

(1999) 12 MAD CK 0049

In the Madras High Court

Case No : A.A.O. No's. 1312 and 1391 of 1998 and C.M.P. No's. 4439 to 4441 of 1999

Anugraha Jewellers Ltd. and Another

APPELLANT

Vs

K.R.S. Mani and Others

RESPONDENT

Date of Decision : 17-12-1999

Acts Referred:

Companies Act, 1956 — Section 397, 398, 402, 403
Penal Code, 1860 (IPC) — Section 477A

Citation : (2002) 111 CompCas 501

Hon'ble Judges : A. Raman, J

Bench : Single Bench

Advocate : Arvind P. Datar, for the Appellant; C. Hari Krishnan, for B. Ravi Raja, for the Respondent

Final Decision : Dismissed

Judgement

A. Raman, J.—These appeals are preferred against the order passed by the Company Law Board, Southern Region Bench, Chennai, on

September 23, 1998, in Company Petition No. 16 of 1997 (since reported in K.R.S. Mani v. Anugraha Jewellers Ltd. [2000] 100 Comp Cas

665 .

2. Respondents Nos. 1 to 4 hold 15.5 per cent, shares in Anugraha Jewellers Ltd. They filed the petition under Sections 397, 398, 402 and 403

of the Companies Act, 1956, alleging certain acts of oppression and mismanagement in the affairs of the company.

3. The gist of the case :

There has been irregularity in the allotment of shares to the petitioners. Funds from the company have been siphoned off in the form of loans and

advances to certain companies. The appointment of the managing director is neither legal nor proper. The petitioners were removed from the

board in an irregular manner. There is defalcation of stock. Mainly on the basis of the above allegations, which have been stated above broadly,

the application was filed by the respondents herein as petitioners before the Company Law Board.

4. The averments made by the petitioners were replied by the respondents by filing a detailed reply and denying the various allegations. It is seen

from the proceedings of the Company Law Board that on behalf of the appellants herein, an objection was also raised to the maintainability of the

petition on the ground that already a complaint has been registered, alleging certain irregularities and, therefore, a parallel proceeding cannot be

permitted under law. It was also put forward by the appellants that the respondents herein have also moved the civil court, viz., the Subordinate

Judge, Coimbatore. Therefore, as there is already a complaint, alleging certain irregularities, which is pending investigation, and as on identical

grounds, the respondents" have also filed a suit before the sub-court, the present application is not maintainable in law.

5. The Company Law Board held that it was appropriate that the management of the company should be entrusted for some time to an

independent person so that the inter disputes between the promoters do not affect the business of the company any further and, therefore, the

Board appointed one Aghoramurthy, former Regional Director of the Department of Company Affairs, as the administrator. Aggrieved by the said

order, the present appeal is preferred, challenging the said decision of the Company Law Board.

6. Anugraha Jewellers was incorporated as a public limited company on December 8, 1994. The company was promoted by the sons of K.

Ramakrishna Pillai, who started and established jewellery business in the name and style of K.R. and Sons Jewellery. The main object of the

company is to carry on business of goldsmiths, silversmiths, jewellers, gem and diamond merchants and to do all manufacturing of and dealing in

jewellery, their components and accessories. The inauguration of the company was on December 8, 1994, and by public issue, a sum of Rs. 2.5

crores was raised. The paid-up capital of the company is Rs. 5 crores and the capital is Rs. 5 crores. The petitioners before the Company Law

Board held 15.5 per cent, of shares. The appellants herein hold 18 per cent, of shares. About 67.5 per cent, of the shares are held by the public.

7. Before we take up the issues for consideration, it will be appropriate to state the law on this point. A single judge of this court held in the

decision in *Vivek Goenka v. Manoj Sonthalia* [1993] 2 MLJ 163 ; [1995] 83 Comp Cas 897 that it is the duty of the court to recognise the

corporate democracy of a company in managing its affairs, and that it is not for the court to restrict the powers of the board of directors. It further

held that it will not be open to this court to interdict the functions of the board managed company and the court shall not interfere with the day-to-

day functions, management and administration of a company, unless it is established that the decisions taken by the board are ultra vires the Act or

the articles of association of the company. Further, it held that it is not for the court to dictate to the board as to how it should function. When the

matter comes before the court, the court is not concerned with inter se relationship of the parties. But, it has to keep in mind the corporate

democratic principles.

8. In yet another decision of this court in *G. Kasturi v. N. Murali* [1992] 74 Comp Cas 661, it has been held that the principle of quasi-partnership

is applied to a small private company founded on a personal relationship involving mutual confidence as between the members. The interests of the

shareholders and that of the company must always be preferred over the interests of any one else irrespective of the position occupied by him. It

further held that prejudice to the company's interest to be shown only u/s 398. While referring to the demand by minority shareholders for

additional shares and the refusal of such request, the court observed that it is not a case of oppression and that the refusal by the managing director

of a company to allow publication of certain news items will not affect public interest.

9. In *Nurcombe v. Nurcombe* [1985] 1 All ER 65 ; 3 Comp LJ 163 (CA), it was held that a minority shareholder's action in form, is nothing more

than a procedural device for enabling the court to do justice to a company controlled by miscreant directors or shareholders. Since the procedural

device was evolved so that justice can be done for the benefit of the company, whoever comes forward to start the proceedings, must be doing so

for the benefit of the company, and not for some other purpose. It follows that the court has to satisfy itself that the person coming forward is a proper person to do so. The court is entitled to look at the conduct of a plaintiff in a minority shareholder's action to satisfy itself that he is a proper person to bring the action on behalf of the company ; and that the company itself will benefit. A particular plaintiff may not be a proper person, because his conduct is tainted in some way which under the rules of equity may bar relief. He may not have come with ""clean hands"" or he may have been guilty of delay.

10. It is relevant in this context to refer to a passage from Gower's Principles of Modern Company Law, where it is observed as follows (page 652 of 4th edition):

The right to bring a derivative action is afforded to the individual member as a matter of grace. Hence, the conduct of a shareholder may be regarded by a court of equity as disqualifying him from appearing as plaintiff on the company's behalf. This will be the case, for example, if he participated in the wrong of which he complains.

11. Vaughan Williams LJ., has observed in *Towers v. African Tug Co.* [1904] 1 Ch. 558 as follows :

I think that an action cannot be brought by an individual shareholder complaining of an act which is ultra vires, if he himself has in his pocket, at the time he brings the action, some of the proceeds of that very ultra vires act. Nor in my opinion, does it alter matters that he represents himself as suing on behalf of himself and others.

12. It was held in the decision in *V.M. Rao and Others Vs. Rajeswari Ramakrishnan and Others*, that the oppression complained of must affect a person in his capacity or character as a member of the company ; harsh or unfair treatment in any other capacity, for example, as a director or creditor is outside the purview of the section. There must be continuous acts constituting oppression up to the date of the petition. The events have to be considered not in isolation but as a part of a continuous story. It must be shown as a preliminary to the application of Section 397 that there is just and equitable ground for winding up the company. The conduct complained of can be said to be oppression only when it could be said that it is burdensome, harsh and wrongful oppression involves at least an element of

lack of probity and fair dealing to a member in matters of his

proprietary right as a shareholder. The exercise of the inherent right of shareholders, in such circumstances, to elect their directors cannot be

contended as constituting oppression. The majority shareholders are not bound to accept the views of the minority shareholders. If it is a lawful

exercise of power by the majority, the minority shareholder is bound by the same.

13. Now, in the background of the pronouncements of law as reported in the decisions referred to above, it would be appropriate to deal with the

case of the parties on hand. The main grounds on which the petition was filed are : Irregularity in the allotment of shares to the petitioners; siphoning

off of funds of the company in the form of alleged loans ; irregular removal of petitioners-directors from the board ; invalidity in the appointment of

the managing director. The last accusation is that there is a defalcation.

14. The Commissioner has actually noted excess stock as regards gold ornaments. It is not in dispute that K.R.S. Mani, who is the first respondent

herein, lodged a complaint on September 22, 1996, which was registered in CrI. No. 28 of 1996 in City Crime Branch, u/s 477 of the Indian

Penal Code, 1860. The complaint against K.R. Loganathan and his two sons is regarding misappropriation of Rs. 3 crores. It appears that after

consulting the legal advisor to the Commissioner of Police and after satisfying that a prima facie case under Sections 406 and 477A of the Indian

Penal Code has been made out against K.R. Loganathan, the managing director of the company and two others, the case was registered in CrI.

No. 28 of 1996 in City Crime Branch, under Sections 406 and 477A of the Indian Penal Code. This complaint was laid on September 22, 1996,

and the case was registered on September 22, 1996.

15. While so, a suit was filed on the file of the Sub-Court, Coimbatore, in O. S. No. 945 of 1996 by K. R. S. Mani, K. R. S. Anand Kumar, K.

R. S. Suresh and L. Prakash as plaintiffs against Anugraha Jewellers Ltd. and K. R. Loganathan, as defendants Nos. 1 and 2 respectively. The

reliefs asked for are that the resolution purported to be passed at the second annual general meeting of the company on September 4, 1996,

removing the first plaintiff from the office of whole-time director is illegal, invalid and not binding on the first plaintiff; (ii) a permanent injunction

restraining the defendants, any officers and agents of the first defendant-

company from interfering in any manner with the discharge of duties by the first plaintiff as whole-time director ; (iii) declaration that the resolution passed on September 4, 1996, removing the second plaintiff from the office of the vice-president is illegal and for consequential injunction; (iv) declaration that the resolution passed on September 4, 1996, removing the third plaintiff from the office of vice-president is illegal and for permanent injunction restraining the defendants in that regard ; and (v) for declaring that the fourth plaintiff upon retirement as a director at the annual general meeting held on September 4, 1996, has been re-elected as a director of the first defendant-company and for consequential injunction with reference to the same.

16. The plaint proceeds on the footing that the second defendant completely withheld information whatsoever sought by the plaintiffs and they were kept in the dark and that no board meeting was convened by the defendants in spite of the requisition of the plaintiffs. There was gross discrepancy between the account as was circulated to the directors and the auditor report submitted in newspapers publication (Economic Times). The plaintiffs raised detailed clarifications regarding such discrepancies and misappropriation of funds and that at the time of meeting on September 4, 1996, a number of goondas were present outside the meeting hall. An atmosphere of threat and intimidation was built up by the second defendant to confront the plaintiffs and cow them down. Resolutions were not properly proposed or seconded. There was no proper poll taken and the procedure required under law was not followed, and thus, the resolutions are invalid in law.

17. It is to be pointed out that the respondents herein have filed this petition before the Board on identical grounds. It is also to be pointed out that there was yet another suit filed with reference to the affairs of the company. Thus, we find that there were proceedings already initiated and pending with reference to the dispute between the parties vis-a-vis, the company of which they were directors and shareholders. A complaint was laid which was registered under Sections 406 and 477A of the Indian Penal Code. Apparently, the investigation on the said complaint is pending. There was also the suit filed with reference to the resolution dated September 4, 1996. There was another proceeding by way of another suit

between the parties with reference to the affairs of the company. When proceedings have been already initiated, it is really understandable as to why the petition was filed before the Company Law Board. It may be that after the initiation of this proceeding, the plaintiffs in the suit might have withdrawn the suit. But that will not erase the effect of the action taken by them. This only will indicate the absence of bona fides in the proceedings initiated by the respondents before the Company Law Board. This has to be viewed further in the context of the participation of the respondents herein in some of the very activities which are now questioned by them. Having been a party to certain decisions or actions, the respondents would now file an application before the Board accusing the appellants herein of those acts. This would only underline the oblique motive in filing the application.

18. I have already referred to the ruling in Nurcombe's case [1985] 1 All ER 65; 3 Comp LJ 163 (CA), where it has been pointed out that the court has to satisfy itself that the person who comes forward is a proper person to do so. If it is shown that the person, who has come forward has a conduct tainted in some way, then the court will not be justified in allowing the person to maintain such an application. In other words, as held in Gower's Principles of Modern Company Law (fourth edition 1979) if he had participated in the wrong of which he complains, he cannot maintain an action.

19. Here, the actions of the respondents filing an application before the Board has to be viewed from that angle. Rightly or wrongly, they have already initiated steps under law. They have not only set the ball rolling by initiating criminal action, but also by resorting to civil action. They are parties to the transaction, which now they question. In such circumstances, one has to hold that the actions of the respondents in filing the application before the Board is a mala fide one. They ought not to have been allowed to maintain such an application. Therefore, in this view of the matter, to begin with, it has to be held that the application filed by the respondent before the Company Law Board is but one born of mala fide intention and has been initiated only with a view to harass the appellants further. A person cannot be allowed to take different stand at different points of time. He cannot be allowed to question certain actions to which he was

a party. Such an attitude should not only be deprecated, and if it is permitted, it will affect the smooth administration and would only encourage people to resort to such proceeding at the slightest provocation and without any rhyme or reason. Hence, the respondents are not proper persons. They cannot maintain such an action. By their conduct, they have demonstrated that they are not entitled to maintain an action.

20. With regard to the allegations of discrepancy, in the stock, the Commissioner's report reads as follows :

Physical verification of the jewels jointly conducted by both parties in my presence tallied with the stock statement with negligible difference. No

other stock of raw-gold, silver, precious stones etc. was reported in the Coimbatore show room. No stock of any kind was also reported in the

company's factory at Coimbatore which is housed behind the showroom in the same building. A quantity of 575.490 grams of gold was reported

to be with the following artisans as on November 16, 1998, as work-in-progress for making jewels.

I called upon Hari Loganathan, director of the company to arrange for production of the above quantities of gold for my verification on November

18, 1998 at Coimbatore. The artisans at Serial Nos. 1 and 2 above turned up. The gold stock brought by the artisan at Serial No. 2, above,

Nandu was verified jointly by Hari Loganathan and K.R.S. Anand Kumar in my presence with reference to the carbon copy of the relevant issue

voucher. Finally, in view of the extreme positions taken by the parties, the matter could not be proceeded further and had to be left at that. Though

the quantity is not material, the stocks to remain with the artisans since May, July and September, 1998, is prima facie for too long a time.

21. The Commissioner has referred to in para, 2(4), to the stock position as per the computer stock statement and physical stock. He has stated

as follows :

Gold stock as per computer statement -- 2,130,510 gms.

Stock as per physical verification -- 2,188.375 gms.

Difference -- 57.865 gms. (excess)

Silver articles as per computer statement -- 8,219.830 gms.

Stock as per physical verification -- 2,281.34 gms.

Difference -- 352.350 gms. (excess)

Precious stones as per computer statement -- 2,396.75 gms.

Stock as per physical verification -- 2,281.34 gms.

Difference -- (-115.41 gms.).

22. The reasons for the difference as above have been explained in the company's letter dated December 23, 1998.

23. From the report of the Commissioner, we find that there was no discrepancy in the stock. In fact, the stock on hand as regards gold and silver

was found to be in excess. Regarding precious stones, they were with the artisans and of course they were with the artisans for considerable time.

It is stated that the artisans would require minimum six months to make certain types of gem-studded jewels, though the respondents would say

that it cannot take more than a month. One of the artisans also appeared before the Commissioner and has stated about it. Therefore, the

Commissioner report shows clearly that the allegations made by the respondents are patently false. The report of the Commissioner does not

support any prima facie case in favour of the respondents.

24. The main accusation is that a sum of Rs. 1.37 crores was siphoned off by way of loans and advances to different parties. The company paid

Rs. 45 lakhs on May 31, 1995, and Rs. 20 lakhs on July 22, 1995 to A. M. Consultancy. The first payment was made by way of cheque drawn

on Punjab National Bank and the second payment was made by way of demand draft obtained from Tamil Nadu Mercantile Bank. The cheques in

both the cases were issued under the joint signatures of K. R. S. Anand Kumar and Hari Loganathan. A sum of Rs. 16.32 lakhs was received

back on September 4, 1995, thus leaving the outstanding of Rs. 48.68 lakhs. In the accounts, interest at 18 per cent. has been provided for up to

March 31, 1996. There was also a letter of confirmation dated March 31, 1996, signed on behalf of A. M. Consultancy, acknowledging the

principal sum of Rs. 48.68 lakhs and the accumulated interest of Rs. 7.58 lakhs. The Commissioner called upon the debtor A. M. Consultancy to

state the purpose for which the amount in question was borrowed. A reply was sent, stating that the amount was received for the purpose of

subscribing to the shares of Anugraha Jewellers from the public issue as well as from the market, and they have purchased the shares and

requested Anugraha Jewellers to take delivery. In spite of reminders, they have not taken delivery and therefore, they do not have to pay any amount to them. It is to be pointed out that the payment was made by way of two cheques, signed not only by Hari Loganathan, but also by one of the respondents, viz., K.R.S. Anand Kumar. Therefore, it is not open to the respondents to state that they did not know anything about the transaction and that it was done without their knowledge or consent or without their authority. Thus, they are parties to the transactions. To disown any knowledge will be, but futile. The accounts show that interest has been provided up to March 31, 1996. Thus, a sum of Rs. 96.32 lakhs was received back, leaving one instalment of Rs. 48.65 lakhs. These transactions have taken place in the year 1995. It is not known why they should wait till 1998 to take action. It is apparent that owing to certain disputes, inter se, and perhaps aggrieved by the fact that at the annual general body meeting, they were thrown out by the shareholders, they have resorted to such application. The respondents stand tainted by their conduct. Having participated, it is not open to them to make it an issue, Nurcombe's case [1985] 1 All ER 65 ; 3 Comp LJ 163 (CA). Hence, this attack peters out. Further, a bad decision cannot be called a mismanagement. The Commissioner was not competent to doubt the genuineness of the transactions in the face of the facts referred to above. The director of the defendant's company has marked a statement before the Commissioner.

25. Now, coming to the issue and transfer of shares, the allegation is that K.R.S. Suresh and K.R.S. Mani have been issued only 1,74,000 shares as against 2,50,000 shares due to them, resulting in short issue of 76,000 shares. The other allegation is that 1 lakh shares of K.R.S. Anand Kumar have been wrongfully transferred to Hari Loganathan by tampering with the transfer deed and manipulating the records. It is also alleged that L. Prakash has been issued share certificates only for 3,30,000 shares as against 3,50,000 shares standing in his name, resulting in non-issue of share certificates for 20,000 shares. It was stated that K.R.S. Suresh had issued a cheque for Rs. 8 lakhs for which two applications were made. One by Mr. K.R.S. Mani for 30,000 shares and another by Mr. Hari Loganathan for 50,000 shares. The consideration of Rs. 5 lakhs was paid on the next day to K.R.S. Suresh by Hari Loganathan by way of cheque drawn on Dena Bank, dated March 24, 1995. Thus, the statement mentions the

return of the said amount to K.R.S. Suresh to Hari Loganathan on the next day. But, the Commissioner has observed that the crucial question is

why K.R.S. Suresh would pay for the application of Hari Loganathan and what authority Hari Loganathan had to appropriate to himself the

remittance received from Suresh.

26. I do not think that the Commissioner was justified in posing such a question, which is clearly beyond his authority or power. The Commissioner

has stated that as against the remittance of Rs. 8 lakhs made by K.R.S. Suresh to the company, he has been issued shares only to the extent of Rs.

3 lakhs and he has a valid claim for issue of shares for the remaining amount of Rs. 5 lakhs. Such a case has not been even projected by the parties

concerned. Thus, we find that there is absolutely no warrant in the peculiar circumstances for the Company Law Board to have intervened at all.

The observations of the Commissioner that K.R.S. Suresh has been issued shares only to the extent of Rs. 3 lakhs and that he has a valid claim for

the remaining 5 lakhs is obviously wrong. It is not even an allegation of the petitioners.

27. Even assuming that there is dispute with regard to issue of shares, the Company Law Board has no authority. Nor, on that ground, can it

supersede the board. There are sufficient provisions in the Companies Act, 1956, to take care of it and resolve it. In this connection, it will be

fruitful to refer to Section 111, Sub-sections (4), (5), (6) and (7) and Section 113 of the Companies Act. With regard to non-issue of shares, the

allegations are denied and the Commissioner has himself stated as follows :

No doubt that the statement also mentions return of the said amount to K.R.S. Suresh by Hari Loganathan on the next day.

28. Therefore, it is not clear how and on what ground, it is open to the Company Law Board to have interfered. The Company Law Board found

that it was treading upon slippery ground. Therefore, the Company Law Board has not been able to decisively say that there has been

mismanagement. For, we find that the Company Law Board has stated as follows (headnote of [2000] 100 Comp Cas 665 :

Even though the petitioners claim that they were not aware of the diversion of the funds, yet, they cannot absolve themselves as the third petitioner

has been a signatory to some of the cheques issued in connection with loans and

advances.

29. Yet, it is not known how on a petition by a person who has been party to such action, the Company Law Board chose to take further action.

30. In para. 36 of its order, while referring to shortage of stock of gold, the Company Law Board has been rather specious. For, it has glossed

over this aspect by saying that because there is excess of stock, it shows that there is possibility of the stock on hand being different from the one

as shown in the stock register. Whereas, the case is that there has been misappropriation and defalcation.

31. With regard to variations in the accounts circulated to the board and the one published in Economic Times, the Company Law Board has

stated clearly that the petitioners are not justified in making this an issue, as we find that the one circulated to the board had been discussed by the

board and the board approved results had been published. I do not find anything from the order of the Company Law Board to show that a

definite finding has been reached by the Company Law Board that there is any mismanagement. The Board has also mentioned in its order that the

board sought the approval of the general body to sell back the building to the petitioners within a year thereafter for Rs. 115 lakhs, and the general

body approved auctioning of the building to the highest bidder. It is not known how, when the general body has approved, it can be stated that the

board or members are acting against the interest of the shareholders. I am not prepared to accept that any question of misconduct would arise at

all. The Company Law Board has simply adopted the reasonings of the Commissioner.

32. In the facts and circumstances, I am unable to accept that there is any proof of misconduct which alone would empower the Company Law

Board to interfere. The Company Law Board has simply adopted, if I may say so, the reasoning of the Commissioner. The jurisdiction of the

Company Law Board or the court is not to decide the dispute between the parties *Shoe Specialities Ltd. v. Standard Distilleries and Breweries*

(P.) Ltd. [1997] 90 Comp Cas 1 (Mad); [1997] 1 Comp LJ 243. The Company Law Board was aware of the fact that it was treading on

slippery ground. For, the Company Law Board has observed that though the petitioners claim that they were not aware of the diversion of the

funds, yet, they cannot absolve themselves as the third petitioner has been a signatory to some of the cheques issued in connection with the loans

and advances. Again, it has observed that the Company Law Board is of the view that the petitioners are not justified in making this an issue as the

board find that the one circulated to the board had been discussed and the board approved results had been published. The Company Law Board

has again pointed out that a decision of the board in general body in a democratic manner may not be subject to judicial scrutiny. Yet, it did so. It

is not known how it can say after all that the annual general meeting was not properly held, yet, how, without any basis, it can say that there is any

act of oppression ?

33. The Company Law Board has thus not agreed with the petitioners on main issues. It also concedes that it will not be proper to interfere with

the democratic functioning of the company. Yet it, in a superficial manner and though conscious of its limitation, has chosen to order this petition. It

cannot be concluded from the materials before the court that respondents Nos. 1 to 4 herein can state that their rights of the shareholders are

affected in any manner. It is not a case, where oppression has been established. In this case, necessary condition u/s 397 has not been complied

with. In the absence of certain specific pleadings, we find that certain observations have been made by the Company Law Board. Necessary

ingredients under Sections 397, 398 and 403 of the Companies Act have not been satisfied in this case.

34. The order of the Company Law Board, therefore, is untenable in law and unjustified on facts. From the very findings given by the Company

Law Board, it is clear that the Company Law Board having found most of the points against the petitioners, somehow have persuaded themselves

to order the petition, which is really surprising. There is no proof of mismanagement. On the materials placed, there is nothing to show that the

company has been acting against the interest of the shareholders. In respect of the transaction that took place in 1995 to which the petitioners were

parties, they have chosen to cite it as a ground, when they filed application before the Company Law Board in the year 1998. Yet having taken

note of this fact, it is strange that the Company Law Board allowed them to take advantage of their own mistake by ordering the petition.

Therefore, I am satisfied that the order passed by the Company Law Board cannot be sustained at all and it has to be set aside.

35. In the result, the two CMAs. are allowed, setting aside the order passed by the Company Law Board. The administrator appointed by the

Company Law Board will hand over immediately the entire management to the board of directors. The cost of the appeal shall be paid by the

respondents. Consequently, C. M. P. Nos. 4439 to 4441 of 1999 shall stand dismissed.