

NATIONAL COMPANY LAW APPELLATE TRIBUNAL
NEW DELHI

COMPANY APPEAL (AT) NO.239 OF 2017

(arising out of Order dated 27th April, 2017 passed by
NCLT, Hyderabad in C.P. No.36/241/HDB/2017)

IN THE MATTER OF:

Mrs Proddaturi Malathi
W/o P. Gopala Krishna,
R/o P.No.8, H.No.40-434, Gopalnagar,
Moula-Ali, Hyderabad-500040

Appellant

Vs

1. SRP Logistics Pvt Ltd & Ors
Regd Office 1-11-242/1, Flat No.304,
3rd Floor, Kishan Residency, Begumpet,
Hyderabad-500016.
2. Mr. Sekhar Pendam,
S/o P. Narayana,
Plot No.14, Prasanna Apartments, D-5,
Saibaba Colony, Sitarampur,
Bowenpally,
Secunderabad-500011

Also at

H.No.8-7-198/5/A, Plot No.131,
PV Enclave, Samatha Nagar, Old Bowenpally,
Secunderabad-500011.

3. Mrs Salalitha Parsha
W/o Sekhar Pendam,
Plot No.14, Prasanna Apartments, D-5,
Saibaba Colony, Sitarampur,
Bowenpally,
Secunderabad-500011

Also at

H.No.8-7-198/5/A, Plot No.131,
PV Enclave, Samatha Nagar, Old Bowenpally,
Secunderabad-500011.

4. Mr Mallesham Mekala,
S/o Laxman,
H.No.1-3-47/ 1, Shanthi Nagar,
Peddapalli, Karimnagar-505172
 5. Mr. Proddaturi Rama Krishna,
S/o P. Krishna
P.No.8, H.No.40-434, Gopalnagar,
Moula-Ali, Hyderabad-500040
 6. The Registrar of Companies,
Andhra Pradesh and Telngana, 2nd Floor,
Corproate Bhavan, Near Central Water Board,
Bandlaguda, Nagole,
Hyderabad-500068
- Respondents

Present: For Appellants:-Mr. V. Seshagiri with Mr. Anchit Tripathi, Advocates.

For Respondent: - Sh P. Chidambaram Company Secretary in Practice for Respondent No.1 and 2.
Mr. Yogesh Raavi, Advocate for Respondent No.2.

JUDGEMENT

BALVINDER SINGH, MEMBER TECHNICAL

1. The appellant has filed the present appeal under Section 421 of the Companies Act, 2013 thereby challenging the order dated 27.04.2017 passed by the National Company Law Tribunal, Hyderabad (hereinafter referred to as the "Tribunal") in CP No.36/241/HDB/2017 whereby and where under the Tribunal disposed of the petition while passing the following order:

"10. In view of the facts and circumstances of the case, we are of the considered view that it would be just and equitable to dispose of the company petition with the following directions:

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a) The Resolution No.1 passed on 10.4.2017 in EOGM with regard to the removal of the [petitioner is set aside.

b) Respondent No.1 Company is given liberty to conduct fresh EOGM within a period of two months from date of the receipt of copy of the order;

c) If company still wants to remove the petitioner as Director of the company, the Company is directed to give proper notice by assigning reasons for her removal and also grant proper time for her response;

d) Company is directed to follow all applicable provisions of the Companies Act, Articles of Association, Memorandum of Association and principles of natural justice in taking decisions.

e) The petitioner is at liberty to approach this Tribunal, if she is aggrieved.

f) With the above directions, CP No.36/241/HDB/2017 is disposed of.

2. Aggrieved by the said order dated 27.4.2017 the appellant has filed the present appeal and sought for the following relief inter-alia:

a) That this Hon'ble Tribunal be pleased to set aside the impugned order, being Order dated 27.4.2017 passed by the NCLT at Hyderabad.

b) That this Hon'ble Tribunal be pleased to call for records from the NCLT, Hyderabad and decide the case on its merits.

c) That this Hon'ble Tribunal be pleased to declare the impugned transfer of shares from Respondent

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No.5 shown in the Annual Return filed for the year 2006 as null and void.

- d) That this Hon'ble Tribunal be pleased to declare the impugned Allotment of shares made on 30.09.2015 and 26.11.2016 as null and void.
- e) That this Hon'ble Tribunal be pleased to declare the impugned Board Meeting held on 30.09.2015, 31.10.2016, 26.11.2016 and 15.7.2017 as null and void.
- f) That this Hon'ble be pleased to declare the impugned EOGM held on 26.11.2016 as null and void.
- g) That this Hon'ble tribunal be pleased to declare the impugned appointment of Mr. Mallesham Mekala (Respondent No.2) as Additional Director as null and void.
- h) That this Hon'ble Tribunal be pleased to declare Annual Return filed for the period 31.3.2016 as null and void.
- i) That this Hon'ble Tribunal may be pleased to set aside the Board Meeting held on 15.7.2017 as null and void.

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3. Similar reliefs were sought by the appellant in the Company Petition filed before the National Company Law Tribunal, Hyderabad Bench, Hyderabad.

4. This Tribunal vide order dated 28.07.2017 directed that ***“In the meantime, if any Boards Resolution is passed for removal of appellant from the post of Director, the same shall not be given effect to until further orders of the Appellate Tribunal.”***

5. Back ground facts in a nut shell as are as follows:

- I. M/s SRP Logistics Pvt Ltd i.e. 1st Respondent was incorporated as private company by the Appellant and Respondent No.5 along with Mr. Sekhar Pendam (2nd Respondent). The Company was incorporate with authorised share capital of Rs. 500000 (50000 equity shares of Rs. 10 each). At the time of incorporation Appellant and 2nd Respondent subscribed for 5000 shares each and 5th Respondent was allotted with 10 shares constituting ratio in percentage 49.99, 49.99 & 0.10 respectively. The 1st Respondent Company issued 39,990 equity shares of Rs.10 each during the financial year 2005-2006 to the existing shareholders maintaining the same ratio

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but replaced 5th Respondent as a shareholder of 1st Respondent with 3rd Respondent who is wife of 2nd Respondent.

- II. On 30.9.2015 by passing a shareholder special resolution the authorised capital raised from 5,00,000 (50000 shares of Rs. 10 each) to a 15,00,000 (150000 of 10 each) Board Resolution was passed whereby the paid up capital of the 1st Respondent was increased from Rs.5,00,000/- to Rs.15,00,000/- & allotted increased 1,00,000 shares. With allotment of those shares the shareholding pattern changed and shareholding of Appellant reduced from 49.99% to 28.58%.
- III. During the Board Meeting dated 21.10.2015 a Notice was issued to convene EOGM on 25.11.2016 for further increasing the share capital of the 1st Respondent and on the said date the share capital was further increased to Rs. 40,00,000. On 26.11.2016 a General Meeting and Board Meeting was conducted for further allotment which further reduced shareholding of Appellant to 14.29%, 4th Respondent was also inducted into the 1st Respondent as Additional Director.

IV. A Notice for conducting an Extra-Ordinary General Meeting on 10.04.2017 was served with an agenda to remove the Appellant as a Director of the Company and to regularize 4th Respondent as the Director. Aggrieved by the Notice and the acts of the 1st Respondent, the appellant approached Tribunal. The Tribunal passed an interim order "It is not in dispute that 1st Respondent has a right to remove a Director unless he has been appointed as Life Time Director. It is also not in dispute that any shareholder has a right to give notice to 1st Respondent for removal of any director, by citing sufficient reasons for the same. In pursuant to such notice, the Board of directors, is supposed to consider the reasons, if any, is satisfied, then the concerned Director can be given notice giving opportunity to respond. In the instance case, as stated above, the notice for removal and notice given to the petitioner is on the same date, which shows how mechanically the respondents are acting on their whims and fancies. We have perused the notice dated 15.03.2017 and it did not contain reasons for the proposal for removal of the petitioner as Director. There is no reason assigned

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in the notice, then petitioner cannot be expected to give reply

In view of the above facts and circumstances, we are of the considered opinion that the proposed EGM, going to be held on 10.04.2017 is permitted to be continued and the decision taken against the interest of the petitioners shall be kept pending until further orders. Post the case on 27.04.2017”

6. The appellant stated that in the year 2005-2006, the shareholding of the 5th Respondent was transferred to 3rd Respondent in violation of Section 56 of the Companies Act, 2013. It is further alleged that the Company right from its inception was making profits and there was no occasion for it to increase its authorized capital. However, the very purpose of increasing authorized capital without following the due procedure as contemplated under the Companies Act, 2013 was to oppress appellant.

7. It is further contended that appellant challenged the allotment of shares made by the 2nd Respondent in favour of 3rd Respondent in blatant violation of Section 62 of the Companies Act, 2013 as being oppressive and prejudicial to the appellant and the 1st Respondent.

8. It was further pointed out by the Appellant that the share application money available with the 1st Respondent for allotment of shares as demonstrated in the Balance Sheet for 2014-15 was Rs.842601/- The allotment of Rs.10,00,000/- was made in excess of the share application money. It is stated that the differential amount of Rs.1,57,399/- was received by the Respondents in cash which is impermissible under the provisions of the Companies Act, 2013. Due date for allotment of shares against which allotment was pending as on 31st March, 2015 was 1st June, 2015 as per the Notification dated 31st March, 2015 issued by the Ministry of Corporation Affairs. It was categorical submission of the appellant that no notice for the said increase of share capital along with the said allotment was issued to the appellant.

9. In response the respondents while denying the allegations has submitted that the share allotments on 30.09.2015 were made with due notice and complete knowledge of the appellant. Shares were allotted to the appellant to the extent of share application money pending and received from the appellant. This allotment of shares was done with the consent and presence of all the three directors of the company who were also 100% shareholders

of the company. Therefore, appellant's allegations qua Section 62 of the Companies Act, 2013 are meritless. It was further argued that Appellant does not dispute that she was a participant and signatory to this Board Meeting and she had full knowledge of the allotments of shares that were made on 30.09.2015. The appellant also attended the Board Meeting dated 31.10.2016. The appellant herself attended EGM dated 25.11.2016 and participated in the resolutions. It is further submitted that 10 shares held in the name of 5th Respondent were transferred to 3rd Respondent with clear consent and understanding and where 5th Respondent had never challenged the transfer.

10. We have heard the parties and perused the record; before projecting our opinion on impugned order it is necessary to discuss Section 62 of the Companies Act, 2013.

62. Further issue of share capital

(1) Where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered—

(a) to persons who, at the date of the offer, are holders of equity shares of the company in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares by sending a letter of offer subject to the following conditions, namely: —

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(i) the offer shall be made by notice specifying the number of shares offered and limiting a time not being less than fifteen days and not exceeding thirty days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined;

(ii) unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favour of any other person; and the notice referred to in clause (i) shall contain a statement of this right;

(iii) after the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, the Board of Directors may dispose of them in such manner which is not disadvantageous to the shareholders and the company;

(b) to employees under a scheme of employees' stock option, subject to special resolution passed by company and subject to such conditions as may be prescribed;

or

(c) to any persons, if it is authorised by a special resolution, whether or not those persons include the persons referred to in clause (a) or clause (b), either for cash or for a consideration other than cash, if the price of such shares is determined by the valuation report of a registered valuer subject to such conditions as may be prescribed.

(2) The notice referred to in sub-clause (i) of clause (a) of sub-section (1) shall be

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dispatched through registered post or speed post or through electronic mode to all the existing shareholders at least three days before the opening of the issue.

(3) Nothing in this section shall apply to the increase of the subscribed capital of a company caused by the exercise of an option as a term attached to the debentures issued or loan raised by the company to convert such debentures or loans into shares in the company: Provided that the terms of issue of such debentures or loan containing such an option have been approved before the issue of such debentures or the raising of loan by a special resolution passed by the company in general meeting.

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11. On perusal of the Section 62 read with its corresponding Section 81 of Companies Act, 1956 brings out the notable change in the applicability of the Provision of further issue of shares in private companies. Section 81 of the Companies Act, 1956 was not applicable to private companies even though Apex Court in various cases has caste heavier duty on the Directors to act bona fide in the interest of the company. Hon'ble Supreme Court in **Dale & Carrington Invt. (P) Ltd. v. P.K. Prathapan, (2005) 1 SCC 212** at page 224 has held that:

"11. Validity of allotment of equity shares

(d) We may also test the alleged act of allotment of equity shares in favour of Ramanujam from a legal angle. Could it be said to be a bona fide act in the interest of the company on the part of Directors of the

company? At this stage it may be appropriate to consider the legal position of Directors of companies registered under the Companies Act. A company is a juristic person and it acts through its Directors who are collectively referred to as the Board of Directors. An individual Director has no power to act on behalf of a company of which he is a Director unless by some resolution of the Board of Directors of the company specific power is given to him/her. Whatever decisions are taken regarding running the affairs of the company, they are taken by the Board of Directors. The Directors of companies have been variously described as agents, trustees or representatives, but one thing is certain that the Directors act on behalf of a company in a fiduciary capacity and their acts and deeds have to be exercised for the benefit of the company. They are agents of the company to the extent they have been authorised to perform certain acts on behalf of the company. In a limited sense they are also trustees for the shareholders of the company. To the extent the power of the Directors are delineated in the Memorandum and Articles of Association of the company, the Directors are bound to act accordingly. As agents of the company they must act within the scope of their authority and must disclose that they are acting on behalf of the company. The fiduciary capacity within which the Directors have to act enjoins upon them a duty to act on behalf of a company with utmost good faith, utmost care and skill and due diligence and in the interest of the company they represent. They have a duty to make full and honest disclosure to the shareholders regarding all important matters relating to the company. It follows that in the matter of issue of additional shares, the Directors owe a fiduciary duty to issue shares for a proper purpose. This duty is owed by them to the shareholders of the company. Therefore, even though Section 81 of the Companies Act, 1956 which contains certain requirements in the matter of issue of further share capital by a company does not apply to private limited companies, the Directors in a private limited company are expected to make a disclosure to the shareholders of such a company when further shares are being issued. This requirement flows from their duty to act in good faith and make full disclosure to the shareholders regarding affairs of a company. The acts of Directors in a private limited company are required to be tested on a much finer scale in order to rule out

any misuse of power for personal gains or ulterior motives. **Non-applicability of Section 81 of the Companies Act in case of private limited companies casts a heavier burden on its Directors. Private limited companies are normally closely held i.e. the share capital is held within members of a family or within a close-knit group of friends. This brings in considerations akin to those applied in cases of partnership where the partners owe a duty to act with utmost good faith towards each other. Non-applicability of Section 81 of the Act to private companies does not mean that the Directors have absolute freedom in the matter of management of affairs of the company. In the present case Article 4(iii) of the Articles of Association prohibits any invitation to the public for subscription of shares or debentures of the company. The intention from this appears to be that the share capital of the company remains within a close-knit group. Therefore, if the Directors fail to act in the manner prescribed above they can in the sense indicated by us earlier be held liable for breach of trust for misapplying funds of the company and for misappropriating its assets.**

26. On the question of issue of fresh share capital, it was held to be illegal to issue shares to only one shareholder. This was held to be a violation of common-law right of every shareholder. **Common law recognised a pre-emptive right of a shareholder to participate in further issue of shares. However, in India in view of Section 81 of the Companies Act, such a right cannot be found for sure. However, the test to be applied in such cases, which requires the court to examine as to whether the shares were issued bona fide and for the benefit of the company, would import such considerations in case of private limited companies under the Indian law. Existence of right to issue shares to one director may technically be there, but the question whether the right has been exercised bona fide and in the interests of the company has to be considered in the facts of each case and if it is found that it is not so, such allotment is liable to be set aside."**

12. The provisions with regard to further issue of capital contained in Section 62 of Companies Act, 2013 is now made applicable to the private companies as well. The mandatory requirements of Section 61 are that existing equity shareholder of the company shall get an offer of further issue of shares in proportion to their holding, time to be given to accept or reject the offer, renounce in favour of the any other person. The issuance of further shares to any other person than existing shareholders or employees of the company shall be at fair value reached at by the valuation report of registered valuers.

13. The 1st Respondent is a closely held company which increased its authorised share capital twice and paid capital thrice since its incorporation. We have noticed that the company is running into profits. The contention of the Appellant that there were no new requirements of funds in the company and such increase in subscribed & paid share capital has been made to oppress her by reducing her shareholding to minority. The appellant has raised questions of the acts of the respondent which have not been dealt with in the impugned order the Tribunal. Here reference is required to be made on the clause 2(4) of Articles of Association of respondent no. 1 which says that “the shares shall be under the control of the Directors who

may allot or otherwise dispose of the same or any of them to such persons, either at premium or at par or discount and at times as the directors may think fit..." The above provision shows the discretion of the Directors to allot shares but such discretion can be exercised by the Board of Directors in a duly conducted meeting in absence of which there is no allotment. The Appellant has challenged the board meetings held; the tribunal should have reached to some finding to such challenge.

Further, the averment raised by the appellant as to whether company has complied with notification G.S.R. 241(E) issued by Ministry of Corporate Affairs dated 31.03.2015 also requires due consideration of the Tribunal.

14. It is worth noticing from the impugned order itself that the Appellant approached the Tribunal and put its grievances under section 59, 241, 242, 244 of the Companies Act with prayers of transfer of shares, allotment of shares and meetings deciding allotment to be declared null and void. Tribunal except deciding on the issue of removal of the appellant/petitioner, has not dealt with any other grievances/prayer of the Appellant and disposed of the petition without dealing with the merits. Allotment of

equity shares disproportionate to the holding of the existing shareholders is act of oppression of R-2 and R-3 was one of the main issues put for consideration before the Tribunal. The shareholding of the appellant reduced to almost 14% from 49.99.

15. Yet the Tribunal without going into the merits of the case had disposed of the Company Petition. Section 62 clearly specifies the manner in which the shares of a company are to be offered and it is only when the party to whom it has been offered declines or is deemed to have declined, that the shares are to be distributed among the other shareholders of the company. The appellant further argued that the increased of paid up capital of the 1st Respondent is in violation of Section 62 of the Companies Act, 2013 which brought the combined shareholding of 2nd and 3rd Respondent at more than 50% of the total shareholding of the 1st Respondent & reduced the shareholding of the appellant to 14.29% on 26th November, 2016 prejudicial to the interest of the appellant with the sole view to oppress her.

16. We have seen the facts of the case and to our mind the approach of NCLT, Hyderabad to pick and choose the issues is not appropriate on not giving any findings on the

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oppression committed against the appellant, if any. The Tribunal has not given any findings on the issues relating to share capital and oppression committed against the appellant and have dealt with the matter relating to removal of the appellant from the directorship.

17. We, therefore, remand back the matter to the Tribunal to deal with the issues raised in the petition on merit. However, in the meantime National Company Law Tribunal, Hyderabad may pass an order that if any Board Resolution is passed for removal of the appellant from the post of Director, the same shall not be given effect till the disposal of the case by it. We expect that the National Company Law Tribunal (NCLT), Hyderabad will decide the matter expeditiously in terms of Section 422 of the Companies Act, 2013.

(Justice S.J. Mukhopadhaya)
Chairperson

(Justice A.I.S. Cheema)
Member(Judicial)

(Mr. Balvinder Singh)
Member(Technical)

New Delhi
Dated: 06-11-2017

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