IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 30-04-2008

CORAM

THE HONOURABLE MR. JUSTICE P.K.MISRA
and
THE HONOURABLE MR. JUSTICE S.TAMILVANAN

O.S.A.Nos.308, 309, 312 of 2006
and O.S.A.No.91 of 2007
and
M.P.NOs.1 and 2 of 2006

O.S.A.No.308 of 2006

Reserve Bank of India
having its Central Office at
Mumbai and Regional Ofice at
Fort Glacis, Chennai. .. Appellant/Objector

vs.

M/s. Integrated Finance Company Ltd.,
a company incorporated under the
Companies Act 1956, and having its
Registered Office at
"Vairams", 112, Thyagaraya Road,
T.Nagar, Chennai - 600 017
Rep. by Mr.P.B.Appaiah, Director. .. Respondent

O.S.A.No.309 of 2006

1. Integrated Finance Company Depositors Association
(Regn. No.K.471/2005)
Rep. By its vice President,
Mr.Josey Oommen,
Kannothra Guest House,
Kanjikuzhi, Kottyam - 686 004.

2. K.K.Thomas @ Vijayan
3. Zaharia Thomas
4. Johnson Thomas
5. Ramadas Panickar
6. Santom Kaloor
7.Trentin John
8. Pillai.P.K.S
9. Saramma George
10. Kurian C.P.

11. Thomas Mathew
12. Mathai Mathews
13. Isaac Abraham
14. Mammen George
15. Ammini Jacob
16. K.V.Joseph
17. Mathai Mathew
18. Joseph A.Thomas
19. Mrs.Ammini Jacob
20. Mrs. Mary Josey
21. Thomas P.A.
22. Sally Thomas .. Appellants/Objectors 19 to 24 & 8 to 22

vs.

M/s. Integrated Finance Company Ltd.,
Rep. By its Managing Director
Mr.George Kurivilla,
No.112, Thyagaraya Road,
T.Nagar, Chennai - 600 017. .. Respondent

(Appellants 3 to 7 rep. by their
Power of Attorney
K.K.Thomas @ Vijayan)

(Appellants 8 to 22 rep. by their
Power of Attorney
Josey Oommen)

O.S.A.No.312 of 2006

M/s. Popular Kuries Limited,
having its Registered Office at
High Road,
Thrissur - 680 001.
Represented by its Authorised Signatory. .. Appellant/objector

vs.

M/s. Integrated Finance Company Ltd.,
a company incorporated under the
Companies Act 1956, and having its
Registered Office at
"Vairams", 112, Thyagaraya Road,
T.Nagar, Chennai - 600 017
Rep. by Mr.P.B.Appaiah, Director. .. Respondent

O.S.A.No.91 of 2007

Mrs. Elizabeth Antony. .. Appellant

vs.

M/s. Integrated Finance Company Ltd.,
a company incorporated under the
Companies Act 1956, and having its
Registered Office at
"Vairams", 112, Thyagaraya Road,
T.Nagar, Chennai - 600 017
Rep. by Mr.P.B.Appaiah, Director. .. Respondent

These Appeal are filed under Order XXXVI Rule 11 of O.S. Rules against the order of the learned single Judge dated 19.08.2006 passed in C.P.No.160 of 2005.

For Appellants : Mr.T.Poornam in O.S.A.No.308 of 2006
Mr.V.Prakash, Senior Counsel
for Mr.P.V.Ravichandran in
O.S.A.No.309 / 06
Mr.T.Suresh in O.S.A.No.312 of 2006
Mr.K.F.Manavalan in O.S.A.No.91/2007

For Respondent : Mr.Arvind P.Datar, Senior Counsel
for Mr.P.H.Arvindh Pandian

Supporting the
Respondent : Mr.K.M.Vijayan, Senior Counsel
Mr.Vijay Narayan, Senior Counsel
Mr.R. Viduthalai, Senior Counsel
Mr.Chandrasekhar

COMMON JUDGMENT

P.K. MISRA, J.

Company Petition No.160 of 2005 was filed under Section 391 of the Companies Act, 1956 (hereinafter referred to as "the Act") by M/s. Integrated Finance Company Limited (hereinafter referred to as "the Company"), a private company incorporated under the Companies Act, for getting approval of the Scheme of arrangement / compromise between the said company and some of the creditors, namely, the deposit holders and bond holders.

1.1 The Company is a non-banking finance company incorporated under the Act and engaged in the business of hire purchase and lease. Expressing its inability to carry on its business on account of

various factors, the Company presented a Scheme under Section 391 of the Act for an arrangement / compromise with the class of creditors, namely, the bond holders and deposit holders.

1.2 The salient features of the Scheme as contained in such petition are to the following effect :-

> "4. PAYMENTS TO FIXED DEPOSIT HOLDERS / BOND HOLDERS
>
> 4.1 The Company would settle all the deposit holders up to maturity value of Rs.20,000/- as and when it falls due.
>
> 4.2 The scheme would provide for the following.
>
> (a) Conversion of all the deposit holders and bond holders into secured convertible debentures carrying on interest of 6% p.a. convertible into equity before the expiry of 1 year from the date of allotment with an option to the company to prepay the value of debentures before the due date of conversion. The conversion price will be determined taking into account the valuation laid down by SEBI guidelines.
>
> (b) The debentures will be issued with periodical interets payment option to the deposit/ bond holders who are holding regular interest payment option presently and for those deposit/ bond holders holding payment of interest under cumulative option, interest will be added to the value of the debenture for conversion at the time of maturity.
>
> (c) By virtue of this scheme, all the deposit holders and bond holders would become secured creditors in the books of IFCL at the first year. The Trustees for the Bonds would be the Debenture Trustees in the post scheme scenario and a Debenture Trust Deed charging the assets of Rs.125 crores of receivables, accrued interest, investments, assets and available stock on hire would also be made so as to comply with all the norms for the purpose of fully convertible debentures.

4.3. By virtue of the conversion, the outflow of the company would be a quarterly payment of interest depending upon the type of deposit/ bond held by the creditors. At the end of the tenure the debentures would either be redeemed or converted as equity shares at the given appropriate exit route as the Company is a listed company and a fairly large tradable market capitalization being available for the liquidation of these converted shares. The conversion of deposit holders/ bond holders into secured convertible debentures and thereafter into equity shares of the company will ensure their benefits since the company established new lines of business such as financial BPO and is in the process of expanding the same.

4.4 The reduction in interest rates would result in cash flows from operations. Apart from this Rs.125 crores of stock hire being available which would be used for funding the operations.

4.5 A detailed cash flow will be furnished as may be directed by the Hon'ble High Court giving out particulars of amount of recoverable from the stock on hire and through revenue generation from operations.

4.6 The scheme is not offered to the Banks since the stock on hire pledged / hypothecated is about Rs.80 crores as against their dues of Rs.62 crores. Since none of the banks interest is prejudiced nor any of the assets charged to them, this scheme is not being offered to them and it is only the deposit holders and bond holders whose right are being dealt with in the Scheme of Arrangement and compromise. Thus there is no direct or indirect interest of the Banks being prejudiced or affected.

5. Since this scheme does not envisage cash outflow at the first instance and does seek to convert the depositors and bond over a period of time into shareholders there is no requirement of fresh infusion of cash.

6. IMPLEMENTATION OF SCHEME

6.1 The Scheme if approved by the deposit holders and bond holders with such modifications, as may be assented by the Company, shall be submitted to this Hon'ble Court for confirmation and if confirmed, shall become binding with all deposit holders, bond holders and the Company.

6.2 On completion of the scheme, the Company shall have discharged all the liability to fixed deposit / bond holders.

7. EFFECT OF THE SCHEME

7.1 In view of the above Scheme being offered, all the parties agree that:

a) with the terms of the Scheme all liabilities of the Deposit Holders and Bond holders shall be deemed as fully discharged.

b) No claims shall be raised by any deposit holders or bond holder to whom this Scheme is offered and

c) No claim can be made against any group companies of IFCL their associates or any other person, promoters, directors, past and present, in respect of matters relating to IFCL.

d) This scheme if approved and ordered by this Hon'ble Court shall be binding on the Company and all parties to the scheme."

1.3 In C.A.Nos.854 and 855 of 2005, arising from C.P.No.160 of 2005, the learned single Judged ordered convening and holding of the meetings of the bond holders and deposit holders on 10.8.2005 separately for the purpose of considering the Scheme of arrangement / compromise. On the basis of Company Appln.Nos.1105 to 1110 of 2005, the learned single Judge nominated a retired District Judge as an Observer of the meeting to ensure fair and free participation of the bond holders and deposit holders. The meetings have been held under the Chairmanship of the Court appointed Chairman and also the Observer. The Scheme was approved and report was published in various newspapers indicating that the Scheme had been approved by majority of the bond holders and deposit holders in accordance with the provisions of Section 391(2) of the Act. A report was filed before the single Judge along with the Observer's report. Pursuant to the notice, the Regional Director, Ministry of Company Affairs, filed a report, wherein it was indicated that since the company proposes to convert the debentures to equity shares to the bond holders and deposit holders, the Company had to comply with Section 81 of the Act.

2. The Integrated Finance Company Depositors Association, an Association representing the depositors and several other depositors, filed objections raising several contentions regarding the validity of the Scheme. Objections were also raised by the Reserve Bank of India (RBI).

2.1 Certain other Associations representing the deposit holders, debenture holders also intervened supporting the Scheme. Similarly, an Association of the employees also intervened supporting the Scheme.

3. During pendency of Company Petition No.160 of 2005, the petitioner had filed Company Appln.Nos.1409 & 1410 of 2005 forbearing Respondents 1 to 6 in such Applications from initiating any proceeding either civil or criminal in nature against the Directors of the petitioner company and for granting stay of commencement of the suit or proceedings against the company, during pendency of such C.P.No.160 of 1995.

4. Ultimately, the learned single Judge sanctioned the Scheme, subject to the condition that the Scheme will not exonerate or protect the Directors and those in charge of the affairs of the Company from any proceeding that may be contemplated either under the provisions of the Companies Act or under any other Act for any statutory violation.

5. The Reserve Bank of India has filed O.S.A.No.308 of 2006, the Integrated Finance Company Depositors Association filed O.S.A.No.309 of 2006, M/s. Popular Kuries Limited filed O.S.A.No.312 of 2006 and Mrs. Elizabeth Antony has filed O.S.A.No.91 of 2007 against such order dated 19.8.2006.

6. We have heard Mr.V. Prakash, Senior Counsel appearing for the appellant in OSA.No.309 of 2006, Mr.T. Poornam, Counsel appearing for the appellant in OSA.No.308 of 2006, Mr.T. Suresh, Counsel appearing for the appellant in OSA.No.312 of 2006 and Mr.K.F. Manavalan, Counsel appearing for the appellant in OSA.No.91 of 2007, who have assailed the legality and validity of the order passed by the learned single Judge.

Mr. Arvind P. Datar, Senior Counsel appeared for the company, the main contesting respondent in all the appeals, in support of the order passed by the learned single Judge. Senior Counsels, Mr.K.M. Vijayan, Mr. Vijay Narayan and Mr.R. Viduthalai have also appeared for various Associations representing the depositors supporting the scheme. Similarly Mr. Chandrasekhar appearing for the employees Association has also supported the scheme.

7. The main contention raised by the learned counsels appearing in various appeals is to the effect that by sanctioning the Scheme, many of the provisions of the Reserve Bank of India Act, 1934, hereinafter referred to as "the RBI Act", are being violated, which is impermissible in law. Learned Senior Counsel appearing for the appellant in OSA.No.309 of 2007, while adopting the submission and supporting such contention of the learned counsel for RBI, has further submitted that if the Scheme is implemented, it would be an indirect approval of the various acts of omissions and commissions on the part of the persons in charge of the affairs of the Company, which should not be permitted. It has been further submitted by him that under the Scheme all the bond holders and the deposit holders those who had deposited Rs.20,000/- or less, would be left with a convertible debenture of most uncertain value. It has been further submitted that since many of the working class people had invested their entire life saving being lured by various tall promises made, the Scheme, if finalised, would jeopardise their interest, which should not be permitted.

8. Learned Senior Counsels appearing for the respondent Company and some of the depositors have supported the Scheme and contended that in view of various factors, which are beyond the control of the company, it has become no longer possible for the company to carry on its usual business and, therefore, the Scheme should be adopted so that instead of winding up a company efforts can be made to revitalise the company as per the terms and conditions contained in the Scheme.

9. Chapter V of the Act contains the relevant provisions relating to compromises and arrangements. Sections 391 to 393 are relevant. On a bare perusal of these provisions, it is obvious that while considering the question as to whether the Scheme should be sanctioned or not, the Courts are required to concentrate on the procedural wisdom, commercial wisdom as well as the legal wisdom. In other words, the Courts are required to find out as to whether the procedural aspects contained in Sections 391 and 393 of the Act are complied with. Once it is found that the procedural requirements have been fulfilled, the next question is whether the scheme is commercially just and fair. Apart from the above, the Courts are also required to find out whether the Scheme is violative of any of the provisions of law or opposed to public policy.

10. After analysing the relevant provisions contained in Sections 391 and 393 of the Act and referring to several decisions, the Supreme Court, in the decision reported in AIR 1997 SC 506 (Miheer H.Mafatlal vs. Mafatlal Industries Ltd.,), observed :

> "28-A . . . (1) The sanctioning court has to see to it that all requisite statutory procedure for supporting

such a Scheme has been complied with and that the requisite meetings as contemplated by section 391(1)(a) have been held.

(2) That sanction put up for sanction of the court is backed up by the requisite majority vote as required by section 391(2).

(3) That the concerned meetings of he creditors or members or any class of them had the relevant material to enable the voters to arrive at an informed decision for approving the Scheme in question. That the majority decision of the concerned class of voters is just and fair to the class as a whole so as to legitimately bind even the dissenting members of that class.

(4) That all necessary material indicated by section 393(1)(a) is placed before the voters at the concerned meetings as contemplated by section 391(1).

(5) That all the requisite material contemplated by the proviso to section 391(2) of the Act is placed before the court by the concerned applicant seeking sanction for such a Scheme and the court gets satisfied about the same.

(6) That the proposed Scheme of compromise and arrangement is not found to be violative of any provision of law and is not contrary to public policy. For ascertaining the real purpose underlying the Scheme with a view to be satisfied on this aspect, the court if necessary, can pierce the veil of apparent corporate purpose underlying the Scheme and can judiciously x-ray the Scheme.

(7) That the company court has also to satisfy itself that members or class of members or creditors or class of creditors, as the case may be, were acting bona fide and in good faith and were not coercing the minority in order to promote any interest adverse to that of the latter comprising of the same class whom they purported to represent.

(8) That the Scheme as a whole is also found to be just, fair and reasonable from the point of view of prudent men of business taking a commercial decision beneficial to the class represented by them for whom the Scheme is meant.

(9) Once the aforesaid broad parameters about the requirement of a Scheme for getting sanction of the court are found to have been met, the court will have no further jurisdiction to sit in appeal over the commercial wisdom of

the majority of the class of persons who with their open eyes have given their approval to the Scheme even if in view of the court there could be a better Scheme for the company and its members or creditors for whom the Scheme is framed. The court cannot refuse to sanction such a Scheme on that ground as it would otherwise amount to the court exercising appellate jurisdiction over the Scheme rather than its supervisory jurisdiction."

11. Mr.V. Prakash, learned Senior Counsel appearing for the appellant in O.S.A.No.309 of 2006, on behalf of Integrated Finance Company Depositors Association has raised several questions touching upon the pros and cons of the Scheme and has submitted that it would have been more appropriate for the Company to come out with any better offering as most of the deposit holders or the bond holders had practically invested their life time saving. He has painted a very dismal picture of the projections highlighted in the Scheme.

12. Since the Scheme has been approved by the learned single Judge, obviously the appellate court under ordinary circumstances should be slow to interfere with such discretionary order and should interfere only in case of any glaring illegality in the proceedings or material irregularity in the procedure adopted.

12.1 Keeping in view the scope of Section 391 of the Companies Act, we do not think that it is for the appropriate Company Court dealing with such application under Section 391 or for that matter and even far less, for the appellate court to go into the nitty-gritty of the various suggestions in the Scheme. It is indeed very difficult for the Company Court or the Appellate Court to consider the financial wisdom of a particular proposal because the courts are not equipped with necessary expertise and more particularly when the overwhelming majority of the bond holders and depositors had agreed to a particular proposal.

12.2 Law is well settled that a Company Court in such a scenario is not expected to substitute its own wisdom for that of the stake-holders, who give consent to a particular Scheme. Thus, wise or otherwise, a Scheme is ordinarily beyond the jurisdiction of the Company Court and the Appellate Court except in those rare cases where one can see that the Scheme itself on the face of it so unreasonable that no man of ordinary prudence can accept such a scheme.

12.3 In the facts of the present case, we do not think that we can characterise the Scheme as so outrageously improper as to invite the wrath of the Court.

13. While considering the question as to whether there has been procedural irregularity or not, Mr.V. Prakash, learned Senior Counsel, submitted that since most of the depositors were residents of the State of Kerala, it would have been more convenient for such depositors if the meetings of the depositors and the bond holders would have been held within the State of Kerala rather than at a distant place like Chennai.

13.1 Learned single Judge, while considering such submission, has observed that since the Registered Office of the Company is at Chennai, there was nothing illegal in directing the meetings to be held at Chennai and to ensure proper holding of the meetings, the Court had appointed an Observer.

13.2 Though it may be true that possibly any suitable place within the State of Kerala would have been more convenient, we do not think it would be appropriate on our part to set the scheme at naught merely because the meetings were held at Chennai, more particularly when there is no acceptable materials on record to indicate that the depositors and the bond holders within the State of Kerala found it difficult to attend the meetings at Chennai.

14. One other contention regarding procedural irregularity, however,which requires serious consideration, revolves round the order passed by the RBI vide letter dated 18.1.2005 and the effect of non-disclosure. Such letter refers to the fact that the RBI had conducted an inspection of the books of accounts in exercise of power under Section 45N of the RBI Act. The relevant portion of the letter is as follows :-

> "... The inspection revealed that the company has violated the provisions of the Reserve Bank of India Act, 1934 and the Directions issued thereunder as detailed below:
>
> i) Net Owned Fund (NOF) of your company was negative at (-) Rs.10666.06 lakh as on March 31, 2004 as against the reported NOF at Rs.2194.00 lakh. The working of the assessed NOF is furnished in Annexure-1. The company has thereby violated the provisions of Section 41-1A(1) of the RBI Act by not maintaining the statutory minimum required NOF of Rs.25 lakh.
>
> ii) As on March 31, 2004, the company's credit exposure to the following companies were in excess of 15% of the company's reported owned fund of Rs.2877.00 lakh as on September 30,2003.
>
> a. Sree Maruti Textiles Ltd (Rs.887.34 lakh)
> b. Ravishankar Industries Pvt Ltd. (Rs.789.96 lakh)
> c. Gemini Indus and Imaging Ltd (Rs.915.23 lakh)
> d. Gomathy spinners (Rs.724.98 lakh)

e. ATV Projects India Limited (Rs.998.46 lakh)
f. Krishna Petrochem Ltd (Rs.599.20 lakh)
g. Vatan Dyechem Exports Limited (Rs.471.41 lakh)

The company has thereby violated the provisions of Para 12 of the NBFC Prudential Norms (Reserve Bank) Directions, 1998 (hereinafter referred to as the Prudential Norms Directions).

iii) The company has not classified its assets in accordance with the asset classification norms stipulated by Reserve Bank of India (details of wrong classification of assets are furnished in Annexure-II). The company has thereby violated the provisions of paragraph 7 of the Prudential Norms directions.

(iv) Gross Non-Performing Assets of the company, assessed at Rs.15603.16 lakh, were very high and formed 69.31% of the total credit exposures of the company.

v) The company has not made adequate provision in respect of its Non Performing Assets as detailed in Annexure III. As a result, there is short provisioning to the extent of Rs.12575.33 lakhs. The company has thereby violated the provisions of paragraph 8 of the NBFCs Prudential Norms (Reserve Bank) Directions.

vi) As the NOF of the company is negative, it has not maintained the minimum capital adequacy ratio and has thereby violated the provisions of Paragraph 10 of the prudential Norms Directions. ..."

15. The contention raised by the learned counsel for RBI and the Senior Counsel for the appellant in OSA.No.309 of 2006 is to the effect that this vital aspect relating to the affairs of the company, which was under the scrutiny of the RBI had not been disclosed, even though under Section 391(2), the Company is required to disclose all relevant factors.

16. Section 391(2) of the Act envisages that if the Company files an application under Section 391(1), it should disclose in its affidavit the latest financial position, auditor's report and any investigation pending under Sections 235 to 251 and the like. According to the learned counsels for the appellants and more particularly the counsel for RBI, the appellant in OSA.No.308 of 2006, non-disclosure of an order relating to Section 45MB and regarding other aspects highlighted in the letter dated 18.1.2005, amounted to non-disclosure of an investigation initiated under Section 45MB of the RBI Act. It is further contended that at any rate since recording of compromise or agreement under Section 391 has

got far reaching consequences, the company is required to disclose all relevant factors which reflect upon its financial position so that the persons required to consider such scheme of arrangement or compromise would be in a position to take an informed decision based on the facts and circumstances.

17. Learned Senior Counsel appearing for the Company, on the other hand, submitted that as per the provisions contained in Section 391(2) of the Act, the company is required to disclose about any investigation pending under Sections 235 to 251 of the Act and it cannot be said that non-disclosure of a matter pertaining to Section 45MB of the RBI Act was in any way violative of the mandates contemplated under Section 391(2). It has been further contended that the direction of the RBI to the effect that the company should not receive any further deposit, has not been violated as the company has not accepted any deposit, but had received only bonds. It is submitted that since the respondent company was exempted from Chapter XII of the Public Deposits (Reserve Bank of India Directions) Act, it cannot be said that by receiving bond, any direction of the RBI had been violated.

17.1 The submission of the Senior Counsel for the Respondent is that there was no flouting of directions and the Company had clarified the questions in its correspondence.

17.2 The core question is not whether the Company had flouted some of the directions. The more important question is whether the Company should have disclosed the aspects arising out of the order dated 18.1.2005 to enable the depositors and the bond holders to take an informed decision.

18. While seeking permission of the Court for compromise, etc., as envisaged under Section 391 of the Act, the Company is required to act fairly and in a transparent manner. This includes the duty of disclosing all relevant facts and circumstances. It is true that technically speaking there was no investigation pending under Sections 235 to 251 of the Act. However, the fact that the RBI had initiated action contemplated under Section 45MB of the RBI Act and had issued several directions in the letter dated 18.1.2005, the relevant portion of which has already been extracted, was an important and relevant aspect which ought to have been disclosed in order to enable the depositors or the creditors to take an appropriate decision after being aware of all the relevant facts and circumstances. The requirement is for disclosure of any investigation pending under Section 235 to 251 and the like. This latter expression is indicative of the fact that the company is required to disclose about all relevant investigation or enquiry, even though such investigation may not be strictly under Sections 235 to 251 of the Companies Act.

19. In our considered opinion, non-disclosure of the action taken and initiated by the RBI as apparent from the letter dated 18.1.2005 amounted to non-disclosure of relevant facts required to be disclosed under Section 391(1) read with Section 393(1) of the Act, thus vitiating the bonafides of the Company and thereby violating the procedural safeguards.

20. The contention raised by Mr.T. Poornam on behalf of RBI and also supplemented by Mr.V. Prakash relating to the alleged illegality of the Scheme, however, stands on a still stronger footing. We now proceed to deal with such contention in greater detail.

21. Learned counsels have invited our attention to Chapter III-B of the RBI Act. This Chapter was inserted by way of amendment vide Act 55 of 1963. The heading of the Chapter is "Provisions relating to Non-Banking Institutions receiving deposits and financial institutions".

As per Section 45-I(aa) "company" means a company as defined in section 3 of the Companies Act, 1956 (1 of 1956), and includes a foreign company within the meaning of Section 591 of that Act.

As per Section 45-I(e) "non-banking institution" means a company, corporation or co-operative society.

As per Section 45-I(f) "non-banking financial company" means -
(i) a financial institution which is a company;
(ii) a non-banking institution which is a company and which has as its principal business the receiving of deposits, under any Scheme or arrangement or in any other matter, or lending in any manner;
(iii) such other non-banking institution or class of such institutions, as the Bank may, with the previous approval of the Central Government and by notification in the Official Gazette, specify.

21.1 Section 45-Q provides that the provisions of Chapter III-B shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by virtue of any such law.

21.2 Section 45-QA is as follows :-

> "45-QA. Power of Company Law Board to order repayment of deposit.- (1) Every deposit accepted by a non-banking financial company, unless renewed, shall be repaid in accordance with the terms and conditions of such deposit.

(2) Where a non-banking financial company has failed to repay any deposit or part thereof in accordance with the terms and conditions of such deposit, the Company Law Board constituted under Section 10-E of the Companies Act, 1956 (1 of 1956), may, if it is satisfied, either on its own motion or on an application of the depositor, that it is necessary so to do to safeguard the interests of the company, the depositors or in the public interest, direct, by order, the non-banking financial company to make repayment of such deposit or part thereof forthwith or within such time and subject to such conditions as may be specified in the order."

22. In the light of the above provisions, it is contended by the learned counsels appearing for the appellants that as per Section 45QA(1), every deposit accepted by a non-banking financial company is required to be repaid in accordance with the terms and conditions of such deposit, unless it is renewed. Learned counsels have further submitted that in the present case the Scheme has been mooted only with a view to avoiding repayment of the deposits and the Scheme contemplates that instead of repaying the amount in accordance with the terms and conditions of the deposit, such amount shall be considered as convertible debentures with interest at the rate of 6% which would be converted as equity shares within a period of one year. Such a provision contained in the Scheme or arrangement is against the provisions of Section 45QA(1) as the company is not repaying the amount, but issuing convertible debentures which has to be converted into equity shares.

23. Mr.Arvind P. Datar, learned Senior Counsel appearing for the Company, submitted that even under the Scheme, deposits are being repaid, though not in cash, but, in another form inasmuch as convertible debentures are being issued to them. He has further submitted that the expression "repaid" in Section 45QA does not mean that it must be repaid in cash and not by any other method and, in the present case, the repayment is contemplated in the shape of a convertible debenture. Mr.K.M. Vijayan, Mr.R. Viduthalai, Mr. Vijay Narayan, learned Senior Counsels appearing for various depositors' Associations, and Mr. Chandrasekhar, appearing for the employees' Association, have supplemented such submission.

24. On a careful consideration of the submissions made by the learned counsels of either side on this score, we are unable to accept such ingenious submission made by the learned counsels for the Company and others supporting the Scheme. Chapter III-B, which was inserted by way of amendment, has been obviously incorporated with a view to protect the depositors and to avoid exploitation by non-banking financial institutions. Section 45Q itself makes it very clear that the provisions of the Chapter III-B shall have effect

notwithstanding anything inconsistent therewith in any other law. The Companies Act as well as the RBI Act are Central Acts. Chapter III-B, which was inserted by Act 55 of 1963 with effect from 1.12.1964 is obviously a later legislative provision.

25. That apart, Section 45Q makes it very clear that the provisions contained in Chapter III-B shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force. It is therefore obvious that the provisions contained in Section 45QA, which are intended to protect the depositors must have primacy over any other law inconsistent with such provision. It may be that Sections 391 to 393, which are the specific provisions regarding Scheme of arrangement or compromise relating to any company, can be invoked in respect of a non-banking financial company. However, when such provisions for making a scheme of arrangement or compromise are invoked, it is obvious that the scheme of arrangement or compromise should not contravene any specific provision of law relating to non-banking financial company. As apparent from the decision of the Supreme Court in AIR 1997 SC 506 (cited supra), a scheme of arrangement / compromise, if it is illegal or opposed to public policy, cannot be sanctioned by the Court. The provisions contained in the Scheme, whereunder the statutory liability of a company to repay the depositors in accordance with the terms and conditions of the deposit is being flouted, cannot be considered as a legal clause meriting acceptance by the Court.

26. It appears that even if such an objection was raised before the learned single Judge as apparent from para 44 of the judgment, no specific answer had been furnished. It is of course true that while dealing with an allied contention raised by the counsel for the RBI regarding the violation committed by the Company in accepting the deposit in violation of the provisions of the Act, the learned single Judge has referred to Section 45QA, which recognises the power of the Company Law Board to order repayment of any such deposit, if it is necessary to safeguard the interest of the company.

27. In para 83 of the judgment, the learned single Judge has concluded :-

> "83. In this connection the learned counsel made a reference to the decision of the Karnataka High Court reported in (2005) 5 CLJ 78 (MAHARASHTRA APEX CORPORATION LT., Inre.) on the question of violation of the RBI Act while considering the plea for approval to the Scheme. It was decided therein that the provisions of Section 391 of the Companies Act being a complete code by itself, the violations projected as such could not stand in the way of granting the approval to the Scheme once the statutory

formalities stated in the Act are complied with. While it cannot be denied that the Court while granting approval to a Scheme does not sit as a Court of appeal, and once the formalities are complied with in the matter of granting approval, any violation spoken of as regards other enactments are matters which deserve consideration under the relevant provisions of that statute and on that score the approval to a settlement reached cannot be negatived. These provisions operate on different field. Consequently, the objection by the RBI is overruled."

28. As already indicated, the provisions contained in Chapter III-B shall have effect notwithstanding any other law to the contrary. This would obviously include Section 391 of the Companies Act. If the direct impact of a scheme of arrangement / compromise under Section 391 would be offending the provisions contained in Chapter III-B, to that extent, the Scheme under Section 391 must give way. Axiomatically any scheme of arrangement / compromise sought to be approved must be consistent with Chapter III-B of the RBI Act. Apart from the statutory obligation emphasised in Section 45QA of the RBI Act, jurisdiction has been vested with the Company Law Board to pass appropriate orders as contemplated under Section 45QA(2). However, that is a discretion exclusively vested with the Company Law Board and cannot be whittled down by taking recourse to Section 391 of the Act. By virtue of Section 45QA(2), the Company Law Board is now clothed with power to order repayment of the deposits accepted by a non-banking financial company in case of default in making payment of the principal amount with interest thereon. Such discretionary power of a statutory authority cannot be circumvented by the stratagem of an arrangement projected under Section 391 of the Act.

29. Mr. Arvind P. Datar, learned Senior Counsel, has also contended that the provisions similar to those contained in Chapter III-B of the RBI Act had been included in the shape of Section 58A in the Companies Act and Section 391 of the Companies Act being a specific provision in the very same statute, would be operative even in respect of the companies which are required to follow the provisions contained in Section 58A of the Act. Similarly, according to him, notwithstanding the provisions contained in Chapter III-B of the RBI Act, a scheme under Section 391 of the Act can be approved even in respect of non-banking financial companies.

29.1 We are not suggesting that Section 391 of the Act is not applicable to a non-banking financial company. What has been emphasised by us in the present judgment is that while entering into an arrangement or compromise under Section 391, such arrangement or compromise should be consistent with the statutory provisions, which may be contained in the very same Companies Act or may be contained in any other statute. In our considered opinion, if any scheme containing the arrangement or compromise is accorded sanction under

Section 391 of the Act, such scheme should be consistent with the mandatory statutory provisions. As already emphasised, in view of the provisions contained in Section 45Q, the provisions contained in Chapter III-B of the RBI Act including the provisions contained in Section 45QA(1) and (2) must be given their due importance.

30. Learned single Judge appears to have relied upon (2005) 5 CLJ 78 (cited supra) to come to a conclusion that Section 391 of the Act being a complete Code by itself, violation of any other provision cannot stand in the way of granting approval to the scheme once the statutory formalities are complied with.

31. We are unable to subscribe to such a view. The duty of the Court dealing with a matter under Section 391 of the Act is not confined to ensuring compliance with the procedural safeguards as contemplated under Section 391 and Section 393 of the Act. The Court must see whether the scheme of arrangement / compromise is not opposed to public policy or opposed to any law. In the present case, the Scheme, being contrary to the provisions contained in Section 45QA of the RBI Act, could not have been accepted. It may be true that the Company Law Board has jurisdiction to direct repayment of the deposit, but that is a matter which comes exclusively within the jurisdiction of the Company Law Board and cannot be abrogated or abridged by incorporating terms and conditions in a petition under Section 391 of the Act, which have the effect of nullifying the wholesome provisions contained in Chapter III-B of the RBI Act.

32. Learned counsel appearing for the contesting respondent has placed reliance upon a Division Bench decision of the Kerala High Court reported in Vol.99 Company Cases 2000 Page 54 (MRS. VILASINI JAYAPRAKSH v. ST. MARY'S FINANCE LTD.) in support of the contention that the provisions contained in Section 45QA of the RBI Act empowering the Company Law Board to give direction can be considered as subservient to the provisions contained in Section 391 of the Act.

33. In the aforesaid case, the Company Law Board in reference to application under Section 45QA(2) had indicated that since an application under Section 391 of the Companies Act, 1956 was pending, it was not appropriate for the Company Law Board to pass any order on the application filed under Section 45QA(2) till the disposal of the application under Section 391 of the Act. In the appeal taken to the High Court, the Division Bench held that this order passed by the Company Law Board was on the basis of the relevant consideration and the fact that proceedings under Section 391 was pending, cannot be considered as irrelevant. However, in our opinion, this decision does not go to the extent of laying down as a matter of proposition of law that, while dealing with an application under Section 391, the order recording an arrangement which is contrary to any statutory provision, can be accepted.

34. The importance of the jurisdiction vested with the Company Law Board under Section 45QA can also be gauged from the fact that if the order passed by the Company Law Board under Section 45QA (2) of the RBI Act is not complied with, the defaulting person can be prosecuted under Section 58B(4-AAA). It is of course true that under Section 58B(4-AAA) only the violation of the order passed by the Company Law Board is considered as punishable, but mere non-payment of the deposit within the time stipulated per se is not punishable. Though this fine distinction between 45QA(1) and an order under Section 45QA(2) is there, in our opinion, the ultimate effect in the present compromise is to render the provisions contained in Section 45QA nugatory.

35. It is no doubt true that the Company Law Board has certain discretion in the matter but, ultimately the Company Law Board, while deciding the matter under Section 45QA(2), has to take into account the relevant facts and circumstances and an order is required to be passed. At that stage, if such order is not complied with, prosecution is contemplated. The relevant factor to be considered here is, by virtue of the agreement the entire provisions contained in Section 45QA read with Section 58B(4-AAA) become practically redundant so far as the present company is concerned.

36. Keeping in view the over riding nature of the provisions contained in Chapter III-B of the RBI Act and the necessity felt by the Parliament to enact a specific provision for non-banking financial institutions, in our considered opinion, a compromise under Section 391 of the Act has to be in consonance of the provisions contained in Chapter III-B of the RBI Act including the provisions contained in Sections 45QA(2) and 58B(4-AAA) of the RBI Act.

37.The learned Senior Counsels representing some of the employees and the depositors have contended that by virtue of the action now approved by the learned single Judge, the company can continue to exist thereby protecting the interest of numerous employees as well as majority of the depositors, who had supported the Scheme.

38. We are afraid that in view of our conclusion that the Scheme being contrary to the statutory provisions and to some extent can even be said to be opposed to pubic policy, cannot be approved.

39. For the aforesaid reasons, the Original Side Appeals are allowed and the order of the learned Single Judge is set aside. Consequently, the connected miscellaneous petitions are closed. No costs.

Learned counsel for Respondent No.1 has prayed that he intends to file an appeal against this judgment before the Supreme Court and, therefore, operation of this judgment may be suspended for a reasonable period.

Learned counsel appearing for the appellant objected to this request stating that necessary prayer should be made before the appellate court.

In the peculiar facts and circumstances of the case, we suspend the operation of the judgment for a period of three weeks from to-day.

sd/-
Asst.Registrar

/true copy/

Sub Asst.Registrar

dpk

To
The Sub. Asst. Registrar, O.S., High Court, Madras.

+2 ccs To Mr.T.Suresh, Advocate, SR.25925
+2 ccs To Mr.P.V. Ravi Chandran, Advocate, SR.25763 & 26471
+4 ccs To Mr.P.H.Aravindh Pandian, Advocate, SR.26520 & 25940
+2 ccs To Mr.T.Poornam, Advocate, SR.25924

O.S.A.Nos.308, 309, 312 of 2006
and O.S.A.No.91 of 2007

ra [co]
gkg/8.5