Privy Council Appeal No. 84 of 1937

Srimati Premila Devi and others - - - - *Appellants*

v.

The Peoples Bank of Northern India Limited (in liquidation) - - - - - *Respondents*

Gobind Ram Kapur - - - - - *Appellant*

v.

Same - - - - - - *Respondents*

Dunni Chand - - - - - - *Appellant*

v.

Same - - - - - - - *Respondents*

Consolidated Appeals

FROM

THE HIGH COURT OF JUDICATURE AT LAHORE

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 17TH OCTOBER, 1938

Present at the Hearing:

LORD WRIGHT
LORD ROMER
LORD PORTER
SIR SHADI LAL
SIR GEORGE RANKIN

[*Delivered by* LORD ROMER]

These are three consolidated appeals from the order of the High Court of Judicature at Lahore dated the 10th March, 1936, made upon an application by the Official Liquidator of the respondents the Peoples Bank of Northern India, Limited. The question to be determined is whether the appellants should be placed upon the list of contributories notwithstanding the fact that in the year 1933 the directors of the Bank purported to forfeit the appellants' shares, and removed the appellants' names from the register of members in respect thereof.

The Bank was incorporated in the year 1925 under the Indian Companies Act with a capital of 50 lacs of rupees divided into 50,000 shares of Rs.100 each. These shares, all of which were issued, were called "A" shares. In the year 1926 the capital was increased by another 50,000 shares

of Rs.100 each, of which 25,000, called "B" shares, were then issued. In 1929 some of the remaining 25,000 shares were issued and were called "C" shares, but with these the present appeals are not concerned. On the issue of the "A" and "B" shares Rs.50 per share had been called up.

Of the articles of association of the Bank (before they were amended in manner hereinafter stated) those that are material for the present purpose were as follows:—

"*Article* 34.—*Notice requiring payment of arrears.*—Whenever any call, or instalment of a call, payable by any member shall not have been paid on the appointed day, the Company may at any time thereafter during such time as such call or instalment shall remain unpaid, send a notice requiring payment by such further day, and at such place or places where the calls of the Company are usually made payable, of such calls or instalments, in arrear, with interest thereon, at the rate of 9 per cent. per annum from the day on which such call or instalment ought to have been paid, and such notice shall state, that in the event of non-payment at the time and place appointed of the arrear incurred and interest thereon, together with such expenses (if any) as may be incurred in and about the collection or recovery of such call or instalment and interest or any of them, the share in respect of which such call was made will be forfeited without further notice.

"*Article* 35.—*If such notice be not complied with, the share may be forfeited.*—If the requisitions of any notice given pursuant to clause 34, shall not be complied with, any share in respect of which such notice shall have been given may, without further notice at any time thereafter, unless payment of all calls, interest and expenses, due in respect thereof has been made, be forfeited by a resolution of the Directors to that effect.

"*Article* 36.—*Forfeited shares to become property of the Company.*—Any shares forfeited under these Articles shall be deemed to be the property of the Company, and may be sold or re-allotted or otherwise disposed of, in such manner as the Directors shall approve.

"*Article* 37.—*Forfeiture may be remitted.*—Until any share so forfeited shall be sold, re-allotted or otherwise disposed of, the forfeiture thereof may, at the discretion and by a resolution of the Directors, be remitted on such terms as the Board may in their discretion think fit.

"*Article* 40.—*Calls to be made at the discretion of Directors.*—All calls in respect of shares shall be made at the discretion of the Directors and shall be payable to the person or persons and at the time and place or places appointed by them.

"*Article* 44.—*Interest on calls in arrears.*—If the call or instalment of a call payable in respect of any share is not paid by the day appointed for payment thereof the holder for the time being of such share shall be liable to pay interest for the same at the rate of Rs.9 per cent. per annum from the day appointed for payment thereof to the time of actual payment.

"*Article* 45.—*Power to receive in advance moneys uncalled.*—The Directors may, if they shall think fit, receive from any member willing to advance the same, all or any part of the moneys for the time being remaining uncalled on his share beyond the calls then actually made, and in case they shall so think fit they shall pay dividend upon the moneys so paid in advance or upon so much thereof as shall from time to time remain in advance of the calls then made upon the share, in respect of which such advance has been made, in addition to the dividend payable on such part of the Capital as is actually called and paid up.

> "*Article* 46.—*Power to pay interest on advance in lieu of dividend.*—If the Directors shall see fit to receive in advance any such moneys, aforesaid, they may pay interest upon the same, or upon so much thereof as shall from time to time remain in advance of the calls, at such rate not exceeding 6 per cent. per annum as they shall think fit, such interest to be in lieu of the dividend provided by the preceding clause upon such moneys so paid in advance.

On the 29th September, 1931, the Bank suspended payment. Shortly afterwards a scheme of arrangement between the Bank, its creditors and shareholders was prepared, and after being approved in the usual way at meetings of the creditors and shareholders was duly sanctioned by the Court under section 153 of the Indian Companies Act upon the 22nd December, 1931. The details of that scheme are not relevant to these appeals. But by the 25th July, 1932, it had become evident that the scheme was not likely to attain the end which its promoters had in view, namely, the successful resuscitation of the business of the Bank, and accordingly on the last-mentioned date an amended scheme of arrangement was brought before the Court. In the meantime the directors had by resolution dated the 15th March, 1932, made a call of Rs.20 in respect of the "A" and "B" shares, of which Rs.10 was to be paid on or before the 30th April, 1932, and Rs.10 on or before the 20th May, 1932. The amended scheme was in due course submitted to meetings of the creditors and shareholders respectively, and having been approved by them was sanctioned by the Court on the 15th November, 1932.

The only provisions of this scheme that are relevant to the present appeals are those contained in clause 6, which so far as material is in these terms:—

> "6. That for the purposes of the revival of the Bank it be distinctly laid down that further calls on capital of 'A' and 'B' class shares of which Rs.50 and 25 lacs have been respectively subscribed will not exceed 25 per cent., 20 per cent. having been already called; thus leaving only a further call of 5 per cent. to be made. This 25 per cent. call will be redistributed into 5 calls of 5 per cent. each payable every half year starting from 1st July, 1932."

This clause is not expressed as clearly as it might have been, but their Lordships entertain no doubt as to its meaning. Before the month of March, 1932, Rs.50 had been called up on each of the "A" and "B" shares. On the 15th of that month a further Rs.20 had been called up as already stated. The clause provided that for the purpose of the revival of the Bank—i.e., for the purpose of the scheme—a further call of Rs.5 should be made in respect of such shares and no more. Had the clause stopped there the dates for payment of the Rs.20 call would have been those already fixed by the directors, viz., as to Rs.10 thereof the 30th April, 1932, and as to the remaining Rs.10 the 20th May, 1932. The further call of Rs.5 would have become payable on such date as might be fixed by the directors when making the call under article 40. But the clause went on to fix the dates on which both the Rs.20 call already

made and the Rs.5 to be made thereafter should be paid. The whole 25 per cent. was " redistributed " and was to be paid in five instalments of 5 per cent. each payable on the 1st July, 1932, the 1st January, 1933, the 1st July, 1933, the 1st January, 1934, and the 1st July, 1934. It only remained for the directors to pass a resolution making the further call of Rs.5 under article 40, and such call would by virtue of the scheme become payable on the 1st July, 1934. No further resolution was necessary in respect of the Rs.20. In the words of clause 6 it had " already been called." The resolution of the 15th March, 1932, therefore, remained unaffected except that the dates for the payment of the Rs.20 were altered.

It is to be observed that one effect of the amended scheme when it came into operation on the 15th November, 1932, was to make the instalment payable on the 1st July, 1932, a call in arrear. Another effect was that " A " and " B " shareholders who had punctually paid the call made on the 15th March, 1932, were probably entitled to be treated as having paid moneys on their shares in advance of calls within the meaning of articles 45 and 46. These circumstances no doubt introduced some complication into the matter. But it was nothing compared to the complications introduced by the subsequent proceedings of the directors to which attention must now be called. On the 18th January, 1933, they held a board meeting. Their Lordships regret to say that the record of proceedings supplied to them on these appeals would seem to have been prepared with the view of making the discovery of any particular document as laborious a task as possible. But a diligent search, (for no assistance will be obtained from the index of reference), will reveal a minute of this board meeting. According to this minute the directors, after referring to clause 6 of the scheme, and recording the fact that many shareholders had made default in payment of the 10 per cent. calls made in the preceding March in whole or in part, passed the following resolutions:—

> " (*a*) That the remaining call of 5 per cent. on ' A ' and ' B ' shares as provided for in clause 6 of the Annexure A be made now under Article 34 payable on or before the 26th February, 1933, and that these shareholders who are partly or wholly in default of already outstanding calls should be called upon under Article 35 to pay up the arrears due with interest at 9 per cent. per annum calculated from due dates to 31st January, 1933; at the registered office of the company at Lahore, Bharat Buildings, on or before the 26th day of February, 1933, in office hours, and that notices to this effect as required by Articles 34 and 35 respectively be served on all ' A ' and ' B ' shareholders and also on the defaulters, intimating to the latter, i.e., defaulters at the same time that in the event of non-payment at the time and place appointed all the arrears incurred and interest thereon together with such expenses (if any) as may be incurred in and about the collection or recovery of such calls and interest or any other, the share in respect of which such calls were made will be forfeited without further notice; and that a meeting of the Board will be held on 27th February, 1933, to effect forfeiture of the defaulters of the two 10 per cent. calls and the 5 per cent. call or any of them; and that to the defaulters

who pay up at least 5 per cent. on account of three calls (two of 10 per cent. each of 15th March, 1932, and one of 5 per cent. of 18th January, 1933), made before the 26th February, 1933, as an instalment under clause 6 of the revised scheme.

" (*b*) A compromise under Article 37 be offered to those shareholders who accept the following terms in regard to the amounts due on account of three calls totalling 25 per cent. and interest due up to 31st January, 1933, in terms of clause 6 of the Annexure A and but having paid 5 per cent. as per terms of compromise proposed before the 26th February, 1933, and agreeing to pay the remaining 20 per cent. of calls and interest due as above cited:—

" 5¼ per cent. on all shares held by him on or before 15th June, 1933.

" 5¼ per cent. on all shares held by him on or before 15th December, 1933.

" 5¼ per cent. on all shares held by him on or before 15th June, 1934.

" 5¼ per cent. on all shares held by him on or before 15th December, 1934.

at the Head Office of the Bank between office hours on working days and further agreeing that in the event of making a default in any of the instalments as fixed here above, the Banks Board could take the action as provided for in Articles 34, 35, and 36 of the Banks Articles of Association."

These resolutions betray a complete misappreciation on the part of the directors of clause 6 of the scheme. They had no right whatsoever to make the remaining call of 5 per cent. payable on or before the 26th February, 1933. It is, moreover, quite apparent that in passing this resolution they treated the clause as in no way affecting the dates originally fixed for payment of the 20 per cent. call made in March, 1932, and that they were requiring payment of the whole of this call (so far as not already paid) on or before the 26th February, 1933. This again they had no right to do. The most that they could have done in respect of this 20 per cent. call was to send a notice under article 34 requiring payment by the 26th February, 1933, of the two instalments of 5 per cent. payable on the 1st July, 1932, and the 1st January, 1933, with interest at 9 per cent. per annum from those dates respectively, with an intimation that the shares would be forfeited in default of payment of such instalments, interest and expenses as mentioned in the article. It would also have been within the competence of the directors after any such forfeiture to offer a compromise under article 37 to those members who had paid 5 per cent. before the 26th February, 1933. But they would have had no conceivable right to make it a term of such compromise that the instalments that were payable under the scheme on the 1st July, 1933, the 1st January, 1934, and the 1st July, 1934, should be paid on any other dates.

It is perhaps understandable that the directors should have failed to appreciate the true effect of clause 6 of the scheme and have thought that it in no way altered the dates for payment of the 20 per cent. call made in March, 1933. What is not so understandable is that entertaining the views

they did as to the meaning of the clause they should at the same meeting have passed the following resolution:—

> "Resolved that the following sub-clauses be added to Article 46 (by two extraordinary general meetings).
>
> "That such shareholders who had paid the 20 per cent. of two calls 10 per cent. each payable on 30th April, 1932, and 20th May, 1932), before the 18th January, 1933, shall be paid interest at the rate of 6 per cent. per annum from date of payment up to 31st January, 1933, and thereafter interest will run on the non-adjusted balance out of the remaining 15 per cent. as per clause 3 hereof at the rate of 6 per cent. per annum under Article 46 treating the balances at any time as an advance.

Article 46 was subsequently amended in accordance with this resolution. What may be the meaning of the words "non-adjusted balance out of the remaining 15 per cent. as per clause 3" their Lordships are quite unable to determine. But it is plain that interest could only be allowed to the shareholders who had already paid the two calls of 10 per cent. if those calls were in truth payable on the 1st July, 1932, the 1st January, 1933, the 1st July, 1933, and the 1st January, 1934, instead of on the 30th April, 1932, and the 20th May, 1932; that is to say, if the dates originally fixed for payment had been altered by the scheme. The calls would not otherwise have been paid in advance. But, however this may be, the directors on the 23rd January, 1933, sent to the holders of the "A" and "B" shares a notice of the further call of 5 per cent. to be paid on or before the 26th February, 1933, stating that, in default of payment on or before that date of this further call and of the two previous calls of 10 per cent. each (which they described as payable on the 30th April and the 20th May, 1932, respectively), with interest on such two previous calls at 9 per cent. per annum from the date of the calls to the 31st January, 1933, the shares would be forfeited without any further notice. It was also stated that shares could be restored after forfeiture on the basis of the compromise mentioned in resolution (*b*) passed on the 18th January, 1933. A draft copy of the compromise was enclosed with each notice.

On the 25th March, 1933, another board meeting was held. By resolutions passed at this meeting the shares of such shareholders (including several of the present appellants) as had neither made any payment in pursuance of the notice nor accepted the terms of the compromise were forfeited. The shares of those members (including the remaining appellants) who had paid 5 per cent. on or before the 25th March, 1933, and had accepted the compromise were not forfeited at this time. But later on default was made by them in paying the instalment of 5¼ per cent. payable under the compromise on the 15th June, 1933, and by the 11th November, 1933, the shares of all the appellants had been forfeited by the directors.

On the 22nd May, 1935, an order was made for the winding up of the Bank, the Official Liquidator being appointed the liquidator. By this time the names of all

the appellants had been removed from the register of members in respect of the shares which the directors had purported to forfeit. In the cases where the directors had been able to sell the shares the purchasers' names had been entered on the register. The Official Liquidator, however, inserted the names of all the appellants in the list of contributories, contending that their shares had not been validly forfeited and that their names had been improperly removed from the register. In order to have it determined whether this contention was well founded he applied to a Judge of the High Court of Judicature at Lahore to have the list of contributories settled by the Court. The question of principle involved was in due course referred by the learned Judge to a Division Bench consisting of the Chief Justice and Munroe J. and they delivered their judgment on the 16th March, 1936. They held in effect that the resolutions of the directors of the 18th January, 1933, were inconsistent with clause 6 of the amended scheme and that the forfeiture of the appellants' shares were *ultra vires* the Bank and of no effect. They rejected the contention of the appellants that the action of the directors had been ratified by the creditors and shareholders, holding that such ratification even if proved could not validate an *ultra vires* transaction. But they further held that there was no such ratification in fact. They accordingly accepted the application of the Official Liquidator and ordered the rectification of the register of members so as to include the names of the the appellants and others in the like position and settled their names upon the list of contributories. From that decision the appellants, having obtained the necessary leave, now appeal to His Majesty in Council.

In their Lordships' opinion the learned Judges of the Division Bench came to a right conclusion.

Upon confirmation by the Court of the amended scheme of arrangement that scheme became by virtue of section 153 of the Indian Companies Act binding upon the creditors, the shareholders and the Bank alike. Its terms could thereafter only be varied by order of the Court after the variation had been approved at meetings of the creditors and shareholders. It was not, therefore, possible for the Bank or its directors or shareholders whether by resolution or ratification or otherwise to alter the dates fixed by clause 6 of the scheme for payment of the 20 per cent. called up in March, 1932, or the 5 per cent. called up on the 18th January, 1933. It necessarily follows that the resolution of the directors on the latter date requiring the whole 25 per cent. to be paid with interest on or before the 26th February, 1933, was an attempt on their part to do something that was *ultra vires* the Bank.

The offer to the shareholders of the compromise was equally beyond the powers of the Bank or its directors. For apart from the fact that the powers conferred upon the directors by article 37 only arise after the share has been forfeited, neither the Bank nor its directors could vary the scheme under the guise of a compromise with a shareholder.

The resolutions (*a*) and (*b*) of the 18th January, 1933, except in so far as they made the call of 5 per cent., and the purported forfeitures of the appellants' shares that followed upon them were, therefore, inoperative and void.

It was said on behalf of the appellants that, inasmuch as on the 18th January, 1933, the two instalments payable on the 1st July, 1932, and the 1st January, 1933, were in arrear, the Bank through its directors could have validly forfeited the appellants' shares. This is true. But it is plain from the terms of the resolutions of the 18th January, 1933, and of the notice sent to the shareholders on the 23rd January, 1933, and of the resolution of the 25th March, 1933, that the shares forfeited on this last date were being forfeited for default in payment of the 25 per cent. by the 26th February, 1933. This latter resolution was in these terms:—

> "The shareholders in respect of the following 'A' and 'B' class shares having made default in respect of calls of 25 per cent., 20 per cent. having been called on 15th March, 1932, and 5 per cent. on 18th January, 1933, and having neither offered any compromise as allowed by the General Board Resolution No. 2 dated 18th January, 1933, nor having made any payment in terms thereof, it is hereby resolved that these shares be and are forfeited. . . ."

It was further contended on behalf of the appellants that inasmuch as the shares of those who had paid at least 5 per cent. by the 25th March, 1933, were not forfeited until later, and they were given further opportunities of availing themselves of the compromise, the resolution just set out should be regarded as merely forfeiting the shares for non-payment of the 5 per cent. payable on the 1st July, 1932. This in their Lordships' judgment is an impossible contention in view of the facts already detailed. It is true that had the shareholders affected by the resolution paid the 5 per cent., their shares would not have been forfeited at that time. They would have been given a further opportunity of paying. But from those who had paid nothing, the directors may well have thought that nothing was likely to be obtained in the future. Their shares were accordingly then and there forfeited; they were forfeited, however, for non-payment of the 25 per cent., and not merely for non-payment of the 5 per cent.

This may seem to be somewhat technical; but in the matter of the forfeiture of shares, technicalities must be strictly observed. And it is not, as is sometimes apt to be forgotten, merely the person whose shares are being forfeited who is entitled to insist upon the strict fulfilment of the conditions prescribed for forfeiture. For the forfeiture of shares may result in a permanent reduction of the capital of a company. It will suffice to take the present case as an example. If the forfeitures are upheld the appellants remain liable, no doubt, for the whole 25 per cent. called up in March, 1932, and in January, 1933. But they will escape liability altogether in respect of the uncalled 25 per cent., and this is a matter that vitally affects the creditors. These

creditors cannot be deprived of their right to have this 25 per cent. made available for payment of their debts without due cause.

The creditors are, therefore, entitled to see that the power of forfeiting shares is exercised strictly. Where the power of a company to forfeit shares has arisen, the articles of association usually contain provisions as to the sending of notices and the like that may be regarded as being inserted merely for the protection of the shareholder affected. Such provisions may properly be regarded as being directory only and capable of being waived by the individual shareholder. But no waiver by him can confer upon the company or its directors a power of forfeiture that they do not possess, as for example, a power to forfeit shares for non-payment of calls that are not yet due.

It was, however, strenuously contended on behalf of the appellants both before the High Court and before their Lordships that the forfeitures in question had been ratified by the whole body of creditors and shareholders. Such ratification, it was said, was to be implied from the fact that various balance sheets with reports thereon of the directors showing that the shares in question had been forfeited had been issued to the shareholders; that the forfeiture of the shares had also been mentioned and discussed at meetings both of creditors and shareholders; and that no creditor or shareholder had ever challenged the validity of the forfeitures.

In view, however, of the binding character of the scheme sanctioned by the Court, no variation of or departure from that scheme could be validated by the mere acquiescence of the shareholders and creditors, as has already been pointed out in an earlier part of their Lordships' judgment. But even if it be assumed that the forfeitures could be made valid by ratification, there is no evidence to which their Lordships' attention has been called to justify the conclusion that such ratification was in fact given. As was said by Lord Chelmsford in *Spackman* v. *Evans*, L.R. 3 H.L. 171, at p. 234:—

> "To render valid an act of the directors of a company which is *ultra vires*, the acquiescence of the shareholders must be of the same extent as the consent which would have given validity from the first, viz., the acquiescence of each and every member of the company. Of course, this acquiescence cannot be presumed unless knowledge of the transaction can be brought home to every one of the remaining shareholders."

By knowledge of the transaction Lord Chelmsford clearly meant knowledge of the invalidity of the transaction. Lord Cranworth in the same case said this (p. 194):—

> "Looking to all which was thus done, I should certainly hold that the conduct of the continuing shareholders amounted to a ratification of the illegal or irregular acts of the directors, provided it be clear that the shareholders knew that they were illegal or irregular. . . ."

Much to the same effect was said by Sir Barnes Peacock in delivering the judgment of this Board in the case of *Irvine* v. *Union Bank of Australia,* 2 A.C. 366 at p. 375:—

> "Their Lordships think that it would be competent for a majority of the shareholders present . . . at an extraordinary meeting convened for that object, and of which object due notice had been given, to ratify an act previously done by the directors in excess of their authority; and they are not prepared to say that if a report had been circulated before a half-yearly meeting distinctly giving notice that the directors had done an act in excess of their authority, and that the meeting would be asked by confirming the report to ratify the act, this might not be sufficient notice to bring the ratification within the competency of the majority of the shareholders present at the half-yearly meeting."

There can in truth be no ratification without an intention to ratify, and there can be no intention to ratify an illegal act without knowledge of the illegality. In the present case there is nothing whatsoever to show that in the balance sheets or reports or at any meeting, the attention of the creditors or shareholders was called to any illegality or irregularity in the forfeitures of the shares, or that at any material time they had any knowledge of any such illegality or irregularity. Least of all were they told that they were being invited by their silence or otherwise to ratify the forfeitures that had taken place. It was on these grounds that the plea of ratification was rejected, and in their Lordships' opinion was rightly rejected, by the learned Judges of the High Court.

A belated attempt was made by Mr. Pringle on behalf of some of the appellants to show that their shares had been forfeited not for default in payment of the calls of 25 per cent. made in March, 1932, and January, 1933, but for default in payment of the calls of 50 per cent. made on the original allotment of the "A" and "B" shares. But no such contention was put forward in the High Court or in the printed case for the appellants. The contention is indeed in flat contradiction of some of the statements made in the case. In these circumstances it is far too late to advance any such contention now.

It only remains to mention one other matter. It is said by the appellants that the liquidator is attempting to charge them with interest on the unpaid calls and that the liability of the appellants as contributories is inconsistent with liability on them to pay such interest. Upon this question their Lordships express no opinion. The only question before them is whether the appellants have been rightly placed upon the list of contributories; and this question should, in their Lordships' judgment, be answered in the affirmative. What the result of this may be is a question that will have to be determined hereafter in the course of the liquidation. It does not arise on this occasion.

Their Lordships are of opinion for the reasons they have given that these appeals should be dismissed with costs, and they will humbly advise His Majesty accordingly.

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In the Privy Council

SRIMATI PREMILA DEVI AND OTHERS

v.

THE PEOPLES BANK OF NORTHERN INDIA LIMITED (IN LIQUIDATION)

GOBIND RAM KAPUR

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DELIVERED BY LORD ROMER

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