ORIGINAL CIVIL.

Before Mrs. Justice Sujata Manohar

NORMAN J. HAMILTON *v.* UMEDBHAI S. PATEL.*

Sale of Goods Act, (III of 1930), Secs. 59—Securities Contracts (Regulation) Act (XLII of 1956), Secs. 13, 2(h), 2(i) and 21—Suit for payment of instalments of price for sale of shares in a private limited company. Defence that plaintiffs had represented that there was no existing liability of the company and the Tax authorities had made heavy demands in respect of tax dues of the company for a period prior to sale of shares—Whether under s. 59 of the Sale of Goods Act the defendants were entitled to reduction in price in view of discoveries of debts and the entire price is extinguished—Absence of particulars of damages by way of set-off—Bombay High Court (Original Side) Rules, 1957, rr. 135 and 136—Whether contract for purchase of shares was illegal under the provisions of Securities Contracts (Regulation) Act, 1956—"Marketable Securities"—Noscitur sociis.

If more than a year after the agreement the tax authorities reopened the assessments of the company, it cannot be said that the plaintiffs had made a wrong representation that there was no existing liability. But even assuming that the plaintiffs had committed a breach of condition, which the defendants had treated as a breach of warranty, under s. 59 (*1*) (*a*) of the Sale of Goods Act, 1930 it was open to the buyer to set up against the seller the breach of warranty in diminution or extinction of the price.

Where goods not answering to the description contracted for are delivered to a buyer, two alternatives are open to him: (a) the buyer may either reject the goods and obtain a refund of the price if he has already paid it and sue for damages for non-delivery, or (b) he may accept the goods and sue for damages for a breach of warranty. In the latter case it is open to the buyer to pay the price and file a separate suit for damages for a breach of warranty. It is also open to him in the event of the seller bringing his suit for recovery of price to plead damages for defective delivery as a set-off to the claim of price. In addition to the general damage that he may set-off in this manner, if he has suffered any special damages it is open to him either to file a counterclaim or a separate suit for its recovery. In any case the claim which the buyer has against the seller is a claim in damages.

Benjamin on Sale of Goods, 1950 edn., p. 555, *Kingston* v *Preston*[1], Mulla's Sale of Goods and Partnership Acts, Fourth edn., p. 239, *Sha Thilokchand Poosaji* v.

**Decided, July 15, 21 and 24, 1978.* O.C.J. Summary Suit No. 487 of 1972

1 (1773) cited in *Jones* v. *Barkley* (1781), 2 Doug. 685.

Crystal & Co.[2], *Mangilal* v. *Shantibai*[3], *National Traders* v. *Hindustan Soap Works*[4], *Kanak Kumari* v. *Chandan Lall*[5], referred to.

The claim for damages by the buyer must be so pleaded by the buyer by way of a set-off. In the absence of particulars given by the defendants about their claim for damage allegedly suffered by them in diminution or extinction of the plaintiff's claim for price, and in the absence of affidavit of documents filed by the defendants, it would not be possible for them to prove their claim in damages.

Adjustment of the defendants' claim for damages against the plaintiffs' claim for price was not possible. Adjustment on an account can only be in respect of ascertained amounts. Unliquidated claim in damages cannot be adjusted against a claim for price. Since the claim of the defendants under s. 59 of the Sale of Goods Act is in the nature of damages, it is also not possible for the defendants to adjust their claim for damages against the plaintiffs' claim for price.

It would not be correct to say that the shares of a private limited company are marketable securities. A marketable security must be such that it can be readily sold in the market. A private limited company by definition restricts the right of transfer of its shares. Hence its shares cannot be readily sold in the market. If the definition of "security" in s. 2(*h*) of the Securities Contracts (Regulation Act) is read along with the definition of "stock exchange" in s. 2(*j*) of the said Act it becomes clear that the purpose of the Securities Contracts (Regulation) Act, 1956 is to control securities which are normally dealt with in the stock exchange, that is to say shares of a public limited company. The definition of "securities" in s. 2(*h*) would exclude from its purview shares which are not marketable, such as shares in a private limited company. Such shares by their very nature are not freely transferable in the market. Their transfer is restricted in the manner provided in the articles of association of the private limited company concerned. These shares cannot be quoted in the market because they cannot be dealt with on the stock exchange.

Bangalore Water Supply and Sewerage Bd. v. *Rajappa*[6], *Swantraj* v. *State of Maharashtra*[7] and *Sri Nasiruddin* v. *S. T. Appellate Tribunal*[8], followed.

Noscitur a sociis. "The meaning of a word is to be judged by the company it keeps". It is legitimate to construe the words in an Act with reference to the words found immediately connected with it.

S. D. Parekh, with *Mrs. S. D. Nanavati*, for the plaintiffs

Ashok N. Mody, with *Jagdish Mehta*, for the defendants.

MRS. MANOHAR J. This is a suit filed by the plaintiffs to recover from the defendants a sum of Rs. 53,500 together with interest.

The plaintiffs had entered into an agreement with the defendants dated December 23, 1966 under which the plaintiffs had agreed to sell to defendants Nos. 1 to 4 1,000 ordinary and 2,300 redeemable cumulative preference shares of a company known as A. MacRae and Co. Private Ltd. for a total price of Rs. 3,10,000. Out of these shares, 125 ordinary shares and 520 redeemable cumulative preference shares belonged to one Mrs. Khambatta, who was a non-resident. Hence it was agreed between the parties that if there was any difficulty in the sale of the shares belonging to Mrs. Khambatta, defendants Nos. 1 to 4 would purchase in any event, 875 ordinary shares and 1,780 redeemable cumulative preference shares of the company from the plaintiffs for a price of Rs. 2,77,500. Out of this purchase price, Rs. 10,000 was to be paid on the signing of the agreement and the balance of Rs. 2,67,500 was to be paid by ten equal annual instalments of Rs. 26,750. The first of such instalment was to be paid

2 [1955] A.I.R. Mad. 481.
3 [1956] A.I.R. Nag. 221.
4 [1959] A.I.R. Mad. 112.
5 [1955] A.I.R. Pat. 215.
6 [1978] 2 S.C.C. 213.
7 [1975] 3 S.C.C. 322.
8 [1975] 2 S.C.C. 671.

on or before December 31, 1967 and the subsequent instalments were to be paid on or before December 31, of each succeeding year till the entire price was paid to the plaintiffs. The defendant No. 5 guaranteed the above payments to the plaintiffs. Accordingly the plaintiffs sold and delivered to defendant Nos. 1 to 4,875 ordinary and 1,780 redeemable cumulative preference shares of A. MacRae & Company. Defendants Nos. 1 to 4 paid to the plaintiffs a sum of Rs. 10,000 on the signing of the agreement. They however did not pay any of the annual instalments as agreed between the parties. The present suit is to recover the amount due to the plaintiffs under the fourth and the fifth instalments. Apparently the agreement does not contain any provision regarding acceleration of payment in the event of a default. Hence separate suits have been filed by the plaintiffs to recover the amounts of the instalments as and when the amounts became due.

The defendants have admitted the above facts. Their defence, however, is that at the time when the agreement was entered into, the plaintiffs had represented to the defendants that there was no existing liability of the company. It was on the basis of this representation that the defendants purchased the above shares, which admittedly gave a controlling interest in the above company to the defendants (the only other shareholder being Mrs. Khambatta). The defendants, however, after the purchase of these shares received notices from third parties and from Sales Tax and Income Tax authorities making large claims against the company for taxes and penalty for a period prior to 1966. In their written-statement the defendants have not given any particulars about the notices from third parties. They have, however, stated that the Income Tax Department by its notices dated February 7, 1968 reopened the company's assessment for the years 1958-59 to 1962-63 and passed reassessment orders in February and March 1971. They have also received a notice of demand dated February 14, 1975 from the Income Tax authorities for Rs. 8,63,509. They have also stated that in or about December 1966 the Sales Tax authorities seized the books of the company and made a heavy demand amounting to several lacs of rupees in respect of the sales tax dues of the company for a period prior to the sale of the said shares. The defendants have, therefore, claimed that they have suffered damages to the extent of at least the entire purchase price of the shares. They have claimed that under s. 59 of the Sale of Goods Act they are entitled to a reduction in price in view of these discoveries of debts and the entire price is now extinguished. The defendants have also pleaded that under the provisions of the Securities Contracts (Regulation) Act, 1956 the above contract for the purchase of shares is illegal and it cannot be enforced.

On these pleadings the following issues arise for consideration :

1) Whether the plaintiffs made representations as mentioned in para. 1 (b) of the written statement?

2) Whether the original 1st defendant and the defendants Nos. 2 to 4 agreed to purchase the entire share capital of the company relying on the said representations as mentioned in para. 1(c) of the written statement?

3) Whether it was a condition of the said contract that there were no outstanding debts of the said company and that if it was found that there are debts the same would be paid by the plaintiffs as mentioned in para. 1 (b), (g) and (j) and para. 2 of the written statement?

4) Whether the plaintiffs become and are liable to pay the amounts in respect of the said debts as mentioned in para. 2 of the writen statement?

5) Whether the original 1st defendant and defendants Nos. 2 to 4 have elected to treat the said breach as breach of warranty and are entitled to a reduction in price and the entire price is extinguished as claimed in para. 2 of the written statement ?

6) Whether the said agreement is illegal and void as claimed in para. 3 of the *written statement* ?

7) Whether the defendants are liable to pay any amount to the plaintiffs and if so what amount ?

8) Whether the plaintiffs are entitled to any relief and if so, what ?

Issue No. 5 raises an important question which may be considered first, namely whether there is any breach of a condition and/or warranty by the plaintiffs which can be set up by the defendants in diminution or extinguishment of their liability to pay the price under s. 59 of the Sales of Goods Act. The defendants rely in this connection on cls. 5 and 6 of the agreement dated December 23, 1966. These are as follows :

"5. The purchasers are purchasing the said shares with the knowledge that the assets of the company consist only of the name of the company, the right to occupy as a monthly tenant the premises in United India Building at Sir Phirozsha Mehta Road, Bombay, in which the registered office of the company is situated and the furniture fittings and fixtures in the said premises, a list whereof is set out in the schedule hereto.

6. The vendors hereby declare that there is now no debt or liability due by the company. In the event of its being established that any debt or liability was due by the company on the date hereof which the company is liable to pay, the vendors shall personally pay the same."

Under cl. 6 the plaintiffs have declared that on the date of the agreement there is no debt or liability due by the company. They have further covenanted with the defendants that if the company becomes liable to pay any debt or liability which is due by the company on the date of the agreement, the plaintiffs would *personally pay the same. The question is : Is this a condition of the contract* as contemplated under s. 12 of the Sale of Goods Act ? and if so, whether the plaintiffs committed any breach of this condition ? Basically the contract is a contract for the sale of shares. A declaration about the liabilities of the company is not a stipulation with reference to the goods which are being sold, namely the shares. In the event of it being found that the company did have existing liabilities, it would not be open to the defendants to reject the shares. Clause 6 itself provides that in such a case the liability would be discharged by the plaintiffs and the company would not have to bear the burden of this liability. The declaration in the first part of cl. 6 is closely linked with the subsequent provisions of cl. 6. Read as a whole, cl. 6 of the agreement is in the nature of an indemnity which the plaintiffs have given to keep the company indemnified against any claims of the type described therein being made against the company. It is not even an indemnity given to the purchaser. Hence the purchaser cannot *claim any amount from the plaintiffs under this clause. The only party who has* any claim against the plaintiffs is the company. Hence this clause does not stipulate any condition and/or warranty regarding the goods sold. It is not a condition governing the contract for sale of shares between the plaintiffs and the defendants. It is only in the nature of a collateral stipulation.

Benjamin on Sale of Goods, 1950 edn. has laid down various tests for determining whether a representation or statement made in the contract is a condition or not. At p. 555 he quotes with approval the ruling laid down by Lord Mansfield in *Kingston* v. *Preston*[1], namely,

"...that the dependence or independence of covenants is to be collected from the evident sense and meaning of the parties, and that however transposed they might be in the deed, their precedency must depend on the order of time in which the intent of the transaction requires their performance".

Among the tests laid down by him for determining this intention are (2) "When

1 (1773) cited in *Jones* v. *Barkley* (1781), 2 Doug. 685.

a covenant or promise goes only to part of the consideration, and a breach of it may be paid for in damages, it is an independent covenant, not a condition" and (5) "Where from a consideration of the whole instrument it is clear that the one party relied upon his remedy, and not upon the performance of the condition by the other, such performance is not a condition precedent". In the present case under cl. 6 of the agreement the plaintiffs may become liable to pay any amount to a third party whether it be Rs. 500 or Rs. 5 lacs. The price of the shares in the contract is not determined with reference to this uncertain liability. This becomes clear from cl. 6 itself which provides a remedy for any breach of the stipulation that is there laid down, namely that "there is now no debt or liability due by the company". The remedy provided is for the company to sue on the indemnity which is given by the plaintiffs under this clause. Hence cl. 6 is not a condition of the contract.

Secondly, it is not at all clear whether the plaintiffs have committed any breach of cl. 6 of the agreement. What cl. 6 states is that on the date of the agreement there was no existing liability. If more than a year after the agreement the Income Tax authorities reopened the assessments of the company, it cannot be said that the plaintiffs have made a wrong representation. But even assuming that the plaintiffs have committed a breach of the condition, which the defendants have treated as a breach of warranty and s. 59 of the Sale of Goods Act applies, what is the nature of the claim which the defendants have to make under s. 59 of the Sale of Goods Act ? Section 59 of the Sale of Goods Act is as follows :

"59. *Remedy for breach of warranty.* (*1*) Where there is a breach of warranty by the seller, or where the buyer elects or is compelled to treat any breach of a condition on the part of the seller as a breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods; but he may—

(*a*) set up against the seller the breach of warranty in diminution or extinction of the price; or

(*b*) sue the seller for damages for breach of warranty.

(*2*) The fact that a buyer has set up a breach of warranty in diminution or extinction of the price does not prevent him from suing for the same breach of warranty if he has suffered further damage".

Under sub-s. (*a*) of s. 59 it is open to the buyer to set up against the seller the breach of warranty in diminution or extinction of the price. Basically this is a claim in damages for defective goods which the buyer has against the seller. He is entitled to set-off his claim for damages for defective supply of goods against the seller's claim for price. In Mulla's Sale of Goods and Partnership Acts, fourth edn., p. 239 it is stated that

"from the definition of warranty in s. 12(*3*) it is clear that a breach of it gives rise to a claim for damages only on the part of the buyer".

In *Sha Thilokchand Poosaji* v. *Crystal & Co.*[2], a division bench of the Madras High Court has also taken the view that where goods not answering to the description contracted for are delivered to a buyer, two alternatives are open to him : (a) the buyer may either reject the goods and obtain a refund of the price if he has already paid it and sue for damages for non-delivery, or (b) he may accept the goods and sue for damages for a breach of warranty. In the latter case it is open to the buyer to pay the price and file a separate suit for damages for a breach of warranty. It is also open to him in the event of the seller bringing his suit for recovery of price to plead damages for defective delivery as a set-off to the claim of price. In addition to the general damage that he may set-off in this manner, if he has suffered any special damages it is open to him either to file a counter-claim or a separate suit for its recovery. In any

2 [1955] A.I.R. Mad. 481.

case the claim which the buyer has against the seller is a claim in damages. The same view has been taken in *Mangilal* v. *Shantibai*[3] and *National Traders* v. *Hindustan Soap Works*[4]. The authorities have been unanimous in holding that the remedy for a buyer where he has accepted the goods is only to sue for damages.

It has been argued that the claim under s. 59 (*1*) (*a*) is a special statutory claim in diminution or extinction of price. It proceeds on the assumption that because the goods are defective they are not worth the price agreed upon. Hence less price should be paid for inferior goods. In this connection reliance is placed on *Kanak Kumari* v. *Chandan Lall*[5]. But a perusal of this judgment only confirms the finding that the claim under s. 59 is a claim in damages. In fact the learned Judges say that the buyer has got an option to split up his claim for total damages into one *for general damages which he can set up against the seller in diminution or extinction of price* and the other for special damages for which he can bring a separate action. A claim of the buyer under s. 59 (*1*) (*a*) is therefore a claim for damages.

If this is so, the claim for damages by the buyer must be so pleaded by him. Such a claim has to be pleaded by way of a set-off. In the present case in their written-statement the defendants have not pleaded any claim as and by way of a set-off. The rules of the Bombay High Court (O.S.) provide for the manner in which a set-off should be pleaded. Rules 135 and 136 are as follows :

"135. *Set-off by defendant.* A defendant in a suit for the recovery of money in addition to his right of pleading a set-off allowed under Order VIII, rule 6, of the Code of Civil Procedure, may set-off a claim for damages provided it arises out of the same transaction as the transaction in the suit. Such set-off shall have the same effect as a cross-suit so as to enable the Court to pronounce a final judgment both on the original and the cross-claim and the plaintiff (if so advised) shall be at liberty to file a written statement in answer to the set-off within four weeks after service upon him or his attorneys of a copy of the defendant's written statement.

136. *Court or Judge may disallow set-off.* The Court or a Judge may on the application of the plaintiff at any stage of the proceedings in a suit, if in the opinion of the Court or Judge such set-off cannot be conveniently disposed of in the pending action or ought not to be allowed, refuse permission to the defendant to avail himself thereof, and require him to file a separate suit in respect thereof."

The reason why a set-off requires to be specifically pleaded and replied to is that the claim which is so made is a separate claim for which the plaintiff may have his own defence which he should be allowed to set up and in respect of which proper issues can be framed and evidence led. If this is not done, substantial injustice can be caused to the plaintiff. In the present case, although liberty was given to the defendants to file a counter-claim they have neither filed a counter-claim nor a set-off. The defendants have not even quantified the damages which they claim to have suffered. Apart from stating that the damages would be more than the price that they would have to pay under the contract, they have not given the actual quantum of damages which they claim from the plaintiffs. They have also not paid any Court-fees on this claim for damages. Under the circumstances, it will not be possible for them to rely on this claim for damages in diminution or extinction of the plaintiffs' claim for price.

There is also a further difficulty in the way of the defendants. The defendants have not given the particulars of damages which they have suffered any where in the written-statement. In the absence of any particulars being given about the damage which they have suffered, I do not see how they can prove the quantum of damages. What is more, the defendants have not filed any affidavit of documents. Directions were given in the matter as far as back as August

3 [1956] A.I.R. Nag. 221.
4 [1959] A.I.R. Mad. 112.
5 [1955] A.I.R. Pat. 215.

3, 1972. Directions were also given on that day to place the suit on board in June 1973 for trial as a contested short cause. Thereafter the matter was adjourned on a number of occasions. From February 1977 to April 1978 admittedly a number of letters have been written by the advocates of the plaintiffs calling upon the defendants to file their affidavit of documents but to no avail.

As the plaintiffs are from Coonoor, at the instance of the plaintiffs the matter was placed for directions for fixing a date of hearing also on a number of occasions. On March 28, 1978 an order was passed placing the suit for hearing and final disposal on April 19, 1978, subject to overnight part-heard. Even then, the defendants did not make any affidavit of documents. The matter thereafter came up before me for directions for a fixed date as the plaintiff was coming from outside Bombay. At this stage also nobody appeared or behalf of the defendants to point out that any time was required by the defendants for filing their affidavit of documents. Therefore, I placed the matter on board for hearing and final disposal on July 12, 1978 and directed that it should come high on board. It was only when the actual hearing of the matter started that Mr. Mody, who appears for the defendants, stated that he wanted to tender his clients' affidavit of documents containing 112 documents, all in support of their claim for damages. Even at that stage the affidavit was not affirmed but was affirmed thereafter. There is really no explanation why this affidavit of documents should not have been filed much earlier and why inspection of the documents on which the defendants seek to rely should not have been given to the plaintiffs. The only explanation given by Mr. Mody is that the files containing the documents were not traceable and some of those documents were traced only in March 1978. Even so the matter had been fixed for hearing subject to over-night part-heard on April 19, 1978 and if the defendants were at all serious about pressing their claim for damages, they would have made their affidavit of documents before April 19, 1978. The defendants have not chosen to do so till July 12, 1978. In view of this conduct of the defendants, I saw no reason take this affidavit of documents on file which would have entailed a further adjournment of a matter which had been specifically fixed for hearing on this day. Hence I rejected the affidavit of documents. In the absence of these documents, it will not be possible for the defendants to prove their claim for damages.

Since the claim of the defendants under s. 59 of the Sale of Goods Act is in the nature of damages, it is also not possible for the defendants to adjust their claim for damages against the plaintiffs' claim for price. Adjustment of an account can only be in respect of ascertained amounts. Unliquidated claim in damages cannot be adjusted against a claim for price. Secondly, an adjustment can only be in respect of cross claims between the same parties. In the present case, the price for the shares is payable by the defendants as purchasers of these shares to the plaintiffs. As far as the claim set up by the defendants under cl. 6 of the agreement is concerned, it is a claim which the company has against the plaintiffs for indemnity in case the company is called upon to discharge a liability covered under the clause to a third party. Under this clause the plaintiffs have incurred an obligation to discharge the liability of the company. I do not see how any claim made by the company on the plaintiffs under cl. 6 of the agreement (no such claim is made so far) can be availed of by the defendants in mitigation of their liability to pay the price of the shares to the plaintiffs. It is, therefore, not possible for the defendants to adjust their liability to pay the price against the claim of the company for damages. Hence a mere statement in the written-statement that the defendants have suffered damages which they can set up in extinction of price will not be of any avail to the defendants.

Issues Nos. 1 to 4 deal with the question of alleged misrepresentations made by the plaintiffs to the defendants. Here again, the claim of the defendants against the plaintiffs for these misrepresentations would be a claim for damages

and the defendants face the same difficulty as far as their plea for damages on this count is concerned and its proof. Hence issues Nos. 1 to 5 are decided against the defendants.

The only issue which now survives is issue No. 6. According to the defendants, the agreement dated December 23, 1966 is a direct agreement between the parties for the purchase of shares. The agreement has taken place in Bombay. Neither party to the agreement is a member of the Stock Exchange. Hence the agreement violates s. 13 of the Securities Contracts Regulation Act, 1956, which provides as follows :

13. If the Central Government is satisfied, having regard to the nature or the volume of transactions in securities in any State or area, that it is necessary so to do, it may, by notification in the Official Gazette, declare this section to apply to such State or area, and thereupon every contract in such State or area which is entered into after the date of the notification otherwise than between members of a recognised stock exchange in such State or area or through or with such member shall be illegal."

By a notification dated November 29, 1957 s. 13 has been made applicable to Greater Bombay. As a result, the present contract is in contravention of the provisions of s. 13 and is illegal. Secondly, the agreement provides for payment of price of the shares by annual instalments. It is, therefore, not a 'spot delivery contract' as defined under s. 2 sub-s. (*i*) of the Securities Contracts (Regulation) Act, 1956 (hereinafter called the 'Act'). A 'spot delivery contract' is defined under the Act as follows :

"'spot delivery contract' means a contract which provides for the actual delivery of securities and the payment of a price therefor either on the same day as the date of the contract or on the next day, the actual period taken for the despatch of the securities or the remittance of money therefor through the post being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality;"

In order to qualify as a 'spot delivery contract' the contract for sale of shares must provide for actual delivery of shares and the payment of price either on the same day as the date of the contract or on the next day, etc. It is, therefore, clear that the present contract which provides for payment of price by instalments is not a spot delivery contract. It is, therefore, not exempt under s. 18 of the Act from being governed by s. 13 of the Act. Hence, according to the defendants, this contract is an illegal contract by virtue of the provisions of s. 13 of the Securities Contracts (Regulation) Act read with the notification. It should be noted however that the contract is not covered by the notification dated January 27, 1969 issued under s. 16 of the Act which prohibits all forward contracts except those of the types specified in it. The present contract was made on December 23, 1966, long prior to the date of this notification.

Now in order to appreciate this contention of the defendants, we have to examine whether the Securities Contracts (Regulation) Act, 1956 applies to the suit contract. The suit contract is for the sale of shares in a private limited company. It is also a contract under which admittedly the controlling interest in the private limited company is transferred from the plaintiffs to the defendants. Does the Securities Contracts (Regulation) Act apply to such contracts ? In order to answer this question one must first examine the definition of "securities" under the Act.

'Securities' are defined under s. 2 (*h*) of the Act as follows :

"'securities' include—

(*i*) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

(*ii*) Government securities and

(iii) rights or interest in securities."

Prima facie the definition covers all shares of any incorporated company whether private or public. There is no exclusion of shares of a private limited company from the definition of 'securities' under the Act. Taken at its face value, it would appear that the sale of shares in a private company is also governed by the provisions of this Act. Mr. Mody, who appears for the defendants, has also drawn my attention to the heading preceding to s. 21 which is as follows : "Listing of securities by Public Companies". He has argued that the distinction between a private company and a public company was present to the minds of the legislators when the Act was enacted and if the intention was to exclude shares of a private company from the provisions of the Act, this would have been expressly so provided. According to him, there is no ambiguity either in the definition of 'securities' or in the rest of the provisions of the Act and they apply to all types of shares whether in a private limited company or in a public limited company. In support of his contention that the plain meaning of the words should be accepted he has relied upon a number of authorities a list of which is separately appended as List I. There could be no quarrel with the proposition advanced by Mr. Mody that where the words are clear and unambiguous they must be given effect to. But in the present case, from the way the definition is worded it is far from clear what the meaning of the words used in the definition clause is. In the definition of 'securities' given in the Act, the material words for the present purpose are "shares and other marketable securities of a like nature". Firstly, what is the meaning of the word 'marketable' when used in conjunction with 'securities' and secondly, whether the phrase 'other marketable securities of a like nature' colours the preceeding words and restricts their meaning in any way. The word 'marketable' can have a number of connotations. It is often loosely used as meaning 'saleable.' In this sense, any commodity which is capable of being sold is said to be 'marketable'. But essentially by 'marketable' we mean something which can be offered for sale in a market. Hence goods become marketable when there is a market or a place where the goods of the type in question can be readily sold. The word "marketable" thus implies a certain ease or facility in selling. Mr. Mody urged that the word 'marketable' in the present definition should be construed simply as 'saleable'. All shares which can be sold whether by a private treaty or through the Stock Exchange or in any other manner are to be considered as marketable securities. Shares of a private limited company can also be sold though there may be some restrictions on their transfer. Hence, these shares are also marketable. Therefore, according to him, even assuming that the words "or other marketable securities of a like nature" govern the preceeding word "shares", the shares of a private limited company being marketable securities would be covered by the definition.

I do not think it would be correct to say that the shares of a private limited company are marketable securities. As discussed earlier, the word "marketable" implies a certain ease in selling. When used in conjunction with the word "securities" it connotes that the securities which are to be termed as marketable possess a high degree of liquidity. Webster's Third New International Dictionary defines "marketable" in conjunction with securities as "enjoying a high degree of liquidity" (vide page 1383). A marketable security must, therefore, be such that it can be readily sold in the market. A private limited company by definition restricts the right to transfer its shares (see s. 3, Companies Act, 1956). Hence its shares cannot be readily sold in the market. In this connection the definition of "Stock Exchange", which is given under the Act, is also relevant. Section 2(j) defines "Stock Exchange" as follows:

"'stock exchange' means any body of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities."

If the definition of 'security' is read along with the definition of 'stock exchange', it becomes clear that the purpose of the Act is to control securities which are normally dealt with on the stock exchange, that is to say, shares of a public limited company.

Nosciture a sociis is a well known maxim of interpretation of words used in statutes. This rule of interpretation says that "the meaning of a word is to be judged by the company it keeps". It is, therefore, legitimate to construe the words in an Act with reference to the words found immediately connected with it. In the present case, the words "other marketable securities of a like nature" are words of a general character which would apply to all the preceding words, namely, "shares, scrips, stocks, bonds and debentures". According to Halsbury's Laws of England, third edn., vol. 36, p. 600, as a matter of ordinary construction where several words are followed by a general expression which is as much applicable to the first and other words as to the last, that expression is not limited to the last, but applies to all. If both these principles are applied, then, 'shares' have to be construed in such a way that their meaning would be limited to 'marketable securities'. Construed in this manner, the definition of 'securities' would exclude from its purview shares which are not marketable, such as *shares in a private limited company. Such shares by their very nature are not* freely transferable in the market. Their transfer is restricted in the manner provided in the articles of association of the private limited company concerned. These shares cannot be quoted in the market because they cannot be dealt with on the stock exchange. In fact, a perusal of the Rules of the Bombay Stock Exchange makes it clear that such shares are disqualified from being listed on the Stock Exchange because one of the basic requirements for listing of shares on the Stock Exchange is that they should be freely transferable. It is, therefore, clear that though it may be possible to sell the shares of a private limited company in an individual case after complying with the conditions provided under the articles of association of the Company concerned relating to such a transfer, these shares are not marketable securities as contemplated under the Act. In the present case, therefore, by applying the maxim of *Noscitur a sociis* the word 'shares' takes its colour from the words 'other marketable securities of a like nature'. This maxim has been frequently applied for construing in a number of cases which have been cited before me. I need not refer to all such cases. The latest application of this maxim can be found in *Bangalore Water Supply and Sewerage Bd.* v *Rajappa*[6], which deals with the meaning of the word 'Industry' in the definition clause of the Industrial Disputes Act, 1947. In analysing the meaning of the word 'Industry' their Lordships Jaswant Singh and V. D. Tulzapurkar JJ. have applied this maxim in the following words (p. 299) :

> "...However, bearing in mind the collocation of the terms in which the definition is couched and applying the doctrine of *noscitur a sociis* (which, as pointed out by this court in *State of Bombay* v. *The Hospital Mazdoor Sabha*[7] means that, when two or more words which are susceptible of analogous meaning are coupled together they are understood to be used in their cognate sense. They take as it were their colour from each other, that is, the more general is restricted to a sense analogous to a less general. Expressed differently, it means that the meaning of a doubtful word may be ascertained by reference to the meaning of words associated with it)..."

A list of other cases which were quoted before me in connection with the application of this maxim is annexed as List II.

It is thus permissible to read the definition of 'securities' so that it applies to only securities which are marketable, that is to say, those securities which

6 [1978] 2 S.C.C. 213. [1960] A.I.R. S.C. 610, s.c. 62 Bom. L.R.553.

7 [1960] 2 S.C.R. 866, s.c.

enjoy a high degree of liquidity and can be freely bought and sold in the open market.

This interpretation is strengthened if we examine the background in which the Act was passed, the mischief which was sought to be suppressed by the Act and the statement of objects and reasons for framing this legislation. For the correct interpretation of a statute it is permissible to examine all these data. The present Act was initially drafted by a committee which was specially appointed for the purpose of examining a legislation for regulation of stock exchanges, contracts and securities, which was popularly known as the Gorwala Committee. The Securities Contracts (Regulation) Act, 1956 was passed on the basis of the recommendations made by this committee. In the draft Bill which was prepared by this committee the definition of 'securities' is basically the same as the definition of 'securities' under the present Act which is framed on the basis of this draft Bill. In the report of this committee the problem which was placed by the Government before the committee has been described thus in paragraph 2 :

"2. The problem which Government have asked us to examine is the manner of regulation of stock exchanges. This must be taken to imply that, from the point of view of the public interest, Government considers, firstly, that stock exchanges do fulfil a legitimate and useful function in their own sphere and, secondly, that that function needs to be properly regulated".

The Report goes on to say,

"A consideration of the functions of a stock exchange is perhaps the most suitable starting point for the formulation of an approach to the problem of regulation. The legitimate function of a stock exchange is to provide, consistently with the larger public interest, a forum and a service which are so organised, in the interests of both buyers and sellers, as to ensure the smooth and continual marketing of shares. Buyers or sellers of shares are of different kinds. There are those who buy shares to invest or sell shares for ready cash. It is the interests of these that must be kept constantly in mind, since it is for them primarily that the stock exchange exists. There are also those who buy in the hope to sell at a profit or sell in the hope to buy at a profit. In popular language, they are speculators as distinguished from genuine investors, though the two groups of course are by no means mutually exclusive, for, by way of example, a man who has bought to invest may later persuade himself to sell to make profit. Nevertheless, the existence of a body of speculators is one of the main features of almost all the stock exchanges with which we are concerned."

The committee was asked to suggest ways and means of preventing or controlling speculation in shares of public limited companies. This was the purpose for which the committee was formed and pursuant to whose report the present Act was passed. The whole purpose of the Act, therefore, was to prevent speculation in shares on the Stock Exchange. The sale of shares of a private limited company was not under consideration before this committee. After this committee made its report a Bill embodying its recommendations was presented to Parliament. This Bill was passed and has become the present Act. The statement of objects and reasons which accompanied the presentation of the Bill before Parliament states as follows : (Government of India Gazette (Extra.) 1954, Part II, S. II, page 783) :

"The object of this Bill is to provide for the regulation of stock exchanges, and of transactions in securities dealt in or them with a view to preventing undesirable speculation in them."

It goes on to say that Gorwala Committee was appointed for the purpose of considering the draft proposals of the Government on the subject of stock exchange regulation and to submit a revised draft Bill and to make any other recommendations which it though fit. The report of this committee and the draft Bill

prepared by it were circulated to all the principal Stock Exchanges in this country, Chambers of Commerce and other interested associations and after considering all these comments the present Bill has been framed. It says thereafter that "the Bill, as now drafted, broadly follows the recommendations contained in the report of the Gorwala Committee". *It is thus clear that the main* purpose of passing this Act was to regulate speculation in shares on the Stock Exchanges and to regulate the mechanism of stock exchanges for this purpose. At no point of time was there any proposal to regulate dealings in shares of a private limited company. The public does not have any substantial interest in such shares and basically there is no speculation in such shares. The shareholders of such companies know fully well what they do when they sell these shares. There is, therefore, no public mischief in the sale of such shares which is sought to be prevented by the present Act.

An examination of the scheme of the Act also makes it clear that the Act is not meant to apply to shares of a private limited company. The preamble to the Act says as follows :

> "An Act to prevent undesirable transactions in securities by regulating the business of dealing therein, by prohibiting options and by providing for certain other matters connected therewith."

Since there is no question of any speculation in the shares of a private limited company, there could be no question of preventing undesirable transactions in such shares. Secondly, the Act does not provide any machinery for regulating the business of dealing in shares of a private limited company. The machinery that is provided under the Act of regulating dealings in securities is the machinery of the Stock Exchange. Sections 3 to 12 of the Act deal with Stock Exchanges and the manner in which their work is to be regulated. An important section in this connection is s. 9, which regulates making of bye-laws of recognised Stock Exchanges. Section 9 (*m*) provides for bye-laws being framed for listing of securities on the Stock Exchange. Since under ss. 13 to 20 it is open to the Government to insist that certain types of transactions of sale of shares must be effected through the stock exchange, it becomes imperative to provide for listing of securities on the stock exchange. Under ss. 21 and 22 power is given to the Central Government to compel listing of securities by public companies and a right of appeal is also given against a refusal by the stock exchanges to list such securities. No such provision has been made in respect of shares of private limited companies. If shares in such companies were also to be covered by the Act, it would have been necessary to provide a suitable machinery through which such shares could have been sold but no such provision is made in the Act because it was never contemplated that such shares would be covered by the Act.

Similarly, bye-laws of the Bombay Stock Exchange also do not deal with the listing of shares in private limited companies. By their very nature these shares are not freely transferable and they are not dealt with on the stock exchange.

The application of the Act to the shares of a private limited company would also result in tremendous hardship. In a number of cases it would become extremely difficult, if not impossible, to sell such shares. It is true that 'spot delivery contracts' are excluded from the purview of the Act. It has been argued that shares of a private limited company can be sold by making spot delivery contracts. *But in practice articles of association of a number of private limited* companies impose restrictions on their transfer : for example, the articles often provide that such shares should be offered for sale to the existing members of the company at a valuation that may be fixed by the auditors. It would be very difficult, if not impossible to make spot delivery contracts in such cases. Secondly, under the Act it is open to the Government even to impose restrictions on spot delivery contracts. It has next been argued that sale of such shares can

take place if the Stock Exchange so permits. But this would be putting the shareholders of such shares entirely at the mercy of the Stock Exchange. I do not see how even under s. 28 such shares can be exempted from the operation of the Act, because no public interest is involved in the transfer of such shares and s. 28 sub-s. (2) provides that only where the Central Government is satisfied that in the interests of trade and commerce or the economic development of the country it is necessary or expedient so to do it may specify any class of contracts as contracts to which the Act may not apply. Therefore, individual transactions of sales of shares in a private limited company cannot be exempted under this section.

The fact that the Act only applies to large scale dealings in shares of public limited companies can be seen in a number of sections. For example, even under s. 13 a power to issue a notification is granted to the Central Government if it is satisfied that having regard to the nature or volume of the transactions in securities in any State or area that it is necessary so to do. The notification dated November 29, 1957 which has been issued under this section also states that the Central Government is satisfied having regard to the nature or the volume of transactions in securities in the area comprising the Greater Bombay that it is necessary so to do. Hence bearing in mind the mischief that was sought to be prevented by the Act and bearing in mind the hardship that would result to the owners of shares in a private limited company, if the Act were to be applied to such shares, it is permissible to restrict the definition of 'securities' to cover only marketable securities. In this connection reference may be made to *Swantraj* v. *State of Maharashtra*[8], where the Supreme Court has construed the Drugs and Cosmetics Act, 1940. Krishna Iyer J. states that,

"Every legislation is a social document and judicial construction seeks to decipher the statutory mission, language permitting, taking the one from the rule in *Heydon's*[9] *case of* suppressing the evil and advancing the remedy." (p. 323).

It is true that if the word 'shares' is taken in its literal meaning, the shares in a private limited company would be covered by the Act. It is also true that normally when the language of the Act is clear it is not open to look at the surrounding circumstances relating to the framing of the Act, such as statements of objects and reasons or the question of mischief which is sought to be prevented. But where there are sufficient indications in the Act itself, that the Act is limited in its application to certain types of shares, it is possible to look at all these in order to prevent the mschief which was sought to be suppressed and to advance the remedy. In fact, in the present case, it would be unjust if the Act is interpreted literally ignoring all these factors. In *Sri Nasiruddin* v. *Appellate Tribunal*[10], Ray C. J. has stated thus (p. 680):

"...If there are two different interpretation of the words in an Act, the Court will adopt that which is just, reasonable and sensible rather than that which is none of those things. If the inconvenience is an absurd inconvenience, by reading an enactment in its ordinary sense, whereas if it is read in a manner in which it is capable, though not in an ordinary sense, there would not be any inconvenience at all; there would be reason why one should not read it according to its ordinary grammatical meaning."

In view of these circumstances and looking to the provisions of the Act as a whole, in my view, the present contract which is a contract of sale of shares in a private limited company is not governed by the provisions of the Securities Contracts (Regulation) Act, 1956 and it is, therefore, not illegal.

It has been further argued by Mr. Parekh, who appears for the plaintiffs, that this is not a contract merely for the sale of shares but it is a contract under which controlling interest in a company was transferred from one party to

8 [1975] 3 S.C.C. 322.
9 [1584] 3 Co. Rep. 7a.
10 [1975] 2 S.C.C. 671.

another and that such a contract is also not covered under the Securities Contracts (Regulation) Act, 1956. As I have already come to the conclusion that the shares of a private limited company are not governed by the provisions of this Act, it is not necessary for me to go into this aspect of the question.

Under the circumstances, issue No. 6 is decided in the negative. The contract is legal and binding on the parties.

The defendants have admitted having entered into the agreement dated December 23, 1966. They have also admitted that apart from the sum of Rs. 10,000, which was paid on the signing of the agreement, no further amount has been paid by the defendants to the plaintiffs. As I have already stated, their only defence is a cross-claim for damages arising by reason of certain misrepresentations made by the plaintiffs at the time when the said agreement was entered into, and as a result of breach of cl. 6 of this agreement. I have already stated why this claim of the defendants cannot be allowed.

In the result, there will be a decree in favour of the plaintiffs as prayed. Plaintiffs' advocate's fees are quantified at Rs. 7,000.

LIST I.

1 *State of Bombay* v. *Hospital Mazdoor Sabha*, [1960] A.I.R. S.C. 610.
2 *Venkataramana Devaru* v. *State of Mysore*, [1958] A.I.R. S.C. 255, at p 266.
3 *Jage Ram* v. *State of Haryana*, [1971] 1 S.C.C. 671, at p. 676.
4 *Express Newspaper Ltd.* v. *Union of India*, [1958] A.I.R. S.C. 578, at p. 622.
5 *C.I.T., W.B.* v. *Vegatables Products Ltd.*, [1973] 1 S.C.C. 442.
6. *S.T. Commr., U.P.* v. *Parson Tools & Plants, Kanpur*, [1975] A.I.R. S.C. 1039, s.c [1975] 4 S.C.C. 22, at pp. 27-29.
7 *S.T. Commr., U.P.* v *Mangal Sen*. [1975] A I R. S.C. 1106, at p. 1110.
8 *C.I.T. v. T. V. Sundram Iyengar (P) Ltd.*, [1976] 1 S.C.C. 77, at p. 84.
9 *State of Haryana* v. *Jiwan Singh*. [1976] 1 S.C.C. 99, at p. 100.
10 *Sri Nasiruddin* v. *S.T. Appellate Tribunal*, [1975] 2 S.C.C. 671, at p. 680.
11 *State of Rajasthan* v. *Leela*, [1965] A.I.R. S.C. 1296, at p. 1299.
12 *I.-T. Commr.* v. *Indian Bank Ltd.*, [1965] A.I.R. S.C. 1473.

LIST II.

1 *Bageshwari Charan* v. *Jagannath Kuari*, [1932] A.I.R. P.C. 55, at p. 56, s c. 34 Bom. L.R. 463.
2 *State of Assam* v. *Ranga Muhammad*, [1967] A.I.R. S.C. 903, at p. 906.
3 *Amar Chandra* v. *Excise Collector, Tripura*, [1972] A.I.R. S.C. 1863, at p. 1868.
4 *State of Bombay* v. *Hospital Mazdoor Sabha*. [1960] A.I.R. S.C. 610, at pp. 613 and 614.
5 *Dr. D. M. Surti* v. *State of Gujarat*. [1969] A.I.R. S.C. 63, at p. 67.
6 *M. K. Ranganathan* v. *Govt. of Madras*, [1955] A I.R. S.C. 604, at p. 609.