

DICTUM

“Summary of Judicial Pronouncements”

PRIOR SPECIAL RESOLUTION required to convert Loan into Share Capital

– Raj Singh Chopra and others v. Jagat Singh Chopra and Vikram Singh Chopra

[National Company Law Appellate Tribunal, New Delhi, Company Appeal (AT) No. 360/2017]

[January 23, 2018]

BACKGROUND

In Raj Singh Chopra vs. Jagat Singh Chopra, Freyaship Services Private Limited and Raj Singh Chopra filed company petition against the order passed by NCLT Kolkata wherein the impugned order cancelled the purported allotment of 26,000 equity shares issued against Loan outstanding in favour of Mr. Raj Singh Chopra. The learned counsel argued that NCLT could see from the record that enhancing capital base of the company was in the interest of the company but still went on to cancel the purported allotment made in favour of Mr. Raj Singh Chopra. Also, Mr. Raj Singh Chopra had extended loan to the company when Section 81 of old Act was applicable and when conversion was made, then it should be done according to the old act only and not as per new act.

Section 81 of the Companies Act, 1956 (‘old act’), now Section 62(3) of the Companies Act, 2013 (‘new act’), provides the mechanism for conversion of debentures or loans into shares of the company. The old Act specifies that there is no requirement of passing **SPECIAL RESOLUTION** at the time of raising money for conversion of loans or debentures into shares of the company. The New Act, which is effective from April 1, 2014, mandates that company to pass **PRIOR SPECIAL RESOLUTION** having option to convert such debentures or loans into Shares of the Company and Section 117(3)(a) of the Companies Act, 2013 mandates Company to file Form MGT-14 with the concerned ROC within prescribed time.

In the case *Raj Singh Chopra and others v. Jagat Singh Chopra and Vikram Singh Chopra*, the NCLAT upheld the decision of NCLT, and ruled that when the new act is in force and conversion of loan has to be done, the conversion would be permissible only as per the new provisions. In view of Section 62(3) when the question of issue of further share capital is taken up, conversion of loan into share capital would be permissible provided there was special resolution passed by the Company in General Meeting which granted option as a term attached to the loan raised by the Company permitting conversion of such loan into share of the Company.

Issues of the Case

1. Whether Loan can be converted into Share Capital of the Company without prior special resolution at the time of availing such loan?
2. Whether loan availed at the time before April 1, 2014 require prior Special Resolution as well?

Tribunal’s Ruling

NCLT in *Raj Singh Chopra and others vs. Jagat Singh Chopra and Vikram Singh Chopra* (‘Case’) held that:

1. The Company can convert the loan into Share Capital of the company only if the company had passed **special resolution** at the time of raising such Loan and Company has a proof that such resolution was passed during that time.
2. There is nothing to show that such resolution had been passed at the time of raising of Loan and the requirement to file Form MGT-14 for submission of Special Resolution with ROC had been followed, prior to the raising of the Loan.
3. NCLT invoked section 62(3) of the Companies Act, 2013 even when the loans were raised before new act was not in force and cancelled the allotment of 26,000 Equity Shares allotted to Mr. Raj Singh Chopra against the Loan Outstanding.

Appellate Tribunal’s Ruling

NCLAT holds that it will not interfere with NCLT order stating that:

1. There is no substance in the argument of the learned counsel for the Appellants that Section 62(3) of the Companies Act, 2013 could not have been applied as Loan was raised, Section 81 of the Companies Act, 1956 was enforceable and no such requirement of passing Special Resolution prior availing such Loan.

Our Views

1. Conversion of Loan or Debentures into Share Capital of the company requires passing of **Special Resolution** at the time of raising such Loan or issuing such Debenture.
2. Passing of special resolution will not be diluted considering the fact that Loan has been raised or Debentures had been issued prior to applicability of Companies Act, 2013.

Let’s Talk

For a deeper discussion on how this issue might affect your business, please contact:

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