

(2005) 08 MAD CK 0049

In the Madras High Court

Case No : C.P. No. 201 of 1996 and C.A. No. 1275 of 1999

ICICI Venture Funds Management Limited

APPELLANT

Vs

Neptune Inflatables Limited
V.G.P. Finances Limited Vs
Official Liquidator

RESPONDENT

Date of Decision : 09-08-2005

Acts Referred:

Companies Act, 1913 — Section 227(2), 230

Companies Act, 1956 — Section 536(2)

Constitution of India, 1950 — Article 141

Provincial Insolvency Act, 1920 — Section 28, 28(1), 28(2), 28(7), 55

Citation : (2005) 127 CompCas 1 : (2005) 6 CompLJ 420 : (2005) 4 LW 134

Hon'ble Judges : D. Murugesan, J

Bench : Single Bench

Final Decision : Allowed

Judgement

D. Murugesan, J.—An important question, as to whether the disposition of the property of a company made during the interregnum between

the presentation of the petition for winding up and passing of an order for winding up, would be ab initio null and void, has arisen in this application.

2. The company in liquidation approached the applicant vide its letter dated November 10, 1995, for a loan of Rs. 1 crore for expansion activities

as well for the purpose of acquisition of assets. In response to the said letter, the applicant informed the company in liquidation, vide its letter dated

November 24, 1995, agreeing for advancement of loan up to a maximum of Rs. 70 lakhs. Pursuant to the said correspondence, a loan agreement

dated December 1, 1995, was entered into between the applicant and the company in liquidation, in and by which it was agreed as follows :

1. That the lender will disburse the said amount of loan periodically to the

borrower.

2. That the lender will while disbursing the loan amount periodically consider the payment record of the borrower for the purpose of determining

the quantity of the disbursement.

3. That the borrower will, if necessary, create security as desired by the lender in terms of the assets of the borrower, present and future.

4. That the borrower will, without any hesitation, provide necessary securities in terms of the assets of the borrower in consideration of the dues

payable by the borrower to the lender and to the satisfaction of the lender.

5. That the borrower will discharge the entire loan by means of sale of its assets, if necessary, to the lender.

6. That the lender and the borrower will execute separate agreements at the time of receiving the amount of loan periodically.

7. That the borrower will not assign or transfer its assets given to the lender as security until the discharge of the entire amount of loan.

8. That in case of any dispute, the courts at Madras alone shall have jurisdiction.

3. Following the above loan agreement, the applicant and the company in liquidation entered into four loan agreements dated January 1, 1996,

January 30, 1996, February 7, 1996 and January 10, 1997, for a sum of Rs. 10 lakhs, Rs. 25 lakhs, Rs. 25 lakhs and Rs. 5,20,901, respectively.

There is no dispute at the Bar that the loan amounts were paid by way of cheques and the receipt of the said amounts have been shown in the

balance-sheet of the company. In terms of the loan, the company also mortgaged the property in question in favour of the applicant on January 31,

1997. The said charge was also intimated to the Registrar of Companies in Form Nos. 8 and 13 and the same was registered on February 26,

1997. As the company did not repay the amounts, in consideration of the amounts and in terms of the deed of mortgage, by two sale deeds dated

February 11, 1999 and February 16, 1999, the property in question was sold in favour of the applicant and possession was also handed over.

4. It appears that, in the meantime, the company petition for winding up was presented on October 14, 1996 and the company was ordered to be

wound up on March 10, 1999. Following the order of winding up, the official liquidator issued a notice to the applicant on June 1, 1999, for

handing over of the assets and effects of the company in liquidation. An

inspection was carried on in the premises on June 8, 1999 and the office premises was locked by the official liquidator indicating the fact that possession was taken over. In the circumstances, the applicant has approached this court for a direction to the official liquidator to deliver possession of the property in No. 5/364, (New No.) Mootakaran Chavadi, Thuraipakkam, Old Mahabalipuram Road, Chennai-600 096.

5. It is the case of the applicant that the transaction was bona fide and in terms of Sub-section (2) of Section 536 of the Companies Act, 1956, all transactions are not ab initio void and if the applicant is able to satisfy the court that the transaction is bona fide, it would not be declared as void by this court. Learned counsel would further submit that from the sequence of facts it could be seen that the transaction was bona fide and the entire consideration as to the property was also paid to the company in liquidation by way of cheques and the payments had also been received and the charge was also intimated to the Registrar of Companies. In support of the said submission, learned counsel relied upon the judgments of the Supreme Court in Pankaj Mehra and Another Vs. State of Maharashtra and Others, and in Sankar Ram and Co. v. Kasi Naicker 2003 AIR SCW 3732.

6. On the other hand, the official liquidator submitted that the sale deeds are not bona fide. According to the official liquidator, all transactions are void against the official liquidator in terms of Sub-section (2) of Section 536 of the Companies Act. He would also submit that the judgments of the Supreme Court relied upon by learned counsel for the applicant would be applicable only in case of day-to-day transactions for the administration of the company and not for the sale of the property or assets. Hence, he submitted that the transaction was not bona fide.

7. I have carefully considered the rival contentions. The application came up for consideration earlier before the learned single judge who, by an order dated November 29, 2004, dismissed the same. The applicant preferred O. S. A. No. 13 of 2005 questioning the said order. A Division Bench of this court, by an order dated March 7, 2005, passed the following order :

We are of the view that the question raised in the appeal is covered by the decision of the Supreme Court in the case of Pankaj Mehra and

Another Vs. State of Maharashtra and Others, , wherein the Supreme Court has construed Section 536(2) of the Companies Act in paragraph 14

of the judgment and after considering the judgment of the Bombay High Court in the case of Tulsidas Jasraj Parekh v. Industrial Bank of Western

India AIR 1931 Bom 2 ; the judgment of the Gujarat High Court in the case of Navjivan Mills Ltd., In re [1956] 59 Comp Cas 201 and the

judgment in the case of Gray's Inn Construction Co. Ltd., In re [1980] 1 All ER 814 (CA) and held that it is difficult to lay down all dispositions of

property made by a company in the interregnum between the presentation of a petition for winding up and the passing of the order for winding up

would be null and void. The Supreme Court held that if such a view is taken, the business of the company would be paralysed, for the company

may have to deal with very many day-to-day transactions, make payments of salary to the staff and other employees and meet urgent

contingencies and an interpretation which could lead to such a catastrophic situation should be averted.

The decision of the Supreme Court is an authority for a proposition that the disposition of the property made by the company after the presentation

of the winding up petition, but before passing the order for winding up does not automatically become null and void and in each case the court has

to examine whether the transfer of the property is valid or void in law.

We are of the view that unless the court declares the transaction and transfer to be valid, it should be treated as void u/s 536(2) of the Companies

Act and to declare a transaction as valid, the court shall examine the facts on the basis of the evidence that may be let in by the parties to find out

whether the transaction is valid or not. We find that the learned judge has proceeded on the basis that a transfer made after the presentation of the

petition and before the order of winding up, would be void automatically. We are of the view that the learned judge should consider the question

whether the transaction would be valid or not on the basis of the evidence that may be let in by the parties. Since that exercise has not been done,

we, without expressing any opinion on the merits of the case, are inclined to remit the matter to the learned judge to decide the question afresh as

to whether the transfer of the immovable properties is valid or not on the basis of the evidence that may be let in by the parties.

8. On the above backdrop, the application is remanded for fresh hearing and disposal. Section 536(2) contemplates avoidance of transfers or

disposition of any property of a company after the commencement of the winding up proceedings, as such proceedings are void. The date on

which the petition for winding up is filed shall be the date from which the winding up proceedings are deemed to have commenced for the purpose

of applicability of the provisions of Section 536(2) of the Companies Act. It is the case of the official liquidator that as the winding up proceedings

commenced on October 14, 1996, the sale deeds executed on February 11, 1999 and February 16, 1999, are void in terms of Section 536(2).

The question as to the avoidance of transfer under Sub-section (2) of Section 536 of the Companies Act came up for consideration before the

Supreme Court in Pankaj Mehra and Another Vs. State of Maharashtra and Others, . As the application of the provision of Section 536(2) is

discussed in detail, the relevant paragraphs of the Supreme Court judgment are reproduced below (pages 423 to 426) :

In the above backdrop alone we can consider the impact of the legislative direction in Section 536(2) that any disposition of the property of the

company made after the commencement of the winding up (i.e., after the presentation of a petition for winding up) shall be void. There are two

important aspects here. The first is that the word "void" need not automatically indicate that any disposition should be ab initio void. The legal

implication of the word "void" need not necessarily be a stage of nullity in all contingencies. Black's Law Dictionary gives the meaning of the word

"void" as having different nuances in different connotations. One of them is of course "null, or having no legal force or binding effect". And the

other is "unable in law, to support the purpose for which it was intended". After referring to the nuances between void and voidable the

lexicographer pointed out the following :

"The word ""void"" in its strictest sense, means that which has no force and effect, is without legal efficacy, is incapable of being enforced by law, or

has no legal or binding force, but frequently the word is used and construed as having the more liberal meaning of ""voidable"".

The word ""void"" is used in statutes in the sense of utterly void so as to be incapable of ratification, and also in the sense of voidable and resort must

be had to the rules of construction in many cases to determine in which sense the Legislature intended to use it. An act or contract neither wrong in

itself nor against public policy, which has been declared void by statute for the protection or benefit of a certain party, or class of parties, is

voidable only".

For discerning the legislative idea in employing the word "void" in the context set out in Section 536(2) of the Companies Act the second aspect to

be noticed is that the provision itself shows that the word void is not employed peremptorily since the court has power to order otherwise. The

words "unless the court otherwise orders" are capable of diluting the rigour of the word "void" and to choose the alternative meaning attached to

that word.

In *Chittoor District Co-operative Marketing Society Ltd. v. Vegetols Ltd. (In Liquidation)* [1987] (Suppl.) SCC 167 a two-judge Bench of this

court considered a plea for validation of payments made by a company after presentation of a petition for winding up. One set of payments were

made before the passing of the winding up order and the other set of payments were made thereafter. This court declined to validate such

payments on the ground that--

"there is no evidence to show that those payments were made either under compulsion of circumstances in order to save or protect the property of

the company or that there was any commercial compulsion to enable it to run its business". (SCC p. 169, para. 4)

The decision only indicates that such payments could have been made valid if evidence was adduced to show that there was compulsion of

circumstances. In fact, this decision lends support to the interpretation that the payments which were made after the commencement of winding up

proceedings, would not become ab initio void.

An early decision of a Division Bench of the Bombay High Court in *Tulsidas Jasraj Parekh v. Industrial Bank of Western India* AIR 1931 Bom 2

was sought to be relied on by most of learned counsel who argued for different appellants. The question which the court considered therein

pertained to Section 227(2) of the old Companies Act, 1913, which was identical to Section 536(2) of the present Act. Certain payments made

by a company after commencement of the winding up proceedings were

questioned and the Division Bench considered the scope of the sub-section and noticed that the principle had been borrowed from the English Companies Act. Hence some of the English authorities were also referred to by Marten C.J., who spoke for the Division Bench. The learned judges stated thus (page 10) :

"Now here as regards Section 227(2) the court has to steer a middle course between two extremes. On the one hand the words of the section are wide enough to include any sale or payment that a company may make after the date of the winding up petition. On that basis any business would practically have to be stopped if a petition was presented, because it would be unsafe to dispose of any of the company's assets. For instance, a mill company might not be able to buy a ton of coal for the use of its furnaces, or, on the other hand, it might not be able to sell any of its goods in the ordinary course of business. Consequently, the court has very properly laid down that, speaking generally, any bona fide transaction carried out and completed in the ordinary course of current business will be sanctioned by the court u/s 227(2). On the other hand it will not allow the assets to be disposed of at the mere pleasure of the company, and thus cause the fundamental principle of equality amongst creditors to be violated. To do so would in effect be to add to the preferential debts enumerated in Section 230 a further category of all debts which the company might choose to pay wholly or in part".

It is useful to refer to the reasoning adopted by a Division Bench of the Gujarat High Court in *Navjivan Mills Ltd., In re* [1986] 59 Comp Cas 201 in favour of adopting a pragmatic attitude when a company court was approached for approval of certain dispositions which a company made after presentation of a petition for winding up. A clear distinction was drawn by the Division Bench between the period till the passing of the order for winding up and thereafter, so far as dispositions are concerned. The following reasoning is useful for consideration of the issues involved

(headnote) :

The court can exercise the jurisdiction u/s 536(2) of the Companies Act, 1956, of giving directions validating proposed transactions pending a petition for winding up but before the winding up order is made for the obvious reason that unless these transactions are saved from the

consequence which may ensue, if, at all, on an order of winding up being made, the company might find it difficult to keep itself going and its business might be paralysed. The purpose underlying the investment of the power in court is for the benefit and the interest of the company so as to ensure that a company which is made the subject of a winding up petition may nevertheless obtain the money necessary for carrying out its business and so as to avoid its business being paralysed. If that is the purpose and object of the section, it would hardly be proper and just to stultify the power and restrict its operation since otherwise it is bound to be counter-productive in the sense that the very purpose of keeping the company as a going concern so as to ensure the interest of the shareholders and creditors would be defeated".

In *Gray's Inn Construction Company Ltd., In re* [1980] 1 All ER 814 the Court of Appeal (Civil Division) considered the principle on which

discretion of the court to validate the dispositions of property made by a company, during the interregnum between presentation of a winding up

petition and the passing of the order for winding up, has been dealt with. Section 227 of the English Companies Act, 1948 is almost the same as

Section 536(2) of the Indian Companies Act. Dispositions which could be validated are mentioned in the decision. The said decision was cited

before us in order to emphasise the point that courts would be very circumspect in the matter of validating payments and the interest of the

creditors as well as the company would be kept uppermost in consideration. Be that so, the said decision is not sufficient to support the contention

that disposition during the interregnum would be irretrievably void.

It is difficult to lay down that all dispositions of property made by a company during the interregnum between the presentation of a petition for

winding up and the passing of the order for winding up would be null and void. If such a view is taken the business of the company would be

paralysed, for, the company may have to deal with very many day-to-day transactions, make payments of salary to the staff and other employees

and meet urgent contingencies. An interpretation which could lead to such a catastrophic situation should be averted. That apart, if any such view is

adopted, a fraudulent company can deceive any bona fide person transacting business with the company by stage-managing a petition to be

presented for winding up in order to defeat such bona fide customers. This consequence has been correctly voiced by the Division Bench in the impugned judgment.

9. In the above judgment, the Supreme Court has laid down the law that the term ""void"" need not automatically indicate that any disposition should be ab initio void and the legal implication of the word ""void"" need not necessarily be a stage of nullity in all contingencies. The Supreme Court has also laid down that the provision itself shows that the word void is not employed peremptorily since the court has power to order otherwise and the words ""unless the court otherwise orders"" are capable of diluting the rigour of the word ""void"" and to choose the alternative meaning attached to that word. In order to find out as to whether the transaction is void or not, the company court should consider the facts and arrive at a conclusion as to whether the transaction was bona fide or not. In the event, on the facts, the court comes to the conclusion that the transaction was not bona fide, by applying Sub-section (2) of Section 536, the court could declare such transaction as void. On the other hand, in the event the court is of the opinion that the transaction was bona fide, it will not declare such transaction as void under the above provision.

10. The analogous provisions of Sections 28 and 55 of the Provincial Insolvency Act (5 of 1920) came up for consideration before the Supreme Court in Sankar Ram and Co. Vs. Kasi Naicker and Others, . While construing the above provisions, the Supreme Court has held as follows :

The object of Section 28 of the Act is to secure unrestricted right to dispose of the insolvent's property after an order of adjudication is made.

This section clearly states that during the pendency of the insolvency proceedings, the creditor shall not commence any proceeding against the property of the insolvent in respect of his debt without the leave of the Insolvency Court. On making an order of adjudication, the whole of the property of the insolvent shall vest in the court or in a receiver, as the case may be, in terms of Sub-section (2). An obligation is placed upon the insolvent to assist the official receiver to realise the assets. When Sub-section (1) is read along with Sub-section (7), the effect would be an order of adjudication which relates back to the date of presentation of insolvency petition and the order of adjudication takes effect from the date of the

presentation of the insolvency petition. Consequently, vesting of property under Sub-section (2) also relates back to the date of presentation of the insolvency petition. Combined reading of Sub-sections (1), (2) and (7) makes the position clear that the interest of the creditors is safeguarded, parties are put on notice against attempt to transfer the property after the date of presentation of the insolvency petition by the petitioners or others relating to his property and also to warn the intending purchasers or transferees that they are taking the risk of purchasing or getting the property transferred in their names during the pendency of the insolvency proceedings from the date of presentation of the petition itself and even before passing of an order of adjudication. In the absence of such provisions, by design, the claims and interests of the creditors could be defeated by effecting transfer of properties after filing the insolvency petition and before passing an order of adjudication. Sections 28 and 55 of the Act are to be read together. Where the transfer has been made by the insolvent after presentation of the insolvency petition, the transfer cannot be held as void ab initio but its validity or otherwise depends upon a consideration of the question whether the conditions specified in Section 55 are or are not satisfied. If the view of the High Court affirming the view of the District Court that the protection of Section 55 was not available to the appellant even on satisfying the requirements of Section 55, the said provision, although is on the statute book, does not serve any purpose or it is redundant or superfluous....

Proviso to Section 55 of the Act protects bona fide transactions mentioned in Clauses (a) to (d) of Section 55. As per the proviso, in order to give protection to transactions mentioned in the said section, two conditions are to be satisfied--(1) that any such transaction takes place before the date of the order of adjudication, and (2) that the person with whom such transaction takes place has not at the time notice of the presentation of any insolvency petition. By implication flowing from the said proviso, any transaction that takes place after the date of the order of adjudication does not get protection of the proviso to Section 55 whether or not the person with whom such transaction takes place has any notice of the insolvency petition by or against the debtor.

11. It is the contention of the official liquidator that the judgment of the

Supreme Court in Pankaj Mehra and Another Vs. State of Maharashtra

and Others, would be applicable to the day-to-day transactions and not to the facts on hand. I am unable to agree with the said submission. Law

declared by the Supreme Court is binding on all courts under Article 141 of the Constitution of India. Of course, the applicability of the law

depends on the facts of each case. The facts of this case, which have been elaborately extracted above, needs further reference. Even much before

the winding up proceedings commenced on October 14, 1996, the applicant has entered into a loan agreement with the company in liquidation on

December 1, 1995, i.e., ten months prior to the commencement of proceedings. The agreement preceded earlier correspondences between the

applicant and the company in liquidation. The amounts to the tune of Rs. 65,20,901 were paid by way of four cheques as evidenced by four

agreements dated January 1, 1996, January 30, 1996, February 7, 1996 and January 10, 1997, and a mortgage deed was also executed by the

company in liquidation on January 31, 1997, followed by a declaration by the managing director of the company creating charge on the property.

In the regular transaction, the company also registered the charge with the Registrar of Companies on February 26, 1997. As the amounts

borrowed were not paid by the company in liquidation as agreed to in the above four agreements, the property was sold by way of sale deeds.

The loan agreements dated December 1, 1995, January 1, 1996, January 30, 1996 and February 7, 1996, were all entered into six months prior

to the date on which the winding up petition was presented. It is not the case of the official liquidator that after the winding up proceedings had

commenced, the company in liquidation, in order to defeat the right and deceit the secured creditors, transacted with the applicant. It must be

noted that there was no transaction in respect of the property till a mortgage deed was executed on January 30, 1997. Much prior to the same, the

company in liquidation had entered into the agreements for repayment of the loan amounts. In the absence of mala fide intention on the part of the

company in liquidation in the transaction to deceive the creditors, the transaction must be construed as bona fide. As far as the applicant is

concerned, nothing is produced before this court to contend that it entered into the agreements, mortgage deed, etc., only with the knowledge that

the company petition for winding up was pending. The fact that a sum of Rs. 65,20,901 was advanced by the applicant to the company in

liquidation was only for its developmental activities. Such transaction, in my considered view, cannot be considered as not to be bona fide. On the

facts of this case, the judgments of the Supreme Court in Pankaj Mehra and Another Vs. State of Maharashtra and Others, and Sankar Ram and

Co."s case [2003] AIR SCW 3732 are squarely applicable. On the facts of this case, the provisions of Sub-section (2) of Section 536 cannot be

made applicable and consequently the contention of the official liquidator that those judgments are applicable only to day-to-day transactions is not

acceptable, as the judgments of the Supreme Court apply to all bona fide transactions of the company and could not be limited only to the day-

today transactions.

12. For the foregoing reasons, the applicant is entitled to succeed in the application. Accordingly, the application is allowed as prayed for with a

direction to the official liquidator to deliver possession of the property in question to the applicant.