
(1992) 04 MAD CK 0040

In the Madras High Court

Case No : Company Petitions No's. 93 and 101 of 1984

D.C. Kothari and another

APPELLANT

Vs

Assistant Registrar of Companies

RESPONDENT

Date of Decision : 24-04-1992

Acts Referred:

Companies Act, 1956 — Section 372, 372(12), 372(13), 372(14), 372(2)

Citation : (1992) 04 MAD CK 0040

Hon'ble Judges : S. Marimuthu, J

Bench : Single Bench

Advocate : S. Govindswaminathan, for the Appellant; V. Srinivasamoorthy, for the Respondent

Judgement

Maruthamuthu J.

1. Company Petition No. 93 of 1984 has been filed by two erstwhile directors of the Investment Trust of India Ltd. The other Company Petition

No. 101 of 1984 has also been filed by another director of the same company. Both the petitions have been filed u/s 633(2) of the Companies

Act, 1956, for directions regarding notice under rule 23C of the Companies (Court) Rules, 1959. Both the petitions may be disposed of together

by a common order.

2. The averments contained in both the applications are generally that these petitioners were the directors of the Investment Trust of India Ltd., a

company having its registered office at Kothari Buildings, 117, Nungambakkam, Madras-600 034, from June 9, 1980, to July 4, 1983; from June

9, 1980 to August 26, 1982 and from June 2, 1977 to June 23, 1982, respectively. The aforesaid company was incorporated in the year 1946

with the sole object of carrying on the business of the investment trust by

investing in shares, stocks, debentures and other types of securities. The memorandum of association will clearly bring out the aforesaid object and, accordingly, the shares and other securities were bought for investment and were kept for long-term and sold only rarely. In the year 1975, the objects clause of the memorandum of the company was enlarged, empowering the company to undertake certain other activities like hire-purchase, leasing, industrial financing, etc. However, even after such amendment, the basic character of the company as an investment company continued unchanged, and the company continued to acquire shares as a result of which, the earnings from investments rose from 0.91 lakhs in 1976 to 2.42 lakhs in 1979. Further, this company has also been classified by the Central Government as an investment and trust company in the Central Government publication Directory of Joint Stock Companies issued in 1980. While so, the respondent, the Registrar of Companies, by letter dated January 6, 1982, raised a query whether the company's investment in shares of other companies are within the limits of section 372 of the Companies Act. For the same, a detailed reply was sent on January 29, 1982, stating that the company is an investment company and that the provisions regarding the ceiling prescribed u/s 372 of the Companies Act are not applicable to it. It was further submitted that after being satisfied by this explanation there was no further query by the respondent, nor was any action taken by the respondent against the company or its directors.

3. Again, by letter dated September 26, 1984, addressed to the directors of the company, the respondent stated, that from the balance-sheets of the company as on December 31, 1979, December 31, 1980, December 31, 1981, and December 31, 1982, and from the paid-up capital reflected in the balance-sheets, it was noticed that the investments made by the company were in excess of the limits specified in the first proviso to section 372(2) of the Companies Act, 1956. It was further stated since these investments were made without following the provisions of sub-section (4) of section 372 of the Act, why penal action should not be initiated against the company and the directors for contravention of the aforesaid provisions of the Act. For the same, the company has also sent a detailed reply dated October 29, 1984. However, as the petitioners apprehend that the respondent may initiate action, the petitioners have filed the

present company petition praying this court to exercise its powers

u/s 633, sub-section (2) of the Act and relieve the petitioners from any liabilities arising from the contravention of the first proviso to section 372,

sub-section (2) and section 372, sub-section (4) of the Companies Act, 1956, as set out, in the show-cause notice dated September 26, 1984.

4. The respondent, Registrar of Companies filed counters raising the following contentions. At the outset, the petition u/s 633(2) of the Act filed by

the petitioners is not maintainable, since as per the aforesaid section, every officer claiming relief u/s 633(2) has to file a separate petition and

establish to the satisfaction of the court, that he has acted honestly and reasonably. Further, the claim of the petitioner-company as an investment

company is not maintainable in law. After diversification of its business in 1975, the company's income from investments is meagre and ranks III or

IV place as per the details given in the counter. Inasmuch as the company is changed to a financial company and the income from the financial

business is the major income of the company, the company is not an investment company. Again, regarding the term "Principal business" though

there is no definition under the Act as commonly understood, principal business means the prime business carried on by the company at the

relevant point of time and the major source of income, etc. Applying these principles and also as revealed by the company's own account that the

income from investment business forms only a negligible part in the total turnover of the company, the company ceased to be an investment

company. Clauses 7, 8, 8A and 8B of the memorandum of association referred to by the petitioners are in the nature of incidental objects with

wide clauses covering many business. However, since the company is not engaged in the business of financing the financial enterprises in India as

seen from its balance-sheet, there is no question of applying section 372(14) for exemption. It is incorrect to state that the petitioners have acted

honestly and reasonably. As there are no convincing reasons for the grant of such relief, the powers u/s 633(2) of the Act cannot be exercised by

the court. In the circumstances, the respondent would pray for the dismissal of the aforesaid company petitions.

5. The following points arise for consideration in these petitions :

(1) Whether the petitioner company continues to be an investment company and

could claim that the first proviso to section 372(2) of the Act will not be applicable to it ?

(2) Whether the petitioner company can invoke exemption u/s 372(14) of the Act ?

(3) Whether the petitioners have acted honestly and reasonably and are entitled to any relief u/s 633 of the Act ?

6. It is an admitted fact that the company in question was originally started as an investment company and was investing in shares, debentures and

securities. But, in the year 1975, the said activities of the company have been extended to other fields such as hire-purchase, leasing, etc., and,

accordingly, the memorandum of association was also amended. It is not in dispute that pursuant to such amendment, the company extended its

activities to the financial lines. Now, the dispute leading to the filing of the present petitions arose from a letter communicated by the Registrar of

Companies dated January 6, 1982, in respect of the accounts filed for the year 1979, seeking a query whether the company's investment in shares

of other companies was within the limits of section 372 of the Companies Act. The company has sent a reply on January 29, 1982, thereto stating

that the company being an investment company, the provisions of section, 372(2) and (4) of the Companies Act, are not applicable to it. However,

it seems that there was no further communication between the parties till September 26, 1984, when the respondent sent a show-cause notice to

the petitioners and the other directors, and the company, stating that it is reflected from the balance-sheets of the company as on December 31,

1979, December 31, 1980, December 31, 1981, and December 31, 1982, and from the subsidiary capital (originally stated in the show-cause

notice as paid-up capital which is admitted by the respondent in the counter-affidavit as mistake) the investments made by the company in the other

companies, were in excess of limits specified in the first proviso to Section 372(2) of the Companies Act, 1956, and that those investments were

made without following the procedures mentioned in section 372(4). Consequently, the respondent directed the petitioners to show cause why

penal proceedings should not be initiated against the company for such violations.

7. The petitioner-company seems to have sent a detailed reply on October 29, 1984, followed by a further reply dated January 12, 1985, stating

that the show-cause notice issued by the respondent is not sustainable on several grounds as stated in the reply letters. Notwithstanding the sending of such replies, the petitioners would apprehend that the respondent may initiate criminal proceedings and so they have approached this court, praying that this court should exercise its powers u/s 633(2) of the Companies Act, and relieve the petitioners from any liability resulting from the contravention of the proviso to section 372(2) and section 372(4) of the Companies Act as set out in the respondent's show-cause notice dated September 26, 1984.

8. Learned senior counsel, Mr. Govindaswaminathan, appearing for the petitioners, submitted that the show-cause notice dated September 26, 1984, issued by the respondent is not sustainable on several grounds. He stated that the company in question is an investment company primarily with the object to carry on business of investment in shares, debentures and securities and that the shares were purchased and kept for long time. He added that the memorandum of association will also clearly prove that the object of the company is to make investment in shares, etc., and also basically, the company is an investment company. It was further submitted that it was no doubt in the year 1975, the activities of the company were enlarged to other fields such as hire-purchase, etc., as shown in the memorandum of association, but that notwithstanding such change of enlarging such activities, the investment in shares figured as prime business and hence the character of the business, i.e., investment on shares, was unchanged, and that, therefore, the company still continues to be an investment company. In support of this contention, learned senior counsel would rely on the Central Government publication entitled Directory of Joint Stock Companies issued in 1980 and also the classification issued by the Ministry of Law and Justice and Company Affairs, stating that the words in section 372 ""whose principal business is the acquisition of shares would imply that the company concerned is expected to hold the shares acquired by it for a reasonable time. Further, on the earlier occasion when the respondent raised such a query by his letter dated January 6, 1982, for which the petitioner-company has given a detailed reply dated January 29, 1982, the respondent was satisfied with the explanations and did not raise any further query, and that being so, the respondent cannot take up

the issue again. It was submitted that as there is no change of circumstances warranting such revival of the proceedings, the company still continues to be an investment company and that the restrictions prescribed in the proviso to section 372(2) will not apply to the petitioner company in view of the provisions of section 372(13).

9. In reply to this argument, Mr. V. Srinivasamoorthy, learned counsel appearing for the respondent, would submit that it is incorrect to state that the company continues to be an investment company. He submitted that even though the company originally carried on the business of investment in shares, debentures and securities, it has, however, in the year 1975, changed its activities to those of hire-purchase, leasing, real estate, etc., and that from a perusal of the balance-sheets submitted by the company at the relevant point of time it will undoubtedly reveal that financial activities other than investments have become the prime business. He, therefore, contended that the company had lost its character or an investment company. In support of the contention, learned counsel for the respondent would rely upon the following figures :

10. In view of the above, learned counsel would contend that the petitioner company ceased to be an investment company and that hence the company cannot seek protection u/s 372(12) of the Act. On a careful consideration of arguments of both sides, I am inclined to accept the case of the respondent. Even though the company was originally incorporated with the principal object of carrying on the business of investments in shares, debentures and securities and which it carried on for quite some time, the business of the company in the other fields are comparatively extensive as borne out from the balance-sheets, after the expansion of its activities in the year 1975 in the other fields such as hire-purchase, etc. Therefore, even though the prime object of investments stand on record, at the relevant point of time, in practical aspect, the principal business of the company has changed into other activities, attracting the application of the provisions of section 372(2) and (4) of the Companies Act. The contention of learned senior counsel for the petitioners that since the respondent did not initiate further proceedings on the earlier occasion pursuant to the first letter dated January 6, 1982, and the company's reply dated January 29, 1982, consequently, the respondent cannot initiate action

pursuant to the present show-cause notice, is not sustainable. I am of the view that the company in question is not an investment company and hold

this point against the petitioner.

11. Mr. Govindaswaminathan, learned counsel appearing for the petitioners, next contended that even assuming that the company had lost the

character of investment company due to the subsequent enlargement of its financial activities, still in view of the exemption granted u/s 372(14), the

company is exempt from the purview of section 372, sub-sections (2) and (4), and that on this ground also, the impugned action taken by the

respondents is not sustainable in law. Section 372, sub-section (14) reads :

372(14). This section shall not apply -

(a) to any banking or insurance company;

(b) to a private company, unless it is a subsidiary of a public company;

(c) to any company established with the object of financing, whether by way of making loans or advances to, or subscribing to the capital of,

private industrial enterprises in India, in any case where the Central Government has made or agreed to make to the company a special advance

for the purpose or has guaranteed or agreed to guarantee the payment of moneys borrowed by the company from any institution outside India;

(d) to investments by a holding company in its subsidiary;

12. A perusal of the above provision will make it clear that unless the company is established with the object of financing private industrial

enterprises in India, the question of seeking exemption will not arise. In the present case, the balance-sheets of the company will reveal that the

company, of course, engaged in financing, but not to any private industrial enterprises in India to any company and so, it is not a subsidiary of any

public company as mentioned in sub-section (14) of section 372. In the circumstances, there can be no basis or justification in seeking exemption

u/s 372(14). The grant of exemption u/s 372(14) cannot apply to the petitioners. On a careful consideration, I hold this point also against the

petitioner company.

13. Learned senior counsel would finally argue that in any case even assuming that the petitioner-company is not an investment company or is not

coming within the purview of exemption provision, still the alleged violation of

the provisions of the first proviso to section 372, sub-sections (2) and (4) could be treated only as a technical violation at the worst, and taking into consideration the circumstances under which such violation could have been made, i.e., on the bona fide impression that the company is an investment company, the petitioners must be deemed to have acted honestly and reasonably. It was submitted that having regard to all the circumstances of the case, they may fairly be excused by exercising the powers of this court u/s 633 and be relieved from any liability as mentioned in the show-cause notice dated September 26, 1984. But, learned counsel for the respondent submitted that since the petitioner were fully aware of the fact that the nature of their business substantially changed, and, consequently, the company has lost the character of investment company, it cannot be said that they acted honestly or reasonably and that, therefore, the question of invoking the jurisdiction of this court u/s 633 is not justified. On a consideration of the facts and circumstances of the case, I find that no doubt the company was started with the main object of carrying on the business of investments in shares, debentures and securities, but later, due to enlargement of its activities, the main object of the company had switched over to other than investments, which the petitioners were fully aware of and which led to the loss of the character of the company as an investment company and that they cannot claim to have acted honestly or reasonably. The petitioners who must be aware of the procedures as well as the restrictions made in the Companies Act, ought to have taken care to follow the provisions of amendments of the Act and the guidelines given by the Registrar of Companies. I have no other option except to reject the contentions of the petitioners.

14. In the result, both the petitions, C.P. Nos. 93 and 101 of 1984, are dismissed, but without costs.