(1970) 12 AHC CK 0006

Allahabad High Court

Case No: Company Application No''s. 25 and 26 of 1969

Premier Motors (P.) Ltd.		APPELLANT
	Vs	
Ashok Tandon and Others		RESPONDENT

Date of Decision: Dec. 18, 1970

Acts Referred:

- Companies (Court) Rules, 1959 - Rule 79
- Companies Act, 1956 - Section 391, 391(2)
- Evidence Act, 1872 - Section 114

Citation: (1971) 41 CompCas 656

Hon'ble Judges: M.H. Beg, J

Bench: Single Bench

Advocate: S.N. Varma, for the Appellant; R.K. Gulati, J.N. Tewari, G.P. Tandon, K.S. Hajela, Suresh Pd., Ambika Pd., T.N. Sapru, Bharatji Agarwal, V.C. Misra and G. Malviya, for the Respondent

Final Decision: Dismissed

Judgement

M.H. Beg, J.

There are two connected applications before me made under Rule 79 of the Companies (Court) Rules, 1959, read with Section 391(2) of the Companies Act (hereinafter referred to as " the Act "), each for the sanction of a scheme to liquidate debts.

2. The first application is a sequel of application No. 26 of 1969 made by M/s Premier Motors (P.) Ltd. (hereinafter referred to as "the Premier Motors") u/s 391(1) of the Act for holding a meeting of its creditors who had lent money to the company under contracts for payment of 12% interest and re-payment of the principal amounts at the end of the periods contracted for. There were 710 such depositors whose deposits amounted to Rs. 33,50,000. The paid up capital of the company was Rs. 7,00,000 divided into equity shares of Rs. 100 each. It was alleged that there had

been a continuous loss for four years prior to applying u/s 391(1) of the Act, on May 16, 1967, in the company''s business of selling motor cars, trucks, buses and automobile parts on account of substantial cuts in the allotment of quotas of cars and chassis of trucks and buses, the Chinese and Pakistan aggressions, and high taxes. Therefore, the company was said to be unable to meet the demands of its depositors as and when the periods of deposits matured.

3. The second application No. 26 of 1969 under Rule 79 of the Companies (Court) Rules, results from Company Application No. 25 of 1969 made u/s 391(1) of the Act by an allied concern known as M/s Premier Credit and Motors (P.) Ltd. (hereinafter referred to us " the Credit Motors "). The grounds for the application of the Credit Motors were that there were about 711 similar depositors with various deposits amounting to Rs. 27,50,000 whose deposits could not be paid back. The fully paid up capital of the Credit Motors was Rs. 6,00,000 divided into equity shares of Rs. 100 each. The business 0f this company appears to have been to invest money, to finance merchants, to undertake " all kinds of financial and commercial operations", and, particularly, to provide credit to persons to purchase motor cars, motor lorries, motor buses, scooters, motor-cycles, coolers, tape-recorders, radios, radiograms and other similar goods on hire purchase system. The Credit Motors alleged that it had suffered a very serious loss due to an embezzlement on a large scale of rupees 14 lacs committed by one Mr. Lamba who had already been convicted by a criminal court in respect of certain charges of fraud brought by another company. Other causes of losses alleged by the Credit Motors were the abnormally high prices, high taxation, particularly after the Chinese and Pakistani wars, and the failure of customers buying trucks on a hire purchase system to make the stipulated payments. Both the companies appear to have had common sets of directors and shareholders. Both the applications u/s 391(1), made on the same date, were connected and a common order governing both the applications was passed by me on October 8, 1968, for the holding of a meeting of the unsecured creditors of each of the two companies.

4. The first term of the proposed scheme of the Premier Motors, submitted with the application u/s 391(1), was that all unsecured creditors of the company on the date of the filing of the scheme will be paid the contractual rate of interest up to the date of filing of application. But, from the date of the petition the contractual rate of interest was to cease to apply. A full and final discharge of the liability of the unsecured creditors to the extent of 60 per cent. of the amount due was promised in the following manner :

(i) 10% within three years of the sanctioning of the petition ;

(ii) 25% within one year from the date of the payment of the first installment ; and

(iii) balance of 25% within one year from the date of the payment of the second installment.

5. It was further provided that the existing board of directors will continue to function and carry on business of the company with Rs. 5,00,000 which will be set apart for carrying on business. The account of the company with respect to five lacs to be set apart was to be kept separate from the existing accounts. It was contemplated that the profits made out of future business carried on with the five lacs will not be subject to the scheme, but the creditors were to have a claim against the assets of the company, including the five lacs set apart and the profits accruing therefrom, in case 60% of the repayment of the capital assured to the unsecured creditors could not take place.

6. A briefer but similar scheme was put forward by the Credit Motors with only four terms. The second of these was that the unsecured creditors will be paid by the company 35% of the amount due in the following manner :

(a) 10% within three months of the sanctioning of the petition by this court,

(b) 12 1/2% within one year from the date of the payment of the first instalment,

(c) balance 12 1/2% within one year from the date of the payment of the second installment.

7. The fourth condition of the scheme was that the existing board of directors shall continue to function and was to be empowered to realise the outstanding dues of the company. The first and the third conditions provided that the contractual rate of interest shall cease on the date of the filing of the petition and that the scheme would not be applicable to the liabilities of the company incurred after the filing of the petition.

8. Apparently, the object of the two schemes was to get a breathing time and to provide for a definite repayment of the creditors to the extent of 60% only, in the manner indicated in the proposed scheme of the Premier Motors, and 35% of the amount due to the unsecured creditors of the Credit Motors. After that, the questions of means and mode of payment of the remainder of the amounts due were left unspecified. Presumably, the creditors were to be left to such steps as may be open to them under the law after the payment of 60% of their dues to Premier Motors and 35% of their dues to the Credit Motors. Neither of these two schemes was for the total liquidation of the debts of the unsecured creditors.

9. On November 27, 1967, however, a revised scheme of compromise was put forward on behalf of the Premier Motors, the first condition of which was that the company agreed to pay to all the unsecured creditors cent per cent. of the value of their unsecured deposits up to May 15, 1967, together with the interest at the contractual rate, and, thereafter, at the rate of 6% per annum out of the assets of the company and future profits. It was also proposed there that the company, in order to inspire confidence in the creditors and to safeguard their interests, will have three representatives of the unsecured creditors as directors on its board and

not more than two directors representing the shareholders so as to make a board of five directors. The chairman of the board of directors was to be a creditor''s director, but the executive director may be a shareholder. The object of this scheme was stated to be " to pay dues in full to the unsecured creditors as early as possible out of the assets current and in future of the company ". It was put down there that, if this court so orders, the condition relating to the new management of the company will take immediate effect so that the new management will decide, within a period of six months, the mode and manner of payment to the creditors. It was indicated that the proposals were put forward in order to distribute all the available liquid assets of the company to its creditors pro rata as and when the directors think fit. It was proposed that, if on the expiry of six months from the taking over of the management by the new board of directors, the hope of repayment of all the creditors in full is not justified, the unsecured creditors may recommend, within a reasonable period of time, the voluntary liquidation of the company, and, thereupon, the company was to be wound up and its assets distributed to the depositors pro rata. The new scheme made it clear that the directors of the Premier Motors and Credit Motors were to be the same.

10. A similar revised scheme was put forward on behalf of the Credit Motors on November 27, 1967. In this also it was provided that 100% of the value of the unsecured deposits as they stood on May 15, 1967, together with the interest and contractual rate of interest up to that date, will be paid back to the unsecured creditors, and, thereafter, interest at the rate of 6% will be paid out of the assets of the company and future profits. The other conditions were similar to the one indicated above relating to the management of the Premier Motors. It became clear that the management of the two companies was really the same. It appears that a number of depositors of the two companies are also common.

11. On 8th of October, 1968, each of the two revised schemes was ordered to be placed for consideration before a meeting of unsecured creditors, shareholders, and directors of each company to be held at Delhi under the chairmanship of Sri P. N. Pachauri, an advocate of this court, whose name had been suggested by the depositors of Lucknow. There was a tussle between the creditors of Lucknow and those of Delhi as to where the meetings were to be held. It was submitted on behalf of Lucknow creditors that the head offices of the two companies were in Lucknow, but the Delhi creditors were said to be in an overwhelming majority. Hence, meetings were fixed at Delhi, but the chairman proposed by the creditors from Lucknow was appointed to preside at and submit his reports on the meetings. It was clarified by this court that the meetings were to be of unsecured creditors, but the shareholders and directors may be present only to explain the position of the company concerned to the creditors. The directors and shareholders were to have a right of voting at the meeting only if they were unsecured creditors themselves. The voting powers were to be determined by the values of the deposits made by the creditors.

12. The chairman submitted his report on the meeting of the creditors of the Premier Motors on 24th February, 1959, showing that the scheme attached to the report was passed unanimously by the meeting of the creditors, but, when the scheme as a whole was put to vote, one Sri B. B. Chaudhari of Chandigarh, who held the proxies of depositors of the value of Rs. 40,000, had voted against the scheme and the rest voted for it. The meeting was attended either personally or by proxy by 410 depositors only representing Rs. 16,21,774 out of Rs. 33,50,000 that is, less than fifty per cent. of the total deposits. The chairman also reported that Sri P.L. Tandon, a chartered accountant of Kanpur, had placed the position of Premier Motors before the meeting on the basis of the provisional balance-sheet up to 30th November, 1968, and, as a result of information supplied to him, he assessed the realisable assets of the company at Rs, 21,00,000 (21 lacs), approximately.

13. The scheme, as passed by this meeting of the unsecured creditors of Premier Motors, revealed that the total amount payable stood at Rs. 28,39,135 after paying 5% of the principal amount to the unsecured creditors. The scheme contains a statement of the financial position of the company showing secured debts of Rs. 3,72,908.40 nP. The sales tax and Income Tax arrears of the company are shown at Rs. 6 lacs, but the amounts were said to be disputed. One of the conditions of the scheme is " that the account books held in the custody of the Central Bureau of Investigation be made available to sales tax and Income Tax departments for the proper assessment and proper determination of liabilities ". It is difficult to see how this condition could be binding upon the Central Bureau of Investigation. The fixed and current assets of the company, as shown in the balance-sheet on 30th November, 1968, are valued at Rs. 31,67,028. But, the total expected realisation from the sales of the assets is estimated at Rs. 24,88,096. It is thus clear, from the statements in the proposed scheme, as passed at the meeting of the creditors, that the company is unable to satisfy the debts of its unsecured creditors even if the company was to be wound up. Trade and current liabilities are shown at Rs. 1,69,130.30 and Rs. 2,65,636.35 are shown as debts due to Credit Motors so that the outstanding liabilities to unsecured creditors are shown at Rs. 32,73,901.75 n.P. There is a statement in the scheme that a payment of 64% can be made out of the assets after deducting 5% already shown as paid. One of the modes of payment agreed upon was the allotment of all the shares of Hind Auto Industries of Lucknow to the unsecured creditors pro rata at face value. An assurance was given that efforts will be made to sell the residential properties of the company for distribution of the proceeds amongst the unsecured creditors within a year. It is then stated " that the balance amount will be paid in annual installments of not less than 5% for the next five years hereafter ". Then, there is a condition that " the balance thereafter will be paid in three equal annual installments in three years after the aforesaid five years". It is also provided that, after repayment of 100% of the capital, interest will be paid at 6% per annum from May 16, 1967, on unpaid balances within two years of the last payment towards repayment of 100% of the sums deposited. In

order to inspire confidence amongst the creditors three representatives of the unsecured creditors were to be appointed as directors and not more than two directors as representative of shareholders on the board of directors. The chairman was to be a creditor-director. The election of the director representing the creditors held at the meeting itself was to be binding. It was further provided that the three directors representing the unsecured creditors will be amongst the six directors of India Motor Corporation (P.) Ltd. which is not a party to those proceedings. Another condition in the scheme was. that, if an offer of payment of 75% or more of the deposits and interest up to May 15, 1967, to the unsecured creditors is received by this court through the chairman, within a fortnight from the date on which the meeting was held, that is to say, 15th February, 1969, that offer was to be accepted so that the company will transfer all its assets and liabilities to the person coming forward as a purchaser. Furthermore, it was provided that the accounts of the company will be audited expeditiously in detail and fully by some senior chartered accountant to be appointed by the board of directors. It was also promised that unsecured creditors will be provided with audited balance-sheets and profit and loss accounts every year.

14. The chairman''s report on the meeting of the unsecured creditors of the Credit Motors, supplemented by the additional information applied on 4th August, 1969, shows that the meeting of this company, held on 14th February, 1969, was attended personally or by proxies by 496 depositors only, the value of whose deposits were Rs. 19,42,950 out of the total number of 711 depositors who had deposited Rs. 27,50,000. Sri Dmanath Dinesh, a depositor, who was then working as the chairman of the board of directors on behalf of the unsecured creditors, explained the position to the meeting. It was mentioned in the report that Sri P. L. Tandon, a chartered accountant of Kanpur, also explained the financial position of the company, as it appeared from the provisional balance-sheet of 30th November, 1968, and how a distribution of 40% of the unpaid balance could be made to the creditors. After several creditors had asked questions and addressed the meeting, the scheme was shown to have been unanimously passed after electing Sri R. K. Vaish, Sri Dinanath Dinesh, and Sri H. C. Bahri as directors of the company. It may be mentioned that these were the three representatives of the unsecured creditors of the Premier Motors elected for their board of directors presumably because the creditors who had actually interested themselves especially in the affairs of both the allied companies and collected proxies were common.

15. It may be mentioned here that on July 15, 1968, a proposed scheme had also been put forward by certain creditors with a supporting affidavit of Shri H, N. Tandon, the executive director of the Credit Motors, in which, although it was stated that this company had suspended its business, the prospect of repayment of 68% of the amounts due to depositors was held out and it was also stated that this company was also hoping to take over the entire business and assets of the India Motors (P.) Ltd. of Kanpur. But, apparently, these hopes had not fructified so that

the scheme actually passed stated that only Rs. 10,20,000 was expected to be available for distribution among the depositors by the sale of the fixed and current assets of the company after deducting the secured loans from the U. P. State Financial Corporation and the liability to pay sales tax. It appears from the scheme passed that 10% of the deposits had already been paid and that 40% of the deposits could be paid in half yearly installments of 8% each, the first installment beginning on 31st August, 1969. In other words, the assurance held out was of payment of deposits up to 50% only. So far as the remaining amount was concerned, the only hope held out was that, after the appointment of the Credit Motors as agents of the Premier Motors, further business and sources of income would be available to the Credit Motors to enable further payments. It was also provided, in the final scheme of the Credit Motors, that it will be open to the directors to sell or otherwise transfer all the assets of the company to discharge its liabilities under the scheme which stated that the loans of depositors, as they stood in the books of the company on May 16, 1967, will "be treated as at par in the matter of repayment of their loans ". The last condition of this scheme was that the accounts of the company shall be audited expeditiously and in detail and fully by a senior chartered accountant to be appointed by the board of directors.

16. Although a number of creditors supported both the schemes before this court, a minority has vehemently opposed the scheme in each case and has urged that the scheme is nothing more than an attempt to throw dust into the eyes of the creditors and to deprive them of the money they had deposited on the assurance of profitable returns for the periods of their deposits together with the repayments of their loans. The manner in which the deposits were accepted almost up to the time when the applications u/s 391(1) of the Act were filed, when the inability of the companies to meet their liabilities must be evident to the directors, was pointed out. It was urged that the real object of each scheme was to throw a cloak of legal protection over the misdeeds of the directors committed in the past. Attempts were made to take me into the details of individual transactions in the past and during the pendency of the proceedings in this court u/s 391 of the Act. The extent to which the unsecured creditors were informed of the actual position and financial capacity of each company to repay the loans, before they agreed to the scheme, was questioned. It was submitted that at least the Premier Motors was a sound profit making concern which could very well repay all its unsecured creditors and the rates of interest contracted for. It was, therefore, submitted that the mere passing of the schemes by a majority of creditors in each case was insufficient. It was urged that before the scheme is sanctioned by this court it has to be satisfied : firstly, that the unsecured creditors who gave their consent were fully and honestly informed of the actual resources and likely profits to be earned in order to make their consent real ; secondly, that each scheme is fair, reasonable, and workable, so that a man of ordinary prudence and acumen in business, placed in the position of an unsecured creditor, could accept it ; thirdly, that conditions precedent to holding of a valid

meeting of the creditors of the same class were present, that is to say, those whose debts had matured before the filing of the petition and those whose debts matured after the filing of the petition belonged to the same class ; and, fourthly, that the conditions specifically prescribed by statute for the grant of a scheme u/s 392(2) of the Act were fulfilled. It was submitted that the schemes were unacceptable as the requirements mentioned above were not satisfied here.

17. I will take up the third objection first, as it really amounts to an objection to the order made by me on 8th of October, 1968, for holding the meetings. Notices were directed to be sent to all the depositors when applications were filed u/s 391(1) of the Act. Counsel for the unsecured creditors were heard before the order of 8th October, 1968, was passed. No objection was taken that separate classifications, and, therefore, separate meetings of unsecured creditors whose debts had matured and others whose debts had not matured were needed.

18. Section 391 of the Act enables arrangements or compromises to be made "between a company and its creditors or any class of them". Section 390(c) of the Act lays down clearly that "unsecured creditors who may have filed suits or obtained decrees shall be deemed to be of the same class as other unsecured creditors". Thus, the classification here contemplated appears to be between secured and unsecured creditors only. Hence, the argument based on the distinction between the depositors who had obtained decrees and those who had not obtained decree against the company, supported by a reference to Rajshahi Banking Corporation Vs. Surabala Debi was not helpful here. Reliance was also placed on In re United Provident Assurance Co. Ltd. [1910] 2 Ch. 477 where it was held that :

".....holders of shares partly paid with the uncalled balance paid in advance of calls and carrying interest are a different class to holders of fully-paid shares."

19. The question, however, in such cases is not whether some distinction between rights of different unsecured creditors can be made out, but, whether the holding of a meeting of a set of creditors, treated as a single class, is likely to adversely affect the interest of any part of that class viewed apart from others in it. In the case before me, the interests of all the unsecured creditors, irrespective of the time when their debts matured, appear to be identical. The company alleges inability to pay any of its unsecured creditors according to contracts of the same kind with identically similar terms. It could get some relief, if any at all, through an arrangement or a scheme for the discharge of its obligations to all the members of this class on the same grounds. The interests of every one of the whole of this class of creditors required a consideration of the question whether a scheme for repayment of all debts is not more advantageous to each one of them than to wind up the company. In a winding-up, the interests of this whole class will have to be dealt with on the same footing. Hence, their interests are common irrespective of the time when their debts mature for repayment. If any prejudice is likely to result to a section of a particular set of creditors from holding one meeting of a body of creditors, treated

as one class, the question should really be raised before the court passes an order to hold the meeting of all the unsecured creditors as one class. No prejudice to any section has been revealed by treating the whole body of unsecured creditors as one class. No such question was raised even at the meeting held and no decision was shown to have been taken to compel any minority to sacrifice its separate rights or interests for the benefit of the majority. All were to be repaid or deprived of their dues in equal proportion. This objection is, therefore, overruled.

20. The fourth objection, which is far more serious and has an important bearing on the first two objections, also may be taken up next. If a company is in a position to pay its debts fully, together with the interest contracted for, it cannot be said that a scheme for the repayment of its debts, which has the effect of altering contracts between parties, by reducing the rate of interest payable and giving an indefinite or unreasonably long extension of period of repayment of debts, without a just or reasonable cause, is a bona fide scheme. Indeed, if such is the position of a company, no application u/s 391(1) would be maintainable. If a company is unable to pay its debts, according to its contracts with its creditors, the question would arise whether a scheme for repayment or a winding-up of the company is more advantageous for the creditors. Whether a scheme is advantageous to creditors or just and reasonable or bona fide can only be judged in the light of information fairly supplied to the court It is for this reason that a proviso was added to Section 391 of the Act by the Central Act 31 of 1965. It reads as follows :

"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."

21. I have already indicated how each scheme provided for a regular audit of the accounts and assures the unsecured creditors that they will be given copies of the audited balance-sheets every year. It is, therefore, very surprising that, in spite of several opportunities given to the companies to put forward their latest accounts so as to enable the court to judge the exact paying capacity of each company, it has not been found possible by them to file balance-sheets beyond 30th June, 1969, and that too after orders had been passed specifically calling for further information.

22. On 31st March, 1969, applications were filed on behalf of each of the two companies for sanctioning the schemes under Rule 79 of the Companies (Court) Rules read with Section 391(2) of the Act without filing the necessary balance-sheets containing the information required for sanctioning the schemes. On 13th February, 1970, after hearing arguments at some length) it was indicated by this court to the companies and the creditors supporting the schemes that the schemes for the

liquidation of debts were much too vague and required clarification before they could be sanctioned. It was pointed out that this court, which has to supervise the operation of a scheme, can only sanction schemes which are reasonably clear and definite so as to enable it to supervise the execution of its terms. It seemed clear that the terms in the schemes passed at the meetings did not provide for a complete satisfaction of debts within a reasonable period of time. After an opportunity had been given to each company to clarify the terms still further, so that the clarifications may be incorporated in a modified scheme, the matter came up for arguments again just before the summer vacation.

23. On May 22, 1970, the orders passed on the two applications clearly intimated to each company that there were still three serious complaints against each scheme. They were : firstly, that the scheme is not a bona fide attempt to pay the dues to the creditors but to ward off payment and reduce the liability and, secondly, that the scheme is too indefinite so that it will not result in any tangible advantage to the creditors ; and, thirdly, that there is no certainty that the scheme will actually satisfy the debts within any reasonably definite period of time. In order, however, not to hold up payments to the creditors to the extent promised in each scheme by each company, an interim order was passed in each case permitting payments to proceed in accordance with the scheme awaiting sanction. It was also stated then on behalf of the companies that there were prospects of selling the buildings so that more tangible offers could probably be put forward by July, 1970. Hence, it was ordered by me, on the application of the Premier Motors :

" In the circumstances of the case, it is desirable that the company and the creditors may be given the opportunity of suggesting further modifications for liquidating the debts within a reasonable time, and in particular, for fixing a period within which the debts will be paid up totally together with interest. It is also necessary to have the latest balance-sheets and the statement of accounts and the affairs of the company in view of the proviso to Section 391 of the Companies Act. Learned counsel for the company will supply the details by the 20th July, 1970, on which date the case will be listed for further orders. "

24. A similar order was passed on the application of the Credit Motors showing that the bona fides of the company and its ability to abide by the undertakings given in the schemes was being tested and time was being given to enable the company to supply the information required for compliance with the proviso to Section 391 of the Act. The order ended as follows :

" It is also necessary to have the latest balance-sheets and the statement of accounts and the affairs of the company in view of the proviso to Section 391 of the Companies Act. Learned counsel for the company will supply these details by the 20th July, 1970, on which date the case will be listed for further orders. "

25. As a result of further time prayed for and granted, for supplying the necessary information and then for filing counter-affidavits and rejoinder affidavits, the applications were actually taken up for hearing again in October, 1970. The information supplied to this court with regard to the financial position of each company, which is certainly not the latest as required by the proviso to Section 391(2) of the Act, may now be considered.

26. The last audited balance-sheet of the Premier Motors relates to the year ending on 30th June, 1966, and shows a profit of Rs. 5,602.16 after payment of dividend for 1964-65 and discharge of other liabilities including those to the unsecured creditors. It may be noticed here that, if the company had shown a profit in the year ending on June 30, 1966, the statement, in the application u/s 391(1) of the Act filed on May 16, 1967, that the company had incurred losses in four preceding years, could not be quite correct. After 1966, all the balance-sheets are unaudited provisional balance-sheets. The balance-sheet for the year ending on 30th June, 1967, shows a total loss of Rs. 4,81,224 from which a sum of Rs. 36,259 was deducted as profit for the year 1965-66. It is difficult to make out why this profit was not shown in the previous year. However, the sudden alleged loss is unexplained. It could hardly be due to reasons such as wars with China and Pakistan or high taxation which were given in the application u/s 391 of the Act. No war either with China or Pakistan took place in the year 1966-67, and taxation did not suddenly shoot up in this particular year. It is true that stock-in-trade, which must have included cars and trucks for sale, declined in value from Rs. 12,58,962.43 to Rs. 10,43,101-52. The real reasons for the sudden and enormous rise in the losses shown by this company could only be ascertained if better and more reliable information had been placed before the court or a thorough and suitable enquiry is held on the conduct of its affairs. The provisional and unaudited balance-sheet for the year ending on 30th June, 1968, with the attached provisional profit and loss accounts shows a loss of only Rs. 30, 156, although the stock-in-trade appears to have diminished considerably in value to Rs. 7,75,876. The total loss was stated to be Rs. 4,75,11.87 (sic.) including the loss for the previous year 1966-67. A copy of the provisional balance-sheet on November 30, 1968, however, shows a loss of Rs. 4,79,876.87, for the year 1967-68 and Rs. 7,83,143.25, for the year 1968-69 bringing the total loss to Rs. 12,63,020.22. The provisional balance-sheet for the year ending on 30th June, 1969, shows a net loss of Rs. 8,73,894-44, out of which a loss of Rs. 8,60,000 was shown due to depreciation and loss on sale of old trucks. This is the enigmatic and unexplained state of affairs revealed by such unaudited balance-sheets and profit and loss accounts up to 30th June, 1969, as have been filed by the Premier Motors, which is said to be the more profitable of the two companies. If this is the true state of affairs, it appears that even the Premier Motors is not likely to be able to fulfill the promises held out of repayment in full to the unsecured creditors. Even its scheme appears to be nothing more than an attempt to ward off an inevitable liquidation. It may be mentioned here that this is exactly the conclusion stated in a representation filed on behalf of

the Company Law Board, u/s 394A of the Act, against the scheme of the Premier Motors. The Central Government''s stand also is that this is a fit ease for a winding-up.

27. So far as the Credit Motors is concerned, it was stated, in the very first clause of the earlier scheme of July 15, 1968, that the company was not carrying on any business at all. It has not been said anywhere that the business has been re-started after holding of the meeting on 24th February, 1969. The provisional unaudited balance-sheet together with profit and loss accounts for the year ending on 31st May, 1967, shows a loss of Rs. 11,14,075.08. A similar balance-sheet and profit and loss accounts from 1st June, 1968, to 30th November, 1968, shows a loss of Rs. 10,60,380.02. The next unaudited provisional balance-sheet and profit and loss accounts ending on 31st May, 1969, shows the loss of Rs. 10,80,897.32. It was admitted, on behalf of the creditors supporting this company''s scheme, that its assets and prospects of gain, even if it was to restart business, could not be sufficient to repay the unsecured creditors fully at any time. The prospect of cent per cent. payment to the unsecured creditors does not appear to be anything more than illusory representation made on behalf of the company.

28. The grounds given for not filing the latest balance-sheets and accounts of the two companies are :

firstly, the seizure of the account books of the company by the Central Bureau of Investigation ; and,

secondly, the inability of the companies to get their accounts audited owing to expense involved.

29. So far as the first ground is concerned, it could not be sufficient for failure to put forward the latest accounts and financial position, as there is no allegation that any papers or account books of the two companies were seized during the pendency of the proceedings for holding meetings to consider the scheme and for sanctioning the scheme. This could, therefore, not be a genuine ground for inability to file the latest statements of accounts and of the financial positions of the two companies. The second ground, if there is any truth behind it, only shows that the representations made to the unsecured creditors that they will be provided with audited accounts every year could not be carried out.

30. It may also be mentioned that the printed notices, which were sent to the unsecured creditors for convening the meetings of the two companies, contain the statement that the " directors of the company have no material interest in the proposed compromise or arrangement inasmuch as they are neither the creditors nor are they debtors of the company ". It is surprising to find that, even before sanctioning the schemes, the directors included persons who are interested as unsecured creditors. Directors can only be appointed in ways mentioned in Section 255 of the Act. It is true that the term "arrangement" used in Section 391(1) of the

Act is wider than mere " compromise " so that it may cover appointments made in ways other than those specifically mentioned in Section 255 of the Act, but no scheme has been sanctioned authorising their appointments. Section 255(1) of the Act lays down the mode in which the directors are to be appointed and contains a saving clause showing that they may also be appointed " as otherwise expressly provided in the Act ". Learned counsel for the companies could not explain how the present de facto directors come within the saving clause. No interim orders were passed by this court authorising these directors to manage the affairs of the companies. The complaints made by the objecting creditors to the manner in which the directors have been dealing with properties and funds of the two companies in an unauthorised manner and the pendency of an enquiry by the Central Government, which is admitted by all the parties, also indicate that it is better to order winding-up in the interests of creditors so that the illegalities committed in the management of the two companies are not concealed and those who may be found to have misappropriated the funds or properties of the two companies are ordered to make good the losses or are otherwise dealt with in accordance with law. No report of the enquiry ordered by the Central Government has been filed probably because it has not been concluded. Therefore, it cannot be said that the past directors should be absolved from liability. The schemes contain no terms showing that the past directors will pay any compensation. One of the reasons given for sanctioning the scheme with regard to the Premier Motors, in which the prospect of cent per cent. payment to the unsecured creditors was held out, was that this assurance could be carried out if the company was allowed to function as it was making profits. My attention was drawn to the statement in the provisional unaudited balance-sheet for the period ending 30th June, 1969, where gross profit of the Premier Motors is shown as Rs. 5,54,330.41 and net profit as Rs. 2,11,245.45, but the profit and loss appropriation account shows a loss of Rs. 2,25,140.00 on shares and a net loss of Rs. 8,73,894.55 out of which loss on sales and depreciation of old trucks, as already pointed out, accounted for Rs. 8,60,000. It was contended on behalf of the objecting creditors that the losses were due to large scale misappropriations by the directors and sales of trucks and other properties of the Premier Motors at much too low prices. On the other hand, it was submitted on behalf of the Premier Motors that the trucks were involved in transactions financed by the Credit Motors and had become useless. It is difficult to estimate the capacity of the Premier Motors to carry on business as a profit making concern or of its present management to run the business efficiently. It is, however, possible that if the business is carried on efficiently, the claims of the unsecured creditors may be capable of satisfaction in full some time in future. The actual scheme put forward for liquidation of the dues of the unsecured creditors does not indicate when that time will come. For a definite conclusion on this question more reliable and better information was required which the companies could not, in spite of ample opportunity given for it, provide.

31. The main argument in support of the schemes for which sanction is sought from this court are two :

firstly, that they will enable liquidation of the dues of the unsecured creditors to the maximum extent possible having regard to the assets and resources of the two companies ; and,

secondly, that the schemes have been sanctioned by an overwhelming majority of the unsecured creditors of each of the two companies so that it must be presumed that they know and understand where their advantage lies.

32. It was contended that it was more advantageous for the unsecured creditors to receive payments under the schemes placed before this court instead of a recourse to the procedure for the compulsory winding-up of the two companies. But, as I have already indicated above, the information placed before this court is neither enough nor of such a character as to enable it to hold, with any confidence, that the companies will be able to carry out even the assurances contained in the schemes. It seems to me that, so far as the Credit Motors are concerned, a delay in winding up a concern which has not been carrying on business for more than two years, may only diminish the assets which may be available for liquidation of debts and not increase its resources so as to improve its paying capacity. So far as the Premier Motors is concerned, it may be possible to avert a winding-up provided the profit making capacity of the company is really that which is claimed for it although the unaudited balance-sheets and the profit and loss accounts up to the middle of 1969 do not prove this claim. The first contention advanced in support of the schemes, therefore, fails.

33. The second contention, indicated above, that the schemes should be sanctioned as they are supported by an overwhelming majority of the creditors, unless the objectors discharge the burden of proving that the schemes are not to the advantage of the unsecured creditors, may now be examined. It was pointed out in In re Hindustan General Electric Corporation Ltd. [1959] 29 Comp. Cas. 46, 48, 50 ; In Re: Hindusthan General Electric Corporation Ltd., which is relied upon by the creditors supporting the scheme, that :

" The function and duties of the court in the matter of sanctioning of schemes are well known ".

It was held there :

" Any scheme which is fair and reasonable and made in good faith will be sanctioned if it could reasonably be supported by sensible people to be for the benefit of each class of the members or creditors concerned."

34. The three leading English authorities to which references are generally made in cases where reasonableness or bona fides of a scheme for the benefit of any class of members or creditors is questioned were also cited here. They are In re Alabama,

New Orleans, Texas and Pacific Junction Railway Co. [1891] 1 Ch. 213, 239, 243, 247 (C.A.), In re English, Scottish and Australian Chartered Bank [1893] 3 Ch. 385, 399 (C.A.) and In re Dorman Long & Co. [1934] Ch. 635 : [1935] 5 Comp. Cas. 30 (Ch. D.). It was then held :

" It has been repeatedly held that the onus of proving unreasonableness or unfairness about the scheme or of want of good faith is on those who object to the sanction of the scheme. It is not necessary to refer to many cases on this point but reference may be made to the decision in In re English, Scottish and Australian Chartered Bank [1893] 3 Ch. 385, 399, 414, 415"

35. In In re Alabama, New Orleans, Texas and Pacific Junction Railway Co. [1891] 1 Ch. 213 239, 243, 247 (C.A.) Lindley L. J. said about the duties of the court :

" The court must look at the scheme, and see whether the Act has been complied with, whether the majority are acting bona fide, and whether they are coercing the minority in order to promote interests adverse to those of the class whom they purport to represent ; and then see whether the scheme is a reasonable one or whether there is any reasonable objection to it, or such an objection to it as that any reasonable man might say that he could not approve of it."

Bowen L.J. explained :

" A reasonable compromise must be a compromise which can, by reasonable people conversant with the subject, be regarded as beneficial to those on both sides who are making it. Now, I have no doubt at all that it would be improper for the court to allow an arrangement to be forced on any class of creditors, if the arrangement cannot reasonably be supposed by sensible business people to be for the benefit of that class as such, otherwise the sanction of the court would be a sanction to what would be a scheme of confiscation."

Fry L.J. observed :

" I shall not attempt to define what elements may enter into the consideration of the court beyond this, that I do not doubt for a moment that the court is bound to ascertain that all the conditions required by the statute have been complied with ; it is bound to be satisfied that the proposition was made in good faith ; and, further, it must be satisfied that the proposal was at least so far fair and reasonable, as that an intelligent and honest man, who is a member of that class, and acting alone in respect of his interest as such a member, might approve of it. What other circumstances the court may take into consideration I will not attempt to forecast."

36. In that case, the requirements of the statute were held to have been satisfied and the burden of proving that the majority had acted against the interest of a minority was shown not to have been discharged.

37. In In re English, Scottish and Australian Chartered Bank [1893] 3 Ch. 385, 399, 414, 415 Vaughan Williams J. made observations about the weakness of the position of the creditors of which English courts were conscious after the passing of the Bankruptcy Act of 1869. He, however, thought that, under the Companies Act, greater attention was paid to the wishes of the creditors, this is to say, the majority of the creditors. He pointed out that all the three Lords in appeal in Alabama''s case had considered the advantage of the scheme in a commercial sense. He went on to observe :

" Then Lord Justice Bowen and Lord Justice Fry deal with the matter in much the same way, with this exception, that it is quite obvious that they think that the onus of showing that the scheme is unreasonable is rather on those that object to the scheme than on the majority of the creditors who have supported it. These two judges seem to me to hold that the duty of the court is to approve of the scheme, unless there is something before it which shows it either that the scheme was not made in good faith, or that it is a scheme that, so far from being fair and reasonable, is one that an intelligent and honest man, acting alone in respect of his interests, could not approve of."

38. The learned judge gave a somewhat halting and unwilling sanction to the scheme before him as he thought that he could not refuse to sanction the scheme passed by the majority of the creditors although he felt that much more information could and ought to have been supplied to the creditors before they had approved the scheme. When the matter went up to the Court of Appeal, Lindley L.J., in confirming the scheme, observed that, although it was the duty of the court to see that a dissentient minority was not coerced to sacrifice its interests unjustly, the alternatives to acceptance of the scheme, from the point of view of benefit to the creditors, had to be taken into account. He then observed about the kind of creditors involved :

" They are business men. They have looked at it, they know their own interest, and they have approved the scheme by a vast majority in favour of it."

39. He, therefore, thought that the scheme ought to be confirmed. Lopes L.J. also gave, among the reasons for approving the scheme, the considerations that the Australian creditors had almost unanimously approved the scheme and that no one could know better the state of things in Australia than the Australian creditors. He said :

" They are there upon the spot, they know all the details connected with the bank, they know all the circumstances which are likely to make the bank a flourishing concern or the contrary, and it appears to me that nobody in this country, or anywhere else except Australia, can express a view so cogent with regard to this matter as these Australian creditors. "

40. Smith L.J., although supporting the judgment of Vaughan Williams L.J., " in the main ", thought that it was hypercritical of the judgment of the Court of Appeal in In re Alabama [1891] 1 CJ. 213 (C.A.).

41. In the third important English case on the subject, In re Dorman Long & Co. [1934] Ch.. 635 : [1935] 5 Comp. Cas. 30, 33, 34 (Ch. D.). Maugham J. said about such cases ;

" It is plain that the duties of the court are two-fold. The first is to see that the resolutions are passed by the statutory majority in value and number, in accordance with Section 153, Sub-section (2), at a meeting or meetings duly convened and held. Upon that depends the jurisdiction of the court to confirm the scheme. The other duty is in the nature of a discretionary power, and it has been the subject of two decisions in the Court of Appeal, the first being the case of In re Alabama, New Orleans, Texas and Pacific Junction Ry. Co.[1891] 1 Ch. 213and the second the case of In re English, Scottish and Australian Chartered Bank (1893] 3 Ch. 385"

42. He pointed out that Lindley L.J. had said in In re English, Scottish and Australian Chartered Bank:

" If the creditors are acting on sufficient information, and with time to consider what they are about, and are acting honestly, they are, I apprehend, much better judges of what is their commercial advantage than the court can be.....While, therefore, I protest that we are not to register their decisions, but to see that they have been properly convened and have been properly consulted, and have considered the matter from a proper point of view.....the court ought to be slow to differ from them ".

43. About actually what happens at the meetings, Maugham J. stated the real position as follows :

" In these days, in many of the cases that come before me, only a fraction of the persons who are concerned could get into the room where the meeting is proposed to be held, and in the great majority of cases the proxies given to the directors before the meeting begins have in effect settled the question of the voting once for all. It is perhaps not unfair to say that in nearly every big case not more than five per cent. of the interests involved are present in person at the meeting. "

44. The authorities cited above, which were relied upon by both sides, do not appear to me to lay down anything more than that, in considering the question whether a scheme should be sanctioned, due weight should be given to an approval given by a majority. No doubt a presumption could arise, u/s 114 of the Evidence Act, that everyone knows what is best in his or her interest. One may even agree that a majority could be presumed to judge better than a minority of individuals of a class whether a particular scheme is more advantageous to the class, as a whole, than a winding-up. But such presumptions are optional and not of law. Much depends

upon the facts of each particular case, such as : the kind of persons who pass the resolution, the information with which they were supplied, the circumstances in which they accorded their approval. Such presumptions are only meant to operate as aids for the courts in deciding where the advantage of a set of creditors lies. They do not displace the duty of the court to judge for itself whether a scheme is fair and reasonable or bona fide.

45. In the cases before me there is nothing to show that the majority of unsecured creditors are astute well informed businessmen. On the other hand, the objecting creditors point out, from the long lists of unsecured creditors and their addresses supplied, that the overwhelming majority appear to be petty depositors of lower middle classes who, it is submitted, are likely to have invested their life long savings attracted by the high returns offered. Among them, there seem to be many women. Some of the deposits could, therefore, represent provision made for the maintenance of dependants. It appears from the lists of few proxy-holders and the depositors who were present at each of the two meetings that many proxies were collected by a few interested persons from depositors many of whom seem to have very readily got rid of the duty of deciding what was best for them, either because they had no time or they did not consider themselves competent enough to decide the matter. The creditors could not have been supplied with much useful and necessary information at the meetings. If this court has not been able, after hearing lengthy arguments and analysis of such incomplete information as was placed before the court by the companies, to hold that these schemes are really beneficial to the creditors, I am unable to see how the creditors could have decided this question better at the meetings with such information and explanations as were given to them.

46. Whatever may be the position under the English law or the law under our own Companies Act before the proviso to Section 391(2) of the Act was added in 1965, it is obvious that, as our law stands today, the initial duty of satisfying the court that all relevant materials, including the latest financial position of the company and the latest auditors'' reports and accounts of the company concerned have been placed before the court, so as to enable it to judge where the interests of creditors lie, rests upon the supporters of a scheme. If the court cannot be satisfied that all relevant materials have been placed before the court, it could not be said that such material could be or was actually placed before the unsecured creditors on whose behalf decisions were taken by proxies. It is only after the initial duty laid down by the proviso to Section 391 has been discharged by persons supporting a scheme that the question of considering the effect of decisions of the majority or the weight to be attached to such decisions could arise. The question of onus appears to me, because the material placed before the court actually indicates that a winding-up in each of the two cases is more advantageous to the creditors than the illusory scheme put forward, only to gain time and to prevent further investigation into the way losses have occurred. It follows from this finding that the first two objections of

creditors who opposed the scheme in each case are also well founded. It is, however, left to the parties interested to apply for winding-up orders which may be passed after hearing the parties interested specifically on this question in each of the two cases.

47. In the result, I dismiss each of these two applications with one set of costs to the objecting creditors represented by Mr. R, Gulati in the case of the Premier Motors and one set of costs to the creditors represented by Mr. Bharatji Agarwal in the case of the Credit Motors as these creditors appear to have borne the main burden of opposition to the schemes. The interim orders are vacated. The payments made so far towards the liquidation of the debts daring the pendency of these proceedings will, of course, be treated as a discharge of the liabilities to the extent of payments made. As regards the allotment of shares of Auto Hind Industries, it will be open to the Premier Motors to buy back these shares at par only after the remaining liabilities towards the depositors to whom the shares have been allotted have been discharged.