

(1976) 09 BOM CK 0006

In the Bombay High Court

Case No : Appeal No. 3 of 1975 in Company Petition No. 22 of 1974

Deccan Farms and Distilleries Ltd.

APPELLANT

Vs

Velabai Laxmidas Bhanji

RESPONDENT

Date of Decision : 08-09-1976

Acts Referred:

Companies Act, 1956 — Section 391, 431(1), 433, 434, 447
Securities Contracts (Regulation) Act, 1956 — Section 22

Citation : (1979) 49 CompCas 321

Hon'ble Judges : R.L. Aggarwal, J; B.N. Deshmukh, J

Bench : Division Bench

Advocate : D.R. Poddar and R.C. Desai, for the Appellant; J.B. Chenai, M.U. Patel, for the Respondent

Judgement

Aggarwal, J.—The present appeal is directed against the judgment and order dated 26th November, 1975, passed by a learned single judge of this court in Company Petition No. 22 of 1974.

2. The petitioner, Velabai Laxmidas Bhanji, had given a loan of Rs. 2,500 to a company named Deccan Farms and Distilleries Private Limited on or about 10th September, 1973, for which the said private limited company issued a loan certificate acknowledging the loan of R. 2,500 from the petitioner repayable on 31st August, 1974, being the date of maturity carrying interest thereon at the rate of 15 per cent. per annum. By her attorney's letter dated 26th September, 1974, the petitioner demanded the repayment of the said sum of Rs. 2,500 with interest thereon and by the same letter she gave a statutory notice as required under s. 434 of the Companies Act, 1956. The said statutory notice was addressed to private limited company. It appears that, after the said transaction, the private limited company was converted into a public limited company, and certificate of change dated 19th November, 1973, was duly obtained from the Registrar of Companies. After the said change was made, the public limited company invited subscription from the public and in this connection issued a

prospectus whereby 3,00,000 equity shares of R. 10 each were offered to the public. The subscription was opened on 8th April, 1974, and was to close on 22nd April, 1974. A sum of Rs. 2.50 was required to be paid on application and a further sum of Rs. 2.50 on allotment. It appears that the shares were over-subscribed. The company, however, received Rs. 15 lakhs on the basis of the money paid on application and on allotment in respect of the said 3,00,000 equity shares. The company applied for permission to list the shares on the Bombay Stock Exchange before the expiry of 10 weeks from 22nd April, 1974, as required by s. 73 of the Companies Act, 1956. However, the said permission was withdrawn on 26th April, 1975, on account of the failure on the part of the company to fulfill the various formalities or requirements. Some of the directors of the company filed a complaint with the General Branch, C.I.D., Bombay, in consequence whereof the bank accounts of the company were frozen. Before the bank accounts were frozen, the company utilised about 8 lakhs of rupees out of 15 lakhs of rupees received pursuant to the prospectus for making payment to Messrs. Tawkly Industrial Corporation for the purchase of machinery. It is an admitted fact that the managing director of the company Shri A. B. Patil and his brother, Shri I. B. Patil, who was also a director of the company, are interested in the said Tawkly Industrial Corporation. Although the hands of Shri A. B. Patil were tied down with the freezing of the company's bank accounts, nevertheless he obtained certain orders from this court for withdrawal of moneys. The said account has been naturally reduced to that extent.

3. Reverting to the said letter of demand and the statutory notice dated 26th September, 1974, the public limited company by its letter dated 8th October, 1974, did not dispute its liability and, on the other hand, expressed its extreme regret for the inconvenience caused to the petitioner. It was also stated that the company was trying its best to repay as soon as funds were in its hands.

4. On 28th October, 1974, the petitioner presented a winding-up petition under s. 433(e) of the Companies Act, 1956, on the ground that the company was unable to pay its debts. The petition was accepted on 11th December, 1974. On 15th January, 1975, notice was served upon the company which was made returnable on 5th February, 1975. There was no contest to the admission of the petition and, in the circumstances, the petition was ordered to be admitted and advertised on 14th February, 1975. After being advertised in Times of India and in the government Gazette, the petition came up for hearing on 14th April, 1975, when the company applied for adjournment on the ground that it wanted to settle the matter with the petitioner. At that hearing, it was pointed out to the learned company judge that the company was making payments to other creditors and had in fact paid a sum of Rs. 8,000 to one Anantrao Jadhav & Co. of Kolhapur. In these circumstances, an interim injunction restraining the company and its directors either by themselves or through their employees, servants or agents from disposing of any property or assets of the company as well as from disbursing any amount on behalf of the company until further orders was passed. When the matter came up for hearing on 18th June, 1975, neither

the company nor its directors nor the attorneys on record appeared and a winding-up order was passed which was, however, set aside on 3rd July, 1975. The company filed its affidavit dated 22nd July, 1975, opposing the winding-up petition. In para. 5 of the affidavit, the company admitted its liability to the petitioner and submitted that at present the company is having more than Rs. 7,00,000 liquid cash in the company's various bank accounts, and that due to disputes and differences between the two groups of directors, the management of the company is under a deadlock. It was also pointed out that a false complaint was lodged by some of the directors with the police authorities, as a result of which the amount lying in the banks has been frozen, and the company intended to file a writ petition challenging the validity of the police order freezing the bank accounts of the company. It was also stated that the company had given an ultimatum to various banks to the effect that if their bank accounts were not released, necessary legal action would be taken against them. It was also stated that a sugar plant was a very profitable project and it is hoped that in a very short period the company will be able to pay dividends as also about 300 people in the rural area will get employment opportunities in the company's project which is in a backward area. It was submitted that the company had substantial funds and capacity to start their project and it was only due to non-co-operation of the directors and the deadlock in the management that the company had suffered.

5. During the pendency of the present winding-up petition, the company's then attorneys, M/s. Manilal Kher Ambalal & Co., took out a judge's summons dated 29th August, 1975, asking for permission to withdraw and to pay to themselves a sum of Rs. 15,000 from the account of the company with the Bank of India, Fort Branch, to enable them to defend the present Company Petition No. 22 of 1974 and three other Company petitions Nos. 17 of 1974, 4 of 1975 and 6 of 1975, all for winding up of the company, and another Company Application No. 16 of 1975 for issue of share certificate, and a criminal case pending before the Metropolitan Magistrate. Another reason advanced for the said payment of Rs. 15,000 was that the company desired to prepare a petition for sanctioning a scheme including preparation of and printing of the scheme; thirdly, petition against police authorities for release of books, etc.; fourthly, petition against the Stock Exchange challenging their arbitrary decision of desisting the company; fifthly, petition for convening an annual general meeting; and, lastly, a suit against B. B. Consulting & Engineering Pvt. Ltd. to recover Rs. 51,000, being advance paid by the company towards machineries. It is not necessary to refer to the other prayers of the said judge's summons as they are not relevant for the purposes of this appeal.

6. Notice also may be taken of another Company Petition No. 14 of 1975 filed by Dhunji H. Dhunjibhoy, one of the directors of the company. This was also a petition for winding up of the company on the ground that it is just and equitable that the company should be wound up. In support of this, six circumstances were alleged : (1) That the managing director of the company is carrying on business

of the said company in a fraudulent manner and/or in a manner detrimental to the interest of the company. (2) That the managing director does not command the confidence of the petitioner and the other directors named, Dr. R. R. Hattiangadi, Mr. V. J. Ghatge, Mr. P. R. Kibe and Mr. K. R. Moorthy, and that there is a complete lack of probity on the part of the said managing director. (3) That on account of failure to hold the annual general meeting, there is no properly constituted board of directors to control the management of the said company. (4) That the object for which the said company was incorporated has substantially failed and it is impossible to carry on business in the said company in the near future, and there is no reasonable hope that the said company will carry on any business in the near future. (5) That the auditor of the company has given a report which given the assets and liabilities position of the company as at 31st March, 1973, and 30th September, 1973. Since then the company's books have been audited up to 30th April, 1974, and a balance-sheet has been prepared but with qualified remarks; a profit and loss account of the company has been submitted directly by the auditors to the Registrar of Companies without the signature of the petitioner and/or the said four directors. (6) That the prospectus states that an application will be made to the Bombay Stock Exchange for permission to deal in and for an official quotation of the equity shares of the company. The Stock Exchange has refused permission and/or has not granted permission, and, in the circumstances, by reason of the provisions of s. 73 of the Companies Act, the allotment of shares made by the company has become void and the company has become liable to to pay all moneys received from applicants in pursuance of the said prospectus.

7. When the present winding-up petition reached hearing on 26th November, 1975, before the learned single judge the company's present attorneys, M/s. Poddar and Co., made an application for adjournment on the grounds as stated by Mr. Poddar before us that his firm had been engaged on 24th November, 1975, and that he wanted time to go through the papers and was also considering the question of presenting a scheme. The learned company judge refused the application for adjournment and proceeded to hear the petition on merits. At the hearing, the petitioners in Company Petitions Nos. 17 of 1974, 4 of 1975 and 6 of 1975 appeared and supported the petitioner in the present petition. These three other petitioners were also the creditors of the company in the sums of Rs. 3,000, Rs. 5,000 and Rs. 5,000. According to Mr. Chinai, he had also appeared in support of the Company Petition No. 14 of 1975 and had supported the present petition for winding up. However, neither his appearance nor of his attorneys in Company Petition No. 14 of 1975 is shown. None the less, we have no reason to disbelieve the statement of the learned counsel that he in fact appeared in the said petition and supported the winding up of the company.

8. The learned company judge passed an order winding up the company and appointed the official liquidator to take charge of the assets, properties and all the records of the company. In view of the winding-up order passed in the present company petition, rightly by virtue of s. 447 of the Companies Act, 1956,

no separate order for winding up was passed in the other company petitions except as regards costs.

9. Mr. Poddar, appearing on behalf of the appellant-company, has raised four contentions before us. In the first place, he contended that the petition ought to have been adjourned, inasmuch as he had come on record on 24th November, 1975. His application for adjournment was not a frivolous application but a bona fide one. He submitted that the refusal to grant adjournment has caused miscarriage of justice to the company. We do not find merit in this contention. The petition was admitted on 5th February, 1975, without contest and thereafter advertised. The company had filed its affidavit-in-reply challenging the passing of the order for winding up. Several adjournments were obtained on behalf of the company, the last of which was on 12th November, 1975, on the ground that the client was sick and an adjournment for two weeks was sought. The mere fact that the company had chosen to change its attorneys on 24th November, 1975, when the matter was fixed for hearing on 26th November, 1975, could be no valid ground for adjournment and, in these circumstances, the learned company judge was justified in refusing to adjourn the matter.

10. Mr. Poddar laid great stress on the fact that the company had no funds and by the judge's summons dated 29th August, 1975, it had asked for permission for payment of Rs. 15,000 to its previous attorneys. He vigorously contended that the company's hands were tied and it had no funds to adopt proceedings against the police and the Bombay Stock Exchange at the time when his firm took over the cases of the company. This contention is devoid of any merit. We find that during the pendency of the present appeal, the company continued to make applications to the court for withdrawal of moneys. By two orders dated 27th February, 1976 and 28th April, 1976, amounts to the extent of Rs. 20,250 were allowed to be withdrawn. This included payment of Rs. 4,000 to the present attorneys on record. On being questioned about this amount of Rs. 4,000, we were told by Mr. Poddar that a large amount has been incurred in connection with the scheme prepared by the company under s. 391 of the Companies Act. It is necessary to bear in mind that the above amounts were withdrawn from the separate bank account maintained under s. 73 in respect of moneys received from applicants in pursuance of the prospectus offering 3,00,000 equity shares of Rs. 10 each to the public. Under s. 73, these moneys are required to be repaid with interest to the applicants when the allotment of shares becomes void and cannot be used for any other purpose whatsoever. We seriously doubt the bona fides of the company that on account of want of funds it could not go in appeal against the decision of the Bombay Stock Exchange. We think that this is a false excuse put forth by the managing director of the company, if regard could be had to the fact that a payment of Rs. 8,000 has been made to M/s. Anantrao Jadhav & Co. of Kolhapur. We were told by Mr. Poddar that this amount of Rs. 8,000 was not withdrawn from the subscription moneys. This shows that the managing director has other resources of the company. Again, an amount of Rs. 4,000 has been withdrawn but the managing director has chosen not to file an appeal but

to spend it in his pursuit to present a scheme without bearing in mind his statutory obligations under s. 73.

11. The second contention raised was that the company petition should have been adjourned for six months to enable the company to come out of the deadlock and there would have been no prejudice on that score. In this connection, Mr. Poddar relied upon the paragraph relating to adjournment of petition from Halsbury's Laws of England, Vol. 7, 4th edn., page 615, para. 1030, and also a decision of the Chancery Division in *In re St. Thomas' Dock Company* [1876] 2 Ch D 116. In our opinion, neither the statement from Halsbury nor the authority cited has any relevance to the facts of the present case. The company had sufficient time to come out of its so-called deadlock. The petition was advertised in February, 1975, and the winding-up order was passed in November, 1975. The company had ample opportunity and time. There is no fixed rule of law or principle that the company is entitled to an adjournment for six months as sought to be urged on behalf of the company.

12. The third contention was that the unpaid creditors' right to an order for winding up is not an absolute rule. If the court finds that the winding up is not in the interest of the general body of creditors, it should refuse to wind up the company. In support of this, Mr. Poddar referred to a decision in *In re Greenwood & Co.* [1900] 2 QB 306 and also a decision of the Supreme Court in *Madhusudan Gordhandas & Co. v. Madhu Woollen Industries P. Ltd.* [1972] 42 Com Cas 125 and a decision of this court in *Focus Advertising Pvt. Ltd. v. Ahoora Blocks P. Ltd.* [1975] 45 Com Cas 534 (Bom).

13. In the case before the Supreme Court, creditors to the extent of Rs. 7,50,000 opposed the winding-up petition, whereas creditors demanding Rs. 44,477.56 in all supported the same. In the case of *Focus Advertising P. Ltd.* [1975] 45 Com Cas 534 (Bom) in this court, at the hearing of the petition, affidavits of the eight supporting creditors showed that their claims were of the aggregate value of Rs. 7,68,000 and those opposing the winding up totalled Rs. 3,03,862.07. In all these three cases, the courts considered the wishes of the creditors on both sides. These cases provide a guideline for considering the completing interest of the creditors. The rule is that if there is opposition to the making of the winding-up order by the creditors, the court will consider their wishes and may decline to make the winding-up order. This rule finds place in s. 557 of the Companies Act, 1956. The wishes of the creditors are to be examined by the court. The court has to see whether the case of the creditors opposing the winding up is reasonable and whether there are matters which should be inquired into and investigated if a winding-up order is made. The court can consider the wishes of the creditors "as proved before it by sufficient evidence" as laid down by s. 557. A fact is said to be "proved" when after considering the matters before it, the court either believes it to exist or considers its existence so probable that a prudent man ought, under the circumstances of the particular case, to act upon the supposition that it exists. The creditors who wish that their

wishes should be regarded have to place the necessary evidence before the court. They have to point out reasonable grounds in order to enable the court to ascertain whether the grounds are good. Either the material should be on record or the creditors should place it on affidavit or in some other satisfactory manner to enable the court to determine the competing wishes and make a judicial choice at the hearing. If this is not possible to decide at the hearing, the court can direct that a meeting of the creditors be called and held in such manner as laid down in cls. (b) and (c) of s. 557(1) of the Companies Act, 1956.

14. In the present case, there is no evidence that at the time of the passing of the winding-up order, any of the creditors of the company opposed the petition for winding up. On the other hand, at the time of the hearing of the petition for winding up, three creditors to the extent of Rs. 13,000 had supported the petition for winding up. There is nothing to show that any other creditor was present at the hearing to oppose the present petition for winding up. What was urged on behalf of the company by Mr. Poddar was that a scheme has been presented under s. 391 of the Companies Act, and at the meeting called under the directions of the court under that section, 79 creditors had attended, out of whom 50 creditors to the extent of about Rs. 4,47,000 had voted for the scheme and 26 creditors of the value of about Rs. 88,000 in the aggregate had opposed the scheme. The provision for ascertaining the wishes of the creditors under s. 557 is for a different situation than the one which is contemplated under s. 391. In fact, under s. 391, there is no question of ascertaining the wishes of the creditors by the court. It is a provision for scrutinising the scheme which may be put forth either by the company or by any of the class of creditors or members of the company. In the case before us, at the time of the passing of the order for winding up, there was no evidence at all, much less sufficient evidence, to show that the creditors were opposing the winding up, whose wishes could have been ascertained by the court. It is true that it is not an absolute rule of law that the court is bound to make an order for winding up when the conditions required for winding up exist. It is entirely a matter of judicial discretion. In the present case, in our opinion, the learned company judge has exercised that discretion in a sound and proper manner and there is no reason to interfere with the same.

15. The other question which requires to be considered is whether the order for winding up would benefit the petitioning-creditor or the company's creditors generally. In this connection, Mr. Poddar pointed out that the company has liquid cash of nearly Rs. 7 lakhs, but on account of the obstructive and destructive attitude adopted by some of the directors, the amount is not realisable from the banks as the police has instructed the banks not to allow the operation of the bank accounts. In this connection, the provisions of s. 73 of the Companies Act are being overlooked. Mr. Poddar was grossly in error in treating the amount lying in the bank accounts as an asset available to the company for disbursement at the discretion and sweet will of the company's directors. It is admitted that the Bombay Stock Exchange has withdrawn the permission contemplated under s. 73 since 26th April, 1975, and that no appeal has been filed against that

decision. Sub-section (5) of s. 73 provides that for the purposes of this section, it shall be deemed that permission has not been granted if the application for permission, where made, has not been disposed of within the time specified in sub-s. (1). Sub-section (1), to the extent it is relevant, says that where permission has been applied for before the tenth day after the first issue of the prospectus, or, where such permission has been applied for before that day, if the permission has not been granted by the Stock Exchange before the expiry of ten weeks from the date of the closing of the subscription lists, any allotment made on an application in pursuance of such prospectus shall be void. In the present case, the permission was given subject to certain conditions being fulfilled and since those conditions were not complied with, the permission was revoked. The conditional permission did not amount to grant of the application for permission to deal in shares on the Stock Exchange as contemplated under s. 73(1). The permission intended under that sub-section is an unqualified and wholesome permission. Any qualified permission is as good as not granted and the application should be construed as not disposed of within the time prescribed by sub-s. (1) of s. 73. The amount received from the applicants is required to be kept in a separate account under sub-s. (3) of s. 73 until the permission is granted or the appeal preferred against the refusal to grant such permission is disposed of under s. 22 of the Securities Contracts (Regulation) Act, 1956. The text of sub-s. (3A) of s. 73 reads :

"(3A) Moneys standing to the credit of the separate bank account referred to in sub-section (3) shall not be utilised for any purpose other than the following purposes, namely :-

(a) adjustment against allotment of shares, where the shares have been permitted to be dealt in on the stock exchange or each stock exchange specified in the prospectus; or

(b) repayment of moneys received from applicants in pursuance of the prospectus, where shares have not been permitted to be dealt in on the stock exchange or each stock exchange specified in the prospectus, as the case may be, or, where the company is for any other reason unable to make the allotment of shares."

16. This authorises the utilisation of the money for any one of the two purposes and for no other purpose. The language of s. 73 is simple and clear. This section had been amended by the Companies (Amendment) Act, 1974, whereby greater protection was sought to be given to the investing public, underwriting institutions and trade than higher to before. It also became necessary for the government to have a second look at some of the provisions of s. 73 in view of the judgment in *Union of India v. Allied International Products Ltd.* [1971] 41 Com Cas 127 (SC). Looking to the interest of the investing public, the rate of interest was enhanced from six per cent. to twelve per cent. by the 1974 Amendment, so that the investor received the repayment at a higher interest when the allotment became void under s. 73(1). The 1974 Amendment brought about the substitution of sub-

s. (1) and (5) and insertion of sub-s. (2A), (2B), (3A), and amendment of some other provisions of s. 73 in order to provide several safeguards, but in real life these provisions can be set at naught as in the present case. Although the allotment has become void, yet the moneys have not been repaid with interest in the manner laid down and, on the other hand, over eight lakhs of rupees, out of fifteen lakhs of rupees, have been utilised for purposes other than those specified under s. 73(3A) quoted above. This kind of mischief cannot be avoided unless s. 73 is further amended to prohibit operation of such separate bank account until a company produces the permission of the stock exchange concerned as contemplated under s. 73. It is against such permission that the separate bank account should be allowed to be operated. This case illustrates that more safeguards are needed to give real and effective protection to the investing public, underwriting institutions and trade. There is no check, as this case shows, in misapplying the moneys. In fact, the moneys falling into the coffers of a company pursuant to the prospectus cannot be touched or employed to use unless the conditions contemplated under s. 73 are faithfully complied with.

17. It seems to us that, in using these moneys, the provisions of s. 73 are breached. Such breach is made punishable apart from fixing joint and several liability on the directors. It may be made clear that we are not expressing any opinion on this aspect of the case as the point is not in issue before us. We find that there is no prospect of the company doing any business. There is a complete deadlock among the directors. These directors have filed a winding-up petition on the ground that it is just and equitable that the company be wound up. The majority of the directors do not have confidence and faith in the managing director, Shri I. B. Patil. Large amounts have been paid by them to a concern in which both of them are interested. In these circumstances, it is in the interest of the petitioning creditor and other supporting creditors that the assets of the petitioning creditor and other supporting creditors that the assets of the company should be protected. After all, the object of winding-up by the court is to facilitate the protection and realisation of the assets of a company should be protected. After realisation of the assets of a company with a view to ensure an equitable distribution thereof among those entitled. In our opinion, the winding-up order is in the general interest of all the creditors. However, we make it clear that these observations will not prejudice the scheme which is presented by the company under s. 391 of the Companies Act.

18. The last contention was that the petitioning-creditor should have filed a suit. Winding up is no alternative to the ordinary remedy provided for recovery of a debt. No debt, a winding-up petition is not a legitimate means of selling to enforce payment of a debt, but such a debt should be disputed by the company. There should be some bona fide dispute. In the present case, the debt is admitted. It was admitted in reply to the statutory notice. It was not disputed at the time when the company petition came for admission. It was also not disputed in the affidavit opposing the admission of the petition. In the present case, the deeming provisions of s. 431(1)(a) are clearly attracted as the company has

neglected to pay the debt of the petitioner. There is nothing to show that the petitioner has instituted the present proceedings with any ulterior motive. In these circumstances, the petitioner has rightly availed of the cheap and speedy remedy provided under the Companies Act to creditors who are unable to recover debts, and we see no reason why the petitioner should have been refused this cheap remedy.

19. All the contentions raised on behalf of the company fail.

20. In the result, the appeal is dismissed. The appellant-company is directed to hand over forthwith to the official liquidator all the articles and things of which possession has been taken pursuant to the order dated 2nd February, 1976. The official liquidator to take necessary action immediately. The appellant-company to pay to the respondent costs of the appeal. Costs to come out of the assets of the company.

21. At this stage, Mr. Poddar applies for leave to appeal to the Supreme Court. The same is refused.