

In Re: Jersey India Ltd.

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Court : Company Law Board CLB

Decided On : Feb-12-1997

Reported in : (1997)88CompCas864

Judge : A Ramanathan

Appellant : In Re: Jersey India Ltd.

Judgement :

1. This is a unique petition filed by Jersey India Limited (hereinafter called "the company") under Section 79 of the Companies Act, 1956 (hereinafter called "the Act"), praying for sanction for issue of 23,88,000 equity shares of Rs. 10 each at a discount of 16.67 per cent, as authorised by the resolution of the company passed at its annual general meeting held on September 30, 1996.

2. The facts in this case are that the company was incorporated in October, 1992, and has a paid-up capital of Rs. 10,60,07,000 as on the date of the petition. The above capital was after a public issue of Rs. 482 lakhs made in 1994, which was over subscribed at that time by 15.94 times. The shares of the company are listed on the recognised stock exchanges at Delhi and Mumbai. There are about 20,378 shareholders in the company with break-up as follows : The company in accordance with its defectives set up a plant to produce knitted and dyed fabrics intended for, exports. Due to severe recession in the export market towards the end of 1994, the company ended up with lower price realizations and longer credit periods and a loss of Rs. 260.68 lakhs in the first year of operation, i.e., June 30, 1995. In the second year ended June 30, 1996, a further loss of Rs. 108.98 lakhs

was suffered. Although the company has now improved its turnover substantially and has achieved cash-break even the company's working capital requirements increased and there was a severe cash crunch.

3. According to the company at present, it has additional working capital requirement of about Rs. 200 lakhs. The company approached the ICICI, the lead financial institution for a bridge loan for this amount which was not agreed to. In order to avoid huge interest burden on borrowings, the board of directors of the company have decided to raise funds by issue of 19,90,000-1 per cent, non-cumulative convertible, preference shares (NCCP) of Rs. 10 each aggregating to Rs. 199 lakhs on private placement/ preferential allotment basis to persons other than the promoters, their friends, relatives and associates to be compulsorily converted within 18 months into 23,88,000 equity shares of Rs. 10 each in the ratio of 12 equity shares of Rs. 10 each for every 10-1 per cent, non-cumulative convertible preference shares, resulting in the allotment of equity shares at a discount of 16.67 per cent. This decision is in consultation with the merchant bankers as the condition of the capital market is not conducive to public issue of shares. The current market price of the company's equity shares is ruling between Rs. 3 to 4 per share. In order to keep the cost of raising funds to, the minimum, it is not expedient to issue rights shares. The non-cumulative convertible preference shares will not be listed but the equity shares on conversion will be got listed. Accordingly, the consent of the shareholders under Section 81(1A) for issue of 19,90,000 non-cumulative convertible preference shares in terms of the relevant SEBI 'guidelines through a resolution under Section 79 of the Companies Act has also been passed by the company.

4. After the receipt of the petition notice was issued to the Registrar of Companies to file a status report with regard to the affairs of the company as well as his comments on the present petition. The report received from the Registrar of Companies confirms some of the facts as narrated in the petition. However, he had called for certain additional information from, the company which also has been submitted by the company. The Additional Registrar of Companies was also, present during the hearing of the petition. Shri U. P. Mathur, advocate, reiterated the contents of the petition, cited a precedent from a decision of the Southern

Bench of the Company Law Board in this regard and urged that the prayers be granted.

5. The facts as stated in the petition indicate that the company has been primarily established for export of textiles. It is also noted that the company's exports has increased from year to year. As such the company has a potential for earning foreign exchange. The company has been constrained due to recessionary conditions in the export market in the initial two-year period. Due to the losses incurred in the first and second year, the company has encountered working capital crisis.

The total cash loss during the first two years amounted to Rs. 161.6 lakhs. In the current year, i.e., 1996-97, the company has reported an export turnover of Rs. 217 lakhs in the first quarter itself as against the export turnover of Rs. 155.66 lakhs and Rs. 338.42 lakhs in the previous two years as a whole. As such the trend of the export turnover appears to be encouraging. The company's case for additional working capital due to loss in the initial period is reported to be not favourably considered by the lead financial institution. In the circumstances the company is justified in exploring the capital market for increasing its share capital with an issue of additional 1 per cent, non-cumulative convertible preference shares which in the short run will be least burdensome in terms of cost of finance for the company. Moreover, the company in view of the present capital market conditions has been well advised not to offer the shares to the members or to the public. This is particularly because the market price of the existing equity shares hovers around Rs. 3 to 4. By issuing the non-cumulative convertible preference shares the funds made available to the company will be practically cost free at least for a period of 18 months till they are converted into equity shares. As such broadly the proposal appears to be in the interest of the company.

6. Though the proposal under consideration may not require any further tests to be applied for sanction of the issue of shares at a discount, in view of the precedents cited by Shri U. P. Mathur, since the applicant company is a listed Company and the shares are being offered on private placement basis, it is necessary to consider the following issues at length : The preference shares are proposed to be

converted into equity shares at the rate of 12 equity shares for 10 preference shares which amounts to a conversion at a discount of 16.67 per cent. Section 79 of the Act provides that normally the Company Law Board shall not sanction a higher percentage beyond 10 per cent, unless there are special circumstances. In this case, the company has justified the special circumstances, viz., the depressed market conditions and prevailing very low market price for the share.

Besides this, the company has also highlighted the export potential of the products of this company. As per the prospectus of the company issued in 1994, there is also an export obligation to the extent of US dollars 128.44 lakhs within five years. As such the special circumstances as contemplated in the proviso under Section 79(2) of the Act do exist. Further, it is also noted that with the normal dividend on preference shares at 15 per cent, any allottee could have gained in case of cumulative preference shares a dividend of 21.6 per cent, over the period, of 18 months, whereas in the present case even assuming a dividend is paid for 18 months the same could only be 1.5 per cent. Thus, effectively, there will be a 21 per cent, sacrifice on the part of the subscriber to these preference shares against which he gets a benefit of a discount of 16.67 per cent. As such the quantum of discount appears to be justified.

In case these preference shares are subscribed for by the promoters of the company the percentage of shareholding of the promoters group is likely to go up substantially. This acquisition of additional holding in a listed company by the existing controlling group has to be viewed with disfavour in the light of the present regulations regarding substantial acquisition of shares. Though it is contended in the petition that these shares are being allotted to parties other than the promoters, in case these parties are identified as part of the promoters group, appropriate approvals from the concerned authorities should be obtained.

As per the terms of the issue though the 1 per cent, non-cumulative convertible preference shares will not be listed in the stock exchanges, the converted equity shares would be listed in the stock exchanges. Since the existing equity shares of the company are listed, in case the proposed shares fail to get listed it may create an anomalous situation. If these shares are sold to investors without the clear

distinction that they are unlisted the investors are liable to be burdened with ill-liquid securities. It is the burden of the company to get these shares listed within ten weeks from the conversion of the non-cumulative convertible preference shares into equity shares as provided in Section 73 of the Act.

Accordingly, a suitable condition for sanction is incorporated herein.

Though the company has complied with the requirements of Section 81(1 A) of the Act, being a listed company it may be required to comply with the requirements of the stock exchanges, the SEBI and other concerned authorities. The present sanction does not exempt the company from other compliances as may be required.

" Section 79 contemplates sanction in respect of issue of shares within two months of sanction. The Section has not contemplated a conversion at a discount as such nuances in corporate capital structuring perhaps were not in contemplation earlier. However, the objective behind the legal provision being what it is and since the power to allow more time is vested in the Company Law Board, the sanction relating to conversion at a discount is not beyond the scope of the Section . It is also noted that the company cannot postpone this application for sanction of discount since the party who subscribes to the preference shares which will be automatically converted into equity shares would like to ensure that the availability of discount is a certainty. The company could not also issue the equity shares straightaway at a discount as that would deflate the promoters holding substantially below 25 per cent, as the new shares will be allotted to outsider parties.

7. Keeping in view the above, sanction is hereby accorded to the company to issue 23,88,000 equity shares of Rs. 10 each at a discount of 16.67 per cent, on the conversion of the proposed issue of 19,90,000--1 per cent, non-cumulative convertible preference shares of Rs. 10 each within 18 months from the date of such issue. This sanction will be valid for a period of two months after the expiry of the period of 18 months of issue of non-cumulative convertible preference shares.

The sanction shall, however, be subject to the following conditions, namely :-- (i) The percentage holding of the promoters group shall not be increased by the process of this issue.

(ii) The converted equity shares shall be listed in the stock exchanges of Delhi and Mumbai within ten weeks of conversion.

(iii) The company shall comply with all other statutory requirements relating to the issue of the proposed shares.

(iv) This order shall be valid for a period of 22 months from the date of issue or for a period of two months after the expiry of 18 months of the issue of the non-cumulative convertible preference shares whichever is earlier.

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