CHEMBRA ORCHARD PRODUCE LTD. & ORS. A

v.

REGIONAL DIRECTOR OF COMPANY AFFAIRS & ANR.

(Civil Appeal Nos. 7115-7120 of 2008)

DECEMBER 4, 2008 B

[S.H. KAPADIA AND AFTAB ALAM, JJ.]

COMPANIES ACT, 1956:

s. 391(1) – Application seeking directions to convene a C
meeting of creditors and members to consider Scheme of amalgamation – Ex-parte hearing of -Propriety of – HELD: Application for an order for meeting is a preliminary step at the threshold stage whereat it is not necessary for company to give notice of hearing to the creditors, members and D
shareholders – When r.67 categorically states that summons for directions shall be moved ex-parte, the question of prejudice or rule of natural justice does not come into play – However, while issuing such summons Court is required to apply its mind to check list indicated in r.69 and it needs to E
be **prima facie** *satisfied about genuineness and* **bona fides** *of application – After summons for directions are issued, when meeting is ordered to be convened, requirements of rr. 73, 74 and 76 are to be complied with – Companies (Court) Rules, 1959 – rr. 67 and 69 – Natural justice – Opportunity* F
of hearing.

Miheer H. Mafatlal v. Mafatlal Industries Ltd. **1997 (1) SCC 579, relied on.**.

Sakamari Steel & Alloys Ltd. In re.: **51 Company Cases** G
page 266, approved.

Hind Auto Indo Ltd. v. M/s Premier Motors (P) Ltd. **AIR 1970 Allahabad 165, distinguished.**

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A *Palmer's Company Law,* **referred to.**

Case Law Reference:

1997 (1) SCC 579	**relied on**	**para 8**
B **51 Company Cases page 266**	**approved**	**para 9**
AIR 1970 Allahabad 165	**distinguished**	**para 11**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 7115-7120 of 2008.

C From the Judgment and Order dated 20.8.2007 of the High Court of Karnataka at Bangalore in C.A. Nos. 354 to 359 of 2003.

Shyam Divan, Shamik Sanjawala, Srinivasa Raghavan D and Meenakshi Arora for the Appellants.

The following Order of the Court was delivered:

ORDER

E 1. Leave granted.

2. The short question which arises for determination in these Civil Appeals is whether an application filed by the Company under Section 391(1) of the Companies Act, 1956 F (for short the '1956 Act') seeking directions to convene a meeting of creditors and members to consider a scheme of amalgamation is required to be heard and decided ex-parte as per Rule 67 of the Companies (Court) Rules, 1959?

3. To answer the above question we need to quote G hereinbelow the relevant Rules.

"Rule 2(9) 'Judge's summons' means a summons returnable before the Judge in Chambers or in Court.

H ...

67. Summons for directions to convene a meeting.- An application under section 391(1) for an order convening a meeting of creditors and/ or members or any class of them shall be by a Judge's summons supported by an affidavit. A copy of the proposed compromise or arrangement shall be annexed to the affidavit as an exhibit thereto. Save as provided in rule 68 hereunder, the summons shall be moved ex parte. The summons shall be in Form No. 33, and the affidavit in support thereof in Form No. 34.

68. Service on company- Where the company is not the applicant, a copy of the summons and of the affidavit shall be served on the company, or, where the company is being wound-up, on its liquidator, not less than 14 days before the date fixed for the hearing of the summons.

69. Directions at hearing of summons.- Upon the hearing of the summons or any adjourned hearing thereof, the Judge shall, unless he thinks fit for any reason to dismiss the summons, give such directions as he may think necessary in respect of the following matters: -

(1) determining the class or classes of creditors and/or of members whose meeting or meetings have to be held for considering the proposed compromise or arrangement;

(2) fixing the time and place of such meeting or meetings;

(3) appointing a chairman or chairmen for the meeting or meetings to be held, as the case may be;

(4) fixing the quorum and the procedure to be followed at the meeting or meetings, including voting by proxy;

(5) determining the values of the creditors and/or

A the members, or the creditors or members of any class, as the case may be, whose meetings have to be held;

(6) notice to be given of the meeting or meetings and the advertisement of such notice;

B

(7) the time within which the Chairman of the meeting is to report to the Court the result of the meeting; and such other matters as the Court may deem necessary.

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The order made on the summons shall be in Form No. 35 with such variations as may be necessary."

...

D *73. Notice of meeting.*- The notice of the meeting to be given to the creditors and/or members, or to the creditors or members of any class, as the case may be, shall be in Form No. 36, and shall be sent to them individually by the Chairman appointed for the meeting, or, if the Court so E directs, by the company (or its Liquidator), or any other person as the Court may direct, by post under certificate of posting to their last known address not less than 21 clear days before the date fixed for the meeting. It shall be accompanied by a copy of the proposed compromise or F arrangement and of the statement required to be furnished under section 393, and a form of proxy in Form No. 37.

74. Advertisement of the notice of meeting.- The notice of the meeting shall be advertised in such newspapers and in such manner as the Judge may direct, not less than 21 G clear days before the date fixed for the meeting. The advertisement shall be in Form No. 38.

75. Copy of compromise or arrangement to be furnished by the company.- Every creditor or member entitled to H attend the meeting shall be furnished by the company, free

of charge and within 24 hours of a requisition being made for the same, with a copy of the proposed compromise or arrangement together with a copy of the statement required to be furnished under section 393, unless the same had been already furnished to such member or creditor.

76. Affidavit of service.- The Chairman appointed for the meeting or the Company or other person directed to issue the advertisement and the notices of the meeting shall file an affidavit not less than 7 days before the date fixed for the holding of the meeting or the holding of the first of the meetings, as the case may be, showing that the directions regarding the issue of notices and the advertisement have been duly complied with. In default thereof, the summons shall be posted before the Judge for such orders as he may think fit to make.

...

79. Petition for confirming compromise or arrangement.- Where the proposed compromise or arrangement is agreed to, with or without modification, as provided by sub-section (2) of section 391, the company, (or its Liquidator, as the case may be), shall, within 7 days of the filing of the report by the Chairman, present a petition to the Court for confirmation of the compromise or arrangement. The petition shall be in Form No. 40.

Where a compromise or arrangement is proposed for the purposes of or in connection with a scheme for the reconstruction of any company or companies, or for the amalgamation of any two or more companies, the petition shall pray for appropriate orders and directions under section 394.

Where the company fails to present the petition for confirmation of the compromise or arrangement as

aforesaid, it shall be open to any creditor or contributory as the case may be, with the leave of the Court, to present the petition and the Company shall be liable for the costs thereof.

Where no petition for confirmation of the compromise or arrangement is presented, or where the compromise or arrangement has not been approved by the requisite majority under section 391(2) and consequently no petition for confirmation could be presented, the report of the Chairman as to the result of the meeting made under the preceding rule shall be placed for consideration before the Judge for such orders as may be necessary.

80. Date and notice of hearing.- The Court shall fix a date for the hearing of the petition, and notice of the hearing shall be advertised in the same papers in which the notice of the meeting was advertised, or in such other papers as the Court may direct, not less than 10 days before the date fixed for the hearing."

We also quote hereinbelow Form No.33 and Form No.34:-

FORM NO. 33
[See Rule 67]
[Heading as in Form No. 1]
Company Application No. ..... of 19.....
..... Applicant(s)

Summons for Directions to Convene a Meeting under section 391

Let all parties concerned attend the Judge in Chambers on ..:..,..... day, the.....day of ..... 19... at ..... o'clock in the ..... noon on the hearing of an application of the abovenamed company (or of the applicant(s) abovenamed) for an order (that a meeting (or separate meetings) be held at ..... of (Here enter the creditors or class of creditors, e.g., debenture-holders,

other secured creditors, unsecured creditors, etc., or the members or class of members, e.g., preference shareholders, equity shareholders, etc. of which class or classes, the meeting have to be held) of the above company, for the purpose of considering, and if thought fit, approving, with or without modification, a scheme of compromise or arrangement proposed to be made between the company and the said [here mention the creditors or class of creditors or members, or the class of members] of the said company.

And that directions may be given as to the method of convening, holding and conducting the said meeting(s) and as to the notices and advertisements to be issued.

And that a chairman (or chairmen) may be appointed of the said meeting(s), who shall report the result there of to the Court.

Advocate for the applicant(s)
Registrar.

The affidavit of..... will be used in support of the summons.

[Note:--Where the company is not the applicant, the summons should be served on the company, or, where it is being wound-up, on its liquidator.]"

"FORM NO. 34
[See Rule 67]
[Heading as in Form No. 1]
Company Application No. ..... of 19.....
..... Applicant(s).

Affidavit in Support of Summons

I, ... of etc., solemnly affirm and say as follows :--

1. I am the managing director/secretary/director/ ..../of the said company, (or an auditor of the said

company authorised by the directors to make this affidavit/ or liquidator of the said company in liquidation).

[Where the application is not by the company or its liquidator, but by a member or creditor the above paragraph should be suitably altered.]

2. The company was incorporated on ..... 19..... The document now produced and shown to me is a printed copy of the memorandum, and articles of association of the said company, and also contains copies of all the special resolutions which have been passed and are now in force.

3. The registered office of the company is situated at.....

4. The capital of the company is Rs. ..... divided into ..... (here set out the classes of shares issued and the amounts paid up on each share).

5. The objects of the company are set out in the memorandum of association annexed hereto. They are briefly (here set out the main objects in brief).

6. The company commenced the business of..... (e.g., hides and skins, etc.) and has been carrying on the same since.....

7. [Here set out in separate paragraphs the circumstances that have necessitated the proposed compromise or arrangement, the objects sought to be achieved by it, the terms of the compromise or arrangement, and the effect if any, of the compromise or arrangement on the material interests of the directors, managing director, managing agent, secretaries and treasurers or the manager of the company, and where the compromise or arrangement affects the interests of the debenture holders, its effect on the material interests of the

trustees of the debenture trust deed. A copy of the proposed compromise or arrangement should be marked as an exhibit and annexed to the affidavit]. A

8. [Here set out the class of creditors or members with whom the compromise or arrangement is to be made; where the arrangement is between the company and its members, it should be stated whether any creditors or class of creditors are likely to be affected by it.] B

9. It is necessary that a meeting (or meetings) of the creditors/members (if the meeting is to be only of a class of creditors or a class of members, it should be so stated) should be called to consider and approve the proposed compromise or arrangement. C

10. It is suggested that the meeting (or meetings) may be held at the premises of the registered office of the company or at such other place as may be determined by the Court, and on such date(s) and at such time(s) as this Court may direct; and that a chairman may be appointed for the meeting (or for each of the meetings) to be held. D E

11. It is suggested that notice of the proposed compromise or arrangement and of the meeting may be published once in (here set out the newspapers) and in such other manner as the Court may direct.

F

12. It is prayed that necessary directions may be given as to the issue and publication of notices and the convening, holding and conducting of the meeting(s) proposed above.

G

Solemnly affirmed, etc.

(Sd.) X.Y.
Before me
(Sd.).....
Commissioner for Oaths". H

4. The appellant -Company moved Company Application Nos. 354 to 359 of 2003 before the Karnataka High Court on 17th April, 2003 under Sections 391 to 394 of the Companies Act, 1956 in the form of Judge's Summons for Directions supported by an affidavit to hold a meeting of shareholders and members to consider the proposed scheme of amalgamation. The applications were filed stating that the applicant had entered into the said Scheme under which it was proposed to amalgamate appellant Nos. 1 to 5 into the 6th appellant – Company. This proposed Scheme of Amalgamation was in fact approved by the Board of Directors vide Resolution dated 15th February, 2003 stating that the amalgamation would result in economy of scale. In accordance with Rule 67, Judge's Summons for Directions regarding holding of meetings was moved ex-parte.

5. When the Company Application regarding holding of meeting came before the Company Judge on 15th March, 2004, a query was raised as to whether it was not necessary to hear the share-holders and creditors before issuing directions for holding meeting of share-holders and creditors. Appellant contended that Rule 67, quoted above, did not contemplate the hearing of any person, including share-holders and creditors, before issuing directions for holding of meetings.

6. By impugned judgment dated August 20, 2007, the Division Bench of the Karnataka High Court on reference answered the above question of law stating that hearing of all parties was necessary before the Company Court could issue directions to convene a meeting under Section 391(1) of the Companies Act and that an ex-parte order in that connection could not be passed. It is this order which is under challenge.

7. At the outset, it may be stated that the Companies (Court) Rules, 1959 are enacted in exercise of the powers conferred by Section 643(1)(2) of the Companies Act, 1956. They have force of an Act passed by the Parliament. The said Rules 1959 have statutory force of law. The said Rule 67 in

unequivocal terms states that an application under Section 391(1) for an order for convening a meeting of creditors and/ or members or any class of them shall be by a Judge's Summons supported by an affidavit. Rule 67 further requires the proposed compromise or arrangement to be annexed to the affidavit as an exhibit. Rule 67 is, however, subject to Rule 68 (which deals with a case where the Company is not the applicant). If one reads Rule 67 with Form 33 and Form 34, one find that essentially the Court while issuing such summons is required to apply its mind to checklist indicated in Rule 69 and it needs to be prima facie satisfied about the genuineness and bonafides of the application. One aspect needs to be highlighted. Hearing of the Motion ex-parte does not mean that the Court had not to apply its mind or that the Court is not required prima facie to be satisfied about the genuineness or bonafides. However, it is a preliminary step. One more aspect needs to be mentioned. If hearing is required to be given to contributors, creditors and share-holders, then the entire scheme of Section 391 (which is a Code by itself) would become unworkable. Further, when Rule 67 categorically states that Summons for Directions shall be moved ex-parte, the question of prejudice or rule of natural justice does not come into play. However, there is a rationale for stating that the Summons shall be moved ex-parte and that rationale is that it is an Application for an Order for Meeting as a preliminary step at the threshold stage and at that stage it is not necessary for the Company to give notice of hearing to the creditors, members and share-holders (see: Palmer's Company Law). Further, if one examines Rule 67 in the context of Rule 73, one finds that after Summons for Direction are issued as and when the meeting is ordered to be convened, the notice of the meeting is required to be given to the creditors and/or members or such other classes enumerated in Rule 73. Similarly, under Rule 74 advertisement of the notice of meeting is also required to be published in such newspapers and in such manner as the Judge may direct. This is to be supported by affidavit of service under Rule 76.

A 8. The analysis of the above Rules indicates that there is a clear dichotomy between the threshold stage of issuance of directions to convene a meeting and the subsequent stage of a notice of meeting which is contemplated by Rule 73 and for that precise reason Rule 67 states that the summons shall be B moved *ex-parte*.

9. Our view is supported by various judgments of this Court and the High Courts. As far as the scheme of Sections 391 to 394 of the Companies Act is concerned, we quote hereinbelow Paragraph 28 of the judgment of this Court in the case of C *Miheer H. Mafatlal v. Mafatlal Industries Ltd.* reported in 1997 (1) SCC 579:

"28. The relevant provisions of the Companies Act, 1956 are found in Chapter V of Part VI dealing with D "Arbitration, Compromises, Arrangements and Reconstructions". In the present proceedings we will be concerned with Sections 391 and 393 of the Act. The relevant provisions thereof read as under:

E "391. (1) Where a compromise or arrangement is proposed-

(a between a company and its creditors or any class of them; or

F (b) between a company and its members or any class of them; the Court may, on the application of the company or of any creditor or member of the company, or in the case of a company which is being wound up, of the G liquidator, order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Court directs.

H (2) If a majority in number representing three-fourths

in value of the creditors, or class of creditors, or members, or class of members as the case may be, present and voting either in person or, where proxies are allowed under the rules made under Section 643, by proxy, at the meeting, agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the Court, be binding on all the creditors, all the creditors of the class, all the members, or all the members of the class, as the case may be, and also on the company, or, in the case of a company which is being wound up, on the liquidator and contributories of the company:

Provided that no order sanctioning any compromise or arrangement shall be made by the Court unless the Court is satisfied that the company or any other person by whom an application has been made under sub-section (1) has disclosed to the Court, by affidavit or otherwise, all material facts relating to the company, such as the latest financial position of the company, the latest auditor's report on the accounts of the company, the pendency of any investigation proceedings in relation to the company under Sections 235 to 251, and the like.

...

393. (1) Where a meeting of creditors or any class of creditors, or of members or any class of members, is called under Section 391,-

(a) with every notice calling the meeting which is sent to a creditor or member, there shall be sent also a statement setting forth the terms of the compromise or arrangement and explaining its effect, and in particular, stating any material interests of the directors, managing directors, managing agents, secretaries and treasurers or manager of the company, whether in their capacity as such

A or as members or creditors of the company or otherwise, and the effect on those interests, of the compromise or arrangement, if, and insofar as, it is different from the effect on the like interests of other persons; and

B *(b)* in every notice calling the meeting which is given by advertisement, there shall be included either such a statement as aforesaid or a notification of the place at which and the manner in which creditors or members entitled to attend the meeting may obtain copies of such a statement as aforesaid.

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The aforesaid provisions of the Act show that compromise or arrangement can be proposed between a company and its creditors or any class of them or between a company and its members or any class of them. Such a D compromise would also take in its sweep any scheme of amalgamation/merger of one company with another. When such a scheme is put forward by a company for the sanction of the Court in the first instance the Court has to direct holding of meetings of creditors or class of creditors E or members or class of members who are concerned with such a scheme and once the majority in number representing three-fourths in value of creditors or class of creditors or members or class of members, as the case may be, present or voting either in person or by proxy at F such a meeting accord their approval to any compromise or arrangement thus put to vote, and once such compromise is sanctioned by the Court, it would be binding to all creditors or class of creditors or members or class of members, as the case may be, which would also necessarily mean that even to dissenting creditors or G class of creditors or dissenting members or class of members such sanctioned scheme would remain binding. Before sanctioning such a scheme even though approved by a majority of the concerned creditors or members the Court has to be satisfied that the company or any other

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person moving such an application for sanction under sub-section (2) of Section 391 has disclosed all the relevant matters mentioned in the proviso to sub-section (2) of that section. So far as the meetings of the creditors or members, or their respective classes for whom the Scheme is proposed are concerned, it is enjoined by Section 391(1)(a) that the requisite information as contemplated by the said provision is also required to be placed for consideration of the voters concerned so that the parties concerned before whom the scheme is placed for voting can take an informed and objective decision whether to vote for the scheme or against it. On a conjoint reading of the relevant provisions of Sections 391 and 393 it becomes at once clear that the Company Court which is called upon to sanction such a scheme has not merely to go by the ipse dixit of the majority of the shareholders or creditors or their respective classes who might have voted in favour of the scheme by requisite majority but the Court has to consider the pros and cons of the scheme with a view to finding out whether the scheme is fair, just and reasonable and is not contrary to any provisions of law and it does not violate any public policy. This is implicit in the very concept of compromise or arrangement which is required to receive the imprimatur of a court of law. No court of law would ever countenance any scheme of compromise or arrangement arrived at between the parties and which might be supported by the requisite majority if the Court finds that it is an unconscionable or an illegal scheme or is otherwise unfair or unjust to the class of shareholders or creditors for whom it is meant. Consequently it cannot be said that a Company Court before whom an application is moved for sanctioning such a scheme which might have got the requisite majority support of the creditors or members or any class of them for whom the scheme is mooted by the company concerned, has to act merely as a rubber stamp and must almost automatically put its seal of approval on such a scheme. It is trite to say that once

A the scheme gets sanctioned by the Court it would bind even the dissenting minority shareholders or creditors. Therefore, the fairness of the scheme qua them also has to be kept in view by the Company Court while putting its seal of approval on the scheme concerned placed for its B sanction. It is, of course, true that so far as the Company Court is concerned as per the statutory provisions of Sections 391 and 393 of the Act the question of voidability of the scheme will have to be judged subject to the rider that a scheme sanctioned by majority will remain binding C to a dissenting minority of creditors or members, as the case may be, even though they have not consented to such a scheme and to that extent absence of their consent will have no effect on the scheme. It can be postulated that even in case of such a scheme of compromise and arrangement put up for sanction of a Company Court it will D have to be seen whether the proposed scheme is lawful and just and fair to the whole class of creditors or members including the dissenting minority to whom it is offered for approval and which has been approved by such class of persons with requisite majority vote."

E

10. In the case of *Sakamari Steel & Alloys Ltd.* reported in 51 Company Cases page 266, the learned Single Judge of the Bombay High Court held that Section 391(1) is not a sign-post but a check-post whereat it is a duty of the Court to F examine the genuineness and the bonafides of the Scheme for itself.

11. A reading of the above judgment would, therefore, show that at the stage of issuance of Summons for Directions to convene a meeting, though the Company Judge has to apply G its mind, prima facie, on the genuineness of the Scheme, basically the entire exercise is to verify whether the numerous conditions prescribed in Rule 69 are satisfied read with Form 33 and Form 34.

H 12. In the impugned judgment, reliance is placed on the

earlier judgment of the Allahabad High Court in the case of *Hind Auto Indo Ltd. v. M/s Premier Motors (P) Ltd.* reported in AIR 1970 Allahabad 165. From a bare reading of that judgment we find that the said case related to interpretation of Section 394A of the Companies Act with which we are not concerned in this case. Be that as it may, there are observations in the said judgment, with respect, with which we do not agree, both on the interpretation of Rule 67 and 69 on one hand as also on the basis of the practical effect of the interpretation given by the High Court in the present case. If at the threshold stage of directions to convene a meeting hearing is required to be given to the members as held in the impugned judgment the scheme of the Companies (Court) Rules 1959 will become unworkable. For the above reasons, with respect, we disagree with the view expressed by the Allahabad High Court in the case of *Hind Auto Indo Ltd.* (supra) and we agree with the judgment of the Bombay High Court in the case of *Sakamari Steel & Alloys Ltd.* (supra).

13. For the aforestated reasons, we allow these civil appeals. Consequently, the impugned judgment is set aside with no order as to costs.

R.P. Appeals allowed.