts of each case. This case and the *Olson's case* was followed in Mutual Life Insurance vs The Rank Organisation.[12] In *Rolled Steel Products Ltd vs British Steel Corporation*[13] the Court of Appeal, following an earlier decision, laid down the tests as follows:

1) Is the transaction reasonably incidental to the carrying on of the company's business?
2) Is it a bonafide transaction ?
3) Is it done for the benefit and prosperity of the company ?

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1 John Crowther Group plc. vs Carpets International plc [1990] BCLC 460.
2 ibid at p. 399.
3 [1985] NZLR 242.
4 [1990] BCC 600
5 Lee vs Chou When Hsien [1985] BCLC 45(P.C.)
6 Guinness plc. vs Saunders [1990] 1 All E.R. 652 H.L.
7 1942] Ch. 304.
8 [1983] BCLC 244.
9 Piercy vs S. Mills & Co Ltd [1920] 1 Ch. 77, Hogg vs Cramphorn Ltd [1967] Ch. 254, Bamford vs Bamford [1970] Ch. 212.
10 Teck Corpn. Ltd vs Miller [1972] 33 Dominion Law Reports (3d) 288; Olson vs Phoenix Industrial Supply Ltd [1984] 9 Dominion Law Reports (4th) 451.
11 [1974] A.C. 821.
12 1985] BCLC 11.
13 [1984] BCLC 466.

The authors of Charlesworth and Morse comment that if directors exercise a power for a proper purpose and in good faith, their judgment is not open to review by the courts. However, although it would be wrong for the courts to question the correctness of the management's decision on a question of management, if bonafide arrived at, when the question is whether the directors exercised a power for one purpose or another, the courts are entitled to look at the situation objectively in order to ascertain how substantial an alleged requirement may have been.[1]

In Mills vs Mills[2] the directors believed that the bonus issue was in the best interests of the company and it was immaterial that one director derived some benefit from the passing of the board resolution. The court held that where a director was also a shareholder in the company he could promote his own interests so long as his dominant motive was to benefit the company.

Similarly, a nominee director appointed by a shareholder owes the same duties to the company as any other director.[3]

On the question of proper purpose Professor Gower summarises the law and comments[4] that apart from raising capital the directors may issue shares to a larger company in order to secure the financial stability of the company,[5] or as part of an agreement relating to the exploitation of mineral rights owned by the company.[6] If so, the mere fact that the incidental and desired result was to deprive a shareholder of his voting majority or to defeat a take-over bid would not be sufficient to make the purpose improper. The author cited the relevant portion of the judgment in the *Howard case*[7] at page 832 as follows :

> ...A dispute arises whether directors ...made a particular decision for one purpose or for another, or whether, there being more than one purpose, one or another purpose was the substantial or primary purpose, the court...is entitled to look at the situation objectively....

The courts therefore have the power to examine whether in fact the power to issue shares was exercised properly or not.

11.7.2 It is more than one hundred fifty years that the British judges pronounced that the trustee-like position of directors was liable to vitiate any contract which the board entered into on behalf of the company with one of their number. A corporate body can only act by agents, and it is, of course, the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such agents have duties to discharge of a fiduciary nature and no one having such duties to discharge, shall be allowed to enter into engagements in which he has or can have, a personal interest conflicting, or which may possibly conflict, with the interests of those whom he is bound to protect.[8]

It is this principle that has been reflected in the enactments in the sub-continent. Sections 105, 130 and 131 of the Act of 1994 carry on the restrictions on the powers of directors while entering into contracts or arrangements which concern the company. A director , thus , must disclose the nature of his interest in a contract or arrangement with the company and cannot vote when that agenda is taken up. Sections 130 and 131 are but successors of sections 91A and 91B of the Act of 1913 and have their parallel provisions in the English Acts of 1929(section 149), Act of 1948(section 199) and the Act of 1985 (section 317).

The possible effects of a statutory provision like these on the general equitable principle were considered in *Hely-Hutchinson vs Brayhead Ltd* [9] and *Guinness vs Saunders*.[10] The

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1 Company Law 14th Ed at page 402.

2 (1938) 60 C.L.R. 150

3 per Lord Denning in Meyer vs Scottish C.W.S. Ltd [1958] S.C.,40,67,68; and per Ungoed-Thomas J. in Selangor United Rubber Estates Ltd vs Cradock [1968] 1 WLR 1555,1613-4.

4 5th. Ed.p.557

5 Harlowe's Nominees Pty Ltd vs Woodside Oil Co (1968) 121 CLR 483, H.C.

6 Teck Corpn. Ltd vs Miller (1972) 33 D.L.R.(3d) 288.

7 Howard Smith vs. Ampol Petrolium Ltd., Supra

8 Professor Gower : Principles of Modern Company Law 5th Ed. p.559-560 citing from observations of Lord Cranworth L.C. in Aberdeen Railway vs Blaikie(1854) 1 Macq. H.L. 461 (H.L. Sc.).

9 [1968] 1 Q.B. 549, C.A.

10 [1990] 2 A.C. 663 H.L.

highest courts of England held that if a director failed to declare his interest the transaction was voidable at the instance of the company and any benefits received by the director are recoverable by the company if it acted while it was still possible to restore both parties to their former positions. In the Guinness case, the company did not succeed in its argument that payments made to the director should be returned because restituitio in integram was no longer possible but succeeded in the result because the contract to pay the director his fees for a successful takeover was approved not by the board but by a committee. It was implicit in the judgments that if a director had declared his interest then he would be able to retain the benefits. The judges in both these cases thought that if a director did not declare his interest then the contract would be voidable at the option of the company. They were only echoing the legal position established in the case of *Imperial Mercantile Credit Association vs Coleman.*[1]

The Calcutta High Court has held in *Rabindra Nath Mitra vs the Emperor*[2] that the contracts contemplated by section 91A of the Act of 1913(predecessor of section 130) in respect of which every director must disclose his interest on pain of the penalty provided for in sub-section (2), include not only contracts entered into at a meeting of directors but also all contracts entered into by or on behalf of the company whether entered into at such meeting or otherwise. These sections were also discussed in the case of *P.Venkata Chalapathi vs Gunther Mills.*[3] The court held that as regards the matter of non-disclosure with which section 91A dealt, a consideration of section 91B (prohibition against voting by interested director) indicated that the mere fact that the section imposed a penalty was no ground for inferring that it prohibited such a contract so as to render it void ab initio. But non-disclosure or voting, where, but for the vote, the contract would not have been sanctioned, would in all cases, render the interested director liable to account for secret profits. In *Pratts (Bom) Ltd vs M.T.Ltd*[4] Sir George Rankin, delivering the judgment of the Judicial committee pointed out [5] that section 91B of the Act of 1913[6] was a concise statement of the general rule of equity. Hence, where a director of a company has an interest as a shareholder in another company or is in a fiduciary position and owes a duty to another company, which is proposing to enter into engagements with the company of which he is a director, he is within the rule.

In V.R.Iyer vs The *Madras Times Printing Co. Ltd*[7] decided only a few months after the insertion of these sections in our law it was held that the directors of a company were agents of the company and trustees for the shareholders of the powers committed to them.

The cases of *K.C.Pandalai vs South Indian General Assurance Co. Ltd*[8] and In *re Sir Hormusji A Wadia*[9] on the interpretation of section 91B of the Act of 1913 may also be referred to.

This, however, does not mean that the directors cannot pass resolutions authorising some of them to operate bank accounts of the company, for this is a mere delegation of the power of the board to certain of their members in the normal course of management of the company. There is no element of personal interest and section 91B of the Act of 1913 is not contravened by the passing of such resolutions.[10]

From the language of section 131 it appears, however, that the word "arrangement" does not cover a general scheme of the type under which, at the time the scheme is approved by the board of directors, no right or liability accrue or are incurred by the members of the company, the directors or the company itself. The word "arrangement" contemplates

1 [1873] L.R. 6 H.L. 189 supra.
2 [1938] 42 C.W.N. 533.
3 AIR 1929 Mad. 353 and AIR 1932 P.C. 244.
4 AIR 1938 P.C.159
5 at page 162 ibid.
6 section 131 of the Act of 1994.
7 I.L.R.(1915) Mad 991.
8 AIR 1942 Mad 95.
9 AIR 1921 Bom. 372.
10 Public Prosecutor vs T.P. Khaitan (1957) Comp.Cas. 77.

transactions in which a director at once becomes interested, in that he either acquires some rights or incurs some liabilities as a result of it. Thus, where a scheme passed by the directors of a certain company only enabled members subsequently to have their dealings in future registered with the company, it was not until such registration took place that any member became interested in the scheme approved by that resolution and it was not a scheme under which any one, in his individual capacity, or any director in his capacity as such, acquired any particular interest, the scheme was not hit by the provisions of section 91B of the Act of 1913.[1] Section 131 does not apply to a private company by virtue of sub-section (3).Where, therefore the articles of a private company did not contain a clause against including an interested director for the purpose of forming the quorum , the meeting , in which the necessary quorum was completed by including the interested director, was valid and the consent given by the votes of the other directors was a valid consent.[2]

The concern or interest of the director which has to be disclosed at the board meeting must be in relation to the contract or arrangement entered into or to be entered into by or on behalf of the company. The interest or concern cannot be a merely sentimental interest or ideological concern. A relationship of friendliness with directors who are 'interested' in contract or arrangement will not make a person an interested director.[3]

In N.S.Somani vs Saangli Bank Ltd.[4] it was held that under the 1913 Act a contract sanctioned at a meeting which was irregular because an interested director voted thereat and without his vote being counted there would be no quorum, was voidable by the company; if the company chose to affirm the contract, it was a valid contract. This also seems to be the position in English law discussed above.

11.7.3 **Use of Corporate Property, Opportunity or Information** – A corollary of the principle that directors must avoid conflict of interest and duty is that they should not, without the consent of the company, use for their own profit the company's assets, opportunities or information. In *Regal (Hastings) Ltd vs Gulliver*,[5] the House of Lords, in an obviously unmeritorius case, allowed a claim by the purchasers of shares of a company against the previous directors for a profit they made on the sale of shares although the directors could have had the deal ratified in the general meeting and the purchasers of the shares had made a windfall themselves. The House held that the directors were liable to account once it was established that what the directors did was so related to the affairs of the company that it could properly be said to have been done in the course of their management and in utilisation of their opportunities and special knowledge as directors and this resulted in a profit to themselves.

This case was followed in *Industrial Consultants vs Cooley*,[6] *Canadian Aero Service vs O'Malley*[7] and *Boardman vs Phipps*.[8] In the *Cooley* and the *Canadian case* the directors joined the undertaker of a project after resigning from directorship and yet were held to be liable to account for the profits which they made.

In the Cooley case liability was based on the misuse of information which the director concealed from the company. In the Canadian case the decision was based on misuse of a corporate opportunity. Laskin J. said at page 382 of the judgment above :

> ... In my opinion this ethic disqualifies a director or senior officer from usurping for himself or diverting to another person or company with whom or with which he is associated a maturing business opportunity which his company is actively pursuing; he is also precluded from so acting even after his resignation may fairly be said to be prompted or influenced by a wish to

1 Mohan Lal vs Grain Chambors Ltd. AIR 1959 All. 276.
2 Mahesh Co. vs Oil Mills Ltd. AIR 1955 NUC 3576 All.
3 Needle Industries (India) Ltd vs Needle Industries Newey(India) Holding Ltd. [1981] 51 Comp. Cas. 743(S.C.).
4 [1965] 35 Comp. Cas 596(SC)
5 [1942] 1 All E.R. 378
6 [1972] 1 WLR 443.
7 [1973] 40 Dominion Law Reports (3d) 371(Can.S.C.)
8 [1967] 2 A.C.46 (H.L.)

acquire for himself the opportunity sought by the company, or where it was his position with the company rather than a fresh initiative which led him to the opportunity which he later acquired.

In the *Phipps* case the defendants were not directors but a trustee and solicitor to the Trust who had acted as agents of the trustees in relation to a company in which the trust had a substantial but minority shareholding. The Court, while holding that the defendants had to account for the profit of the company however, allowed them some remuneration for their skill but for which the profits would not have been made.

In *Queensland Mines Ltd vs Hudson*[1] the Privy Council held that where the board of the company knew the facts, decided to renounce the company's interest ...in the venture and assented to Mr. Hudson's (the managing director) doing what he could with it at his own risk and for his own benefit, the managing director was not liable to account for the profits made in the venture.

Professor Gower summarises the law and submits that if the board has taken a bona fide decision that the company should reject the opportunity on its merits, it may then permit one or more of its members to take it up.[2]

It follows that a director should avoid a conflict of interest as a director and interest in a business competing with the company. In Thomas Marshall(Exporters) Ltd vs Guinle[3] a managing director had specifically agreed in his service contract not to engage in any other business without the company's consent or disclose confidential information . When he did both after resigning without notice, Megarry V.C restrained him by injunction from dealing with the company's customers and from disclosing any confidential information or trade secrets.

11.8.1 **Loans to Directors** – Section 103 prohibits loans or guarantee or securities in favour of directors. This section follows section 86D of the Act of 1913 which was introduced in the company law of our country by the amending Act of 1936. A further amendment in 1938 extended the operation of the rule to loans to private companies in which any director of the lending company was a member. Section 108 (1) (g) provides that the office of a director shall be vacated if a director or any firm of which he is a partner or any private company of which he is a director accepts a loan or guarantee from the company in contravention of section 103.

A private company may give or guarantee a loan if the loan is sanctioned by the board and the general meeting and does not exceed fifty percent of the paid up value of the shares held by the director in his own name. A contravention of section 103 may, in addition to the vacation of the office of the director, entail a fine of five thousand taka or a simple imprisonment for six months in lieu of fine for every person who is a party to such a contravention. Regulation 78 in the First Schedule to the Act also provides that the office of a director shall be vacated if the director accepts a loan from the company.

Where a loan is made to a director in contravention of the section , the irregularity should at once be set right by the other directors as soon as the fact is brought to their notice. If they fail to do so, though so required and a complaint is made to the Registrar, it has been held that he ought to take it upon himself to set the matter right.[4] Yet a director of a banking company is liable to make good any loss to the bank, if he supports an application for a loan to one of his nominees with knowledge that the statements regarding the financial assets of the borrower are untrue. The director's joint family estate was held to be jointly liable for the loan to the Munim of the director.[5] The cause of action in this case arose before the insertion of section 86D in the Act of 1913(corresponding to section 103 of the current Act) and the director was held liable mainly on the ground of breach of his fiduciary duties. In In re

1 [1978] 52 ALJR 379(P.C.)
2 Principles of Modern Company law 5th Ed. 570 .
3 [1978] 3 WLR 116
4 Subbier vs Laxman Aiyer AIR 1942 Mad.452.
5 People's Bank vs Hargopal AIR 1936 Lah 268.

Indo-Burma Industries Ltd[1] the liquidators of a public company took out a misfeasance summons under section 235 of the Companies Act of 1913. This section gave power to the Court to assess damages against delinquent directors on a winding up of the company. The summons was against the directors and managers of the company for an order compelling them to pay or restore the sums of money which had been advanced to certain firms of which the directors were partners or proprietors. The Calcutta High Court held that the giving of the loans was illegal, as it was prohibited by the Companies Act, was a misfeasance within the meaning of section 235 and that on the facts the directors could not be said to have honestly and reasonably believed that loans like these were justified. The manager was also held responsible for the misapplication of the monies as it was he who advised the directors to give the loans.

Loans to a director are unlawful but not void under the section, so that there is no difficulty in its recovery by the company.[2] This section punishes a director for accepting a loan from the company, and it was made clear in an Indian case that it is only the director who has given the loan who can be punished under the section; the other directors are not liable.[3]

No statutory conditions apply to loans by directors and others to a company, but a director lending money to a company will be in a fiduciary position and will not be allowed to make any unfair bargain.[4] Bangladesh Bank has now required directors of banks to comply with certain requirements which are similar to the provisions of section 103 before taking any loan from the bank.

11.8.2 **Register of Directors** – The fundamental principle underlying the company law of any country is ample disclosure. Section 115 obliges every company to maintain a register of directors, managers and managing agents. The register is open to inspection by every member for at least two hours a day during business hours. Returns have to be filed within fourteen days of any change in the particulars of the persons covered by the section. This section is primarily intended to reveal to the public the persons in control of the company and is a valuable shield against fraud.

But this does not mean that an outsider is deemed to have notice of all that is contained in the register, for notwithstanding the provisions of this section , the appointment of a director still remains part of the 'indoor management' of the company and it would not facilitate the conduct of business, if outsiders were compelled to search the register and find out for themselves whether a person who was permitted to act as a director of the company was a director *de jure*.[5] In *Public Prosecutor vs Coimbatore National Bank*[6] it was held that the word 'who' in sub-section (4) refers only to an officer of the company and not to the company itself, so that in a case against the company for not complying with the provisions of this section, it is unnecessary for the prosecution to prove that anybody connected with the company had knowledge of any change in the particulars to be contained in the register. In this particular case, the Bank had failed to notify to the Registrar under section 87(2) of the Act of 1913 that a particular director had ceased to hold office. It was argued on behalf of the company that the company was only obliged to make an alteration in the register and unless the register was so changed the company was not guilty of any default. Rejecting this contention, Hormel J. held that where a statutory duty is cast upon a company to do something, it must take steps to see that it is aware of all the changes that it has to notify to the Registrar and if it fails to do so, it is liable for the default.

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1 [1957] Comp. Cas. 390
2 Victor Battery Company Ltd. vs Curry's Ltd [1946] Ch 242.
3 State of Madhya Bharat vs Hiralalji AIR 1953 M.P. 26.
4 Re Cleadon Trust Ltd. [1938] 1 Ch. 660 and [1939] 1 Ch.286.
5 D.Padumjee and Co vs N.H.Moosa AIR 1926 Bom 28.
6 AIR 1943 Mad 214.

11.8.3 **Office of Profit** – Section 104 of the Act prohibits a director from holding any office of profit without the consent of the company in general meeting except that of the managing director, manager, or a legal or technical adviser or a banker. Section 108(e) provides that the office of a director shall be vacated if he or any firm of which he is a partner or any private company of which he is a director without the sanction of the company in general meeting accepts or holds any office of profit under the company other than that of a managing director or manager or legal or technical adviser or banker. Regulation 78 in the First Schedule to the Act also provides for the office of a director to be vacated in similar circumstances.

This section would require a chairman of the board of directors to get the required sanction for extra payments made to him at the general meeting if he is also a member of the board. Regulation 54 of the First Schedule Regulations requires a chairman to be appointed from amongst the directors and so where the First Schedule Regulations apply, the Chairman must have any regular extra payments made to him sanctioned at the general meeting. In India the law has empowered the Government to fix the amount of emoluments which would constitute the payment for an office of profit. Also, a relative of a director cannot be appointed to an office of profit without the sanction of a special resolution of the company in India. This however seems a bit too tough on the relative of the director who is penalised because of his relationship to the director. However, the law should make it clear what payments to a director would constitute an office of profit and what constitutes an office of profit.

11.9.1 **Liability of a Director – Contractual Liability** – Once it is accepted that directors act as agents of the company, it follows that they are not personally liable to third parties in transactions they enter into on behalf of the company.[1] In *Dira Dockyard and Engineers Ltd vs BSRS*[2] the Appellate Division held that the directors being agents of the company the general principle of law of principal and agent regulate the relationship of the company and its directors and a director was not liable if he received the loan money on behalf of the company. The directors in that case did not execute any personal guarantee. There was no pleading in that case that the loanee company was a sham and that the directors actually used to benefit themselves by obtaining the loan amount in the name of the company. Section 230 of the Contract Act provides that in the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal, and he is not personally bound by them. Such a contract will, however, be deemed to exist where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad, where the agent does not disclose the name of the principal and where the principal, though disclosed, cannot be sued. If, having authority, the directors make a contract professedly for the company, then only the company is liable on it ; if they have no authority to make the contract, they are still not personally liable on the contract, although they may be liable in damages for breach of an implied warranty of authority. The general rule was thus stated more than a hundred years back by Lord Cairns in Ferguson vs Wilson[3]:

> Wherever an agent is liable, these directors would be liable; where the liability would attach to the principal and the principal only, the liability is the liability of the company....

The directors who have duly acted on behalf of the company are not personally liable to the contracting party, even if the company's failure to carry out the contract is due to the fault of the directors, or if the company could not, at the time the contract was made, fulfill it.

The directors of a company may, of course, contract so as to make themselves personally liable to third parties. This liability may be expressed as when persons asked to supply goods on credit to a small private company are reluctant to do so unless the directors accept personal liability for payment or when, having regard to the terms of the contract and the

1 Palmer's Company Law 20 th Ed.p.559.
2 1995 (III)BLT (AD) 207
3 (1866) L.R. 2 Ch. App.77,89

surrounding circumstances, they must be deemed to have made them personally liable. One familiar instance is that of the directors giving a personal guarantee or mortgaging their personal property to the bank when the bank loans money to the company for a project. The test of the liability is : does it appear from the terms of the contract that the directors are contracting on behalf of the company? If it does, they are protected.

11.9.2 **Liability in Tort** – A director's liability to persons other than the company may also arise in tort. This may happen also under the Companies Act itself, which supplements the general law of tort in this regard. The statutory liability of a director to a third party may arise for example:

a) on an untrue or misleading statement in a prospectus to any subscriber for shares or debentures who has suffered loss or damage; Section 145.

b) on an irregular allotment, to an allottee if loss or damage is sustained; Section 149.

c) in the case of failure to repay money paid with an application for shares, if the minimum subscription has not been subscribed; Section 148(7).

The basis of a director's liability for a defective prospectus is a misleading or untrue statement therein. This will be discussed in details in the next chapter relating to Prospectus.

11.9.3 **Liability to the Company and Penalty** – A director stands in a fiduciary position to the company. It is settled law that apart from fraud, a director is liable for negligence, misfeasance and breach of trust. The Companies Act itself imposes obligations on a director and provides penalties to ensure their observance. A director can, however, escape from liability under section 396 of the current Act equivalent to section 281 of the Act of 1913, if he has acted honestly and reasonably. If he has not, then the company can sue him for loss caused by his tortious act. If the director's misfeasance or breach of trust is discovered after the winding up of the company, then the liquidator or any creditor or any contributory can initiate proceedings under section 331 of the Act corresponding to section 235 of the Act of 1913, for the recovery of the loss to the company from the director. Similarly, section 268 of the current Act corresponding to section 185 of the Act of 1913 empowers the Court after an order for winding up of the company has been passed, to require any contributory or any trustee, receiver, banker, agent or officer of the company to pay, deliver, surrender or transfer any property in his hands to which the company is prima facie entitled. In short, the position is that a director is liable for any loss suffered by the company due to his misdeeds unless he has acted honestly and reasonably. This, no doubt, follows from his peculiar fiduciary position vis-a vis the company.

Directors' duties have already been dealt with in the preceding paragraphs above. Following is a discussion on the degree of negligence which renders a director liable for the loss caused to the company, the application of section 331 of the Act, which makes a director liable for misfeasance or breach of trust and section 396 of the Act which provides a statutory defence for a director who has acted honestly and reasonably and ought fairly to be excused.

11.9.4 **Discretion** – Where a discretion is left to the directors to or not to do a particular act, honest, though imprudent, exercise of such discretion, will not make the directors responsible for negligence. Thus, where a company was formed for the purpose of purchasing a business and the directors were expressly given the power to purchase the same, the directors could not be made liable, although the business ultimately turned out to be ruinous and the facts established imprudence in the exercise of the powers conferred on the directors, but, as they had acted honestly, they could not be held liable as the imprudence was not so great and manifest as to amount to "*crasse negligentia*".[1]

Directors were held liable for dividends paid erroneously out of capital when although they were bound under the Articles of Association of the company to distinguish between

1 Overend and Gurney Co. vs Gibb [1872] 5 H.L. 480.

realised and estimated profits, they failed to do so.[1] So, too, where a dividend (or bonus) was paid by directors on the shares of the company, after it had traded for only eight months, when there had been no proper investigation of the company's trading position and no profit and loss account had been prepared; such payment was held to be improper and the directors were liable to refund the money so paid.[2] Negligence itself is sufficient to make the directors liable and fraud need not be shown. If, however, directors have made a proper investigation of the company's affairs and have bona fide concluded that profits are available for distribution, they are not liable, if it turns out that they made an error of judgment.[3]

Non-attendance at board meetings is not necessarily negligence. The amount of attention to be given to the affairs of the company will depend largely upon the extent to which devolution of duties has been organised, and upon the number of directors. In general, however, directors are bound, as Jessel M.R. observed in *Re Forest of Dean Co.*[4] :

> ...to use all reasonable diligence, having regard to their position, though probably an ordinary director, who only attends at the board occasionally cannot be expected to devote as much time and attention to the business as the sole managing partner of an ordinary partnership; but they are bound to use fair and reasonable diligence in the management of their company's affairs, and to act honestly.

Continuous non-attendance at board meetings may render a director guilty of the breaches of trust which are committed by others, but it is not necessary for a director to attend every board meeting, unless the Articles so provide. The position had been summarised in Palmer's Company Law,[5] as follows –

> ...while the failure to attend board meetings with reasonable regularity is a breach of a director's duty, it depends on the surrounding circumstances and, like the 'reasonable time' in the sale of goods, is a question of fact what is to be understood by 'reasonable regularity.

As to how far directors are justified in relying on the accuracy and honesty of persons to whom the management of the company's affairs is delegated, it is settled beyond doubt that directors, who have properly left the appointment of the staff to the chairman and the advisory director, having no reason to suspect their integrity, cannot be held liable for their misdeeds.[6]

11.9.5 **Exoneration of Directors** – A director may, however, be exonerated if he has acted honestly and reasonably. Section 396 of the Act gives power to the Court to give relief to a person in any proceeding for negligence, default, breach of duty or breach of trust if it appears to the Court hearing the case that the person is or may be liable in respect of the negligence, default, breach of duty or breach of trust, but that he has acted honestly and reasonably and having regard to all the circumstances of the case, he ought fairly to be excused for the negligence, default, breach of duty or breach of trust. That section gives power to a person who apprehends that any claim will or might be made against him in respect of any negligence, default, breach of duty or breach of trust to apply to the Court for relief and the Court may grant him relief as if a case has been pending in front of it . The persons to whom this section applies are directors of a company, managers and managing agents of a company, officers of a company and auditors of the company.

Section 331 of the Act is in direct contrast to section 396; it does not create any rights for a director, but provides a procedure and the standard by which the Court is able to assess damages against delinquent directors. This section provides that where, in the course of winding up of a company, it appears that any person who has taken part in the formation or

1 Re Oxford Benefit Building Ltd [1886] 35 Ch.D. 502.
2 Rance's Case (1870) L.R. 66 Ch. App. 104.
3 Stringer's Case (1869) L.R. 4 Ch.App.475.
4 (1878) 10 Ch.D. 450,452 :
5 20th Ed. p.568.
6 Re City Equitable Fire Insurance Co. (1925) Ch.407; Dovey vs Cory (1901) A.C. 477, Re Kingston Cotton Mills Co. (1896) 1 Ch. 331.

promotion of the company, or any past or present director, manager or liquidator, or any officer of the company has misapplied or retained or become liable or accountable for any money or property of the company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may, on the application of the liquidator, or of any creditor or contributory made within three years from the appointment of the liquidator or of the misfeasance etc, whichever is longer, examine into the conduct of the promoter, director, manager, liquidator or officer and compel him to repay or restore the money or property with interest or to contribute such sum to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust as the Court thinks just.

Whereas section 396 gives a substantive right as well as laying down a procedure of which a defaulter may avail himself at any stage of the company's existence, it is only on a winding up that proceedings may be started against him under section 331. Broadly speaking, section 396 exonerates a director from an innocent breach of his duty or trust if he has acted reasonably, even though he is negligent. If he is guilty of misconduct or dishonesty , then he is liable, on a winding up of the company, to make good the loss caused to the company under section 331. It is to be noted that misfeasance proceedings against a director can be started only on a winding up of the company, for there is no procedure, short of an application for winding up, under the Companies Act 1994, by which a misfeasant director may be brought to task if he has not otherwise defaulted in complying with the various statutory requirements. On a winding up of the company, a director's conduct throughout the active existence of the company is reviewed and the position generally is, that the Courts will not hold a director liable for any loss to the company, unless he is guilty of dishonesty or negligence to an extent which amounts to "wilfully shutting his eyes" to the facts which are before him, for then, not having acted reasonably, he is not entitled to any relief under section 396. The Courts have always held a director liable under section 331, if his negligence amounts to a misconduct. Since an act of misfeasance or breach of trust is also misconduct, a director is often held guilty of breach of trust, or misfeasance under section 331 when in fact he is guilty of a breach of duty resulting from sheer negligence, for, save in extreme cases, the boundary between them is blurred. Since, in the event of a default by a director the Court examines the 'conduct' of a director, it may, and does, order a director to reimburse the company for the loss occasioned by the director's misdeeds, whether it is due to negligence, misfeasance or breach of trust. Section 396 would save a director from mere negligence, unless the company has suffered loss due to it when it will be seen whether he acted honestly and reasonably. This does not mean that directors are not liable for negligence nor that the term 'negligence', 'breach of trust' and 'misfeasance' mean the same thing. 'Misfeasance' is any breach of duty in the conduct of the company's affairs, which causes loss to the company. 'Breach of trust' is confined to a misapplication of the funds of the company. 'Negligence' is failure to use such reasonable skill and diligence as may be expected from persons with their knowledge and experience in the management of the affairs of the company. But all these terms may be described by a common denomination, namely, 'misconduct', and in proceedings under section 331, when a director is not entitled to any relief under section 396, the Courts have sometimes used one term where they should have used another, while examining the conduct of the officers. The result is, however, the same , for if a director has caused loss to the company by his misconduct or breach of duty he must make good the loss under section 331. As pointed out in a note in an English text book[1] on the corresponding section 333 of the English Companies Act, 1948, the section includes all cases in which an officer of a company has been guilty of a breach of duty as such officer, which has caused pecuniary loss to the company, by misapplication of its assets and for which he might have been sued. Buckley points out, further, that nonfeasance is not excluded from the scope of this section. An auditor, who by want of reasonable skill and care, certifies erroneous accounts, may be said to be guilty only of nonfeasance, but it is misconduct, and if it leads to the payment of dividend out of capital, or to the improper payment of a preference

1 Buckley : The Companies Act, 1948 13th Ed. p.674.

dividend, a remedy can be had under this section. Such an act would have exposed the auditor to an action and it is a breach of duty which has caused the company pecuniary loss; it is therefore, within this section.

Negligence, although not mentioned explicitly in the language of section 331, comes within its purview if it amounts to wilfully shutting one's eyes, although any honest and reasonable misfeasance may be exonerated by virtue of section 396. This view is not inconsistent with the dictum laid down in English cases like In *re Etic Ltd*[1] and In *re B. Johnson and Co.*[2] that mere negligence is not within the purview of a misfeasance section , for even Evershed M.R. had to agree in the latter case that in between the two extemes there is obviously a large range of conduct which may or may not be within the section. The position, therefore, is that section 331 contemplates acts of culpable negligence also and any such act that has caused loss to the company is actionable under section 331 either as a breach of trust or as a misfeasance.

Thus, in *Re Union Bank of Allahabad*[3] where the directors of a bank left all management of the bank's affairs in the hands of a manager and never cared to enquire whether the loans were made by the manager on good securities and the manager advanced large amounts to his relatives and friends either without security or on worthless securities and as a result dividends were paid out of capital the directors were held liable for misfeasance for they had not acted reasonably and could not, therefore, be excused under section 281 of the Companies Act 1913, predecessor of section 396 of the present Act. While discussing the liability of directors in this regard, Walsh J. pointed out that in the end the test of legal liability must depend upon the application of section 281 of the Act of 1913 to the established facts of the case.[4] That section would not be applicable unless the directors who took part in such breach of trust had acted not only honestly, but also reasonably, so as to show that they ought fairly to be excused for such a breach of trust. Since the directors had pleaded that they had acted bona fide, Walsh J. entered into a long discussion as to whether " bona fides is an answer to a charge of having misapplied monies of the company by payment of dividends out of capital". His Lordship dealt with the English cases in detail and distinguished the case before him from cases like *Kingston Cotton Mill Company case*,[5] which represented the "high water-mark of the immunity from legal liability of the ornamental and do-nothing director". The learned judge quoted with approval the standard of duty laid down in *Leeds Estates etc. Co vs Shepherd*[6] and the *Oxford case*[7] and pointed out that while their Lordships of the Privy Council had followed in *Profontine vs Granier*[8] the case of *Dovey vs Cory*[9] and found a director not liable for having trusted officers, when they had no cause to suspect them, in the Indian case before him, the directors were guilty of negligence in that they never took steps to go through the accounts. It was one thing to be misled by others and it was another not to attempt to do the thing at all.

11.9.6 **Recovery from Directors** – Section 331 of the Companies Act 1994 is merely a procedural section. It provides a method by which a director's action may be reviewed and any loss suffered by the company may be recovered. The Companies Amendment Act 1936 laid down a period within which proceedings must be started i.e., three years from the appointment of the liquidator. This put at rest the controversy whether the cause of action would lapse with the expiry of three years from the date of the misfeasance although the liquidator might not have been appointed by that time.

1 [1928] 1 Ch. 861,873.
2 [1955] 1 Ch.634,649.
3 AIR 1925 All.519.
4 ibid at p. 520.
5 [1896] Ch.D. 331
6 (1887) 36 Ch.D. 787
7 (1886) 35 Ch.D. 502.
8 (1907) A.C. 101
9 (1901) A.C. 477.

This does not mean that the scope of the section has been enlarged by the amendment. The Allahabad High Court has held in *Benares Bank Ltd. vs Sri Prakasha Bhagwan Das and others*[1] that sub-section (1) of the section has imposed a new condition on the liquidator, without depriving the objects of his suspicion of the benefits of the ordinary canons of the law of limitation. The jurisdiction of the Court remains discretionary and it may be that in a proper case, the Court may still view lapse of time as a sufficient reason for refusing to exercise its jurisdiction in the liquidator's favour.

Although section 331 is only a procedural section, it is a powerful weapon against a delinquent director, as either of the persons most interested, namely, the liquidator on behalf of the defunct company, a creditor or contributory can initiate proceedings for any misfeasance or breach of trust. The section provides an additional mode by which a liquidator can recover monies lost by the company and orders passed under this section do not bar suits against a third party.[2] Similarly, the barring of an application under this section does not prevent the liquidator from seeking a remedy by a regular suit.[3] As to what must be specially averred by the liquidator in a petition under section 331, the Lahore High court has held that such a petition is not bad merely because it does not state the specific amount claimed. He must, however, bring all facts on which the claim is based to the notice of the Court. The amount of the compensation is to be assessed, not by the liquidator, but by the Court.[4]

Section 331 requires as a condition for its operation that it should appear that the respondent, being a past or present director or officer of the company, has misapplied or retained or become liable or accountable for money of the company or has been guilty of misfeasance or breach of trust in relation to the company. The condition being fulfilled, there must be an application by the liquidator or any creditor or contributory ; the Court may then examine the conduct of the respondent. Relief is by an order to restore or repay the money or property or to contribute such sum to the assets of the company by way of compensation in respect of the misfeasance or breach of trust as the Court thinks fit. This section provides an alternative method for enforcing the liabilities which might have been enforced by a suit. The Court, in an application under this section, has a discretion in assessing the amount of the compensation and is not bound, as a Court hearing a suit would be, to give a decree for the whole loss suffered. section 331 provides a convenient method by which , in the course of winding up a company, the same Court may deal with all the internal affairs of the company.

The liquidator is not required to mention a specific sum that he claims and his application is not bad in law if he omits to do so. The hearing of an application under this section is summary in nature and the rules contained in the Code of Civil Procedure are not to be followed strictly.[5]

Mere negligence on the part of a director may not amount to a breach of duty, as the Courts are inclined to exonerate a director under section 396 in such a case. But if his negligence amounts to nonfeasance resulting in a loss to the company, the director's acts may be reviewed under section 331 and misfeasance proved. Hence, where a director , not only did not exercise care in ascertaining the true state of affairs of the company but also wilfully shut his eyes to it until a very late stage in its history, it was held that he was guilty of negligence amounting to misfeasance.[6] The director concerned had failed to enquire whether it was proper to entrust the management of his company to another company, whose directors were controlled by a person whose antecedence was unknown to him, a procedure which had invoked criticism in an auditor's report.

Different terms have been used by the Courts to indicate the degree of negligence which appfoaches a breach of trust or misfeasance. In *National Bank of Upper India vs D.N. Sapru and others*,[7] the directors could, under the articles, delegate the authority and power to a

1 AIR 1946 All.269,274
2 Dehra Dun Mussoorie Electric Tramway Co. Ltd vs Hansraj and others AIR 1935 All. 995,999.
3 Billimoria vs Mary D'Souza AIR 1926 Lah. 624,626.
4 Mulk Raj vs Official Liquidators, People's Bank AIR 1938 Lah.658,664.
5 Monroe J. in Mulk Raj vs People's Bank AIR 1938 Lah. 658,663-4.
6 Subbayya vs Machayya AIR 1942 Mad 365, 367.
7 AIR 1926 Oudh 243.

committee. When the company suffered loss as a result of breach of trust by a member of the committee it was held, on a misfeasance summons taken out under section 235 of the Act of 1913 equivalent to section 331 of the present Act that the directors were not liable, unless they were guilty of 'wilful neglect or default'. The case of *Re City Equitable Fire Insurance Co.*[1] was referred to. In the English case it was held that an act or an omission to do an act was wilful, where both knowledge and intention were present; but if that act or omission amounted to a breach of that person's duty, and therefore to negligence he was not guilty of wilful neglect or default, unless he knew that he was committing and intended to commit a breach of his duty or was recklessly careless in the sense of not caring whether his act or omission was or was not a breach of duty.

This does not mean that directors can, with impunity, neglect their ordinary duties over a long period. In *Govind vs Rangnath*[2] the directors met at extremely irregular intervals and the business was left to the managing agents. The case of *Re City Equitable Insurance Co.*[3] was discussed in detail but the director concerned was not held liable in the particular case as the application against him was time barred. The Madras High Court followed the English case referred to above in *Doss vs Connell*,[4] that a person is not guilty of wilful negligence unless he knows that he is committing and intends to commit, a breach of his duty, or is recklessly careless in the sense of not caring whether his act or omission is or is not a breach of duty and that the directors are entitled to rely on their subordinates. The fiduciary position of the directors makes them liable to replace the moneys of the company which they use for an ultra vires purpose.[5] The liability of a director, whether for negligence, misfeasance or breach of trust, arises from his fiduciary position vis-a-vis the company, although this liability may be based on his position as a trustee and on the contract between him and the company contained or implied in the articles.[6] A director will not be liable if he has lost the capital in legitimate business dealings, but in so far as being entrusted with the monies of the company, a director is jointly and severally liable for breach of trust if, for example, he has applied assets to other than the company's defined objects. Thus, if the directors enter into a contract and make a payment on it during the winding up proceedings , they do so at their own peril for such payments are void under section 227(2) of the Companies Act ,1913 corresponding to section 322 of the current Act. The directors in this case could not be said to have acted reasonably within the meaning of section 396 of the Act and the English cases of In *re Claridge's Patent Asphalt Co*[7] and *In re Allsop*[8] where directors were exonerated under a statutory provision corresponding to section 396 of our Act was distinguished. The English directors had also acted ultra vires but in doing so they had taken the best legal advice available, whereas in the Indian case the directors were not misled by an outsider and had taken part deliberately in ultra vires acts.

Similarly, a director is bound to exercise his powers for the benefit of the company and for that alone. He cannot withdraw from the till of the company and mix it with monies belonging to him; he cannot take a mortgage in his own name as security for the whole sum representing to the mortgagor that the security of the monies advanced on the mortgage was his own. If he does so, he is guilty of breach of trust. The fact that the act was not concealed from the auditors does not obviate his guilt.[9] Since the director's fiduciary position vis-a -vis the company arises partly out of the contract in the Articles of Association, an application under section 331 against a director will be treated, so far as the law of limitation applies, as a case of breach of contract.[10]

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1 [1925] 1 Ch. 407.
2 AIR 1930 Bom 372.
3 Supra
4 AIR 1938 Mad. 124,128
5 Kathiawar Trading Co. Ltd vs Virchand Dipchand(1894) ILR 18 Bom. 119.
6 Peninsular Locomotive Co. vs Langham Reed and others AIR 1937 Pat. 293.
7 [1921] 1 Ch. 543.
8 (1903} 51 W.R. 644.
9 In re A. E. Alexander and Co. Ltd AIR 1925 Cal.852,855.
10 Karachi Bank Ltd vs Shewaram and others AIR 1933 Sind 103,107.

The standard of duty and the liability of a director is thus a curious blend of the law of contract and trust. Not as rigid and limited as the powers of a trustee for a specific purpose, the directors are nevertheless, subject to the strictest scrutiny as to how they have applied the assets of the company. Hence, before section 396 can be applied in their favour, it must be shown that the directors had acted reasonably as well as honestly. Thus, they are guilty of a grave breach of duty if they allow the managing director to dissipate the company's funds by gambling in differences.[1] Also, where the managing director of a bank induces directors to pay dividends partly out of what was really capital, he may be said to have misapplied the company's money and hence is guilty of misfeasance and breach of trust. The Court can compel a director, in such a case, to contribute a reasonable sum by way of compensation, as well as hold him liable under the Penal Code.[2] As the prime object of holding directors liable for acts of misfeasance is to protect the investing public and the creditors, the Courts will hold guilty of misfeasance a director who has not observed the various statutory duties imposed on him, if loss results thereby. Thus, allotment of shares to a person who has not applied for shares or who has not paid the sum due on application is illegal and directors who make such allotments are guilty of misfeasance, for it is equivalent to being a party to a calculated and deliberated fraud in the flotation of the company.[3]

If directors misuse their powers as directors for their own advantage, the transaction as against the company is of no effect and the court will not enquire whether the company derived any benefit from it. Thus, in *E.B.M.Company vs Dominion Bank*[4] all the shares of a company were held by three directors , the remaining two shares being held by two ladies, each of whom was also a director. The three male directors, without consulting the two ladies, pledged the company's property to secure the debt of one of the directors under a so-called "unanimous" resolution. The transaction was held to be absolutely void and the Court refused to consider whether, in effect, it was for the benefit of the company.

A director is, however, not responsible for fraud practised by fellow-directors and will not be liable if co-directors issue false reports and balance sheets provided that books are properly kept and audited and there are no circumstances arousing suspicion.[5]

A director must not fetter his discretion to act for the best of the company. This does not mean, however, that he is guilty of a breach of duty because he is a member of the trade union of employees.[6] Section 331 will apply only to the conduct of a director as such, and for something done by him before he was a director he could not be held responsible.[7] Following the proposition that a director is responsible only if he has acted as a director, the Lahore High Court went on to hold a few years later in *Sri Ram vs Nur Mohammad*[8] that section 235 of the Act of 1913(i.e. section 331 of the current Act) cannot be applied for enforcing sums due under contracts between the company and other persons, whether they happen to be directors or not. The liquidator had, in this case, sought to make an ex-director liable for afrears of rent owed by him to the company. The Court held, however, that the terms of section 235 showed that the section was intended to provide a summary procedure for the recovery of money or property misapplied or retained by a director or other officer of the company. It could be invoked for the purpose of compelling the persons enumerated in that section to repay or restore sums which had come into their hands by virtue of their position as there defined. In Province of West Pakistan vs Gurmani,[9] Faruqui J. held that the main object of section 235 of the Act of 1913 was to increase the assets of the company by making a director and other persons named therein to contribute to the assets of the company by way of

1 T. Chettiar vs Rajagopalam AIR 1944 Mad. 536,538.
2 Doulat Rai vs Emperor ILR(1915) Lah 471.
3 Indian States Bank Ltd. vs Sardar Singh AIR 1934 All. 855,863.
4 AIR 1937 P.C.279.
5 T. Chettiar vs Rajagopalam AIR 1944 Mad. 536,538.
6 Boulting vs A.C.T.A.T [1963] 2 WLR 529.
7 Hans Raj Bhandari vs Liquidator, Lahore Bank AIR 1915 Lah 132,134.
8 AIR 1925 Lah 194,195.
9 PLD(1965) Kar.110.

compensation in respect of any misapplication , retainer, misfeasance or breach of trust. This section appears in Part V of the Act , which relates to the winding up of the company and, having regard to its provisions, it is clear that it is attracted only when the company as such has suffered. Where there was no evidence or suggestion of such loss, the application under section 235 would be dismissed with costs.[1] This was a case of take-over of a company with liabilities and onus was on the applicant to prove that the directors had not acted bona fide.[2]

The Court has no power to make an order against all the directors for all acts of misfeasance without finding which director is responsible for what.[3] There must be a specific allegation against a particular director.[4] But liability of directors of a company who act in concert and are liable in respect of acts of misfeasance and malfeasance, was joint and several in respect of breaches of trust committed by them and all of them may be made equally liable severally and jointly.[5]

But where the directors abstain from making enquiries and approve acts of mismanagement, they cannot escape liability, as their conduct , in that case will amount to wilful misconduct and they are liable by being deliberately negligent.[6] Earning of low profits, or failure to recover debts of the company inspite of taking adequate steps do not amount to misfeasance and there ought to be some breach of trust resulting in loss to the company.[7] The section would include an auditor if he is guilty of neglect of duty or misfeasance.[8] Receiver or manager appointed by debenture holders are not officers within the meaning of this section.[9] An application by the liquidator under this section will not be barred because a suit, by the company itself while it was a going concern, had failed.[10]

There must be an application by the liquidator, creditor or contributory under this section and where the official liquidator makes application only against a delinquent managing director and other directors are also found to have also contributed to the mismanagement of the company, the Court will not award damages against them.[11]

For a proceeding under this section, the conduct need not be criminal. The section covers breach of duty although such a conduct need not be criminal.[12] A creditor or contributory making an application under this section must have pecuniary interest and a fully-paid shareholder of a company, where the liabilities of a company exceed its assets, may not apply.[13] In *Official Liquidator vs P.A. Tendolkar*[14] the Supreme Court of India commented that such proceeding under section 235 of the Act of 1913 cannot authorise passing of orders to compel heirs or legal representatives to do anything.[15] For a different view see *Official liquidator vs Dr. Sailendra Nath Sinha*.[16] Also see *Official Liquidator vs Parthasarathi Sinha*[17] where the Supreme Court of India held that proceedings under this section could be continued against heirs of delinquent directors but no order could be passed against them under this section. De facto directors are within the purview of this section.[18]

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1 ibid. at p.117.
2 Also see Official Liquidator vs Mathura Prasad [1963] 1 Company Law Journal 108(All) on this point.
3 In re Central Calcutta Bank Ltd.AIR 1959 Cal 625.
4 Official Liquidator vs Joginder Singh Kohli [1978] 48 Comp. Cas.357.
5 Offl.Liquidator, Modern Transporters P. Ltd vs Mulk Raj Mehta [1971] 41 Comp. Cas. 573.
6 In re F.& C.Osler(India) Ltd. [1976] 46 Comp. Cas. 698.
7 Bholanath Kundu vs Bholanath Kundu & Co.P.Ltd.[1987] 61 Comp. Cas. 10(Cal).
8 Re Thomas Gerrard and Son Ltd. [1967] 2 All E.R. 525.
9 Re Johnsons & Co. (Builders) Ltd[1955] 2 All E.R. 775.
10 Jaipur Vastra Vyopar Sangh Ltd.,In re [1970] 40 Comp. Cas 1140.
11 In re National Sugar Mills Ltd. (1978) 48 Comp. Cas. 339(Cal).
12 Maylayalee Bank Official Liquidator vs P.S. Mannadian (1963) 33 Comp. Cas 955 (DB)(Mad).
13 Halsbury's Laws of England 4th Ed. Vol 7 Para 1194.
14 (1973) 43 Comp. Cas 382
15 Also see In re Peerdan Juharmal Bank Ltd (1958) 28 Comp. Cas.546; Official Liquidator vs Maganlal Hirachand Shaha (1980) 50 Comp. Cas. 762, Modern Transporters Ltd vs Jagadishraj Mehta (1977) 47 Comp. Cas.302.
16 (1973) 43 Comp. Cas.107.
17 (1983) 53 Comp. Cas 163.
18 Official Liquidator Navarashtra Publishing Co. Ltd. vs Ashok Kumar (1976) 46 Comp.Cas. 572.

The Court has power to apportion the sums to be paid by directors and others as compensation to the company.[1] But the proceedings under this section are available only against persons expressly mentioned in the section.[2] Misfeasance proceedings are summary proceedings to compel delinquent directors and officers to make good the loss.[3] On amalgamation of a company with another, misfeasance proceedings initiated by transferor company can be continued by transferee company.[4]

It is well-settled that in applications under section 235 of the Act of 1913 the allegations of the nature of misfeasance, non-feasance, malfeasance, misapplication or breach of trust, etc., are serious in nature which must be specific and the application must contain narration of the specific acts of commission and omission on the part of each of the directors , quantifying the loss to the company arising out of such acts of omission etc. The burden of proof rests on the official liquidator.[5]

Where procedure is laid down in the Companies Act and Rules thereunder, the Code of Civil procedure is not applicable.[6] Court has power to order delivery of books of company which are in possession of somebody else.[7] The power of the Court under section 235 of the Act of 1913 is discretionary.[8] But the Court cannot entertain a time-barred application.[9] A claim for damages against a liquidator for acts of misfeasance can only be granted by High Court under the Act and not by an ordinary civil court.[10]

Prosecution for criminal offence and proceeding under section 235 of the Act of 1913 can proceed simultaneously.[11]

Although section 331 is a weapon in the hand of the liquidator, creditor or contributory to recover damages from a delinquent director or officer, this section applies only after the company has been ordered to be wound up.

11.9.7 **Penal Liability of Directors** – The Companies Act 1994 tries to ensure that the management runs the company properly and lays down numerous rules which the directors and officers of the company must observe. Any breach of these duties is treated as a statutory offence and penalties follow, unless the officers can claim relief under section 396 of the Act. This section follows section 281 of the Act of 1913 and most of the cases that have been reported are under the old section 281 of the previous Act. In most cases the officers of the company come before the Court, after being threatened with prosecution by the Registrar or some other regulatory body(like the S.E.C.) for some default and if the Court is of the opinion that the default is accidental, the Court may exempt such officers from liability under this section. It is a general practice that the courts will grant relief to the officers and the directors , provided that they are not guilty of dishonest motives and it is not too late to intervene. Perhaps such a liberal outlook is helpful to the members of the new commercial class that is coming up now, as most of them are neither knowledgeable nor skilled in company practice and may face undue hardship by an over-zealous enforcement of the statutory penalties.

Thus, the provisions of section 281 of the Act of 1913(corresponding to section 396 of the current Act) have been interpreted to relieve officers of their negligence, carelessness,

1 Re Morecambe Bowling Ltd. (1969) 1 All E.R. 753.
2 In re Supreme Bank of India Ltd. (1964) 34 Comp. Cas. 34.
3 B.Mehta and Co.vs. Puranmal Bubna [1979] 49 Comp. Cas. 98.
4 Merchants Bank Ltd vs M.Dharmasambarthani Ammal [1967] 37 Comp. Cas. 227.
5 Official Liquidator vs Raghawa Desikachar [1975] 45 Comp.Cas. 136(S.C.);In re Supreme Bank of India Ltd.[1964] 34 Comp. Cas. 34;Official Liquidator vs R.C. Marathe[1980] 50 Comp. Cas. 562.
6 Mulk Raj vs Official Liquidator, People's Bank [1938] 8 Comp. Cas. 248.
7 Gopalaswamy Gounder vs Krishnaswami Gounder [1940] 10 comp. Cas. 290.
8 Sham Lal Diwan vs Official Liquidator, U.P.Oil Mills Ltd [1933] 3 Comp. Cas. 365.
9 Bharat Nidhi Ltd vs Trade and Industries Corpn Ltd. [1962] 32 Comp. Cas. 442.
10 Muni Lal Peshawaria vs Balwant Raj Kumar [1964] 34 Comp. Cas. 717.
11 P.K.Nedungadi vs Malayalee Bank Ltd. [1972] 42 Comp. Cas. 120;Sailendra Nath Sinha vs State (1954) 24 Comp. Cas. 539.

lack of caution, provided the same were not committed with any improper motive or fraudulent intent or if they were due to honest misapprehensions of fact or ignorance of law or of the correct state of the company's affairs. But in each case the party seeking relief must make the fullest and most candid disclosure before the High Court. If proceedings have already been started against the director or officer concerned, the court hearing the case can exonerate the delinquent under section 396(1). But the High Court in its original jurisdiction will provide relief only if proceedings are threatened but not yet started. The language of sub-section (2) is clear in this respect.

The then East Pakistan High court ruled in In the matter of *Elahee Baksh and Co. Ltd*[1] that sub-section (2) of section 281 of the Act of 1913 applies only before the proceedings have been commenced. The person who has committed a default or is liable for negligence may come to the High Court for relief from consequential liability in anticipation of proceedings but once proceedings have commenced, according to the provisions of sub-section (1) the only court that has power to relieve the defaulting person from liability is the court hearing the case. When the managing director of a company received a summons from the S.D.O. , North Chittagong, summoning him and the other directors of the company to appear before him to answer a charge of violating the provisions of section 104 of the Act of 1913 (return of allotment to be filed) he moved the High Court for an extension of time as the failure to comply with the provisions of section 104 was purely accidental. Hamoodur Rahman J., however, cited the English case of In *re Gilt Edge Safety Glass Ltd*[2] and said that he could intervene only to a limited extent although he was satisfied that the delay in filing of the return was purely accidental and it was just and equitable to grant relief. This case was followed by the High Court Division in 1992.[3]

After initiation of proceedings, the High Court has no jurisdiction to grant relief.[4]

In *Crescent Bolts and Nuts Manufacturing Co. and others vs Registrar Joint Stock Companies*[5] the petitioners admittedly committed default by not filing summaries of share capital with the Registrar for the years 1952 to 1956, as required under section 32 of the Companies Act, 1913; further, they contravened section 72 of the same Act which required a company to give notice of the situation of its registered office to the Registrar; lastly, they failed to comply with section 87 of the Act by not sending returns to the Registrar regarding the directors, managers and managing agents for the years 1951 and 1955. The company and officers pleaded ignorance of law and prayed for exemption under section 281 of the Act of 1913 on the ground that they had acted honestly and bonafide. The Karachi Bench of the West Pakistan High Court held that the company was not competent to ask for relief under this section, that the persons named in the section could apply if they apprehended that action would be taken against them. Justice Qaderuddin said at page 34 of the judgment that it was not easy to distinguish between mere forgetfulness and inadvertence on the one hand and deliberate negligence on the other. If a show cause notice is given , then those whose fault is accidental get the opportunity of rectifying their mistakes and those who persist in their default can be shown to have been wilful. The power which is vested in the Registrar for commencing prosecution is not meant to be abused and that it is an abuse of power if the Registrar sleeps over defaults for years and then launches prosecution.

Even when the Registrar of Companies filed a criminal complaint despite notice of a petition for relief under this section for apprehended liability, the petition was maintainable and could be disposed of by the Court with an appropriate order.[6] That same Court held earlier that the object of this section was to provide against undue hardship in deserving cases and it was proper to relieve persons, who, though technically liable in law, ought to be excused rather than subjected to legal proceedings.[7]

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1 PLD(1958) Dac.378.

2 [1940] 1 Ch.D. 495.

3 Dr. Shorful Haque vs The State (1992) 12 BLD (HCD) 387.

4 Sri Krishna Prasad vs Registrar of Companies [1978] 48 Comp. Cas. 397.

5 PLD(1959)Kar.32

6 P.S.Bedi vs Registrar [1985] 2 Comp.L.J. 122(Delhi).

7 Om Prakash Khaitan vs Shree Keshariya Investment Ltd [1978] 48 Comp. Cas.85.

The words 'any proceeding' makes this section apply to all legal proceedings, civil, criminal or otherwise. The fact that a person is a director of the company purely on account of some special skill or service does not by itself exonerate him from liability. He must, like any other director, satisfy the Court that he fulfils the criteria to obtain relief from liability under this section.[1] But see *G.D.Bhargava vs Registrar of Companies*[2] for the proposition that offences under the Penal Code fall outside this section. If a person is convicted, then no relief can be granted under this section.[3] It cannot be said that the granting of relief to a liquidator under this section in a trial for failure to file the statements within time can be equated with an order of discharge or acquittal.[4]

The Indian Courts have held that the words of this section are confined to relieve 'officers' of the company from fines and penalties, and not the company from calling, holding or conducting annual or even other meetings of the companies according to the statute. This provision does not permit suspending the operation of the relevant sections of the Companies Act in respect of such meeting and extend such time.[5]

In Bangladesh, in cases for condonation of delay, relief is sought under section 396 of the Act. However, in view of the amended language of section 81 of the Act which enables the Registrar to extend time for holding the general meeting there is some controversy whether the High Court can extend time for holding the general meeting and whether it is possible to hold a general meeting without the permission of the Court. Section 183 speaks of extension of time under section 81 but this extension refers to an act by the Registrar. In *Social Marketing Co. vs Mr. Mahbubuzzaman*[6] the High Court Division held that the Court was competent to condone the delay in holding the annual general meeting under section 76 of the Act of 1913 but a meeting called by the company after the expiry of the statutory period was not valid.[7] The Delhi High Court however held that since under section 633 of the Indian Act (corresponding to section 396 of our Act) the Court may relieve officers of the company wholly or partly from liability on account of defaults on such terms as it may think fit, so acting under this section the courts grant time within which the default must be redeemed only by way of condition to the grant of relief.[8]

The English Court of Appeal has held that this section will apply in proceedings against an officer including a director for breach of his duty to the company as an officer and does not apply to claims made by a stranger to the company against an officer or director to enforce a civil liability.[9]

In *Burno Regazzi vs Registrar, Joint Stock Companies*[10] the directors admitted their defaults in complying with the provisions of sections 77 and 134 of the Companies Act 1913 as they did not file the statutory report and the summary of share capital and balance sheet. On getting a notice from the Registrar they filed some of the documents late. The lawyer for the Registrar relied on the case of *Bhagirath Chandra Das vs Emperor*[11] where the Calcutta High Court held that the directors had wilfully and knowingly permitted the company to fail to carry out its legal duties. Qaderuddin J. held that it was reasonable to conclude that their default commenced with their forgetfulness and if that was the case, then it was possible that they were not able to think of their omission and rectify it until they were reminded of it. He

1 Re Beejay Engineers Pvt. Ltd [1983] 53 Comp. Cas. 918.In re Supreme Bank of India Ltd [1964] 34 Comp. Cas.34.

2 [1970] 40 Comp. Cas.664.

3 Dulal Chandra Bhar vs State of West Bengal [1962] 32 Comp. Cas.1143.

4 Pylo Luka Muricken vs Registrar of Companies [1977] 47 Comp. Cas.291(Ker).

5 In re Coal Marketing Co. of India Ltd. [1967] 37 Comp. Cas. 720(Cal);In re Bank of Deccan Ltd.(1960)30 Comp. Cas.284.

6 (1993)13 BLD(HCD) 569

7 Also see Sultan Siddique Raisul Jalil Chowdhury vs. Spectra Net Ltd. 4 BLC (1999) HC 348.

8 In re Swastic Benefits (P.) Ltd [1968] 38 Comp. Cas.325.

9 Customs and Excise Comminssioners vs Hedon Alpha Pvt. Ltd(1981) 2 All E.R. 697 (CA).

10 PLD(1959)Kar. 48

11 AIR 1948 Cal. 42.

rejected the argument that it was not the duty of the Registrar to remind of the default because the applicants could come to the Court only after they had apprehension that any claim might or will be made against them. The Registrar was duty bound to keep an eye on the compliance of the law by the companies and their officers and 'there is thus a connection between the duties of the Registrar and the applications which are made for obtaining relief under section 281 of the Act...punishment has not been prescribed by the law out of vindictiveness but with the intention that the law should be observed. It is therefore, proper in relation to those defaults in which knowledge, willfulness, honesty and reasonableness are relevant considerations that those who are entrusted with the duty of enforcing the law should give an opportunity to the defaulters to explain and rectify their mistakes and after giving the opportunity to watch whether they react honestly and reasonably or not...'[1]

As to the matters to be disclosed in a petition under section 281 of the Act of 1913, Mr.Justice Hamoodur Rahman has observed in In the matter of Elahi Baksh and Co.[2]:

> ...Now, In the matter of the Chittagong Lending and Shipping Co.Ltd, decided by me on 24th. of February, 1956, I have already fully discussed the relevant law and indicated the circumstances in which this court will exercise the jurisdiction given to it to extend the time....But in each case the party seeking to be so relieved must make the fullest and most candid disclosure before this Court and in such an application a mere statement that the omission was accidental or inadvertent, without giving with sufficient particularity the reasons for the breach of the statutory duty imposed by the act, will not be sufficient....

The case of *In re Coal Marketing Co. of India (P) Ltd.*[3] may also be referred to. The satisfaction of the Court is not a mere ritual.

Most of the statutory duties imposed on the directors and other officers of a company are sought to be enforced by means of penal provisions. But the Act usually provides that an offence will only be committed if the breach of duty was done "knowingly and wilfully"; both knowledge and intent must be proved. Thus under section 32 of the Act of 1913(section 36 of the current Act) a company was required to make a list of at least once a year of all persons who, on the day of the first or ordinary general meeting in the year, were members of the company. If a company made a default in complying with the provisions of the section, then under sub-section (5) the company and its officers who 'knowingly and wilfully authorises or permits the default' should be liable to fines. In *Sundar Das vs Emperor*[4] it was held that only intentional default is within the ambit of this section. Otherwise the default would be merely inadvertent and being unintentional, the accused should not be convicted. Similarly, where officers took legal advice and acted accordingly, it was held that they could not said to have been knowingly parties to the default.[5] Also, where there was no annual general meeting held as required by section 76 of the Act of 1913 (section 81 of the current Act) and it was held that the company's officers could not be punished under section 32 of that Act for not maintaining the list of members on the day of the general meeting, it was because they did not 'knowingly and wilfully' permit the default under that section.[6] Before an officer of a limited company can be convicted under section 134 of the Act of 1913(section 190 of the Act of 1994)for default in submitting to the Registrar the balance sheet laid before the company at a general meeting, if no such general meeting has been held, then, it is necessary in the first instance, to show with reference to the provisions of section 76 of the Act of 1913 (section 81 of the current Act) that the officer was knowingly a party to the default in holding the general meeting.[7]

A director cannot take advantage of his own lapses and where no annual general meeting was called in one year and no balance sheet was laid before the company at the general

1 PLD (1959) Kar 48, 50
2 PLD(1958) Dac.378
3 [1967] 37 Comp. Cas. 720.
4 AIR 1929 Lah.836.
5 Sree Minakhi Mills Co. vs Assistant Registrar AIR 1938 Mad. 640.
6 Surendra Nath Sarkar vs Emperor AIR 1942 Cal.225.
7 Rajkumari Kusari vs Registrar AIR 1918 Cal.190.

meeting the director could not take the defence that this default was because no general meeting was held as the accused himself was a party to the default in holding the general meeting.[1]

'Having acted reasonably' means having acted in the way in which a man of affairs with reasonable care and circumspection could be reasonably be expected to act in such a case. It should be supported with good reasons or should be one which a reasonable person might reasonably make. Failure to take legal advice is not 'acting reasonably'[2]. Nor will relief be granted to directors who act blindly at behest of any majority shareholders or other controlling authority without taking ordinary care and caution.[3]

Relief was granted when the directors had acted promptly before the issuance of the show cause notice,[4] or where the directors had started the corrective process as soon as they learnt about the manipulation of accounts of the Company before it came to the knowledge of the Registrar.[5] Relief should be prayed for only if the applicant has acted honestly.[6] Where delay in preparation of accounts and in sending copy to the Registrar involved no malafides or dishonesty, relief can be granted under this section against apprehended proceedings.[7] In this case the directors could not prepare balance sheets as there was a conflict between the company and the income tax authorities. Also, where directors of a company fail to lay annual accounts at annual general meeting by relying on a circular of the Company Law Board in India, they can be relieved under this section.[8] Power to relieve liabilities also applies to a case of ultra vires acts.[9]

In order that a conviction under section 36 (for not maintaining and sending to the Registrar a list of the members), section 83 (for not holding the statutory meeting) and section 190 (for not forwarding a copy of the balance sheet to the Registrar) of an officer of a company may be sustained , the prosecution has to prove that the particular officer knowingly and wilfully authorised or permitted the defaults. The offence is complete if the officer of the company knew of the defaults and permitted them and it was not necessary to prove that he wilfully authorised those defaults.[10] Similarly, for the purpose of convicting the officers for these technical offences, it is not necessary that there should be fraud or dishonesty on the part of the directors, nor can it be said that because the default is of a technical nature, a nominal sentence is called for.[11] It was held in *Batliwala, Sons and Company vs Emperor*[12] that the requirements of section 73 of the Act of 1913 (section 78 of the current Act)would be satisfied if the name of the company had been published with the necessary conspicuousness and legibility outside the room used as the company's office, but inside the building in which it was situate. But where the interests of the public are vitally concerned, the Courts adopt a strict attitude. In *Tota Ram vs Emperor*[13] the balance sheet of a company should have been made out and filed with the Registrar on 20 August but was not in fact submitted till 22 October, and consequently the chairman of the board of directors and the managing agents of the company were convicted.

In *Supt. and L.R.Bengal vs Akhil Bandu*[14] it was held that the expression 'wilfully' used in the Companies Acts, both in the sub-continent and in the United Kingdom, meant nothing

1 Devendra Nath Das Gupta vs Registrar AIR 1917 Cal.1.
2 Re Duomatic Ltd. [1969] 1 All E.R.161; Secy of State for Education vs Metropolitan Borough of Tameside [1976] 3 All E.R. 665,695.
3 Selangor United Rubber Estates Ltd vs Craddock[1968] 2 All E.R. 1073.
4 G.M.Mohan vs Registrar,Karnataka. [1984] 56 Comp. Cas.265
5 In re Tri Sure India Ltd [1983] 54 Comp. Cas.197.
6 T.V.Angappan vs Coimbatore Murugan Mills Ltd [1983] 54 Comp. Cas 5.
7 In re Filmistan (P.) Ltd [1959] 29 Comp. Cas.34.
8 Harrisons Crosfield(India) Ltd vs Registrar [1980] 50 Comp. Cas.426 Ker.
9 In re Claridge's Patent Asphalte Co. Ltd. (1921) 1 Ch. 543.
10 Ballav Das vs Mohan Lal AIR (1936) Cal. 237.
11 Bhagirath vs Emperor (1947) 48 Cr.L.J.236.
12 (1941) 43 Bom L.R.105
13 AIR 1916 Lah.199.
14 AIR 1936 Cal. 680, 683

more nor less than the spontaneous action of a person who was a free agent. It was, of course, to be interpreted according to the facts of each case. In *Baidya Nath Biswas vs Emperor*[1] current expenditures had been debited to organisation expenses when it ought to have been debited to revenue accounts in the balance sheet, so that the balance sheet contained a false statement and the question was whether liability under section 282 of the Act of 1913(section 397 of the current Act) had been incurred. The Calcutta High Court was of the opinion that it was not necessary that the statement should be such as to deceive any one or that it should have been dishonestly made.

But the Bombay High Court took a different view in In *re Shamdasani*[2] and held that in order to attract the penalty under section 282 of the Companies Act, 1913 (section 397 of the current Act) false statements in the balance sheet should be made wilfully knowing them to be false. The controversy was settled in *Srinivas Mall vs Emperor*[3] where the Privy Council held that unless the statute, either clearly or by necessary implication, ruled out mens rea as a constituent part of the crime, a defendant should not be found guilty. The Calcutta High Court held in *Pulin Chandra vs Emperor*[4] that the language of section 282 did import an element of mens rea.

Apart from offences made punishable by the Companies Act, directors may also be liable for offences under the Penal Code for fraud, misrepresentation and so forth.[5]

Section 195 of the current Act (section 138 of the Act of 1913) provides for investigation into the affairs of the company by the government at the instance of one-tenth of the shareholders and if from any such report of investigation it appears that any person has been guilty of a criminal offence, criminal proceedings may be instituted. Section 333 of the current Act (section 237 of the Act of 1913) provides for prosecution of directors, shareholders, managers and other officers in the course of winding up of the company either at the instance of the Court on its own or the liquidator or on the application of any interested person.

The above-mentioned provisions for inspection of the affairs of the company, while it is a going concern and for prosecution of delinquent directors, when the affairs of the company are being reviewed in liquidation are good sanctions against fraud or other criminal activities by those who are in control of the management of the company. They provide procedure by which directors may be prosecuted, independent of the Code of Criminal Procedure,1898, so that, if directors are guilty of offences which come within the purview of section 333, they can be prosecuted without the leave of the Company Judge.[6] A penal enactment in a special statute is no bar to a prosecution under the Penal Code. Thus penalty for falsification of books in the Companies Act (seven years under section 232) does not nullify any other sanction offered by any other statute. The purpose of the Companies Act is to facilitate the enforcement of the general law and not to hinder it.[7] The provisions of the Companies Act do not exclude a private complaint of a criminal offence committed in relation to a company.[8] Section 333 uses much the same words as section 203 of the Act (section 141A of the Act of 1913) regarding filing of criminal cases against delinquents after investigation. The whole scheme of the section appears to be enabling rather than mandatory or exclusive. The Court may order the liquidator to prosecute or to refer the matter to the Registrar. The Registrar may refuse to prosecute and the liquidator, with the previous sanction of the Court may prosecute. In *Emperor vs Vishwanath*[9] it was held that there is nothing to prevent a private person making a complaint to a Court of offences under the Companies Act or the Penal

1 AIR 1935 Cal.741.
2 AIR 1929 Bom.443
3 AIR 1947 P.C. 135.
4 AIR 1948 Cal 190
5 Daulat Rai vs Emperor AIR 1915 Lah.471. (case of offence under section 409 and 477A of the Penal Code).
6 Emperor vs Bishen Sahai AIR 1937 All. 714,716.
7 ibid.
8 Surendra Nath vs Kalipada Das AIR 1940 Cal. 232.
9 AIR 1942 Sind 9

Code against directors or officers of the company in relation to the company even if the company is being wound up.

11.10.1 **Failure to File Returns etc.** – The Companies Act provides for returns to be filed of various acts of companies. Section 151 of the Act (corresponding to section 104 of the Act of 1913) requires returns of share allotments to be filed at the Registrar's office within sixty days. Penalty for not filing the returns on time is one thousand taka for each day of default. The Registrar has been given the power to extend time for filing such returns. The Court can extend the time if it finds that the delay was accidental or due to inadvertence.

Section 159 of the Act (corresponding to section 109 of the Act of 1913) provides that a mortgage or charge on the properties of a company will be void against the liquidator and any creditor of the company unless the prescribed particulars of the mortgage or charge are registered at the Registrar's office within twenty one days after the date of its creation. Section 171 of the Act (corresponding to section 120 of the Act of 1913) provides that the Court may extend the time for such registration if the non-filing of the particulars of the mortgage or charge was due to inadvertence or accidental or for sufficient cause and the position of creditors has not been prejudiced thereby and that it is just and equitable that relief should be granted. Section 172 of the Act (corresponding to section 121 of the Act of 1913) requires a company to inform the Registrar within twenty-one days of satisfaction of the mortgage or charge.

Section 183 of the Act (corresponding to section 131 of the Act of 1913) provides that the directors must place before the company in annual general meeting a balance sheet made upto a date not earlier than nine months before the date of the meeting unless time for holding the annual general meeting has been extended under section 81 of the Act in which case the period will be extended to that extent. A penalty of upto five thousand taka follows if the legal requirements are not obeyed.

The Dhaka High Court has, in several cases, dealt with the defaults by the directors in obeying the above requirements and have generally been lenient when the company or the directors have explained the delay and no harm has been caused to anybody. In *Dhakeswari Cotton Mills Ltd. vs Registrar of Joint Stock Companies*[1] the Dhaka High Court interpreted section 121 of the Act of 1913 which required satisfaction of a charge or mortgage to be registered with the Registrar. The Registrar required separate returns of part satisfaction of charges by a company from 1952 to 1955 and threatened to prosecute the officers of the company unless the directors did so. The company challenged this in a writ petition. Justice Ispahani, delivering the judgment of the writ court rejected the argument of Mr. M. Asir, the learned Advocate-General that although the word "part" is not used in section 121 of the Act of 1913, it should be read as so done for the convenience of the public. The Court looked into sections 138 and 139 of the new Indian Companies Act, 1956 which specifically used the word "partly" and held that since the legislature in the Act of 1913 did not use the word "partly" so part satisfaction of charges need not be registered. Since section 172, now in Bengali, uses the term "all" before the words "satisfaction of mortgage of charge" so it is now wide open whether the word 'all' qualifies the word "satisfaction" or "charges".

In *Syed Alim Mansur vs Registrar*[2] the High Court extended the time for registration of mortgage where the mortgage was not registered at the registrar's office within 21 days due to inadvertence on the part of the company and such intention was unintentional and without any malafide motive and no prejudice was caused to the members or the creditors of the company.

In *Messrs. Green and White Ltd vs Registrar*[3] the High Court held that the word 'created' in relation to a mortgage or charge in section 109 of the Companies Act 1913 (section 159 of the current Act) means 'registered' under the provisions of the Registration

1 (1957)VII PLR(Dac.)122.
2 42 (1990) DLR 43
3 15(1963)DLR492

Act as the mortgage mentioned in that section does not come into existence until the deed of mortgage is registered.

In *The Eastend Agencies & others vs Alhaj Mafizuddin and others*[1] the Court explained the provisions of the Companies Act 1913 (section 183 of the current Act) regarding preparation of balance sheet of a company and held that all that this section provided was that at the annual general meeting the accounts of the company were to be submitted and such accounts must be made upto a date not more than nine months previous to the date of the meeting, that is to say, whenever the meeting was held within the time allowed by section 76 of the Act of 1913 (section 81 of the current Act).

In *Anwar Jute Baling Ltd.*[2] it was held that delay in filing returns of the allotment of shares to the Registrar under section 104 of the Act of 1913 (section 151 of the current Act) within the time prescribed therein due to bonafide mistake and inadvertence without any ulterior motive may be condoned and time may be extended by the High Court for filing such returns. The case of *Elahee Baksh and Co. Ltd*[3] was referred to and the observations of Mr Justice Hamoodur Rahman were quoted.

The Court followed the same principles as enunciated in that case, namely, *that the court will exercise its jurisdiction to extend time to relieve companies of their negligence, carelessness or lack of caution provided the same were not committed with improper motive or fraudulent intention but were due to honest misapprehensions of fact or ignorance in fact of the law or of the correct state of affairs.*

But in each case, the party seeking to be so relieved must make the fullest and most candid disclosure.

In *Landale and Morgan (Pakistan) Ltd.*[4] the High Court held that filing of the vendor's agreement with the Registrar of Joint Stock Companies was not necessary where bonus accrued to the shareholders are not paid in cash but adjusted by issue of shares of the like amount to the shareholders. Also, return of allotment of shares was filed with the Registrar in due time and subsequent detection of mistake in the return in regard to the number of shares does not nullify the fact of filing the return in due time.

The Bangladesh courts will look whether the director or officer concerned was acting innocently and the delay in filing the statutory return was due to bonafide mistake or not. However, a practice has grown in the Dhaka High Court that at the time of condoning the delay the Court insists on a voluntary contribution by the company concerned to a charity. This salutory custom is not to be found in any other country and in at least one respect the Bangladesh Court has stolen a march over courts in other countries.

11.10.2 **Avoidance of Liability** – Section 102 of the Act of 1994 (section 86C of the Act of 1913 inserted in the company law by the Amendment Act of 1936) expressly states that save as provided in the section itself, any provision, whether contained in the articles of a company or in any contract with a company or otherwise for exempting any director, manager or officer of the company or any person employed by the company as auditor from or indemnifying him against any liability which by virtue of any rule of law would otherwise attach to him in respect of any negligence, default or breach of duty or breach of trust of which he may be guilty in relation to the company shall be void. Such officer may however be indemnified against any liability incurred by him in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or in which he is acquitted or in connection with any application under section 397 of the Act. This section prevents an abuse of power in framing the articles by the promoters and persons in control of the company.

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1 20(1968)DLR 1056.
2 21(1969) DLR 413
3 PLD(1958)Dac.378
4 22(1970)DLR 793

PROMOTERS AND PROSPECTUS

12.0 Sections 134-151 of the Company Act of 1994 deal with prospectus and the responsibilities and liabilities of those who issue prospectus.

12.1 Section 2(14) of the Companies Act of 1913 defined a prospectus as meaning any prospectus, notice, circular, advertisement or other invitation, offering to the public for subscription or purchase any shares or debentures of a company but did not include any trade advertisement which shows on the face of it that a formal prospectus has been prepared and filed. For some strange reason the new Act of 1994 omits this definition of a prospectus although section 135 provides for matters to be set out in the prospectus. It provides that every prospectus issued by or on behalf of a company, or by or on behalf of any person who is or has been engaged or interested in the formation of a company shall state the matters and set out the reports specified in Parts I and II of Schedule III of the Act. That section further provides that a condition requiring or binding an applicant for shares in or debentures of a company to waive compliance with any of the requirements of the section or purporting to effect him with notice of any contract, document or matter not specifically referred to in the prospectus shall be void. Sub section (3) of that section provides that no one shall issue any form of application for shares in or debentures of a company, unless the form is accompanied by a prospectus which complies with the requirements of the section.

This sub-section shall not apply if the form of application is issued either in connection with a bonafide invitation to a person to enter into an underwriting agreement with respect to the shares or debentures or that these securities are not offered to the public. A director or other person responsible for the prospectus shall not incur any liability by reason of any non-compliance with, or contravention of the section if he did not know of any relevant matter not disclosed or that the non-compliance or contravention arose from an honest mistake of fact on his part or that such non-compliance or contravention was in the opinion of the Court dealing with the case, immaterial and the delinquent ought reasonably to be excused. The section shall not apply to the issue to existing members or debenture holders of a company a prospectus or form of application relating to shares in or debentures of the company whether an applicant for securities will or will not have the right to renounce in favour of other persons or to the issue of a prospectus or form of application relating to shares or debentures which are, or are to be, in all respects uniform with shares or debentures previously issued and for the time being dealt in or quoted on a recognised stock exchange. The requirements to be put in a prospectus in the schedules referred to in the section broadly conform to the matters that were required to be set out in the previous Act of 1913 (section 93).

Section 136 states that a prospectus inviting persons to subscribe for shares in or debentures of the company shall not include a statement purported to be made by an expert unless the expert is a person who is not or has not been engaged or interested in the formation or promotion, or in the management of the company. The expert, in other words, must be impartial and not connected with the formation or management of the company. An expert must give his written consent to any of his statement being published in the prospectus.

Section 138 provides that before a prospectus is issued, it must be registered with the Registrar by filing a copy thereof with the Registrar. The copy shall have endorsed thereon or attached thereto any consent to the issue of the prospectus by an expert under section 137 and a copy of every contract required by clause 16 of Part I of Schedule III to the Act to be specified in the prospectus (terms of contracts to appoint managing director, manager or managing agent appointed two years before the prospectus or every other material contract entered two years before the prospectus). The copy should also contain any reasons for adjustment as mentioned in clause 32 of Part II of Schedule III.[1] However, Part II of Schedule III does not have clause 32. The correct part is Part III of Schedule III. Every prospectus sent to the Registrar's office shall on the face of it state that a copy has been delivered for registration and specify any document required by that section to be endorsed on or attached to the copy so delivered, or refer to the statements included in the prospectus which specify those documents. The Registrar shall not register a prospectus unless the requirements of sections 134 to 138 have been complied with and the prospectus is accompanied by the consent in writing of the person, if any named therein as the auditor, legal adviser or banker or broker of the company. No prospectus shall be issued more than ninety days after the date on which a copy thereof is delivered for registration. In case a prospectus is issued without registration with the Registrar, every person who is knowingly a party to the issue of the prospectus shall be punishable with fine which may extend to five thousand taka, a paltry punishment indeed for not registering the prospectus.

12.2 **Requirements of the SEC** – The Securities and Exchange Commission requires every prospectus to be approved by it before issue in case of public companies. Section 2A of the Securities and Exchange Ordinance 1969 provides that no company shall, except with the consent of the Commission make in Bangladesh any public offer of securities for sale. The SEC has not relaxed its control over issue of shares to the public and at present all prospectus should have the approval of the SEC. In the draft Guidelines on approval of prospectus or offer for sale the SEC has reiterated that no person shall issue in Bangladesh any prospectus or offer for sale without approval of the Commission; and such prospectus or offer for sale must include a statement that the approval of the Commission has been obtained to the issuance of such prospectus or offer for sale.

Section 140 of the Companies Act 1994 relates to allotment of shares and debentures to be dealt in on Stock Exchange. Where a prospectus states that an application has been or will be made, for permission for the shares or debentures offered thereby to be dealt in a stock exchange then such application should be made within a fixed period and if such permission has not been sought for or not granted then all monies received from applicants in pursuance of the prospectus should be returned; in default, the directors of the company shall be jointly and severally liable to repay that money with interest at the rate of five percent above the bank rate. A director can escape liability if he proves that the delay in payment of the money was not due to any misconduct or negligence on his part. The monies received on account of the said prospectus being issued should be kept in a separate account.

The Public Issue Rules 1998 radically change the approach of the SEC while approving prospectus. Emphasis is on a full and adequate disclosure. These Rules will enable the investors to make transparent investment decision. The SEC in the past evaluated the merit of an offer before it went for subscription, but now the investors themselves would assess the risk factors and make decisions accordingly. The market regulators, however, ensure full and fair disclosure in the prospectus in terms of the Rules.

12.3 Section 141 of the Companies Act provides that where a public company does not issue a prospectus on or with reference to its formation, or which has issued such a prospectus but

1 sub-section (2)(b)(ii)

has not proceeded to allot any of its shares or debentures offered to the public for subscription , shall not issue any of its shares or debentures unless there has been delivered to the Registrar for registration a statement in lieu of prospectus signed by every director or proposed director of the company and containing the informations in Parts I-III of Schedule IV. If the statement in lieu of prospectus includes any untrue statement the persons who authorised the delivery of the statement shall be punishable with fine or imprisonment or both. A statement will be untrue if it is misleading in the form and content and if there is an omission which is calculated to mislead, the omission shall render the statement in lieu of the prospectus untrue.

Section 142 provides that where a company allots or agrees to allot any shares in or debentures of the company with a view to all or any of those shares or debentures being offered for sale to the public, any document by which the offer for sale to the public is made shall for all purposes be deemed to be the prospectus issued by the company. An allotment or an agreement to allot shares or debentures will be deemed to be made with a view to offer them to the public if it is shown that an offer for sale to the public was made within six months after the allotment .

Section 145 provides for liability for statements in prospectus. Where a prospectus invites persons to subscribe for shares in or debentures of a company, every person who is a director of the company at the time of the issue of the prospectus, and every person who has authorised that his name be used as a director or or has agreed to become a director after an interval of time and every promoter of the company, and every person who has authorised the issue of the prospectus shall be liable to pay compensation to all persons who subscribe for any shares or debentures on the faith of the prospectus for all loss or damage they may have sustained by reason of any misleading or untrue statement therein, or by reference unless he can prove that he had reasonable ground to believe and in fact believed that the statement was true or represented the facts or that having consented to become a director he withdrew his consent before the issue of the prospectus or that the prospectus was issued without his consent and that on becoming aware of its issue he forthwith gave a reasonable public notice that it was issued without his knowledge or consent. In that case he will be entitled to be indemnified by the directors against all damages that he may suffer because his name has been inserted in the prospectus.

Section 145 provides that if a prospectus contains untrue statement and a subscriber suffers loss thereby then he can claim damages from every person who is a director of the company at the time of the issue of the prospectus or has authorised himself to be named and is named in the prospectus either as a director or has agreed to become a director either immediately or after an interval of time and every person who is a promoter of the company or authorised the issue of the prospectus. Such a person can escape liability if he proves that having consented to become a director of the company he withdrew his consent before the issue of the prospectus and that it was issued without his authority or consent or that the prospectus was issued without his knowledge or consent and that on becoming aware of its issue , he forthwith gave reasonable public notice that it was issued without his knowledge or consent or that after the issue of the prospectus and before allotment he, on becoming aware of any untrue statement , withdrew his consent to the prospectus and gave reasonable public notice of the withdrawal and reasons therefore. He can also escape liability if the untrue statement is purported to be made on the authority of an expert or of a public document and he had reasonable ground to believe and did believe that the statement was true. If a person's name is specified in the prospectus as a director of the company without his consent then he is entitled to be indemnified for any liability suffered by him from the directors or other persons who authorized the issue of the prospectus.

Sections 146 and 147 provide criminal liability and penalty for misstatements in the prospectus and for fraudulently inducing persons to invest money which may be imprisonment for a term upto two years for misstatements and imprisonments for a term which may extend to five years or fines upto fifteen thousand taka.

Sections 148-150 of the Act seek further to protect the interests of the company and the investors . Section 148 provides that no allotment shall be made of share capital of a company offered to the public for subscription unless the amount stated in the prospectus which in the opinion of the directors must be raised by the issue of share capital in order to provide the sums for certain expenses mentioned in the section has been subscribed for and at least five percent thereof has been subscribed in cash. The expenses to be provided for are the purchase price of any property to be defrayed out of the issue and preliminary expenses including commission to be paid for subscribing for shares. If the money for the minimum subscription has not been raised within a period of one hundred eighty days after the issue of the prospectus or within forty days from the closing date of subscription lists , whichever is earlier, all money received from applicants for shares or debentures shall be forthwith repaid to the subscribers without interest and if any money has not been paid within that date the directors of the company shall be jointly and severally liable to repay that money with interest at the rate of five percent above bank rate after expiry of the aforesaid period. This allows the company to enjoy other people's money which they are obliged to keep in a scheduled bank for at least that period. Sub-section (8) of that section provides that no allotment shall be made of any shares in, or debentures of the company in pursuance of a prospectus issued until the beginning of the eighth day after the first issue of the prospectus or until the eighth day after a public notice has been issued by a person under section 145 seeking to exclude, diminish or limit his responsibility.

An allotment made without a statement in lieu of prospectus as required by section 141 of the Act or in contravention of section 148 of the Act as to the minimum subscription being raised is voidable at the instance of the allottee within one month after the allotment or one month after the holding of the statutory meeting.

Section 150 of the Act provides restriction on commencement of business by providing that a company shall not commence any business or exercise any borrowing powers unless the minimum subscription mentioned in section 148 has been raised and every director has paid to the company on each of the shares contracted to be taken and there has been filed with the Registrar a duly verified declaration by the secretary or one of the directors that these conditions have been complied with, and in case where a prospectus has not been issued a statement in lieu of the prospectus has been filed with the Registrar. This section does not apply in the case of a private company.

Section 151 requires every company to file with the Registrar a return of allotment of shares to be made within sixty days showing the number and nominal amount of the shares, the names, addresses of the allottees and the amount if any, paid or due on the shares. If shares have been purchased otherwise than in cash then the vendor's agreement for such issue should also be filed with the Registrar. The Registrar may increase the time for filing if application is made to him before the expiry of the said sixty days. If default is made in complying with the requirements of this section the officers of the company will be liable to a penalty of thousand taka for each day that the default continues unless the High Court Division grants relief on the ground that the default was accidental or due to inadvertence or that it is just and equitable to grant relief.[1]

12.4 A company may have a choice of various methods whereby its securities can be offered to the public. In practice, it will normally engage the services of an issuing house (a merchant bank) and a stockbroker as sponsors of the issue and the method chosen will depend on their advice. There is not much competition in this country between the issuing houses and the road to such public issue is still murky. The SEC lays down stringent rules and the Dhaka Stock Exchange has its own requirements so that the company will have to comply with three sets of issue requirements – under the Companies Act, under the Securities Exchange Ordinance as required by the SEC and under the Listing Regulations of the Stock Exchange. Regulation 8 of the Listing Regulations of the Dhaka Stock Exchange provides that the

1 National Tea Company Ltd. vs Registrar of Joint Stock companies 5 BLC (HCD) 98

prospectus or the offer for sale must not only conform to the requirements of the Companies Act and the Securities Exchange Ordinance and the rules of the SEC but also state that the amount of public issue shall be in accordance with the 'consent order' of the Commission and the basis of the allotment shall be in accordance with the 'consent order' of the Commission. The prospectus or offer for sale with the proforma application form shall have to be published in one national daily newspaper at least seven days in advance but not more than thirty days before the due date of the opening of the subscription list. The company shall make available to the Exchange and to the bankers to the issue printed copies of prospectus and applications for shares shall be accepted only through bankers to the issue whose name shall have to be included in the prospectus or offer for sale. The directors or the associated companies , as the case may be, shall not participate in subscription of shares offered to the general public. The company shall take a decision within ten days of the closure of subscription list as to what applications have been accepted or are successful and shall refund the application money in case of unaccepted or unsuccessful applications within ten days of such decision. In case the application for listing is refused by the Exchange, for any or whatsoever reasons, the company shall forthwith pay without interest all money received from applicants in pursuance of the prospectus or the offer for sale, and any such money is not repaid within ten days after the company becomes liable to repay it , the directors of the company shall be jointly and severally liable to repay that money with interest at the rate of one percent for every month or part thereof from the expiration of the tenth day. It is not clear however how this last requirement will be enforced because if the application for listing is refused the Exchange will have little control over that company and the company then will not be bound to obey this directive of the Exchange.

In case of over subscription the company shall immediately submit to the Exchange copies of the ballot register of successful applications. The company shall despatch all allotment letters of shares in marketable lots within forty days of the closing of subscription list and all share certificates within 90 days of the date of issue of the allotment letter to all the successful applicants under intimation to the Exchange. A default in complying with these regulations attract a penalty of Tk 1000 for every day the default continues.

The company or the offerors shall, within six weeks of closing the subscription list, pay brokerage to the members of the Exchange at the minimum rate of one percent of the value of the shares actually sold through them. The company shall split allotment letters and letters of right into marketable lots within ten days of receipt of such applications. The company shall consolidate or split as may be required by a holder in writing, share certificates into marketable lots within forty five days of receipt of such application.

A company wishing to raise money by inviting offers from the public will therefore have to comply with the three fold requirements of the Companies Act, the SEC, and the Stock Exchange Listing Regulations.

12.5 **Promoter – Who is** – The initial reaction that most of us feel when we hear the word "Promoter" has been best described by Professor L.C.B. Gower in his book '*Modern Company Law*'.[1] He expresses the sentiments of most people thus :

> If in a psycho-analyst's consulting room, we were asked to say what picture formed in our minds at the mention of the expression "company promoter", most of us would probably confess that we envisaged a character of dubious repute and antecedents who infests the commercial demi-monde with a menagerie of bulls, bears, stags, and sharks as his familiars, and who, after rising to affluence by preying on the susceptibilities of a gullible public, finally retires from the scene in the blaze of a sensational suicide or Old Bailey trial. In other words, we would envisage someone whose profession it was to form bogus companies and foist them on the public to the latter's detriment and his own profit....

That famous author however hastens to add that even in their Edwardian heyday they formed only the minutest fraction of those whom the law classifies as promoters and a much

1 5th Ed. P. 296.

more typical, if less romantic ,example would be the village grocer who converts his business into a limited company. Not only a person who undertakes to form a company with reference to a given project is a promoter but a person who has taken a much less active and dominating role e.g., any individual or company that arranges for someone to become a director, places shares, or negotiates preliminary agreements.[1] The expression 'promoter' will cover also a person who subsequently helps to arrange the promotion of the capital of a company.[2] But those who act in a purely ministerial capacity, e.g., legal advisers and accountants, will not be treated as promoters merely because they undertake their normal professional duties, although they may have agreed to become directors.[3] Who is a promoter is therefore a question of fact and this expression has not been defined.

In the U.S.A., SEC Rule 405(a) defines a 'Promoter' as a person who acting alone or in conjunction with other persons, directly or indirectly takes the initiative in founding or organising a business enterprise.

The requirement that no company shall make an issue of shares to the public without the consent of the SEC and in that case the SEC will insist on the prospectus to be issued according to its guidelines and the requirements of the Companies Act 1994, means that no offer to the public can be made without a prospectus being issued as per the requirements of the law. The idea is that private offers need not be regulated because in a private situation, the offeree investor can make 'face to face' inquiries of the offeror and in any case, the cost of preparation of a prospectus cannot be justified. The concept of 'offer to the public' is not comprehensively defined. It is necessary to ascertain whether there is some special relationship between the offeror and members of the offeree group, or some rational connection between the common characteristics of the offerees and the offer made to them. If there is no special relationship or rational connection , the offer would be to a section of the public.[4] Because of the difficulties in identifying an 'offer to the public' the Australians, have, in section 82 of their Corporations Law given a definitional provision. In Australia the 'offer to the public' test has been substituted by some broad prohibitions on offers without a prospectus, coupled with express exemptions in cases where the offer is essentially private or the offeree can look after itself.

The point is that the offer is such as to be open to anyone who brings his money and applies in due form, whether the prospectus was addressed to him on behalf of the company or not.[5] An offer to shareholders of an existing company of shares in a new company in exchange for existing shares is not an offer to the public.[6]

12.6 **Duties and Liabilities of Promoters** – The Companies Act is largely silent on the duties of the promoters except for imposing liability for untrue statements in listing particulars or prospectuses to which they were parties . The courts, however, were examining the possibilities of abuse by a promoter and in the last quarter of the nineteenth century laid down that anyone who could properly be regarded as a promoter stood in a fiduciary position towards the company with all the duties of disclosure and accounting which that implied. He must not make any profit out of the promotion without disclosing it to the company.

In the first leading case on the subject, Erlanger vs New Sombrero Phosphate Co.[7] Lord Cairns said that the promoters :

> ...stand... undoubtedly in a fiduciary position...I do not say that the owner of property may not promote and form a joint stock company and then sell his property to it , but I do say that if he does he is bound to take care that he sells it to the company through the medium of a board of directors who can and do exercise an independent and intelligent judgment on the transaction....

1 Jubilee Cotton Mills vs Lewis [1924] A.C. 958 H.L.
2 Lagunas Nitrate Co. vs Lagunas Syndicate [1899] 2 Ch. 392,428.
3 Re Great Wheal Polgooth Co. [1883] 53 L.J. Ch. 42.
4 Corporate Affairs Commission (South Australia) vs Australian Control Credit Union [1985] 157 Commonwealth Law Reports 201, 208.
5 Nash vs Lynde [1929] A.C. 158 (H.L.).
6 Govt. Stock and Other Investment Co. Ltd. vs Christopher [1956] 26 Comp. Cas.210(Ch.D.).
7 (1878) 3 App. Cas.1218, 1236

Since the Salomon case[1] however it has not been doubted that a full disclosure to the members would be equally effective as all the members in that case acquiesced in the sale to the company of the assets of the proprietor at an obviously over priced valuation. But as Professor Gower points out[2] the promoter cannot escape liability by disclosing to a few cronies, who constitute the initial members, when it is the intention to float off the company to the public or to 'induce some other dupes to purchase the shares'. As Lord Halsbury said in Gluckstein vs Barnes[3] :

> ...It is too absurd to suggest that a disclosure to the parties to the transaction is a disclosure to the company...They were there...to cheat the shareholders and this, forsooth, is to be treated as a disclosure to the company, when they were really there to hoodwink the shareholders....

The disclosure must be to either an independent board of directors or the potential members and a partial and incomplete disclosure will not do; the disclosure must be explicit.[4]

If the promoter acquires property after the commencement of the promotion he is presumed to do so as a trustee for the company so that he must hand it over to the company at the price he gave for it unless he discloses not merely the profit which he proposes to make but also informs the company of its right to call for the property at its cost price.[5] In such a case nothing short of unanimous consent of all the shareholders of the company should entitle the promoters to retain his gains, for not even a resolution of the general meeting should authorise an expropriation of the company's property.[6] Professor Gower cites the decision of *Omnium Electric Palaces vs Baines*[7] and concludes that all seems to turn on the intentions of the promoter at the time of the purchase; on whether he intended to buy for himself for re sale to the company or to buy initially for the company. In the former case his only duty is to disclose; in the latter he cannot subsequently change his mind and seek to act as vendor rather than a trustee.[8] The duty of a promoter is not only to refrain from making wilfully false statements but actively to disclose the whole truth.

A promoter cannot effectively contract out of his duties by inserting a clause in the articles whereby the company and the subscribers agree to waive their rights.[9]

12.7 Bangladesh is in a nascent stage so far as the law relating to investor protection is concerned. The stock exchange regulations and the SEC requirements are updated every now and then and although the stock exchange is performing much better than it did a few years earlier the regulations should be strictly observed. Once the public confidence falls it will be difficult to gain it back. The law does not define a prospectus and there is no prohibition against 'door to door' sale of shares. The enforcement of the law being lax here once the investor is duped and his money taken off him it will be difficult for him to avail of the remedies . The SEC and the Stock Exchange regulations should aim at preventing fund raising frauds rather than trying to stop the crimes later on.

12.8 **Liability of Promoter** – The statutory liability of a promoter may arise :

a) on an untrue or misleading statements in a prospectus to any subscriber for shares or debentures who has suffered loss or damage (section 145);

b) on an irregular allotment, to an allottee if loss or damage is sustained (section 149); and

c) in the case of failure to repay money paid with an application for shares, if the minimum subscription has not been subscribed. (section 148(7)).

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1 [1897]A.C.22 ,H.L.
2 Modern Company Law, 5th Ed. p. 298-99.
3 [1900] A.C. 240,247
4 Gluckstein vs Barnes, ibid.
5 Professor Gower: Modern Company Law 5th Ed p.299.
6 Cook vs Deeks [1916] 1 A.C. 554,P.C.
7 [1914] 1 Ch. 332.
8 at p.300.
9 see Gluckstein and Omnium case above.

12.9 The basis of a director's liability for a defective prospectus is a 'misleading or untrue statement' in the prospectus. There is no statutory definition of the term 'misleading or untrue statement' in the Act of 1994. Under the general law of tort, the directors and others responsible for a prospectus containing false and misleading statements, were liable only on an action for deceit, if a director was proved to be guilty of actual fraud.[1] A director was not liable in damages for a false statement in a prospectus, if he honestly believed it to be true, though there is no reasonable ground for the belief. Gross negligence is not deceit and an innocent misrepresentation is not deceit . The statement must be made with knowledge that it is false or in reckless disregard as to whether it is true or false.[2]

"Recklessness" exists where there are circumstances from which a jury can infer that the defendants in doing what they did, did not care whether what they said was true or false and had no honest belief in its truth.[3] Further, the misstatement must be as to a material fact. Whether a mis-statement is material or not depends on the facts of each case. The whole prospectus has to be considered in deciding whether a particular statement is likely to influence the mind of an intending applicant for shares. Lastly, the plaintiff must have been induced to enter into the contract as a result of such mis-statement and must have suffered damage thereby.

In *S. Chatterjee vs Dr. K.L.Bhava*,[4] a director was sued for damages in tort for making fraudulent statements in the prospectus . The plaintiff's claim appeared to have been founded solely in tort . The High Court discussed in detail the tort of deceit , as understood in the sub-continent, and the measure of damages that one was entitled to in such a case. Thus, where the plaintiffs were induced to purchase worthless shares of a company by false representation, in an action for damages based on deceit, fraud and injury must concur. There must be proof of fraud and proof of the fact that fraud has resulted in damages, for the tort of deceit is not complete till the false report is acted upon. But once it is shown that someone was induced to buy shares which, but for the misrepresentation he would not have purchased, the tort of deceit is complete and various remedies are then available to him. Rescission, restitution, damages or enforcement of a constructive trust are some of the remedies for fraudulent misrepresentation. An agent of the company misrepresented facts about the financial position of a company and the position of its shares in the market. Induced by the fraudulent misrepresentation, the plaintiff bought shares in the company. The managing director and a relation of his benefited by this transaction. It was not unreasonable to infer that the managing director was primarily responsible for the agent's representations, in order that unyielding and unprofitable shares held by him and his relative might be disposed of. On the basis that the principal is liable for his agent's fraud, the managing director was held liable for damages suffered by the plaintiff as a joint tort-feasor with the agent.

A director is not liable under the general law of tort for damages suffered by the plaintiff, if he had an honest belief in the statement he made. The Privy Council has observed in Baron Uno Carl vs Rolf de Mare and others[5] that the question is not whether the director in any given case honestly believed the representation to be true in the sense assigned to it by the Court on an objective consideration of its truth or falsity, but whether he honestly believed the representation to be true in the sense in which he understood it, albeit erroneously, when it was made . In this case, representation was made in a prospectus that about "one third of the capital has already been subscribed in Denmark". The word "subscribed" did not mean that one-third of the capital had already been subscribed in cash, and consistent with the representation, formation expenses of the company and the acquisition of patent rights could be met by allotting fully-paid shares.[6] In the circumstances the view of the trial judge,

1 Derry vs Peek [1889] 14 A.C. 337.
2 Arkwright vs Newbold [1881] 17 Ch.D. 301.
3 Regina vs Russel (1955) 1 W.L.R. 77.
4 AIR 1960 M.P. 323,
5 [1959] 3 W.L.R. 108.
6 Ibid at page 114.

formed after seeing and hearing the director give evidence that he did honestly believe the representation to be true ought not to be lightly dismissed. The Judicial Committee pointed out, however, that this general proposition is no doubt subject to limitations.[1] The meaning placed by the defendant on the representation made may be so far removed from the sense in which it would be understood by any reasonable person as to make it impossible to hold that the defendant honestly understood the representation to bear the meaning claimed by him and honestly believe it in that sense to be true. Otherwise, and in absence of fraud a director is not liable to compensate a shareholder whose only other remedy is against the company - a suit for rescinding the contract of allotment of shares, and claim a refund of the money paid by him.[2]

12.10 This , however, is the position of a director in the general law of tort. Under section 145 of the Act of 1994, corresponding to section 100 of the Act of 1913, to enforce a claim for compensation against a director, it is not necessary to prove fraud or deceit by him. This section introduced in the sub-continent the remedy provided in England against directors by the Director's Liability Act of 1890. The onus of proof is shifted to the director to prove that he is innocent. Once the plaintiff has proved that he has sustained damage by reason of an untrue statement in a prospectus, his action will succeed, unless the defendant disproves responsibility for the prospectus in one of the ways mentioned therein or unless he proves that he had reasonable ground to believe and did, upto the time of allotment, believe that the statement was true. Like the corresponding section in the English Companies Act, 1948 and the amended Indian Companies Act of 1956, and section 100 of the Act of 1913 section 145 of the Act of 1994 only provides relief to persons who "subscribe for" shares or debentures as opposed to those who "purchase" them on the faith of the prospectus and, therefore, although the remedy is not expressly limited to mis-statements in a prospectus issued by or on behalf of a company, it seems clear that it only applies to them. Hence it will not afford any relief to those who purchase from existing shareholders or underwriters unless the company has made the allotment with that in view. In the old but famous case of *Peek vs Gurney*[3] it was held that in order to succeed, the plaintiff must show that he was one of a class of persons included in the prospectus.

Although the section only applies where the company is responsible for the prospectus, no liability is cast on the company itself. Those liable to pay compensation are,

1) every person who is a director of the company at the time of the issue of the prospectus,
2) every person who has authorised the insertion of his name and is named in the prospectus as a director or as having agreed to become a director either immediately or after an interval of time,
3) every promoter of the company and
4) every person who has authorised the issue of the prospectus. *(Sub-section(1)).*

Rescission remains the remedy against the company.[4] In *Venkataramayya vs Indian Industrial Bank Ltd*[5] it was held that where before allotment of shares in a limited company two of the directors mentioned in a prospectus retired, and the fact of retirement was not communicated to the allottee of shares, the allottee of the shares would be entitled to rescind the contract of allotment of shares and claim a refund of the monies paid by him. To avail of this remedy all that the plaintiff need show is that there has been a material change in the prospectus since he made his offer and he is then entitled to decide that with this material change the prospectus of the company is not sufficiently attractive to warrant him in subscribing his money. Misrepresentation or fraud would seem to be of importance only regarding the remedies he may have against the guilty directors.[5]

1 Venkataramayya vs Indian Industrial Bank Ltd.AIR 1930 Mad. 325.
2 (1873) L.R. 6 HL 377.
3 Re Kent County Gas Light and Coke Co. (1913) 1 Ch 92.
4 AIR 1930 Mad 325.
5 T.S.R.Iyer vs S.I.Rubber Works AIR 1942 Mad 656.

A shareholder must exercise the option of rescission within a reasonable time.[1]

The remedy of claiming damages against the directors, promoters etc. is in addition to the remedy of rescission of contract. It is interesting to note that damages cannot be recovered from the company unless the allotment of shares is also rescinded.[2] In this case the company was unlimited and was described throughout as partnership. But the rule was applied to a limited company in *Re Addlestone Linoleum Co.*[3]

This section, however, exonerates a director if he can prove that,

a) with respect to every misleading or untrue statement not purporting to be made on the authority of an expert or of a public official document or statement, that he had reasonable ground to believe and did upto the time of the allotment of the shares or debentures, as the case may be, believe that the statement fairly represented the facts or was true;

b) with regard to every misleading or untrue statement purporting to be a statement by or contained in what purports to be a copy of or extract from a report or valuation of an expert, that it fairly represented the statement, or was a correct and fair copy of or extract from the report or valuation, provided that the director, promoter or person who authorised the issue of the prospectus shall be liable to pay compensation as aforesaid if it is proved that he had no reasonable ground to believe that the person making the statement, report or valuation was competent to make it and had given the consent to the issue of the prospectus and had not withdrawn it to the knowledge of the defendant; and

c) with respect to every misleading or untrue statement purporting to be a statement made by an official person or contained in what purports to be a copy of or extract from a public official document that it was a correct and fair representation of the statement or copy of or extract from the document; or if it is proved –

   i) that having consented to become a director of the company he withdrew his consent before the issue of the prospectus, and that it was issued without his authority or consent; or

   ii) that the prospectus was issued without his knowledge or consent, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent; or

   iii) that, after the issue of the prospectus and before allotment thereunder, he, on becoming aware of any misleading or untrue statement therein, withdrew his consent thereto, and gave reasonable public notice of the withdrawal, and of the reason therefore.

This section is a great deterrent to negligence by directors and promoters who must not only show that they had an honest belief in the truth of the statement in the prospectus but also that there existed reasonable grounds for such belief. Thus, the uncorroborated statements of a vendor or promoter of a company afford no reasonable ground for believing them to be true and misleading statements made in a prospectus on the faith of such statements will not be protected as statements made on the reports of an expert.[4] For honest errors of judgment directors are not liable, provided they acted with reasonable care. Where a company was formed to take over and work a rubber plantation from a syndicate and the directors issued a prospectus containing untrue statements as regards the area and number of trees on the estate, but the statements were made on information from a member of a firm, from which the syndicate had purchased the estate, it was held that the directors were not guilty of gross negligence in believing the information and were, therefore, not liable as on a misfeasance.[5]

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1 Shrimoni Sugar Mills Ltd. vs Devi Prasad [1950] 20 Comp. Cas. 296(All).
2 Hoyldsworth vs City of Glasgow Bank (1880) 5 App. Cas.317, H.L.Sc.
3 [1887] 37 Ch. D. 191, C.A.
4 Adams vs Thrifts [1915] 1 Ch. 557; (1915) 2 Ch 21.
5 Re Brazilian Rubber Plantations [1911] 1 Ch. 425.

The wrong complained of is independent of contract. In *Rajah of Nilambar vs A.W.Dwarkadoss and others*[1] the plaintiff was induced to buy shares on the basis of a misrepresentation in the prospectus. Later on, in a suit for damages under section 100 of the Companies Act of 1913, one defence pleaded by the directors was that the action was time-barred, as it was filed more than two years after the cause of action arose (time limit for bringing an action for compensation for malfeasance, misfeasance or non-feasance independent of contract under Article 36 in the first schedule of the Limitation Act) but before three years had elapsed (Article 115 gives three years time for compensation under the law of contract). Kunhi Raman J. agreed with the trial judge that the cause of action was founded in tort and it was a civil wrong committed by the defendants. The directors who had formed the company were making representations with the object of inviting members of the public to apply for shares in the company. The plaintiff was misled by the misrepresentations contained in the prospectus. The contract when the shares were allotted was between the plaintiff and the defendant company and not with the directors of the company. The wrong complained of by the company happened before the formation of the contract. Article 36 of the Schedule to the Limitation Act would apply.

The next question that arises is whether a director is saved from liability if the document inviting persons to subscribe for shares in the company , although it purports to be prospectus is not, in the strict sense of the term, what it purports to be, because it does not comply with the requirements of the Companies Act. It has been held in *S.S. Chettiar vs A.A.Ranga Rama Naicker*[2] that the definition of a prospectus in the Act of 1913 includes a document inducing a person to buy shares, so that its authors are liable under section 100 of the Act of 1913 even though the provisions of the Act requiring a prospectus to be filed with the Registrar or giving all the particulars required to be given under the Act are not complied with. Directors should not be allowed to take advantage of their own wrongs or laches either by not filing the prospectus or by omitting particulars which they have a statutory duty to include in a prospectus.

The compensation recoverable from the directors under section 145 of the Act is not in the nature of a statutory penalty; like damages in tort it must be estimated and awarded with reference to the loss sustained. This point has long been established in England under the Director's Liability Act,1890, which made the directors liable to pay compensation for damages resulting from mis-statements even in the absence of a fraud. Section 3 of the Director's Liability Act, 1890 corresponds roughly to section 100 of the Act of 1913 and section 145 of the Act of 1994. Under the Act a liability is imposed on the directors to pay compensation which does not, in the least, resemble a " penalty, damages or sum of money" without any reference to the loss sustained.[3]

As to the principle on which damages are assessed in these cases, Collins M.R. has said[4] that it is not an action for breach of contract and therefore, no damage is recoverable in respect of prospective gains which the person contracting was entitled to expect.[5]

It is an action in tort for the wrong of being induced to part with his money and, therefore, prima facie, the damage recoverable cannot exceed the loss sustained, which is measured by the money which was in his pocket and is now in the possession of the company.

It was held in *Broome vs Speak*[6] that in determining the fair value regard is also to be had of subsequent events. Although the value of the shares is not to be ascertained at the period subsequent to his purchase taking into account, for the benefit of the plaintiff, subsequent events which depreciated their value, yet those events, if they shew that the company was originally, with the capital which it had got, a company which was worthless,

1 AIR 1944 Mad 431
2 AIR 1934 Mad. 641.
3 Thompson vs Clanmorris [1900] 1 Ch.718,726.
4 McConnell vs Wright [1903] 1 Ch.546.
5 Peek vs Derry [1887] 37 Ch.D. 541.
6 [1903] 1 Ch. 586

must be regarded as evidence of what was the value of the shares immediately after they were allotted to the plaintiff. Buckley J. considered the law laid down by Cotton L.J. in *Peek vs Derry*[1] and said that the question should not be answered by finding what was the market value of the shares at the date of the allotment for it might be that the market value was raised by the very misrepresentation of which the plaintiff was complaining.

Lastly, the "untrue statement" complained of under the section must be a statement which is in fact untrue, not a statement which the director believes to be untrue, and it is immaterial that the statement was not fraudulent.[2] The statement must be untrue as understood by those who read it, and not in the sense intended by those who made it.[3] The meaning understood by those who issue it becomes all-important when such persons are charged with fraud... the object of the Director's Liability Act (corresponding to section 145 of the Act of 1994) was to remove the defect in law brought to light by the decision in *Derry vs Peek*[4] and to impose upon those who issue prospectus the duty to take reasonable care not to make untrue statements.[5]

12.11 Liability of a director to compensate for losses sustained by shareholders may also arise under section 148 and 149 of the Act of 1994. These sections correspond to sections 101 and 102 of the act of 1913. Where a new company invites the public to subscribe to its shares, the statutory provisions relating to the minimum subscription have to be complied with, and no shares must be allotted, unless the minimum subscription has been paid by applicants for shares and the sums payable by them for the shares constituting the minimum subscription have been paid.[6]

If the minimum subscription has not been received within one hundred and eighty days after the first issue of the prospectus, or within forty days from the closing date of subscription lists as specified in the prospectus, whichever is earlier, all money received from applicants must be forthwith repaid to them without interest, and, if any such money is not so repaid within that period the directors are jointly and severally liable to repay the money with interest at the rate of five per cent above bank rate.

Section 149 provides that an allotment made by the company in contravention of the provisions of section 141 or 148 shall be voidable at the instance of the applicant within one month after the holding of the statutory meeting. A director of a company who knowingly contravenes or permits or authorises the contravention of those sections are liable to compensate the company and the allottee for any loss, or damage suffered. "Knowingly contravening" in this provision means contravening with knowledge of the facts upon which the contravention depends.[7] It is immaterial whether the directors were aware that the facts of which they had knowledge constituted a contravention of the section or were unlawful. Knowledge will not be imputed to a director who was not present at the meeting at which the resolution to make an irregular allotment was passed, so as to render him liable under the section if he is present at a subsequent meeting when the minutes are confirmed.[8]

The Lahore High Court has held in *Mutual Bank of India Ltd.vs Sohan Singh*[9] that the minimum amount payable on application of each share (at least five per cent) applies to all allotments of shares and any allotment which is made without payment of at least five per cent of the nominal value of the shares by the applicants is therefore invalid. But the Calcutta High Court has held that there is nothing in section 101 of the Act of 1913(corresponding to section 148 of the Act of 1994) which forbids the directors of a company to allot shares to applicants who neglect to pay the application money in terms of the prospectus, once the first

1 Supra
2 Shepheard vs Broome [1904] A.C. 342.
3 Greenwood vs Leather Shod Wheel Co. [1900] 1 Ch. 421.
4 [1889] 14 App. Cas.337.
5 Lindley M.R. in Greenwood's Case [1900] above at page 434.
6 Section 148.
7 Burton vs Bevan (1908) 2 Ch. 240.
8 Palmer's Company Law 20th Ed. p.191.
9 AIR 1936 Lah.790

allotment has been regularly made, although it may be that a provision in the prospectus empowering them to do this would be an infringement of the Act.[1]

Section 149 of the Act of 1994 corresponding to section 102 of the Act of 1913 makes a director liable to pay compensation for any loss suffered by a third party by reason of contravention of any of the provisions of the preceding sections. Section 150 forbids a company from commencing any business or exercise any borrowing powers unless shares held subject to the payment of the whole amount thereof in cash have been allotted to an amount not less in the whole than the minimum subscription. In *Indian States Bank Ltd. vs Sardar Singh*,[2] the directors had allotted shares without having received the minimum subscription or the money due on application for shares. They had obtained the certificate for commencement of business and commenced business without paying the application and allotment money due on their shares, in violation of section 101(1) of the Act of 1913 (corresponding to section 148(1) of the Act of 1994). The directors were held liable to pay compensation to the company under section 102(2) of the Act of 1913 (i.e.,section 149(2) of the Act of 1994). They were also liable under section 235 of the Act of 1913 which gives the Court power to assess damages against delinquent directors on a winding up of the company. (section 331 of the Act of 1994). As to the nature and quantum of a director's liability under sections 101 and 102(2) of the Act of 1913 (corresponding to sections 148 and 149(2) of the Act of 1994), Young J. said[3] :

> ...Under sections 101 and 102(2) the liability of those defendants who were directors appears to be the same. They must compensate the company and the shareholders for 'any loss, damage or costs which company or the allottees may have sustained or incurred thereby'. The loss or damage directly flowing from the breach of duty under section 101 include the loss and damages occasioned by the carrying on of the business which never could have been commenced but for the improper allotment. The loss and damage would therefore appear to be the total losses of the company which include amounts due to creditors and shareholders....

An irregular allotment of shares made by the directors in excess of their powers may be subsequently ratified by the shareholders at a general meeting.[4]

Pre-incorporation Contracts – The Appellate Division has observed that there is no bar in law for a company which is going to be registered to act in its name or on its behalf prior to the registration and that upon registration act or acts so done prior to the registration if ratified by the company become the act of the company.[5]

12.12 Section 75 (1) of the Companies Act of 1994 provides that in a limited company the liability of the directors or of any director may, if so provided by the memorandum, be unlimited. Of course, before a person becomes a director of such a company, his attention must be drawn to this fact, and if any default is made in this regard, he has a right of indemnity against those responsible for the default.

12.13 **Liability to a Third Party** – A director may be liable in damages to a third party for breach of a particular statutory provision although that provision does not explicitly say that he is so liable. Thus a violation of section 93 of the Act of 1913 (particulars to be included in the prospectus) corresponding to section 135 of the Act of 1994, may give right to a personal right of action in favour of a subscriber.

A person who is a complete stranger to the company cannot file a suit to restrain the company from issuing a prospectus on the ground that it contains misleading statements. The remedy is available to a person who has suffered loss or damage on the faith of the prospectus.[6]

12.14 **Return of Allotments** – Section 151 requires a company to file return of allotment of shares to the Registrar. Different considerations apply if an allotment is made in cash than when an allotment is made otherwise than cash. It was held in Landale and Morgan Ltd.[7] that

1 In re Happy India Insurance Co. Ltd I.L.R.(1939) 2 Cal 512.
2 AIR 1934 All. 854
3 ibid at p.864.
4 Bamford vs Bamford [1968] 2 All E.R.655 affirmed in (1969) 1 All E.R. 969.
5 Capital Tower Ltd. vs Mirpur Mazar Co-Operative Market Society Limited and others 9 MLR (AD) 141
6 Kisan Mehta vs Universal Luggage Mfg. Co.Ltd.Bombay [1988] Comp. Cas. 398.
7 22 D.L.R. 793.

filing of the vendor's agreement to the Registrar's office is not necessary where bonus accrued to the shareholders are not paid in cash but adjusted by issue of shares. Relying on certain old English decisions Justice Nurul Islam said that this was a simple question of adjustment of accounts and "this payment is certainly in cash." This case also held that where return of allotment was filed in due time subsequent detection of mistake in the Return in regard to the number of shares does not nullify the fact of filing the return in due time. The court will not interfere merely on the ground that the consideration is inadequate unless the contract is fraudulent or shows on the face of it that the consideration given to the company is illusory. In such a case, the shareholder will be liable to pay for the shares in full.[1] An agreement to allot shares is not a transfer of property, as the company is not the owner of the shares and does not attract stamp duty as a conveyance.[2]

The expression "allotment" has not been defined in the Act. What is termed allotment is generally more or less the acceptance by the company of the offer to take shares. To take the common sense, the offer is to take a certain number of shares or such a less number of shares as may be allotted. That offer is accepted by the allotment either of the total number mentioned in the offer or a less number, to be taken by the person who made the offer. This constitutes a binding contract to take that number according to the offer and acceptance.[3] The Indian Supreme Court held that 'allotment' means the appropriation out of the previously unappropriated share capital of a company, of a certain number of shares to a person. Till such allotment the shares do not exist as such. It is on allotment in this sense that the shares come into existence.[4] In *Golkonda Industries Ltd. vs Registrar of Companies*[5] a Full Bench of the Delhi High Court has held that where a return of allotment is made and it is otherwise in order, the Registrar cannot inquire into the legal validity of the matters contained in the return.

In *Shree Gopal Paper Mills Ltd. vs C.I.T., Central Calcutta*[6] the Supreme Court held that vesting of bonus shares takes place from the date of the company's resolution and not from the date of actual allotment.

12.15 **Commissions and Discounts** – Sections 152-156 deal with payments of commissions and discounts while allotting shares.

A company can pay commissions to any person in consideration of his subscribing or agreeing to subscribe, whether absolutely or conditionally for any shares in the company if such payment is authorised by the articles and the payment is shown in the prospectus or statement in lieu of prospectus.[7] A company not being a financial institution cannot take loan and give interest [8]

It shall be lawful for a company to issue shares at a discount if the issue is authorised by the company in general meeting and so sanctioned by the Court. The discount must not exceed ten percent and not less than one year must have elapsed since the date on which the company was entitled to commence business. The shares so issued at a discount must be issued within six months after the date on which the issue is sanctioned by the Court or within such extended time as the Court may allow. Every prospectus relating to the issue of shares and every balance sheet issued by the company subsequently to the issue of shares must contain particulars of the discount.[9]

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1 Aloe Estate vs R.B.Seth Hiralal Kalyanmal (1970) Comp. Cas.1116.Hongkong and China Gas co. Ltd vs Glen [1914] 1 Ch. 527.

2 Secy. Board of Revenue, Madras vs Madura Mills Co. Ltd. ILR (1937) Mad. 559;Raj Sachdeve vs Board of Revenue AIR 1959 All.595.

3 In re Florence Land and Public Works Co. [1885] 29 Ch.D. 421 at 426;Sri Gopal Jalan and Co. vs Calcutta Stock Exchange Association [1963] 33 Comp. Cas. 862(SC).

4 ibid.

5 [1968] 38 Comp.Cas.165.

6 AIR 1970 SC 1750.

7 Section 152.

8 AKM Abdul Latif vs Banani Metal Limited and others 52 DLR 62

9 Section 153.

Section 154 deals with issue of redeemable preference shares. A company limited by shares, if so authorised by the articles , may issue preference shares which are at the option of the company liable to be redeemed. No such shares shall be redeemed except out of the profits of the company which would otherwise be available for dividend or out of the proceeds of the fresh issue of shares made for the purposes of the redemption or out of the sale proceeds of any property of the company. No such shares shall be redeemed unless they are fully paid. Where any such shares are redeemed otherwise than out of the proceeds of a fresh issue, there shall out of profits which would otherwise have been available for dividend be transferred to a reserve fund called "the capital redemption reserve fund" a sum equal to the amount applied in redeeming the shares and the provisions relating to the reduction of share capital shall apply as if the capital redemption reserve fund were paid up share capital of the company. Where any such shares are redeemed out of the proceeds of a fresh issue, the premium if any, payable on redemption, must have been provided for out of the profits of the company before the shares are redeemed. There shall be included in every balance sheet of the company which has issued redeemable preference shares a statement specifying what part of the issued capital of the company consists of such shares and the date on or before which such shares are to be redeemed. The redemption will have to be effected on such terms and in such manner as may be provided by its articles. The company may issue new shares in place of the redeemed shares.

12.16 **Further Issue of Capital** – Section 155 (1) provides that where the directors decide to increase the subscribed capital of the company by issue of further shares within the limit of the authorised capital then such further shares shall be offered to the members in proportion, as nearly as circumstances admit, to the capital paid up on the existing shares held by such member, irrespective of class, at the date of the offer; such offer shall be made by notice specifying the number of shares offered and specifying the time limit, not being less than fifteen days from the date of the offer, within which the offer, if not accepted will be deemed to be declined. If the offer is so declined, the directors may dispose of the same in such manner as they may think most beneficial to the company. Sub-section (2) provides that notwithstanding anything contained in sub-section (1) shares may be offered to any person whether or not those persons are included in the sub-section.

This sub-section (2) in fact negates the entire effect of sub-section (1). This particular provision was absent in the corresponding section 105C of the Act of 1913. Section 81 of the Indian Act of 1956 provides that the further shares may be offered to any other person if so inter alia be authorised by a special resolution of the company. The draftsmen of the new Act of 1994 omitted to insert this very relevant consideration and the effect of this law is now doubtful.

In normal cases a detailed notice may not be necessary.[1] It was held in In *re Simco Securities Trust Ltd.*[2] that when a shareholder renounces any of the rights shares offered to him in favour of a third person the Board cannot refuse to allot the shares to a third person unless the articles provide for the same.Although under sub-section (2) further shares may be offered to any person yet such discretion cannot be arbitrary.[3]

12.17 **Payment of Interest Out of Capital** – Section 157 of the Act permits interest to be paid out of capital if the share money was raised to defray the expenses of construction work or if the project cannot be made profitable for a long time. Provided that –

(a) no such payment shall be made unless the same is authorised by the articles or by a special resolution;

(b) this has sanction of the government;

(c) the sanction may be given after enquiry and may mention the period of enquiry and the rate of interest;

1 Jadabpore Tea Co. Ltd. vs Bengal Dooars National Tea Co. Ltd (1984) 55 Comp. Cas. 160.

2 (1971) 1 WLR 1455 Ch.D.

3 Dr. Manjurul Islam vs Al Rajhi Hospital 1 Law Guardian (HCD) 46

(d) the payment of interest shall not operate as reduction of capital; and

(e) the accounts of the company shall show the share capital on which, and the rate, at which interest has been paid out of capital during the period to which the accounts relate.

12.18 **Limitation of Time for Issue of Certificates** – Section 158 requires every company to make ready for delivery the certificates for all shares and debentures etc. within 90 days of the allotment. There is a fine of five hundred taka per day the default continues.

It is not necessary that the certificates should be ready for delivery to the complainant.[1] For this and other cases see para 9.1.1 above.

1 Muhammadullah vs Mokbul Ahmed (1992) 44 DLR(H.C.) 107.

SECURITIES AND CHARGES

13.1 Sections 159 to 176 deal with informations relating to charges and sections 178-180 deal with debentures and floating charges.

13.1.1 **Charge** – The Companies Act 1994 does not define a charge. The English and the Indian Acts do so and mention that a "charge" includes a mortgage.[1] Section 9 of the Australian Corporations Law defines a "charge" as 'a charge created in any way and includes a mortgage and an agreement to give or execute a charge or mortgage, whether on demand or otherwise.'

Ford and Austin's Principles of Corporations Law,[2] point out the difference between a mortgage and a charge. A mortgage is a conveyance of land under the general law or an assignment of chattels by the mortgagor to the mortgagee as security for discharge of some obligation, such as payment of interest and principal of a loan. The conveyance is subject to proviso for reconveyance if the obligation is performed. The security may be redeemed on discharge of the obligation. In a legal mortgage – one given by a legal owner – the mortgagor's equitable interest in the property, the equity of redemption, will end if the mortgagee obtains foreclosure under court order or statute. If the mortgage is equitable and the mortgagor fails to perform, a court will order that the legal title be transferred to the mortgagee.

By contrast with both a legal and equitable mortgage, an equitable charge does not contemplate any change of ownership from the chargor to the chargee. An equitable charge imposes burden on the property. That does not take away the chargor's interest and the chargor continues to own the property, subject to the right of the chargee to be paid out of the proceeds of the sale if the obligation secured is not performed.

Browne-Wilkinson V.-C., accepted the following as a description of a security interest :

> Security is created where a person ('the creditor') to whom an obligation is owed by another ('the debtor') by statute or contract, in addition to the personal promise of the debtor to discharge the obligation, obtains rights exercisable against some property in which the debtor has an interest in order to enforce the discharge of the debtor's obligation to the creditor. [3]

13.1.2 **Fixed and Floating Charges** – In respect of companies as creators of charges it is necessary to distinguish between a fixed security (whether a mortgage or charge) and a floating security.

Following is a short description of the difference between the two types of charge as given in *Ford and Austin's Principles of Corporations Law*.[4]

> A fixed security is intended by the parties to attach to a specific item of property described in the instrument creating the security (the instrument of charge) in such a way that the chargor

1 Section 124 of the Indian Act and section 396 of the English Act of 1985.
2 7th Ed. p.685-6.
3 Bristol Airport Plc. vs Powdrill [1990] Ch.744.
4 7th.Ed.para 19.190

cannot dispose of the item of property free of the charge without the chargee's consent. A fixed security is sometimes called a specific security and is often referred to as a fixed charge.

In *Re Yorkshire Woolcombers Association Ltd*[1] Romer L.J. said that if a charge had the three characteristics set out below it was a floating charge :

1) it is a charge on a class of assets of a company, present and future;
2) which class is, in the ordinary course of the company's business, changing from time to time;
3) it is contemplated by the charge that , until the holders of the charge take steps to enforce it, the company may carry on business in the ordinary way as far as concerns the class of assets charged.

A floating security is intended by the parties to cover a class of property but not to attach to specific items within the class until some future event occurs. Until the event occurs the chargor is free to dispose of items within the class in the ordinary course of business so that the taker from the chargor acquires the property free of the charge. That enables a company to borrow on the security of a stream of assets flowing into and out of its ownership. A floating security is commonly called a floating charge.

13.1.3 **Floating Charge** – The foundation case of a floating charge is *Holroyd vs Marshall*[2] ; this case held that the creation of a mortgage in the nature of a floating charge on machineries acquired after the mortgage created priority of claim over an execution creditor. In *Re Panama, New Zealand & Australian Royal Mail Co.*[3] a company charged the 'undertaking and all sums arising therefrom' with repayment of a principal amount at a specified date and interest in the meantime. Before the date for repayment the company went into liquidation. The court held that the chargees had a charge on all the properties of the company, present and future, and that their claim ranked ahead of the claims of unsecured creditors.

This made it practicable for companies to borrow on their circulating assets such as stock in trade and book debts. The floating charge can enable a creditor to get an all-embracing security. The charge remains floating and the company free to use the assets subject to the charge until the charge is converted into a fixed charge. The ending of the freedom is called 'crystallisation of the charge'. Until then, in the absence of anything to the contrary in the instrument creating the charge, the company can, if it is acting in the ordinary course of business –

* sell assets to a purchaser who will take a good unencumbered title;
* create fixed charges so that the taker of a fixed charge will be entitled to payment out of the asset ahead of the holder of the floating charge ; and
* pay debts.

Transactions outside the ordinary course of business include:

* a disposition by a failing company having no significance other than as a calculated attempt to frustrate the chargee: *Hamilton vs Hunter*[4];
* dispositions made by provisional liquidators outside their power; provisional liquidators take over from directors while an application for a winding up order is pending[5] :

The phrase "ordinary course of business" may even cover the sale of the company's whole undertaking in exchange for securities in another company provided such sale is authorised by the objects clause in the company's memorandum.[6]

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1 (1903) 2 Ch. 284,295
2 (1862) 10 HLC 191.
3 (1870) LR 5 Ch.App.318.
4 (1982) 7 ACLR 295.
5 Re Bartlett Estates Pty. Ltd(1988) 14 Australian Company Law Reports.512.
6 Re Borax Co. [1901] 1 Ch.326,C.A.

Ford and Austin however note that unless the instrument of charge provides otherwise, the mere fact that a disposition is exceptional does not put it outside the company's implied freedom.[1] They cite the decision of *Reynolds Bros (Motors) Pty Ltd vs Esanda Ltd*[2] where several tractors transferred to a finance company thirteen days before the chargee of the floating charge appointed a receiver was held to be a valid transfer free from the clutches of a floating charge. The sale occurred while the company was free to sell on the basis that a transaction maintaining the company as a going concern is within the freedom even though it is exceptional. Also see *Re H H Vivian Co. Ltd.*[3] for a supporting view and *Torzillu Pty. Ltd vs Brynac Pty Ltd.*[4] where the contract to transfer premises was avoided against the chargee of a floating charge because the financial position of the seller was known to the buyer and the controlling shareholders of the buyer and seller company were close associates and the terms of payment were leisurely. The parties may have agreed to reduce the company's freedom by their contract embodied in the instrument of charge. In *Fire Nymphs Products Ltd vs The Heating Centre Pty. Ltd*[5] a charge allowed the company to dispose of charged assets only in 'the ordinary course of its ordinary business'. The company distributed heating units manufactured by FNP. The company agreed to return title of some units to FNP while the company remained in possession of them as bailee with FNP's authority to sell them. Within a month a finance company appointed receivers to the company. The receivers sold units. FNP sued to recover the value of the units sold. The claim was rejected because the return of the units was not in the ordinary course of the company's ordinary business. The charge also provided that an attempt to dispose outside the ordinary course of business of the company would cause the floating charge to become a fixed charge. Therefore, FNP took the returned units subject to a fixed charge in favour of the finance company.

A floating charge is said to crystallise into a fixed charge on events implied by law or defined in the instrument of charge. The fixed charge is only an equitable charge , so the competition will be between that earlier equitable interest and a later acquired interest which depending on the company's transaction , may be a legal interest or an equitable interest.

Appointment of a liquidator causes crystallisation. Another instance is (quite frequent in western countries but not so much found in the sub-continent) when a secured creditor appoints a receiver to take control of company assets and sell them to enforce the creditor's debt, or successfully applies to the Court to appoint a receiver.

A third event – namely, cessation of the company's business – can cause crystallisation, at least where it amounts to the company ceasing to be a going concern.[6]

Instruments of charge often provide for crystallisation on any of a wide range of events of default by the company. Chargees try to have the charge crystallise ahead of various types of claims that might be made by third persons, such as an attempted execution of judgment against the company. The courts now accept that the company and the chargee are free to contract on the matter of when the crystallisation will occur. A construction of the language under which there would be waiver relating back gives the chargee protection between the occurrence of the event and the chargee's learning of it. The chargee has an opportunity to assess the position[7]:

Where provisions are ambiguous the Court will lean away from the construction which allows automatic crystallisation. In *Re Bismarck Pty. Ltd.*[8] a clause of a debenture provided that money owing should 'at the option of the mortgagee immediately become due and payable without necessity for any demand or notice and this security shall become

1 Principles of Corporations Law 7th Ed. para 19.210.
2 [1983] 8 ACLR 422.
3 [1900] 2 Ch. 654.
4 [1983] 8 ACLR 52.
5 [1988] 14 ACLR 274.
6 Re Margart Pty Ltd [1984] 9 Australian Company Law Reports269 cited by Ford and Austin:Principles of Corporations Law 7th Ed. para 19.220.
7 Dovey Enterprises Ltd vs Guardian Assurance Public Ltd. [1993] 1 New Zealand Law Reports 540.
8 [1981] Victorian Reports 527

enforceable and the right of the company to deal for any purpose with the mortgaged property or any part thereof shall forthwith cease on the happening of certain prescribed events'. Jenkinson J. interpreted the clause as postponing crystallisation until the debenture holder exercised the option conferred by the occurrence of a prescribed event. Although there was some doubt as to the validity of automatic crystallisation provisions, the matter seems to be settled beyond dispute by the judgment of *Hoffman J. in Re Brightlife Ltd.*[1] upholding the validity of a provision enabling the floating charge holder to serve a notice of crystallisation on the company. He saw crystallisation as being a matter of agreement between the parties and on this reasoning there can be no objection to a charge being made to crystallise on the happening of a specified event.

The Australian Law Reform Commission recommended in Report No. 45 on the 'General Insolvency Inquiry'(1988) para 196 that companies legislation should provide for crystallisation to take place only–

- when a public act (entry into possession of the company's property by a receiver, an agent of the chargee or the chargee itself or appointment of a liquidator, or administrator) has occurred; or
- a notice that the charge has become fixed has been lodged with the registering authority.

A similar provision will make life easy for our banks and finance companies and their clients in this country as this will clarify the law which the companies find too complicated at times.

13.1.4 *No particular form of words is necessary to create a floating charge; it suffices if the intention is shown(a) to impose a charge on assets both present and future,(b)the assets are of such a nature that they would be changing in the ordinary course of business, and (c) the company is free to continue to deal with the assets in the ordinary course of its business.*[2]

Professor Gower notes[3] that for a clear grasp of the nature of a floating charge, two important factors must be kept in mind. First, probably the most significant feature for identifying the floating charge is that the company retains management autonomy with respect to the assets subject to the charge. Thus the essence of the charge is not determined by the nature of the property over which it is created but rather by the degree of freedom accorded to the company to deal with this property in the normal course of business.[4] In *Dawson vs Isle*[5] the Court held that a fixed charge had been created in favour of a bank over book debts(in this case bill of exchange) where the charge provided that the company could not charge or assign these debts *and, most importantly, had to pay the proceeds into an account with the chargee bank which the company could not operate without the consent of the bank.* It was the absence of the ability to use the book debts in the normal course of business that deprived the charge of the character of floating. But see Re Brightlife Ltd.[6] where the Court held that a floating charge had been created where the company could pay the proceeds of charged book debts into its bank account and use them in the normal course of business. To preclude a charge from being a floating charge, the restriction must substantially deprive the company of the power to deal with its assets in the normal course of business.

Although a floating charge relates to future assets it is a present charge and not a future one. In *Re Margart Properties Ltd.*[7] a bank enforced its floating charge after the commencement of the company's winding up and the liquidator argued that the payment of the proceeds of the realisation was invalid because of the provisions of the Insolvency Act

1 [1987] Ch. 200
2 Professor Gower citing cases in Modern Company Law. 5th Ed. page 413.
3 ibid.p.414
4 Siebe Gorman & Co. Ltd. vs Barclays Bank Ltd.[1979] 2 Lloyd's Reports 142.
5 [1906] 1 Ch. 633.
6 [1987] Ch.200.
7 [1985] BCLC 314.

which invalidated any disposition of the company's property after the commencement of the winding up. The argument failed for the reason that the disposition of the company's property took place when the charge was created and not when the charge was enforced; the floating charge is an existing charge and not one arising in the future when the charge is enforced or when it crystallises.[1]

The same author notes another aspect of a floating charge that the floating charge provides less than perfect security. Because of the management autonomy accorded to the company with respect to the charged assets, the company can create security interests that have priority to the floating charge : a floating charge will be deferred to any subsequent fixed legal or equitable charge created by the company over its assets. Similarly, if debts due to the company are subject to a floating charge , the interest of a floating charge holder will be subject to any lien or set off that the company creates with respect to the charged assets prior to crystallisation.

For a floating charge is not regarded for this purpose as an immediate assignment of the chose in action ; it becomes such only on crystallisation.[2] See *Cretanor Maritime Co. Ltd. vs Irish Marine Management Ltd*[3] where the company's assets were subject to an injunction, against their removal from the jurisdiction, obtained by an unsecured creditor. On the application of the holder of the debenture whose charge had crystallised the court discharged the injunction. Also see *Capital Cameras Ltd. vs Harold Lines Ltd.*[4], a case of successful application of a receiver to dismiss a mareva injunction.

The crystallisation of a subsequent floating charge does not have the effect of crystallising a prior floating charge in the absence of a term to that effect in agreement creating the prior charge.[5]

To get better protection a chargee may require that a floating charge contain provision that restricts the right of the company to create charges that have priority to or rank equally with the floating charge (called a negative pledge clause); such restrictions are strictly construed.[6] The parties however share the floating charge by amendment of the deed of charge.

A company cannot create a floating charge on the same assets ranking in priority to or pari passu with the original floating charge.[7]

Professor Gower however notes that while obviously the fixed charge accords superior protection, there are sound reasons for taking a floating charge.[8] First, where a subsequent holder of a registrable charge is deemed to have notice of a negative pledge clause then this accords priority to the floating charge holder. Second, the charge provides security against unsecured creditors. Third, the floating charge holder will be able to take steps to enforce the charge and give him considerable control over the company's affairs. Fourth, the holder of a floating charge will have some measure of control over the company even without taking any steps to enforce it. Lastly, the holder of a floating charge will be able to block the appointment of an administrator.

13.2.1 **Registration of Charges** – Section 159 provides that every mortgage or charge created by a company and being either–

a) a mortgage or charge for the purpose of securing any issue of debentures; or

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1 Prof. Gower: ibid page 414.
2 Professor Gower : ibid page 415.
3 [1978] 1 W.L.R. 966,C.A.
4 [1991] 1 WLR 54.
5 Re Woodroffes(Musical Insruments) Ltd. [1985] 2 All E.R.908.
6 Brunton vs Electrical Engineering Corporation [1892] 1 Ch. 434; Robson vs Smith [1895] 2 Ch.118, English and Scottish Mercantile Investment Company Ltd vs Brunton [1892] 2 Q.B. 700,C.A. and Re Castell and Brown Ltd [1898] 1 Ch.315(if the title deeds are left with the company, an equitable mortgagee by deposit will take priority.)
7 Re Benjamin Cape and Co. [1914] 1 Ch.800; Re Automatic Bottle Makers Ltd. [1926] Ch.412,C.A.
8 ibid at page 417.

b) a mortgage or charge on uncalled share capital of the company, or

c) a mortgage or charge on an immovable property wherever situated or interest therein; or

d) a mortgage or charge on any book debts of the company, or

e) a mortgage or charge, not being a pledge on any moveable property of the company except stock-in-trade, or

f) a floating charge on the undertaking or ,shall, so far as any property of the company, security on the company's property or undertaking is thereby conferred,

be void against the liquidator or any creditor of the company, unless the prescribed particulars of the mortgage or charge, together with the instrument, if any, by which the mortgage or charge is created or evidenced or a copy thereof verified in the prescribed manner are filed with the Registrar for registration within twenty one days after the date of its creation; any contract or obligation for repayment of the money thereof secured shall not be prejudiced and when a mortgage or charge becomes void for non-registration, it shall immediately become payable.

Provided that if the mortgage or charge created out of Bangladesh comprises property outside Bangladesh the said period of twenty one days shall be counted by excluding the period which would be necessary to receive the instrument in Bangladesh .Where the mortgage or charge is created in Bangladesh comprising property outside Bangladesh the instrument creating or purporting to create the mortgage or charge or a copy thereof may be filed for registration notwithstanding that further proceedings may be necessary to make the mortgage or charge valid and effectual in the country where the property is situate.

If a negotiable instrument has been given to secure the payment of any book debt of the company the deposit of the instrument for the purpose of securing an advance to the company shall not for the purpose of registration be deemed to be a charge on the book debts of the company; similarly, the holding of debentures entitling the holder to a charge on immovable property shall not be deemed to be an interest in the immovable property.

Sub-section (2) of section 159 provides for a constructive notice to all those who subsequently acquire the property of the fact of the mortgage registered according to the section.

Section 160 provides that where a company acquires a property which is subject to a charge required to be registered it shall cause the prescribed particulars of the charge to be registered within twenty one days of the acquisition of the property together with a certified copy of the instrument of charge. If the company defaults then every officer who is knowingly a party to the default will be liable to a fine of one thousand taka.

Section 161 requires that where a series of debentures containing or giving by reference to any other instrument, any charge to the benefit of which the debenture holders of that series are entitled pari passu is created by the company , it shall be sufficient compliance of section 159 if there are filed with the Registrar within twenty one days after the execution of the deed containing the charge or, if there is no such deed, within twenty one days of the execution of the debenture series the following particulars:

a) the total amount secured by the whole series;

b) the dates of the resolutions authorising the issue of the series and the date of the covering deed, if any, by which the security is created or defined;

c) a general description of the property charged;

d) the names of the trustees, if any from the debenture-holders ; and

e) the deed or a copy thereof verified in the prescribed manner containing the charge or if there is no such deed one of the debentures of the series;

Provided that , where more than one issue is made of debentures in the series, there shall be filed with the Registrar for entry in the register particulars of the date and amount of each issue. An omission to do this however does not affect the validity of the debentures issued. The Registrar is under an obligation to register the particulars and the deeds filed under section 161 of the Act.

Where any commission, allowance or discount has been paid or made either directly or indirectly by the company to any person in consideration of subscribing for debentures, particulars of the discounts etc. paid shall have to be filed along with the returns of debentures and mortgages filed at the Registrar's office.[1]

The returns filed by the company containing the details of the mortgages and charges are to be entered in a Register of Mortgages to be kept by the Registrar. The Register shall contain the date of creation of the mortgage, the amount secured by it, short particulars of the property mortgaged and the names of the mortgagees and the chargees. The Registrar shall keep open for inspection of the public the Register on payment of a specified fee. (Section 163).

The Registrar shall also maintain an index to Register of Mortgages and Charges in a chronological manner and with the prescribed form and with the prescribed particulars of the mortgages and charges. (Section 164). The Registrar shall give a certificate signed by him of the registration of the mortgage or charge and such certificate shall be conclusive proof of the fact of registration of the charge and mortgage as required by law. (Section 165). In practice however, it takes some time for companies to obtain this certificate and this is awkward when foreign debenture holders ask for such a certificate.

The company issuing the debentures shall cause a copy of every certificate of registration to be endorsed on the debenture or certificate of debenture stock.[2]

Section 167 provides for two important features of such registration. If the company fails to register the mortgage or charge any person interested may do the same. Secondly, any modification in the terms and condition of the charge shall have to be registered also by the company. It is quite often that the debenture holder causes the charge or the mortgage to be registered simply because otherwise the charge or mortgage will be void against the liquidator or any creditor.

Section 168 requires every company to keep a copy of every instrument creating the charge or mortgage at its registered office.

If any person causes a Receiver to be appointed under any provision contained in the debenture, he shall cause a notice of the fact to be sent to the Registrar's office and the Registrar shall have the notice entered in the register of mortgages and charges. The Receiver shall file an account of receipts and expenditures of the property taken possession of by him with the Registrar.[3]

Section 171 of the Act gives the Court the power to rectify the register of mortgages if the Court is satisfied that –

a) the omission to register the mortgage or charge within twenty one days of its creation or any mis-statement with regard to it or the omission to give to the Registrar of the payment or satisfaction of the debt for which the mortgage or charge was created, was accidental or due to inadvertence or due to some other cause;

b) the omission is not of a nature to prejudice the position of creditors or share holders of the company; or

c) on other grounds it is just and equitable to grant relief.

The Court in such a case may, on the application of the company or any person interested, on such terms as may be just and expedient, order that the time for registration of the mortgage or charge be extended or the omission or mis-statement be rectified and may make order as to the cost of the application. The section protects rights acquired in respect of the property concerned prior to the time when the mortgage or charge is actually registered.[4]

Section 172 provides that the company shall give intimation of the payment of satisfaction of any mortgage or charge to the Registrar within twenty one days of such

1 Section 162 of the Act.
2 Section 166.
3 Section 170.
4 sub-section 2.

satisfaction. The Registrar shall then send a notice to the mortgagee of the satisfaction and ask him to show cause within 14 days why the satisfaction of the mortgage or charge shall not be entered in the Register of Charges and Mortgages. If no cause is shown the Registrar shall enter the satisfaction in the Register and shall give a copy of the satisfaction of the mortgage or charge to the company. If cause is shown by the mortgagee or chargee the Registrar shall inform the company of this fact.

Section 173 provides for a penalty of upto taka 1000 per day if a company defaults in registering the charge or mortgage or its satisfaction for every officer who is knowingly a party to the default. Penalties also follow for not complying with the provisions of the Act regarding registration of mortgages and delivery of debentures without complying with the provisions of the Act.

Section 174 of the Act requires every company to keep a register of mortgages and enter therein all mortgages and charges specifically affecting the property of the company and all floating charge on the undertaking of the company giving in each case the description of the property mortgaged or charged , the amount of the mortgage or charge and except in the case of securities to the bearer, the names of the mortgagees. An omission entails a fine of two thousand taka for a director or officer or manager of the company who permits or authorises the omission of any entry required to be registered in the company's register of mortgages.

Section 175 entitles a creditor or member of the company to inspect the register of mortgages and charges without payment of any fee and any other person to do the same on payment of a nominal fee. If inspection is refused the Court can order such inspection and also may impose fine on the company.

Section 176 provides that a company shall keep open every register of the debenture holders for the inspection of its debenture holders and shareholders. The register shall be kept open for inspection for at least two hours a day but may remain closed for inspection for a period not exceeding thirty days a year. A copy of a trust deed for securing any issue of debentures shall have to be given to every holder of debentures. If inspection or copy is refused then the company is liable to a fine and the Court may order such inspection or copy to be furnished.

13.2.2 **Further Statutory Requirements of Debentures and Floating Dharges** – Section 177 of the Act provides for perpetual debentures or debentures redeemable only on the happening of a certain contingency. Section 178 permits a redeemed debenture to be re-issued unless the conditions of the issue provide otherwise or the debentures have been redeemed in pursuance of any obligation on the company so to do , not being an obligation enforceable only by the person to whom the redeemed debentures were issued or his assigns. The re issue can be done either directly or through a nominee of the company. On a re-issue the person entitled to the debentures shall be deemed to have the same rights as if the debentures had not previously been issued. If the company has paid the debts secured by the debentures it shall not automatically be deemed to have redeemed the debentures for the purpose of section 178.

Section 179 provides that a contract with a company to take up and pay for any debentures of the company may be enforced by a decree for specific performance.

Section 180 equates for the purpose of payment of preferential debts the appointment of a receiver on behalf of the holders of debentures secured by a floating charge and the appointment of a liquidator in a winding up proceeding. The preferential debts to be paid in case of a winding up are also granted preferential status in the case of a case of a receiver appointed by the debenture holders.

13.3.1 In the U.K. section 245 of the Insolvency Act 1986 provides that a floating charge created in favour of an unconnected person within 12 months of the commencement of the winding up or the making of an administrative order shall be invalid unless it is proved that the company was solvent immediately after the creation of the charge. In the late twentieth century courts have developed the view that once the company is on the verge of insolvency

it must deal with its assets with the interests of its creditors in mind. There is also a notion that even a solvent company is not free to dispose of its assets except for proper corporate purposes.[1] There is no corresponding provision in our law. It is tempting to create a floating charge when directors realise that liquidation is imminent and give themselves or their preferred creditors preference over other unsecured creditors. Sooner or later this problem will arise in this country and the law makers will have to address the problem.

The protection given to creditors by requiring charges to be registered fulfils a range of purposes. As Professor Gower points out[2] it provides a picture of the state of the encumbrances on a company's property, something which is obviously of interest to those contemplating entering into a secured lending transaction with the company. Registration operates to protect the security holder by providing him with a certain degree of protection as to the validity and priority of the charge once it is registered. This in turn benefits the company by enabling it to give the chargee the guarantee of such protection. The chargee may take advantage of the presumption that registration has conferred validity on the charge and may assign the charge outright. Registration is also of interest to credit analysts, liquidators, receivers, shareholders and prospective investors.

It should be remembered that where a negotiable instrument has been given to secure the payment of any book debts of the company the deposit of such instruments shall not be treated as a charge on the book debts of the company. This is because registration would destroy the negotiability of the instrument. Similarly, it is doubtful whether fixed charges on bank accounts and fixed charges on shares held in a subsidiary will have to be registered. A deposit at the bank would normally not be a book debt, although not necessarily in all situations.[3]

The Register of Charges maintained at the Registrar's office may not accurately reflect the extent of the incumbrances on the company's property. However, it does give a prospective investor or creditor a notice that some charges have been created and then it is for him to find out the full extent of the charge.

13.3.2 **Non Registration** – Failure to comply with the registration requirements leads to fines and it is quite a common scene in the Company Bench of the High Court Division to find lawyers coming up with petitions for condonation of delay in filing particulars of charges with the Registrar. The immediate motive is to save the company from a fine of up to one thousand taka for every day the default continues and the Dhaka High Court has so far been liberal in condoning the delay although this would invariably cause the company to make a donation to some charity. The case law on this will be dealt with in paragraph 13.5.1.

However, the most potent sanction is that non-registration destroys the validity of the charge.[4] Unless the prescribed particulars of the mortgage or charge are filed within twenty-one days of their creation , the charge or mortgage will be void against the liquidator and any creditor of the company.[5] It may be void even against a subsequent chargee who has notice.[6] The main sufferer is of course the chargee and not the company. To give redress to a creditor section 167 permits a person interested in the charge to register it at the cost of the company. If however this is not done the consequences are grave for the chargee and any prudent creditor will make sure on its own that the charge is registered. To reduce the hardship section 159 provides that the charge is void to any extent for non-registration and the whole of the sum secured becomes repayable on demand. This, of course, is an incentive for the

1 ANZ Executors & Trustee Co. Ltd. vs Quintex Australia Ltd. [1990] Australian Corporations and Securities Reports 676.

2 Modern Company Law 5th Ed. 426

3 See Re Permanent Houses(Holdings) Ltd [1988] BCLC 583; Northern Bank Ltd. vs Ross [1991] BCLC 401, C.A.

4 section 159(1)(f).

5 ibid.

6 Re Monolithic Building Company [1915] Ch. .643, C.A.;Midland Bank Trust Co. Ltd vs Green [1980] Ch. 590.

company to register. The contract for repayment of the money is however not prejudiced (section 159) and a chargee may take steps to enforce it. An unsecured creditor will not have any locus standi to prevent the holder of a void charge from enforcing it.[1] This although he will get protection against an unregistered charge if the company goes into liquidation.

In the U.K. section 95 of the Amendment Act of 1989 introduced a provision in the English company law (section 400) that a charge can be registered outside the 21 day period without a court order. In this country, invariably a court order under section 171 will be required for the Registrar to register the charge. There is of course the risk that a subsequent chargee will be registered first and thus gain priority. The English decisions have held that the court will not exercise its jurisdiction to order that a charge registered out of time has priority to a charge which has already been registered.[2]

Where the registered particulars of the charge are not accurate the charge is void to the extent of the rights not disclosed as against a liquidator or person who acquires for value an interest or right over the property. The court can rectify the omission or mis-statement if it is just and equitable to grant relief.[3]

Registration does not cure any flaw in the charge itself and the validity of the charge can be challenged. Further, registration does not create a priority point and if a charge is registered at a particular date it may still be postponed to a charge registered later but created earlier within 21 days of its registration. However, registration is a necessary, although not sufficient, condition to obtain priority. On registration of a charge the Registrar issues a certificate (section 165) and it is a conclusive evidence that the requirements of registration have been complied with. This will be evidence that the particulars were delivered no later than the date stated on the certificate. This is important to decide whether the charge was registered within twenty one days of its creation. The certificate increases the liquidity of the security interest since an assignee of the interest will want to be assured that the charge has been validly registered.

13.3.3 **Debenture** – There is no precise definition of a debenture in the Act and one has to examine what the different authors of different countries have commented on this. Professor Gower summarises the essential feature of a debenture as being a type of transferable security (resembling shares) whereby a company can raise finance in the form of loan capital instead of share capital.[4] He however apprehends that problems may arise, for in recent years, developments in banking and commercial circles have led to the invention of a remarkable array of new and highly sophisticated types of "securitised " loan investments as a result of which finance, which would formerly have been raised by a straightforward bank loan (for most purposes not a debenture) may be obtained through the issue of instruments, some of which for most purposes unquestionably are debentures and others of which may or may not be.[5] At common law a company issues a debenture when it delivers its acknowledgment in writing of a debt it owes, whether existing or newly created but negotiable instruments such as bill of exchange and promissory notes as well as deeds of covenant are excluded.[6] When a public company raises loan finance from the investing public the company may, instead of creating a series of debentures, raise a single fund of debenture stock from which the company can issue to each subscriber a certificate declaring that the holder is entitled to be a creditor for a definite sum of money, being part of the stock. That would allow holders of debenture stock to transfer any fraction of the monetary sum represented by their holdings, something which cannot be done by a holder of a debenture.

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1 Re Ehrmann Bros. Ltd. [1906] 2 Ch. 697.

2 Re R.M.Arnold & Co. Ltd. [1984] BCLC 535;Re Fablehill Ltd. [1991] BCLC 830; Re Chantry House Development plc. [1990] BCLC 813.

3 Section 171.

4 Gower's Principles of Modern Company Law 6th Ed. p. 323.

5 ibid.

6 Handevel Pty Ltd vs Comptroller of Stamps (Vic) [1985]157 CLR 177;62 ALR 204.

13.3.4 **Enforcement of Debentures** – A floating charge may be enforced by the appointment of an administrative receiver. The debenture holders (or rather the trustees) will normally appoint a receiver either under a power given by the debenture or by court. Where the appointment is pursuant to the provisions in the debenture it should be made certain that the conditions justifying the appointment are fulfilled. However in this country invariably it is the Court that will exercise this power and it is rare that the debenture holders will appoint a receiver to take possession successfully. The position is different in western countries where the law places few constraints on the right of the security holder to enforce the charge and in this sense it is prosecurity holder. But in Bangladesh if the company resists a takeover by the Receiver, the security holder will have to take shelter of the Court which will be more likely to issue a show cause notice on the company resulting in delays of months if not years by which time the company will have transferred its assets. The English law is exhaustive as to the powers of the Receiver but our law is woefully silent on the subject and with the explosion of financial activities financed by public borrowings sooner or later this problem will be faced by the business community.

Charlesworth and Morse: Company Law[1] classifies the remedies of debenture holders into two classes. If a debenture confers no charge, a debenture holder is an ordinary unsecured creditor. If there is default in the payment of principal or interest he may either sue for the principal or interest and, after obtaining judgment, levy execution against the company, or petition the court either for an administration order or winding up of the company. When a charge is conferred on the company's assets by way of security, and default is made in the payment of principal or interest, a debenture holder, or the trustees, where there is a trust deed , may , in addition to the remedies available to an unsecured debenture holder, exercise any powers conferred by the debentures or the trust deed , e.g., of appointing a receiver of the assets charged, of selling the assets charged or of taking possession of the assets and carrying on the business; if the debenture or the trust deed does not contain powers in that behalf, the trustees may apply to the court for the appointment of a receiver and manager, or an order for sale or foreclosure.

When the debenture is an "all moneys" debenture, e.g., one for all sums owed to a bank, the demand for payment need not specify the exact sum due and a receiver may be appointed once reasonable time to make payment has passed.[2] A demand for an amount less than the full amount due will be sufficient for the appointment of a receiver, although there is no authority if the demand is excessive, i.e., for more than the amount due.[3] In England, where there are numerous debentures of the same class, a debenture holders' action is usually brought. This is brought by one debenture holder on behalf of himself and all other debenture holders of the same class as himself. In it a claim may be made for :

1) a declaration that the debenture holders are entitled to a first charge on the property of the company;
2) if there is a trust deed, the enforcement of the trust;
3) an account of what is due to the debenture holders;
4) the enforcement of the charge by sale or foreclosure;
5) the appointment of a receiver or manager.[4]

If the assets require immediate protection an application for the appointment of a receiver is made.[5] A debenture not supported by consideration is fictitious.[6]

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1 14th Edition page 688.
2 Bank of Baroda vs Panessar [1987] Ch. 335.
3 N.R.G. Vision Ltd vs Churchfield Leasing Ltd. [1988] 4 BCC 56.
4 Palmer's Company Precedents (16th. ed.), Pt.III, p.498.
5 Re Continental Oxygen Co. [1897] 1 Ch. 511.
6 Ram Kumar vs. Buxar Oil and Rice Mills AIR 1960 Cal 764.

13.4.1 **Receiver** – In general terms the appointment of a receiver paralyses the powers of the company and its administration in favour of the receiver. He entirely supersedes the company in the conduct of its business, deprives it of all powers to enter into contracts, or to sell, pledge or otherwise dispose of the property put into possession of or under the control of the receiver and manager. Its powers in these matters are entirely in abeyance.[1]

The fact that a receiver is an agent of the company does not mean that he must carry out its orders and he is not an officer of the company or liable in general as such.[2]

Contracts which were binding on the company when the receiver was appointed continue to bind the company. Although a receiver has a discretion he should not disregard contracts if to do so would damage the company's goodwill or affect the realisation of its assets, especially if it seems that the company is likely to trade.[3]

A receiver owes fiduciary duties to the company.[4] The main aim of the receiver is to obtain enough money from the company to pay off his debenture holders.

Regardless of any power in a trust deed or debenture, the court has power to appoint a receiver and manager in three cases–

a) when the principal sum has become repayable or interest is in arrear;

b) if the company is wound up-even if this is for the purpose of amalgamation or reconstruction;

c) if the security is in jeopardy, even though interest is being paid.[5]

If a company is wound up after a receiver is appointed (and this is possible) the receiver continues in possession of the property subject to the charge and is not prevented from selling it.[6] On the other hand even though a winding-up has commenced the debenture holders are not prevented from appointing a receiver or asking the court to appoint one.

13.5.1 **Rectification of Register of Mortgages** – Since the register of mortgages is a good evidence whether a charge exists on the property of a company or not the Court has been given power to rectify it. For a legal practitioner this is the most important section as businessmen in our country, being new as they are in the field , quite often omit to register a charge in time and so do their creditors and as a result after some time they realise the omission or mistakes and rush to the lawyer's chamber who will no doubt in a sombre manner draw their attention to the drastic results that follow non-registration of the charge and then draw up a petition to the court for condonation of the delay or the omission or correction of any mistake in filing the particulars of the charge. The courts in this country have generally been lenient in rectifying the register of mortgages but mainly because in most cases there has been no case of competing equities. Whereas in Bangladesh this power is given to the Court the Indians have amended the law in 1974 and have substituted Company Law Board for the High Court as having power to rectify. In Bangladesh there is a shortage of company law knowing persons and the idea of a Company Law Board is far fetched. However the two sections (i.e., section 171 of the Bangladesh Companies Act and section 141 of the Indian Act) are otherwise common.

In England this power was previously exercised by the Court and the English courts have held that this is a discretionary power. The courts may insist to be fully informed of the circumstances which have given rise to the omission to register within the proper time and the evidence should not, as is so often the case, merely state that the matter was accidental and due to inadvertence without particularising the reasons for the breach of the statutory

1 'House of Lords in Moss Steamships vs Whinney [1912] A.C. 254.

2 Re B. Johnson & Co(Builders) [1955] 2 All E.R. 775.

3 Re Newdigate Colliery [1912] 1 Ch. 468.

4 Nugent vs Nugent(1908) 1 Ch. 546; Cuckmere Brick Co. vs Mutual Finance Ltd. (1971) 2 All E.R.633 and Standard Chartered Bank vs Walker [1982] 3 All E.R. 938(a similar duty towards a person who has guaranteed the company's overdraft).

5 Smith and Keenan's Company Law Sixth Ed. p.326.

6 ibid. at page 327.

requirements and the surrounding circumstances. There is a statutory right in the mortgagee or chargee to come to the Court to be relieved of the consequences of his own negligence and lack of caution provided that the Court is satisfied that the omission to register was not with any fraudulent intention but was "in the words of the Companies Act,1948,[1] 'due to inadvertence' or to 'some other sufficient cause'".[2] The secretary of the company being wrongly advised by the counsel that no registration was necessary would be an example of such inadvertence. [3] The words 'accidental or due to inadvertence' have been given liberal interpretation. The Court's order is without prejudice to the rights of parties acquired prior to time when such charge shall be actually registered.[4] Similar provision is found in section 171(2) of our Act. Lord Denning M.R. in *Resinoid and Mica Products Ltd*[5] held that time should not be extended after liquidation had commenced because this would prejudicially affect the rights of the parties which are determined on the commencement of the winding up. In this case the application was not made for a long time and filed only when liquidation was imminent. For a different view, reference may be had to In *re Mechanisations Ltd.*[6] The chargee should, when he discovers that the charge is not registered, immediately apply for extension of time if he wants to register.[7]

In an application for extension of time the Court will not go into the question of validity of the charge.[8] The Court will not exercise this power to order the deletion of a whole registration under this section where the Registrar has issued a certificate of registration.[9] If however a certificate has wrongly been issued this can be challenged in a writ petition.

In *Dhakeswari Cotton Mills Ltd. vs Registrar*[10] a division bench of the Dhaka High Court held that under section 121(1) of the Companies Act 1913 (corresponding to section 172(1) of the present Act) it is the duty of the company to intimate to the Registrar the payment or satisfaction of any charge or mortgage created by the company and requiring registration under section 109 of the Act of 1913 (section 159 of the present Act). "Payment or satisfaction" in the context means full payment or full satisfaction and not part payment or part satisfaction. The Registrar required the company to file all the memorandum of satisfaction in separate forms duly showing the amount of part payment or part satisfaction made in each year under section 121(1) of the Act of 1913 and launched prosecution against the company which then filed a writ petition against the Registrar. Mr. S.R.Pal appearing for the company argued that the words "payment or satisfaction of any charge or mortgage" appearing in that section should be given their natural meaning and the word "part" should not be imported into the language of the section and so far as a charge or mortgage is concerned , the law does not recognise partial redemption and therefore sub-section (1) of section 121 applies only to cases where there has been full payment and full satisfaction of any charge or mortgage. Mr. S.R.Pal also referred to sections 138 and 139 of the Indian Act of 1956 which provided for registration of part payment or satisfaction of any charge and by analogy he argued that in the absence of any such provision in our law, the words "payment or satisfaction" cannot be construed to mean " part payment or part satisfaction." Mr. M.Asir, the then Advocate General, appearing for the Registrar argued that the word "part" should be imported in the language of the section because it would be for the convenience of the public if part payments are registered with the Registrar so that the public would know the exact financial position of the company concerned and that the amendment of the Act in India was merely illustrative to make the old idea of part payment clear.

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1 section 101

2 Re Kris Ltd[1948] 2 All E.R. 1105(Ch.D).

3 ibid.

4 See Re Joplin Brewery Co. Ltd.[1902]1 Ch.79 and Re M.I.G.Trust [1933] Ch.542.

5 [1982] 13 All E.R.677

6 [1966] Ch.20.

7 Victoria Housing Estates Ltd. vs Ashpurton Estates Ltd. [1982] 3 All E.R.665.Also see In re Reshma Estate(P) Ltd.[1977] 47 Comp. Cas. 447(Bom.) .

8 Re Heathstar Properties Ltd [1966] 1 All E.R. 1000 Ch.D.

9 Re C.L.Nye Ltd [1970] 3 All E.R. 1061.

10 (1956)7PLR(Dac) 122

The Court relied on some interpretations given in the Law Lexicon and the language of Order XXI, Rule 2(1) of the Code of Civil Procedure which contemplated satisfaction of a decree in whole or in part, and observed that section 84 of the law before the English Companies Act of 1948 did not contemplate a part satisfaction of the charge or mortgage and relied on the commentary in the Buckley's Companies Act that the corresponding sections in the earlier Acts applied only where the debt secured by the charge had been wholly paid or satisfied. The Court thus held that the words "payment or satisfaction of any charge or mortgage" means full payment or full satisfaction of any charge or mortgage.

The law should make clear that a part satisfaction of the charge or mortgage should also be registered because that would give an investor or creditor a better picture of the financial health of the company. Quaere, what happens when a charge is created in favour of three creditors pari passu and two of the creditors are paid off? Does it constitute part satisfaction of the charge or full satisfaction so that it should be registered? It is submitted that the company should register such satisfaction of charge given to two out of three charge holders.

Section 109 of the Act of 1913 (corresponding to section 159 of the present Act) came up for further consideration in *Messrs Green and White Ltd vs Registrar*.[1] The word "created" in sub-section (1) was held to include registration of a mortgage so that if a deed of mortgage was executed on 13-7-61 but registered on 2-9-61 under the Registration Act the deed may be registered with the Registrar of Joint Stock Companies within 21 days of 2-9-61.This, in spite of the argument of Mr Syed A.B.Mahmud Hossain, the then learned Senior Government Pleader that section 47 of the Registration Act provides that a registered document shall operate from the time which it would have commenced to operate if no registration thereof had been required or made, and not from the time of its registration. Sattar J. delivering the judgment held that if the document has been executed earlier, it will be operative from the date of the execution as between the parties to the document but in no view can it be said that the mortgage has been brought into existence on that date.

In *Syed Alim Mansur vs Registrar*[2] a single judge extended time for registration and said as follows :

> ... I am of the opinion that where on the failure on the part of the company or its members the deed could not be registered with the Registrar of Joint Stock Companies within 21 days of its creation as envisaged in section 109 and the failure is bonafide and is due to inadvertence on the part of the company or its members and where due to such omission no prejudice is caused either to the members of the company or to its creditors the extension of the period is necessary in order to protect the interests of the shareholders as well as the creditors and in that view of the matter it is just and equitable to extend the period for registration of the deed of mortgage with the Registrar of Joint Stock Companies....

In all the three cases cited above the judges argued themselves to take a position whereby the company got relief in Court.

1 15 D.L.R.(1963) Dac. 492.

2 42 D.L.R.(1990) 43.

BALANCE SHEET AND ACCOUNTS

14. Sections 181-192 deal with balance sheet, statements, books etc.

14.1 When the first legislation controlling the corporal activities were enacted in the mid - nineteenth century the idea was that promoters would find it in their own interests to publish a certain amount of information regarding the projects they were embarking thus reducing uncertainty in the minds of creditors, shareholders and other interested parties , and to the extent they omitted to do this, it would be upto the members and others dealing with the company, its officers and agents to protect their interests by making appropriate contracts with the parties concerned. Disclosure requirements were therefore minimal until the last part of the nineteenth century and the preparation of financial statements for a company were really a domestic matter, of concern only to directors and shareholders, unless the rights of third parties were directly affected.

14.1.1 Towards the end of the nineteenth century views about mandatory disclosure gradually began to change and formal accounts were beginning to be used for extraneous purposes like income tax etc. There was concern about the inequality of information and manipulation of data and the view that unsecured creditors had insufficient information on which to base their decisions gained a certain currency. The result was that statutory audit was introduced in 1900 in England and in 1908 the newly created 'public' class of companies were required to file their balance sheets. However, the majority of the companies, being private companies, were still exempted from these provisions.[1] In England gradually it was accepted more and more that the affairs of the modern corporation were often of interest to a much wider constituency than just the existing body of shareholders. This was given impetus by the decision in *R. vs Kylsant*[2] and the creation of the Securities and Exchange Commission in the United States of America which recognised a far greater amount of state control over corporate activities.

14.1.2 The Cohen Committee in England recommended in 1945 that the preparation of group accounts should be made mandatory and companies should be required to prepare an income statement truly reflecting its name. This principle was enshrined in the English Companies Act of 1948 which was followed largely in the Indian Companies Act of 1956 as amended from time to time. In Bangladesh certain changes were made in the chapter relating to balance sheet and accounts which seek to incorporate in a rudimentary form the notion of a true and fair disclosure but the detailed requirements of a balance sheet in England, the E.C. countries or even in India have been ignored in the Act of 1994. In England further changes were made in the law relating to balance sheet and accounts as a result of the Jenkins Company Law Committee Reports in 1962. Further, the Accounts Standards Committee set up in 1969 issued a number of mandatory statements concerning the preparation and

1 Charlesworth and Morse: Company Law 14th Ed. p. 506.
2 [1932] 1 K.B. 442.

publication of companies' annual accounts. This was supplemented in England by the EC's attempts to harmonise accounting regulations within the European Common Market countries and the Companies Acts of 1980 and 1981 incorporated most of the accounting and disclosure proposals contained in the EC's Second and Fourth Council Directives, dealing respectively with capital maintenance and distributions and individual company accounts. The Companies Act 1989 implemented the requirements of the Seventh and Eighth Council Directives, the former relating to group accounts and the latter to eligibility for appointment as a company auditor. In Australia accounting standards now emanate from the Australian Accounting Standards Board (AASB) which was established under section 225 of the Australian Securities Commission Act 1989. The AASB standards apply to entities that are required to report under the Corporations Law, i.e., principally companies, certain non-companies and disclosing entities which are trusts. The AASB has been setting requirements which have far reaching influence on the disclosure by public companies.

The accounting standards in the western countries have adopted some new concepts. They rely on the concept of 'entity' to identify the business enterprises which must report. For example, in dealing with consolidated accounts and 'related party disclosure' the AASB have set the standards to define the circumstances in which one entity controls another. (AASB 1024 and AASB 1017).This 'self standard setting' by the accounting profession has sometimes led to arguments whether the AASB requirements conflict with the law.

Proper company accounts are relevant because the fundamental principle underlying the Companies Acts has been that of disclosure and to ensure their accuracy through a professional audit. In Bangladesh, the standard of auditing is sometimes not to the extent it protects the interests of the public in the West. The law itself is only indicative and the accountants have taken upon themselves to impose international accounting regulations like those in England or Australia but they quite often rely on the informations supplied by the company management to draw up their reports. The Institute of Chartered Accountants of Bangladesh (ICAB) has adopted some of the prescribed guidelines of the International Federation of Accountants (IFAC) but the central issue lies in their implementation.

14.2.1 Section 181 of the Act of 1994 has improved upon section 130 of the old Act of 1913 which required every company to keep proper books of account. Following the requirements of section 209 of the Indian Act of 1956 and certain amendments made in the said Act in 1965, our present Act of 1994 requires the books of account to show not only details of all sums of money received and expended by the company , the sales and purchase of goods by the company and its assets and liabilities but also in the case of a company engaged in production , distribution, marketing, transportation, processing, manufacturing, milling, extraction and mining activities, particulars relating to utilisation of material, labour and other items of overhead costs. Our new Act has more importantly, adopted the much sought after principle that the books of account should give a 'true and fair view' of the state of affairs of the company and explain its transactions.[1] There is no supplementary provision or guideline how to achieve the golden fleece. The formula 'true and fair' is used rather than some more definite standard such as 'correct' or 'accurate' in apparent recognition that financial statements cannot be limited to recording objectively ascertainable facts but must include some items of information that are based on subjective estimation. For example, the balance sheet may show a fixed asset at its depreciated value. In deciding what annual depreciation rate should be adopted, estimates must be made of the effective life of the plant and of its realisable value at the end of its life. Another example lies in the valuation of the trading stock.[2] If a company defaults in keeping proper books of account then those who are in the top management like managing director, executive director, general manager or manager shall be punishable with imprisonment upto six months or fine upto five thousand taka.

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1 Sections 181(2)and 185(1).

2 Ford and Austin's Principles of Corporations Law 7th Edition para 10.190.

If a director fails to take all reasonable steps to secure compliance with this section he may be liable to a penalty. It is a defence if the person charged proves that he or she had reasonable grounds to believe, and did believe, that a competent and reliable person was charged with the duty of seeing to compliance and was in a position to discharge that duty.[1] However, if the managing director retrenches accounting staff so that the accounts cannot be kept properly then he is guilty of non-compliance with this section although he engaged a consulting firm and ultimately a major accounting firm.[2] In *Van Reseema vs Flavel*[3] the company did not keep any accounting records but only the source materials which evidenced the transactions. The Full Court of the Supreme Court of South Australia held that 'accounting records' include books of prime entry such as the cash book and journal, ledgers and also a range of source materials. It is duty of the Board to ensure that regular books of account are maintained and even if a general meeting does not have to be convened because company is ordered to be wound up this section will come into play.[4]

Plea that company is not functioning is no defence for failure to comply with the section.[5]

The common law adds to the statutory requirements and obliges the directors , as part of their duty of care to the company, to establish and monitor financial control system.[6]

Section 181(3) entitles a director to inspect books of account kept at the registered office of the company. This can be done either personally or through an agent.[7]

Right under this section can be enforced through Court.[8] Section 182 of the Act of 1994 corresponding to section 209A of the Indian Companies Act permits the Registrar or an authorised government officer to inspect the books of account of companies. This section is new in our law. This law does not authorise the Government to touch every paper but only those which have the character of books of account.[9]

Section 183 provides that the company must lay before the annual general meeting a balance sheet together with the profit and loss account or in the case of a company not trading for profit, an income and expenditure account. This section corresponds to section 131 of the old Act of 1913 , section 210 of the Indian Act and section 148 of the English Companies Act 1948. This section is the most important section to provide for the accountability of those who control and manage the company to those who invest in the company. The profit and loss account or the income and expenditure account shall be upto a period nine months before the meeting is held or in the case of a company carrying on business or having interest outside Bangladesh upto twelve months preceding the meeting. The period will correspondingly change if time is extended by the Court under section 81 for holding the meeting. The Registrar has a discretion for extending the period upto three more months if an application is made to him before the expiry of the said nine or twelve months. This period for which the account relates shall be known as the financial year and it may not exceed fifteen months. The balance sheet and profit and loss account or income and expenditure shall be caused to be audited by the auditor of the company. A copy of the balance sheet shall be kept in the registered office of the company along with a report of the board.

The Board's Report shall be attached to the balance sheet before being placed in the general meeting.[10] The directors shall comment on the state of the company's affairs, any reserve to be carried on, dividends if any recommended and material changes and commitments,

1 ibid at para 10.070.
2 ASC vs Fairlie [1993] 11 Australian Company Law Cases 669.
3 [1992] 10 Australian Company Law Cases 291.
4 In re Bhavnagar Vegetable Products Ltd. [1977] 47 Comp. Cas.128.
5 Madan Gopal Dey vs State [1969] 39 Comp. Cas.119 Cal.
6 Ford and Austin; AWA Ltd vs Daniels t/a Deloite Haskins & Sells[1992] 10 ACLC 933.
7 Sugarbhai Alibhai vs Amtee Properties (P.) Ltd [1984] 55 Comp. Cas. 734(Bom.) and V.Vakharia vs Supreme General Film Exchange Co. Ltd [1948] 18 Comp. Cas.34.
8 Maharaj Kumar Mahendra Singh vs Lake Palace Hotels [1958] 28 Comp. Cas. 805.
9 Karupunni C.V. vs Joint Director, Company Law Board [1986] 59 Comp. Cas.814.
10 section 184.

if any, affecting the financial position of the company which have occurred between the end of the financial year and the date of the report. The Board's Report shall deal with any changes which have occurred during the financial year in the nature of the business of the company or its subsidiaries and in the class of business in which the company has an interest. It shall give the fullest information and explanations in its report on every reservation, qualification or adverse remark contained in the adverse report. This section corresponds to section 131A of the previous Act, section 157 of the English Act of 1948 and section 217 of the Indian Act. A director is not necessarily personally responsible for reports and balance sheets stated to be issued "by order of the directors".[1] A director may be liable to individual shareholders who act in reliance upon a negligent mis-statement made in the Director's Report since a director has a duty to take care in making such statement.[2]

14.2.2. **Dividend and Reserve** – In its narrow sense "dividend" means that part of the profits which the company decides to pay to its shareholders. It was defined by Stirling L.J. in Re Crichton's Oil Co.[3] as being "prima facie a payment made to the shareholders while the company is a going concern; after the commencement of the winding up dividend is no longer payable". Dividends may be paid only in accordance with the company's memorandum and article.[4]

Articles usually require dividends to be declared by the company before they become payable.[5] Articles could provide that the profits will be applied in a certain way as soon as they are ascertained.[6]

A dividend is declared in the general meeting (Articles 51 and 96-103 of Schedule 1 Regulations to the Companies Act 1994) but this may not exceed the amount recommended by the directors. Interim dividends may be declared by the directors (Regulation 97 of the Schedule 1 Regulations) and no dividend shall be paid otherwise than out of profits of the year or any other undistributed profits. (Regulation 98 of Schedule 1 Regulations).

Dividends are paid according to the amounts paid on the shares and the directors may, before recommending any dividend, set aside out of the profits of the company such sums as they think proper as a reserve or reserves which shall, at the discretion of the directors, be applicable for meeting contingencies and no dividend may bear interest against the company. (Regulations 99,100 and 103 of Schedule 1 Regulations).

Although dividends can be paid only out of profits the English Courts found that 'profits' was an elusive and baffling concept better left to accountants and businessmen. Unfortunately, however, when litigation ensued it had to be decided by lawyers after listening to the expert evidence of accountants. The result was often one which baffled lawyers, accountants and businessmen alike. What the courts seem to have decided can be briefly summarised as follows:

a) So long as the properly presented accounts of the company showed a trading profit for the accounting period (normally a year) that could be distributed by way of dividend without regard to losses made in previous years; in other words 'nimble dividends', as the Americans describe payments in such circumstances, were permissible.

b) A realised profit made on the sale of a fixed asset could also be so distributed and according to the English Courts (but not Scottish Courts) so could an unrealised profit on a revaluation of fixed assets.[7] Both the English and the Scottish Courts accepted that such profits could be used to pay-up a bonus issue. Buckeley J. in Dimbula Case (1961) did not see how that could be possible unless the profits were distributed by way of dividend.

1 Denham & Co. Re[1884] 25 Ch.D. 752; also see Dovey vs Corey [1901]A.C. 477.
2 Hedley Byrne & Co. Ltd. vs Heller & Partners Ltd [1964] AC 465.
3 [1902] 2 Ch. 86, 95.
4 Oakbank Oil Co. vs Crum [1882] 8 App Cas 65 at 71.
5 Bond vs Barrow Maematite Steel Co [1902] 1 Ch 353.
6 Evling vs Israel & Oppenheimer [1918] 1 Ch. 101.
7 Dimbula Valey (Ceylon) Tea Company vs Laurie [1961] a Ch. 353.

c) Accumulated profits of previous years could also be so distributed unless they had been capitalised by a bonus issue or transfer to the capital redemption reserve.[1]

The English law has now been amended to provide a standard for calculating profits that may be available for dividend but since our law is similar to that prevailing in England before the amendments there so professor Gower's summary of the pre 1981 position is relevant in our country. The effect of the Dimbula valley case has been done away with in England and Australia by the amendments.

In practice, it is unusual for private companies to declare dividends. Many such companies are small family concerns where all the shareholders also act as the directors. Such companies will usually distribute profits by way of directors remuneration instead of by way of formal declaration of dividends – a practice dictated by taxation considerations. Shareholders in public companies are much less likely to be directors and therefore would expect that dividend payments would be made in the usual way when profits are made available. For listed public companies, a failure to maintain a significant level of dividend pay out each year can have a serioud impact on their share price.[2] Shareholders are known in this country to have forced the company to declare dividends in excess of what is recommended by the directors irrespective of the fact that there may not be any profit available for the dividend – an extreme case of what is known as 'short-termism' problem.

The Indian Courts have held that transferee of a share whose share has not yet been registered as a member in the company's share register is entitled to the dividend declared by the company during the interim period as a beneficiary of a trust from the transferor who will be deemed to be trustee holding the dividend in trust for the transferee.[3]

No clause contained in the Articles or Schedule I Regulations can override the provisions of section 184.[4] This case also held that only the general body of the company is competent to create a general reserve.

The Institute of Chartered Accountants in England defines a reserve as 'an amount set aside out of profits and other surpluses which are not designed to meet any liability, contingency, commitment or diminution in value of assets known to exist as at the date of balance sheet.'[5] The ultimate authority to create a general reserve is the general body although it acts on the proposals made by the Board.[6] But the date creating the Reserve is the date of the board resolution.[7] The fact that there is a mass of undistributed profits cannot automatically make it a reserve. The accounts must show whether it is a general or special reserve.[8] The directors while recommending dividend to the shareholders can allocate funds to reserve and intimate the shareholders what they propose to do.[9] The directors cannot recommend dividends but can only recommend the quantum to the general meeting. Once these are approved by the general meeting, the dividend becomes a debt.[10]

The Calcutta High Court held that the procedure of adjourning the annual general meeting cannot be adopted to by-pass the requirements of this section that the balance sheet

1 Gower: Principles of Modern Company Law Sixth Edition page 281 on the pre 1981 position in England.
2 Farrar's Company Law Fourth Edition page 207.
3 R. Mathalone vs bombay Life Assurance Co. Ltd. AIR 1953 S.C. 385; Chunilal Khasalds Patel vs. H.K. Adyaru AIR 1956 S.C. 655; Howrah Trading Co. vs. I.T. Commissioner AIR 1959 S.C. 775.
4 Southern Roadways Ltd. vs CIT [1981] 51 Comp. Cas. 513.
5 'Recommendations on Accounting Principle, No. VI, para 43 as cited in Ramaiya's Guide to the Companies Act 11th Ed. page 667.
6 Southern Roadways Ltd. vs CIT Supra.
7 CIT vs Oswal Woollen Mills Ltd [1981] 51 Comp. Cas. 733.
8 Income Tax Commissioner vs Century Spinning and Manufacturing Company Ltd. AIR 1953 S.C. 501.
9 CIT and Business Profits Tax, Madras vs Vasantha Mills Ltd. [1957] 27 Comp. Cas. 483.
10 Kesoram Industries vs Commissioner of Wealth Tax AIR 1966 S.C. 1370;Vazir Sultan Tobacco Co. Ltd. vs CIT AIR 1981 S.C. 2105.

and profit and loss account must be placed within a certain time.[1] If there is a default in laying the balance sheet before the annual general meeting then this a distinct offence from the one in not calling the meeting in time.[2] The fact that auditors had not sent the same is not a good excuse in India.[3] However, in a Dhaka case, in an application for condonation of delay in holding the annual general meeting a plea was taken that the auditors were not able to prepare the balance sheet in time because there was a dispute with a loan giving agency as to how much money was due and the High Court condoned the delay.[4]

Section 185 provides that the balance sheet shall contain a summary of the property and assets and of the capital and liabilities of the company giving a true and fair view of the affairs at the end of the financial year. These shall be in the form set out in Schedule XI to the Act or as near thereto as circumstances permit. Similarly, every profit and loss account shall also give a true and fair view of the profit or loss of the company and shall comply with the requirements of Schedule XI so far as is applicable. An insurance or a banking company will conform to their own governing laws and it will be enough if they do so.[5]

A statement which lumped together assets valued on one principle with assets valued on another, and tangible with intangible assets, is not a compliance with section185.[6] A clear provision of the Form cannot be whittled down by general consideration as to the object of a balance sheet.[7] A secret reserve must be revealed in the balance sheet and not concealed.[8]

Section 186 requires the balance sheet of a holding company to include certain particulars of its subsidiaries. There shall be attached to every balance sheet of a holding company the balance sheets, profit and loss accounts, reports of directors and auditors of the subsidiary companies. If the persons who are responsible for maintaining the books of account under section 181 do not prepare the balance sheet in the manner required then they may be liable to a penalty as well as imprisonment for six months. A director is not liable however if the complainant does not prove that the company has no professional management such as managing director or manager and also that a particular director was connected with the default.[9] This section is new and corresponds to section 212 of the Indian Companies Act and is aimed at presenting a whole picture of the group enterprise.

Section 187 enables the holding and subsidiary companies to coincide their financial years with the approval of the government. The holding company may by resolution authorise its representative to inspect the books of account kept by any of its subsidiaries.[10]

A balance sheet and the profit and loss account or income and expenditure account shall be signed on behalf of the Board, in the case of a banking company, by the manager or managing agent and by three directors or by all directors if their number is less than three and in the case of any other company by the manager, managing agent or secretary and by not less than two directors including the managing director.[11] Where the presence of the directors in Bangladesh is less than the required number the documents shall be signed by all directors present in Bangladesh and there shall be a statement signed by the directors giving reasons for the non-compliance. The balance sheet and the profit and loss account and the income

1 Bejoy Kumar Karnani vs Asstt.Registrar of Companies [1958] 28 Comp. Cas. 293.

2 See Appaya vs State [1952] 22 Comp. Cas. 78;Viswanathan vs Asstt. Registrar, Joint Stock Companies AIR 1953 Mad. 558 and Registrar vs Subimal Chandra Mallick [1980] 50 Comp. Cas. 770.

3 State vs Linkers Pvt. Ltd AIR 1968 Patna 445;Registrar of Companies , West Bengal vs Proshad [1986] 59 Comp. Cas. 780.

4 Company Matter 13 of 1996:In the matter of Saleh Carpet Mills Ltd-Md. Badrul Haque ...Petitioner; Judgment delivered by Monowaruddin J. on 20.6.96.

5 sub-section 5.

6 Galloway vs Schill Sebohm and Co. [1912] 2 K.B. 354.

7 Shamdassani vs Pochkanwalla AIR 1927 Bom.414.

8 Palmer's Company Precedents,15th Ed.Pt.1, page 716.

9 Registrar of Companies, West Bengal vs S.Prashad, Supra.

10 Section 188.

11 Section 189.

and expenditure account shall be approved by the board of directors before they are signed on behalf of the board and before they are submitted to the auditors.

Section 190 enshrines the other fundamental principle of company law that anybody who wants to deal with a public company may have an idea of its financial affairs by a search at the Registrar's office. This section provides that after the balance sheet and profit and loss account or the income and expenditure account have been laid before a company in an annual general meeting or where such meeting has not been held then three copies of those documents shall be filed with the Registrar's office within thirty days of the meeting or the last day on which the meeting should have been held. The copies shall be signed either by the managing director, managing agent or manager or secretary of the company or if there be none of these, by a director of the company. The copies of the balance sheets, profit and loss accounts etc. shall be accompanied by all the documents which should accompany these balance sheets or profit and loss accounts etc.

In the case of a private company copies of the balance sheet and copies of the profit and loss account shall be filed with the Registrar separately. In the case of a private company which is not subsidiary of a public company, no person other than a member of the company shall be entitled to inspect or to obtain copies of the profit and loss accounts of the company. If the annual general meeting at which the balance sheet and profit and loss account were placed does not adopt the balance sheet or, if the annual general meeting of the company has not been held in any year, a statement of that fact and of the reasons therefore shall be annexed to the balance sheet and to the copies thereof required to be filed with the Registrar. (sub-section 2).If a company makes a default in filing the copies of the balance sheet and profit and loss account then it and every officer of the company who knowingly and wilfully authorises or permits the default will be liable to a continuing penalty not exceeding one hundred taka for every day the default continues. This section has improved on the old section 134 of the Act of 1913 and corresponds to section 220 of the Indian Act and section 127 of the English Act of 1948.

If a general meeting is not held in time then the company does not commit an offence if it does not file with the Registrar copies of the balance sheet and profit and loss account because the responsibility of sending three copies of these documents arise only after the balance sheet and profit and loss account have been laid before the company in the annual general meeting.[1] But see *Bhagirath vs Emperor*[2] where the default to hold the meeting was due to the fault of the director concerned. The prosecution must prove that the offender was a director and also the responsible officer at the relevant time.[3] Failure to comply even after receiving notice from Registrar is wilful default.[4] It is not necessary to file a copy of balance sheet within thirty days of annual general meeting which has been adjourned; it may be filed within 30 days of adjourned meeting if it is held within permissible time limit of 15 months from last meeting.[5] Sections 76 and 133 of the old Act of 1913 created two distinct offences, viz., one for not holding the general meeting and one for not laying the balance sheet before the general meeting. Hence there was no case of the accused being prosecuted twice for the same offence.[6] Where Registrar has issued notice of default to all directors, but gets no response, prosecution may be launched against all directors, as 'officers in default'.[7]

Where directors are deemed to have retired under articles of association , they are not liable to file annual return or balance sheet relating to a period after retirement.[8] In a case under the corresponding section 134 of the Act of 1913 the Calcutta High Court held that the plea that the accounts had been called for by criminal courts and therefore the Company was

1 State of Andhra Pradesh and another vs Andhra Provincial Potteries AIR 1973 S.C. 2429.
2 AIR 1948 Cal 42.
3 Bipin Behari Nayak vs Registrar [1988] 63 Comp. Cas. 271.
4 Registrar vs Orissa Paper Products Ltd. [1988] 63 Comp. Cas. 460.
5 Subal Dutt and Sons vs Assistant Registrar [1986] 59 Comp. Cas. 822.
6 Viswanathan vs Asstt. Registrar AIR 1953 Mad 558.
7 Asstt. Registrar vs Southern Machinery Works Ltd. [1986] 59 Comp. Cas.670.
8 S.R.Y. Ramakrishna Prasad, In re [1963] 33 Comp. Cas 548.

unable to comply with the requirements of section 134, is not a valid excuse and can be of no avail for not filing the balance sheet.[1]

Previously a private company did not have to file copies of balance sheets and profit and loss account with the Registrar. The law allows a member of a private company to inspect or obtain copies of the balance sheet and profit and loss account but what about an alleged member who claims to be a member but those in control of a company denies him that status? These sort of cases are quite frequent and lawyers are often asked to advise an alleged member about their rights to inspect the documents filed by the company. It will be a long time before he goes to the Court with an application for rectification of the share register of the company, succeeds and then is entitled to inspect the balance sheets and profit and loss accounts etc.

Section 191 gives a member a statutory right to receive copies of balance sheets, profit and loss account, auditors report and every other document required by law to be attached to these documents at least fourteen days before the meeting they are to be placed in. Equal right is given to a debenture holder. The member or debenture holder has a right to obtain a copy of the balance sheet and all documents that are required to be attached to it. If default is made in this regard the company and every officer is liable to a penalty not exceeding five hundred taka and the Court, apart from imposing the penalty, may also by order direct that the copy demanded shall forthwith be furnished to the person concerned.

Section 192 requires a company which is a banking company or insurance company or deposit, provident or benefit society to prepare a statement every first day of February and first day of August every year in the form of schedule XII to the Act and that statement together with a copy of the last balance sheet are to be displayed at a conspicuous place in the registered and branch office of the company. Every member and every creditor of the company shall be entitled to a copy of the same on payment of a nominal sum. This section does not apply to a life insurance society or to a provident insurance society to which the provisions of the Insurance Act applies.

14.3.1 The *Dhaka Stock Exchange Limited* in its Listing Regulations has required that a company intending to list and continuing to list should abide by certain rules relating to balance sheets.

Regulation 6 lists the documents to be filed at the time a company applies for listing and includes among these statements of audited accounts for the last five years or for a shorter number of years if the company is in operation only for such shorter period.

Regulation 16 requires every listed company to send to the Exchange its financial results, both in the case of half yearly and annual accounts , in such form as may be prescribed by the Securities and Exchange Commission as soon as these are approved by the company.

Regulation 36(A) provides that when a dividend (interim or final) is declared after the close of a financial year, an announcement shall be made to the Exchange. It shall be accompanied by a statement showing comparative figures of turnover figure, gross operating profit, gross profit, income from other sources, provision for taxation and net profit after taxation. (Sub-regulation(8)). Sub-regulation (9) provides that the company shall make available to the Exchange and to all shareholders in the form set out in half yearly statements before the expiry of one month from the half year period. Such financial statements shall be signed by the chairman or the chief executive and the finance director or in his absence the chief accountant. The company shall make available to the Exchange financial statements before the expiry of 3 months before the end of each financial year even if the figures are provisional and subject to audit. Regulation 37 lists the informations the annual published accounts and report should give. These include a full list of investments held outside the group as investments by the company, holdings in Associates and Subsidiaries with the relative percentage, a distribution schedule of each class of equity, a Directors' Report containing additional informations to those required by the Companies Act,1994, thus probing deep into the financial health of the company.

1 Ajit Kumar Chatterjee vs Emperor [1934] 4 Comp. Cas.54 Cal.

Regulation 41 provides that the Council of Directors of a company should ensure that all the requirements are met on a continuing basis so long as the company remains on the official list of the Exchange. Delay in submission of documents including half yearly reports, annual provisional accounts and audited accounts entail a fine of Taka 500 for every day the default continues.

The Securities and Exchange Commission in its Guidelines on Approval of Prospectus or Offer for Sale of Securities requires an applicant for permission to issue prospectus to submit financial statements and disclosure prepared in conformity with the Companies Act 1994, the Securities and Exchange Rules and the "international accounting standards", and audit thereof to be carried out in accordance with the "international standards of auditing". The terms "international accounting and auditing standards" is, to say the least , vague and does not mean anything other than a true and fair view of the financial state of affairs of the company.

Those Guidelines also require filing of audited balance sheet, profit and loss account and cash flow statement, and notes thereto of the company made upto a date not earlier than six months from the date of prospectus or offer for sale " in conformity with the Companies Act 1994 and International Accounting Standards;". The Auditor's Report shall state the compliance or otherwise of the compliance or otherwise of the requirements of the Companies Act 1994, the Securities and Exchange Ordinance 1969, "the International Accounting Standards, and the International Standards of Auditing".

The Auditor's Report under paragraph 24 of Part II of the Third Schedule to the Companies Act should accompany the application as well as a discussion and analysis of financial condition of the company by the management.

In its "Guidelines for Issue of Capital by Public Companies" the Commission requires that in order to ensure proper issuance of securities by a public company, a company must fulfill certain requirements to obtain consent of the Commission for issue of capital under section 2A of the Securities and Exchange Ordinance. These include filing of Auditor's Certificate or audited financial statements of the Company evidencing the capital already raised by the company. These statements should be for five years or since the incorporation of the company whichever is shorter.

The SEC in its Guidelines on Issuance of Right Shares dated 11 February 1995 provides that if an issuer of right shares which may be renounced in favour of general investors wants to avail of the exemption from obtaining prior consent or recognition from the Commission then it should include certain informations in the "Right Share Offer Document". Included in these are cash flow statement, profit and loss account, balance sheet and notes to the accounts of the issuer made upto a date not earlier than three months from the Document and a statement for profit and loss and dividend for each of the five years immediately preceding the Document or such shorter period during which the issuer was in commercial operation , together with a certificate by the auditors that such accounts have been examined and found correct by them.

14.4.1 The international and our own accounting standards lay stress on the accounts giving a "true and fair view" of the financial affairs of the company. The exact meaning of the phrase is unclear. However , it seems that adherence to normal accounting practice may be a prima facie evidence of giving a " true and fair view ".Thus the claim that accounts were misleading because they included property at original cost rather than at current market value was rejected by an English Court because normal practice had been followed.[1] Charlesworth and Morse in their book on *Company Law*[2] cites an unreported case (the Argyll Foods case) where the company wished to record "economic substance" at the expense of "legal form" and chose, with the agreement of the auditors, to consolidate into its group financial statements for the year ending December 1974 the accounts of a company, even though it did

1 Re Press Caps Ltd.[1949] Ch.434.

2 14th Ed.p. 524.

not acquire full control of it until after the group's balance sheet date. In so doing it was in breach of the Companies Act and Statement of Standard Accounting Practice. The magistrates who heard the case decided that the accounts did not show a true and fair view, and subsequently the Department of Trade and Industry which had brought the prosecution issued a statement interpreting the decision as confirming its view that the "true and fair view override" is confined to the disclosure requirements of the Companies Acts and that it does not enable companies to depart from the other provisions in the Acts. In such circumstances it would seem appropriate where necessary to indicate the underlying economic substance in notes to the accounts or in supplementary proforma statements.

14.4.2 **Disclosure Obligations** – Ford and Austin note that some significant disclosure obligations arise at common law.[1] Consistent with their duty to protect sensitive company information in a competitive society, they are obliged to shareholders to protect and promote a fair and reliable market for shares in the company. It can arise where shareholders need information to make individual decisions about their investments as in the case of a takeover.[2] The same authors note that unless the legislation imposes on directors duties owed to members, or directors assume duties in tort to members, directors owe their duties in relation to information to the company. Directors do not ordinarily stand in a fiduciary relationship to members and their duties in relation to the provision of information cannot be based on any such relationship. But those duties are implicit in the provisions of the Corporations Law underlying the organisation of meetings of members and the constitutional duties of directors in connection with meetings that are imposed by legislation.

Directors who act in good faith have wide latitude in deciding how best to resolve the conflict between the duty to safeguard company interests against competitors and the duty to inform members. But the courts have power to find a breach of duty where the withholding of information or the disregard of members' needs for information is excessive.[3] Directors of a company that has made losses and is insolvent are not entitled to conceal their company's losses.[4]

14.4.3 **Balance Sheet – What is** – The Institute of Chartered Accountants , while giving evidence before the Cohen Committee in England described the function of a balance sheet as an "endeavour to show the share capital , reserves...and liabilities of the company at the date as at which it is prepared and the manner in which the total moneys representing them are distributed over the several types of assets. A balance sheet is thus a historical document and does not, as a general rule, purport to show the net worth of an undertaking at any particular date, of the present realisable value of such items as goodwill, land, plant and machinery, nor, except in cases where the realisable value is less than cost, does it normally show the realisable value of stock-in-trade."[5]

It is clear from a reading of the relevant sections of the Act that a balance sheet and profit and loss account does not become final until these are placed before the general meeting of shareholders and they approve of it.[6] But failure to hold annual general meeting is no defence for default to lay the balance sheet and profit and loss account before the meeting.[7] Where the Registrar condones the delay in holding the general meeting, he must be deemed to have condoned the delay in filing a balance sheet before the general body at its meeting.[8]

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1 Principles of Corporationa Law 7th Ed.para 10.030.
2 Gething vs Kilner [1972] 1 W.L.R. 337; Morgan Crucible Co plc.vs Hill Samuel Bank Ltd [1991] 1 All E.R. 148.
3 Re Castlereagh Securities[1973] 1 New South Wales Law Reports 624.
4 NCSC vs Greater Pacific Investments Pty. Ltd. [1989] 15 ACLR 373,379.
5 Cohen Committee Report para 98.
6 Commissioner of Income Tax vs National Industrial Corporation [1982] 52 Comp. Cas. 535.
7 State of Bombay vs Bandhan Ram Bhandani [1961] 31 Comp. Cas.1 SC; Assistant Registrar vs Mati Begum [1979] 49 Comp.Cas.651 Cal.
8 Ramanujam Applaswamy, In Re [1941] 11 Comp. Cas.177.

There are conflicting decisions regarding power of the Registrar to condone the delay in laying the balance sheet before the general meeting. The Calcutta High Court has held that he cannot condone such delay.[1] But the Madras High Court has held that the Registrar has power to extend even the period of eighteen months relevant to first account.[2]

14.5.1 **Balance Sheet as an Acknowledgments of Debt** – A question is often asked whether or not the inclusion of a debt in the balance sheet amounts to an acknowledgment of the debt by the company.

In *Jones vs Bellgrove Properties Ltd.*[3] it was held that a statement in the balance sheet "to sundry creditors" certain sum of money amounted to an acknowledgment for the purpose of Limitation Act.[4]

The *Jones case* (1949) was not followed in *Re Transplanters Holding Co. Ltd*[5] where the directors had made an acknowledgment in favour of themselves. A balance sheet showing fees due to directors has been held not to amount to an acknowledgment because the directors are all interested to pass a resolution that would bind the company. Also see *Re Coliseum(Barrow)*[6], where the directors being interested, could not vote on the matter, distinguished in *Ledingham vs Bermejo Estancia Co.*[7] where the Board was held to have acknowledged debts in the balance sheet with the authority of the company. In *Re Bharatpur Oil Mills Ltd.*[8] the Court left out the signing of the balance sheet by an interested director while examining whether it was properly authenticated or not. In *Re Compania de Electricidad etc.*[9] the Chancery Division held that the balance sheet must reach the creditor to be effective enough to save limitation. Also see *Shaw vs Shaw*[10] and *Kashinath vs New Akot C.G.& Pressing Co.*[11] where an entry in the balance sheet did not entitle the creditor to sue upon as an account stated because the mere signing of a balance sheet by a director does not make an account stated involving a fresh promise by the director to pay the amount debited to him therein.

It seems that a balance sheet is a good evidence of acknowledgment of any liability of the company but the Courts may be more strict if they find that the directors or those who are in control have taken advantage of their position to write off a debt or confirm a debt in their favour. It may be on technical grounds of the director being interested in the deal and therefore not able to vote on the Directors' Report or on the ground of "fraud-on- minority".

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1 Bhagirath Ch. Das vs Emperor [1947] 17 Comp. Cas.93;

2 Registrar vs Dalmia Cement Ltd.[1954] 24 Comp. Cas. 485.

3 [1949] 2 K.B. 700 C.A.

4 Also see Re Atlantic and Pacific Fibre Importing and Manufacturing Co. Ltd [1928] Ch. 836;Consolidated Agencies Ltd vs Bertram Ltd. [1964] 3 All E.R. 282; [1965] A.C.470(PC);Rajah of Vijanagram vs Official Liquidator [1962] 32 Comp. Cas.1(SC);Re Gee & Co.(Woolwich)Ltd [1975] Ch .52 ;Ledingham vs Bermejo Estancia Ltd[1947] 1 All E.R.749 on whether an entry in the balance sheet amounts to an acknowledgment for the purpose of limitation.

5 [1958] 1 WLR 822

6 [1930]2 Ch.44.

7 [1947] 1 All E.R. 749.

8 [1969] 39 Comp. Cas. 670.

9 [1978]3 All E.R. 668

10 [1935] 2 K.B. 113

11 AIR 1951 Nag 255

AUDITORS

15.1.1 Sections 210-220 of the Companies Act deal with audit and auditors. These sections replace sections 144 and 145 of the Act of 1913.

15.1.2 Section 210 of our Act is different from the previous law in its form and follows section 224 of the Indian Companies Act. An auditor shall be appointed at the annual general meeting with his previous consent and the company shall give intimation to the auditor within seven days of his appointment. The auditor will then inform the Registrar within thirty days whether he has accepted or refused to accept the same. Sub-section (3) makes it very difficult to remove an existing auditor unless he is not qualified for re-appointment or has declined to continue. A resolution removing him and appointing somebody else shall not be passed unless a notice to that effect has been issued prior to the meeting and the resolution has been passed on the ground of death, incapacity or dishonesty or disqualification of the retiring auditor. Sub-section (4) empowers the Government to fill the vacancy if the meeting does not appoint an auditor and it is for the company to tell the Government the fact of the failure to appoint the auditor. Sub-section (6) provides that the first auditor or auditors of a company may be appointed by the board of directors who shall hold office until the conclusion of the first annual general meeting. Such first auditor may be removed and another auditor appointed in his place if he has been nominated by a member and a notice of not less than fourteen days has been given of the nomination before the meeting. The members in general meeting may appoint an auditor if the Board does not appoint the auditor. The Board may fill up a casual vacancy of an auditor except where the auditor resigns in which case the casual vacancy may be filled up by the general meeting.[1] The remuneration of the auditor shall be fixed by the appointing body, i.e., the general meeting or the Board or the Government as the case may be.

The Court may appoint an auditor to audit for past years in an application under section 233 of the Act.[2]

15.1.3 Section 211 lays down the procedure to be followed if an existing auditor is to be removed. This section provides that a special notice is required for removal of an auditor or for appointing somebody else. In the previous law it was made clear that such a notice was to be given by a member *but the current Act does not say who may give such notice.* The company is to send a copy of the notice to the auditor who will have a right to make a representation which may be circulated to the members unless it is too late to do so. The company or any other person aggrieved may approach the Court to stop such circulation on the ground that the representation was defamatory.

15.1.4 An auditor must be a chartered accountant within the meaning of Bangladesh Chartered Accountants Ordinance. Certain persons are prohibited from acting as auditors, e.g., an officer or employee of the company, a debtor to the company for more than one

1 sub-section 7.

2 Md. Faruk vs Abdul Hamid BLD (1998) AD 236= (199) 51 DLR (AD) 48.

thousand taka or a director or the holder of shares exceeding five percent in nominal value of the subscribed capital. If a person is disqualified from acting as an auditor of the holding or subsidiary then he cannot act as auditor for any company of the group.

Section 213 lays down powers and duties of auditors. This section corresponds to section 145 of the Act of 1913. An auditor shall have right of access at all times to the books and accounts of the company and may require any information or explanation from officers of the company. This section lays down certain responsibilities the auditors must perform, namely, enquiry whether loans and advances made by the company on the basis of the security have been properly secured and whether the terms on which they have been made are not prejudicial to the interests of the company or its members. This alone seems to be a formidable task as even the most experienced auditor or lawyer will not be able to comment on the adequacy of the security. Only obvious lapses may be detected. Such enquiry shall also take into account several other matters, e.g., whether transactions of the company represented merely as book entries are prejudicial to the interests of the company or whether in the case of a company not being a banking or investment company assets represented by shares and securities have been sold at a loss or whether loans and advances made by the company have been shown as deposits or whether personal expenses have been charged to revenue account and whether cash has been actually received by the company where shares have been allotted for cash. The auditor is to make a report to be presented in the annual general meeting on the accounts examined by him and on every balance sheet and profit and loss account and whether these give a true and fair view of the company's affairs at the end of the financial year. The stress on having a 'true and fair view' is new and is in conformity of the standard to be had in preparing a balance sheet and profit and loss account.[1]

The power to call for information and explanation from the officers of the company gives the auditor the power to call for informations and explanations from managing and other directors because the definition of an 'officer' in section 2(o) of the Act includes a 'director'.[2]

Section 214 applies the rights of an auditor to inspect the accounts of the company to its branch offices. Section 215 requires that the auditor's report shall be signed only by the auditor so appointed or if the auditor is a firm then by its partners.

The auditor's report is to be read before the company in general meeting and an auditor has a right to attend the general meeting.(sections 216 and 217). The preference shareholders and debenture holders have the same rights to receive and examine the balance sheets , profit and loss account , and the auditor's report as are enjoyed by ordinary shareholders. (section 221).

15.2.1 An auditor plays a vital role in protecting the interests of the public because "if reliance is to be placed on accounts, it is essential that they should be true and fair and that is more likely to be the case if someone independent of the company has vetted them and certified that they are. If, however, that certification is to be relied on, the scrutineer must be competent as well as independent. Hence the Companies Acts have attempted to ensure that company auditors are both."[3]

The Act tries to ensure that auditors are properly qualified. They must be chartered accountants and the Institute of Chartered Accountants have a strict standard for their students which ranks as one of the best in the recognised professions of the country. This was the requirement also in the Act of 1913 . The present Act however improved upon the previous law by inserting provisions that an auditor may not be removed except on the ground of death, incapacity or dishonesty or disqualification of the retiring auditor. (section 210(3)). This ensures that an auditor cannot be removed merely because he may not dance to the tune of the management of the company. However, it may be difficult to prove dishonesty or incapacity on the part of an auditor who will be more likely to commence legal

1 section 185.

2 In re Bhavnagar Vegetable Products Ltd [1977] 47 Comp. Cas. 128.

3 Professor L.C.B.Gower : Principles of Modern Company law 5th. Ed. page 477.

proceedings to clear his name resulting in litigation that may prove far damaging to the company. This is all the more so if in fact the auditor has uncovered facts which put the management into disrepute and the management strikes back to cover their misdeeds. There are complaints that an auditor can in effect, be never removed.

The Act further lays down in detail the specific duties an auditor must perform in doing his job. They must probe into the financial affairs and report on whether the loans and advances were properly secured or not and whether or not transactions of the company which are represented merely as book entries are prejudicial to the interests of the company and whether securities were sold at a price less than they were bought and whether loans and advances made by the company have been shown as deposits or personal expenses have been charged to revenue account and cash has been actually received for shares allotted for cash. (section 213(2)). Also whether the accounts reflect a true and fair view of the state of the companies affairs.[1]

The auditors have thus quite an onerous duty and the Act tries to ensure that they are not hindered in discharging their duties by giving them free access to the books, accounts and vouchers of the company and ask for such information and explanation as he thinks necessary for discharging his duties.[2] An auditor may attend the meeting in which the balance sheet and profit and loss accounts are placed to explain or defend any statement he has made. (section 217). He has to produce his working papers when so ordered by the Court and cannot object on the ground of professional confidence.[3]

15.3.1 **Duties of an Auditor** – In other countries cases have been reported where the standard of duty of an auditor has been examined in the background of the legal requirements . An auditor must not only examine the books to ascertain what the books show, but also to ascertain that the books show the " true and correct representation of the state of the company's affairs."[4]

The Indian courts have held that an auditor should not merely rely on the statement of the management as regards matters which are capable of direct verification by him from books and accounts and vouchers.[5] An auditor is bound to verify the assets of a company himself and not rely on the verification done by persons appointed by the company.[6] In respect of a technical matter an auditor may take the opinion of an expert.[7]

The Supreme Court of India has observed that " the audit is intended for the protection of the shareholders and the auditor is expected to examine the accounts maintained by the directors with a view to inform the shareholders of the true financial position of the company. The directors occupy a fiduciary position in relation to the shareholders and in auditing the accounts maintained by the directors, the auditor acts in the interests of the shareholders who are in the position of the beneficiaries.[8]

An auditor who reports confidentially to the directors the insufficiency of the securities on which the capital is invested and the difficulty of realisation, but who only reports to the shareholders that the value depends on realisation, with the result that the shareholders ignorantly approve an improper dividend, is liable to make good the amount paid. An auditor should not be content with a certificate that securities are in the possession of any person or body of persons, however trustworthy, unless the certificate is given by a person or other person who in the ordinary course of business would usually be entrusted with securities.[9]

Lord Denning described the attitude that an auditor should have thus:

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1 section 213(3).
2 section 213(1).
3 Chantre Martin & Co. vs Martin [1953] 2 All E.R. 691.
4 Stirling J. in Leeds Estate Co. vs Shepherd [1887] 36 Ch.D. 787,802.
5 Controller of Insurance vs H.C.Das AIR 1957Cal 387.
6 Instt. of Chartered Accountants vs Rajaram [1960] 30 Comp. Cas. 67.
7 Registrar vs P.M.Hedge AIR1954 Mad 1080.
8 Instt. of Chartered Accountants vs P.K.Mukherjee [1968] 38 Comp. Cas.628.
9 Halsbury's Laws of England 4th Ed. Vol 7 para 672.

> ...His vital task is to take care to see that errors are not made, be they errors of computation, or errors of omission or commission, or downright untruths. To perform this task properly, he must come to it with an enquiring mind - not suspicious of dishonesty, I agree - but suspecting that someone may have made a mistake somewhere and that a check must be made to ensure that there has been none.... [1]

The duty to state whether in his opinion a true and fair view is given by the balance sheet and the profit and loss account is his personal one and if he has relied on the opinion of the company's accountant and has adopted it without further ado, then the auditor has no cause of action against the accountant in case he is sued by the company for wrongly stating that a true and fair view is given.[2] The extent of an auditor's duty to use reasonable skill and care was well described at the end of the nineteenth century by Lopes L.J. in *Re Kingston Cotton Mill (No 2)*[3] when he said: 'He is a watch-dog, but not a blood-hound'.

Although auditors are not 'blood-hounds' they are expected to have a high capacity to perceive financial irregularities. Thus if the accounts of a company over five years showed profits and dividends were declared and paid each year although in fact, in the first year only a small profit was obtained and in the subsequent years losses were incurred and the discrepancy was due to the fraud of the managing director who falsified the books by including fictitious items in the stock valuation and including expenses incurred in one period into another, the auditors were held to be liable in proceedings brought by the liquidator. Pennycuick J. held that the auditors were put on enquiry by their discovery of invoices altered by the managing director and then should have completely examined all the purchase invoices and informed the board. In this case, the misfeasance proceeding against the managing director was compromised and the auditors were held liable to pay to the company an amount equal to the dividends and the tax paid on the fictitious profits.[4] Where there was material before the auditor to arouse suspicion he should have at least appraised of it in his report to the shareholders.[5] The auditor is appointed by the shareholders to look into the accounts of the company and he should not accept the version given by the directors.[6] Auditors must check that company's securities in fact exist and are in safe custody.[7]

A person exercising any profession or calling will be liable for negligence resulting in failure to exercise due care and skill to any person relying upon his careless advice or information, despite the absence of contractual relationship with him, unless when giving such advice or information he disclaims any personal responsibility.[8] An accountant cannot claim immunity from third party liability except where he acts judicially.[9]

Donovan J. observed in a Canadian case that though the auditor may be only a watch-dog he will not have performed the functions of his office, if after one howl, he retreats under the barn or if he confines his protests to a fellow watch-dog.[10]

While the Act imposes statutory duties on the company and its directors with respect to the accounting and auditing processes it also imposes duties directly on the auditor e.g., to report certain matters in the auditor's report (section 213(3)(d)). In *AWA Ltd. vs Daniels*[11] Rogers J. held that breach of the statutory provision which obliges the auditor to form an opinion on whether the company has kept proper accounting records and to give particulars

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1 Fomento(Sterling Area) Ltd. vs Selsdon Fountain Pen Co. Ltd.[1958] 1 W.L.R.45,61.

2 Dominion Freeholders Ltd. vs Aird [1966] 2 New South Wales Reports 293.

3 [1896] 2 Ch.279.

4 Re Thomas Gerrard & Sons Ltd. [1968] Ch. 455.

5 Registrar vs Arunajatai [1962] 32 Comp. Cas. 1153.

6 Ganesan vs Joscelyne A.K. [1957] 27 Comp. Cas. 114;Trisure India Ltd.vs A.F.Ferguson and Co. [1987] 61 Comp. Cas 548.

7 City Equitable Fire Insurance Co. Ltd. Re [1925] Ch. 407.

8 Hedley Byrne & Co. Ltd vs Heller and Partners Ltd [1964] A.C. 465.H.L.

9 Arenson vs Casson Beckman Rutley and Co. [1975] 3 All E.R. 901 H.L.;JEB Fastners Ltd vs Marks,Bloom & Co. [1981] 3 All E.R. 289.

10 International Laboratories Ltd vs Dewar [1933] 1 Dominion Law Reports 34.

11 [1992] 7 ACSR 759.

of shortcomings, (equivalent provision in our Act is section 213(3)(d)) confers a cause of action on the company for damages which it suffers as a result of the auditor's default.

The Privy Council had a similar view in an appeal from New Zealand in *Deloitte Haskins & Sells vs National Mutual Life Nominees Ltd.*[1] Where an auditor wants to verify a matter by enquiry of the company's officers, care must be used in choosing the appropriate officer. Apart from the obvious need to consider the officer's level of authority in the company, any personal interest of the officer must be taken into account. If the finance manager draws increasingly for personal use, the auditor should have checked with the personal manager whether these were authorised or not.[2]

> The court's standard is the legal standard of care and skill. That standard calls for such reasonable standards as will meet the circumstances of today, including modern conditions of business and knowledge concerning them.[3]

15.4.1 **Breach of Duty and Loss** – Ford and Austin note that " the aim of a court in awarding damages is, in general, to put the injured party, so far as money can do it, in the position he or she would have occupied if there had been no default..." Although there is still some argument about formulation , the weight of authority favours a 'but for' test of causation to be applied in a common sense or practical way: but for the default would the loss have occurred ? Even if a default caused a loss in that sense , the person in default may still not be liable. If it is a breach of contract, the person in default will not be liable if the loss is outside what the contracting parties can be taken to have reasonably contemplated when they contracted. In a case of tort the party in default will not be liable if the loss could not reasonably have been foreseen at the time of the default. Even then, a party in default will not be held liable if the sole cause of the loss was an independent intervening act of another person or event, not being one which the defaulting person had contracted to guard against."[4] In *Columbia Coffee & Tea Pty. Ltd vs Churchill*[5] Rolfe J. of the Supreme Court of New South Wales held that proximity of duty of care could be established in certain circumstances by a potential investor. In *Alexander vs Cambridge Credit Corp Ltd*[6] auditors were found not to have used reasonable care and skill when they failed to detect that values of certain assets were overstated but not held to be liable because the loss was not of a kind that the parties should be considered to have had in their reasonable contemplation when they made the contract for the conduct of the audit. In *Deloitte Haskins and Sells vs National Mutual Life Nominees Ltd*[7] the auditors did not report on the company's insolvency for which the trustee of depositors was held to be liable to the depositors. The Privy Council disagreed with the Court of Appeal of New Zealand and held that even if the auditor had reported at the proper time the trustee would have suffered the loss because the trustee would suspend the operation of the company causing a run on the company. The test was whether had the auditor not been negligent the loss could have been avoided.

In *R Lowe Lippman Figdor and Franck vs AGC*[8] the Supreme Court of Victoria held in a case against an auditor for negligence that a duty of care in a case for negligent wrong statement would lie only when the auditor made the representation to induce the plaintiff to take a particular course of action. This decision will make life much easier for an auditor for then a third party cannot sue the auditor for negligence. The Supreme Court of South Australia however, did think that such an intention to induce the plaintiff to act or not to act

1 [1993] 2 All E.R. 1015.
2 Arthur Young and Co. vs WA Chip and Pulp Co. Pty. Ltd [1988] 13 ACLR 283.
3 See Ford and Austin's Principles Of Corporations Law 7th Ed. section 10.570 where the authors cite a number of cases including Pacific Acceptance Corp Ltd vs Forsyth [1970] 92 WN (NSW), 29; and Northumberland Insurance Co.Ltd.(in liq)vs Alexander [1984] 8 ACLR 882. and other cases.
4 Principles of Corporations Law 7th Ed. section 10.580.
5 [1992] 9 ACSR 415.
6 [1987] 12 ACLR 202.
7 [1993] 2 All E.R. 1015.
8 [1992] 8 ACSR 380.

would not always be an essential ingredient of a claim against an auditor. All the three cases cited above involved claims for damage by a financier against an auditor.[1] In *Galoo Ltd. vs Bright Grahame Murray*[2] the English Court followed the Australian case law, particularly the *Cambridge Credit Corp. case (1987)*[3] and held that although the auditor's negligence had induced the company to borrow and trade unprofitably , it did not cause the debts and trading losses. The Court seemed to infer from the Australian case law that causality was to be determined 'by the application of the Court's commonsense' rather than a strict 'but for' test.

The House of Lords narrowed the common law liability of the auditors in tort when it held that the auditor of a public company's accounts owes no duty of care to members of the public at large who may rely on the accounts in deciding to buy shares in the company. Lord Jauncey observed at page 660 of the judgment[4] :

> (1) that the responsibility for the preparation of accounts giving a true and fair view of the company's financial state is placed fairly and squarely on the shoulders of the directors;
>
> (2) that the role of the auditors is to provide an independent report to the members on the proper preparation of the balance sheet and profit and loss account and as to whether these documents give a true and fair view....Their role is thus purely investigative rather than creative;
>
> (3) that the company's accounts, including the auditor's report, will be furnished to all members of the company as well as to debenture holders and any persons entitled to receive notice of general meetings...to any member of the public who chooses to examine the company's file in the office of the Registrar of Companies.

In *James McNaughton Papers Group Ltd vs Hicks Anderson & Co*[5] the Court of Appeal held that accountants who prepared draft accounts for a takeover bid for consumption of the company was not liable to the acquirer for negligence. However, where an acquirer relied on audited annual financial statements and unaudited half-yearly statements in the course of a contested take over bid and there was a letter circulated by the auditors making forecasts of profits the auditors were held liable to the acquirer because auditors had made express representations in the course of the take over bid.[6] Note that in this case also the Court of Appeal held that auditors did not otherwise have a duty of care to a potential acquirer.

The English Courts thus seem to be strict while determining the standard of an auditor's duty but are lenient while saddling them with liability. An auditor will have to pay for the loss caused by his negligence or omission to attain his standard of duty only where the proximity between the lapse and the loss is not only clear but is its only cause. In any event where the auditor has acted honestly and reasonably the Court may grant relief under section 396 of the Act of 1994.

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1 Esanda Finance Corp. Ltd vs Peat Marwick Hungerfords [1993] 11 ACLC 908.
2 [1994] BCC 319
3 supra.
4 Caparo Industries plc vs Dickman [1990] 2 WLR 358; [1990] 2 A.C. 605, H.L.
5 [1991] 1 All E.R. 134.
6 Morgan Crucible Co.plc vs Hill Samuel Bank Ltd [1991] 1 All E.R. 148.

INSPECTION AND INVESTIGATION

16.1.1 Sections 193-209 of the Act deal with inspections and investigations by the Government into the affairs of a company. The provisions relating to investigations by inspectors appointed under these sections complement the law relating to balance sheets, audit and protection of minority shareholders . However, these provisions are, in practice, used more for personal reasons rather than by the government genuinely seeking to protect the interests of investors in a company.

16.1.2 **Registrar's Power** – Section 193 empowers the Registrar to call for explanation from the company either when there is any objection from a member against a document or when the Registrar is of the opinion that an explanation or information is necessary for obtaining full particulars of the document; then the Registrar may call from the company to produce such books or papers as may be required by him. The officers of the company are obliged to furnish such information or explanation and if they do not do so the Court may on the application of the Registrar and upon notice to the company order such document to be produced as in its opinion may reasonably be required by the Registrar.

On receipt of the information or explanation the Registrar may annex the same to the original document and also may direct the company to correct the documents so that these disclose a full, fair and true statement of the matters to which these relate or report the matter to the government(sub-section 5). If the Registrar thinks on materials placed before him by a member, contributory or creditor or any person interested in the business of the company that the affairs of the company are being carried on in fraud of its members, creditors or persons dealing with the company or for a fraudulent purpose or that the affairs of the company are not being managed in accordance with the Act he may, after giving the company an opportunity of being heard, by a written order, call on the company for information or explanation or to produce any document within a certain time. If upon investigation the Registrar finds that the representation made to him was false he may disclose the name of the informant to the company. For powers of the Registrar under this section see *Coimbatore Spinning and Weaving Mills Ltd vs M.S. Srinivasan.*[1]

16.1.3 Section 194 empowers the Registrar to seize documents by an application to a magistrate of the first class having jurisdiction where upon information the Registrar has reasonable grounds to believe that books and papers relating to a company may be destroyed, mutilated, falsified or secreted. The Registrar will have to return the documents so seized within thirty days after retaining copies or extracts from them.

Section 195 provides that the government may appoint inspectors to investigate the affairs of any company and to report thereon in such manner as the government may direct, if an application is made, in the case of a company having a share capital, by holders of at least one-tenth of the shares issued or in the case of a company having no share capital by at least one-fifth of the members or if the Registrar reports to the Government under section 193(5) discussed above.

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1 AIR 1959 Mad.229.

The investigation under this section is no more than a fact finding mission.[1] Any investigation under this section or under section 197 is not an effective alternative for a winding up petition.[2] The shareholders are entitled to have an investigation into the affairs of the company but the inspector is not accountable to them.[3] Such an investigation will be a comprehensive one and may include the affairs of the company in the hands of the receiver or manager appointed by the debenture holders.[4] It is not necessary that the inspector should hold the investigation himself.[5]

The application by members for investigation must be supported by such evidence as the government may require for the purpose of showing that the applicants have good reasons for requiring the investigation.(section 196).

16.1.4 **Appointment of Inspector** – Section 197 gives the government an independent power to appoint an inspector to investigate the affairs of a company if either the company has, by a special resolution, or the Court, by an order declares that the affairs of the company ought to be so investigated or simply where the government is of the opinion that certain circumstances are prevailing for such investigation. Such circumstances are that the business of the company are being conducted with intent to defraud its creditors, members or for a fraudulent or unlawful purpose or in a manner oppressive to any of its members or if the company was formed for any fraudulent or unlawful purpose, or if the persons concerned in the formation or management of the company are guilty of fraud, misfeasance or other misconduct towards the company or its members, or if the members are being kept in the dark with respect to affairs of the company. Such inspectors shall not be a firm, body corporate or associations.[6]

16.1.5 **Jurisdiction of Court** – The "Court" referred to in section 197(a) is the Court having jurisdiction under section 3 of the Act. Mere allegations are not sufficient to support an application to the Court for appointment of an inspector. The materials before the Court should satisfy the Court that an investigation is necessary into the affairs of the company.[7] A solitary instance of mismanagement already corrected may not justify the appointment of an inspector under this section. The Court will see whether the majority have abided by their fiduciary obligation.[8] After passing an order under this section the Court has no further power to interfere and take further proceedings in the matter.[9]

Sub-section (b) of section 197 gives power to the Government to act under certain circumstances. Under the corresponding provision in India the Company Law Board there now, since 1988, has the power to act for the Government.[10] The Supreme Court of India has held that an order under this sub-section may shake the credit of the company but an investigation under this provision is essentially of an exploratory nature. It is not hit by the provision of any fundamental right under the constitution. However, the words 'in the opinion of the Government' indicate that the opinion must be formed by the Government and of course it is implicit that the opinion must be an honest one and in forming the opinion the government must have before it circumstances suggesting certain inferences like fraud, misfeasance or misconduct or withholding of certain information and an order passed malafide or for dishonest or corrupt purpose is liable to be quashed.[11] An investigation into

1 Raja Narayan Bansilal vs Maneck Phiroz Mistry AIR 1961 S.C. 29.
2 Mool Chand Gupta vs Jagannath Gupta & Co.(P) Ltd AIR 1979 S.C. 1038.
3 R.vs Board of Trade, Ex parte St. Martin Preserving Co. Ltd. [1964] 2 All E.R. 561.
4 ibid.
5 Titagarh Paper Mills Co. Ltd. vs Union of India (1986) 59 Comp.Cas 94.
6 section 198
7 Sumanthy U.A. vs Dig Vijay Chit Fund Ltd. (1983) 53 Comp. Cas. 493.
8 Kusumasursi vs Mathrubhumi Printing and Publishing Co. ltd. (1983) 54 Comp. Cas. 370.
9 In re Nadar Press Ltd.Amritharaj vs Ramaiah Nadar (1968) 38 Comp. Cas. 337.
10 section 237(b) of the Indian Companies Act.
11 Barium Chemicals Ltd. vs Company Law Board [1966] 36 Comp. Cas.639.

the affairs of the company is a very serious matter and it should not be ordered except on good grounds. The appointment of an inspector is likely to receive much press publicity as a result of which the reputation and the prospects of the company may be adversely affected.[1] The investigation hereunder is not the same as referring the matter to police for investigation.[2] This section does not contemplate a roving and fishing enquiry with a view to establishing that there has been a fraud or misconduct or misfeasance. The offence must be there and then the investigation can take place.[3] There should be at least a prima facie case.[4] The government should proceed reasonably in forming the opinion and when exercise of the power by the government is challenged in the writ jurisdiction, the government should place or disclose some materials to justify its action. Allegation that there is a doubt that statutory auditors of company are not acting independently makes out a prima facie case for investigation.[5] An investigation should be carried out quickly and with adroitness and subtlety.[6] Merely because certain companies form a group and there are transactions between these companies, it cannot be presumed that transactions are malafide or entered into with a view to defraud or act in a manner detrimental to some or all of the concerns so as to justify action under this section.[7]

Having allowed inspector to conduct an enquiry and having extended full co-operation to him without challenging validity of his appointment, company cannot be permitted after submission of an adverse report by inspector, to challenge in a writ petition to conduct enquiry.[8] The investigation is not in the nature of a judicial or quasi-judicial nature and it is not essential that the inspector originally appointed should complete the entire work.[9] A report of the inspector is not to be disclosed to the public before its acceptance by the government *Swadeshi Cotton Mills Ltd vs Swadeshi Polytex*[10] but a Court is entitled to look at the report as evidence.[11]

Any evidence used before the inspector may be used in subsequent proceedings by the company or its liquidator to redress wrongs done to the company, e.g., against the company's auditors.[12] The English Courts have further held that the inspector's function is investigatory and not judicial but they must, in view of the consequences which may follow from their report , act fairly and, before they condemn or criticise a person, give him a fair opportunity to answer what is alleged against him.[13] In this case the persons who were required to give evidence were not entitled to see the transcripts of evidence of witnesses. But see Testro *Bros. Pty. Ltd. vs Tait*[14] where the majority of the High Court of Australia held that the inspector need not, before a report on the company's affairs, give the company an opportunity of answering or explaining matters which, if unanswered or unexplained, might give rise to adverse findings or comments in the report.

Lord Denning has observed that the considerations which are to be borne in mind in respect of an enquiry under the Companies Act are :

a) it is a very special kind of enquiry. It is not a trial. There is no accused, no prosecutor, no charge. It is simply an investigation;

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1 Rohtas Industries Ltd. vs S.D.Agarwal [1969] 39 Comp. Cas. 781(S.C.).
2 Indian Express(Madurai)(P.)Ltd. vs Chief Presidency Magistrate [1974] 44 Comp. Cas. 106.
3 Modi Industries Ltd. vs Union of India [1982] 52 Comp. Cas. 589(Delhi).
4 P.Sreenavasan vs Yoosuf Sagar Abdulla & Sons (P.) Ltd. [1983] 53 Comp. Cas. 485.
5 New Central Jute Mills Co. Ltd vs Deputy Secretary [1966] 36 Comp. Cas. 512 (Cal); Deputy Secretary vs Sahu Jain Ltd. [1970] 40 Comp. Cas. 83(Cal).
6 New Central Jute Mills Co. Ltd vs Deputy Secretary [1966] ibid. See also Jiyajeerao Cotton Mills Ltd. vs Company Law Board [1969] 39 Comp. Cas. 856.
7 Ashoka Marketing Ltd vs Union of India [1981] 51 Comp. Cas. 634.
8 Titagarh Paper Mills Co. Ltd. vs Union of India [1986] 59 Comp. Cas. 94(Cal).
9 New Central Jute Mills Co. Ltd. vs Deputy Secretary [1966] supra.
10 [1982] 52 Comp. Cas. 483.
11 Travel and Holiday Clubs Ltd., In re [1967] 2 All E.R. 606 (Ch.D.).
12 London and County Securities Ltd vs Nicholson [1980] 3 All E.R. 861.
13 Re Pergamon Press Ltd.[1971] Ch.388.
14 [1963] 109 C.L.R.353.

b) there is none to present a case to the inspector and he has to do it all by himself;

c) the investigation is in private. This is so because witnesses may say something defamatory of someone else, and it would be quite wrong for it to be published without the party affected being able to challenge it;

d) the inspectors have to make their report. They should state their findings on the evidence and their opinions on the matters referred to them. They should make it with courage and frankness, keeping nothing back. Before they condemn or criticise a person they must act fairly by them.[1]

The House of Lords has held that the government may withhold publication of the inspector's report in the public interest if publication would inhibit a criminal investigation and or prejudice the fair trial of anyone subject to such investigation.[2]

A minority shareholder may use an inspector's report to support his own position to wind up the company on the just and equitable ground.[3] In England there have been instances where the government appointed inspectors to find out about the true ownership of the shares of a company,[4] or for finding out the payments on a take over bid.[5]

Section 199 gives such an inspector appointed by the government the power to investigate into the affairs of any related company, i.e., a member of a group of holding and subsidiary companies as well as a company which was at the relevant time managed by the same managing director, managing agent or manager as the company being investigated by the government. The inspector may also investigate any other body corporate whose board of directors comprise nominees of the company being investigated or is accustomed to act in accordance with the directions of the company, or any of the directors of the company or any company whose directorship is held by any of the employee or nominee of the first mentioned company. A managing agent, managing director, manager or associate of such managing agent may also be investigated by the inspector. However, government permissions may have to be obtained in certain of these cases.[6]

Section 200 entitles the inspector, with the previous approval of the government, to ask for preservation and production of books and documents related to the investigation from officers and employees of the company. The inspector will have to return the books and documents after six months but may call for these again. If the person who is under obligation to help the inspector do his job fails to do so he may face a fine upto five thousand taka or a jail term upto six months. If the inspector apprehends that the books and accounts of the company may be distorted, mutilated or falsified or secreted, he may seize these with the help of the Magistrate.[7]

The inspector shall make a report to the Government and the Government shall forward a copy of the final report to the company and its associates and to any member, managing agent or creditor for a prescribed fee.[8]

If the government is of the opinion that any person is guilty of any offence criminally punishable in connection with the affairs of the company which has been investigated, the government may prosecute such a person.[9]

If the government thinks from the report of the inspector that the company should be wound up it may present to the Court a petition for winding up and/or an application under section 233 of the Act for protection of minority interest.[10]

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1 Maxwell vs Dept. of Trade and Industry [1974] 1 Q.B. 523,533.
2 R vs Secretary of State of Trade and Industry [1989] 1 W.L.R.525.H.L.
3 Re St. Piran Ltd. [1981] 3 All E.R. 270.
4 The Savoy Hotel Investigations in 1953 by Mr. E. Milner Holland Q.C.
5 Re Ashborne Investments Ltd.[1978] 2 All E.R. 418.
6 sub-section 2.
7 section 201.
8 section 202.
9 section 203.
10 section 204.

The government may also bring proceedings for recovery of any property of the company that has been investigated if the damage has been done due to the fraud, misfeasance or other misconduct[1] and also may recover costs of the investigation and other proceedings from those who may be convicted under a prosecution brought under section 203.[2]

A company may itself, by a special resolution, appoint inspectors to investigate its affairs and such inspectors shall have the same powers as a government appointed inspector.

The report of an inspector so appointed either by the company or the government shall be treated as evidence in any legal proceeding as evidence of the opinion of the Registrar in relation to any matter contained in the Report.[3]

The above provisions allow the shareholders of the company and the inspector to investigate into the affairs of the company. They cannot, however, compel the legal adviser to disclose any privileged communication except that of the name and address of his client and the banker of the company as to any information as to the affairs of any of their customers.[4]

The investigation procedures given above supplement the remedies given to an ordinary shareholder if the affairs of the company are being conducted in a manner that is unfair to the interests of the company.

1 section 205
2 section 206.
3 section 208.
4 section 209.

COMPROMISE AND ARRANGEMENTS

17.1.1 Section 228 provides that where there is a compromise or arrangement between a company and its creditors or any class of them, or between the company and its members or any class of them, the Court may, on the application in summary way of the company or of any creditor or member of the company order a meeting of the creditors or members to be called, held and conducted in the manner as the Court directs. If seventy five percent of the creditors or members as the case may be, present or by proxy approve of the compromise or arrangement then it shall be binding on all including the liquidator, if any. The order shall be valid only after a copy has been filed with the Registrar and annexed with every copy of the memorandum. The Court may at any time after the application has been made , stay any proceeding or suit against the company on such terms it thinks fit and proper. This section gives power to the Court to save the company in difficult financial situations.

Section 229 provides that where a petition has been made under section 228 and it is shown that the compromise or arrangement is made in connection with a scheme for the reconstruction of any company or amalgamation of any or two more companies and that under the scheme the whole or any part of the undertaking or property of the company is to be transferred to any other company the Court may, either by the order sanctioning the compromise or arrangement or by any subsequent order, make provision for any of the following :-

a) the transfer to the transferee company of the whole or any part of the undertaking and of the property or liabilities of any transferor company;

b) the allotting or appropriation by the transferee company of any shares, debentures, policies or other like interests in that company, which under the compromise or arrangement are to be allotted by that company to or for any person;

c) the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company;

d) the dissolution of any transferor company but without winding it up;

e) the provision to be made for any person, who, within such time and in such manner as the Court directs, dissents from the compromise or arrangement;

f) such incidental, consequential and supplemental matters as are necessary to secure the reconstruction or amalgamation.

A property transferred under section 229 by the Court may be done free from any charge.

Where a company acquires the shares of another company by way of transfer of shares and if the offer has been accepted by the holders of not less than three fourths in value of the shares the transferee company may give notice to a dissenting shareholder that it desires to acquire his shares. The transferee company will be then bound and entitled to acquire the shares of dissenting shareholders on the same terms on which under the scheme or contract the shares of the approving shareholders are to be transferred to the transferee company. This section in effect enables shareholders who command seventy five percent of the shares of the company to come to an arrangement with another company to acquire their and the shares of

the minority shareholders if the minority shareholders do not command more than twenty five percent shares. The minority shareholders can of course protest to the Court if they can prove that the scheme is really to acquire the shares of the minority or to reduce their percentage in the transferee company. Ordinarily, when fresh shares are issued all shareholders are to be given the offer to buy the shares pro rata. This is because the legislature intends that if shares are issued , all existing shareholders will get an equal chance to take these new shares. However, if the shares of a company are transferred to another company formed separately by the majority shareholders commanding 75% majority in value then the shares of the transferor company may be transferred to that company pursuant to a scheme thus diluting further the minority shareholders.

17.1.2 These sections relating to schemes under compromise and arrangement correspond to sections 425 – 427A of the English Companies Act 1985 and sections 206 – 208 of the English Companies Act 1948. Section 228 of our Act can be used whether the company is a going concern or is in the course of winding up. It will not , for example, be necessary where it is desired to alter rights attached by the articles to a class of shares where the articles provide a method for the variation of such rights. On the other hand, if no provision exists enabling the company to vary the rights attached to a class of shares , it will only be possible effectively to alter any such rights either with the consent of every holder of the shares whose rights are to be varied or following the procedure laid down in section 71 of the Act or by means of a scheme of arrangement under section 228. Section 10 does not prohibit an alteration of special rights by this procedure.

The utility of sections 228 and 229 is more evident when creditors are concerned. Prima facie no creditor can be bound by the agreement of the company with the other creditors or by an agreement between the latter. A compromise approved by a great majority of creditors might be rendered ineffective if a comparatively small creditor were to object . It is one of the purposes of section 228 to meet this situation.

The effect of a scheme under this section is 'to supply by recourse to the procedure thereby prescribed , the absence of that individual agreement by every member of the class to be bound by the scheme which would otherwise be necessary to give it validity.'[1]

Palmer's Company Law cites examples of the working of this section.[2] Thus, by means of this section a scheme has, e.g., been effected where creditors were required to give up their security and where their debts were replaced by fully paid shares of the company.[3] Similarly, creditors who were not willing to accept as their debtor a company to whom their debtor company's assets were transferred under a scheme , were bound to accept a composition.[4]

The section applies to "compromises" or "arrangements". In *Sneath vs Valley Gold, Ltd.*[5] and in other cases it was held that there can be no compromise unless there is some dispute, e.g., as to the power to enforce rights or as to what those rights are.

No such limitation applies to an "arrangement". In *Mercantile Investment and General Trust Co. vs International Co. of Mexico.*[6] Fry L.J. said that "the power to compromise does not include the power to give up one chose in action, namely, a secured debenture, in exchange for another chose in action of a totally different kind, namely, a preference share, in the absence of all disputes as to the rights of the creditor, of all difficulty in enforcing those rights , and of any suggestion that the full fruits of these rights could not be obtained. Such a transaction might be described as an exchange, possibly as a barter, or an arrangement."

The section does not extend to arrangements which are ultra vires the company , nor where – as in the case of a reduction of capital – the Act provides that a specified procedure must be followed to make a transaction effective, that procedure cannot be evaded by means

1 Younger J. in Re Guardian Assurance Co.[1917] 1 Ch. 431,441.
2 20th Ed. p.664.
3 Re Empire Mining Co. [1890] 44 Ch.D. 402.
4 Re Brownfield Guild Pottery Society [1898] W.N. 80.
5 [1893] 1 Ch.477
6 [1891] 1 Ch. 484

of a scheme under this section.[1] If, however, the normal procedure is followed, no difficulty arises, thus in one case a reduction of capital, a subsequent increase, and a stay of a winding up were all dealt with in a scheme.[2]

17.1.3 The first step is a summons to the court asking the court to convene the necessary meetings. This application is normally made by the company but any creditor or member may do so and a proceeding under this section may be commenced against the company's wishes. The court does not itself consider at this point what classes of creditors or members should be made parties to the scheme. That is for the petitioner to decide, in accordance with what the scheme purports to achieve. If, for example, rights of ordinary shareholders are to be altered , but those of preference shareholders are not touched, a meeting of ordinary shareholders will be necessary but not of preference shareholders. It is however necessary for at least one class meeting to be held in order to give the court jurisdiction under this section. If meetings of the proper classes have not been held, the court may not sanction the scheme. In *Sovereign Life Assurance Co. vs Dodd*[3] Bowen L.J. said at page 583 :

> It seems plain that we must give a meaning to the term 'class' as will prevent the section being so worked as to result in confiscation and injustice, and that it must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.

In that case the court found that persons whose interests were dissimilar had been treated as a single class and it refused to sanction the scheme.

17.2.1 The question of what constitutes a creditor and what constitutes a class of creditors may present certain difficulty. In general any person having a pecuniary claim against the company capable of estimate is a creditor. Creditors can be divided into three categories of preferential creditors, secured creditors and unsecured creditors. Those who have a common security, e.g., holders of debentures ranking pari passu will comprise a class; but where each of a number of creditors have similar though not common security the position may not be the same.[4]

17.3.1 **Exercise of Court's Discretion** – The application for the Court's approval is made by petition of the applicants and may be opposed by members and creditors who object to the scheme. The duties of the court are, first, to see that the resolutions are passed by the statutory majority in value and number at a meeting or meetings duly held and then to see whether the proposal is such that an intelligent and honest man, a member of the class concerned and acting in respect of his interests might normally approve.[5] The same judge (when he was Lord Maugham) said in *Carruth vs I.C.I.*[6] that too much weight should not be placed on majority votes when it can be shown that " the majority of the class has voted, or may have voted, in the way it did because of its interests as shareholders of another class." Thus Templeman J. did not approve of a scheme of arrangement, by holding that proper meetings had not been convened and held because a wholly-owned subsidiary of the transferee company already holding 53% of the shares to be acquired should not have been regarded as a member of the same class as the other shareholders and accordingly the court had no jurisdiction to sanction.[7]

Palmer points out[8] citing old decisions that the court has no power to usurp the right of the class of members or creditors to decide whether they approve the scheme; if, therefore, a class whose interests are affected by a scheme neither assents to the scheme nor approves it at a meeting in accordance with the section, the court cannot confirm the scheme even if it

1 Palmer ibid. page 665.
2 Re Stephen Walter & Sons [1926] W.N. 236 discussed in Palmer,ibid.
3 [1892] 2 Q.B. 573.
4 Palmer 20 Ed. .page 668.
5 Maugham J. in Re Dorman Long and Co. [1934] Ch.635.
6 [1937] A.C.707,769.
7 Re Hellenic Trust Ltd.[1976] 1 W.L.R. 123.
8 20 Ed. at page 669

considers that the class concerned is being fairly dealt with, or that it would approve the scheme. The court will not, however, upset a scheme for minor irregularities, as where consent of a class has been subsequently obtained , and where the necessary majority of one class was absent when the petition was presented, the court allowed a fresh petition to be presented subsequently when the necessary majority was later obtained, without requiring the other class meetings to be held again. The court must also be satisfied that those who attended the meeting are fairly representative of the class and that the statutory majority did not coerce the minority in order to promote interest adverse to those of the class whom they purport to represent. If for instance there were altogether 1000 shareholders holding 10,000 shares in all , the court would be unlikely to be satisfied by the statutory majorities at a meeting at which 10 members holding 100 shares in all were present and voted.[1]

The fact that the scheme is approved by the statutory majority is a strong indication that it is a fair one. But if it is shown that a substantial proportion of that majority are in a position to gain more from the scheme than other members of the class by reason of their interests in some other capacity, then the court may have a different view. Thus where creditors are to give up something in favour of shareholders , and some of the creditors are also shareholders, the interests of those persons as shareholders may be sufficient to obtain for them a greater benefit in that capacity than they sacrifice as creditors.[2]

At the turn of the twentieth century, Lindley M.R. said that the power must, like all other powers , be exercised subject to those general principles of law and equity which are applicable to all powers conferred on majorities and enabling them to bind minorities. It must be exercised, not only in the manner required by law, but also bonafide for the benefit of the company as a whole, and it must not be exceeded. These conditions are always implied, and are seldom if ever, expressed.[3] The House of Lords held in *Adelaide Electric Co. vs Prudential Assurance*[4] that the alteration in the place of payment from England to Australia did not vary the rights of shareholders notwithstanding that the Australian currency unit was worth less than the British Pound. Professor Gower cites cases where interferences with shareholders' rights were not held to be actionable at law.[5] Thus, when preference shares were non participating as regards dividend but participating as regards capital, a capitalisation of undistributed profits in the form of a bonus issue to the ordinary shareholders was not a variation of the preference shareholders' rights notwithstanding that the effect was to deny them their future participation in those profits on winding up or reduction.[6] A reduction of capital by repayment of irredeemable preference shares in accordance with their rights on a winding up was not regarded as a variation or abrogation of their rights.[7]

An amalgamation cannot be used to by-pass other statutes. If the laws of tenancy are affected by amalgamation of two companies whereby the transaction was held to be a transfer of the tenancy without the sanction of the landlord then the transferee company would be liable to be evicted.[8]

An application under this sub-section can be made by a creditor or member even in the case of a company in winding up.[9]

Schemes of compromise and arrangement can only transfer such rights , powers, duties and property as are capable of being lawfully transferred by a party to the scheme if no section of the Companies Act existed. If any part of the scheme includes anything which the parties cannot bind themselves to do then that part of the scheme has to be treated as a

1 Palmer ,ibid.
2 Re Wedgewood Coal and Iron Co. [1877] 6 Ch.D. 627.
3 Allen vs Gold Reefs of West Africa Ltd.[1900] 1 Ch. 656, 671.
4 [1934] A.C. 122.
5 Principles of Modern Company Law (5th Ed.)p.542.
6 Dimbula Valley Tea Co.vs Laurie [1961] Ch.353. Re Mackenzie and Co.Ltd [1916] 2 Ch.450.
7 Scottish Insurance Corp. vs Wilson and Clyde Coal Co. [1949] A.C. 462 H.L.;Prudential Assurance Co. vs Chatterley Whitfield Collieries [1949] A.C. 512 H.L. and Re Saltdean Estate Co. Ltd. [1968] 1 W.L.R. 1844; House of Fraser vs AGCE Investments Ltd.[1989] A.C. 387.
8 General Radio and Appliances Co.Ltd vs M.A.Khader AIR 1968 S.C. 1218.
9 In re Travencore National and Quilon Bank [1939] 9 Comp. Cas.14: AIR 1939 Mad 318.Rajendra Prasad Agarwalla vs Official liquidator [1978] 48 Comp. Cas. 476.

nullity.[1] The word "arrangement" in this section is liable to be treated widely. When a proposed scheme affected the contractual relationship subsisting between the companies and its members by requiring the company to register a third party applicant in place of existing members as the holder of the company's shares, the scheme was an arrangement.[2] A surety is not affected by an arrangement between the company and the creditors.[3]

A scheme may be open to criticism but unless it is shown to be unfair the court will not interfere.[4] The section gives the Court the widest discretion to approve any sort of arrangement between the company and its shareholders.[5]

The court should be satisfied that the resolution is passed by the statutory majority, that those who took part in the meeting are fairly representative of the class that the scheme as a whole, is a reasonable one and there is no lack of good faith on the part of the majority.[6]

In Halsbury's Laws of England[7] the authors discuss "reconstruction" and "amalgamation" and comment that neither of these two words has any precise legal meaning. Where an undertaking is being carried on by a company and is in substance transferred , not to an outsider, but to another company consisting substantially of the same shareholders with a view to its being continued by the transferee company, there is a reconstruction. It is none the less a reconstruction because all the assets do not pass to the new company, or all the shareholders of the transferor company are not shareholders in the transferee company, or the liabilities of the transferor company are not taken over by the transferee company. "Amalgamation" is a blend of two or more existing undertakings into one undertaking ; the shareholders of each blending company becoming substantially the shareholders in the company which is to carry on the blended undertakings. There may be amalgamation by the transferor of one or more undertakings to an existing company.

The court has been given wide powers to give directions or modify the compromise or arrangement for its proper working and that a mere discussion by shareholders of proposed modifications at a properly requisitioned meeting would not affect either the scheme or the court's powers.[8]

In approving a scheme of reconstruction and amalgamation the court is bound to consider the proposals and decide whether they are fair and reasonable taking everything into consideration.[9]

On the question of acquisition of the shares of the dissenting minority it has been said that a valuation of shares is only an expression of opinion, and it may be made on one or other or more of a number of bases but the final test of the value of a thing is what it will fetch if sold. Where shares are quoted on the stock exchange the stock exchange markings are a satisfactory indication of the value of the shares.[10]

The valuation must be on the basis of a going concern and not on a break up valuation.[11] Where a large majority of shareholders have approved of a valuation the burden is upon the petitioner to prove unfairness.[12] The valuation can be attacked not only on the ground of fraud but also for arithmetic mistake or miscarriage of justice e.g., if the figure itself was so extravagantly large or so inadequately small that the only conclusion would be that there was some error.[13]

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1 Re Skinner [1958] 3 All E.R. 273; Nokes vs Doncaster Amalgamated Collieries Ltd.[1940] 3 All E.R. 549 HL;Re "L" Hotel Co. Ltd.[1946] 1 All E.R. 319.

2 Re Savoy Hotel Ltd. [1981] 2 All E.R. 646,657.

3 Punjab National Bank Ltd vs Vikram Cotton Mills Ltd. [1970] 40 Comp. Cas.927(SC).

4 In re Sussex Brick Co. Ltd [1960] 2 W.L.R. 665; M.G. Investment and Indusrial Co. Ltd. vs New Sharrock Ltd. [1972] 42 Comp. Cas. 145.

5 Re National Bank Ltd. [1966] 1 All E.R. 1006(Ch.D.).

6 In re Coimbatore Cotton Mills Ltd and Lakshmi Mills Co. Ltd [1980] 50 Comp. Cas.623,630.(Mad).

7 4th Ed. Vol VII para 1539

8 Pravin Kantilal Vakil vs Rohini Ramesh Save[1985] 57 Comp. Cas. 31 (Bom).

9 See Bengal Bank Ltd vs Suresh Chakravarthy [1951] 21 Comp. Cas. 315(Cal);In re Bengal National Textile Mills Ltd. [1986] 59 Comp. Cas.956 (Cal).

10 Re Press Caps Ltd [1949] 1 All E.R. 1013(CA).

11 Jones vs Jones [1971] 2 All E.R. 676.

12 In re Grierson etc.[1967] 1 All E.R. 192.

13 Dean vs Prince [1954] 1 All E.R. 749. Burgess vs Purchase and Sons Ltd.[1983] 2 All E.R.

CONVERSION OF PRIVATE COMPANY INTO PUBLIC COMPANY

18.1.1 Section 231 of the Companies Act provides for conversion of private company into public company.

18.1.2 If a company alters its articles of association so that these do not contain the special provisions relating to a private company as are by section 2(1) of the Act required for the formation of a private company and if the company has seven members then it shall be a public company from the date of the alteration. It shall within a period of thirty days from the date of the alteration file with the Registrar either a prospectus or a statement in lieu of prospectus containing the particulars set out in Parts I and II of Schedule IV subject to the provisions contained in Part III of that Schedule. In case of an untrue statement in that document the person who authorised the issue of such a document shall be punishable with imprisonment for upto two years or with a fine of upto five thousand taka or with both unless he can show that upto the time of issue of the prospectus he had reasonable ground to believe that the statement was true. Such a statement shall be deemed to be untrue if it is misleading in the form and content in which it is included or there is an omission which is calculated to mislead.

Although the section does not say so it is obvious that the prospectus or the statement in lieu of prospectus shall give a true and fair view of the affairs of the company as in the case of a regular prospectus since those documents must conform to the requirements of the Schedule IV of the Act.

18.1.3 Section 232 provides for amendment of articles for conversion of a public into a private company by excluding the articles which relate to a public company and include therein provisions relating to a private company. Prior to this the written consent of secured creditors will have to be obtained and the shares will have to be delisted if these are quoted in the stock exchange.

PROTECTION OF MINORITY SHAREHOLDERS

19.1.1 Section 233 of the Companies Act reflects the concept that has swept the entire corporate world in the last fifty years, namely that those who are not in the control of management of the company should have a direct mode of complaint to the Court if they can show that the affairs of the company are being run in a manner which is prejudicial to the interests of the company. This section has been inserted in our company law after a long felt need for enabling the Court to interfere if it finds that the majority in the company are operating in a manner that is oppressive to the interests to the minority. The genesis of this section is section 210 of the English Companies Act 1948 which provided an alternative remedy to winding up in cases of oppression. This provision gave any member of the company the right to petition the Court that the affairs of the company were being runin a manner oppressive to some part of the members including himself and the Court, if it found that the allegation was true but that to wind up the company would unfairly prejudice those members but otherwise the facts would justify the making up of a winding up order on the ground that it would be just and equitable that it should be wound up and then the Court might, with a view to bringing to an end the matters complained of, make such order as it thinks fit, whether for regulating the conduct of the company's affairs in future, or for the purchase of the shares of the company by other members of the company or the company itself. The Court could also make an alteration or addition to the company's memorandum or articles of association and these changes could not be altered by the company without leave of the Court.

Section 397 of the Indian Companies Act follows the English law and provides that any members of a company who complain that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members including any one or more of themselves may apply to the Company Law Board (until 1988 this was to be made to the Court) provided such members constitute one tenth of the number or issued share capital of the company and if the Board is of the opinion that the allegation is true and that to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding-up order on the ground that it is just and equitable that the company should be wound up then the Board may, with a view to bringing to an end the matters complained of, make such order as it thinks fit.

19.1.2 Section 233 of our Companies Act essentially follows the Indian law although it is pretty certain that the Courts will look to the English decisions given after 1948 when examining whether in law the Court should interfere in a case where this section is invoked for a direction to protect interests of the minority. Section 233 follows the Indian requirement that the applicants to the Court must show, in case the company has a share capital that they have one-tenth of the shares issued , or in case that the company does not have a share capital that they comprise not less than one-fifth of the number of persons registered as members. This requirement of having a minimum number of shares or members is to prevent frivolous applications being made but may result in hardship where shares are quoted in the stock

exchange and are dispersed. The applicants may either individually or jointly bring to the notice of the Court that–

(a) the affairs of the company are being conducted or the powers of the directors are being exercised in a manner prejudicial to one or more of the members or debenture holders or in disregard of his or their interest;

(b) the company is acting or is likely to act in a manner which discriminated or is likely to discriminate the interest of any member or debenture holder;

(c) a resolution of the members, debenture holders or any class of them has been passed or is likely to be passed which discriminates or is likely to discriminate the interest of one or more of the members or debenture holders and pray for such order as necessary for safeguarding his or their interest and also the interest of any other member or debenture holder.

The Court shall, on receipt of the application, shall send a copy thereof to the Board of the Company. After hearing the parties, if the Court is of the opinion that the interest of the applicant has been or is likely to be prejudiced then it may make such order as it thinks fit including a direction to cancel or modify any resolution or transaction or to regulate the conduct of the company's affairs in future in a specified manner or amend any provision of the memorandum and articles of association.

Where the Court has ordered amendment of the memorandum and articles of association of the company, the company shall not, without leave of the Court, make any amendment therein or take any action which is inconsistent with the Court's direction.

The company shall within fourteen days from the making of an order under section 233, inform the Registrar in writing of such order and send him a copy thereof . In default the company and every officer of the company who is responsible for the default shall be liable to a fine not exceeding one thousand taka.

19.2.1 The Bangladesh law differs from Indian, English and Australian law (section 260 of the Australian Corporations and Securities Legislation) in that those laws require the applicants to show that the affairs of the company or the act complained of are likely to cause 'unfair prejudice' to the petitioners whereas the Bangladesh law speaks of only 'prejudice' to the petitioner. This, in theory, means that the Bangladesh Court should be under less restraint in using the power under this section. Further, Bangladesh law permits an action to be brought when there is discrimination regarding the interest of any member or debenture holder. The Australian law mentions that an act or resolution of the company, if is 'unfairly' discriminatory, may cause the Court to interfere. The Indian law does not mention anything about discrimination nor does the English law but it is clear that if discrimination is proved then that would tantamount to oppression on members.

19.2.2 There have been only a few reported decisions upto writing of this manuscript on the application of section 233 in Bangladesh. The decisions in other countries will no doubt be closely followed by the High Court Division here and we propose to discuss those decisions to get an idea of the possible interpretation the Court will give our statute.

19.2.3 **Who can Apply** – Section 233 read with section 195 means that holders of one-tenth of shares in the case of a company having a share capital and in the case of a company not having a share capital one-fifth of the members are eligible to apply. While in England and Australia any shareholder can apply, Bangladesh has followed the Indian principle and has restricted the right to apply to a minimum ten percent shareholdings presumably to avoid unnecessary litigations. In western countries the court costs awarded to the winner are adequate and the loser will be faced with a heavy burden thus discouraging frivolous applications. In this country where court costs are not awarded adequately any shareholder can start a series of litigations and cause the company a lot of trouble. However, this detracts from the main rationale behind the section, namely to protect the minority shareholders

whatever their shareholdings may be. It is illogical to say that a minority has no right to protect itself unless it is at least 10% minority. The Calcutta High Court has held that majority can apply for relief under this section.[1] Dhaka High Court has held that unless the applicants are minority shareholders, i.e., less than fifty percent, they have no right to apply for protection under this section.[2] In another case between the same parties another judge observed that cause of action in a matter under section 233 is recurrent.[3]

The language of the section is clear that the applicant must be a shareholder of the company. What happens if the personal representatives of a deceased shareholder wants to complain ? Pennycuick J. made an obiter in *Re Jermyn Street Turkish Baths Ltd*[4] that even without registration as members, the personal representatives of a deceased member had to be regarded as members of a company for the purposes of an application to protect minority shareholders rights. However, in view of the requirement that in order to become a shareholder a person's name has to be entered in the share register (section 32(2)) it is doubtful whether a person whose name has not been entered on the share register can directly apply under this section. To obviate this difficulty section 459(2) of the English Companies Act extends the application of section 459(1)' to a person who is not a member of a company but to whom shares in the company have been transferred or transmitted by operation of law, as those provisions apply to a member of the company; and reference to a member or members are to be construed accordingly'. The Bangladesh Companies Act should, but does not, have such a provision.

An application under this section is representative in character and shareholders have right to be added as party to the proceeding.[5] When a shareholder's rights as a director are affected an application under this section is maintainable.[6]

19.2.4 Having established the locus standi, the petitioner must show that the company's affairs are being, or have been , conducted in a manner which is prejudicial to one of its members or there is discrimination regarding the interests of a member or debenture holder. Whereas sub-section 1(a)and (b) contemplate conduct of a continuing nature sub-section (c) speaks of a resolution that may discriminate or is likely to discriminate the interest of one or more of the members. Section 210 of the English Companies Act 1948 contemplated conduct of a continuing nature but the House of Lords said in Scottish Co-operative Wholesale Society vs Meyer[7] that the court in construing this section had to have regard to business realities and not legal technicalities.

19.2.5 **Affairs of the Company** – There is no definition of what constitutes the 'affairs' of the company in section 233. It has been held to be a phrase with a 'wide' meaning and to be capable of covering a company's 'good will, its profits or losses, its contracts and assets including its shareholding in and ability to control the affairs of a subsidiary, and perhaps in the latter regard a subsidiary...'.[8] In *Re BSB Holdings Ltd*[9] the transfer of broadcasting business which was originally carried out by the parent company to its wholly owned subsidiary and the subsequent merger of the subsidiary with a third company was held to be conduct in the affair of the parent company. In the case of *Re a Company exp. Nicholas (No 002470 of 1988)*[10] the Court of Appeal held that the withholding of money owed to a subsidiary company by a parent company that exercised financial control over it could

1 Ramashankar Prasad vs Sindhri Iron Foundry (P) Ltd AIR 1966 Cal 512.
2 Moksudur Rahman vs Bashati Property Development Ltd 49 DLR (1997) 539.
3 Moksudur Rahman vs Bashati Property Development Ltd. 3 BLC (1998) 224.
4 (1970) 1 W.L.R. 1194, reversed [1971] 3 All ER 184
5 Pramod Kumar Mittal vs Andhra Steel Corporation Ltd. (Cal) [1982] 2 Comp.L.J.629,655.
6 In re Albert David Ltd. 68 CWN 163.
7 [1959] A.C 324,343
8 Morgan vs Flers Avenue Pty. Ltd [1986] ACLR 692,704 : a case of section 260 of the Australian Corporation Law , 1989).
9 (1992) BCC 915
10 [1992] BCC 895

constitute acts done in the conduct of the subsidiary's affairs. In *Re a Company* (No. 001761 of 1986)[1] the judges made a distinction between conduct in the company' and conduct dehors the company'. Conduct such as being 'rude, domineering, disruptive and aggressive towards customers and members of staff of the company' or asking ' the secretary to park the director's car ' or even to request transfer of their shares to her and to resign as directors ' are acts in personal capacity and *de hors the company*. The principal allegation of unfair prejudice was that the respondent, a shareholder in the company, had, without informing the other shareholders, paid off the company's bank loan and had taken a transfer of the bank's security. This was held by Harman J. as an act in the personal capacity. The judge further commented that if a director stole cash from the company's safe, it would be an act dehors the company'. *It would, however, be otherwise if the director in question used his dominant position in the company to stifle any proceedings by the company against himself which will then constitute an 'affair of the company'.*

In *Scottish Co-operative Wholesale Society Ltd vs Meyer*[2] Viscount Simonds, Lord Denning and Lord Morton all agreed that the inaction of directors who knew of damaging course of conduct by a shareholder (a course of conduct which if called to the company's attention , the company would probably have been able to ratify), was conduct in the affairs of the company and oppressive.

In *Re Stewarts (Brixton) Ltd.*[3] a director's conduct in setting up a rival business and/or channeling work which rightfully belonged to the company to the new company in breach of his fiduciary duties to the company was held to be misconduct in relation to the affairs of the company.

What happens when a person is appointed to the board of directors of a company by another company ? In *Morgan vs 45 Flers Avenue Pty. Ltd.*[4] the court held that such a director would not be acting in the affairs of the appointing company when voting at the board of directors of the company to which he was appointed. This is of special importance in our country where the Government or statutory corporations quite often appoint their representatives in the board of a company where they have some stake.

Also see *Charterbridge Corporation Ltd vs Lloyds Bank Ltd.*[5] The director must consider the interests of the company of which he is a director and not the company appointing him. However, this seems to be an unrealistic attitude in the case of group companies because the economic reality of group activity should be recognised. This section may apply to a receiver of a company.[6]

19.3.1 **Act or Omission of Company** – Before a proposed act justifies relief under this section, the act or omission complained of must be implemented or about to be implemented. A mere discussion will not do.[7]

The act must be that of the company i.e., the Board.[8]

The acts of shareholders with respect to matters over which they had exclusive competence would be the acts of the company.[9] However, acts of shareholders in general meeting in matters other than those within their exclusive competence are not treated as those of the company. In the *Northern Counties case*[10] Walton J. agreed with submission of counsel that when the members of the company assembled in a general meeting pass resolutions these are resolutions by members of the company, and not by the company itself.[11]

1 [1987] BCLC 141
2 [1958] 3 All E.R.66
3 [1985]BCLC 4
4 [1986] 10 ACLR 692
5 [1969] 2 All E.R. 1185.
6 Ex p. St.Martins Preserving Co. Ltd. [1965] 1 Q.B. 603.
7 Re a Company (No.004475 of 1982) [1983] Ch. 178.
8 Automatic Self-Cleansing Filter Syndicate Company Ltd vs Cunninghame [1906] 2 Ch.34, Salmon vs Quin & Axtens Ltd. [1909] 1 Ch.311, Breckland Group Holdings Ltd vs London & Suffolk Properties Ltd. [1989] BCLC 100.
9 Northern Counties vs Jackson and Steeple [1974] 1 W.L.R. 1133 at 1143.
10 ibid
11 ibid at 1144.

19.3.2 Initially it has been held that the oppression to the complainant had to be suffered by him in his capacity as such and not for example, as a director or creditor.[1] In the Harmer case cited above although Jenkins L.J. agreed in principle with the qua member requirement, he said that the sons as members, and not merely as directors, were oppressed by the father's autocratic conduct and the fact that the oppressed members were also directors was not a disqualifying circumstance.

It is not clear whether any breach of articles could constitute as oppression to members although it is probably true that certain breach of articles could be oppressive to members in the capacity of members. In our law although section 233 does not speak of oppression, yet the word prejudice will be applicable in its place.

However, in *Re a Company (No 002567 of 1982)*[2] Vinelott J. held that though the petitioner's rights as a shareholder was not affected yet his right to participate in the management of the company under the agreement and to be paid remuneration was a matter to be redressed under this section. In *Re a Company (No.00869 of 1985)*[3] Hoffman J. said that he found the distinction between members and outsider rights difficult to follow. However, in *Re a Company (No. 00477 of 1986)*[4] the same judge while accepting that the interest of members as members must be prejudiced against, went on to quote Lord Wilberforce in Re Westbourne Galleries[5] that 'there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals with rights, expectations and obligations inter se which are not necessarily submerged in the company structure'. The member's interests as a member who has ventured his capital in the company's business may include a legitimate expectation that he will continue to be employed as a director, and his dismissal from that office and exclusion from the management of the company may therefore be 'unfairly' prejudicial to his interests as a member.

In *Re Ringtower Holding plc.*,[6] Peter Gibson J. said that a member had an expectation that the company's affairs would be conducted in a particular way. However, his interest as member depends on, inter alia, proof of a legitimate expectation.[7]

19.4.1 **Prejudice and Petitioner's Legitimate Interests** – The English Act mentions 'unfair prejudice' to the members. Our Act mentions only 'prejudice' to the members. This means that the petitioner in Bangladesh should be put to less rigorous proof of fraud or oppression on minority. In *Re a Company(No. 00477 of 1986)*[8] Hoffman J. cited the case of *Re Westbourne Galleries Case*[9] and pointed out that the member's rights under the articles of association and the Companies Act could be treated as an exhaustive statement of his interests as a member. Further equitable considerations might arise, e.g., a personal relationship between shareholders involving mutual confidence, an agreement that some or all should participate in the management and restrictions on the transfer of shares which would prevent a member from realising his investment. If the agreement to run the company in a particular manner is incorporated outside the articles this may be regarded as part of the member's rights under this section.[10] However, this may not apply to large public companies.[11] If there is no agreement then it will depend on the issues involved and the nature of the companies in question, its pre-incorporation history.[12] The petitioner's appointment as a non-executive director may give him a legitimate expectation to be consulted on policy matters relating to the company's affairs.[13]

1 Elder vs Elder & Watson Ltd [1952] Scottish Cases 49, 57; Re Lundie Brothers Ltd. [1965] 1 W.L.R. 1051,1058; Re Harmer Ltd.[1959] 1 W.L.R. 62, 83, 87; Re Bellador Silk Ltd.[1965] 1 All E.R. 667.

2 [1983)1 W.L.R.927,933.

3 [1986] BCLC 382,387.

4 [1986] BCLC 376,378.

5 [1973] A.C. 360, 379.

6 [1989] 5 BCC 82; [1989] BCLC 427.

7 Re J.E. Cade & Son Ltd [1991] BCC 360.

8 [1986] BCLC 376, 379.

9 That the shareholders be allowed to take part in the management of the company is well established and judicially recognised as in "quasi-partnership concern. Ebrahimi vs Westbourne Galleries Ltd. [1973] A.C. 360; [1971] 1 All E.R. 561.

10 Russel vs Northern Bank Development Corp. Ltd. [1992] BCLC 1016, HL.

11 Re Blue Arrow [1987] BCLC 585,590.

12 Murray's Judicial Factor vs Murray and Sons [1993] BCLC 1437,1449.

13 Re Elgindata Ltd [1991] BCLC 959.

In the case of a public company, there is usually no underlying personal relationship and shareholders are more interested in dividend yield and less concerned with the day-to-day running of the company. The interests of a member in a quasi-partnership company are in employment and participation. Lord Hoffman and the House of Lords however shifted from the purchase 'legitimate expectations' to 'equitable considerations' determined by reference to the bargain which the members of the company had struck even in informal, non-legally enforceable understanding between members.[1]

19.4.2 **Exclusion from Management** – The petitioner must establish a clear link between his capacity as member and his interest in management. Can a husband who was a joint venturer in the company and whose shares were temporarily registered in his wife's name , complain when he is discharged as an employee? Not, Hoffman J. held but "the jurisdiction to remedy conduct 'unfairly prejudicial' to the interests of members enables the court to protect not only the rights of members under the constitution of the company but also the rights, expectations and obligations of the individual shareholders inter se...".[2]

In *Re Blue Arrow plc.*[3] it was held that it was impossible in public companies to infer any legitimate expectation to remain president from arrangements outside those embodied in the formal constitution of the company as outside investors were entitled to assume that the whole of the constitution was contained in the articles read with the Companies Act.

19.4.3 **Excessive Remuneration** – is clearly detrimental to the interests of a member. Although this is a matter of internal management[4] the Courts have used this section to challenge these payments. In *Re Cumana Ltd.*[5] the Court of Appeal agreed that remuneration of 365,000 British Pounds over a 14 month period was excessive and unfairly prejudicial to the interests of the petitioner given the circumstances of the case.

19.4.4 **Inadequate Dividends** – Quite often investors in companies, especially members of private company or a closely held public company come to a lawyer's office complaining that they have invested their money but get no dividend while those in control of the company seem to be living a comfortable life with the company's money. The question arises whether a shareholder has an interest in the recommendation and declaration of dividends where funds are available for that purpose ? The Jenkins Committee of England was of the opinion that such conduct should be within the scope of the section.[6]

Where the company had not paid reasonable dividends to its ordinary shareholders despite being able to do so minority shareholders could not petition for relief under the statutory provision. This was held to be so even though some of the other ordinary shareholders who had suffered the same deprivation of dividends had been compensated for this to some extent by receiving reasonable but not excessive remuneration as directors of the company.[7] However, in a similar case where the minority complained of inadequate dividends the minority was held to be entitled to relief under section 459 of the English Act.[8] The *Sam Weller* case has more support in an earlier House of Lords case.[9]

A failure to declare and a failure to pay a dividend after it had been declared can both be unfairly prejudicial.[10] It is settled law however that in the absence of anything to the contrary

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1 O'Neill vs. Phillips (1999) 2 B.C.L.C. 1, H.L.; See also Re J E Cade and Son Ltd. (1991) B.C.C. 360; (1992) B.C.L.C. 213 where Warner J refused to superimpose further rights and obligations arising from its own concept of fairness.

2 Re a Company(No. 003160 of 1986) [1986] 2 BCC 99,276.

3 [1987] BCLC 585.

4 Smith vs Croft [1986] 1 W.L.R. 580

5 [1986] 2 BCC 99,453.

6 Cmnd.1749(1962) para 212. See Re Sam Weller & Sons Ltd [1990] BCLC 80;Re a Company (No.00370 of 1987) ex p. Glossop [1988] BCLC 570; [1988] 1 W.L.R.1068

7 ex p.Glossop ibid.

8 Re Sam Weller & Sons Ltd [1990] BCLC 801.

9 Scottish Co-operative Wholesale Society vs Meyer [1959] A.C.324.

10 Warner J. in Re Elgindata Ltd. [1991] BCLC 959,991.

in the articles a company cannot be compelled to declare a dividend, and no action can be brought for its recovery until it has been declared.[1]

19.4.5 **Take-over Situations** – Hoffman J. held in *Re a Company (No 008699 of 1985)*[2] that the directors of a company had acted in a manner unfairly prejudicial to the interests of the petitioner by favouring a lower bid for the company's shares from a company promoted by the directors in preference to a higher bid from a trade competitor.

19.4.6 **Proportionate Shareholding** – Section 155(1) of the Companies Act 1994 requires directors to make a proportionate offer to the existing shareholders when the company makes a new issue of share capital. However, sub-section (2) waters down the rigors of this section and provides that further share can be offered to a person who is not entitled to be offered under sub-section (1). There is no case law whether this sub-section will make the entire section ineffective or sub-section (2) will apply only when sub-section (1) is exhausted. In England where articles similar to sub-section (1) are quite often found it has been held in cases of attempted dilution that the proportionate shareholding held by each shareholder is often of great importance.[3] Any attempt to dilute a shareholder's holding in the company will be prejudicial to his interests.[4]

19.4.7 **Alteration of Articles of Association** – A company can alter its articles of association by a special resolution (Section 20).This must be done for the benefit of the company as a whole. In *Allen vs Gold Reefs of West Africa*[5] it was held that a company could alter its articles so as to impose a lien on shares of existing holders in respect of existing debts.

19.5.1 **The Rule in Foss vs Harbottle** – In case of a wrong done to a company, the proper plaintiff according to the rule in Foss vs Harbottle[6] to complain is the company itself, and the Courts will not, ordinarily, allow a shareholder to bring an action to remedy such a wrong. Further, where the alleged wrong is a transaction which may be regularised by a simple majority of the members no individual action of the members will be allowed, because if the majority can challenge the transaction, there is no reason why the majority cannot sue. Applying this principle, where an act can be validly done or sanctioned by a special resolution or is ultra vires the powers given in the memorandum of association, this Rule will not bar an individual action because then the simple majority cannot pass the resolution complained of. As to whether the court can interfere in internal management of the company see also the observations of the Kerala High Court in *Marikar (Motors) vs M.I. Ravikumar.*[7]

19.5.2 **Fraud on Minority** – Professor Gower observes that the exact meaning of the expression " fraud on minority" is not easy to determine but it is clear that both "fraud" and "minority" are used somewhat loosely.[8] There need not be actual deceit nor is it necessary that those who are injured should be minority. The injured party will be the company itself. Lord Davey came close to describing it as "acts of a fraudulent character" of which "familiar examples are when the majority are endeavouring directly or indirectly to appropriate to themselves money, property or advantages which belong to the company or in which the other shareholders are entitled to participate".[9] Professor Gower classifies the incidents of "fraud on minority" in several categories and these have been followed generally by other scholars.

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1 Bond vs Barrow Haematite Steel Co. [1902] 1 Ch. 353; Buenos Ayres Great Southern Railway Co. Ltd. vs Preston [1947] Ch. 384.

2 [1986] BCLC 382,387

3 Clemens vs Clemens Bros Ltd. [1976] 2 All E.R. 268; Greenhalgh vs Arderne Cinema Ltd. [1950] 2 All E.R. 1120.

4 Re a Company (No 002612 of 1984) [1985] BCLC 80; [1986] BCLC 430.

5 [1900] 1 Ch. 656.

6 (1843) 2 Hare 461

7 [1982] 52 Comp. Cas.362(367-370)

8 Principles of Modern Company Law : 5th Ed. p. 593.

9 Burland vs Earle [1902] A.C. 83,93.

19.5.3 One instance of "fraud on minority" is a resolution permitting expropriation of company property. In *Menier vs Hooper's Telegraph Works*[1] the majority shareholders exercised their controlling interest in the company to have a pending action compromised to their own advantage. They were thus, gainers of property to the exclusion of the minority. This was held to be expropriation of the company's property. In *Cook vs Deeks*[2] it was held that when directors diverted to themselves contracts which they should have secured for the company, they would be holding the benefits of the contract on trust for the company. The directors had this action ratified by the company in general meeting and yet were found to be holding the same for the benefits of the company. In *Regal (Hastings) Ltd. vs Gulliver*[3] however, the House of Lords commented that the directors would not have been liable to account for the profits if they had the transaction ratified in the general meeting. In this case the directors had taken advantage of information which they acquired as directors of the company. Hence, Professor Gower explains the apparent confusion by saying that in the earlier case it was the duty of directors to acquire the contracts on behalf of the company whereas in the latter case the directors did not misappropriate any property of the company. Such a resolution ratifying the appropriation of the company's property must be passed "bonafide in the interests of the company".[4]

19.5.4 **Resolutions Relieving Directors' Liability** – If directors want to have a particular transaction ratified by the company in general meeting so that they are not liable for any loss caused to the company then they must show that all material facts are disclosed to the members attending the meeting and that the resolution is passed in the interest of the company.[5]

19.5.5 **Resolutions to Expropriate Members' Shares** – In Brown vs British Abrasive Wheel Co[6] the holders of 98 % shares wanted to amend the articles of association so as to enable the holders of 90 % shares to forcibly acquire the shares of the minority. This was done in the bonafide interest of the company but was by the court on the ground that the benefits would enure to the majority only. This decision was distinguished in *Sidebottom vs Kershaw Leese & Co.*[7] by the Court of Appeal . In this case the minority shareholder had an interest in a competing company. An amendment of the articles allowing the directors to forcibly acquire shares of a person holding interest in a competing company was upheld by the Court because it was obviously beneficial to the company. In *Dafen Tinplate Co. vs Llanley Steel Co.*[8] the court struck down a resolution to insert a new article empowering the majority to buy out any shareholder as this may not be in the interests of the company. However, in *Shuttleworth vs Cox Bros. Ltd*[9] the Court of Appeal left it to the members to decide what would be in the best interests of the company and observed that the court would interfere only if the members had acted in bad faith. This case concerned with a resolution to amend the articles with a view to remove a director by the board. Professor Gower comments that if the same principle applies to expropriation of shares, it is difficult to understand why section 429 of the English Act (equivalent to our section 230 of our Act) was needed.[10] It is worthwhile to mention that the Court of Appeal refused to allow the holders of 90 % shareholders to acquire the shares of the 10 % minority under the corresponding section 209 of the English Act of 1948.[11]

19.5.6 **General Principle** – Professor Gower summarises the sort of duty which a member and a director has with regard to the affairs of the company by saying that they must act "bona fide in the interests of the company." This however, does not mean that they will

1 [1874] L.R. 9 Ch. App.350
2 [1916] 1 A.C. 554, P.C.
3 [1942] 1 All E.R. 378
4 Rolled Steel Products Ltd. vs British Steel Corporation [1986] Ch. 246.
5 Professor L.C.B. Gower : Modern Company Law 5th Ed. p.596; also see section 102 of the Act of 1994.
6 [1919] 1 Ch. 290.
7 [1920] 1 Ch. 154
8 [1920] 2 Ch. 124
9 [1927] 2 K.B.9.
10 Modern Company law :5th Ed. p.598.
11 Re Bugle Press Ltd. (1961) Ch. 270.

ignore their own interests and raises a question on the relationship between fraud on the minority and acting bonafide in the interests of the company. The classic case on this point is that of *Greenhalgh vs Arderne Cinemas Ltd.*[1] where the majority shareholders passed a special resolution amending the articles of association enabling the transfer of shares to an outsider ignoring the pre emptive rights of a minority shareholder. The minority shareholder challenged the resolutions as a fraud on minority which the Court of Appeal held not to be. Evershed M.R., nevertheless went on to discuss what is meant by the phrase " bona fide for the benefit of the company as a whole ":

> ...It means that the shareholder must proceed on what, in his honest opinion is for the benefit of the company as a whole.... That is to say the case may be taken of an individual hypothetical member and it may be asked whether what is proposed is, in the honest opinion of those who voted in its favour, for that person's benefit....a special resolution of this kind would be liable to be impeached if the effect of it were to discriminate between the majority shareholders and the minority shareholders , so as to give the former an advantage of which the latter were deprived....

Goulding J. however held in *Mutual Life vs Rank Organisation*[2] that this did not mean that there could be no discrimination so long as the directors acted fairly as between different shareholders.

In *Australian Fixed Trusts Pty Ltd vs Clyde Industries Ltd*[3] the Court restrained a company from proceeding to change articles which would operate adversely to the interests of custodian trustee shareholders. The amendment would have prevented a custodian trustee from voting in respect of shares held in that capacity unless the majority of beneficial owners of the shares had directed the trustee as to the manner in which the votes should be cast. The article unfairly discriminated against the minority custodian trustees , and there was no ground on which a reasonable person could decide that the article was for the benefit of the company as a whole.

In *Re Holders Investment Trust*[4] Megarry J. refused to confirm a capital reduction scheme on the basis that he had to be satisfied that the voting by preference shareholders had been validly passed bona fide in the interest of that class. In *British American Nickel Corpn vs O'Brien*[5] the Privy Council seemed to have held that the obligation of a class member to consider the interests of the class as a whole is greater than that of a member voting at a general meeting to consider the interest of the company as a whole. In Clemens vs Clemens Bros. Ltd.[6] issue of further shares to directors and trustees of an employees' share-ownership scheme that would deprive the plaintiff of the chance to block the passing of a special resolution was struck down. It did not matter whether those proposals were oppressive to the plaintiff or that no one could reasonably believe that they were for the benefit of the plaintiff. The plaintiff succeeded because the resolutions were "unfairly prejudicial" .

19.6.1 Professor Pennington comments that the Court's jurisdiction is equitable in character although originating in a statutory provision; this is because the concept of prejudicial (in the U.K. it is 'unfairly prejudicial') conduct toward the petitioner is akin to the equity notions of oppression, unfair and inequitable conduct and taking improper advantage of the petitioner's vulnerable position. The elements which induce the court to give or withhold equitable remedies are therefore relevant, and the elasticity of the remedies which may be given is as great, if not greater, than that of equitable remedies in general.[7] In Re Charnley Davies Ltd. (No.2)[8] Millet J. observed that an allegation of independent illegality was not necessary to found a successful petition for protection of minority shareholders and that in case of breach of duty the same facts may give rise to a complaint both of breach of duty and of unfair prejudice.The court may give injunctive relief if the act complained of is likely to be repeated even though that particular act has now become impossible.[9] Lack of confidence in the majority coupled with an offer by the majority

1 [1950] 2 All E.R. 1120,C.A.
2 [1985] BCLC 11
3 [1959] 59 State Reports (NSW) 33
4 [1971] 1 W.L.R. 583
5 [1927] A.C. 369
6 [1976] 2 All E. R. 268
7 Pennington's Company Law 7th Ed. p. 886.
8 [1990] B.C.C. 605; [1990] B.C.L.C. 760
9 Re Kenyon Swansea Ltd [1987] BCLC 514.

to purchase the minority is not actionable under this section.[1] Professor Pennington cites cases where relief has been given e.g., if equity shares are allotted by the directors to themselves or their associates without regard to the petitioner's and other members' statutory rights to subscribe for so many of the new shares as are proportionate to their existing holdings and where the petitioner was removed from the directorship by other directors, who were the majority shareholders of a private company so that they might compel the petitioner to sell his shares to them under a provision of the articles, after which they intended to sell the company's assets at an enhanced price.[2]

Relief will be given if those in control of the company fail to comply with the requirements of the Companies Act as to the holding of annual general meetings or the annual presentation of the company's accounts to the members. Also, if they divert a business opportunity from the company to another undertaking which they control.[3] A minority shareholder can petition the Court for relief if there has been fundamental breach of the rules and where the majority endeavoring directly or indirectly to appropriate to themselves money, property, or advantages which belonged to the company.

The Court can make any just order beyond the relief sought for, to bring the affairs of the company to its right track to safe guard the interest of the minority shareholders.[3A] In an unreported decision *Nurul Hoque Chowdhury vs. Mrs. Mahzabin Chowdhury*[3B] His Lordship Justice A. B. M. Khairul Haque held that the acts of a director must pass the test of reasonability and fairness. Judgment was delivered on 18 Nov 2002.

A minority shareholder has no right to invoke protection under this section if his complaint is based solely on a lack of business ability on the part of the company's directors and their carelessness in conducting the company's business.[4] Similarly, no relief was given when the petitioner's complaint was that parent company sold the subsidiary's products and applied the proceeds of sale in discharging the parent company's debts so making the subsidiary insolvent when the parent company's directors decided on this course of action as a matter of policy to avoid the parent company becoming insolvent.[5] The court refused to interfere where the majority were buying out parts of the company's business to the exclusion of the minority because the only alternative was to sell to outsiders and this would saddle the company and the shareholders with heavy tax burden and the price paid on the buy-out was as high if not higher than that may be obtainable on a sale to any outsider.[6] The directors and majority shareholders in this case did not seek to obtain an unfair advantage and the business decision they intended to carry out was made in good faith to enable the company's business to be continued. Professor Pennington in this connection cites the case of *Re Saul D Harrison Sons plc*[7] and comments that a decision by the company's directors to change or expand the company's business despite trading losses, or despite the fact that its profits are attributable wholly to its investment income and not to carrying on the business for which it was formed, will not induce the court to give relief to a minority shareholder, nor the allegation that the shareholders as a whole would benefit from the company being wound up.[8] The English Court has interfered when in a private company the minority shareholder ceases to act as a director as a result of personal difference of temperament with the other directors and the controlling shareholders do not make an offer to acquire his shares at a reasonable price.[9] But the minority shareholders are not unfairly prejudiced if they are not able to take up rights issue of shares although this would result in dilution of their percentage of shareholdings.[10] If directors do not see eye to eye then it is not unfairly prejudicial act to procure the dismissal of the minority director in a general meeting and to purchase the shares of the dismissed director at a fair price.[11] Professor Pennington comments that if the petitioner is able to seek relief by exercising his voting power the court will not interfere but

1 Re a Company (No 006834 of 1988) [1989] BCC 218.
2 Company Law 7th Ed. p. 889.
3 Re a Company (No 00789 of 1987) [1989] 5 BCC 792 and Re London School of Electronics [1986] Ch.211 cited in Pennington ibid p.890. 3A. Syed Al Nesar Ahmed vs Nafisa Choudhury and ors. 53 DLR (AD) 83.
3B. Company Matter No.20 of 2002.
4 Re Five Minutes Car Wash Services Ltd [1966] 1 All ER 242.
5 Nicholas vs Soundcroft Electronics Ltd [1993] BCLC 360.
6 Re Posgate and Denby (Agencies) Ltd [1987] BCLC 8.
7 [1994] 2 BCC 475
8 Company Law 7th.Ed 893.
9 Re a Company (No.007624 of 1984) [1986] BCLC 362.
10 ibid.
11 Re a Company [1987] 1 WLR 102.

cites an Australian decision where the court intervened because the petitioners controlled the management but did not have the majority shareholding.[1]

19.6.2 The petitioner must prove conduct or an omission which is prejudicial to the interest of the petitioner as a member of the company.[2] Thus, the petitioner cannot complain that the company must purchase his shares under statutory powers because then he is complaining as a potential seller of shares and not as a member of the company. Similarly, when the minority shareholders had no contractual or other rights to purchase the shares of the majority , they could not complain if the majority sold their shares to others without giving the petitioners an opportunity to purchase them.[3] In *Re a Company*[4] the petitioner as a minority shareholder had no cause to complaint under this section that the company had broken a contract to appoint him as a consultant. However, in another case it was held that the board must give impartial advice on the merits of an offer to purchase the shares.[5] Similarly, where the company is little more than a partnership depending on mutual confidence and the petitioner was removed from the board this may amount to an act which is unfairly prejudicial to the petitioner unless the removal is not to exclude him from the benefits of his shareholding.[6] The Court of Appeal gave special consideration to quasi partnership companies in deciding whether or not to give relief and held that the court would take into account not only the rights conferred on them by the company's constitution and an agreement entered at the time of forming the company but also the legitimate expectations of the shareholders.[7]

The court may decide to give relief even if the persons responsible for the prejudicial conduct have transferred their shares *(Re a Company*[8]*)* but may refuse to interfere if the petitioner is the transferee of shares of a quasi-partnership company and complains of unfair or discriminatory treatment of the original shareholder.[9] If the majority commits an act of oppression in a capacity other than as a member then also the court may give relief.

The House of Lords held that the minority shareholders were entitled to relief from opression caused by the majority shareholder, a co-operative society, managing its own affairs so as deliberately to ruin the company.[10] Lord Simonds and Lord Keith were of the opinion that the society's majority shareholding in, and consequent control of the company, cast an obligation on it to manage its own affairs so as to deal fairly with the company, and any unfair dealing by it must be treated as part of the conduct of the company's affairs, because the company had no power to resist.[11] Professor Pennington comments, after reviewing recent decisions, that it may be well that as a result of the court's decisions in cases where the company was formed by its original shareholders and directors to carry on a business undertaking which would be managed by them personally (a quasi partnership) that there is now a fiduciary relationship between the shareholder/ directors and that they do owe each other fiduciary duties comparable to those of partners.[12]

The act complained of must have been done in relation to the conduct of the company's affairs. If a shareholder and director calls for immediate payment of a loan from the company although the company lacks liquidity this will not be a ground for action under this section because this is not an act in relation to the company.[13] A single bench of the High Court Division held that the creation of debentures to cover the alleged loans of a company in favour of its majority shareholders deemed to have been accrued by a revaluation of assets uted by way of a dividend was a matter fit to be redressed under section 233 as being act prejudicial to the interest of a company.[14]

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1 Company Law 7th Ed. 894.Also see Re Jermyn St Turkish Baths Ltd. (1970) 3 All E.R. 57; but see 49 DLR (1997) 539 and para 19.2.3.
2 Re a Company (No.004475 of 1982) [1983] Ch.178;(1983)2 All E.R.36.
3 Re Ringtower Holdings plc [1989] 5 BCC 82.
4 (No.003843 of 1986) [1987] BCLC 562
5 Re a Company (No.008699 of 1985) [1986] BCLC 382.
6 Re O C (Transport) Services Ltd [1984] 1 BCC 68.
7 Re Saul O Harrison and Sons plc [1994] BCC 475,490,500.
8 [1986] 2 All E.R. 253;[1986] 1 W.L.R. 281
9 See Pennington's Company Law 7th. Ed p.897.
10 Scottish Co-operative Wholesale Society Ltd. vs Meyer [1959] A.C. 324.
11 ibid at p. 342.
12 Company Law 7th Ed. p.900.
13 Re a Company (No.001761 of 1986) [1987] BCLC 141.
14 A.B.S. Safdar and others vs. People's Republic of Bangladesh and others, 20 BLD (HC) 210. The matter is on appeal.

19.6.3 **Conditions for Obtaining Relief** – Even if the director or majority shareholders have been guilty of improper or irregular conduct, so that there is a prima facie case for relief, it will be refused if the motive of the petitioner is to force the directors to run the company according to his wishes.[1] Relief may be refused if the petitioner has accepted the improper conduct of affairs of the company without protest.[2]

Delay may also defeat the remedy,[3] because this may indicate lack of good faith. However, even if the petitioner has taken some sort of retaliatory steps against the action complained of this will not prevent him from getting relief although it may have a bearing on the form and extent of the relief he is entitled to get. The court may refuse relief under this section if relief is more readily available under a provision of the company's memorandum and articles or under some specific provisions in the Act.[4] But the fact that the petitioner could bring a derivative action will not deprive him of relief under this section.[5]

Further, if there is no asset left in the company then the court may refuse remedy because then winding up of the company may be a more suitable remedy.[6] But it need not be proved that the company can be saved again or that there is an alternative relief available.[7]

19.6.4 **Remedies Available** – are mentioned in sub-section (3) of section 233. When an application is admitted the same is not liable to be dismissed/rejected summarily without hearing on merit, unless such application is absolutely incompetent being without jurisdiction.[8] The court may make such order as prayed for or as it deems fit including a direction to cancel or modify any resolution or transaction or to regulate the conduct of the company's affairs or to amend the provisions of the memorandum or articles of association. Under parallel provisions in the English Companies Act the court ordered appointing or removing directors.[9] Professor Pennington mentions that this power includes appointing a receiver to manage the company's business temporarily and such orders that alter the voting and other rights of classes of members.[10] He comments that the court has wide discretions and the only limitation is that the order it makes must be relevant and appropriate in order to give relief from the matters complained of.[11] He further cites a South African decision to argue that such limitation on the court's inventiveness in devising an appropriate remedy to relieve the prejudicial conduct of a company's affairs seems to be that it cannot alter rights held by the parties in capacities other than those of members or directors of the company. Thus, controlling shareholders found guilty of oppression could not be compelled to submit to a variation of rights conferred by debentures of the company which they held, even though their oppressive conduct had been facilitated by their also being debenture holders.[12] The petitioner must however, ask for specific relief.[13] Where as a result of oppression Company has been brought to a stage where it has to be wound up, wronged shareholders are still entitled to the remedy, i.e., by making oppressor buy their shares at a fair price.[14]

Section 233 of our Act does not mention that the court may order the purchase of the complaining petitioner's shares by others or the company and this seems to be a serious lapse. This provision is found in the English Act of 1985 as amended[15] and is obviously a saving provision. The High Court Division ordered in a particular case directing majority shareholders to purchase the shares of the minority where the Court found that the minority was locked out of management. The Court also explained in a great detail the scope of application of this section in

1 Re Bellador Silk Ltd [1965]1 All E.R.667.
2 Re R.A. Noble & Sons (Clothing) Ltd [1983] BCLC 273.
3 Re Jermyn St. Turkish Baths Ltd [1971] 3 All E.R. 184
4 Re a Company, ex p. Kremer [1989] BCC 365.
5 Re a Company [1986] BCLC 68.
6 Vindi vs Abbey Leisure Ltd. [1990] BCLC 342.Also see Re Hailey Group Ltd.[1993] BCLC 459.
7 Scottish Co-operative Wholesale Society Ltd. vs Meyer [1959] A.C. 324.
8 Nahar Shipping Lines Limited and another vs Homera Ahmed and others 52 DLR 585.
9 Re H R Harmer Ltd [1958] 3 All E.R. 689
10 Company Law 7th Ed. p.903.
11 ibid.
12 Pennington's Company Law 7th. Ed. p. 906, citing Irvin and Johnson Ltd vs Oclofse Fisheries Ltd. [1954] (1) SA 231.
13 Re Antigen Laboratories Ltd. [1951] 1 All E.R. 110.
14 Scottish Co-operative Society Ltd. vs Meyer [1959] A.C. 324; [1958] 3 All E. R. 66.
15 Section 461(2)(d)

the background of English, Indian and Australian law and gave a liberal interpretation to the section.[1] The same judge however in an earlier case refused to go into factual dispute and avoided the issue of fraud by holding that the Court is to see whether the resolutions adopted are unfair to the Company and the minority. He held that power given to managing director to operate account in Bangladesh and abroad is prejudicial to the interest of the company and its members.[2] In the same case the Hon'ble Company Judge Mr. Justice K. M. Hasan made an unwarranted comment (at paragraph 28) that a prior board resolution is needed before articles are amended. This, it is submitted, is not a requirement of law and has no support in any of the legal literatures in U.K., Australia, India and other countries.

Majority shareholders against whom allegations of oppression have been made can be given first option to purchase shares.[3]

19.6.5 **Concept of Prejudice** – Section 233 requires the petitioner to show that an action prejudicial to his interest is being committed. In the U.K. the concept is of unfair prejudice.

Although the section does not say so , undoubtedly the courts here will look to see whether there is any element of unfair prejudice.

In deciding whether there is any such prejudice the House of Lords observed that there is no appeal on merits from management decisions to courts of law, nor will courts of law assume to act as a kind of supervisory board over decisions within the powers of management honestly arrived at.[4]

It is not necessary for a petitioner to show any actual irregularity or an invasion of his legal rights or a lack of probity or want of good faith towards him on the part of those in control of the company and the courts will not confine the granting of relief to situations where there has been an illegal act.[5] Otherwise the power of the courts will be circumscribed by the company's memorandum and articles. Harman J. was prepared to hold that the making of a rights offer to soak up the funds of the petitioner so that he would lack the resources to bring an action against the company would constitute unfair prejudice.[6]

Prejudice includes cases where the value of his shareholding in the company has been seriously diminished or at least seriously jeopardised by reason of a course of conduct on the part of those persons who have had de facto control of the company.[7] In Nafisa Choudhury vs United Food Complex Ltd. and another[7A] it was held that the Court will interfere when there is pecuniary loss and to bring the affairs of the company to its right track, the managing director was allowed to function as per the articles of association.

Thus in *Scottish Co-operative Wholesale Society vs Meyer*[8] where the majority were conducting the affairs of the company in such a manner that the share value was being depleted the Court held that this was an act of oppression within the meaning of section 210 of the English Act of 1948. If there is a failure to conduct the affairs of the company properly from a procedural point of view so that the improprieties resulted in the invalidity of an allotment of shares to the petitioner then this may be a case of 'unfair prejudice'.[9]

The English section 459 (corresponding to our section 233) cannot be limited to cases in which the value of members' shareholdings has been seriously diminished or jeopardised.[10] This means that any harm done to the petitioner's legitimate right enjoyed by virtue of his shareholdings or any interests recognised by the court would constitute prejudice. *Mc Guinness & Anor, Petitioners*[11] indicates that unreasonable delay in convening a meeting upon receipt of a member's requisition was held to constitute prejudice since 'justice delayed is justice denied' and

1 Homera Ahmed and others vs Nahar Shipping Lines Ltd. and others 22 BLD (HCD) 67 = 7 BLC (HC) 107. The Appellate Division refused to grant leave against that decision 9 MLR (AD) 58 = 56 DLR (AD) 36.
2 Md. Shahadat Hossain vs Base Textile Ltd. 21 BLD (HCD) 585 = 54 DLR 583.
3 KL Ahuja vs SK Ahuja [1983] 53 Com. Cas 60 (Delhi); Chander Krishan Gupta vs Pannalal Girdhari Lal (p) Ltd. (1984) 55 Comp. Case 702 (Delhi); Also see Re a Company exp schwarcz Noz [1989] BCLC 427.
4 Lord Wilberforce in Howard Smith vs Ampol Petroleum Ltd.[1974] A.C. 821,832.
5 Re Norvabron Pty.Ltd {1987} 11 ACLR 279,290.
6 Re a Company (No. 001761 of 1986) [1987] BCLC 141,143.
7 Slade J in Re Bovey Hotel Ventures Ltd.(dt. 31 July 1981, unreported, but referred to in R. A. Noble & Sons (Clothing) Ltd. [1983] BCLC 273. 7A. 53 DLR 81
8 [1959] A.C. 324
9 Re a Company (No. 00789 of 1987) [1989] 5 BCC 792,800,801.
10 Nourse J. in Re a Noble & Sons (Clothing) Ltd., supra.
11 [1988] 4 BCC 161,167.

'delay is prejudicial to the interests of the petitioner who seeks to work out a legal remedy'. The directors were acting within the terms of the Companies Act and yet were held to have been acting prejudicial to the interests of the minority shareholders who had more than ten per cent of the shares issued and had a right to convene the meeting themselves. The payment by a shareholder of the company's debts to a bank and transfer of the security to him without giving notice to the company would not constitute an unfair prejudice.[1]

Even exercise of legal right may still be unfairly prejudicial. Thus, a member had a legitimate right to take part in management of a quasi-partnership company if he had a legitimate expectation to continue to be a director of the company.[2]

The petitioner is not disentitled from applying under this section even though he may have applied for convening an extraordinary general meeting to the Court.[3] However, if a petition under section 233 is pending it may be considered improper for the respondent to take recourse to calling an extraordinary general meeting of the company to secure the removal of the petitioner.[4]

19.7.1 Although section 233 speaks of the affairs of the company being conducted in a manner prejudicial to the members it is obvious that the prejudice caused to the member should be unfair. The English Act clearly mentions unfair prejudice to be shown by the petitioner and the concept of 'unfairness' to be proved is ingredient in our law.[5] Slade J. said in that case that it was not essential to show that the respondents acted as they did in the conscious knowledge that this was unfair to the petitioner or that they were acting in bad faith; the test is whether a reasonable bystander observing the consequences of their conduct, would regard it as having unfairly prejudiced the petitioner's interests.

Unfairness is a familiar concept but it was intended to confer a wide jurisdiction upon the court and it would be wrong to restrict that jurisdiction by confining it to infringement of legal right.[6]

Thus, if the company makes a call on partly paid up shares for putting pressure on the petitioner it was held to be prejudicial to the petitioner. Also, the calling of an extra ordinary general meeting seven months after requisition without sound reason was held to be unfairly prejudicial to another group of shareholders who had the requisite number of shareholdings to call an extraordinary general meeting themselves.[7] Denial to the shareholder of his right to vote and receive dividend is an act of oppression.[8] However, denial of access to or inspection of books of account or dividends below actual profits may not constitute acts of oppression.[9]

19.7.2 The central theme of the section is the concept of unfairness. It is not necessary for the petitioner to show that the persons who have had de facto control of the company have acted as they did in the conscious knowledge that this was unfair to the petitioner or that they were acting in bad faith; the test is whether a reasonable bystander observing the consequences of their conduct, would regard it as having unfairly prejudiced the petitioner's interests.[10] Hoffman J. in Re a Company (No. 008699 of 1985) said that 'unfairness is a familiar concept employed in ordinary speech, often by way of contrast to infringement of legal right. It was intended to confer a very wide jurisdiction upon the court and.... it would be wrong to restrict that jurisdiction by adding any gloss to the ordinary meaning of the words'.[11] A resolution of directors may be perfectly legal and yet oppressive and conversely a resolution which is in contravention of the law may be in the interests of the shareholders and the company.[12]

1 Re a Company (No. 001761 of 1986) [1987] BCLC 141.
2 Re a Company (No. 00477 of 1986) [1986] BCLC 376. Also see para 19.3.2, 19.4.1 and 19.4.2 above.
3 Re El Sombrero Ltd. [1958] 3 All E.R.1;Re Whitechurch Insurance Consultants Ltd.[1993] BCLC 1359.
4 Re Sticky Fingers Restaurant Ltd. [1992] BCLC 84,88.
5 Re Bovey Hotel Ventures Ltd.(1981) cited by Nourse J. in Re RA Noble & Sons (Clothing) Ltd [1983] BCLC 273
6 Hoffman J. in Re a Company (No.008699 of 1985) [1986] BCLC 382,388.
7 McGuinness & Anor, Petitioners [1988] 4 BCC 161.
8 Mohanlal Chandumal vs Punjab Co. Ltd Bhatinda AIR 1961 Punjab 485.
9 Lalita Rajya Lakshmi vs Indian Motor Co. AIR 1962 Cal 127.
10 Slade J. in Re Bovey Hotel Ventures Ltd.(unreported) cited by Nourse J. in Re RA Noble & sons (clothing) Ltd.[1983] BCLC 273.
11 Supra.
12 S.H.Ganpat Ram vs Sivaji Jubilee Cotton and Jute Mills Co. AIR 1965 Guj 96,103.Also see Elder vs Elder AIR 1952 Scottish Cases 49; Needle Industries (India) Ltd vs N.I.N.H. Ltd.AIR 1981 SC 1298.Shanti Prasad Jain vs Kalinga Tubes Ltd. AIR 1962 Orissa 202;Hindustan Co-operative Insurance Society Ltd.In re AIR 1961 Cal 443.

Misappropriation of money in the past is not a continuing wrong.[1] This section protects the interest of a shareholder and not a director.[2]

19.8.1 **Factors which the Court may Consider** – The courts may take into account the petitioner's conduct in deciding whether the alleged act of the respondent is unfair.[3]

Any offer made to buy out the petitioner may also be relevant factor in deciding the remedy to be given to the petitioner under this section. In *Re a Company (No 004377 of 1986)*[4] Hoffmann J. remarked that where there was an irretrievable breakdown in relations between members of a corporate quasi-partnership, the exclusion of a member from management and employment was not ipso facto unfairly prejudicial conduct which entitled him to petition under this section. He went on to say that the question of unfair prejudice must depend on whether, if there is to be parting, it is reasonable that he should leave rather than the other member or members and on the terms he is offered for his shares or in compensation for his loss of employment.

If the articles provide a method for determining the fair value of a party's shares, a member seeking to sell his shares on a breakdown of relations with other shareholders should not ordinarily be entitled to complain of unfair conduct if he has made no attempt to use the machinery provided by the articles... a provision that the auditors, or some independent persons, shall fix a ' fair value' for the shares, gives the auditors precisely the function which a court would have to perform under this section.[5] This leads to a dangerous situation that the courts might refuse a petition under this section in the light of an offer made to purchase the petitioner's shares. This is specially relevant because quite often articles contain pre-emption provisions.

In *Re Castleburn Ltd.*[6] the articles contained pre-emption clauses on the happening of a certain event like ceasing to hold office as a director and on the happening of that event the majority wanted to compulsorily buy the shares of the minority and the auditors fixed the price of the minority shareholders at less than the price of the majority shareholders; the minority complained of unfairness but the court held that this was not an allegation of wrongful conduct against the respondents and the dispute was over the terms on which the respondent should buy out the petitioner. Where the shares are valued on a discount basis then the pre-emption article is of great importance but such a provision may be disregarded where the articles provide some arbitrary or artificial method of valuation[7] or where there has been bad faith on the part of the respondents[8] or where the valuer was not wholly independent of any connection with the respondents or the transactions of which the complaint was made.[9]

19.8.2 Where the articles only provide a common form pre-emption provision that a member wanting to transfer his shares must offer the same first to other shareholders at a fair value to be fixed by the auditors no occurrence of prejudicial conduct is contemplated.

However, if there is presence of unfairly prejudicial conduct this clause should not bar a minority shareholder from complaining under this section. Nor should the respondents' offer to buy out the petitioner.[10]

But if there is no unfairly prejudicial conduct , then no complaint can be made. In the typical case in which relations between shareholders have broken down without obvious fault on either side the appropriate way to resolve the problem is for one or more shareholders to buy the shares of the other or others and the company's articles provide a means for determining the fair value of those shares, it should not be necessary to resort to (section 233) unless and until the operation of the articles has failed to provide an adequate solution.[11] However, in a later case the matter was left open by the Court of Appeal in England.[12]

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1 Stadmed Private Ltd vs Kshetra Mohan Saha AIR 1968 Cal 572.
2 ASM Shamsul Islam Rashedi vs Satellite Fishing Ltd. and others 54 DLR 28.
3 Re London School of Electronics [1986] Ch. 211.
4 [1987] 1 WLR 102.
5 Hoffmann J. in Re a Company, (1986) Supra.
6 [1989)]5 BCC 652
7 Re a company (No.004377 of 1986), Supra
8 ibid.
9 Re Boswell(Steels) & Co. Ltd [1989] 5 BCC 145,151.
10 Ex P. Holden [1991] BCLC 597; the transfer of shares here according to the pre-emption provision would deprive the petitioner of locus standi in the petition and so an order preventing transfer was made.
11 Re a Company (N0. 007623 of 1984) [1986] BCLC 362 at 368 per Hoffman J.
12 Re Abbey Leisure Ltd. [1990] BCC 60.

19.8.3 Where an act of the Board is not a fraud on the minority, the act is ratifiable. If duly ratified by the general meeting, the minority has no derivative action under exception to the rule in *Foss vs Harbottle*, as the members in general meeting can vote for their own personal interests.[1] If however the act complained of is prejudicial and if a reasonable man would consider the action to be to the detriment of the company, the action is unfair and even if duly ratified, the minority can still come under this section to the Court for protection. Even if the unfairly prejudicial conduct has been put right retrospectively it would still be unfairly prejudicial.[2]

19.8.4 **Motive of Majority** – In common law, the minority has no right or interest to examine the motive of the majority. Yet, the exercise of these powers may still be prejudicial to a minority's interest or legitimate expectation. However, in an action under section 233 of the Act, the motive of the controlling shareholders can be relevant. The court should decide if a reasonable man would regard the majority's conduct as unfairly prejudicial in that light.[3] It has been also held that the directors' duty to act for proper purposes was a duty owed to shareholders directly and not to the company as such.[4] This is because of the word 'interest" in the section as this allows courts to give relief even if strictly speaking the member has no right to complain at common law. In *Re a Company*[5] (a case for winding up) Vinelott J. found 'considerable force' in the argument that the phrase 'unfairly prejudicial to the interest of some part of the members ' in the English Act of 1948 would admit the contention that there is ' unfair exclusion from the management of the affairs of the company, if the interest of the minority shareholder under the agreement, express or implied, that he will be allowed to participate and to be paid remuneration is affected though his strict rights as a shareholder may not be.' Hoffman J confirmed a similar view in *Re a Company (No 008699 of 1985)*.[6] Thus, allotment of shares to dilute the minority's shareholding may be attacked on the ground that the allotment is for an improper purpose and not in the best interests of the company and therefore unfairly prejudicial.[7] This leads to the teasing question if it was bona fide in the company's interests to make a rights issue but to do so would have the effect of diluting the minority's shareholding then would the court give priority to the minority's interests. Probably not. In a similar case, Hoffman J. found that the directors were acting reasonably in what they believed to be the interests of the company but went on to add : 'Nevertheless, I do not think that the bona fides of the decision or the fact that the petitioner was offered shares on the same terms as other shareholders necessarily means that the rights issue could not have been unfairly prejudicial to his interests. If the majority know that the petitioner does not have the money to take up his rights and the offer is made at par when the shares are plainly worth a great deal more than par as part of a majority holding(but very little as a minority holding), it seems to me arguable that carrying through the transaction in that form could, viewed objectively, constitute unfairly prejudicial conduct.'[8]

As to the meaning of the phrase 'bona fide for the benefit of the company as a whole', the decision in *Allen vs Gold Reefs of West Africa Ltd.*[9] may be referred to.

Motive is relevant. As Latham CJ said in an Australian case that before the exercise of a discretionary power by directors will be interfered with by the court, it must be shown that they have acted for an improper motive.[10]

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1 Hogg vs Cramphorn [1967] Ch. 254.
2 Re Kenyon Swansea Ltd. [1987] BCLC 514.
3 See Rider (1979) CLJ 148; North West Transportation Co. vs Beatty [1887]12 AC 589;Burland vs Earle (1902) AC 83; Regal (Hastings) Ltd vs Gulliver [1942] 1 All ER 378;Northern Counties Securities Ltd. vs Jackson and Steeple Ltd [1974] 1 WLR 1133; and Clemens vs Clemens Bros. Ltd [1976] 2 All ER 268.
4 Re a Company (No 005136 of 1986) [1987] BCLC 82.
5 [1983] 2 All ER 854, 859
6 [1986] BCLC 382.
7 Re Cumana [1986] 2 BCC 453,495.
8 Re a Company(No 007623 of 1984) [1986] BCLC 362.
9 [1900] 1 Ch.656,671; Greenhalgh vs Arderne Cinemas Ltd [1951] Ch.286,291 Clemens vs Clemens [1976] 2 All ER 268; Sterndale MR in Sidebottom vs Kershaw Leases [1920] 1 Ch.154,168,172;Dafen Tinplate Co.Ltd vs Llanley Steel co. [1920] 2 Ch.124.
10 Mills vs Mills [1938] 60 CLR 150.

19.8.5 Delay may be a factor in granting relief to the petitioner. A delay of two and a half years was excused because the petitioner's solicitors and accountants were attempting to discover what had happened.[1]

Delay by itself will not bar the remedy but if the delay is evidence of acquiescence or condonation of a wrongful act, the court may not exercise its discretion in granting relief.[2] If the court is satisfied that the conduct arising from a single oppressive act will be a continuous course of oppression in its effect and there is no prospect of remedying the situation by the voluntary act of the party responsible for the act complained of, the court is competent to interfere by appropriate order.[3]

19.9.1 **Summary** – Whilst it is essential that the relevant prejudice has been caused unfairly, the test is an extremely wide one and allows the court to have regard to any circumstances that it considers to be relevant. Save by reference to decided cases , it is difficult to predict how the court will exercise its discretion. The court can take into account any of the following factors :

(1) Any misconduct on the part of the petitioner.[4]

(2) Any alternative remedy available to the petitioner; indeed in requiring a petitioner to accept a reasonable offer for his shares or to submit to the procedure of pre-emption provisions in the articles, the court is holding that the petitioner has another, more appropriate remedy. The mere fact that the petitioner may have another remedy , for example a common law action for damages based upon the same facts does not prevent the presentation of the petition.. Re a Company (No 0047 of 1986)[5] Nor is an unfair prejudice petition precluded by the fact that a derivative action might lie in respect of the conduct complained of.[6] Stay of proceedings under this section was not granted simply because there was an arbitration clause.[7]

(3) Any offer made to the petitioner.[8]

(4) The motives of those in control of the company. Even though discrimination between shareholders, whether intentional or not is not an essential ingredient of unfairness[9] many types of conduct will be unfairly prejudicial if the purpose or effect thereof is discriminatory in some way between shareholders but will not be so if those concerned have made a bonafide commercial decision in the interests of the company. The declaration of dividends and directors' salaries are two good examples. A rights issue is generally taken to be in the best interests of the company but may be discriminatory in certain circumstances. In Re Cumana[10] the directors were held to be acting reasonably if the majority knew that the petitioner did not have the money to take up the rights issue then it might constitute unfairly prejudicial conduct if the shares are offered at par when they are worth actually much more.

(5) Any delay in presenting the petition.[11]

Certain general principles should be remembered. Business agreements entered into freely are not unfair and if the conduct complained of involves merely the exercise of business judgment, the court will be extremely reluctant to interfere. But if the conduct complained of contains an element of conflict of interest between those in control and the

1 Re D R Chemicals Ltd [1989] 5 BCC 39.

2 Re Bengal Luxmi Cotton Mills Ltd [1965] 35 Comp. Cas.187(Cal);Re Hungerford Investment Trust Ltd vs Turner Morrison & Co. Ltd ILR [1972] 1 Cal 286.

3 Sindhri Iron Foundry(P) Ltd , In the matter of [1964] 34 Comp. Cas.510;68 Cal W.N. 118.

4 Re London School of Electronics [1986] Ch.211;

5 [1986] BCLC 376; [1986] BCC 99,171.

6 Re A Company [1986] BCLC 68; Re Stewarts Brixton Ltd [1985] BCLC 4 and Re Charnley Davis [1990] BCC 605,625.

7 Surendra Kumar Dhawan and another vs P.Vir and others [1977] 47 Comp. Cas 276(Delhi).A petition under this section cannot be stayed under section 10 C.P.C. :P.K.Guha vs W.B.Pharmaceuticals (Cal) [1982] 1 Comp. L.J. 199,203-205.

8 Re a Company(No 003843 of 1986) [1987] BCLC 562.

9 Re Sam Weller Ltd.[1990] Ch.682,691,

10 [1986] 2 BCC 22,453 and D.R.Chemicals Ltd. [1989] 5 BCC 39. But see Re A Company (No 007623 of 1984) [1986] BCLC 362

11 See Section 19.8.5 above.

minority shareholders the court will be less reluctant to interfere. Instances are : exclusion of quasi-partners, payment of dividends, payment of remuneration to directors and associates, rights issues, and dealings with associated persons.

The question sometimes arises as to whether an act in contravention of law is per se oppressive. In India the law contemplates an oppressive act within the ambit of the corresponding section. The Supreme Court of India commented as follows :

> ...an isolated act, which is contrary to law, may not necessarily and by itself support the inference that the law was violated with a malafide intention or that such violation was burdensome, harsh and wrongful. But a series of illegal acts following upon one other can, in the context lead justifiably to the conclusion that they are a part of the same transaction, of which the object is to cause or commit the oppression of persons against whom these acts are directed. [1]

The court has power to investigate charges even though the petition has contained no specific prayer for any relief.[2] The court has power to give directions to the board of directors for proper functioning of company.[3]

19.9.2 The court has been given a wide power to cancel or modify any resolution or transaction, to regulate the conduct of the company's affairs in future in such manner as specified by the court and even to amend any provision in the company's memorandum and articles of association.[4] The prime concern for the Court is to consider what order would fit and not exacerbate the dispute.[5]

In an unreported decision in the case of Anwar Hossain and another vs Uttara Valley Ltd. and others (Company Matter No. 4 of 2002) decided on 17 July 2004 his Lordship Mr. Justice Shah Abu Nayeem Mominur Rahman held that in order to attract the provisions of section 233 of the Companies Act there is no necessity to show a continuous act of oppression and where the company itself has suffered loss because of the act of majority shareholders an application under section 233 can not be disallowed merely on the ground that the petitioner has not come with clean hands. The Court declined to cancel the registered sale deeds in the said case under section 233 of the Companies Act and held that a civil court action is proper. The Court gave an option to the majority shareholders to buy the minority shareholders at a price to be determined by chartered auditors. The Court also observed that the jurisdiction under section 233 is wider than given in the corresponding section 397 of the Indian Act.

19.9.3 **Scope in Bangladesh** – Even before the introduction of this section in our Act, Justice Mustafa Kamal made a forward looking statement in 1985 that 'although there is no provision in our Companies Act analogous to section 210 of the Companies Act, 1948 of U.K. and section 397 of the Companies Act of India, still ex debito justiciae this court can pass appropriate orders for mitigating oppression on minority shareholders.'[6]

An auditor can be appointed for past years by the court in an application under section 233 of the Companies Act.[7]

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1 Needle Industries India Ltd. vs Needle Industries Newey (India) Holdings Ltd [1981] 51 Comp. Cas. 743,780. See Mohanlal Ganapatram vs Sayaji Jubilee Cotton and Jute Mills Co. Ltd AIR 1965 Guj 96.

2 Syed Muhammad Ali vs R. Sundramoorthy and others AIR 1958 Mad 587.

3 Lord Krishna Sugar Mills Ltd vs Smt. Abnash Kaur [1974] 44 Comp Cas 210(Delhi).

4 See section 19.6.4 above

5 Re Macro (Ipswich) Ltd. [1994] 2 BCLC 354.

6 Motiur Rahman vs May Industries 37 DLR (1985) 41,46.

7 Md. Faruk vs Abdul Hamid BLD (1998) (AD) 236.

MANAGING AGENTS

20.1.1 Sections 116-125 of the Act deal with managing agents. These sections correspond to sections 87A to 87I of the Act of 1913 which were inserted in our company law in 1936 recognising for the first time the important role that a managing agent used to play in the corporate world in the then British India.

20.1.2 **Origin and Development** – The managing agency system is a distinctive feature of company management in the sub-continent. This unique institution has no parallel in any other country and is a product of circumstances peculiar to the Indian sub-continent. It suited so well the needs of the commercial classes after the abolition of the East India Company's monopoly that it flourished and became embedded in the industrial structure of our country for more than a century.

Its origin can be traced in the historical, economic and geographical conditions which prevailed in the sub-continent in the third decade of the nineteenth century. Essentially, the result of British enterprise in India, the system was gradually developed by the older British managing houses, which were the first to realise the potentialities of developing trade between Britain and India and in trade by private traders and merchants.

British contact with India had begun in the sixteenth century, when Queen Elizabeth I granted a Charter to the East India Company giving it a monopoly to trade with the East Indies. The Company's servants were allowed to augment their paltry salaries by carrying on private trade in India. This they did through representatives, agents or agency houses, which subsequently came to be known as mercantile houses. This went on till the end of the eighteenth century, when the trade monopoly of the Company with India was curtailed by the Charter Act of 1793 and permission was given to private merchants to export native commodities to India in the Company's ships. The monopoly was finally abolished by the Charter Act of 1813. This abolition marked the beginning of a new era of English commercial activity in India, as it resulted in the transfer of the privilege of carrying on trade between Britain and India to a large number of private British traders and merchants, who used the existing agency houses. With the increase in their number and the development of commercial activity the importance of these houses increased and new agency houses came into existence. The long distances from the ports to the places where articles for export were produced, which were the first to receive the attention of these mercantile houses, facilitated the growth of this system while the absence of an investing class and the lack of even the elementary facilities, which were elsewhere provided by a capital market, brought the trade and industry of this period more and more under the control of the mercantile houses, which in many cases provided both finance and the promotional services necessary for the flotation of new undertakings in which they were described as managing agents. Thus, history, geography and economics, all combined to create and develop a system which, in some of its distinctive features, still retains a unique character.

Originally the function of these mercantile houses primarily consisted in importing British goods and exporting Indian goods and raw materials, as agents of the British agents or firms. In fact, vested interests in England were at one time sufficiently powerful to compel

the East India Company to concentrate on the export from India of the raw material necessary for manufacturers in England.[1]

In addition to their commercial and trading functions , the Calcutta mercantile houses also carried on financial activities and were responsible for introducing modern banking in India as an extension of trade in the European community there. These houses later frequently acted as investment bankers and provided funds for the establishment and operation of indigo plantations and so forth. Later, when tea gardens, jute mills and other kinds of industry were started, the same mercantile houses aided and became agents for them. Such was the important position held by some of those mercantile houses that their managers were sometimes called "Merchant Princes".

In due course of time the bulk of business controlled by the Englishmen came to be entrusted to these houses in India which later on came to be called managing agency houses or firms.[2]

The managing agency houses took advantage of the expanding English commerce trying to earn money from the Colonies and there was a mushrooming of business in India having connection with British counterparts. The managing agency houses supplied directors to look after the British company's interests in India and soon it became an invariable practice for newly – formed companies to entrust their business in India to these managing agencies, who looked after the company's interests while the investors and the board of directors in England quietly enjoyed the fruits of their enterprise without having to bother about the management. In return , the managing agency houses were remunerated handsomely on the basis of fixed pay and commission. They also gave advice and supplied technical know-how to would-be investors and helped them to promote companies here, in which, they would, normally secure a large interest. They would also promote companies themselves and retain a controlling interest in them. In practice the terms and conditions agreed upon between the agency houses and the managed companies were embodied in a written agreement and often formed part of the memorandum and articles of association of the managed company. Thus, the managing agency system is purely a product of British colonisation of India:

That the emergence of managing agency system was a result of lack of native expertise to run a commercial enterprise on a corporate basis is evident from the fact that in the United States of America where the British set up their colonies, no such system evolved because there was an ample supply of local indigenous talent. Corporate activity was common in America and the American investor was well able to look after the business himself. The service that the managing agency houses rendered in carrying on the trade between India and Britain was not required in America because of the proximity between the centre of production and the market itself. Circumstances peculiar only to the sub-continent were responsible for the growth of the managing agency system here.

Able Indian merchants followed in the footsteps of English mercantile houses; Parsis, Gujaratis and Marwaris promoted companies of which they became the managing agents. The "swadeshi movement" of 1905 gave added impetus to indigenous business and many new companies were founded, which were controlled by existing managing agencies. The managing agents rendered valuable service by providing money and technical know-how in an emerging market and it was a common feature for an entrepreneur to call upon a managing agency for assistance. Whereas in England and the United States it was customary to reward promoters by grants of cash or allocation of shares, Indian managing agencies were rewarded for the services rendered in promoting a company by being appointed a managing agent on generous terms. Promotion and management were performed by the same agencies resulting in concentration of control and management of capital in a few hands.

Strangely enough, not till 1936 did the Legislature see it fit to control exploitation by the managing agents in India. Possessing the technical know-how and the capital, those people

1 Report of the Indian Industrial Commission 1916-1918 (Calcutta 1918) paragraph 105.

2 Managing Agents: Their Powers and Functions by R.K.Goel-Journal of the Indian Law Institute, Vol.3 page 393.

were in a commanding position and by means of unconscionable contracts with the companies they promoted and managed , they devoured most of the profits earned. This alone discouraged the small-scale investors from acquiring interests in commercial corporations and situation became so blatantly unfair that Parliament intervened in 1936 and passed the Indian Companies (Amendment) Act, 1936, by which, for the first time , managing agents were given statutory recognition and restrictions were imposed on their activities. Since 1947 there had been a bitter controversy raging in both India and Pakistan as to whether the system had outlived its utility. There was little change in the law between 1947 and 1971 and the restrictions imposed by the Amendment Act of 1936 continued to exist but any managing agent appointed by a company would have to have the sanction of the Controller of Capital Issues who would certainly impose restriction on their salaries. In Bangladesh ,the Act of 1994 continues with the restrictions on managing agencies and any appointment of a managing agent has to have the approval of the Securities and Exchange Commission.

This system is meeting its natural death in Bangladesh and it is unusual for Bangladeshi companies to have managing agents now. We shall be dealing with the restrictions in the Companies Act of 1994 and some of the case law that illustrated the working of the system in the past.

20.1.3 **Position of a Managing Agent** – The powers of a managing agent spring entirely from the contract of managing agency, subject to the statutory restrictions thereon. As the Indian Companies Act was, upto 1936, almost a verbatim reproduction of the English law, which did not recognise the system of managing agency, the managing agents had a free hand to enter into management contracts with the company. Even after the Amendment Act of 1936, inserting sections 87A to 87I in the Companies Act of 1913 relating to managing agents, their powers were determined in accordance with the law of contract so that they were usually able to secure contracts which placed but few restrictions on their powers of management. Thus Mr.R.K.Goel cites the case of the Rodier Textile Mills Ltd,[1] where clause 3 of the managing agency agreement, after stating that the managing agents shall be under the control and direction of the directors, provided in explicit terms that, in respect of exercise of powers specifically defined in other clauses of the agreement, the managing agents "shall not be under the control and direction of the directors". The excepted powers covered almost the whole field of management, including appointment and dismissal of servants and officers, making of purchase and sales, nominating attorneys and signing contracts.

The managing agents not only usurped all the powers of management but swamped the board of directors with their nominees. Another method of securing control was to issue to themselves or their nominees deferred shares of low nominal value but with voting rights equal to those of ordinary shares of a much higher value.

The difference between a managing agent and a manager is that a managing agent derives his powers under a contract with the company and may be a person, firm or company[2] whereas a manager is an individual who may act subject to the superintendence, control and direction of the board of directors under a contract of service.[3] A managing agent enjoys much greater autonomy than a manager and a typical managing agency contract if entered into in the United States, would be probably struck down as an illegal abdication of the directors' duty to manage. Thus, in *Abercombie vs Davies*[4] the plaintiffs, minority stockholders in a corporation asked the court to declare invalid an agreement between the majority stockholders and their "agent-directors" for the management of the business. It was held that the agreement was an unlawful attempt to encroach upon the directors' exercise of

1 Journal of the Indian Law Institute, Vol. 3, 393,404

2 Section 2(l) of the Act of 1994

3 Section 2(k) of the Act of 1994.

4 (Delaware 1956) 123 Atlantic Reporter (2nd.) 893

independent business judgment and might possibly permit a director's action to be dictated by an outsider.

The Supreme Court of India held in *Jute and Gunny Brokers Ltd. vs Union of India*[1] that service of notice on the managing agent of a company would be good service on the company even though the managing agent were itself a corporation.

The managing agent has thus a very high contractual status and because of this the managing agent is not entitled to enforce his rights by a writ of mandamus.[2]

What then is the nature of an office of managing agency ? It has been held that for the purpose of taxation a managing agency is a business and profits therefrom are assessable.[3] Also, the Supreme Court of India has held that the office of managing agency is not only a business, but is " property' within the meaning of section 4(3)(i) of the Income Tax Act,1922.[4]

In *Octavius Steel and Co. Ltd vs Commissioner of Income Tax*[5] the Supreme Court of Pakistan rejected the argument of Mr Suhrawardy that the connection between the managing agent and the managed companies was of a professional or vocational character. Cornelius C.J. held that the managing agents were 'running these companies efficiently and producing profits from year to year and they are not content with seeing things at second hand.'[6]

This case was distinguished from the Steel Brothers Case[7] where the managing agents whose head quarters were in London, were to get a commission on all sales of products.

Whatever rights a managing agent has, therefore, spring from the contract of managing agency. In fact his position is that of a party contracting with the company and any change in the agreement must be ratified by the company and the managing agent in order to be effective.[8]

20.1.4 **Appointment of and Vacation of Office of Managing Agents** – The terms of the appointment of the managing agents are embodied in the agreement between him and the company. They are sometimes entrenched in the memorandum and articles of association. Sections 116 and 117 of the Act of 1994 impose conditions on appointment of managing agents. Section 116 lays down that no managing agent shall hold office for more than twenty years and not more than ten years at a time. The agent is of course protected by way of having a charge on the assets of the company by way of indemnity for all liabilities or obligations properly incurred by the managing agent on behalf of the company.[9]

Section 117 (a) permits a company to remove a managing agent by a resolution passed in the general meeting if the agent is convicted of a non-bailable offence. Similarly, the office of a managing agent shall be deemed to be vacant if he is adjudged insolvent.[10] Section 117 further lays down that a transfer of his office by a managing agent shall be void unless approved by the company in general meeting. Provided that where a managing agent is a firm, a change in the partnership shall not be deemed to operate as a transfer of the office of managing agent, so long as one of the original partners shall continue to be a partner of the managing agent's firm.[11] A charge or assignment of his remuneration or any part thereof

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1 [1962] Comp. Cas. 845.

2 Arunchalam Chettiar vs Kaleeshwar Mills Ltd. AIR 1957 Mad.309 distinguishing In re Albert Mills Co. Ltd (1872) 9 Bom H.C.R. 438 which had held that the High Court had jurisdiction to enforce by mandamus the rights of a duly elected director. Also see Maqbool Elahi vs Khan Abdul Rahman PLD(1960) S.C. 266.

3 Lakshminarayan Ram Gopal vs Govt of Hyderabad AIR 1954 SC 364.

4 J.K.Trust, Bombay vs Commissioner of Income Tax J.K.Trust, Bombay vs Commissioner of Income Tax , AIR 1957 SC 846.

5 PLD(1960) S.C. 371.

6 ibid at page 378.

7 (1951) 19 I.T.R. 435.

8 Bhagwanji Morarji Goculdas vs A.C. Works Ltd AIR 1944 Bom 205.

9 section 116(3).

10 sub-section (b) of section 117.

11 subsection (c)

effected by a managing agent shall be void against the company.[1] On the winding up of the company the contract of management with the managing agent is automatically terminated, without prejudice to the right of the managing agent to recover any monies recoverable by the managing agent from the company. Provided that where the court finds that the winding up is due to the negligence or default of the managing agent himself, the managing agent shall not be entitled to receive any compensation for premature termination of his contract of management.[2]

Section 117(f) of the Act provides that the appointment of a managing agent, the removal of a managing agent and variation of managing agent's contract of management shall not be valid unless approved by the company in general meeting.

Section 117 is the corresponding section of section 87B of the Act of 1913. It was held by the Dhaka High Court in the case of *Eastend Agencies vs Mafizuddin*,[3] that the proviso to section 87B(c) to the Act of 1913 simply means that when managing agency happens to be a firm, transfer of the interest of the original partners to new comers shall not be considered as a transfer of the office of the managing agent so long as at least one of the original partners continue to be a partner of the managing agent's firm and no approval of the members of the managing agency by the managing agent's firm is called for. There seems to be an error in the reporting of this case as the last three words are not there in the case report but the whole sentence without these three words seem to be meaningless. On this point see also The Associated Industrial Engineers vs P.A. Jabbar Sahib and others.[4]

A transfer by the managing agent of a company of his office amounts to a transfer of his liability under a contract and would be void against all others without the consent of the company. Hence section 87B(c) of the Act of 1913 would apply also to the case of the transfer of the office of the managing agent to himself and certain others.[5]

Section 117 (d) of the Act restrains the voluntary alienation by the managing agent of his remuneration to the detriment of a company. But it does not bar a compulsory sale at the instance of a creditor.[6]

It has been further held in that case that in view of section 87B(f) (i.e., section 117 (f) of the current Act) , the board of directors has authority to appoint new firm of partners to continue the work of managing agents only by way of temporary arrangement until the members of the company appoint the managing agent under the powers vested in them by section 87B(f) of the Act of 1913.[7]

Where the articles provide that the managing agents are removable by an extra ordinary resolution of the company, passed at an extra ordinary general meeting , of which six months notice should be given and at which persons holding not less than three quarters of the issued ordinary capital of the company are present, an ordinary resolution at a general meeting passed by a majority of sixty-eight percent of the shareholders entitled to vote dismissing the managing agent is inoperative and invalid.[8]

The managing agency agreement, being in essence, a contract of service, the managed company can remove a managing agent for misconduct or incompetence. The Judicial Committee of the Privy Council held that in considering the degree of misconduct that will justify the termination of the employment of the managing agents, the same principle applies as in the case of master and servant. In each case the question must be whether the misconduct proved or reasonably apprehended has such a direct bearing on the employer's

1 ibid.subsection (d).

2 ibid sub-section (e).

3 20 D.L.R. 1056

4 AIR 1953 Mad 197.

5 Ramchandera vs Chinubhai AIR(1944) Bom 76.

6 Pursattamdar Gujrati vs Lala Baijnath Prasad AIR 1941 Cal 240.

7 ibid. at para 28.

8 Ramkissendas vs Satya Charan Law (1946) 50 C.W.N. 310; affirmed by the Privy Council on this point in AIR 1950 P.C. 81.

business in which he is employed as to seriously affect the employer's business or the efficient discharge of the employee's duty. [1]

Neither the Act of 1913 nor the Act of 1994 provides for a managing agent resigning his office. Although it was for the managed company to complain if its managing agent unexpectedly resigned, in practice what usually happened was that a managing agent resigned in favour of a new-comer either in collusion with the latter or with his full knowledge, on the tacit understanding that the retiring managing agent would receive suitable compensation from the company for loss of office.

20.2.1 **Right to Manage** – The rights of a managing agent to manage a company are contained in the managing agency agreement. Sometimes they are also entrenched in the memorandum and articles of association of the company. This, however, does not give the managing agent an inviolable protection, as the courts are prone to view such a provision in the constitution of the company as mere evidence of the contract of managing agency. This contract is a service contract and the courts are reluctant to burden a company with an undesirable managing agent, whether or not his services are guaranteed by the constitution of the managed company.

In the early case of *N.M.Panday vs Gordon*[2] the court refused to compel a company to retain a managing agent although the directors had no right to interfere in the management of the company and the managing agents were appointed for twenty five years under the memorandum and articles of association of the company.

However, in the case of *Ramkissendas vs Satya Charan Law*[3] it was held that the courts will set aside the dismissal of a managing agent, if it has not been done according to the procedure laid down in the articles of association.

If the managing agent has no more right to enforce a contract entrenched in the memorandum and articles of the company than a third party, can he do so if he holds shares in the managed company and sues as a shareholder for a declaration that the company is bound to obey its constitution? The Bombay High Court rejected this plea in *Ramkumar Potdar vs Sholapur Spinning and Weaving Company*[4] and said that the real purpose of the plaintiff seemed to be to enforce specifically a contract of personal service. In this the Bombay High Court seemed to differ from the Madras High Court which refused to strike out a clause in the memorandum of association of a company which took away the power of the company to terminate the managing agency.[5]

The Bombay High Court held that sanction of the court was not necessary for an alteration of a provision in the memorandum of association relating to appointment of a managing agent as this was merely a detail of management for the purpose of carrying on the business of the company.[6]

Section 10 of the Acts of 1913 and 1994 specifically exempt from its operation any provision in the memorandum of association relating to the appointment of a manager or a managing agent.

20.2.2 **Right to Remuneration** – The main reason why the old mercantile houses undertook the management of the business of companies incorporated in the far-off British Isles was the handsome remuneration they received under their managing agency contracts, which generally gave them fat salaries and commission in consideration of the exercise of their special skills in conducting business in India. The Act of 1936 introduced provisions in the

1 Morarji Goculdas and Company vs Sholapur Spinning and Weaving Company AIR 1944 P.C. 17. relied on by the Indian Supreme Court in K.T.Chettiar and another vs K.M. Chettiar AIR 1961 S.C. 1225.

2 ILR(1991) 6 Bom 266

3 AIR 1950 P.C. 81

4 AIR 1934 Bom 427

5 Venkataramana vs Coimbatore Bank AIR 1924 Mad 126

6 Ramchandra vs Chinubhai AIR 1944 Bom 76.

Companies Act of 1913 which limited their remunerations to office allowances and a percentage of the net annual profits of the company.[1]

Any stipulation for remuneration additional to, or in any form other than, the remuneration allowed shall not be binding on the company unless sanctioned by a special resolution of the company.[2] The law also defines what is meant by 'net profit' and lays down the method and principle of its calculation but exempts a private company not being a subsidiary of a public company and an insurance company.[3] This is probably because the profits of an insurance company are calculated on actuarial methods.

The managing agents were held to be entitled to remuneration for services rendered and for expenses incurred in promoting the company although no agreement had in fact been executed.[4] Another example where the managing agents were entitled to recover expenses incurred on behalf of the company and just compensation for loss of office is *Re Karnal Electric Supply Company Limited.*[5]

These were cases of unfair dealing by the directors of the managed company and the court hastened to put things right. In the vast majority of cases, however, the managing agency contracts were unconscionable bargains forced on the managed companies by people who bled them white until the intervention by the legislature and insertion of section 87C in the Act of 1913 now retained in its entirety in the Act of 1994. The Controller of Capital Issues had, previously, and now the Securities and Exchange Commission requires that the remuneration to managing agents should not exceed five to seven and half percent of the net profits of the company.

As to at what point of time profits accrue and the managing agent earns his remuneration the cases of *Commissioner of Income Tax, Madras vs Thiagarava Chetty and Co*[6] and *Commissioner of Income Tax vs Chamanlal Mangaldas*[7] and Cotton Agents Ltd vs Commissioner of Income Tax[8] *Commissioner of Income Tax, Delhi vs The Delhi Flour Mills,*[9] *Godrej and Company vs Commissioner of Income Tax Bombay*[10] and *S.Ganesan vs A.K.Josceleyne*[11] may be referred to.

The right to receive a remuneration as stipulated in the managing agency agreement is a contractual right and the company is bound to pay compensation if the managing agents's services are arbitrarily dispensed with. The Madras High Court held that the contract of managing agency could not be terminated by a resolution of the board of directors and continued upto the time the company went into liquidation. [12]

20.3.1 **Investigation of Managing Agents** – In 1968 during the Pakistan period by a further amendment of the Companies Act, section 87BB was inserted in the Act of 1913. This section, now reproduced in section 118 of the Act of 1994 provides for investigation of managing agents. If the Government has reason to believe that the managing agent of a public company has been guilty of fraud, misfeasance or breach of trust in connection with the conduct or management of the affairs of the company or has been conducting the affairs of the company for a fraudulent or unlawful purpose or has so conducted or managed the affairs of the company as to deprive the shareholders of a reasonable return on their investment then the Government may after giving the managing agent an opportunity of

1 section 87C(1) corresponding to section 119(1) of the Act of 1994.
2 ibid sub-section (2).
3 ibid sub-section (3)(4).
4 Meenakhi Mills vs Callianji and Sons AIR 1935 Mad 799.
5 [1956] Comp Cas 387.
6 AIR 1953 S.C.527.
7 AIR 1960 SC 1336.
8 AIR 1960 SC 1279.
9 AIR 1959 SC 185.
10 [1954] Comp Cas 35.
11 [1957] Comp Cas 114.
12 The Associated Industrial Engineers vs P.A. Jabbar Sahib and others AIR 1953 Mad 197.

being heard, appoint an investigator to enquire into the affairs of the company to report on the conduct of the managing agent. The shareholders of a company shall be deemed to have been deprived of a reasonable return on their investment if, having regard to enterprises similarly placed, the company is unable to or does not declare any or an adequate dividend for a continuous period of three years.[1]

The investigator has powers to enter the premises of the company or the office of the managing agent and may call for and inspect the books of account and take these into his custody. He has the same powers as are vested in a court under the Code of Civil Procedure with regard to summoning and enforcing the attendance of any director or officer of the company or compelling the production of any books of account and issuing commissions for examination of witness and any proceeding before the investigator shall be deemed to be a judicial proceeding.[2]

If the government after considering the report submitted by the inspector is of the opinion that it is necessary in the interest of efficient management of the company, the government may, after giving the managing agent an opportunity of presenting his case, modify the terms of the managing agent's agreement of management or require him to carry out changes in the management or accounting procedures or remove the managing agent or any director nominated by him from office.[3] The managing agent so removed shall not be entitled to be paid any compensation or damages and the government may appoint an administrator to manage the affairs of the company.[4]

This is a big power given to the government to interfere in the management of the company and this law was made in the hey days of managing agencies mostly rampant in the then West Pakistan. The law was passed to bring powerful commercial houses in line with the government. Fortunately not many cases of application of this law was made in the then East Pakistan and after liberation in Bangladesh.

20.3.2 **Restrictions on Managing Agents** – Sections 120 and 121 of the Act of 1994 replicate sections 87D and 87E of the Act of 1913. Managing agents, like directors, are not permitted to take loans from the company and cannot enter into any contract for the sale, purchase and supply of goods and materials with the company except with the consent of three-fourths of the directors present and entitled to vote on the resolution.[5]

Also, no company which is under the management of a managing agent shall make any loan to or guarantee any loan made to any company under management of the same managing agent. This restriction shall not apply to a loan or guarantee to a company under its own management or to a subsidiary.[6]

Section 122 prohibits a company other than a company whose principal business is the acquisition and holding of shares, stocks, debentures or other securities from purchasing shares or debentures of any company under management by the same managing agent unless the purchase has been previously approved by a unanimous decision of the board of directors of the purchasing company.

Section 123 restricts the powers of a managing agent to issue debentures except with the authority of the directors and within limits set by them and a power to invest the funds of the company or any delegation of any such powers to a managing agent shall be void.

A managing agent is further prohibited from engaging in business which is competing with business of the managed company[7] and may not appoint more than one-third of the total number of directors in the board of a company other than a private company.[8]

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1 ibid: Explanation to sub-section 1.
2 ibid : sub-section (2)and (3)
3 ibid: sub-section (4)
4 ibid : subsections (5) and (8).
5 section 120(1)(5).
6 section 121 (1)
7 section 124
8 section 125.

20.3.3 All these sections seek to ensure that a managing agent , while managing a company, is not given the freedom to control its purse for his own purposes to the detriment of the investing shareholders. However, there are loopholes in the restrictions on managing agents. Thus, although section 122 regulates inter-company investments, there is no limit on the amount of inter-company investment which can be made with the unanimous approval of the board of directors of the purchasing company. Also, there is no bar if one of the companies has no managing agent even though the managing agent concerned may be otherwise interested in the company.

20.4.1 **Liabilities of a Managing Agent** – The Companies Act, in general, provides for liabilities of the directors, officers, managers and managing agents of a company for any misfeasance or non feasance done. For example, section 398 provides penalty for wrongful withholding of property belonging to the company; this applies equally to any director, managing agent, manager or other officer or employee of the company.

A managing agent is bound to exercise the duty of skill and care that his position demands and he will not be allowed to take advantage of his own defaults. Thus, the managing agents were liable to pay back the money which they raised by mortgaging the company's factories although they claimed (but could not prove) that they had lent the money.[1]

The question that the court would ask was whether the misconduct proved or reasonably apprehended had such a direct bearing on the employer's business in which he was employed , as to seriously affect the employer's business or the efficient discharge of the employee's duty.[2] If a managing agent commits any default in the course of his duty , he cannot avoid liability on the plea that the statute punishes a 'manager' and not a 'managing agent'. The management of the company, being entrusted to a managing agent, the courts will expect him to perform the duty of a manager if he is, in fact, in charge of that job.[3]

A managing agent is a servant of the company but, because of the large powers and duties entrusted to him , he has a duty to protect the interests of the company. He cannot take advantage of his position to make profits and he is accountable to the company for any gains he makes.[4]

The various provisions of the Act of 1994 which oblige any officer of a company to return the company's property in case of a winding up, apply to a managing agent. Section 335(1)(b) provides that a managing agent will be punished with imprisonment for a term of two years, if he does not deliver upto the liquidator all property that remains in his custody at the time of the winding up of the company, and which he is legally bound to return. Section 398 provides a penalty for wrongful withholding the company's property and gives power to the court trying the offence to order the managing agent to refund it. Section 331 gives power to the court to assess damages against a delinquent director, manager, liquidator and any other officer of the company, if the latter has misapplied, retained or been guilty of misfeasance or breach of trust in relation to the conduct of the affairs of a company. Although a managing agent is not named specifically, there is little doubt that these sections apply to him, if he, in fact, was in charge of the management, for, the courts will not distinguish between a managing agent and manager in this regard.[5] However, if a managing agent is charged under the Penal Code, then he must be proved to be guilty of an offence within the ambit of the Penal Code. In the case of *A Sarkar vs Emperor*[6] the court rejected the accusation that the managing agent was extravagant as no judge or lawyer without an intimate knowledge of business can estimate how much or how little it is necessary to spend on management.

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1 Indo Enamel Works Ltd vs Ihsan Elahi PLD 1953 Lah 375.
2 Morarji Goculdas and Co. vs Sholapur Spinning and Weaving co.AIR 1944 PC 17.
3 Tota Ram vs Emperor AIR 1916 Lah 199.
4 India Sugar Refineries Ltd vs Estate of Ramalingam (1953) Comp Cas 107 (Mad).
5 Tota Ram vs Emperor AIR 1916 Lah 199 .In re Verappau AIR 1944 Mad 424.
6 (1935) ILR 63 Cal 18.

20.5 **Conclusion** – Ever since 1947 a controversy has been raging on whether the managing agency system has outlived its utility and should be abolished. The Pakistan Company Law Commission was of the opinion that although the system had bred serious abuses in the corporate sector it should be progressively abolished. In Bangladesh the law imposes certain restrictions and the system is left to have a natural death as entrepreneurs need no managing agent to help them set up an industry and there is no need for any managing agency which is becoming increasingly rare and will soon be a relic of the colonial past.

WINDING UP

21.1.1 Sections 234-321 of the Companies Act 1994 deal with winding up of a company. The Act divides in Part V in several chapters the modes of winding up, the provisions relating to contributories , winding up by court, official liquidators, powers of court, enforcement of and appeals from orders, voluntary winding up, members' voluntary winding up, creditors' voluntary up, and winding up subject to supervision of court. As most cases concern winding up a company by court we shall be dealing with the case law on that topic with a topic wise discussion of the other chapters.

21.1.2 A company may be wound up either by the court or voluntarily or subject to the supervision of the court.[1] A voluntary winding up may be either a members' voluntary winding up[2] or a creditors voluntary winding up.[3]

Companies registered under the Act can be put to an end only either through the machinery of a winding-up or its name being struck off the register under section 346 of the Act. If a company is not duly registered under the Act or is an illegal association then it is doubtful whether the court can wind it up.[4] But unregistered companies coming under Part IX of the Act may be wound up under section 372. Liquidation proceedings cannot be challenged in writ petitions.[5]

A company in liquidation, though the administration of its affairs has passed to the liquidator, retains its complete existence . If the liquidation should be annulled the company will resume its powers.[6] But a winding up order which becomes final cannot be rescinded and the proper course is to apply for an order staying the proceedings under section 253 of the Act.[7] To wind up a foreign company it is not necessary to show that a foreign company should have its registered office within the jurisdiction of the court; it is enough if it is shown that the company has an office and has assets and liabilities within the jurisdiction or carries on business in this country.[8] A banking company can be wound up under the provisions of the Bank Companies Act and with its assets and liabilities a separate banking company can be formed under section 77 of the said Act. The most famous example of this is the vesting of the assets and some liabilities in Bangladesh of the Bank of Credit and Commerce International S.A. in Bangladesh in a newly formed banking company, the Eastern Bank Ltd.

21.2.1 **Contributories** – Section 235 provides that in the event of a company being wound up, every present and past member shall, subject to certain qualifications, be liable to

1 section 234 of the Act of 1994.
2 section 286
3 sections 297-305.
4 Re National Debentures and Assets Corporation [1891] 2 Ch. 505.
5 Md. Abu Yusuf vs Bangladesh and ors (1993) BLD (AD) 154.
6 Viscount Cave in Employers Liability Assurance Corporation vs Sedgwick Collins & Co. (1927) A.C. 95.
7 Re Intermain Properties Ltd .[1986] BCLC 265 Ch.D.
8 See In re Mercantile Bank of Australia [1892] 2 Ch. 204; In re Calcutta Jute Mills Ltd. ILR 5 Cal 888.

contribute to the assets of the company to an amount sufficient for payment of its debts and liabilities and the costs, charges and expenses of the winding up. However, a past member shall not be liable to contribute if he has ceased to be a member for more than a year or for debts contracted after he ceased to be a member or unless the existing members are unable to satisfy the contributions required to be made by them. In the case of a company limited by shares no contribution shall be required from any member exceeding the amount if any, unpaid to the shares in respect to which he is liable. In the case of a company limited by guarantee, no contribution shall be required from any member exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up.

In the winding up of a company limited by guarantee which has a share capital (this is of a rare species nowadays) every member shall be liable to pay the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up and an amount to the extent of any sums unpaid on any shares held by him.[1]

A shareholder of a company limited by shares or guarantee , therefore is liable to pay only upto the amount contracted by him to be paid in the memorandum of association by him or his predecessor in interest. Any new shareholder will be deemed to be aware of the constitution of the company and hold the shares subject to its conditions (section 22) and does contract for a liability only upto the extent provided in the memorandum and articles of association of the company.

21.2.2 The relevance of being a contributory or not is seen when the court examines whether a petitioner for winding up has anything to gain if a company is wound up. If the petitioner is a fully paid shareholder and has nothing to gain if a company is wound up because there will be no surplus asset the court may look hard at his motive for presenting a petition for winding up. The court will not, as a rule, order a winding up on a contributory's petition unless he alleges in the petition, and proves at the hearing, at least to the extent of a prima facie case, that there will be assets for distribution among the shareholders or that some disadvantage would accrue to him by virtue of his membership which could be avoided or minimised and a purely private advantage will not suffice.[2]

Unless there are sufficient interests a contributory has no interest in winding up. However, if there is any chance that the assets will be of some value, the court will entertain the petition.[3] A contributory's petition which is opposed by majority of the contributories will usually not be granted except in a case of bad conduct by the majority[4] or the main objects of the company have failed.[5] If directors who are not contributories wish to bring a petition they must be acting unanimously.[6]

A single bench of the Dhaka High Court held that a petition for winding up by a fully paid up share holder on the ground of insolvency of the company per se cannot be said to be not maintainable but the Court looks askance at such petition as his interest is least affected in winding up, he being a fully paid share holder. There is nothing to lose by the continuance of the company and nothing to gain by its winding up. The court will, therefore, seldom use its discretion in such a case unless the petitioner makes out a special case or there is a strong ground for interference justifying the use of its discretionary power on just and equitable ground.[7] The case related to a petition for winding up on the ground that it was just and equitable that the company should be wound up. A large number of decisions were cited at the Bar on the relevance of the wishes of the majority of creditors and shareholders but the

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1 sub-section (2).

2 Charlesworth and Morse : Company Law 14th Ed. p.450 citing Re Rica Gold Washing Co.[1879] 11 Ch.D. 36 (C.A.);Re Martin Coulter Enterprises Ltd [1988] BCLC 12;Re Instrumentation Electrical Services Ltd [1988] 4 BCC 301 and Re Chesterfield Catering Co. Ltd [1976] 3 All E.R. 294.

3 Re Martin Coulter Enterprises Ltd. Supra.

4 Re Middlesborough Assembly Rooms Co [1880] 14 Ch.D. 104

5 Re German Date Coffee Co. Ltd [1882] 20 Ch.D. 169; Re Perfectair Holdings Ltd [1989] 5 BCC 837.

6 Re Instrumentation Electrical Services Ltd [1988] 4 BCC 301.

7 Mahmudur Rahman vs Manipur Tea Co. 28 DLR (1976) 133.

court also considered the fact that the petitioners being a fully paid shareholder had nothing to gain . The court relied on Indian decisions and noted that a fully paid share holder of an insolvent company who has really no interest in a winding up must make out a very special case indeed and the ground of company's inability to pay its debt is virtually unavailable to him.[1] The court further cited from Palmer's Company Precedents that a fully paid-up shareholder is a contributory, and as such, entitled to present a winding up petition but it is desirable, if possible, however, to allege the existence of assets available for contributories.[2]

A member's liability to contribute is restricted to so much of the amount left unpaid on their shares.[3]

Section 237 terms a contributory as a person liable to contribute to the assets of a company in the event of its being wound up. It refers to only past and present members and their legal representatives and not to debtors.[4]

Mr. Justice Mainur Reza Chowdhury has said that it would appear from the definition of "contributory" and his liability as narrated above that it means a shareholder member of the company who is required to contribute to the assets of the company in the event of its being wound up i.e., those shareholders who have not fully paid for the shares allotted to them ; no contribution shall be required from any member who has fully paid for his shares. It therefore appears that a contributory means a holder of partly paid shares.[5] In that case the court was dealing with a preliminary objection to a petition for winding up that the applicant had no interest in the winding up, he being a shareholder of a company which held shares in the company sought to be wound up. The learned judge relied on an English decision *Re Chesterfield Catering Co Ltd.*[6] that in order to establish his locus standi to petition for the winding up of a company, a fully paid shareholder had to show that he had a sufficient interest in that, if the company were wound up, he would, as a member, receive some advantage or avoid or minimise some disadvantage which would accrue to him by virtue of his membership of the company and that the mere fact that the petitioner would derive some private advantage from a winding up unconnected with his membership could not constitute a sufficient interest. In the instant case before the Dhaka High Court the petitioner who was not even a shareholder of the company sought to be wound up was held to have had no locus standi to file the petition for winding up.

Section 238 provides that the liability of a contributory shall create a debt payable at the time specified in the calls made on him by the liquidator. This is a statutory debt.[7] The liability can only be extinguished by payment.[8] For the purpose of limitation the time will commence when the call is made.[9]

Sections 239 and 240 provide for cases where a contributory dies or becomes insolvent. In case of death his legal heirs shall be liable to contribute to the assets of the company[10] and in case of insolvency the assignee shall represent him and the estate of the insolvent shall have to bear the costs of any payment by way of contribution to the assets of the company.[11]

21.3.1 Winding Up by Court – Section 241 is one of the sections that are seen most often on the list of cases in the Company Bench of the High Court Division. This section provides for circumstances in which a company may be wound up by the Court. These are :

1 V.V.Krishna Iyer and Sons vs New Era Manufacturing Co. AIR 1965 Ker 241 cited by the Dhaka High Court at page 150.

2 28 (1976) DLR at p. 157.

3 Eve J. in In re City of London Insurance Co. Ltd [1932] 1 Ch 226; In re Apex Film Distributors Ltd [1960] 1 All E.R. 152.

4 Re Lakshmi Flour Mills Co AIR 1926 All 101;Re Marran and Co. AIR 1937 Oudh 377; Punjab S. Chhatar vs Lahore Bank AIR 1932 Lah 648.

5 Mazharul Haque vs Bulk Management Ltd. 48 DLR (1996) 453,456= (1996) BLD (HC) 575; also See Rehana Ahmed vs Nahar Shipping Lines Ltd. 44 DLR 256 (HC).

6 [1976] All E.R. 294

7 Marulasiddanna Gowda vs Liquidators, Mysore Malleable Iron and Steel Foundry Ltd AIR 1963 Mys 61.

8 In re Apex Film Distributors Ltd (1960) 1 All E.R. 152; Montgomery vs Sikdar Iron Works Ltd AIR 1932 Cal 691.

9 Narasingha Iyengar vs Official Assignee of Madras ILR 54 Mad 153.

10 section 239

11 section 240.

i) if the company has by special resolution resolved that the company be wound up by the court;

ii) if default is made in filing the statutory report or in holding the statutory meeting;

iii) if the company does not commence its business within a year from its incorporation, or suspends its business for a whole year;

iv) if the number of members is reduced, in the case of a private company below two, or, in the case of any other company, below seven;

v) if the company is unable to pay its debts;

vi) if the court is of opinion that it is just and equitable to wind up the company.

Section 242 follows up and explains when a company will be deemed to be unable to pay its debts. These will be if a creditor to whom the company is indebted for a sum exceeding taka five thousand then due gives a notice to the company to pay the sum and the company neglects to pay the sum for three weeks or if execution or other process issued on a decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part or if it is proved to the satisfaction of the court that the company is unable to pay its debts and in doing so the court shall take into account the contingent and prospective liabilities of the company.

Section 245 provides that an application for winding up of a company shall be presented either by the company or by any creditor (including a contingent or prospective creditor) or contributory or by the Registrar.

A contributory shall not be entitled to present a petition for winding up a company unless either the number of members is reduced in the case of a private company, below two, or in the case of any other company below seven or the contributory has had held the shares for at least six months in the eighteen months before the petition for winding up was presented.[1] The Registrar shall not be entitled to present a petition for winding up of a company except on the ground that it appears from the financial condition of the company as disclosed in the balance sheet or from the report appointed under section 195 or in a case falling within section section 204 (which authorises the Registrar to present such a petition if it so appears to the Government from the Report of the Inspector under section 202 of the Act) after a previous sanction of the Government has been obtained for such presentation. No such sanction shall be given unless the company has been given an opportunity of being heard.[2] A petition for winding up of a company on the ground of filing the statutory report or in holding the statutory meeting shall not be presented by any person except by a shareholder nor before the expiration of fourteen days after the last day on which the meeting ought to have been held.[3] The court shall not give a hearing to the petition for winding up by a contingent or prospective creditor until a reasonable security has been given.[4]

Once a company has been ordered to be wound up it shall operate in favour of all the creditors and of all the contributories in the company as if the winding up order was made on a joint petition of a creditor and of a contributory.[5]

A winding up of a company by the court shall be deemed to commence at the time of the presentation of the petition for winding up.[6]

The court may pass such order as it deems fit including adjournment, dismissal of the petition, interim orders or adjourning the hearing conditionally or unconditionally,[7] and when a winding up order has been made or a provisional liquidator appointed, no suit or other legal proceedings shall be proceeded with or commenced against the company except with leave of court.[8]

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1 section 245(a).
2 section 245 (b).
3 section 245(c).
4 section 245(d).
5 section 246.
6 Section 247.
7 section 249
8 section 250.

A copy of winding up order shall have to be filed by the petitioner with the Registrar within thirty days of the making of the order and the Registrar shall then register a summary thereof in his books relating to the company and shall notify in the official gazette that such an order has been made. The winding up order shall be deemed to be notice of discharge to the servants of the company except when the business of the company is continued.[1]

The court may, at any time after an order for winding up has been made, on the application of a creditor or contributory, make an order staying the proceedings either altogether or for a limited time on such terms and conditions as the court thinks fit if the court is satisfied that such order for stay should be made.[2] The court in matters relating to winding up may have regard to the wishes of the creditors or contributories.[3]

21.4.1 Sections 241 and 242 of the Companies Act 1994 correspond to sections 162 and 163 of the Companies Act 1913 and sections 433 and 434 of the Indian Companies Act 1956.

The Indian Courts have held that the word 'may' in the beginning of section 241 means that the court has discretion in taking a decision under all clauses of that section. The discretion, no doubt, is to be exercised in a judicial manner.[4] Also that a winding up order is not granted mechanically as a matter of course on proof of certain facts and the provisions of section 242(1) determine when the requirements of section 241(e) will be deemed to be fulfilled but they do not lay down when a winding up order must necessarily be passed. But the court may, if there are sufficient counter balancing equitable grounds , deny an immediate winding up order, or, in appropriate cases, even refuse it altogether inspite of the proved inability of a company to pay its debts.[5]

On the question of failure to commence business the Patna High Court has held that the decisive question is whether there is a reasonable hope of the company commencing or resuming business and doing it at a profit and whether the substratum of the company has disappeared. The court also commented that in English law in the matter of winding up the wishes of the creditors and contributories have to be taken into consideration and the court may call a meeting for ascertaining their wishes. If a company is solvent and there are no allegations of mismanagement , and it is hopeful of doing profitable business in future, it is not necessary to wind it up only because it suspended its business for over a year.[6] Where the past delay in commencement of business is sufficiently accounted for and where the court is satisfied that there is a likelihood of the business being resumed, it may not exercise its discretionary power against the company but if the court is satisfied that no business has been or is likely to be commenced, it should pass an order for winding up of the company on the petition of the shareholders. Suspension of business for a whole year is usually deemed as an indication of absence of intention to carry on the business, unless suspension has been satisfactorily accounted for.[7] Only business which is authorised by memorandum is to be considered to determine whether company has suspended its business.[8] Company does not cease to carry on business if it transfers its undertaking to a subsidiary company.[9] But when business did not commence within a year and thereafter company remained totally closed for about a year and there was no hope of its functioning in near future, winding up would be justified.[10] If the business of a company has been stopped for more than one year and the number of shareholders falls below two the company is liable to be wound up.[11]

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1 section 252.

2 section 253.

3 section 254.

4 New Kerala Chits & Trades (P) Ltd vs Official Liquidator [1981] 51 Comp. Cas. 601(Ker).

5 Aluminium Corpn. of India Ltd vs Lakshmi Ratan Cotton Mills Co. Ltd [1970] 40 Comp. Cas. 259 (All).

6 Registrar of Companies vs Bihar Wire & Wire Products (P) Ltd [1975] 45 Comp. Cas.194 (Pat.).

7 In re Kaithal Cotton and General Mills Co. Ltd [1961] 31 Comp. Cas. 461 (Punj);Malabar Iron & Steel Works Ltd vs Registrar [1963] 33 Comp. Cas.886 (Ker).

8 K.G.Krishnan Ananthakrishnan vs Burdwan Cutwa Railway Co. Ltd [1978] 48 Comp. Cas.611 (Cal);

9 In re Eastern Telegraph Co. Ltd. [1947] 2 All E.R. 104.

10 Registrar vs Shreepalpur Cold Storage Ltd [1974] 44 Comp. Cas. 479(Pat).

11 Vega Sweaters (Pvt) Ltd. 52 DLR (HC) 372; 8 BLT (HCD) 226.

21.4.2 **Inability to Pay Debts** – Section 241 (e) provides that the Court may wind up a company if it is unable to pay its debts.

A debt must be a determined or definite sum of money payable at a future date. Where a company acts as guarantor for repayment of a loan , and the principal has defaulted , the amount guaranteed has become a debt for which a petition for winding up will lie.[1] Winding up is a last resort and cannot be insisted merely because company is unable to repay its debts so long as it can be resurrected by a scheme or arrangement.[2] A company should be kept alive rather than wind it up if there is a possibility of revival and its being commercial successful.[3] Where winding up will gain nothing except realisation of security of petitioner and no unsecured petitioner supports petition, Court may refuse to pass winding up order.[4] Even if conditions of section 163(1)(i) of the Companies Act 1913 are satisfied, it is discretion of Court to pass an order for winding up.[5] The Supreme Court of India has held that there are sufficient safeguards in the Companies Act to prevent a frivolous petition for winding up actuated by ulterior motive or to use it as pressure tactics.[6] The court held that the company judge had a discretion not to give directions at the stage when the petition comes to him for admission but to merely issue a notice to the company before giving directions. If upon receipt of the notice the company appears and satisfies the judge that the debt is bona fide disputed or that the presentation of the petition is mala fide actuated by an ulterior motive or an abuse of the process of the court certainly the judge may decline to admit the petition. This was a case where the company sought an injunction to restrain the alleged creditor whose claim it was disputing on the ground that the officer acting on behalf of the company had no authority to represent and bind the company. The Supreme Court refused the injunction holding that such a prayer for injunction would offend section 41(b) of the Specific Relief Act but went on to observe that the company judge had a discretionary power not to admit the petition for winding up. This is also the procedure practised in the Dhaka High Court where the company judge may, and often does, give prior notice to the company before admitting an application for winding up.

A winding up petition is not a legitimate means of seeking to enforce payment of a liability the nature of which is bonafide disputed by the company as its defence is not a cloak to evade the payment of the alleged loan.[7] Where the petitioner failed to show that the assets of the company were not sufficient to meet his claim and that the company's substratum was gone or that the company was commercially insolvent, the Court refused to wind up the company. An application under section 241 is a very serious matter and it amounts to killing of a company and the petition would be liable to be rejected.[8]

The Indian courts have held that winding up proceedings are not for recovery of disputed debts and cannot be stayed on ground that the agreement governing the particular item of debt contains an arbitration clause.[9]

It must be shown that a debt exists and that the company is unable to pay its debts.[10] Maintainability of petition depends not on inability to pay the debt of the petitioner but the inability, on the whole, of the company to pay its debts and when it is evident that the company is unable to pay its debts and position is not likely to improve, court may order winding up.[11]

1 Ram Bahadur Thakur & Co. vs Sahu Jain Ltd. [1981] 51 Comp. Cas. 301(Delhi).

2 Navijan Trading Finance (P) Ltd. In re [1978] 48 Comp. Cas. 402 (Guj).

3 New Swadeshi Mills Ltd vs Dye-Chem Corpn [1986] 59 Comp. Cas. 183(Guj);Sudarshan Chits Ltd vs Sukumaran Pillai [1985)]57 Comp. Cas 85 (Ker).

4 Karnatak Vegetable Oils & Refineries Ltd vs Madras Industrial Investment Corporation Ltd [1954] 24 Comp. Cas.249(Mad).

5 Thakar Govind Singh vs Merchant Mohani Flour Mills Ltd. [1944] 14 Comp. Cas. 184 (Lah).

6 Cotton Corpn of India Ltd vs United Industrial Bank Ltd. [1984] 55 Comp. Cas 423 SC.

7 Ahmed Ispahani vs. Free School Street Property and another 3 BLC [1998] AD 212.

8 Mohiul Islam vs Century Properties Development Ltd. and others 7 BLC (HCD) 248.

9 William Jacks & Co (India) Ltd vs Saraswati Industrial Syndicate Ltd [1986] 59 Comp Cas 876 (Punj.& Har); Hind Mercantile Corpn Ltd vs J.H.Rayner & Co Ltd [1971] 41 Comp Cas 548.

10 New India Corpn vs Nandanvan Mfrs. & Traders Ltd [1983] 54 Comp Cas 32 (Ker).

11 Kermeen Foods (P.) Ltd ,In re [1985] 58 Comp. Cas 156 (Guj).Bachharaj Factories Ltd vs Hirjee Mills Ltd [1955] 25 Comp. Cas 227.

Petition for winding up is maintainable even if debt which was not time barred when the petition was presented had become barred by the time the case was heard.[1]

The machinery for winding up will not be allowed to be utilised merely as a means for realising debts due from a company.[2] Even if liabilities exceed the assets the company may still be able to meet the demands of the creditors.[3] It is not correct to consider any hope or expectation that the company might obtain assets in future when there is no right to those assets.[4] Where the debt is undisputed and yet the company refuses to pay a winding up petition lies.[5]

When share application money became refundable and was not paid and there was a deadlock among directors then the company was ordered to be wound up.[6]

Where a debt is bonafide disputed or there is a counter claim then these will be taken as good grounds for refusing to pay.[7] If a debt is undisputed but the quantum is disputed the court may still wind up the company. The principles on which the Court will act are (a) the defence of the company is in good faith (b) the defence is likely to succeed in point of law (c) the company adduces prima facie evidence of the facts on which its defence lies.[8]

The Indian Supreme Court also cited from *Palmer's Company Law*[9] to comment that the Court will regard the wishes of the majority in value of the creditors, and if they object to a winding up order, the Court in its discretion may refuse the order.

Where the company has a genuine and serious cross claim against the petitioning creditor, the petition should be either dismissed or stayed.[10] Winding up proceeding is not available if there is a bonafide dispute about existence and amount of debt.[11]

Where the balance sheet of a company acknowledged a debt but the directors' report mentioned that the debt was time barred the Calcutta High Court held that this was a sufficient indication that the debt was disputed.[12]

It was settled law that the Court would not allow a winding up petition to decide a bonafide dispute as to debt. But the court should make a winding up order against a company which had established that it had a genuine and serious cross claim capable of extinguishing the petitioner's debt where it was satisfied that the interest of the company and its creditors during the litigation of the cross claim would be better protected by the appointment of a liquidator.[13]

21.4.3 The Dhaka High Court has held that no occasion arises for involving provision of section 162 of the Act of 1913 when all the assets and properties of the mortgagor company are assigned and mortgaged to the Bank and specific remedy and procedure are provided in President's Order 129 of 1972; a temporary inability to pay the debt should not be an occasion for winding up a company that being opposed to the state policy.[14] It is not clear what the court meant to be state policy although it did state that to wind up a company because of a temporary inability to repay an outstanding public debt runs counter to national interest. Justice S.M. Hossain however made a curious observation that clauses (v) and (vi) of section 162 of the Companies Act, 1913 are an equitable provision. Clause (vi) is clearly an equitable provision but the provision to wind up a company on the ground that it is unable to

1 Modern Dekor Painting Contracts (P.) Ltd vs Jenson & Nicholson (India) Ltd [1985] 58 Comp. Cas. 255.
2 Bukhtearpur Bihar Light Rly. Co Ltd. vs Union of India AIR 1954 Cal 499; In Amalgamated Commercial Traders (P.) Ltd vs Krishnaswami [1965] 35 Comp. Cas 456(SC);Buckley on the Companies Act 13 th Ed. p.451.
3 A.C.K. Krishnaswamy vs Stressed Concrete Construction Ltd [1964] 34 Comp. Cas 6(Mad).
4 Babylos Bank SAL vs Al-Khudairy. [1987] BCLC 232 CA.
5 Cornhill Insurance p.l.c. vs Improvement Services Ltd [1986] BCLC 26Ch.D.
6 Deccan Farms and Distilleries Ltd vs Bhelabhai Laxmidas Bhanji [1979] 49 Comp. Cas 321.
7 M. A. Khan vs S.C. Constructions AIR 1960 Mad 254;Md. Amin & Bros.Ltd. vs Dominion of India AIR 1952 Cal 323;Amalgamated Commercial Traders (Pvt) Ltd vs A.C.K. Krishnaswamy [1965] 35 Comp. Cas 456 SC; In re Federal Chemical Works Ltd [1964] 34 Comp Cas 963;J.N. Roy Chowdhury (Traders) P. Ltd. vs. Jainti Enterprises [1987] 61 Comp Cas 504.
8 Madhusudan Gordhandas and Co. vs Madhu Woollen Industries Pvt Ltd [1972] 42 Comp. Cas. 125 SC.
9 21st Ed page 742; In this regard also see In re P&J Macrae Ltd. [1961] 1 All E.R.302.
10 In re L.H.F.Wools Ltd [1969] 39 Comp Cas 934 (CA).
11 Tamanna-e-Jahan vs Paper Converting and Packaging Ltd. and others 7 BLC (HCD) 443 = 10 BLT (HCD) 449
12 Raghunath and Son P.Ltd. vs Pandann Tea Co. Ltd [1978] 48 Comp. Cas 577.
13 In re Richbell Information Services Inc. (Times Law Report 21 January 1999).
14 BSB vs Mujibullah (1977) 29 DLR 67.

pay its debts may not be entirely based on equity although the court does have an amount of option while acting under this clause.[1]

The Dhaka High Court has held that when a debt due by a company is established and remains unsatisfied, it is not under discretion of the court to refuse a creditor an order for winding up of the company. The court is to consider the nature of the money owing to the creditor. If it is legally recoverable as when the petitioner is admittedly a landlord and the defendant company is unable to pay its rent, the application for winding up the company is maintainable. Justice Md. Mozammel Hoque referred to a Bombay case *Goal Bros & Co. vs Yashodan Chits Fund Ltd*[2] to hold that a landlord may petition for winding up a company.[3] The same judge relied on his decision to hold a few months later that an arrear house rent is the liability of a company and if the company is unable to pay such liability it may be wound up. This in spite of the argument of the company's counsel that the company had assets worth Taka Three Crores against the demand for Taka seven lacs. The Court held that the company had admitted the debts and made part payment of the rentals and was unable to pay its debts and ordered that the company should be wound up.[4]

The Appellate Division of the Supreme Court has held that the basis of an order for winding up a company is its inability to pay its debts. A company must be found to be commercially insolvent when its existing and possible assets are insufficient to meet the existing liabilities, it is heavily indebted to various creditors, all its assets being in mortgage or in pledge and there is no possible chance of profit being made or its business carried out.[5] Although this was a case for winding up on the ground that the company was unable to pay its debts to the bank, the court considered whether it was just and equitable that the company should be wound up and in doing so observed that such opinion was bound to gain ground when it was found that the substratum of the company was gone as its only business had become impossible. The court rejected the contention of the company that the company had secured the loan by creating mortgage of its property and commented that the central question was whether the company was commercially insolvent, because the basis of an order for winding up a company on the ground of its inability to pay its debts is always insolvency. A. T. M. Afzal J. cited from the Halsbury's Laws of England as follows :

> "in such a case it is useless to say that if the assets of the company are realised there will be ample to pay 20 shillings in the pound; this is not the test. A company may be at the same time insolvent and wealthy. It may have wealth locked up in investment not presently realisable but although this be so, yet if it has not assets available to meet its current liabilities it is commercially insolvent and may be wound up."[6]

The learned judge went on to say that a company must be found to be commercially insolvent when its existing and probable assets are insufficient to meet the existing liabilities, it is heavily indebted to various creditors, all its assets being in mortgage or in pledge, and there is no possible chance of a profit being made or its business carried out. The court in the circumstances prevailing in that case held that "the present facts as could be gathered indicate that it has been rendered into a wholly moribund organisation without any glimmer of survival. A winding up order is called for under section 162, clause (vi) of the Act if the Court is of the opinion that it is just and equitable that the company should be wound up".

Considering the fact that initially the application was for winding up the company on the ground that it was unable to pay its debts it was surprising that the court went on to find that it was just and equitable to wind up the company. It is the discretion of the court to wind up a company and the Appellate Division can certainly rely on another clause of section 241 of the Act of 1994 to wind up a company. If a company is out and out a defaulter then it is just and proper that it should be wound up.[7]

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1 In this connection see Paramjit Lal Bhadwar vs Prem Spg & Wvg Mills Co Ltd [1986] 60 Comp. Cas. 420; Aluminium Corpn of India Ltd vs Lakhmi Ratan Cotton Mills Co Ltd AIR 1970 All 452.

2 [1980] 50 Comp Cas 7

3 BRTC vs Ashraf Jute Mills Ltd. 43 DLR(1991) 240.

4 Nizamul Haque vs Sing Bangla Garment 43 DLR(1991) 603. Also see M. A. Gaffar Ltd. vs Sanjari Garments (Pvt.) Ltd. 20 BLD (HCD) 477 = 5 BLC (HCD) 480 = 8 BLT (HCD) 295

5 Agrani Bank vs Bangladesh Tyres Ltd. 43 DLR (AD) 164. Also see Sayeda Haque vs Shams Ltd. and others 6 BLC (HCD) 748

6 ibid at p.168.

7 Thai Airways International Ltd. vs. Air Route Service Ltd. 48 (1996) DLR H.C. 412.

The Dhaka High Court has subsequently held that if a company has again and again defaulted in payments giving the impression that the affairs of the company are not clean and above board, the opinion is that the company is unable to pay its debts and it will be just and equitable if the company is wound up.[1] Justice Hasan referred to the cases where the court has held that a winding up order against a company should be passed only when the company has ceased to be commercially solvent.[2] and agreed in principle that a company should not be wound up unless it is really found commercially insolvent. But the Court also considered the decision referred to in Agrani Bank vs Bangladesh Tyres Ltd.[3] and having referred to the facts the case before him held that the company was unable to pay its debts.

In *Nazrul Islam Khan Badal vs Al Baraka Bank Bangladesh Ltd.*[4] the Dhaka High Court refused to admit a petition for winding up a bank because it was a serious matter especially when the debt was disputed. The court relied on a decision of the Appellate Division *Amin Scales Ltd. and another vs Md. Yakub*[5] where the Appellate Division cautioned that great care should be taken in admitting an application for winding up as it is likely to create alarm in the minds of all creditors of the company, divert its customers away and paralyse its business. If there is genuine dispute the petition may be dismissed or stayed and an injunction may be granted restraining the advertisement of the petition. The same caution was sounded in the case of *Ellal Textile Mills Ltd.*[6] where it was stated that winding up is a serious affair which was evident from a perusal of the entire Part V of the Act.

The position that the Bangladesh judges have taken is therefore that a company will be unable to pay its debts if it is commercially insolvent i.e., it cannot meet its present liabilities However the courts may also find that the company should be wound up on any of the other grounds mentioned in section 241.Also that if the applicant cannot show that he has something to gain his prayer for winding up the company may be refused. The prayer will not be granted however if the debt is genuinely disputed.

21.4.4 The word 'may' at the beginning of the section shows that the Court has a discretion not to wind up even if the company is unable to pay its debts.[7] Where the dispute related only to the mathematical accuracy of the claim and the undisputed sum exceeds the statutory minimum sum a winding up order will be made.[8] If the undisputed liability has been paid by the company but the company disputes the balance claim of the creditor the company will not be wound up.[9] If there is bonafide dispute relating to the existence and amount of the debt winding up proceeding is not available.[10] A foreign creditor can maintain a petition for winding up if its commission was not paid because the local company neglected to obtain the permission of the central bank for remittance of the fund.[11]

Where a petition for winding up is resisted on a substantial ground the Court will usually restrain the prosecution of the petition as an abuse of the process of the Court. This may be even if the company appears to be insolvent.[12] A creditor whose debt is clearly established can present a

1 Eastern Bank Limited vs. Bengal Carpets Ltd. 48 DLR (1996) 392 H.C.
2 Bengal Laxmi Cotton Mills Ltd vs Mahaluxmi Cotton Mills Ltd. AIR 1955 Cal 273
3 Supra.
4 Company Matter 40 of 1991 decided on 15.3.92
5 (1987) BLD (AD) 259
6 38 DLR (AD) 26
7 Paramjit Lal Badhwar vs Prem Spng & Wvg Mills Co. Ltd. [1986] 60 comp. Cas. 420; Aluminium Corpn. of India Ltd. vs Lakshmi Ratan Cotton Mills Co. Ltd.AIR 1970 All 452. BSB vs Mujibullah 29 DLR (1977) 67. Where the debt is disputed bona fide no winding up order will be made.Nazrul Islam Khan Badal's case (supra) and C.R.Chandra vs Tirupati Cottqn Mills Ltd [1971] 41 Comp. Cas. 94;Shadiram & Sons vs Southern Aviation P. Ltd [1978] 48 Comp. Cas 570; N.Ramamurthy Nellai Metal Rolling Mills P. Ltd [1979] 49 Comp. Cas.553(a case of denial by the company of the validity of promissory notes on the ground of collusion).
8 Syndicate Bank vs Southern Oils and Extraction Ltd [1985] 57 Comp. Cas. 81.Pfizer Ltd. vs Usan Laboratories P. Ltd [1985] 57 Comp. Cas 236 (Bom).
9 Re a Company [1984] 3 All E.R.78 Ch.D.
10 Tamanna-e-Jahan vs Paper Converting and Packaging Ltd. and others 7 BLC (HC) 443 = 10 BLT (HCD) 449.
11 Eurometal Ltd vs Aluminium Cables & Conductors P. Ltd [1983] 53 Comp. Cas. 744.
12 Mann vs Goldstein [1968] 1 W.L.R. 1091;Charlesworth and Morse 14th Ed p. 747-8.

petition if there is a persistent refusal to pay the debt.[1] An unpaid creditor is entitled 'ex debito justitae' to a winding up order.[2] This is so even if the company has appealed against the judgment giving rise to the debt[3] or has a disputed claim against the petitioning judgment creditor which is the subject of litigation in other proceedings.[4] Where there is a cross claim the English Courts have held that then it is a matter of discretion of the judge.[5] It is improper to present a petition on the basis of a debt which has never been demanded and for which no opportunity has been given to the company to pay.[6] The petitioning creditor is however invoking a class right and it is improper for him to present a petition for some private purpose. On the other hand if the petition is genuinely for the benefits of the class of creditors malice on his part will not make the petition improper.[7] The Court may have regard to wishes of creditors or contributories by any sufficient evidence.[8] In English law this gives the Court the power to call meetings of creditors to ascertain their wishes and the judge has a wide unfettered discretion to decide whether to make the order or not.[9] Where the company is insolvent the views of the creditors alone will matter. Otherwise the views of the contributories will be considered and in such a case if only a contributory opposes a petition it will usually be granted.[10] The authors of Charlesworth and Morse further comment that where there are different classes of creditors the wishes of those particularly interested will be given most weight and in particular, where the company's assets are not entirely charged in favour of debenture holders the wishes of the unsecured creditors will be primarily considered.[11] Where the assets are entirely charged in favour of debenture holders, if the petition of an unsecured creditor is opposed by the debenture holders the petitioner is entitled to a winding up order unless the opposing creditors can show that there is no reasonable possibility of the unsecured creditors obtaining a benefit from a winding up.[12] The authors of the same edition of Charlesworth and Morse on Company Law further comment that if the petition of an unsecured creditor is opposed by the majority in value of the unsecured creditors, although the Court has a discretion in the matter and the fact of the majority opposition is not conclusive, if they oppose for good reason (e.g., if the assets exceed liabilities and the company is able to continue business) their wishes will prevail in the absence of special circumstances making winding up desirable.[13]

An assignee of a debt can petition[14] even if a petition was presented in respect of the debt before the assignment.[15] A secured creditor including a debenture holder can petition.[16] But the holder of a debenture stock secured by a normal trust deed cannot present a petition as he is not a creditor of the company.[17] A petition cannot be presented by a person with a claim against the company for unliquidated damages.[18]

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1 ibid and Cornhill Insurance plc. vs Improvement Societies Ltd [1986] 1 W.L.R. 114.

2 Re Chapel House Colliery Co. [1883] 24 Ch. D. 259 CA.

3 Re Amalgamated Properties of Rhodesia Ltd (1917) 2 Ch.115 CA.

4 Re Douglas Griggs Engineering Ltd [1963] Ch. 19; Re Fitness Centre (South East) Ltd [1986] BCLC 518;Charlesworth and Morse above p.748.

5 Re L.H.F.Wools Ltd [1969] 3 All E.R. 882 CA.

6 Re A Company [1983] BCLC 492.

7 ibid.

8 section 254.

9 Charlesworth and Morse 14th Ed. p.748-9.

10 ibid and Re Camburn Petroleum Products Ltd Re [1979] 1 W.L.R. 86

11 14th Ed p.749.

12 ibid.and Re Crigglestone Coal Co.Ltd. [1906] 2 Ch. 327 CA.

13 14th Ed p. 749 and Re Vuma Ltd [1960] 1 W.L.R. 1283 CA; Re P&J Macrae Ltd [1961] 1 W.L.R. 229 CA;Re A.B.C. Coupler Co [1961] 1 W.L.R. 243; Re Fitness Centre (South East) Ltd [1986] Butterworths Company Law Cases 518.However, the wishes of the minority may prevail in special circumstances.Re Southard & Co. Ltd [1979] 1 W.L.R. 1198 CA.; Re Home Remedies Ltd [1943] Ch.1;Re B. Karsberg Ltd [1956] 1 W.L.R. 57 CA;Re J.D.Swain Ltd [1965] 1 W.L.R.909 CA.

14 Re Steel Wing Co [1921] 1 Ch. 349

15 Perak Pioneer Ltd vs Petroleum National Bhd. [1986] 3 W.L.R. 105 PC.

16 Re Olathe Silver Mining Co. (1884)27 Ch.D. 278.

17 Re Dunderland Iron Ore Co. Ltd [1909] 1 Ch. 446.

18 Re Pen -y-van Colliery Co. [1877] 6 Ch.D. 477; but see Re A Company [1973] 1 W.L.R. 1566,1577 for a comment by Justice Megarry that contingent or prospective creditors may not be barred

Interests of the workers of a company have to be taken into account while admitting a petition for winding up.[1] The creditor must show that in fact he is a creditor. The company may prove that a debenture or other instrument evidencing a debt was not supported by consideration and was fictitious.[2]

21.4.5 Section 242 provides that a company shall be deemed to be unable to pay its debts if :

(a) a creditor to whom the company owes more than five thousand taka then due gives a notice in writing (by the company or its legal advisor or its agent) by registered post to the registered office of the company requiring the company to pay the sum so due and the company has for three weeks thereafter neglected to pay the sum or to secure or compound for it to the reasonable satisfaction of the ceditor; or

(b) execution or other process issued on decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or

(c) if it is proved to the satisfaction of the Court that the company is unable to pay its debts and in doing so the court shall take into account the contingent and prospective liabilities of the company.

21.4.6 The period of three weeks' neglect referred to in section 242 (a) means a period of three clear weeks excluding the day of service of the demand for payment and the day of presentation of the petition.[3] The authors of Company Law by Charlesworth and Morse 14th edition comment that a creditor will not rely upon a statutory demand where there is risk of dissipation of the assets in the three week interval and that he can employ the more general ground that the company is unable to pay its debts as they fall due.[4] If a debt was due and unpaid and could not be disputed on some substantial ground the presentation of a petition on the third and general ground was amply warranted.[5] A company is also unable to pay its debts if its acceptances have been dishonoured above or has informed a judgment creditor that it has no assets on which to levy execution.[6] The authors of Charlesworth and Morse also comment relying on old English decisions that a company is not unable to pay its debts just because it is carrying on a losing business, if its assets exceed the liabilities.[7] However where the company fails to pay its debts and its assets are not presently available to meet the current liabilities the court may hold that the company is unable to meet its debts.[8] However, although under grounds (b) and (c) of section 242 it need not be shown that the debt owing exceeds Taka Five Thousand in practice the courts will see that the debt exceeds that amount since there must be circumstances which justify an inference that a company is insolvent.[9] On the other hand, where a company refused to pay a debt of 35 British Pounds on the ground that it was too small to be the foundation of a petition, an order was made.[10] Admission in the balance sheet may be an acknowledgment of debt.[11] But debenture or other deeds not supported by consideration are fictitious.[12]

On the question whether a debt of the company not barred by limitation on the date of presentation of a winding up but which gets barred by the date of the winding up order could be entertained by the official liquidator there are differences among the Indian High Courts.

1 National Textile Workers Union vs P.R.Ramakrishnan [1983] 53 Comp. Cas.184 (SC).
2 Ram Kumar vs Buxar Oil and Rice Mills AIR 1960 Cal 764.
3 Re Lympne Investments Ltd [1972] 1 W.L.R. 523.
4 at page 746.
5 Taylor's Industrial Flooring Ltd vs M.S.Plant Hire Manchester Ltd [1990] BCLC 216; CA
6 Charlesworth and Morse, ibid. and Re Douglas Griggs Engineering Ltd (1963) Ch. 19
7 14th Ed p.746.
8 Re A Company (1986) BCLC 261.
9 Charlesworth and Morse above at p.746.
10 Charlesworth and Morse, ibid. citing Re World Industrial Bank (1909) W.N. 148.
11 State Bank of India vs Hegde and Golay Ltd (1987) Comp. Cas. 239 Ker. Also see Jones vs Bellgrove Properties Ltd (1949) 2 K.B. 700; Re Transplanters (Holding Co.) Ltd 1958 1 WLR 822; Ledingham vs Bermejo Estancia Co. [1947] 1 All E.R. 749.
12 Ram Kumar vs Buxar Oil and Rice Mills AIR 1960 Cal 764.

Doubtful, say the decisions in *J.A. Dixit vs Official Liquidator*,[1] *Benaras Cotton and Silk Mills Ltd vs Sulbha Devi Gupta*,[2] *re Chandbali Steamer Service Co Ltd.*[3] A contrary view was held in *S.Abdul Muthalibu vs K.M. Mohammed Abdul Khager*[4] and *Ram Chand Puri vs Punjab Enamelling and Stamping Co. Ltd.*[5] Considering these cases the Delhi High court held that both for the purpose of passing a winding up order as well as for proof of claims, the relevant date should be taken as the date of presentation of the petition for winding up and not the date of the winding up order.[6] In *Shri Ladli Prasad Jaiswal vs The Karnal Distillery Co Ltd*,[7] the Supreme Court of Pakistan held that the rights of the parties in this matter are to be adjudged acecording to the legal position prevailing on the date of the institution of the proceedings for winding up and not on the basis of changes which have since been introduced by the unilateral acts of one party without the consent of the other. In this case the Court refused to apply the alternate remedy under section 153A of the Companies Act of 1913 suo moto. Institution of suits in civil courts does not debar filing of a petition for winding up.[8]

In *Rehana Ahmed vs Nahar Shipping Lines Ltd*[9] the Court cited from the observations of *S.M.Mohsen Ali J. in Mahmudur Rahman vs Monipur Tea Company Ltd*[10] and Professor Gower's book on Modern Company Law that the Court looks askance at a petition by a fully paid shareholder to wind it up on the ground of insolvency of the company as his interest is least affected in winding up. A fully paid shareholder has nothing to lose by the continuance of the company and nothing to gain by its winding up. This case is also an authority for the proposition that the fact that liabilities far exceed the assets does not mean that the company is unable to meet its debts. On this question the Court discussed several Indian decisions[11] but found on the facts of the case before the Court that the company was not commercially insolvent. The Court refused to wind up a Company as the petitioner failed to show that the assets of the Company are not sufficient to meet his claim and company's substratum is gone.[12] Winding up proceeding is different from proceedings under Negotiable Instruments Act.[13]

21.5.1 **Just and Equitable Ground** – Section 242 (vi) gives the Court a wide discretion in winding up a company because it is just and equitable to do so. The general terms of the language used has given rise to a number of judicial observations on the powers of the Court to terminate the affairs of a company on the ground that it is just and equitable to do so.

In *Seth Mohan Lal vs Grain Chambers Ltd*[14] the Supreme Court of India has said that the Court will consider the interests of the shareholders as well as of the creditors. Substratum of the company is said to have disappeared when the object for which it was incorporated has substantially failed, or when it is impossible to carry on the business of the company except at a loss or the existing and possible assets are insufficient to meet the existing liabilities. The Court held on the facts of the case that the company should not be wound up. Also see the old case of *Re German Date Coffee Co Ltd*[15] where the Court discussed the ultra vires doctrine while trying to find whether the substratum of the company was gone or not.

1 AIR 1963 All 284
2 [1985] 3 Comp. Cas.639 (All)
3 [1960] 30 Comp. Cas. 61 (Cal) AIR 1959 Cal 646.
4 [1962] 32 Comp. Cas. 1102 (Mad)
5 [1960] 30 Comp. Cas. 515 (Punj).
6 Indian Turpentine and Raisin Company Ltd vs Pioneer Consolidated Company of India Ltd., [1988] 64 Comp. Cas 169 (Del). Diwan Chand Kapoor vs New Rialto Cinema P. Ltd. [1988] 64 Comp. Cas. 169 (Del); [1986] 60 Comp. Cas. 276(Del)
7 17 DLR (S.C.) 52.
8 Ramakrishna Industries(P.)Ltd vs P.R. Ramakrishnan [1988] 64 Comp. Cas. 425(Mad).
9 44 DLR 256 (HC)
10 28 DLR 133
11 ACK Krishnaswamy vs M/s Stressed Concrete Pvt Ltd; [1964] 34 Comp. Cas 6 (Mad); AIR 1964 Mad 191. Punjab Flying Club Ltd. AIR 1933 Lah 301
12 Mohiul Islam vs Century Properties Development Ltd. and others 7 BLC (HCD) 248.
13 Amir Hossain vs Homeland Footwear Ltd. and others 22 BLD (HCD) 641; 8 MLR (HC) 42. 55 DLR (HC) 478. The Court also observed that when a winding up order was made no other suit against the company shall proceed.
14 AIR 1968 SC 772
15 [1882] 20 Ch.D. 169

The Court has to form an opinion about the equity involved.[1] A shareholder is not necessarily restricted to grounds for complaint which affect him solely as shareholder; equitable considerations of a personal character may be considered.[2] But equitable considerations will not arise merely because the company is a small one.[3] Winding up order was refused in *Re Anglo-Continental Produce Co. Ltd*[4] as there was no evidence of anything to cause prejudice to the rights of shareholders.

The Dhaka High Court has held that a person who is not a shareholder has no right to petition for winding up a company on this ground.[5] The Court cited with approval the decision reported in *Re Chesterfield Catering Co. Ltd*[6] that in order to establish his locus standi to petition for the winding up of a company, a fully paid shareholder had to show that he had a sufficient interest in that, if the company were wound up, he would, as a member, receive some advantage or avoid to minimise some disadvantage which would accrue to him by virtue of his membership of the company.[7]

In *Bengal Waterways Ltd vs Rahimuddin Ahmed*[8] our Appellate Division while interpreting the corresponding section 162 (vi) of the Act of 1913 has held that deadlock in the affairs of the company by itself has not been made a ground under section 162 but clause (vi) provides that if the court is of the opinion that it is just and equitable that the company should be wound up the Court may do so.The Court may wind up a company in case of a deadlock and if the company is a one man company.[8A]

21.5.2- A private company can also be wound up on the principles of dissolution of partnership.[9]

Doctrine of winding up a company on principles of dissolution of partnership could be attracted only in domestic or family companies where shareholding is equally divided and deadlock cannot be resolved under articles.[10]

The Dhaka High Court refused to wind up a company on this ground because there was the provision for a casting vote by the Chairman of the Board and there was no real deadlock; further, that the lack of confidence having arisen out of a personal factor and not because of mismanagement and the Chairman running a parallel business having had no equity in his favour, the company should not be wound up.[11] The Court cited with approval the decisions in the Wilcock's case[12] and the observations of *Donovan L.J. in Re Davis Investments (East Ham Ltd)*[13] that it was not the law that in case of a two-man company, if the shareholders,

1 Shanti Prasad Jain vs Kalinga Tubes Ltd AIR 1962 Ori 202 (real aim was to get control of the company);Amalgamated Commercial Traders Ltd vs A.C.K. Krishnaswami [1965] 35 Comp. Cas. 456[SC],National Conducts (P) Ltd vs S.S.Arora [1967] 37 Comp. Cas. 786(SC) (lack of bona fides); Madhusudan Gordhandas & Company vs Madhu Woollen Industries (P.) Ltd [1972] 42 Comp. Cas. (SC) 125 (not for legitimate purpose).

2 Ebrahimi vs Westbourne Galleries [1972] 2 All E.R. 492; [1973] A.C.360.

3 Re A Company [1983] 1 WLR 927.

4 [1939] 1 All E.R. 99 Ch.D.

5 Mazharul Hoque vs Bulk Management Ltd and others (1996) 16 BLD 576.

6 [1976] All E.R.294.

7 (1996) 16 BLD at p.579-580.

8 34 DLR (AD) 47. 8A. S.M.M. Yusuf vs Bismillah Shipping Lines (Pvt.) Ltd. and others 20 BLD (HCD) 517 = 5 BLC (HCD) 603 = 5 MLR (HCD) 263.

9 ibid. also Ebrahimi Westbourne Galleries Ltd [1972] 2 All E.R. 492; Hind Overseas Pvt. Ltd vs Raghunath Prasad Jhunjhunwala AIR 1976 S.C. 565;Raja Mundory Electric Supply Corpn. Case AIR 1956 S.C. 213;Loch vs John Blackwood Ltd [1924] A.C. 783. Re Yenidge Tobacco Co. Ltd (1916) 2 Ch. 426 Re Davis & Collett Ltd [1935] Ch. 693; Re Cooper (Cuthbert) & Sons Ltd [1937] 2 All E.R. 466.

10 Smt. Abnash Kaur vs Lord Krishna Sugar Mills Ltd [1974] 44 Comp. Cas. 390 (Delhi)C.P.Gnansambandam vs Tamilnadu Transports (Coimbatore)(P.)Ltd [1971] 41 Comp. Cas.26 Mad; In re Anil Drug House Ltd [1971] 41 Comp. Cas.352 (Guj).In re Akola Electric Supply Co. (P) Ltd [1962] 32 Comp. Cas 215 (Bom).

11 M.Al-Amin vs Shafquat Haider 42 DLR 302 HC; see Younus Bhuiyan (Md) vs. Bashati Property Development Ltd. and ors 4 BLC (1999) HC 249 where company was wound up because there was total misunderstanding, deadlock and no chance of compromise between two groups of directors.

12 [1973] 3 All E.R. 93

13 [1961] 3 All E.R. 926

being equal in their shareholding, fall out, one of them alleging that further co-operation was impossible, then the Court, in the absence of a reply from the other shareholder, must at once treat them as though they were partners and order a winding up, as it would, in a partnership case, order a dissolution.

Mr Justice Mustafa Kamal when sitting in the High Court Division observed as follows :

> With regard to deadlock I do not think that there has been any because the Articles of Association are quite clear that the Board of Directors can be comprised of a minimum number of 3 directors and I find that the company is being run by a Board of Directors comprising of 3 directors. With regard to amassing all powers in the hands of Managing Director I find that under Article 39 of the Articles of Association the Managing Director Arif Yunus has been vested with "all absolute Power". It has been held in the case of Ripon Press and Sugar Mill Co. Ltd., Bellary vs V. Gopal Chetty, AIR 1932 (PC)1 that the fact that one of the shareholders has a prepondering voice in the company is of itself not reason for winding up . Besides when the petitioner purchased the shares of his brother Mujibur Rahman he knew about Article 36 of the Articles of Association (Non payment of dividend regularly is also no ground for winding up a company) as has been held in the aforesaid case.[1]

In Bashati Property Development Ltd. and others vs. Younus Bhuiyan and others[2] the Appellate Division held that where a strong case for winding up has been accepted, an application under section 233 by which one faction offered to let the other faction run the Company and thus save deadlock should be rejected.

In a private company where the director was removed lawfully, it was held by the Chancery Division on the facts of the case that it was an abuse of power and a breach of good faith which partners owed to each other.[3]

If a person has subscribed to the company's share on the understanding that he would be made a director a failure to appoint him so by the majority shareholders may justify a winding up order.[4] Not so if the majority agreed to the offer to buy the shares of the minority director at a fair price.[5]

There must be a 'justifiable lack of confidence in the management' grounded on conduct of the directors, not in regard to their private life or affairs, but in regard to the company's business. Furthermore, the lack of confidence must spring not from dissatisfaction at being outvoted on the business affairs or on what is called the domestic policy of the company. On the other hand, wherever the lack of confidence is raised on a lack of probity in the conduct of the company's affairs, then the former is justified by the latter, and it is under the statute just and equitable that the company should be wound up."[6] The Court also rejected the argument that the clause 'just and equitable' should be construed ejusdem generis.[7] The Indian Supreme Court adopted the meaning of 'just and equitable' clause as given by the English Courts but warned that 'whether mismanagement of directors is a ground for winding up under section 162(vi)(of the Act of 1913) becomes a question to be decided on the facts of each case'.[8]

In the absence of malafides the mere exercise of majority strength will not per se entitle the petitioner to succeed but if a member has sufficient ground for presenting a petition for winding up, the size of his shareholding and his motives are irrelevant.[9] However, an order for winding up on just and equitable ground may be made when the majority shareholders deprive the minority of their legal right to appoint and remove their own director in furtherance of their right to participate in management.[10] In Naimur Rahman's case[11] the Court stayed a petition for winding up on the ground that it was presented mala fide. Unless

1 Matiur Rahman vs May Industries Ltd 37 DLR (HC) 41 at page 46.
2 4 BLC (1999) AD page 236.
3 Ebrahimi vs Westbourne Galleries Ltd. Supra.
4 In re Zinotty Properties Ltd [1984] 3 All E.R.754.
5 Re A Company [1983] 2 All E.R. 854.
6 Loch's Case, Supra.
7 ibid at p.789-90.
8 Raja Mundory's case Supra and Hind Overseas P. Ltd vs Raghunath Prasad Jhunjhunwala AIR 1976 SC 565.
9 Bryanston Finance Co. Ltd vs de Vries [1976] 1 All E.R. 25.
10 Re A&BC Chewing Gum Ltd [1975] 1 All E.R. 1017.
11 43 DLR (AD) 169

there has been abuse of majority voting power and it is not possible to carry on the business of the company as a whole, because of the way in which the voting power is held and used, the Court will not make a winding up order.[1]

Mere allegations of mismanagement will not make the company liable to be wound up on just and equitable grounds.[2] In the Dhaka case Justice Md Mozammel Hoque observed that there may be certain irregularities and omissions in the management of the company but it should be treated as matter of internal management. Also see the case of *Pioneer Bank Ltd.*[3] Justice Hoque discussed a decision of the Indian Supreme Court *Rajamundry Electric Supply Corporation Ltd vs A. Nageshwara Rao*[4] to hold that the words "just and equitable" in the section are not to be construed "ejusdem generis" with the other clauses of that section and therefore whether mismanagement of the directors is a ground for winding up is a question to be decided on the facts of each case. The Court rejected a prayer by a fully paid shareholder on the ground that the company was unable to pay its debts because a fully paid shareholder has nothing to gain or lose if a company was wound up on this ground but while citing from another decision of the Dhaka High Court[5] the Court seemed to approve a statement in the earlier case that the Court may use its discretion if the petitioner makes out a special case or there is a strong ground for interference justifying the use of its discretionary power of just and equitable ground. The Court also rejected an argument from the Bar that the company was not paying any dividend and therefore should be wound up. The Court cited the decisions in *Ripon Press and Sugar Mill Co. Ltd vs A. Gopal Chetti*[6] and *Motiur Rahman vs May industries Ltd*[7] to hold that non payment of dividend for a certain period was no ground to wind up a company on the ground that it was just and equitable to do so. In Rehana Ahmed's case another submission was made, that the company was going on heavy losses because of continuous mismanagement. While rejecting this argument on the facts of the case the Court cited the decision reported in a Bombay case of *Cine Industries and Recording Company Ltd*[8] which held that business being carried on at a heavy loss was no ground for winding up if majority shareholders show their confidence in the management. Rehana Ahmed's case was decided before the introduction of section 233 of the Act of 1994 which provides for protection of minority shareholders and held that where petition by a shareholder contains allegations which relate to internal management or mismanagement of the company's affairs, it is a matter for the shareholders themselves to deal with and not one that would call for interference by the Court.

The Calcutta High Court has held that a charge by the petitioner that the cashier and the managing agent were guilty of falsification and manipulation of accounts is not a ground for winding up a company under this clause.[9]

A company was ordered to be wound up when it has not been doing business and was admittedly not in a position to pay debts.[10] In this connection also see the observations of the Appellate Division in Agrani Bank's case[11] where the Court ordered winding up of the company on the ground that it was also just and equitable to do so although the application for winding up was based on the ground that the company was unable to pay its debts.[12] Also see *Registrar vs Shreepalpur Cold Storage P.Ltd*[13] where the subtratum of the company was found to have been gone and the company could not operate except at a loss.

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1 Re Anglo-Continental Produce Company Ltd [1939] 1 All E.R. 99.
2 Rehana Ahmed and others vs Nahar Shipping Lines Ltd 44 DLR 256 (HC).
3 AIR 1914 Bom 190
4 AIR 1956 SC 213
5 Mahmudur Rahman vs Manipur Tea Company Ltd. 28 DLR 133
6 AIR 1932 P.C.1
7 37 DLR 41
8 AIR 1942 Bom 231
9 In re Sulekha Works AIR 1965 Cal 98
10 In re Mulraj T. Mararji [1979] 49 Comp. Cas. 475 Bom.
11 43 DLR (AD) 164
12 supra para 21.4.3.
13 [1974] 44 Comp Cas 497 Patna

The Punjab High Court has commented that the tests to determine whether substance of the company has disappeared or not are-

1. whether the subject matter of the company exists;
2. whether the objects in the objects clause have failed;
3. whether it is impossible to carry on the business except at a loss;
4. whether the existing and probable assets are sufficient to meet the existing liabilities.

The company must pass all the tests to avoid being wound up.[1]

Court will be justified in concluding that the substratum of the company is gone only when the activities of the company have become impossible by operation of law or by unforeseen circumstances.[2] Once the main object of the company fails, unless the shareholders are prepared to carry on other business which is found in the memorandum of association the company must be wound up.[3]

Lord Wilberforce laid down the principles on which the courts will act to wind up a company on just and equitable ground.[4] The super-imposition of equitable considerations require something more than purely commercial considerations the basis of which are laid down in the articles. If an association is based on personal relationship involving mutual confidence and often found where a pre-existing partnership was converted into a limited company or an agreement that all or some of the shareholders shall participate in the conduct of the business or there is a restriction on the transfer of the member's interest in the company so that a member cannot take out his stake and go elsewhere then the court may apply this principle.[5]

An Indian High Court has held that where an alternate remedy for protection of minority shareholders was not pursued the court may refuse to apply the 'just and equitable' ground to wind up a company.[6] But the Delhi High Court has held that it is not necessary that every time a petitioner moves an application for protection of minority shareholders he must also seek relief for winding up.[7]

The petitioner will not be barred from prosecuting both the petitions for winding up on 'just and equitable ground' and praying for relief on the ground of protection of minority shareholders.[8]

The Calcutta High Court refused to allow the petitioner to collect materials upon inspection of the company's documents to supplement the grounds he relied upon.[9]

But the Allahabad High Court has held that there is no rule for holding that the jurisdiction of the Court in considering a winding up petition must be exercised only on evidence which accompanies the winding up petition and further evidence can be rendered after filing the winding up petition.[10]

When objects for which the company was incorporated have disappeared the substratum of the company will be deemed to have gone.[11] Also see the observations of A.T.M. Afzal J. in the Appellate Division that the substratum of the company was gone when its only business

1 O.P.Basra vs Kathal Cotton and General Mills Co.Ltd AIR 1962 Punj 151;Virendra Singh Bhandari vs Nandlal Bhandari & Sons Ltd. [1982] 52 Comp. Cas. 36(MP);In re Cine Industries & Recording Co. Ltd [1942] 12 Comp. Cas. 215(Bom); D.Davis & Co. Ltd vs Brunswick (Australia) Ltd AIR 1936(PC) 114.

2 Malabar Industrial Co. Ltd vs A. John Anthrapper [1985] 57 Comp. Cas.717 (Ker.)Mohanlal Dhanjibhai Mehta vs Chunilal B. Mehta [1962] 32 Comp. Cas. 970 (Guj).

3 K.G.K. Anantha Krishnan vs Burdwan -Cutwa Railway Co. Ltd [1978] 48 Comp. Cas. 611(Cal).

4 Ebrahimi vs Westbourne Galleries Ltd [1972] 2 All E.R. 492 at p. 499,500.

5 ibid. Re Zinotty Properties Ltd (Ch) [1984] 3 All E.R. 754.

6 George vs Athimattan Rubber Co. Ltd AIR 1964 Ker 212.

7 Eastern Linkers (P.) Ltd vs Dinanath Sodhi [1984] 55 Comp. Cas. 462,485.

8 Official Liquidator vs N. Chandravarayanan[1973] 43 Comp. Cas 244

9 In re Sulekha Works Ltd. Supra.

10 Aluminium Corporation of India Ltd vs Lakshmi Ratan Cotton Mills Co.AIR 1970 All 452.

11 Seth Mohan Lal vs Grain Chambers Ltd. AIR 1968 S.C. 772;Madhusudan Gordhandas and Co. Madhu Woollen Industries Private Ltd AIR 1971 S.C. 2600.

had become impossible.[1] The Appellate Division however observed in this case that the basis of an order for winding up a company on the ground of its inability to pay its debts is always insolvency. A company must be found to be commercially insolvent when its existing and probable assets are insufficient to meet the existing liabilities, it is heavily indebted to various creditors, all its assets being in mortgage or in pledge, and there is no possible chance of a profit being made or its business carried out.

The Appellate Division has held that it was not competent to have two prayers of different types in the same petition , i.e., one for rectification of the share register and the other for winding up.[2]

21.5.3 Facts existing at the time of the hearing of the petition are relevant to decide whether it is just and equitable that a company should be wound up and the petitioner should be confined to the grounds he has taken.[3] Mr. Justice Mustafa Kamal held in a High Court case that if on the facts existing when the petition was presented it was then just and equitable to wind up the company, but subsequently it has ceased to be so, a winding up order should not be made.[4] Citing from the English decision that the language of section 222(f) of the English Companies Act of 1948 (similar to our law) is cast in the present tense the learned judge was of the opinion that winding up could not be granted as there were cogent grounds for complaint when the petition was presented but afterwards melted away.

Mr. A. Ramayia in his Guide to the Companies Act refers to three Orissa High Court decisions which illustrate the general application of the principle of winding up on just and equitable ground.[5] e.g., where a company kept on deferring payment of the principal and interest dues in spite of demands, and vacated its registered premises and the managing director was not available to carry on the day to day administration of the company,[6] where the company did not carry on the business for five years as per the auditor's report and the business is not likely to be commenced,[7] and where the business remained suspended for more than six years and the company was left with no funds and assets, due to prolonged mismanagement, and there being no possibility of remedying the situation.[8]

21.5.4 The Editors of Palmer's Company Law *20th Ed.* note[9] that under the 'just and equitable' clause winding up orders have been made where :

(1) the substratum of the company was gone;[10] (principal object was to acquire a particular gold mine in New Zealand the title to which altogether failed);[11] (object was to acquire the undertakings of four other companies carrying on business in Russia, which were confiscated by the Russian Government before they could be acquired); In all these cases the petition was a shareholder's petition, and was opposed by the large majority of the shareholders and the companies were solvent and yet winding up orders were made.[12]

For the purpose of determining whether or not the substratum has gone, wide powers given in general words will be construed as ancillary to the specific objects;[13] but the fact that the objects

1 Agrani Bank vs Bangladesh Tyres Ltd 43 DLR (AD) 164.
2 Ellal Textile Mills vs Abdul Awal 38 DLR (AD) 26.
3 In re Fildes Bros. Ltd [1970] 1 All E.R. 923 Ch.D.
4 Motiur Rahman vs May Industries Ltd. Supra.
5 11th Ed p.1160.
6 Industrial Development Corporation of Orissa Ltd vs Hira Steels & Alloys Ltd. [1982] 52 Comp. Cas. 377(Orissa)
7 Rupa Bharati Ltd vs Registrar of Companies [1969] 1 Comp. L.J. 296(Orissa)
8 In re Orissa Trunks and Enamel Works Ltd [1973] 43 Comp. Cas. 503(Orissa)
9 at page 698
10 Re German Date Coffee Co. [1882] 20 Ch.D. 169 (a German patent to manufacture substitutes of coffee from dates could not be obtained); Re Haven Gold Co [1882] 20 Ch.D.151
11 Re Baku Consolidated Oil Field [1944] 1 All E.R. 24
12 also see Re Eastern Telegraph Co. [1947] 2 All E.R. 104;Re Kitson & Co. Ltd [1946] 1 All E.R. 435.
13 Buckley on the Companies Acts 13th Ed. page 456 citing a number of old cases

of a company included the acquisition of a particular business will not necessarily mean that, if that particular business is disposed of, the company's substratum have gone.[1]

2) the company was a bubble;[2]

3) the company was conceived and brought forth in fraud;[3] (a meeting of shareholders had voted in favour of continuing the business, but false statements had been made at the meeting, and the vote did not, in the opinion of the Court reflect the real wish of the majority).

The mere fact of there having been fraud in the promotion or fraudulent misrepresentation in the prospectus is not of itself ordinarily sufficient to found a winding up order, for the majority of the shareholders may waive the fraud.[4] Fraud not connected with the formation or promotion, but against third parties in carrying on the business, does not ordinarily form a ground for a compulsory order.[5] But if the company is carrying on an illegal business and there be intent to defraud the public then the company may be wound up but not if the company is proceeding to do something which is ultra vires.[6]

4) there was a complete deadlock;[7]

5) the articles provided for a winding up in the event which had happened;[8]

6) one of the principal shareholders refused to produce accounts or balance sheets or to pay dividends, he having a majority of the voting power.[9]

7) the petitioner was excluded from all participation in the business;[10]

8) the principle applied was that in case of a small private company facts which would justify the dissolution of a partnership;[11]

But the same editors of Palmer' book note that where directors , holding half the shares, refused to register as members the executors of a deceased shareholder who held the other half, thus giving themselves complete control, a winding up order was refused.[12]

This clause was at one time relied upon in making orders to wind up companies which had issued debentures in excess of the value of their assets and whose business was being carried on for the benefit of the debenture holders, leaving the unsecured creditors unpaid.[13]

21.5.5 Professor Gower notes that the scope of the two remedies of seeking to wind up a company on just and equitable ground because of unfairly prejudicial conduct and seeking protection of minority shareholders 'is not wholly co-terminous'.[14] The author suggests that a single act or omission may be unfairly prejudicial but is less likely to be regarded as making it just and equitable to wind it up. On the other hand, in case of a deadlock but no unfairly prejudicial conduct, the company may be wound up. However, on a winding up, the Court may after examining the conduct of any person involved in the promotion or management of the company compel him to repay or restore any money retained or misapplied by him.[15]

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1 ibid
2 Re London and County Coal Co. (1867) L.R. 3 Eq. 3
3 Re T.E. Brinsmead & Sons [1897] 1 Ch 45;(1897) 1 Ch 406.
4 Re Haven Gold Mining Co. Supra
5 Re Medical Battery Co. [1894] 1 Ch.444.
6 Buckley on the Companies Acts 13th Ed. page 457 citing old decisions.
7 Re Yenidje Co. Ltd. [1916] 2 Ch.426;Re National Drive-in Theatres [1954] 2 Dominion Law Reports(Canada) 55; Re American Pioneer Leather Co.[1918] 1 Ch. 556.
8 Re American Pioneer Leather Co. Supra
9 Loch vs John Blackwood Ltd. [1924] A.C. 783.
10 Thomson vs Drysdale [1925] Scottish Cases 311.
11 Re Davis & Collett Ltd [1935] Ch. 693;Re Yenidje Tobacco Co. Supra; Rayfield vs Hands (1958) 2 W.L.R. 851,857.
12 Re Cuthbert Cooper & Sons Ltd (1937) Ch. 393.
13 Re Chic Ltd (1905) 2 Ch.345,348;Re Melson (Alfred) & Co.(1906) 1 Ch.841,844,845; Re Clandown Colliery Co. (1915) 1 Ch. 369; Re Crigglestone Coal Co.(1906) 2 Ch. 327.
14 Modern Company Law 5th Ed. page 670.
15 Section 331 of the Companies Act 1994.

It is for this reason that an oppressed member may sometimes welcome the winding up of a company. In an action under section 233 (protection of minority shareholders) the ten percent shareholders applying under that section must prove that the business is being carried on in prejudice to a member but in liquidation the Court may investigate and find out for itself whether a person in control of the business had misapplied or retained the monies of the company.

21.6.1 **Contributory** – Section 237 of the Companies Act 1994 defines a contributory as every person liable to contribute to the assets of the company in the event of its being wound up. Section 235 provides that in the event of a company being wound up, every present and past member shall, subject to the provisions of the section, be liable to contribute to the assets of the company to an amount sufficient for payment of its debts and liabilities and the costs, charges and expenses of the winding up. The section however provides further that a past member shall not be liable to contribute if he has ceased to be a member for one year or upwards before the commencement of the winding up or for liabilities contracted after he has ceased to be a member and it appears that the existing members are unable to satisfy the contributions required to be made by them; also that in the case of a company limited by shares, no contribution shall be required from any member exceeding the amount if any, unpaid on the shares in respect to which he is liable as a present or past member; and in the case of a company limited by guarantee , no contribution shall be required from any member exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up. Section 235 (1)(iv)(v).

A sum due to any member of a company in his character of a member, by way of dividends or profits or otherwise, shall not be deemed to be a debt of the company payable to that member in a case of competition between himself and any other creditor who is not a member of the company. Section 235 (1) (vii).

The liability of the contributory shall create a debt payable at the time specified in the calls made on him by the liquidator. Section 238(1); and in case of his death his liable to pay the debt due to the company. Section 239 (1).

A shareholder of a company which holds shares in a second company has no right to petition for winding up the second company because he cannot derive any advantage or disadvantage and so is not a contributory.[1]

21.6.2 - Section 235 imposes a statutory liability on a shareholder for the amount remaining unpaid on the shares he has taken.[2] The liability is a new one and the limitation starts from the date of the liquidation even though earlier calls have become time-barred.[3] It is a statutory liability.[4] The liability remains even if the shares were forfeited.[5] A contributory cannot claim any set off against calls due from him.[6] The liquidator will settle the list of contributories.

21.7.1 **Who can Apply for Winding Up** – Section 245 provides that an application for winding up can be made by a creditor, the company or a contributory who has held the shares for at least six months in the eighteen months preceding the commencement of the winding up. The Registrar may also apply with the consent of the Government if it appears so necessary from a perusal of the financial condition of the company as disclosed in the balance sheet or from the report of the Inspector appointed under section 195 or if it appears to the Government to do so under section 204.[7] The company must be given a chance of being heard before a petition is filed in this regard. A petition for the winding up on the ground that the company has not held a statutory meeting shall not be filed by anyone other than a shareholder and that too not before the expiration of fourteen days after the last day on

1 Mazharul Hoque vs. Bulk Management (BD) Ltd. 48 DLR (1996) 453 = (1996) BLD (HC) 575.
2 Hansraj vs Asthana 60 I.A. 1;[1932] 2 Comp. Cas. 548(PC).
3 In re East Bengal Sugar Mills Ltd AIR 1941 Cal 143; M.Gowda vs Liquidators AIR 1963 Mys 61.
4 In re City of London Insurance Co. Ltd [1932] 1 Ch 226; In re Apex Film Distributors Ltd [1960]1 All E.R. 152.
5 Ladies Dress Association vs Pulbrook [1900] 2 Q.B. 376.
6 Ebrahim Sait vs South Industrials Ltd AIR 1938 Mad 962.
7 section 245 (b).

which the meeting ought to have been held.[1] A contingent or prospective creditor will have to give security for costs until a prima facie case has been made out to the satisfaction of the court for winding up.[2] A guarantor of the company's debt is a contingent creditor.[3] The Indian Supreme Court has held that the workers of a company are entitled to appear at the hearing of the winding up petition whether to support or oppose it so long as no winding up order was made by the court.[4] In an unreported case a particular cotton mill was wound up and the workers appeared and filed an application for stay of the winding up order and our High Court rescinded the earlier winding up order passed in the latter part of 1971 and restored the management to the workers on their paying the expenses and the monies deposited by the intending buyer of the cotton mill. This happened in the earlier part of 1972 and soon all cotton mills were nationalised and the entire proceedings came to a naught.

21.7.2 Section 246 provides that an order for winding up of a company shall operate in favour of all creditors and all contributories. This, irrespective of who made the petition.

Section 247 provides that a winding up of a company by the court shall be deemed to commence at the time of the presentation of the petition for the winding up. This will extend the time for filing of claims by and against the liquidator of the company.

Section 248 gives specific powers to the court to grant injunction, upon the application of the company or of any creditor or contributory of the company, restraining further proceedings in any suit or proceedings against the company and also to pass similar orders upon such terms as the court thinks fit. The High Court refused to apply this section to grant injunction.[5]

Section 249 gives power to the court to dismiss the petition, adjourn the hearing conditionally or unconditionally or to make any interim order which it deems just . The fact that the assets of the company have been mortgaged to an amount equal to or in excess of the assets or that the company has no assets will not be a consideration in refusing to make a winding up order. The court shall on making of an order for winding up of a company either appoint a liquidator or cause intimation thereof to be sent to the official liquidator.[6] The Supreme Court of India has held that workmen have a right to appear and be heard in a petition for winding up because their livelihood is at stake although they are not persons named in the Companies Act who may be heard in hearing a petition for winding up.[7]

When a winding up order has been made or a provisional liquidator has been appointed , no suit or other legal proceeding shall proceed or commence against the company except by leave of court.[8]

Section 252 requires the petitioner and the company to file with the Registrar a copy of the winding up order within thirty days of the making of it; the Registrar shall then register a summary thereof in his books relating to the company and shall notify in the official gazette that such an order has been made.[9]

A winding up order shall be deemed to be notice of discharge to the servants of the company except when the business of the company is continued.[10]

21.8.1 **Stay of Proceedings** – Section 253 gives power to the court to stay the winding up proceedings, either altogether or for a limited time, on such terms as it thinks fit, on the application of any creditor or contributory. This section has been used to stop or suspend winding up orders made earlier.

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1 ibid sub-section (c).
2 ibid sub-section (d).
3 Anil Vasudev Salgonkar vs Kermeen Foods P. Ltd. (1985) 58 Comp. Cas. 156.Guj.
4 National Textile Workers Union vs P.R. Rama Krishnan AIR 1983 SC 75.
5 Salim Akhter Khan BMA and another vs Advanced Development Technologies Ltd. and others 6 BLC (HCD) 307.
6 ibid sub-section (3).
7 National Textile Workers Union vs Ramakrishnan (P.R.) [1983] 53 Comp. Cas. 184 SC.
8 section 250
9 section 252(2).
10 ibid subsection (3).

Section 250 provides that when a winding up order has been made or a provisional liquidator has been appointed no suit or other legal proceeding shall be proceeded with or commenced against the company except by leave of the court and subject to such terms as the court may impose. The object is to pit all unsecured creditors upon an equality and to put them paripassu.[1] The power of the court to stay proceedings against the company should be exercised judicially and not automatically. The court may examine whether the purpose is to delay proceedings.[2] The Supreme Court of India granted stay of proceedings to avoid conflicting decisions.[3] On the power of the High Court to stay proceedings in a foreign court see *Re Vocalion (Foreign) Ltd;*[4] In re International Pulp & Paper Co.[5] and *Re Colaba Land and Mills Co. Ltd.*[6] Quare where the plaintiff is within the jurisdiction of the local courts and may be restrained by an order of injunction.

Stay of winding up proceedings does not affect cases pending before the company court unless included so in the order.[7] However, for an application under section 250 for stay of proceedings to succeed the petitioner must show that the company is in winding up and cannot question the validity of the winding up.[8]

The word 'suit' in section 250 means a suit instituted for the first time and 'other legal proceedings' are legal proceedings which are other than a suit instituted for the first time. These words do not include appeal, revision etc at the instance of a party other than the official liquidator.[9] The Dhaka High Court clarified that the meaning of the expression 'leave of the court' referred to in section 250 means the consent of the winding up court and not of the executing court.[10] The court relied on the decision in the case of *the Union Bank (in liquidation).*[11] This was however a decision which concerned a banking company and the court held that the liquidation of a banking company was a matter to be dealt with by the High Court under section 61 of the Banking Companies Ordinance. In any event section 3 of the Companies Act having clearly provided that the court having jurisdiction under the Companies Act being the High Court Division there is little doubt that section 250 refers to the High Court Division.

Mr. Justice Md. Mozammel Hoque observed that if the Banking Companies Ordinance is read with section 171 of the Companies Act of 1913(section 250 of the current Act) and the PDR Act then section 171 of the Companies Act cannot be attracted to the certificate proceedings which started long before the order of liquidation.[12]

Winding up order operates in favour of all creditors and with the passing up of a winding up order no suit shall be proceeded with or commenced except with the court's leave.[13]

Mr. Justice Mustafa Kamal sitting in the High Court Division has held that section 171 of the Companies Act of 1913 (similar to section 250 of the Act of 1994) has no application if a company is wound up under the Bangladesh Industrial Enterprises (Nationalisation) Order (P.O.27 of 1972) as the order to wind up the company in that case would be issued by the Government and not by the court. [14]

A division bench of the Dacca High Court following the Lahore decision held that the word 'suit' in section 171 of the Companies Act, 1913 means a suit instituted for the first time and the words 'other legal proceedings' mean legal proceedings which are other than a

1 Lindley L.J. in Re Oak Pitts Colliery Co [1882] 21 Ch.D. 322,329.
2 Official Liquidator, Golcha Properties (P.) Ltd vs Dharti Dhan (P.) Ltd [1977] 47 Comp. Cas. 420(SC).
3 Shree Vallabh Glass Works Ltd vs Industrial Credit and Investment Corporation of India Ltd. [1987] 62 Comp. Cas 101.
4 [1932] 2 Ch. 196.
5 [1876] 3 Ch.D 594
6 [1972] 42 Comp. Cas 168(SC)
7 Central Bank of India vs Atlas Works P. Ltd [1985] 58 Comp Cas 243.
8 Sonajuli Tea & Industries Ltd vs Ashkaran Chatter Singh [1982] 52 Comp Cas 568 (Cal).
9 Kishen Singh vs Industrial Bank of India AIR 1918 Lah 181.
10 Bazlul Ghani (Md) vs The Pioneer Bank Ltd. Comilla 42 DLR (1990) 480.
11 1964 PLD 742
12 Official Liquidator vs Johura Khatun 43 DLR(1991) 558.
13 Uttara Bank vs M/S Rahman Biscuit Factory Ltd. (1980) 32 DLR 45.
14 Abdul Hamid vs Dhakeswari Cotton Mills Ltd and ors. 36 DLR (1984) 257.

suit instituted for the first time. The words 'other legal proceedings' in this section do not include any proceeding arising out of a suit or a proceeding. In other words, they do not include appeal, revision etc at the instance of a party other than the official liquidator. If a party wants to institute a suit or start any legal proceeding for the first time against a company which has gone into liquidation such suit or other legal proceeding shall not be proceeded with or commenced without the leave of the Company Court.[1] Company Court can stay application for winding up if it is an abuse of the process of Court.[2] Liquidation proceedings cannot be challenged in a writ.[3]

21.8.2 The Supreme Court of India has held that the court has jurisdiction to grant leave to proceed with a suit or other proceeding against a company in liquidation at a later stage, i.e., after the commencement of the suit post facto.[4] If a suit is proceeded with without leave and a decree obtained then is the decree a nullity? No, and a subsequent leave may be enough says the Calcutta High Court.[5] A counter claim by a defendant in a suit by the company needs leave of the court.[6] Income Tax proceedings are outside the ambit of section 250 and need no permission of the court to proceed with.[7] Power to stay proceedings is discretionary.[8] The power is applied in the case of voluntary liquidation also.[9] For a historical development of the law in India on this topic see the decision of the Supreme Court of India.[10] Where the court feels that the matter can be disposed of in the winding up proceeding itself it will refuse to grant leave for the institution of a separate suit or proceeding.[11]

An appeal lies from an order refusing to grant leave under section 285 of the Act. So held by the Bombay High Court in *Balakrishna vs Indian Associate Chemical Industries Ltd*[12] under corresponding provisions of the Indian Companies Act.

As to the question of limitation for suits to be filed for or against the company see the Indian decisions referred to in *Best and Crompton Engineering Ltd vs The Official Liquidator*.[13] Also see the unreported decision of a single bench of the Dhaka High Court (Mr.Justice Mustafa Kamal) where the court awarded a decree in favour of the liquidator of Mahalaxmi Bank in liquidation in a suit regarding title to land where the bank was entitled to the decree on the basis of adverse possession although it was itself dispossessed in 1955 and the suit was filed in 1981 because the liquidation started in 1959 and the time since the liquidation started would be excluded (four years before the liquidation).[14] An appeal was pending in the appellate forum at the time of writing this script.

The same decision also held that the Company Court acting under section 61 of the Banking Companies Ordinance 1962 is not a mere civil court determining title and possession leaving the parties to their consequent fate. The Court liquidating a banking company is competent to pass such further order or orders as will ensure a smooth, orderly and early liquidation of the banking company.

1 Sayedul Huq vs Liquidator, Noakhali Union Bank 13 DLR (1961) Dacca 481,483.

2 Dr. Naimur Rahman vs. Shahbajpur Tea Company Ltd. (1991) BLD (AD)138; Amin Scales Ltd. vs. Yakub (1987) BLD (AD) 259.

3 Md. Abu Yusuf vs. Bangladesh (1993) BLD (AD) 154. Also see The Official Liquidator East Bengal Commercial Bank Ltd. vs. Jahura Khatun (1990) BLD (HC) 392.

4 Banshidhar Shankarlal vs Mohd. Ibrahim [1971] 41 Comp. Cas. 21(SC); Suresh Chandra Khashnabish vs Bank of Calcutta [1951] 21 Comp. Cas.110 (Cal).

5 Roopnarayan Ramchandra Private Ltd vs Brahmaputra Tea Co.(India) Ltd [1961] 65 CWN 1060; Srimati Bhagwati Devi Bulna vs Dhanraj Mills (P.) Ltd [1969] 39 Comp. Cas 1023. Also see Roberts Petroleum Ltd vs Bernard Kenny Ltd [1983] 1 All E.R. 564.

6 Langley Constructions (Brixham) Ltd vs Wells [1969] 2 All E.R. 46.

7 Kondaskar (SV) Official Liquidator vs Deshpande [1972] 42 Comp. Cas 168 (SC).

8 Official liquidator vs Dharti Dhan Ltd.AIR 1977 SC 740.

9 Arrah Sasaram Rly co. vs District Board Rohtas [1982] 52 Comp. Cas. (Cal) 326,333,335-

10 Sudarsan Chits (I) Ltd vs G.Sukumaran Pillai AIR 1984 SC 1579.

11 Cotton Corporation of India Ltd vs Radhakrishna Mills ltd. [1993] 76 Comp. Cas. 637.(Mad).

12 AIR 1959 Bom 41

13 AIR 1995 Mad 20.

14 Suit No 1 of 1981 decided on 9 May 1984, Mahaluxmi Bank Ltd (in liquidation) vs Sarat Kumar Kanungo and others.

If a scheme is made to replace the winding up the court must look at the scheme and see whether the Act has been complied with and whether the majority are acting bonafide.[1] The Indian High Courts have observed that the authorities clearly indicate that the court has to ascertain and be satisfied as to –

1. Whether the provisions of the statute have been complied with.
2. Whether the scheme is reasonable and practical.
3. Whether, in approving the scheme the creditors or shareholders had sufficient information and acted honestly and in good faith and
4. Whether considerations of public interest ought, in the opinion of the court to override the decision of the creditors or shareholders.[2]

21.9.1 **Official Liquidator** – Sections 255-266 of the Companies Act 1994 deal with the appointment of the official liquidator (section 255),his resignations, removals, filling up vacancies and compensation (section 256), statement of affairs to be made to the liquidator (section 258), statement by liquidator as to the assets of the company (section 259), custody of company's property (section 260), the appointment of a committee of inspection of the accounts of the liquidator (section 261), powers of the official liquidator (section 262), limit of discretion of official liquidator (section 263), legal assistance to the official liquidator (section 264), responsibility of the liquidator to keep books containing proceedings of meetings and to submit accounts of receipts to the Court (section 265), and exercise and control of liquidator's powers (section 266).

21.9.2 A single judge of the Lahore High Court has held that it is the discretion of the court to appoint the provisional liquidator under section 255(2) and that this discretion must be exercised judicially although it is not essential that the court should find that the company must ultimately go into liquidation.[3]

The liquidator in a winding up by the court is an officer of the court.[4]

The functions of a liquidator are to secure that the assets of the company are got in, realised and distributed to the company's creditors and if there is a surplus, to the persons entitled to it. If the liquidator distributes the assets without making provision for the liabilities he is liable to pay damages to the unpaid creditors.[5]

The statement of affairs to be made to the liquidator under section 258 of the Act is to be filed by the directors or if the liquidator so requires, subject to the direction of the court, a past director, promoter or employee of the company. Such statement shall be in the form of an affidavit containing an account of the assets, debts and liabilities, the names, residence and occupation of the creditors stating separately the amount of secured and unsecured debts with particulars of the securities and also the debts due to the company and the names, residences and occupations of the persons from whom they are due and the amount likely to be realised therefrom.[6]

Section 259 requires the liquidator to file a statement in court as to the amount of the capital issued, subscribed and paid up and the estimated amount of assets and liabilities mentioning separately the cash and negotiable securities, debts due from contributories, debts due to and securities, if any, available to the company, movable and immovable properties belonging to the company, and unpaid calls. The liquidator shall also state the causes of the failure of the company and whether in his opinion further enquiry is desirable as to any

1 In re: Alabama, New Orleans, Texas and Pacific Junction Railway Company [1891] 1 Ch 213 (CA).In re: English, Scottish and Australian Chartered Bank [1893] 3 Ch. 385(CA); In re: Dorman Long and Company Ltd [1934] 1 Ch 635.

2 Bharati Central Bank Ltd ILR [1949] 1 Cal 127;In re: Hindustan General Electric Corporation [1959] 29 comp. Cas 46; P.Appuny vs State Tile Works Ltd [1980] 50 Comp. Cas. 286(Ker) - a case of a scheme prepared by the employees .

3 National Bank of Pakistan vs Punjab Silk Mills Ltd 21 PLD(1969) Lah 194.

4 Megarry J. in Re Rolls Razor Ltd (No 2) [1970] Ch. 576,586.

5 James Smith & Sons (Norwood) Ltd vs Goodman [1936] Ch. 216 CA.

6 section 258(1).

matter relating to the promotion, formation or failure of the company or the conduct of its business. Any fraud committed in formation of the company should also be reported.

Section 260 requires the official liquidator to take into custody all properties of the company and such properties and effects of the company shall be deemed to be in custody of the court. Where Official Liquidator neglects to protect or safeguard the interest of the company any contributory can file an application under section 260.[1]

A committee of inspection consisting of not more than twelve members may be formed to inspect the accounts of the official liquidator.[2]

The official liquidator shall have powers with the sanction of the court to institute or defend any suit or prosecution, to carry on the business of the company so far as may be necessary for the beneficial winding up of the same, to sell the properties of the company either by private contract or public auction, to do all acts in the name of the company including execution of deeds and receipts, negotiable instruments, to raise on the assets of the company any more requisite, and to do any act necessary for obtaining payment of any money due from a contributory and to do all such other things as may be necessary for winding up the affairs of the company and distributing its assets.[3]

The official liquidator is required to keep proper books containing proceedings of meetings.[4] He is also required to prepare the accounts of the company in the prescribed form and have it verified and have these audited and submitted to the court at least twice a year.[5]

The official liquidator shall have regard to any directions given by the creditors, contributories at any general meeting or the committee of inspection in the administration and distribution of the assets of the company.[6] He may apply to the court for directions in a particular manner.[7] and a person aggrieved by a decision or act of the official liquidator may apply to the court and the court may confirm, modify or reverse the act or decision complained of.[8]

21.9.3.1 A liquidator stands in a fiduciary position towards the company. If he sells the property of the company at a nominal price to someone who is really his representative he will have to repay the secret profit. As an officer of the Court the liquidator must maintain an even and impartial hand between all individuals whose interests are involved in the winding up. It is his duty to the whole body of creditors, the whole body of shareholders, and to the Court to make himself thoroughly acquainted with the company's affairs, and to suppress or conceal nothing coming to his knowledge in the course of his investigation which is material to ascertain the exact truth in every case before the Court, and it is for the judge to see that he does his duty in this respect.[9]

On the requirements of the statements of affairs to be made to the liquidator (section 258) the Orissa High Court has held that where the company is in liquidation it is the duty of the ex-director to bring to the notice of the liquidator about the affairs of the company and to comply with the orders of the official liquidator. If the ex-director fails he will be in default in complying with the requirements of the section but in extenuating circumstances a lenient view will be taken.[10] It is for the official liquidator to prove that the default was committed without reasonable excuse.[11]

21.9.3.2 Under section 260 the official liquidator is the statutory custodian of the company's property and the custody of the court is only the notional custody. The actual custody and

1 Bashati Property Development Ltd. and vs Official Liquidator 5 BLC (HC) 368.
2 section 261
3 section 262
4 section 265(1)
5 section 265 (2),(3)(4)
6 section 266(1)
7 ibid sub-section (3)
8 ibid subsection (5)
9 Halsbury's Laws of England para 1111-2 4th ed.
10 Official Liquidator vs Jagannath Das AIR 1967 Orissa 185.Also see Official Liquidator, B.S. Motors P. Ltd vs Jagjit Singh Sawhney and another ILR (1974) 1 Delhi 243;[1974] 44 Comp Cas 381(Delhi).
11 Official Liquidator vs P.K.Bedi etc ILR (1974) 1 Del 809.

control of the company's property is with the liquidator but the court exercises control over the liquidator although this is only a supervisory control.[1] The Supreme Court of India has held that if the principal debtor company has gone into liquidation the guarantor bank must pay. A surety is no doubt discharged under section 134 of the Contract Act by any contract between the creditor and the principal debtor by which the principal debtor is released or by any act or omission of the creditor , the legal consequence of which is the discharge of the principal debtor, but a discharge which the principal debtor may secure by operation of law in bankruptcy or in liquidation proceedings in the case of a company does not absolve the surety of his liability.[2]

A singe judge of the Dacca High Court has observed that under sub-section (2) of section 178 of the Act of 1913 (corresponding to section 260 of the current Act) all the properties and assets of the company shall be deemed to be in the custody of the court from the date of the order of the winding up and under sub-section (1) the official liquidator shall take into his custody or under his control all the property, effect and actionable claims to which the company is or appears to be entitled. Section 229 of the Act of 1913 (corresponding to section 324 of the current Act) makes applicable the insolvency rules in winding up of insolvent companies in respect of the rights of secured or unsecured creditors. In such circumstances section 178 is controlled by section 229 of the Act.[3]

21.9.3.3 **Powers of Liquidator** – If the liquidator sells a property it cannot be interfered with unless sufficient grounds have been disclosed which would justify the conclusion that the discretion has not been judicially exercised by the court. The subsequent offer of a higher bid is no ground for refusing the confirmation.[4] The Calcutta High Court has held that in the case of a compulsory winding up, the debts and liabilities will have to be paid first by the liquidator and then the court shall adjust the rights of the contributories between themselves and distribute the surplus among the persons entitled thereto.[5]

The power under section 261 (1) (b) enables the liquidator to carry on the business of the company so far as may be necessary for the beneficial winding up of the company. Stoppage of work does not mean closure of business and the liquidator may carry on the business.

Court's sanction to commence an action by the liquidator may be in general terms and complaint filed on the basis of such sanction is not invalid.[6]

If the liquidator takes action without the sanction of the Court then it is not automatically illegal or invalid on that ground.[7] For a criminal prosecution sanction may not be necessary.[8]

All debts and liabilities incurred by the liquidator in the carrying on of the business of the company have priority over the general debts and liabilities of the company.[9]

The liquidator is not personally responsible if he acts in the name of the company.[10] A liquidator is an agent employed for the purpose of winding up a company.[11] The Supreme Court of India has held that a liquidator must confine the business of the company to be carried on to the business the company may carry on.[12] Once a sanction is given to the

1 In re Mahaluxmi Cotton Mills Ltd [1960] 30 Comp. Cas 107.
2 M.S.E.B. Bombay vs Official Liquidator, H.C. Ernakulam AIR 1982 Supreme Court 1497.
3 Uttara Bank vs M/S Rahman Biscuit Factory 32 DLR(1980) 45.
4 Premier Insurance Co. Ltd vs Bharat Commerce and Industries Ltd. AIR 1962 Mysore 185;
5 Shahan Purohit vs Jagannath Roy AIR 1969 Cal 424.
6 Mrityunjay vs Provat Kumar AIR 1953 Cal 153.
7 Dr. Sailendra Nath Sinha vs Jasoda AIR 1959 SC 51.
8 J.M.Akhaney vs State of Bombay AIR 1956 SC 575.
9 Re Davis & Co. [1945] Ch 402.
10 S.Hazel & Co. vs Cooper [1933] 1 KB 840.
11 Re Windsor Steam Coal Ltd [1928] Ch 609;(1929) 1 Ch. 151.
12 Ravindra Ishwardas Sethna vs Official Liquidator, Bombay [1983] 54 Comp Cas 702 (SC).

liquidator to carry on the business by the Court the liquidator's powers are not limited by the company's constitution.[1]

21.9.3.4 **Duties and Responsibilities of a Liquidator** – The liquidator has no power to distribute the assets among the contributories without sanction of the court.[2] The court is to scrutinise to see whether there is irregularity or fraud or disposal of property at a grossly inadequate price.[3]

The expression 'control by the court' gives a right to the creditor or a contributory to apply to the court in the matter of exercise of powers by the liquidator.[4]

The Dacca High Court observed that provision in section 179 of the Act of 1913 (corresponding to section 262 of the current Act) has been made to check and control the official liquidator so that no unnecessary litigation is started by the official liquidator or no filmsy defence is put up by the liquidator. Once a litigation is started by an official liquidator with leave of the court no further leave need be taken by any party to a suit other than by official liquidator for preferring an appeal or motion as the case may be against a decision given in such a suit or proceeding.[5]

If the liquidator brings an unsuccessful action he may be personally liable as to costs and these are not limited to the assets of the company.[6]

Where a liquidator carries on the business of the company he does so as the company's agent and is not personally liable on contracts which he enters into as liquidator.[7]

A liquidator is not strictly speaking a trustee for the individual creditors or contributories, his position being that of an agent of the company.[8]

For breach of any of his statutory duties the liquidator will be liable in damages to a creditor or contributory for injury caused to them.[9]

A liquidator should make provision for contingent claims of which he has notice, e.g., where the company, having assigned a lease, is under a contingent liability for the rent[10] or where he knows of possible claims by workmen for injuries not covered by insurance.[11]

If the liquidator pays a doubtful claim which turns out to be unfounded, without taking proper legal advice or applying to the Court for directions , he will be liable to refund the amount paid on a misfeasance summons taken out by a creditor or contributory.[12]

A liquidator will be saved in such a case if he has had obtained exercised all due care beforehand.

Maugham J. described the duties of a liquidator thus:

> ... high standard of care and diligence is required from a liquidator in a ...winding up. He is of course paid for his services; he is able to obtain wherever it is expedient the assistance of solicitors and counsel; and, which is a most important consideration, he is entitled, in every serious case of doubt or difficulty ... to submit the matter to the Court and to obtain its guidance.[13]

Section 266 provides that the official liquidator shall have regard to any direction that may be given by resolutions of the creditors or contributories at any general meeting. The

1 E.R. Naidu vs Madura Srinivas Mills Ltd AIR 1963 Mad 409.
2 Re Phoenix Oil and Transport Co. Ltd [1958] 1 All E.R. 158.
3 N.Dadabhoy vs Official Liquidator AIR 1960 Andhra 429; Soundararajan vs Mohammed Ismail AIR 1940 Mad 42; Brindraban Agarwal vs Official Liquidator AIR 1952 All 113.
4 Navalka & Sons vs Ramanjulu Naidu [1970] 40 Comp Cas 936(SC)
5 Sayedul Huq vs Liquidator, Noakhali Union Bank 13 DLR [1961] Dacca 481.
6 Re Wilson Lovatt & Sons Ltd [1977] 1 All ER 274.
7 Stead, Hazel & Co. vs cooper [1933] 1 K.B. 840.
8 Knowles vs Scott [1891] 1 Ch. 717.
9 Pulsford vs Devenish [1903] 2 Ch. 625.
10 James Smith and Sons (Norwood) Ltd vs Goodman [1936] Ch. 216
11 Re Armstrong Whitworth Securities Co Ltd [1947] Ch 673.
12 Re Windsor Steam Coal Co (1901) Ltd [1929] 1 Ch 151 CA.
13 Re Home and Colonial Insurance Co. Ltd (1930) 1 Ch 102 , 125

liquidator is bound to hand over dividend to the transferee of a share even though his name has not been entered in the share register.[1]

21.9.4 **Powers of Court** – Sections 267-277 deal with the ordinary powers of the Court. The court is to settle the list of contributories and shall cause the assets of the company to be collected and applied in discharge of its liabilities.[2]

A shareholder of fully paid shares cannot be placed on list of contributories without rectifying register and determination of liability in appropriate proceedings.[3]

It may require a contributory, trustee, receiver, banker, agent or officer of the company to pay , deliver, surrender or transfer any money, property or documents in his hands to the liquidator. section 268. Also, the court may order payment of debts by contributory or make calls on the contributories to the extent of their liability.[4]

In a case concerning old section 187 of the Companies Act of 1913 the Indian Supreme Court held that this section confers not merely power but jurisdiction to the High Court to direct payment of the amount due by a contributory and an order passed for payment manifestly is an order passed in exercise of the jurisdiction vested in the High Court by section 3 read with this section.[5]

Such an order, subject to a right to appeal, shall be conclusive evidence that the money was so due. (section 273.) The court shall adjust the right of the contributories among themselves and distribute any surplus among the persons entitled thereto. (section 275.) In case the assets of the company are not sufficient to meet the liabilities the court may order payment out of the assets of the costs, charges, and expenses in such order of priority as the court thinks fit.[6]

After the affairs of the company have been completely wound up, the court may dissolve the company by an order of dissolution . Such order shall have to be reported within fifteen days of the making of the order by the official liquidator.[7]

When winding up proceeding is pending before the Court, the fate of the company with all its assets and liabilities as well as rights of creditors and shareholders are subjudice before the court and this jurisdiction cannot be curtailed by an order under Article 34 of the BSB Order.[8]

When the list of contributories is settled by the Court it is final.[9] Statute barred debt will however not be taken into account.[10] The court will dispense with the settlement of list of contributories where there are surplus assets where all the issued shares are fully paid and rank pari passu and where the number of contributories is not large. The court may however, require inquiries to be made before distribution.[11]

Mr. Justice Badrul Haider Chowdhury while delivering judgment in a case in the Appellate Division where the petitioner sought two reliefs for rectification of the share register and for winding up the company, has held that in a single application two such incongruous prayers cannot be maintained and observed that the remedy of the petitioner also lay in an application for settlement of list of contributories under section 184 of the Act of 1913 (section 267 of the current Act).[12]

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1 Chunilal Khushaldas Patel vs H.K.Adyaru AIR 1956 SC 655.

2 section 267.

3 M/S Alote Estate vs R.B. Seth Hiralal Kalyanmul Kasliwal AIR 1971 S.C. 920.

4 section 269,270.

5 Jyoti Bhusan vs Benaras Bank Ltd AIR 1962 S.C. 403.

6 section 276.

7 section 277

8 BRTC vs. Asharaf Jute Mills Ltd. (1993) 45 DLR (H.C.)282

9 Waryam Singh vs Official Liquidator AIR 1926 Lah 414.

10 Re Art Reproduction Co. Ltd [1951] 2 All E.R. 984

11 Palmer's Company Precedents 17 Ed. p.403;Re Phoenix Oil & Transport Co. Ltd [1957] 3 All E.R. 218.

12 ET Mills Ltd vs Abdul Awal 38 DLR(AD) (1986)26,32.

A reference was made in this case to an observation of the Bombay High Court[1] where the court observed as follows:

> Section 184 incorporates section 38, under which , inter alia, if the name of a person is fraudulently or without sufficient cause entered in the register of members of a company, the person aggrieved or any member of the company apply to the Court for 'rectification of the register.[2]

Mr Justice Hamoodur Rahman of the Dacca High Court has held that an application under section 185 of the Act of 1913 (section 268 of the current Act) can be maintained only against a contributory, trustee, receiver , banker or agent or officer of the company for the purpose of delivering, surrendering or transferring the money or other property which should be in such person's hand and to which the company should be prima facie entitled. But if a bona fide dispute is raised whether the company is entitled or not to the money or the property, there is nothing in the section empowering the court or the liquidator to determine the question. If the party against whom the order is sought submits to the jurisdiction of the court as for example, where it admits that it has the money and it claims to set off for a lesser sum the court can determine the liability. The word 'trustee' in this section means only an express trustee and not a constructive trustee. The words 'other persons' appearing in section 188 of the Act of 1913 (section 271) refers to the category mentioned in section 185 of the Act of 1913 (section 268).[3] The judgment referred to a number of decisions of the English and Indian jurisdictions on the powers of the liquidator and the High Court. In that particular case the court declined to determine the dispute whether any liability was owed to the company.

On the power of the court to order a contributory to pay debts the Privy Council has held that section 269(1) is concerned only with monies due from a contributory other than monies payable by virtue of a call; this section creates a special procedure for obtaining payment of monies and does not create a foundation upon which to base a claim for payment and does not create a new right; this power is discretionary.[4]

Section 270 deals with the court's power to make calls. This is an alternative method by which the liquidator may get payment from a contributory and an order under this section does not make the contributory a judgment debtor.[5] The Madras High Court has held that while the company is a going concern a call seeks to enforce a contractual debt but after a winding up order is made payment of unpaid share money is enforced as a statutory liability.[6] There is no time limit for making a call under this section.[7] It is a new liability to contribute to the assets of the company. While it is quite true that a call made before the winding up was a debt to the company but that does not affect this new liability to contribute.[8]

Section 276 empowers the court in the event that the assets of the company are insufficient to meet the liabilities, to make an order out of the assets , of the costs , charges and expenses, incurred in the winding up in order of such priority as the court thinks just.

If the liquidator commences an action after liquidation and judgment is given against the company with costs, then the decree holder is entitled to the costs of the litigation ahead of any claims to be paid by the liquidator.[9]

Section 277 gives the court jurisdiction to dissolve a company when the affairs of a company have been completely wound up. The Dhaka High Court has held that money

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1 In re the Peninsular Life Assurance Co. Ltd AIR 1939 Bom 24

2 ibid.

3 Official Liquidator of the Economic Aid Corporation Ltd vs Messrs Singh & Co. and another (1958)8 PLR (Dac) 385.

4 Hansraj vs Dehradun Tramways Co. AIR 1933 PC 63.

5 Ex parte Whinney [1884] 13 QBD 476 Ex parte Grimwade [1886] 17 QBD 357.

6 In re Link Industries Ltd [1957] 27 Comp. Cas 468.

7 Collector of Subarkanta vs Shankarlal AIR 1960 Bom 516.

8 Jessels M.R. in Re Whitehouse & Co. [1878] 9 Ch. D. 595.

9 Re Pacific Coast Syndicate Ltd [1913] 2 Ch.D.26 cited in In re Noakhali Union Bank Ltd (In liquidation)16 DLR (1964) 656.

belonging to the company under liquidation cannot be withdrawn and paid to the official liquidator for the purpose of dissolution of another company under liquidation which has no assets of its own to meet the costs and expenses of the dissolution. The Official liquidator is to seek funds from the Government in this connection. The reason given by the court was that the two companies were distinct legal entities.[1]

Once the company was dissolved it ceased to exist and the liquidator could not represent any company. If he wants to perform any act he should have specific authority and the Companies Act contains no such provision.[2]

21.9.5 **Extraordinary Powers of Court** – The court may issue summons to any person suspected of having property of the company or supposed to be indebted to the company or any person whom the court deems capable of giving information concerning the trade, dealing, affairs or property of the company. The court may examine the person on oath and may require him to produce any document in his custody or power relating to the company.[3]

The Supreme Court of India has held that the rules of natural justice are not violated merely by the issue of an order requiring a person or persons to appear before a court for examination under this section without a prior notice being given to him.[4]

If a fraud has been committed in the promotion or formation of the company or by any director or the officer of the company in relation to the company since its formation the court may direct any person who has taken part in the promotion or formation of the company to attend before the court on a particular date and be publicly examined as to the promotion or formation or the conduct or the business of the company.[5]

Misfeasance is a serious charge and the application must contain a detailed narration of the specific acts or omissions on the part of each director quantifying the loss to the company.[6] The court has to be satisfied that same facts are given in the application which entitle the court to find that there is a prima facie case of fraud against the particular person named.[7]

Section 282 provides that all orders made by the court under this Act may be enforced in the same manner in which decrees of such court made in any suit pending therein may be enforced. The Dhaka High Court not having any original side jurisdiction, its execution process to enforce, for example , an order to rectify the share register of a company is to say the least, unclear. Section 283 and section 284 deal with mode of enforcing orders of the Company Court by other courts.

The court may order public examination of promoters, directors etc. under section 279 only if the conditions laid down in that section have been fulfilled. It is enough if facts suggesting fraud have been mentioned in the report of the official liquidator.[8]

Where the report of the official liquidator is filmsy, sketchy or unfair the court will not exercise its jurisdiction or discretion in making an order for public examination.[9] Filing of a misfeasance proceeding against a director does not bar an order under this section.[10] The power under this section may be exercised in the case of an application by the voluntary liquidator. [11]

The Dacca High Court has held that an application under section 196 of the Companies Act 1913 (section 279 of the Act of 1994) must show a prima facie case of fraud against the

1 Hansa International and another vs Eastern Pharma Ltd 48 DLR (1993) 482.
2 Narendra Bahadur Tandon vs Shankar Lal AIR 1980 SC 575.
3 section 278.
4 Satish Charan Law vs H.K. Ganguly AIR 1962 SC 806.
5 section 279.
6 Official liquidator vs Raghava Desikachar AIR 1974 SC 2069.
7 In re Indian State Bank Ltd AIR1933 All 366.
8 Seth Harbans vs National Sugar Mills AIR 1931 Lah 8;Exparte Barnes [1896] A.C. 146.
9 Tejani vs Official Receiver [1963] 1 All E.R. 429(PC).
10 S.Iyer vs P. Brahmayya AIR 1955 Mad 30.
11 Nawroji vs Laxman AIR 1920 Bom 284.

person concerned; merely a general allegation of fraud in the management of the company would not necessarily justify a public examination.[1]

21.9.6 **Appeals from Orders** – Section 285 provides that re-hearing of and appeals from order or decision made or given in the matter of winding up of a company by the court may be had in the same manner and subject to the same conditions in and subject to which appeals may be had from any order or decision of the same Court in cases within its ordinary jurisdiction.

Murshed C.J. observed that it is a well settled principle that an appeal is a creature of law and that no appeal would lie unless the law provides for it. The Act has advisedly made orders passed under it non-appealable except in case of certain sections only. In the Companies Act of 1913 three sections provided for appeals, namely sections 38, 153(7) and 202 equivalent to sections 43, 228 and 285 of the current Act. The appeal provided under section 38 of the old act is no more found in section 43 of the Act of 1994. It is the scheme of the Act which does not countenance an appeal other than those which have been allowed. It is important to remember that the Act provides a complete code of procedure governing appeals and it has precluded appeals from judgments and orders made under the aforesaid sections. The obvious reason for such a scheme is to give a finality to litigations in respect of matters relating to the Act. Orders made under other sections are therefore not appealable.[2]

This decision was followed in another case.[3] Another Division Bench of the East Pakistan High Court reiterated that the Companies Act provides a complete code of procedure governing appeals and it has precluded appeals from judgments and orders made under the Act except those made under those sections. Appeal lies against all orders winding up a company thereby finally disposing of disputes between parties. Section 202 of the Act of 1913 is wide enough to cover appeals against all orders made in the matter of winding up of a company provided such an order finally decides a dispute between the parties or deprives the appellant of a substantial and important right and is not a mere formal or interlocutory order. If order made is administrative in nature an appeal would not lie under section 202 of the Act of 1913.(section 285 of the Act of 1994). A direction to produce documents before the Company Court is an interlocutory order and no appeal lies.[4]

The Supreme Court of India has held that the essence of a judicial order is that there would be two parties and a lis between them which is the subject of adjudication.[5]

An order passed by the company judge on the liquidator to deposit money is not an order on a subordinate court in the matter of compromise and the executing court has jurisdiction to scrutinise the compromise.[6]

An order of penalty imposed under an application under section 196 of the Companies Act of 1913 (section 279 of the current Act) was held to be an appealable order.[7] But this decision was reversed by the Appellate Division on the ground that the company in question being a banking company it fell within the purview of section 66(1) of the Banking Companies Ordinance and no appeal would lie. The Appellate Division found that the provisions of section 66(1) of the Banking Companies Ordinance are wider than those of section 196 of the Companies Act 1913.[8]

After the repeal of the Letters Patent in Bangladesh the significance of a provision providing for appeal in the Companies Act is of little significance. Previously such an appeal would be preferred to a Division Bench of the High Court under clause 15 of the Letters Patent but with the repeal of the Letters Patent the High Court Division has lost its

1 Debendra Nath vs Bangladesh Bank 28 DLR(1976) 402.
2 Dacca Jute Mills vs Satish Chandra 19 DLR(1967)735,738.
3 Jabed Ali Sarker vs Dr Sultan Ahmed 26 DLR 196.
4 Aramit Ltd. ñvs- ANZ Grindlays Plc. 14 BLD (HC) 502
5 Shankarlal Agarwal and ors vs Shankarlal Poddar and others AIR 1965 SC 507.
6 Suruj Mia vs Pioneer Bank Ltd 20 DLR (1968) 1206.
7 Debendra Nath vs Bangladesh Bank 28 DLR (1976) 402.
8 Bangladesh Bank vs Debendra Nath 33 DLR(AD) (1981) 355.

jurisdiction to hear appeals from its own orders and the only appellate forum from the High Court Division is the Appellate Division granting leave to appeal under Article 103 of the Constitution. The High Court Division derives its jurisdiction from law or under the Constitution and the sections in the Companies Act providing for appeals did not provide the forum and the parties are left to file appeals in the Appellate Division. Thus, where in a case of rectification of share register the Division Bench reversed the decision of the single bench and an appeal was preferred to the Appellate Division, the Appellate Division held that the judgment of the Division Bench was a corum non judice. For an appeal to lie against an order of the company judge leave has to be taken under Article 103(1) of the Constitution.[1] The same decision held that the Original Side Rules framed by the Calcutta High Court under clause 37 of the Letters Patent, 1865 were inherited by the erstwhile Dacca High Court and the High Court Division had jurisdiction to hear appeals as long as Letters Patent 1865 was in the statute book. With its repeal by the Law Reforms Ordinance 1978 the Original Side Rules have no existence in the eye of law and therefore no appeal lies from High Court Division to High Court Division.

21.10.1 **Voluntary Winding Up** – Sections 286-290 and sections 306-315 deal with the general provisions which apply to voluntary winding up of companies.

A company may be wound up voluntarily if the period for which the company was formed expires or an event occurs which under the articles calls for dissolution of the company and a resolution is passed in a general meeting of the company to wind it up voluntarily; also if the company has resolved by a special resolution that the company should be wound up voluntarily; further, if the company cannot by reason of its liabilities continue business and passes an extraordinary resolution to that effect.[2]

The voluntary winding up shall commence from the date of the passing of the resolution.[3] The company shall cease to carry on business except so far as may be required for the beneficial winding up thereof.[4]

Notice is to be given of a special or extraordinary resolution to wind up a company voluntarily by advertisement in the official gazette and also in newspaper.[5]

Declaration of Solvency – Section 290 requires a company to hold a meeting of the directors before the date on which the resolution to wind up the company is proposed to make a declaration supported by an affidavit that the company is a solvent one. Where such a declaration is made it has to be supported by a report of the company's auditors on the company's affairs and must be delivered to the Registrar. If such a declaration is made then the winding up is known as the members voluntary winding up. If not then it will be a creditors voluntary winding up.

21.10.2 **Members Voluntary Winding Up** – Sections 291-296 deal with members voluntary winding up. The company in general meeting shall appoint the liquidator for the purpose of winding up the company and distributing the assets of the company. Section 294 provides that the liquidator may transfer assets of the company to another company in lieu of shares or other interests in that company in favour of the shareholders of the company being liquidated if the shareholders of the liquidating company authorise him in this behalf by a special resolution. A dissenting shareholder may ask the liquidator to purchase his interest at a price to be determined by agreement or arbitration. In that case the liquidator must pay him before the company is dissolved.

This section relates only to a members' voluntary winding up but where there is a supervision or a compulsory order a sale can be made under section 262 and all things necessary may be

1 Mustafa Kamal J. in Moqbul Ahmed vs Ahmed Impex 48 DLR(AD) (1996) 82,86.

2 Section 286

3 Section 287

4 Section 288

5 section 289

done under that section. It cannot be intended that the court shall have less power than liquidators. On the contrary, the court has more power , as not being bound by majorities and formalities.[1]

A sale under this section is binding on creditors; their remedy is to come for a supervision or compulsory order. This may in some cases render a supervision order expedient in order to give jurisdiction for the sanction.[2] In sanctioning a scheme of reconstruction by sale to a new company the court will have regard to the wishes of a majority of shareholders and creditors: a dissentient shareholder cannot be compelled to accept shares in the new company or the value put upon his interest by the liquidator, and if he will accept neither the value must be settled by arbitration.[3]

Buckley further comments that agreements under this section commonly provide that members of the selling company shall be entitled to shares in the purchasing company; this is not necessarily an offer to allot, and indeed, is not directly binding as between the member on the one hand and the purchasing company on the other; a document signed by a member of the selling company claiming his due allotment may therefore be a mere application and therefore withdrawable until accepted. This section contemplates a handing over of the assets of the one company to another company in consideration of shares in the latter company, but not the subjecting of the shareholders of the selling company, without their unanimous consent, to fresh liability. An agreement by which the selling company is to take a certain fixed number of shares in the new company, and, if its assets shall prove insufficient for the purpose, is to raise the necessary amount by a call, is not within this section.[4] There is however nothing ultra vires in agreeing to call the uncalled capital and include the proceeds in a sale.[5] Neither is there anything ultra vires in a sale upon the terms that the purchasing company shall pay the debts of the selling company and that if the debts exceed the selling company's assets the selling company shall be debtor to the purchasing company for the deficiency and a call may be made to provide for it.[6]

A shareholder can either (1) assent, or (2) dissent, and within seven days require his interest to be purchased, or (3) dissent and abandon all his interest in the company.[7] Where a company altered its articles so as to take power to carry out an arrangement similar to that provided under this section, without giving dissentient shareholders the option to receive the value of their shares in cash, this was invalid and a dissentient shareholder was entitled to have the value of his shares ascertained and paid as provided in the section.[8]

A notice of dissent given by a transferee not on the register is effectual if he obtains an order for rectification nunc pro tunc by entering his name on the register as of a date, before he dissented.[9]

The liquidator will have to call a general meeting of the company at the end of each year if the liquidation proceeding continues for more than a year.[10]

As soon as the affairs of the company are fully wound up the liquidator shall make up an account showing how the company has been wound up and the assets of the company disposed of and place it before a meeting of the shareholders .Within one week of the meeting the liquidator shall send a copy of the account and a return of the holding of the meeting to the Registrar. The Registrar shall forthwith resister them and on the expiry of three months from the registration the company shall be deemed to be dissolved.[11]

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1 Buckley on the Companies Act 13th Ed. p.585 citing a number of old decisions.

2 ibid

3 Re Imperial Mercantile Credit Assocn. and Re Irrigation Co. of France Exparte Fox [1871] 6 Ch. App 702.

4 ibid at page 585.

5 New Zealand Gold Extraction Co. vs Peacock [1894] 1 Q.B. 622

6 Re Bank of South Australia [1895] 1 Ch. 578.

7 Buckley,ibid at p. 588.

8 ibid.

9 Re Sussex Brick Co. [1904] 1 Ch 598.

10 Section 295

11 Section 296.

Unlike the liquidator in a winding up by the court , a liquidator in a voluntary winding up is not an officer of the court.[1] He is the agent of the company but not of the individual members.[2]

21.10.3 **Creditors Voluntary Winding Up** – Sections 298-305 apply to creditors voluntary winding up. The company shall call a meeting of creditors on the day or the day following the day on which the resolution for voluntarily winding up the company is to be passed and shall cause the notices of the said meeting of creditors to be sent to the creditors along with the notice of the general meeting in which the winding up is proposed. The directors of the company shall cause a full statement of the position of the company and the estimated amount of their claim to be laid before the meeting of creditors to be held and appoint one of their number to preside at the said meeting.[3]

The creditors may appoint their choice for appointment as liquidator and in that case he shall have preference over any nominee of the company for appointment as liquidator. Provided that any director may appeal to the Court against such appointment by the creditors within seven days of the nomination by the creditors.[4]

The creditors may likewise appoint a committee of inspection consisting of not more than five persons (subject to revision by the Court if any).[5]

The liquidator's remuneration is to be fixed by the creditors or the committee of inspection. (Section 301(1)) On the appointment of the liquidator all the powers of the directors shall cease, except so far as the committee of inspection or where there is no such committee, if the creditors sanction the continuance thereof.[6]

The liquidator, in so far as the power to accept shares etc as consideration for sale of property of the company has the same powers as he has in the case of a members and creditors voluntary winding up. (Sections 294 and 303). The liquidator is to call a meeting of the company and the creditors at the end of the year if the liquidation continues for more than a year.[7]

As soon as the affairs of the company are fully wound up the liquidator shall make an account of the winding up showing how the winding up has been conducted and the property has been disposed of and thereupon shall call a general meeting of the company and a meeting of the creditors by advertisement at least one month before the meetings and lay the accounts at the meetings. A return has to made to the Registrar. (Section 305). On application made in the winding up after the registration of the return, but before the expiration of his three months, the court has jurisdiction notwithstanding that the three months elapse before the order is made.[8]

"Fully wound up" means " as far as the liquidator can wind them up " that is when the liquidator has disposed of the assets as far as he can realise them , got in the calls as far as he can enforce them, paid the debts as far as he is aware of them, and done all that he can do in winding up the affairs. Continuing contractual obligations may make a dissolution impossible.[9]

It is not necessary for the affairs of the company to be fully wound up before the liquidator can validly make his return, only that they should be fully wound up so far as the liquidator is aware.[10]

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1 Megarry J. in Re Rolls Razor Ltd (No 2) [1970] Ch. 576.
2 Taylor v Wilson's Trustees [1975] Scottish Cases 146.
3 Section 298.
4 Section 299
5 Section 300
6 Section 301(2)
7 Section 304.
8 Buckley on the Companies Act 13th Ed. p. 593 citing old decisions.
9 ibid at page 594.
10 Re Cornish Manures Ltd [1967] 1 W.L.R. 807

21.10.4 **General Provisions for Voluntary Winding Up** – Sections 306-315 are general provisions for a voluntary winding up. Section 307 provides that the property of a company shall be applied in satisfaction of its liabilities paripassu and shall be distributed among the members according to their rights and interests in the company. The other provisions include powers of the liquidator, arrangement when binding on creditors, power to apply to Court to have questions determined of powers exercised.

Any arrangement between the company and the creditors will be binding on both if sanctioned by an extraordinary resolution and three-fourths of the creditors in number and value. The Court has the power to vary, amend, or confirm the arrangement on the application of any creditor or contributory.[1] The liquidator or any contributory or creditor may apply to the Court to determine any question arising in the winding up of the company.[2]

The winding up of a company shall not debar a creditor or contributory to apply for a winding up by the court, but in the case of an application by a contributory the court must be satisfied that the rights of the contributories will be prejudiced by a voluntary winding up.[3]

The editors of Buckley on the Companies Act comment that if there were transactions requiring investigation or circumstances which called for the exercise of the powers which the court had in a compulsory winding up , a compulsory order will be made.[4] If therefore, a prima facie case of malpractice is made out this will presumably be a ground for making a compulsory order. As a general rule, the right of a creditor was absolute to have a compulsory order if he brought his case within the section.[5]

A voluntary winding up does not automatically operate as a discharge of the company's employees; it has been suggested that it will do so if it takes place because the company is insolvent.[6] Premature termination of a written fixed term agreement may entitle the employee to damages.[7]

When the terms of the contract of employment are to be found in the articles, no damages for breach of contract are recoverable.[8]

This is because the rights under the articles of association may be enforced only by the members qua a member.

The liquidator has a duty to enquire into all claims against the company.[9] Even where the company is solvent, statute barred debts cannot be paid unless the contributories consent.[10]

In every voluntary winding up it is the duty of the liquidator to pay the debts of the company and adjust the rights of the contributories among themselves.[11] He may carry on the business of the company, if he reasonably thinks it is necessary for the beneficial winding up of the company. If he does so, those to whom he incurs obligations are entitled to be paid in priority to the creditors at the commencement of the winding up.[12]

A liquidator may seek guidance of the Court as if the company is being wound up by the Court.[13] In England it has been interpreted that if he is of the opinion that fraud has been committed in the formation of the company or since then, he can obtain an order of the court for the public examination of any promoter, director or other officer of the company.[14] He

1 Section 311.
2 Section 312
3 Section 314
4 13th Ed p.670.
5 ibid. at page 611.
6 Fowler vs Commercial Timber Co. Ltd [1930] 2 K.B. 1 CA per Greer L.J.
7 ibid
8 Re T. N. Farrer Ltd [1937] Ch. 352.
9 Austin Securities Ltd vs Northgate and English Stores Ltd [1969] 1 W.L.R. 529.
10 Re Art Reproduction Co. Ltd. [1952] Ch. 89.
11 Charlesworth and Morse : Company Law 14th Ed. p.801.
12 ibid. at page 802; Re Great Eastern Electric Co. Ltd [1941] Ch. 241.
13 section 312.
14 Re Campbell Coverings Ltd (No 2) [1954] Ch. 225.

can also apply for an order of private examination.[1] The Court is less likely to facilitate a distribution among the members than among the creditors.[2]

21.10.5 **Winding Up Subject to Supervision of Court** – Sections 316-321 provide for winding up subject to supervision of court.

When a company has by special or extraordinary resolution resolved to wind up voluntarily the court may make an order that the voluntary winding up shall continue but subject to supervision of court and on such terms as the court thinks just. (Section 316.) When a petition for this sort of winding up is made the court shall have jurisdiction over suits as in a case of winding up by petition.[3]

The court may have regard to wishes of creditors and contributories and has power to appoint and remove liquidators.[4]

Where an order is made for a winding up subject to supervision , the liquidator may, subject to any restriction imposed by the court, exercise all the powers as if the company was being wound up altogether voluntarily.[5]

The Dacca High Court has held that an order of the company judge directing the liquidator to do a certain act was not binding on the executing Court.[6]

The court will otherwise have all the powers to stay the suits and to make calls etc.[7]

In changing over from a voluntary liquidation to a winding up subject to supervision by court the wishes of the contributories must be taken into consideration[8] unless the company is insolvent.[9] However if the creditors have a genuine feeling that there should be an investigation by a liquidator who was not appointed by the directors then the Court will make an order making it subject to supervision of the Court.[10] The liquidator must not only be independent but also seem to be independent.[11] The Court is bound to have regard to the wishes of all the creditors[12] and if the majority feel that the voluntary liquidation should continue then an order will not be made unless the petitioner can show special circumstances.[13] The motives of the creditors are relevant[14] and in particular of those creditors who are also members and considerations of fairness and commercial morality should be taken into account.[15]

21.10.6 **Supplementary Provisions** – Sections 322-344 make supplementary provisions relating to winding up.

Any transfer of shares made without the sanction of the liquidator after the commencement of the winding up is void.[16]

The court should not interfere with the management of the company's affairs merely because a winding up petition has been presented.[17] Each case must be dealt with on its own

1 See Re Rolls Razor Ltd(No 2) [[970] Ch. 576.
2 Re R-R Realisations Ltd [1980] 1 All ER 1019.
3 Section 317
4 Sections 318-9
5 Section 320(1)
6 Subhkaran Rajghoria vs Pioneer Bank Ltd (in Liquidation) 23 D.L.R.(1971)1.
7 Section 320(2)
8 Re Surplus Properties (Huddersfield) Ltd Re (1984) BCLC 89
9 ibid. but also see Re James Milward & Co. Ltd [1940] Ch 333 CA and in Re Medisco Equipment Ltd. [1983] BCLC 305.
10 Re M.C.H.Services [1987] BCLC 535.
11 Re Lowestoft Traffic Services Ltd [1986] BCLC 81; Re H.J. Tomkins & Sons [1990] BCLC 76.
12 Re Home Remedies Ltd. [1943] Ch 1
13 Re B. Karsberg Ltd [1956] 1 WLR 47 CA; Re J.D.Swain Ltd [1965] WLR 909.
14 Re Falcon (R.J.) Developments [1987] BCLC 437
15 Re Palmer Marine Services Ltd. [1986] 1 W.L.R. 573.
16 Section 322
17 Re A Company [1987] BCLC 200 Ch.D.

facts and particular circumstances.[1] The court is guided by the same principles as those applied by the court in bankruptcy to protected transactions.[2] From the commencement of the floating charge, the mortgagee has an immediate and continuing equitable charge over the mortgagor's assets but it is subject to the right of the company to dispose of or deal with the assets free of or released from the charge to the extent that may properly be implied from the common intention of the parties that the company will continue to carry on its business or operations until the occurrence of some stipulated or contemplated event.[3] Section 323 provides that all claims against the company shall be admissible to proof against the company. Section 324 applies the Insolvency Rules to the winding up of an insolvent company. This is important in view of the Bankruptcy Act.

The Dacca High Court observed that the position of an attaching creditor under the Companies Act (section 229 of the Act of 1913) is similar to that under section 54 of the Provincial Insolvency Act.[4]

If by the terms of his employment, an officer is entitled, if deprived of his office, to a defined compensation, he can prove in the compulsory winding up for that compensation but where one of the terms of the engagement of an officer was that five thousand pounds be paid to him if the company discontinued to employ him, this as matter of construction meant a discontinuance when it was optional with the company either to continue or discontinue the employment – his employment having been terminated by the compulsory winding up, his claim failed.[5] An enforceable pension may be proved for in a winding up,[6] but not a mere voluntary allowance nor a pension payable to a person employed in an ultra vires business.[7]

A contributory of the company, having bought up a debt of the company for less than is actually due, may prove for the whole amount , and not merely for what he has paid for it, but not if he stands in a fiduciary relation towards the company.[8]

In the winding up of an insolvent company, creditors whose debts carry interest are entitled to dividend only upon what was due for principal and interest at the commencement of the winding up. The same principle applies in the case of a surety, who will not be admitted to proof for interest accruing after the commencement of the winding up upon payments made by him for the company, but only for the estimated value of his right to indemnity at the commencement of the winding up. The principle applies whether the company is wound up by the court or voluntarily or under supervision.[9] The assets are to be applied in payment of liabilities subsisting at the time of the winding up order.[10]

Section 325 provides for preferential payments of some debts over others. Government dues payable within the next twelve months before the date of commencement of the winding up, wages and salaries and compensations to be paid under law, provident or pension fund payments, and expenses of any investigation of affairs of the company under section 195 have priority over debts including claims secured by floating charges. Where a liquidator instead of taking any step to give up a property which was held on lease by the company tries to retain the same and use the same for the benefit of the business of the company in liquidation, the rent of the company should be regarded as cost and expenses of the winding up under section 325 and it should be paid in full like any other debt or expense incurred by the liquidator.[11]

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1 Re Steane's (Bournemouth) Ltd [1950] 1 All ER 21.

2 Palmer's Company Precedents Part II, 17th Edn p.298.Also see Re Gray's Inn Construction Co. Ltd [1980]1 All ER 814

3 Re Margaret Pty Ltd. [1984] 9 Aust. Comp. LR 269; Hamilton vs Westpac Banking Corpn and another [1985] BCLC 314; Hamilton vs Hunter [1982] 7 ACLR 295(a New South Wales Decision)

4 M/S Chandpur Mills Ltd vs The Economic Aid Corporation and another 11 D.L.R. (1959) 459.

5 Buckley on the Companies Act 13th Ed. p. 617.

6 Re Houghton Main Colliery Co. Ltd [1956] 3 All ER 300

7 Re Birkbeck Permanent Benefit Building Society [1913] 1 Ch. 400.

8 Buckley on the Companies Act 13th Ed. p.619.

9 ibid at p. 628.

10 ibid at p. 630

11 The Liquidator, Economic Aid Corporation vs The Chandpur Mills Ltd 8 P.L.R. (Dac) 409 D.B.

The Indian Supreme Court observed that while the latter section provides for preferential payments it cannot detract from full effect being given to the earlier section providing for insolvency rules to apply and the only way in which these two sections can be reconciled is by reading them together so as to provide that whenever any creditor seeks to prove his debt against the company in liquidation, the insolvency rules should apply and only that amount which is ultimately found due from him should be recoverable from him after adjustment of mutual dealings and not that the amount due from him be recovered fully while the amount due to him from the company in liquidation should rank in payment after the preferential claims provided under the latter section.[1]

In the matter of preferential payments and claims for priority resting upon a fiduciary relationship the Companies Act merely provides that the provisions of the bankruptcy law would be observed. The question whether a deposit in a particular case can be said to be impressed with a trust will have to be decided on the basis of the terms of the agreement and the facts and circumstances of each case. If the terms of the agreement clearly indicate that the deposit was in the nature of a trust, this will be given effect to inspite of the fact that interest is provided for in the agreement or there is no provision for segregation and the recipient of the money is empowered or authorised to utilize the same in his business. If the agreement does not clearly indicate a trust, the provision for the payment of interest and the absence of any provision compelling the trustee to segregate and earmark the fund specially would lead to the inference that no such trust was created. Any other provision in the agreement relating to the way the deposit is dealt with should also be taken into account to decide whether the security deposit was impressed with a trust or not.[2]

Section 327 provides that any transfer, delivery of goods, payment, execution or other act which would, if made or done against an individual be deemed in his insolvency a fraudulent preference will be deemed to be a fraudulent preference of its creditors. This section has to be read with provisions of the Bankruptcy Act.

The burden of proof lies on the liquidator to prove the fraudulent preference.[3]

A charge created within ninety days after the commencement of the winding up shall be void unless it is proved that the company was solvent at that time.[4]

21.10.7 **Damages etc. against Delinquent Directors** – Section 331 gives the Court the power to assess damages against delinquent directors, promoter, manager or liquidator for any misfeasance, breach of trust in relation to the company. This section corresponds to section 235 of the Companies Act of 1913. This section is to be read with the power of the court to exonerate a director from any liability under section 396 and provides a remedy to the minority shareholders to hold the directors etc to account for their deeds . This section gives court the power to assess and recover damages in civil liability from delinquent directors albeit when the company has been liquidated. In an application under section 235 of the Companies Act of 1913 the impleading of a person who was the transferee account holder of a banking company was held to be proper.[5]

An auditor is responsible if he is guilty of neglect of duty or misfeasance so as to cause loss to the company.[6] The court may apportion the sums to be paid by directors.[7] A misfeasance proceeding abates on the dissolution of the company as there is then no need to augment the assets of the company.[8] The claim must relate to misfeasance or breach of trust in respect of their duties in relation to the company.[9] It provides a procedure to enforce a

1 Official Liquidator vs Smt.Lakshmikutty AIR 1981 SC 1483.
2 Seth Jessa Ram Fatehchand vs Om Narian AIR 1967 SC 1162.
3 Jayanthi Rai vs Popular Bank Ltd AIR 1966 Ker 296.
4 Section 329
5 Khondker Faizur Rahman vs The Official Liquidator 21 D.L.R. (1969)44.
6 Re Thomas Gerrard and Sons Ltd [1967] 2 All ER 525.
7 Re Morecambe Bowling Ltd [1969] 1 All ER 753.
8 In re Lewis & Smart Ltd [1954] 2 All ER 19 Ch.
9 Re Etic Ltd [1928] Ch 861.

remedy which might have been enforced by the company itself.[1] On the duty of the directors expected see the decision reported in *In re Central Calcutta Bank*[2] and *Karnataka Films Ltd vs Chitrakala Movietones Ltd.*[3] On the burden of proof see the decision of the Indian Supreme Court in Official Liquidator vs Raghava Desikachar[4] (initial burden on the liquidator shifts to directors on perusal of books and documents).

Also see *Official Liquidator vs Raghava Desikachar*[5] on the procedure for application to prove misfeasanes.[6] In *Official Liquidator vs Parthasarathi Sinha*[7] the Indian Supreme Court has held that the liquidator retains the cause of action to proceed against the delinquent director's heirs.

Section 331 has been more fully discussed in the chapter relating to directors.[8]

Section 332 provides penalty being imprisonment for a term that may extend to seven years in prison for falsification of books if a director, manager, officer or contributory of any company being wound up destroys, mutilates, alters or falsifies or fraudulently secrets any books, papers or securities or makes or is privy to the making of any false or fraudulent entry in any register, book of document of the company. Section 333 provides that in addition to this offence created the court may ask the liquidator to prosecute any person who is guilty of an offence in relation to the company for which he is criminally liable.

Section 335 creates offence for various omissions to help the liquidator or misfeasance when the company is being wound up. These offences may make the accused liable to be imprisoned for upto two or seven years. If a person within twelve months before the commencement of the winding up or at any time thereafter by any false representation or fraud obtains any property for or on behalf of the company which he does not pay or under any false pretence that the company is carrying on its business obtains any credit which the company subsequently does not pay for or if he pawns, pledges or disposes of any property of the company which has been obtained on credit and has not been paid for, may be punished with an imprisonment which may extend to seven years.

Section 340 gives power to the court to declare dissolution of a company to be void on the application of a person who appears to the court to be interested made within two years of the date of dissolution.

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1 In re City Equitable Fire Insurance Co. Ltd [1925] Ch. 407.
2 AIR 1959 Cal 625.
3 AIR 1952 Mad 481.
4 [1975] 45 Comp. Cas 136
5 AIR 1974 SC 2069
6 See Para 21.9.5 above.
7 AIR1983 SC 188
8 See Paragraphs 11.9.5, 11.9.6 above.

MISCELLANEOUS

22.1 **Power to Make Rules** – The Supreme Court may from time to time, make rules consistent with the Companies Act and with the code of Civil Procedure concerning the mode of proceeding for winding up, voluntary winding up, reduction of share capital and all applications to be made to the Court under the Act. The Rules may also provide in the matter of liquidation for holding and conducting meetings of contributories, settling list of contributories and rectifying the register of members where required, and collecting and applying the assets of the company, requiring delivery of property to the liquidator and fixing a time within which debts and claims must be proved.[1]

New Rules framed by the Supreme Court now lay stress on the practice followed in the High Court Division. As to whether the code of civil procedure will apply see *Moqbul Ahmed vs Ahmed Impex Ltd.*[2]

23.1 **Registration Office** – Section 347 provides that no company shall be registered except at an office of the Registrar within the territorial jurisdiction within which by the memorandum, the registered office of the company is deemed to be established. In Bangladesh companies may be registered with the Registrar's office in either Dhaka or Chittagong depending on their location. Any person may inspect the documents kept by the Registrar on payment of fees not exceeding described in Schedule II to the Act and any person may require a certificate of incorporation or certificate of commencement of business of any company or a copy of any other document to be certified by the Registrar on payment of such fees not exceeding the fees mentioned in the Second Schedule.[3]

Anyone who has however tried to obtain copies of any document filed at the Registrar's office will face the formidable task of convincing the Registrar's office that he is entitled to the certified copies as of any right. First, he will be told that the documents may not have been "accepted" or await acceptance or subject to scrutiny. Any attempt to convince that the applicant has a statutory right to get a certified copy of the document for all its worth will fall in deaf ears. After some 'coaxing' he may get a copy but stamped on it a seal of 'subject to scrutiny'. There is also a myth prevailing in much of the commercial sector of the city that a document has to be accepted by the Registrar's office in order to be valid. The position in law is that the Registrar has to keep in file all documents filed under the Act and is bound to give certified copies on request and payment of the prescribed copies. There is no power in the Registrar to accept or reject the documents . If he thinks that a document is forged or a resolution has not been passed correctly or that the document does not reflect the true position of the records of the company he may take steps as authorised by law but he has no authority to 'accept' or 'reject' these. His acceptance of a document does not render the validity of a document any more legal than a document which is 'subject to scrutiny' or not

1 Section 345

2 48 D.L.R.(AD)(1996) 82; also see Tahmid Ahmed vs. Jalaluddin Jafar Ali Husein 51 DLR (HC) 483 which has held that Company Court cannot review its own decision because the Original Side Rules are not in existance.

3 ibid sub-section 5

accepted. A division Bench of the High Court Division has held that the Registrar has no authority to accept or reject annual filings by a company.[1]

Section 349 enables the court to pass an order, on an application by any member or creditor of the company or the Registrar, directing the company and any officer thereof to file returns to the Registrar's office which by law the company is required to do. This, in addition to any other power to impose penalty on the company or its officers for default in filing returns. Any document which has not been filed in proper time may be filed later on payment of late fees.[2]

The author is not aware of any petition filed in the company bench to force the company to file returns. Complaints have been made about oppression of minority shareholders or that the company should be wound up because it is just and equitable to wind up the company but scarcely any petition is filed to compel the company to file returns. The Registrar's office is also non active in this . There is no computerised system in his office to warn the officers of the Registrar's office if a return is not filed.

23.2 Section 354 in Part VIII of the Act lays down the type of companies capable of being registered. Any company formed whether before or after the commencement of the Act in pursuance of any Act of Parliament other than the Companies Act or being otherwise duly constituted according to law and consisting of seven or more members may register under the Companies Act as a company with unlimited liability or with liability limited by shares or as company limited by guarantee. When a company is about to be registered as a company limited by guarantee the assent to its being so registered shall be accompanied by a resolution declaring that each member undertakes to contribute to the assets of the company, in the event of its being wound up while he is a member, or within one year afterwards, for payment of the debts and liabilities of the company contracted before he ceased to be a member and for costs etc not exceeding a certain amount. In this regard see Schedule VIII to the Act which lays down a form for companies limited by guarantee. The fifth clause contains such undertaking. In the print of the Act of 1994 it is erroneously stated that the Schedule is under sections 7 and 226. In fact these refer to the sections of the old Act.

Section 355 defines a joint stock company as a company having a permanent paid up or nominal share capital of fixed amount dividend into shares of fixed amount or held and transferable as stock or divided and held partly in one way or partly in the other and founded on the principle that only its members shall hold its shares or stock.

As Part VIII to the Act deals with companies formed initially outside the Companies Act and are rare in this country so this book will not go into details regarding such companies save that sections 354-370 deal with such companies. The principles applied are similar to companies registered under the Companies Act of 1994.

24.1 **Unregistered Companies** – Part IX of the Act deals with unregistered companies. Section 371 provides that the expression 'unregistered company' shall not include a company registered as a company under the Companies Act or any other company law but shall include any partnership or association consisting of more than seven members. Section 372 contains provisions for winding up of such unregistered companies. No such company may be wound up voluntarily or subject to supervision of the court. Such a company may be wound up if it is unable to pay its debts. Section 374 provides that the provisions of the Act with respect to staying and restraining suits and legal proceedings against a company at any time after the presentation of a petition for winding up and before the making up of the winding up order shall, in the case of an unregistered company, where the application to stay or restrain is by a creditor, extend to suits and legal proceedings against any contributory of the company.

Section 375 provides that where an order has been made for winding up of a company under this Part no suit or legal proceeding shall be proceeded with or commenced against any

1 BCIC vs Registrar 39 D.L.R.(HC)1.

2 Section 350

contributory of the company in respect of any debt of the company except by leave of the court and subject to such terms as the court may impose.

The Dacca High Court has observed that section 270 of the old Act of 1913 defined the term "unregistered company". 'The second part of the section does not specify what bodies will come within the term "unregistered company" but some particular categories of bodies would be included within the term...it is therefore clear that other partnerships, associations or companies may be included within the meaning of "unregistered company"... therefore, "company" in this section can only mean and must mean a body which has no corporate existence not being registered under the Act.'[1]

Section 377 provides that an unregistered company shall not, except in the event of its being wound up, be deemed to be a company under this Act and then only to the extent provided by Part IX. This provision should not be interpreted narrowly and a scheme for reconstruction will be applicable to shareholders of a company which has its head office in Calcutta but assets here.[2]

25.1.1 **Foreign Companies** – Sections 378-387 deal with foreign companies. These are broadly foreign companies which were carrying on business at the time of commencement of the Act and those which established place of business in Bangladesh after the commencement of the Act.

Section 379 provides that foreign companies which establish a place of business within Bangladesh shall, within one month of the establishment of the place of business deliver to the Registrar for registration –

a) a certified copy of the charter or statutes or memorandum or articles of the company; there should be an English or Bengali version of it in case the language of the charter is not in English.

b) the full address of the registered office of the company;

c) the name and address of persons resident in Bangladesh who are authorised to accept on behalf of the company service of process to be served on the company.[3]

A foreign company shall have to file with the Registrar any particulars of any change of the above information.[4]

Accounts of Foreign Company – Section 380 requires a foreign company to make out a balance sheet and profit and loss account and if the company is a holding company , group accounts in such a form and containing such particulars as necessary for a local company to lay the accounts in a general meeting and deliver three copies of it at the Registrar's office. The Government has power to exempt or allow a foreign company from filing these particulars with such modifications as contained in the notification. Any document not already in English must be translated in English.

Raising of Capital by a Foreign Company – If a foreign company issues a prospectus in Bangladesh then the document shall state the country in which the company is incorporated and publish certain other particulars.[5] It shall not be lawful for any person to issue, circulate or distribute in Bangladesh any prospectus offering to the public for subscription to shares in or debentures of a company incorporated or to be incorporated outside Bangladesh unless before the issue, circulation or distribution of the prospectus in Bangladesh a copy thereof, certified by the Chairman and two other directors of the company as having been approved by a resolution of the managing body, has been delivered to the Registrar for registration. The prospectus should otherwise comply with the requirements of Part X of the Act (e.g.

1 Tobacco Company vs Employers Association 25 DLR (1973) 270,272.
2 In the matter of the Noakhali Union Bank Ltd. 2 DLR (1949) 181
3 Section 379 (1)
4 ibid subsection(3).
5 Section 381

contain the particulars to be given as required by section 389) and should be dated and state on the face of it that the copy has been so delivered to the Registrar. However, because of the foreign exchange restrictions the prospect of a foreign company raising capital is not too likely in this country at the present time.

It shall be an offence if any person goes from house to house of the public offering shares of a company incorporated outside Bangladesh for subscription to or sale of such shares.[1]

Service of Notice on foreign company – A notice may be served on a foreign company by effecting the notice on the person authorised to receive it as per the returns filed with the Registrar under section 379. If the foreign company has not intimated the Registrar about the authorised persons or if they are dead or have ceased to have such authority or refuse to accept it then service may be effected by serving the same the company by leaving it at or by sending it by post to any place of business established by the company in Bangladesh.[2]

Notice of ceasing place of business of a company – If any foreign company ceases to have a place of business in Bangladesh then it shall promptly file with the Registrar a notice to that effect and all its obligations to file any return will cease from that day.[3]

Failure to Comply with Requirements – Any foreign company which fails to comply with the requirements of law required to be filed under Part X of the Act (sections 378 - 392) shall be punishable with fine which may extend to Taka One Thousand and a fine of Taka Five Hundred for each day the offence continues.[4]

The liability of a foreign company under any contract will however be not affected if the foreign company does not comply with the provisions of this Part.[5]

The fees for registering a document by a foreign company shall be as laid down in Schedule II to the Companies Act.[6]

Charges and Receivers etc – The provisions of sections 159-168 and 171-176 shall apply to charges created by a foreign company on property in Bangladesh. Section 391(1).

Section 392 provides that if a Receiver is appointed then the company shall comply with the provisions of Sections 169 and 170. It is not clear however how this provision will be enforced in case the foreign company goes into liquidation in the home country. In this connection see the observations of Megarry J. in *In Re Compania Merabello San Nicholas S.A.*[7] and the discussions in *Re Alloborgia Steamship Corporation;*[8] *Re Eloc Electro-Optieck and Communicatie B.V.*[9]

Whether a restriction in the nature of a Mareva Injunction will issue restraining the company from parting with its assets here pending trial will depend on the facts of each case and the courts may issue such an injunction.[10]

25.1.2 **Establishing a Place of Business** – Buckley cites a Scottish case to comment that a company incorporated outside the country which employs agents within the country but has no office in the country has no place of business with the meaning of the Act.[11]

If however the company has a specified or identifiable place of business here like an office or storehouse or godown then it may be having a place of business here.[12]

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1 Section 390.
2 Section 382.
3 Section 383.
4 Section 384.
5 Section 385. Also see Curragh Investments Ltd vs Cook [1974] 3 All ER 658 Ch.D.
6 Section 386.
7 [1972] 3 All ER 448.
8 [1978] 3 All ER 423.
9 [1981] 2 All ER 1111 Ch.D.; International Westminster Bank plc vs Okeanos Maritime Corpn [1987] BCLC 450 Ch.D.
10 Third Chandris Shipping vs Unimarine [1979] 2 All ER 972 CA.
11 Lord Advocate vs Huron and Erie Loan and Saving Co, 1911 S.C. 612 -Buckley's Companies Act 14th Ed. p.857.
12 Deverall vs Grant Advertising Inc. [1954] 3 All ER 389.

Having a share transfer or share registration office will constitute having a place of business in the country.[1]

If the representative of a foreign company were often coming and staying in a hotel in this country for purchasing machinery, cotton etc., will that constitute having a place of business here? Maybe, if an English decision is relied upon.[2] The American law exempts certain activities from creating a place of business, e.g., maintaining or defending any suit or action, holding meeting of shareholders or directors, maintaining bank accounts or offices for transferring or registering shares, effecting sales through independent contractors, creating evidence of debts, charges on real or personal property or securing or collecting debts or enforcing claims to property of any kind.[3] As to the meaning of "established place of business" the discussions in *Re Oriel Ltd*[4] may be referred to where the fact that the directors had a place of business was not found to be enough to hold that the foreign company had a place of business in the country.

The company must have a degree of continuity and recognisability with respect to its business activities before it will be treated as possessing an established place of business. The test is whether there is some specific location which can be identified as being a place where business of the company is carried on.[5]

The nationality of the corporators constituting the company are irrelevant. It is the place of incorporation that decides the status for the purpose of enforcing the requirements of Part X.[6]

In view of the fact that Bangladesh is an emerging country and urgently needs foreign collaboration it is important that the Government should exercise its discretion while enforcing the provisions of Part X to foreign companies. The sight of foreign companies' representatives regularly crowding the hotels of Dhaka and Chittagong for procuring the contracts in connection with garments manufacturing are common and if the authorities are to enforce the law too rigidly it will only amount to negative interference with foreign investments.

26.1.1 **Legal Proceedings, Offences etc** – Sections 393-400 of the Act contains provisions relating to proceedings and offences under the Companies Act.

Cognizance of Offence – Section 393 (1) provides that no court inferior to that of a Magistrate of the first class shall try any offence under the Companies Act . Every offence under this Act shall be deemed to be non-cognizable under the Code of Criminal Procedure and where the complainant is the Registrar, as in the case of majority of the prosecutions will be, the personal attendance of the complainant before the court trying the offence shall not be necessary.[7]

Security – Where a limited company is the plaintiff or petitioner in any suit or other legal proceeding any court having jurisdiction in the matter may if it appears that the company may not be able to pay costs of the litigation if the defence is successful may require the company to pay sufficient security for costs and may stay proceedings until the cost is paid.[8]

Power of Court to Grant Relief – If a director, manager, managing agent, officer or auditor of a company is being sued for negligence, default, breach of duty or breach of trust then if

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1 Section 387(c); also see Employer's Liability Assurance Corporation vs Sedgwick, Collins and Co [1927] A.C. 95; The Madrid [1937] 1 All ER 216.

2 T. Manufactur Liudvig Rabenewk [1944] 2 All ER 556 Ch.

3 Harry Henn on Law of Corporations p.165

4 [1985] 3 All ER 216.

5 South India Shipping Corpn Ltd vs The Export-Import Bank of Korea [1985] 2 All ER 219.

6 Gramaphone and Typewriter Ltd vs Stanley [1908] 2 K.B.89; Att. General vs Jewish Colonial Association [1901] 1 K.B.123.

7 Section 393(2)

8 Section 395

the Court hearing the case is of the opinion that such person may be liable for any of the said reasons but that he has acted honestly and reasonably and having regard to all the circumstances of the case ought fairly to be excused then the court may relieve him either wholly or partly from his liability on such terms as the court thinks fit.[1]

Where such a person has reason to apprehend that any claim will or might be made against him in respect of any negligence, default , breach of duty or breach of trust he may apply to the court for relief and the court shall have the same power to grant relief as if it was trying the case against him.[2]

It is clear therefore that once a prosecution or action has started only the court trying the case will have jurisdiction to give relief; however if a prosecution or action has not yet been commenced then the Court, meaning the Company Bench of the High Court Division has the jurisdiction to grant relief. This is because sub-section (2) of section 396 speaks of the "Court" meaning the High Court Division under section 3 of the Act. Once the prosecution or proceeding has started the High Court has no jurisdiction in its original statutory jurisdiction to grant relief.[3] The decision in *Anwar Jute Baling Ltd*[4] on the power of the Court to exonerate delay in filing documents may be referred to.

In most of the applications in the Company Bench of the High Court Division one of prayers is to condone the delay in filing a return to the Registrar or for not doing a compulsory act like holding the annual general meeting. This is the section the court should resort to in condoning the delay, for sub-section (2) envisages just this kind of prayer when it gives the court the power to give relief when someone apprehends that an action or proceeding may be taken against him. The application for holding the annual general meeting out of time, if it contains a prayer for condoning the delay in holding past meetings should also mention that the applicant seeks remedy also under this section.

For an exhaustive discussion of the case law on the power, jurisdiction of the court and the manner in which it is exercised see the discussion in connection with the liability of directors in Section 11.9.7 above.

Section 397 provides that whoever in any return , report, certificate, balance sheet or other documents required or for the purposes of any of the provisions of the Companies Act wilfully makes a false statement in any material particular knowing it to be false shall be punishable with imprisonment of either description for a term which may extend to five years as well as fine. The fine referred to in this section means the fine provided in different sections of the Act for not complying with its provisions.

The House of Lords has held that in the case of a statutory offence the mens rea is not material as moral guilt is not the essence of such offence.[5] The language of the section however would indicate that the offender should have some sort of criminal intention because of the retention of the word 'wilfully' in the Act of 1994. Please note that in India the draftsman has done away with the word 'wilfully'. No show cause notice is needed to be given by the Registrar before initiating a proceeding under this section. [6]

Wrongful Withholding of Property – Section 398 provides that any director, manager, managing agent or other officer or employee of the company who wrongfully obtains possession of any property of a company or having any such property in his possession wrongfully withholds it or wilfully applies it to any purpose not permitted by the articles or the Act is punishable with a fine not exceeding five thousand taka; and the court trying the offence may ask the offender to give back the property within a certain time and if he does not do so he is liable to suffer imprisonment for a period not exceeding two years. The complainant in such a case may be the company, a creditor or a contributory.

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1 Section 396 (1)

2 ibid sub-section (2).

3 In the matter of Elahee Baksh and Company Ltd PLD (1958) Dac 378; (1958) 10 DLR 179.

4 21 (1969) DLR Dac 413

5 Warner vs Metropolitan Poilice Commissioner [1968] 2 All E.R. 356 HL

6 K.S.Narasimhachari vs Registrar [1958] 28 Comp. Cas 106 Mad.

The Indian Act has substituted the word 'wilfully' for 'knowingly' thus implying that the offence is completed if the offender has knowledge of the retention of the property.

Legal sanction is necessary for the offender to show that his possession of the property does not constitute an offence under this section. The section applies only where there is no bonafide dispute that the property withheld is the property of the company.[1]

After some difference between the different High Courts in India it was held by the Indian Supreme Court that the section applies to both past and present employees.[2]

Application of Securities – Section 399 provides how monies belonging to employees should be kept . These should be in a scheduled bank. Monies belonging to Provident Fund of employees shall be deposited either in a Post Office Savings Bank Account or invested in the securities mentioned or referred to in clauses (a) to (e) of section 20 of the Trusts Act.

Improper Use of the Word 'Limited' – Section 400 provides that if any person uses the word 'limited' while carrying on trade or business in the name and title of that business then he shall be liable to a fine of taka Five Hundred for each day the offence continues. Note that this section creates an offence for a person to improperly use the word 'limited' whereas section 78 obliges a company whose members' liability is limited to the shares taken by them to publish the word limited on pain of a civil liability for the officers failing to do so of repaying the debts of the company personally.

General Clauses Act to Apply – Section 403 mentions that section 6 of the General Clauses Act shall apply to the interpretation of the Act. The Supreme Court of India has held that this means that section 6 of that Act will apply subject to the provisions regarding repeals and savings etc. in section 402 of the Companies Act.[3]

English and Bengali Text – Section 404 specifically provides that there shall be an authentic English text of the Act but that in case of a conflict the Bengali version shall prevail. There has been a number of printing and careless mistakes in the English version and in such an event a reference to the Bengali version is helpful.

1 Damodar Das Jain vs Krishna Charan Chakraborty and another [1985] 57 Comp. Cas 115 (Bom).
2 Baldev Krishna Sahi vs Shipping Corporation of India Ltd [1988] 63 Comp. Cas 1 (SC).
3 Raj Narayan Bansilal vs Maneck Phiroz Mistry AIR 1961 SC 29; Maharashtra Sugar Syndicate Ltd vs Janardan Ramchandra Kulkarni AIR 1960 SC 794.