

Bajaj Auto Ltd.

Vs

Company Law Board and Others

Bajaj Auto Holdings Ltd.

Vs

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Civil Appeals No. 3480 of 1986 With Nos. 3420-79 of 1986

(S. M. Quadri, B. N. Kirpal JJ)

22.07.1998

JUDGMENT

B. N. KIRPAL, J. -

1. These appeals by special leave arise from the common order of the Company Law Board (Respondent 1) which had partly upheld the decision of Bajaj Tempo Limited (Respondent 2) in declining to register the transfer of its shares in favour of M/s. Bajaj Auto Limited which had been purchased by the appellants. These are essentially two groups of shareholders which control these companies. While "Bajaj Group" has the control of the appellant, it is "Firodia Group" which controls Bajaj Tempo Ltd.

2. Bajaj Auto Limited (appellant in Civil Appeal No. 3480 of 1986) is the holding-Company of Bajaj Auto Holdings Limited (appellant in CAs Nos. 3480 and 3420-79 of 1986) and they, along with other individuals who were members of their group (all of whom are appellants in these appeals) are the existing shareholders of Bajaj Tempo Limited which is a public limited company. Bajaj Auto Limited purchased 50 shares of Bajaj Tempo Limited and Bajaj Auto Holdings Limited purchased 13,150 shares of the said Company. These purchases were made in the year 1983 through different brokers and they were sent to M/s. Bajaj Tempo Limited for transfer of shares in the appellants' names. By three different resolutions dated 29-8-1983, 27-9-1983 and 19-11-1983, the transfer of shares was rejected by Bajaj Tempo Limited. The minutes of the meeting dated 29-8-1983 contained the reasons for refusal to transfer and the resolution passed thereto. The relevant portion of the said minutes is as under :

"The Directors, therefore, after the deliberation and considering all aspects unanimously resolved not to approve the said transfers and declined to register the said transfers considering the facts briefly stated above and grounds briefly summarised as under :

(1) Further acquisition of shares of this Company by Bajaj Group if permitted will lead to interconnection between this Company and the companies of the Bajaj Group which is not desirable in the interest of this Company.

(2) The Bajaj Group is not acquiring the shares of this Company with a view to or for the purpose of genuine investments but with ulterior and oblique motives and purposes including with a view to destabilise the management of this Company.

(3) Bajaj Auto Limited and this Company are competitors in business inasmuch as both are manufacturing light commercial vehicles. The attempt of Bajaj Group to make inroads in this Company by acquiring large block of shares is to cause detriment and prejudice to the Company.

(4) In view of the facts stated above, although absolute discretion is conferred under the Articles of Association of the Company, the Board has carefully considered the matter and has decided to refuse to register the transfers. The transferees in the circumstances are also not desirable persons from the larger point of view of the interest of Bajaj Tempo Ltd., as a whole.

Therefore, the proposed transfers are not in the interest of the Company.

RESOLVED that in pursuance of Article 52 of the Articles of Association of the Company, the transfer of shares submitted in this meeting and hereinbelow mentioned be and are hereby not approved and the Board of Directors do decline to register the said transfers and the Secretary to give to the parties notice of this decision refusing the said transfers in the following terms :

"I have to advise that in the meeting of the Board of Directors held on 29-8-1983 the Board has decided that it will not give its approval to the transfer of the following shares. The transfer forms and share certificates are being returned under a separate cover."

3. It is for the same reason as above that the other transfers were declined by the resolutions dated 27-9-1983 and 19-11-1983.

4. Appeals were then filed by the appellants under Section 111 of the Companies Act, 1956 before the Company Law Board. On the basis of the pleadings before it and the submissions of the counsel for the parties, the Company Law Board formulated the following five issues for its consideration :

"1. Whether the appellants and the respondents are rivals in business ?

2. Whether the purchases of impugned shares were bona fide investments ?

3. Whether the appellants can be termed as undesirable persons ?

4. Whether apprehension of interconnection of the respondent-Company with Bajaj Group is well founded and whether it can be a good ground for refusal to transfer shares ?

5. Whether transfer of 7600 shares, sought to be transferred by Smt. Suman Jain was intra-group transfer and if so, whether the respondent-Company was justified in refusing transfer of these shares ?"

5. By a reasoned order, Issues 1, 3 and 5 were decided in favour of the appellants. It came to the conclusion that the appellants were not rival in business nor were they undesirable persons and by

registering the transfer of 7600 shares, which transfers were intra-group, there would be no change in the overall holding and, therefore, Bajaj Tempo was not justified in refusing the said transfer. Issues 2 and 4 were, however, decided against the appellants and the effect of this was that refusal to transfer 50 shares in favour of Bajaj Auto Limited and 5550 shares in favour of Bajaj Auto Holdings Limited was upheld.

6. In deciding Issue 2, the Company Law Board came to the conclusion that as Bajaj Auto Holdings Limited was an investment company, it was not convincing that it would invest in the shares of Bajaj Tempo by way of investment. It further came to the conclusion that the proposed investment in the shares of the respondent-Company by the appellants was to increase its shareholding and was motivated. It also noted that the return on the shares of the Company did not appear to be adequate enough warranting successive purchases of the shares by the appellants.

7. Dealing with Issue 4, the Company Law Board noticed that on 29-8-1983, the total holding of the appellants' group was about 23.2% in Bajaj Tempo Ltd. At that time, the interconnection limit under the Monopolies and Restrictive Trade Practices Act, 1969 (hereinafter referred to as "the MRTP Act") was 33 1/3% and the said limit has been reduced to 25% w.e.f. 1-8-1984 as a result of amendment in the MRTP Act. The Company Law Board was of the opinion that even though at the time of lodgement of shares the said amendment had not been made, there was a feeling prevalent in trade and industry that the interconnection limit would be reduced to 25%. It then held that the limit up to which shares may be allowed to be acquired by any group in the shareholding of the respondent-Company in such circumstances, has to be the subjective opinion of its Board of Directors and when the acquisition of the appellants "had already reached critical limit of over 23%, which is not widely off the mark of 25%, the apprehension existing in the mind of the Board of Directors of the respondent-Company cannot be assailed". It, therefore, concluded that the apprehension of Bajaj Tempo Ltd. that it was likely to get interconnected with the appellants, in the event of impugned transfer of shares being allowed, was not baseless or ill-founded.

8. Assailing the aforesaid decision of the Company Law Board, Shri Shanti Bhushan and Shri Harish Salve, learned counsel for the appellants, submitted that the power of the Directors to refuse transfer is by way of an exception to the rule that the share transfer should generally be accepted by a listed company. Impugning the findings in connection with Issues 2 and 4 of the Company Law Board, it was contended that the conclusion of the Board that the return by way of dividend on the shares was very low is not the only relevant factor in order to determine whether the purchase of shares was by way of investment. An important factor which has been ignored by the Board was that capital appreciation was more than ample to offset the low dividend return. It was submitted that refusal to transfer was not in the interest of the Company and the non-transfer by the Firodia Group, which controls Bajaj Tempo, was with a view to protect that group's personal interest. It was also submitted that even if the transfers were allowed, the shareholding of the appellants would be below 25% limit. In this connection, it was submitted that it was in the hands of Bajaj Tempo Ltd. to avoid interconnection if any more transfers of shares was sought for, if with the said transfer the transferability would reach the limit of 25%. Our attention was also drawn to the fact that at the relevant point of time, Bajaj Tempo was already a company to whom the provisions of Chapter 3 of the MRTP Act applied by virtue of the provisions of Section 20(a) of the said Act inasmuch as its assets exceeded 20 crores and, therefore, interconnection would not have made any difference. For the view we are taking, it is not necessary to refer to or deal with the other contentions raised by the learned counsel for the appellants.

9. The crucial question is, as to what is the power and scope of the directors to refuse to register the

transfer of shares in the case of a public limited company whose shares are listed on the Stock Exchange. In declining to register the transfer of shares, power is sought to be derived from Article 52 of the Articles of Association of the Company which reads as follows :

"52. The Board may at its own absolute and uncontrolled discretion decline to register or acknowledge any transfer of shares, and in particular, may so decline in any cases in which the Company has a lien upon the shares or any of them, or whilst any moneys in respect of the shares desired to be transferred or any of them remain unpaid, or unless the transferee is approved by the Board, and such refusal shall not be affected by the fact that the refused transferee is already a member. The registration of a transfer shall be conclusive evidence of the approval of the transferee by the Board :

Provided that the registration of any transfer shall not be refused on the ground of the transferor either alone or jointly with any other person or persons indebted to the Company on any account whatsoever except as stated above."

10. The power of the Board of Directors to refuse registering the transfer of shares is now settled when these two adversaries had an earlier round of litigation which culminated in the decision reported as *Bajaj Auto Ltd. v. N. K. Firodia* ((1970) 2 SCC 550). That was the case where Firodia Group (who controls Bajaj Tempo Limited) had applied to Bajaj Auto Limited, one of the appellants in this appeal, for transfer of shares of Bajaj Auto Limited which had been purchased by the Firodia Group. The Board of Directors of Bajaj Auto Limited refused to register the transfers, inter alia, stating that N. K. Firodia and his representatives had acted against the interest of the Company and that it was in the interest of Bajaj Auto to refuse the transfer. The Company Law Board directed Bajaj Auto to register the transfer which led to the filing of the appeal in this Court. Bajaj Auto had placed reliance on its Article 52 of the Articles of Association, which was identical to Article 52 of Bajaj Tempo, and it contended that it gave the Directors absolute and uncontrolled discretion to decline to register any transfer of shares. Dealing with the question relating to the discretion of the Directors, it was observed at pp. 554-55 as follows : (SCC para 12)

"12. Article 52 of the appellant-Company provided that the Directors might at their absolute and uncontrolled discretion decline to register any transfer of shares. Discretion does not mean a bare affirmation or negation of a proposal. Discretion implies just and proper consideration of the proposal in the facts and circumstances of the case. In the exercise of that discretion the Directors will act for the paramount interest of the Company and for the general interest of the shareholders because the Directors are in a fiduciary position both towards the Company and towards every shareholder. The Directors are therefore required to act bona fide and not arbitrarily and not for any collateral motive."

This Court then observed that where the directors give reasons, the Court would consider whether they were legitimate and whether they proceeded on a right or wrong principle. In such a case, the reasons of the directors have to be decided from three points of view. Firstly, whether the directors acted in the interest of the company; secondly, whether they acted on a wrong principle; and, thirdly, whether they acted with an oblique motive or for a collateral purpose. In this connection, reference was made to the observations of this Court in *Harinagar Sugar Mills Ltd. v. Shyam Sunder Jhunjhunwala* (AIR 1961 SC 1669 : (1962) 2 SCR 339 (1961) 31 Comp Cas 387) where it was observed that "the discretion of the directors would be nullified if it were established that the

directors acted oppressively, capriciously or corruptly or in some other way mala fide". After referring to some English decisions, this Court in Bajaj Auto case ((1970) 2 SCC 550) at p.557 observed thus : (SCC para 21)

"21. It follows that where the Directors have uncontrolled and absolute discretion in regard to declining registration of transfer of shares, the court will consider if the reasons are legitimate or the directors have acted on a wrong principle or from corrupt motive. If the court found that the directors gave reasons which were legitimate, the court would not overrule that decision merely on the ground that the court would not have come to the same conclusion."

The Court then examined the facts of that case dealing with three reasons given by the Bajaj Auto for refusing to transfer the shares. It observed that the Directors had a hostile feeling against Firodia and they had the dominant desire to keep Firodia out of the Company. They did not act in the interest of the Company and their discretion was tainted by unfair conduct and unjustifiable attitude against Firodia. The Court rejected the ostensible reasons which were given for refusing the transfer of shares and it observed (at SCC p.560, para 29) that

"the reason given by the Directors was a camouflage to cover their collateral and corrupt motive of preserving the hegemony of the Bajaj Group. The motive is corrupt because the Bajaj Group acted for their personal interest and not in the bona fide general interest of the Company".

Dealing with the third reason, it was observed as follows : (SCC p.560, para 30)"

30. The third reason given by the appellant-Company was that the shares were being acquired by the Firodia Group not with a view of bona fide investment but with a mala fide purpose and evil design of obstructing the business of the appellant-Company. Acquisition or transfer of shares under the articles of the present case does not suffer from any restrictive impediment like pre-emption or personal objections to the transferees. There is no evidence that the transferees belonged to a rival concern. Equally, there is no evidence that the Firodia Group ever obstructed in the management of the Company. On the contrary, the Firodia Group advanced large sums of money. Firodia was largely responsible for the gradual growth of the appellant-Company and for the a prosperity of the Company. It was therefore an abuse of the fiduciary power of the Directors to refuse to register transfer of shares."

In the end, this Court noted that the refusal to register the shares was a sequel to the termination of the appointment of Firodia as Chief Executive and it is manifest that the Director acted for collateral reasons and in their own interest.

11. The shoe now is on the other foot. Whereas in the aforesaid case, it is Bajaj Auto which had refused to register the transfer of the shares in favour of N. K. Firodia & Group, in the present case, it is the N. K. Firodiacontrolled company namely Bajaj Tempo which has refused to register the transfer of shares in favour of Bajaj Auto and its subsidiary company. The strained relationship between the groups, and the animosity among them, has been clearly brought out in the aforesaid judgment of this Court.

12. Mr. R. F. Nariman, learned counsel for Respondent 2, however contended that there were no

personal reasons for declining to register the transfer of shares in favour of the appellants. In this connection, he submitted that during the period September 1982 to July 1983, the Directors of Bajaj Tempo Limited had approved the registration of as many as 42,350 shares in favour of the appellants. It was contended that the Board of Directors of Bajaj Tempo Ltd. had acted in bona fide and reasonable manner even though the share acquisitions by the appellants were part of a plan of action on its part to acquire a large block of shares of Bajaj Tempo Limited. He submitted that it is only when the said share acquisitions had crossed the limit of 24% and a razor-thin margin remained before the danger limit of 25% was reached that the Board decided to draw a line and to put an end to any further share acquisition by the Bajaj Group, leaving an extremely slender margin of safety of only about 0.7%. He further submitted that the Board of Directors had acted bona fide in rejecting the share transfer and the Court should not interfere even though it may not agree with the decision of the Board. There was a genuine apprehension, it was submitted, that if the appellants were directed to continue to acquire further shares in Bajaj Tempo Limited, it might result in the Company becoming interconnected with the Bajaj Group which would result in highly adverse consequences for the Company.

13. We have to consider whether the said apprehension in the mind of the Board of Directors of that Company was genuine and was it the real reason for rejecting to register the transfer of shares. In other words, what has to be determined, keeping in mind the principles enunciated by this Court in Bajaj Auto Ltd. case ((1970) 2 SCC 550) is whether the Board of Directors had acted in the interest of the respondent-Company.

14. As we see it, the power of the Board of Directors to refuse registration of transfer of shares must be in the interest of the Company and the general body of shareholders. No doubt in the year 1983, Section 82 of the Companies Act provided that the shares or other interest of any member in the company shall be moveable property, transferable in the manner provided by the articles of the company. Article 52 sought to give absolute and uncontrolled discretion to the Board of Directors to decline to register or acknowledge any transfer of shares. Even then, as already held in Bajaj Auto Ltd. case ((1970) 2 SCC 550) the Board has to act bona fide, and not arbitrarily and for the benefit of the company as a whole. In the case of a public limited company which is listed with the Stock Exchange, an important right of the shareholder is to be able to sell his shares at a favourable price. It is seldom in the interest of the general body of shareholders that transfer of shares be refused because that will have an adverse impact on the market price of the shares. Free transferability of shares will not artificially deprive its market price. This does not mean that if there is a good reason, then the Board has no power to refuse to register the transfer of shares. This Court while examining the action of the Board of Directors is not expected to exercise original appellate jurisdiction and sit in appeal on question of fact. The judicial review while hearing in appeal from the decision of the Company Law Board would be limited to see whether there was a bona fide exercise of power by the Board of Directors while refusing to register the transfer of shares.

15. The Company Law Board in the present case came to the conclusion that at least two of the reasons stated by the Company while refusing to register the transfer of shares were not correct. It held that the appellants and Bajaj Tempo were not rivals in business and even though there was hostility between the managements of the companies, but that by itself could not mean that the appellants were undesirable persons in the matter of transfer of shares. The only two reasons of the Directors which found favour with the Company Law Board were that the appellants were not bona fide investors and, secondly, there was a genuine apprehension about interconnection of the respondent-Company with the appellants.

16. Reverting to Issue 2, we find that in the resolution of 29-8-1983, what had been stated was that the appellants were not acquiring the shares with a view to or for the purpose of genuine investment "but with ulterior motives and purposes including with a view to destabilise the management of this Company". The alleged reason, therefore, was that the shares were being purchased with ulterior motives and purposes and with a view to destabilise the management of the Company. The Company Law Board appears to have misunderstood this reason and framed the issue as "whether the purchases of impugned shares were bona fide investments". It opined that being an investment company, it was not convincing that the appellants would prefer to invest in the shares of the Company other than the respondent-Company and the purchases were made so as to increase its shareholding in the respondent-Company and are, thus, motivated. It also observed that the return on the shares of the respondent-Company did not appear to be adequate enough warranting successive purchases of its shares and appeared to be lacking in bona fide. In our opinion, this was not a correct approach. Merely because the appellants wanted to increase the shareholding cannot by itself be a ground in law for refusing to transfer the shares. Realising this in the resolution of the Board of Directors, it was alleged that the purchase was not by way of genuine investment but was made with ulterior/oblique motives and with a view to destabilise the management of the Company. There is nothing placed on the record which can possibly persuade anyone to come to the conclusion that the intention of the purchase of shares by the appellants was with a view to destabilise the management of the Company or with an ulterior/oblique motive. Prima facie, it appears to us that even if it is assumed that the appellants were trying to purchase shares with a view to get a controlling interest in the Company, that itself cannot be a ground for refusing to transfer the shares unless and until it can be shown that the purchasers were undesirable persons and after gaining control of the Company, they will act against the Company and the shareholders' interest. In the instant case, the appellants would not even have 25% shares of the Company even if the transfer of shares was registered and, therefore, the threat to the management, assuming that could be a valid reason, could not be regarded as genuine.

17. It was submitted on behalf of the appellants that the Company Law Board overlooked the fact that the return on the investment of such shares is not only by reason of dividend which is obtained but the main income which was expected to arise was from the appreciation in value of the shares. It was submitted by the learned counsel for the appellants that at the time when the purchases were made, the share price was around Rs. 145 per share and presently, it is around Rs. 210 per share. In our opinion, there is merit in this contention. Price appreciation, which may in future lead to issuance of bonus shares or right shares, in the event of increase in capital, is a very valid and good reason for purchasing shares of reputable companies by an investor. Therefore, the reason, which is given for refusing to transfer the shares namely inadequate return on shares, cannot be regarded as being bona fide.

18. As regards the fear of being regarded a dominant undertaking, in the event to there being interconnection between the appellants and the respondent-Company is concerned, it has been contended on behalf of the appellants that the sections pertaining to concentration of economic power in Chapter III of the MRTP Act, i.e., Sections 25 and 26 have been omitted w.e.f. 27-9-1991 and, therefore, as of today, it would make no difference and the said reason cannot be regarded as valid. While it is true that the fear of the respondent-Company being regarded as a dominant undertaking as of today may not arise but what has to be seen is as to whether this could be a genuine apprehension in the mind of the Board of Directors when in 1983, they had declined to register the transfer of shares. The admitted fact is that as on that date, interconnection could have been established only if the appellants had acquired 33 1/3% shares of the respondent-Company. But, it is contended that in view of the Sachar Committee's Report, the Company apprehended that

the Act would be amended so that instead of 33 1/3% shares, it should be 25%. We would, therefore, proceed on the assumption that the figure of 25% had to be avoided by the respondent-Company.

19. It is an admitted fact that even if the purchase of the shares was registered, the total percentage of the holding of the appellants' group would be short of 25%. The existing shareholding at that time was 23.232% and had the transfer of shares been registered then, according to the figures supplied by Mr. Nariman at the time of hearing, the percentage of the holding of the appellants' group would have risen to only 23.408%. The learned counsel for the appellants are right in contending that if fear of the interconnection was the real reason in refusing to register the transfer, then such a reason could not exist at that moment because even with the registration of the transfer, the total mark of 25% would not be reached. We are in agreement with the appellants' submission and are of the opinion that if the number of shares which were purchased had been such that the total mark of 25% could be reached, then the action of the Board of Directors could not have been faulted. But with the registration of the transfer of shares in question, that danger mark would not have been reached. We are unable to accept as correct the appellants' (sic respondents') contention that because the total holding of the appellants' group would then become "dangerously close" to 25%, it was a good enough reason to refuse transfer. There may not have been anything to prevent the Company if, after the shares in question had been registered, any further purchase of shares was made which would have the effect of pushing the holding of the appellants to 25% mark, to reject those subsequent transfers. As the transfers in question would not have resulted in reaching the 25% mark, that cannot be regarded as a valid reason or consideration for refusing the registration of transfer of shares.

20. Faced with this, Mr. Nariman, learned counsel, however contended that because of the provisions of the MRTTP Act in determining the interconnection, the shares held by a financial institution are required to be excluded. He submitted that even if the appellants did not purchase any further shares, but further purchase by financial institutions of more shares could possibly lead to the same result namely of the percentage of holding of the appellants' group going beyond 25%. While it is true that the shareholding of the financial institutions is not to be taken into account in determining whether or not two or more bodies corporate are under the same management because of Explanation IV to Section 2(g) of the MRTTP Act, we find that if the shares in question had been registered, and the existing shareholding of the financial institutions excluded, then the total percentage of shares of the appellants' group would come to only 24.405%. For this percentage to push up to 25%, the financial institutions would have to acquire approximately 27,740 additional shares of Bajaj Tempo Limited, which may not be very likely. In any case, if such a situation did arise namely financial institutions purchasing more shares which would result in the danger mark of 25% to reach, there is nothing in law which would then prevent the Board of Directors of Bajaj Tempo Limited to refuse the registration of transfer in favour of financial institutions. In other words, just as the Directors can refuse to register transfer of shares in the appellants' name in order to avoid interconnection, similarly, and for the same reason, they could refuse to register transfer of such further purchases by financial institutions if such purchase would have had the effect of making the appellants interconnected with Bajaj Tempo Limited. The Company Law Board was, therefore, wrong in rejecting the contention of the appellants that the apprehension of the respondent-Company that it was likely to get interconnected with the appellants in the event of the impugned transfer of shares being allowed was baseless and/or ill-founded.

21. In order to see whether the Board of Directors had acted in furtherance of a personal interest or in the interest of the Company, the resolution dated 29-8-1983 should be read as a whole. It is

apparent that being aware of the state of law, every possible reason was stated in this resolution which could justify the Directors in refusing to register a transfer. Of the four reasons given by the Board, two of them were rejected by the Company Law Board, namely that the appellants were competitors of Bajaj Tempo Limited and that the transferees were not desirable persons from the larger point of view of interest of Bajaj Tempo Limited. There is also nothing on record to show that the purchase of shares by the appellants was with ulterior/oblique motives and purposes and with a view to destabilise the management of the Company. Lastly, we find that the acquisition in question would not have led to the interconnection between the companies and it was not a bona fide exercise of power by the Directors to take into account "further acquisition of shares" of Bajaj Tempo Limited which may take place in future which may then lead to interconnection. It is the extent of shareholding at that point of time which had to be taken into consideration and not future acquisition which may or may not take place. It was submitted by the appellants' counsel that because of the provisions of Section 108-A of the Companies Act as it stood at that time, further acquisitions could not take place so as to bring up the shareholding to 25% without first getting Central Government approval. We, however, need not examine this aspect because, in our opinion, on the facts which existed on the record, we are satisfied that the exercise of discretion by the Board of Directors in refusing to register the shares in the name of the appellants was not bona fide or in the interest of the Company or the general body of shareholders. Accordingly, its decision not to register the transfer of shares was not correct.

22. For the aforesaid reasons, the appeals are allowed. The impugned order dated 28-7-1986 of the Company Law Board is set aside and the resolutions dated 29-8-1983, 27-9-1983 and 19-11-1983 of M/s. Bajaj Tempo Limited are set aside and as a consequence thereof, direction is given to Respondent 2 to register the shares in question within four weeks from the date of this judgment. The appellants will be entitled to cost.