

(1985) 01 GUJ CK 0018

In the Gujarat High Court

Case No : Company Application No. 160 and 236 of 1984 in Company Petition No. 33 of 1983

**In Re: Aryodaya Spinning and Weaving Co. Ltd.
 In Re: Simka Engineering Co.**

Date of Decision : 04-01-1985

Acts Referred:

Companies Act, 1956 — Section 227, 27, 3, 4, 4(1)

Citation : (1986) 60 CompCas 897

Hon'ble Judges : S.B. Majmudar, J

Bench : Single Bench

Advocate : G.N. Shah, for the Appellant; G.N. Desai, for the State Bank of India and IDBI and R.H. Mehta, for the Objecting Creditors, for the Respondent

Judgement

S.B. Majmudar, J.—By Company Application No. 160 of 1984, Aryodaya Spinning and Weaving Co. Ltd., which runs a composite textile

mill in this city has sought direction u/s 536(2) of the Companies Act, 1956, to the effect that utilisation of the further borrowings/new borrowing

financial facilities to be given by the State Bank of India ("SBI", for short) and other banks/financial institutions for running the aforesaid mill be

declared to be authorised, valid and binding on the company and the petitioning creditors u/s 536(2) of the Act. By Company Application No. 236

of 1984, prayer A-1 is sought to be inserted in Company Application No. 180 of 1984 whereby certain charges created by the mill company

pending the main winding-up petition in favour of SBI, financing banker, as listed in the said prayer are sought to be validated under the very same

provision.

2. In order to appreciate the circumstances under which the present company applications are filed, it will be necessary to have a look at certain

relevant facts.

3. Factual backdrop :

Aryodaya Spinning and Weaving Co. Ltd. ("the company" for short) which is governed by the provisions of the Act and is having its registered

office at Asarwa Road, Ahmedabad, has been sought to be wound up at the instance of certain unsecured creditors by this court under the

provisions of the Act. A number of winding-up petitions have been filed against the company. In all, 51 such petitions have come to be filed

beginning with the Company Petition No. 33 of 1983 and ending with Company Application No. 160 of 1984. The textile undertaking run by the

company used to employ about 2,500 workers in all. It appears that over the passage of years, the company suffered financial setback and

became a losing concern. The balance-sheet for the year 1981-82 shows a loss of Rs. 2.50 crores in the profit and loss account of the company.

The company had to purchase various raw materials required for running the mill from the open market. As the company could not pay up the

concerned creditors who had supplied the raw materials, a number of winding-up petitions had been filed in this court as noted above. The first

company petition, being Company Petition No. 33 of 1983, which is treated to be the main winding-up petition, has been filed in this court on

February 24, 1983, and, thereafter, it was followed by a number of other petitions as noted above. During the pendency of those winding-up

petitions, the textile unit of the company which was a losing concern ultimately came to a grinding halt on December 27, 1983. In the meanwhile,

the existing management of the company underwent a change and the present management took over the reins of the company on December 2,

1983. This court admitted Company Petition No. 33 of 1983 on February 10, 1984, and directed the official liquidator to act as provisional

liquidator. At the request of the company, the admission order was stayed up to February 26, 1984. In the meanwhile, an appeal, being O. J.

Appeal No. 2 of 1984, was filed by the company against the admission order of the winding-up petition and appointment of the provisional

liquidator. This appeal came to be admitted by a Division Bench of this court on February 24, 1984. The Division Bench by an interim order

stayed the order admitting the petition and appointment the official liquidator as

provisional liquidator. Within a few months thereafter, the State of Gujarat issued two notifications under sections 3 and 4(1) (a) (iv) of the Bombay Relief Undertaking (Special Provisions) Act, 1958 ("the Relief Undertaking Act", for short), on July 19, 1984, declaring the company to be relief undertaking and directing that all rights, privileges, obligations, liabilities (except the liabilities of banks) accrued or incurred before the said undertaking declared to be period of one year from July 19, 1984. It is obvious that because of the currency of the aforesaid notifications, all other proceedings in various winding-up petitions got stayed and hearing of O. J. Appeal No. 2 of 1984 also remained stayed. The aforesaid notifications declaring the company as a relief undertaking and suspending various proceedings taken against it by its creditors for enforcement of the dues were challenged in Special Civil Application No. 4801 of 1984 by one of the creditors of the company, M/s. Dropwell textile Corporation. The said petition was admitted to a final hearing by a Division Bench of this court on September 8, 1984. This court also granted ad interim relief restraining respondent No. 2 (the present applicant) from transferring the properties by way of collateral security for the satisfaction of any new liability created thereafter without permission of the court. The said order came to be modified by the Division Bench on September 27, 1984, clarifying that the aforesaid interim order restrained only transfer by way of mortgage, hypothecation or pledge or charge by way of collateral security and not any day-to-day transaction of purchase and sale and that the said order did not stand against the working of the company but it certainly stood against encumbering the property of the company by way of hypothecation, mortgage, pledge or charge in respect of the new liability created after the order without permission of the court. However, in the meantime, some efforts were being made by the State of Gujarat in Co-operation with various financial institutions like State bank of India, Industrial Development Bank of India ("IDBI", for short) and other to see that various sick textile units of this city got revived.

4. The SBI which is the financing bank so far as the applicant company is concerned and with which all the movable and immovable properties of the mill company stood hypothecated and mortgaged, by its letter dated July 10, 1984, intimated to the company that the IDBI had offered certain

conditions stated therein by its letter dated June 25, 1984. The bank also informed that the company had also accepted the letter of intent and was taking steps to obtain various reliefs from the State Government or other concerned organisations. The bank also accepted in principle the package recommended by the working group set up by the Union Government and was agreeable to make available to the company various facilities on the terms mentioned in the said letter. The bank was prepared to grant a rehabilitation loan of Rs. 118 lakhs to the company for the following purposes

:

Rs. (in lakhs)

Pressing creditors 15

Labour retionalaisation 55

Arrears of wages and staff credit society 21

Inventory build up 40

131

Less : Promoter"s contribution 13

188

5. By two letters addressed by the IDBI to the chairman of the company dated June 25, 1984, and July 14, 1984, the applicant company was

informed by the IDBI that assistance of Rs. 65 lakhs would be made available for rehabilitating the company. That out of Rs. 65 lakhs, Rs. 52

lakhs would be made available by the IDBI and the ICICI while Rs. 13 lakhs will be made available by the Industrial Reconstruction Corporation

of India. The SBI also agreed to give additional facilities, such as, payment guarantee after realising the existing overdrawn accounts of the mill

company with the bank and by starting two accounts, viz., funded principal amount and funded interest accounts. Thus, from SBI, the company

pursuant to the aforesaid package plan, was to receive financial assistance as under :

Rs. (in lakhs)

Funded principal amount account 429.43

Funded interest account 255.00

684.43

Rehabilitation loans 118.00

Demand cash credit 263.00

Bills discounting purchasing 105.00

Letters of credit 50.00

Ordinary guarantee 82.40

Deferred payment guarantee 96.75

715.15

Total 1399.58

and from the IDBI and the IRCI, by way of rehabilitation, additional amount of Rs. 65 lakhs would be made available.

6. It is obvious that when these additional financial facilities were made available to the company, the concerned financial institutions would like to

see that, as they were sinking such a large amount in the mill company which was otherwise in the doldrums and when trying to resurrect the

company and to put it once again on rails, these financing institutions would insist on the company executing necessary documents accepting these

institutions as secured creditors. The present applications are filed u/s 536(2) of the Act by way of abundant caution by the company with a view

to seeing that if ultimately the winding-up petition gets through, these transactions in favour of the financing institutions may not be held vulnerable

and may not be declared to be void.

* * * *

7. In the course of hearing of Company Application No. 160 of 1984, it was pointed out by learned counsel for the objecting creditors that the

company has sought validation of various financing transactions entered into by the company with SBI during the pendency of the winding-up

petition No. 33 of 1984 which is the first petition in point of time and as these transactions would ultimately stand voided if the company gets

wound up as enjoined by section 536(1) of the Act, grant of prayer (A) in Company Application No. 160 of 1984 will indirectly amount even to

validation of these intermediate transactions entered into by the company in favour of SBI without there being even a prayer for the same and with

out there being proper material as the record in this connection. The aforesaid objections on behalf of the objecting creditors resulted in Company

Application No. 236 of 1984 which the company filed with a view to amending Company Application No. 160 of 1984 by introducing additional

prayer A-1 whereby the charges created by agreement for extension of hypothecation document dated June 6, 1983, and other agreements which

were entered into between the applicant company on the one hand and SBI and other financial institutions on the other after the date of the first

winding-up petition were sought to be declared as authorised, valid and binding on the company u/s 536(2) of the Act. Along with that application,

all relevant documents covering these transactions were annexed as annexures A to G. I will have occasion to refer to these documents in detail in

the later part of this judgment. This company application was replied to by Mr. B. B. Patel, a creditor, who had objected to Company Application

No. 160 of 1984 by filing his affidavit, opposing the judge's summons in Company Application No. 236 of 1984. I heard Mr. G. N. Shah for the

applicant company in both these company applications, Mr. G. N. Desai for SBI as well as IDBI in support of the applications and also heard Mr.

R. H. Mehta, Mr. R. K. Shah and Mr. Y. N. Oza who opposed these applications on behalf of the objecting creditors, hearing being spread over

a number of days.

* * * *

8. S/Shri R. H. Mehta, R. K. Shah and Y. N. Oza for the concerned objecting creditors raised the following contentions in opposition to these

applications.

(1) The present applications are not maintainable u/s 536(2) of the Act as no winding-up order has still been passed against the company. That

such an application can be filed, if at all, after the company is actually ordered to be wound up by this court.

(2) The present applications are not maintainable in view of the additional fact that the notifications have been issued by the State of Gujarat

declaring the applicant company as a relief undertaking under the provisions of the Relief Undertaking Act. In view of these notifications, all

proceedings pertaining to the company have to remain stayed for one year. Under the circumstances, the present applications u/s 536(2) cannot be entertained.

(3) The present applications also cannot be filed and cannot be considered in view of the interim relief order granted by the Division Bench in

Special Civil Application No. 4801 of 1984.

The aforesaid three objections were raised by way of preliminary objections. On merits, further objections were raised as under :

(4) The present applications should be dismissed as the company has not given any details about various transactions which it has entered into with

the financing bank, SBI, nor has it shown how various amounts advanced by SBI for which extension of securities are sought to be made in favour

of bank have been utilised and whether these amounts were necessary and bona fide required for running the mill.

(5) In any case, various amounts sought to be raised by the company from the financing bank, SBI, on the security of its movable and immovable

properties pursuant to impugned transactions are not shown to be bona fide raised for the purpose of running the concern and in the absense of

any such evidence, these applications cannot be granted.

(6) If the present applications are granted, the SBI which was an unsecured creditor to a large extent, of loans which had been granted under

heads of various facilities, exceeding the limits of these facilities, would be converted into a secured creditor and other unsecured creditors would

be practically driven against the wall and would not stand even the remotest chance to get anything towards their dues out of the assets of the

company.

(7) Granting of these applications will amount to giving a charter to the directors of the mill company who might have misconducted themselves in

running of the mills and whose misdeeds and misconduct would get a cloak of protection on account of the order passed in these applications by

this court. Under the circumstances, an irreparable damage would be done to the

mill company as a whole and to its shareholders and even to the creditors.

(8) Granting of these applications will also make available a cloak of protection to various misconducting bank employees who might have given

extra financial facilities to the company even though limits of the facilities under various heads had already got exhausted. Their negligence will get

completely protected by the present order and even on that ground, these applications should not be granted.

* * * *

9. It would be convenient to take up the consideration of preliminary objections first as, even otherwise, it would be in the fitness of things to do

so. So far as the first objection is concerned, it is true that no winding-up order has been passed against the applicant company until now. The

order of advertisement and appointment of the provisional liquidator has already been stayed by the Division Bench in appeal. However, that does

not prohibit the entertaining of proceedings u/s 536(2) of the Act. This aspect of the matter is no longer res integra as there is a direct Division

Bench judgment of this court on the point in Company Application No. 95 of 1984 in Company Petition No. 105 of 1983. The Division Bench of

this court, consisting of B. K. Mehta and D. H. Shukla JJ., speaking through B. K. Mehta J., has ruled that in proper case, applications u/s 536(2)

can be entertained even if no winding up order is passed in pending winding up petition. In view of this pronouncement of the Division Bench, the

first preliminary objection stands overruled.

10. So far as the second preliminary objection is concerned, it is to be noted that Company Application No. 160 of 1984 as well as company

Application No. 236 of 1984 have been filed after the notifications dated July, 19, 1984, under the Relief Undertaking Act came to be issued.

These notifications are still current. However, merely because such notifications have been issued and all proceedings for enforcement of claims of

creditors against the company have been stayed, it does not mean that the company cannot file an application u/s 536(2) of the Act for necessary

reliefs. This question was considered by me in detail while deciding Company Application No. 209 of 1984 in Company Petition No. 163 of 1984

which came to be filed under similar circumstances. By my detailed reasoned

order dated December 3, 1984, I have taken the view that currency of ... notifications under sections 3 and 4 of the Relief Undertaking Act against the company does not debar the said relief undertaking from approaching this court u/s 536(2) of the Act for getting its transactions validated if, on the facts, they deserve to be so validated. Under these circumstances, I do not repeat the detailed reasons given by me in the aforesaid matter for repelling an exactly identical contention to the preliminary objection No. 2. The second preliminary objection also stands overruled.

11. So far as the third preliminary objection is concerned, it is to be stated to be rejected. All that the Division Bench in Special Civil Application

No. 4801 of 1984 has stated is that the company will remain restrained from transferring the properties by way of mortgage, hypothecation,

pledge or charge by way of collateral security for the satisfaction of any new liability created without permission of the court. It must be noted that

the said interim order of September 18, 1984, modified on September 27, 1984, will obviously not cover the transactions entered into by the

company in favour of SBI on June 6, 1983, and October 3, 1983, as well as August 27, 1984, as they have all preceded the interim order of

September 18, 1984, as modified subsequently by the Division Bench. However, all further documents which are to be executed by the company

in favour of the financing agency will have to receive the imprimatur of the Division Bench as provided by the interim order of the Division Bench in

the aforesaid special civil application. In the affidavit supporting Company Application No. 160 of 1984, the secretary of the company has, in para

18 thereof, in terms stated that immediately after the court passes the orders u/s 536(2) of the Act, the company will take steps to place before the

Division Bench in Special Civil Application No. 4801 of 1984, the orders that may be passed in this application and inform the Division Bench

about the progress of the company in its rehabilitation programme. Mr. G. N. Shah for the company made it clear that the company will file

necessary application for permission of this court in the above special civil application for executing the necessary documents which are required to

be executed for implementation of the package deal of rehabilitation assistance which is proposed to be made available by SBI and IRCI to the

applicant company and that such application will be promptly made by the company before the Division Bench of this court in the aforesaid special application. It is, therefore, obvious that the grant of interim order by this court in the aforesaid writ petition does not come in the way of my considering these company applications u/s 536(2) of the Act on merits. All that can happen is that even after these applications are granted, if at all, further permission of the Division Bench will have to be obtained by the company in the aforesaid writ petition before the entire scheme of rehabilitation assistance becomes fully operative for the company. The third preliminary objection also, therefore, stands repelled.

12. So far as the objections on merits are concerned, the fourth objection relates to the fact that no details about the concerned transactions were supplied initially in Company Application No. 160 of 1984. It was vehemently contended on behalf of the objecting creditors by their learned counsel that after the filing of the first winding-up petition, if any dispositions of properties are made by the company sought to be wound up, they would be ipso facto void unless the court otherwise directs. That if clearance is sought u/s 536(2) from this court, details of various transactions should have been candidly and forthwith stated in the applications but that aspect has been kept blissfully vague. There is some substance in the grievance made by the objectors. As Company Application No. 160 of 1984 originally stood, sufficient details about the concerned transaction which the company entered into with SBI after February 24, 1983, were not given. However, by instalments, necessary facts emerged on the record. The concerned dispositions between the date of the first winding-up petition and the date of notification declaring the unit as a relief undertaking were initially not submitted for being validated. However, by cognate Company Application No. 236 of 1984, they were sought to be validated by inserting prayer (1A) in the main Company Application No. 160 of 1984. Now, it must be kept in view that when validation of any disposition pending the winding-up petition is sought by the company to be wound up, all necessary details about the transactions have to be stated from the inception. Nothing can be taken for granted. Only because the grant of such applications u/s 536(2) may have a beneficial effect on the future working of the company and may brighten the prospects for employing large number of workmen who are otherwise unemployed and

starving, the applicant company cannot take it for granted that such an application would be granted as a matter of course without making any effort to put forward all the relevant details of the concerned transactions in a forthright manner before the court.

13. However, on the facts of the present case, it must be stated that during the course of the prolonged hearing of these company applications, all relevant material was produced by the company and SBI stage by stage and by the time these company applications came to be fully and finally argued, all the relevant material was placed before me for scrutiny and consideration. Thus, the initial objection taken regarding absence of sufficient material on record concerning the transactions did not further survive. The fourth objection, therefore, though initially well made out pales into insignificance by emergence of relevant material on record stage by stage. Consequently, in the light of the existing material on record, this objection no longer survives. Before parting with this objection, I must put on record the fact that but for the vigilance exhibited by the objecting creditors through their learned counsel, it would have been difficult for the court to get a comprehensive picture about the transactions in question and it would have been very difficult for the court to grant the present applications. Consequently, due credit for ultimately getting all the relevant material on record must be given to the objecting creditors represented through their learned counsel.

14. So far as the fifth objection is concerned, it was vehemently submitted that the transactions in question which are sought to be validated have not been bona fide entered into for the purpose of running the concern and hence, these applications deserve to be rejected. It is not possible to agree with the aforesaid contention of the objecting creditors. It is now well settled that the object of sub-section (2) of section 536 of the Act is to prevent improper disposition or dissipation of property so as to affect the assets otherwise available for distribution among the creditors of a company in winding-up. But the court has a discretion to uphold all proper transactions. Accordingly, in the event of a winding-up order being made, all transactions since the commencement of the winding-up will be subjected to scrutiny by the liquidator who will take appropriate proceedings to have them declared void or valid by the court. The court usually validates transactions which are honest and in the ordinary course

of the company's business. The expression "unless the court otherwise orders" casts a duty on the judge requiring that "each case must be dealt

with on its own facts and particular circumstances, special regard being had to the question of the good faith and honest intention of the persons

concerned" and the court is free to act according to the judge's opinion of what would be just and fair in each case. The Legislature by omitting to

indicate any particular principles which should govern the exercise of the discretion vested in the court must be deemed to have left it entirely at

large and controlled only by the general principles which apply to every kind of judicial discretion. In the matter of J. Sen Gupta P. Ltd. (In

liquidation) [1962] 32 Comp Cas 876; S. P. Mitra J. laid down the following proposition for guiding the discretion of the court exercising power

u/s 536(2) of the Act (at p. 885) :

(1) The court has an absolute discretion to validate a transaction.

(2) This discretion is controlled only by the general principles which apply to every kind of judicial discretion.

(3) The court must have regard to all the surrounding circumstances, and if from all the surrounding circumstances, it comes to the conclusion that

the transaction should not be void, it is within the power of the court, u/s 536(2) to say that the transaction is not void.

(4) If it be found that the transaction was for the benefit of and in the interest of the company or for keeping the company going or keeping things

going generally, it ought to be confirmed.

15. In the case of Burton and Deakin Ltd., In re [1977] 1 All ER 631, Slade J. at English Chancery Division, while considering an application u/s

227 of the English Companies Act, 1948, which was a provision analogous to section 536(2) of the Indian Companies Act, held (headnote) :

If, on an application u/s 227 relating to a solvent company, its directors placed before the court evidence that they considered that a particular

disposition falling within their powers was necessary or expedient in the interest of the company, and if the court considered that the reasons given

were such as an intelligent and honest man could reasonably hold, the court would normally sanction the disposition notwithstanding the opposition

of a contributory, unless contributory had adduced compelling evidence which proved that the disposition was likely to injure the company. The

court would not, except in the case of proven bad faith or other exceptional circumstances, interfere with the discretion conferred on the directors

by a company's articles of association at the instance of a contributory even if a winding-up petition had been presented.

16. In the aforesaid case, a private limited company, Burton and Deakin Ltd., carried on the business of engineers, machinists, manufacturers and

repairers of motors, lorries and machinery of every description and other objects set out in the memorandum of association. A winding-up petition

was presented against it. In view of the presentation of such petition, Mercantile Credit Co. Ltd. which was usually financing the company became

increasingly restive about the facility offered by it to the company. In these circumstances, since the directors of the company regarded it as

essential for the continued well being of the company's business that it should continue to receive adequate finance on satisfactory terms to maintain

its stock of care, they investigated the possibility of obtaining that finance from sources other than MCC. As a result, they obtained an offer of

finance from Industrial bank of Scotland Ltd. IBS was prepared to grant the company a total facility of Pounds 35,000, the same figure as

originally offered by MCC. However, as a condition of a granting the facility, IBS would require the company's resulting indebtedness to be

secured by a deed of assignment substantially in the form of a draft deed. In the circumstances, the company's directors thought it would be in the

company's interests to take up the facility which had been offered by IBS and to discharge the company's remaining indebtedness to MCC out of

moneys which the company would stand to receive from IBS. It is in these circumstances that a petition u/s 277 of the English Companies Act,

1948, was moved before the Chancery Court. The court, having considered the pros and cons of the situation, took the view that the facility

offered by IBS against security would help the company in its running and it was a bona fide transaction which was required to be cleared. A

Division Bench of this court in Company Application No. 95 of 1984 to which I have made a reference earlier, speaking through B. K. Mehta J.,

had occasion to consider a similar situation where for running and for rehabilitating a company, financial assistance was required to be received by

the company sought to be wound up, from the financiers of the company executing the relevant documents for effecting the requisite securities in

favour of the financing institutions. Reliance was placed on the ratio of Burton's case [1977] 1 All ER 631 (Ch D). The Division Bench, on the

scope and ambit of section 536(2) of the Act, made the following pertinent observations (at page 214 of 59 Comp Cas).

It is well-settled on matter of principle and authority that if the company court is satisfied that a particular disposition of the property of a company

which is the subject-matter of a winding up petition, is necessary or expedient in the interest of the company and particularly its creditors and

shareholders and the transactions are in the ordinary course of its current trade bona fide entered into and completed, and it is in the interest of

every one to preserve the company as a going concern, and if such transactions are not maintained, and the presentation of the petition, groundless

or well founded, would result ipso facto in paralyzing the trade of the company and a great injury without any counter-balance of advantage would

be done to those interested in the assets of the company, it would be in the discretion and duty of the court to validate such transactions.

17. In the light of the aforesaid settled legal position, it is necessary to scrutinize various transactions entered into by the applicant company in

favour of the financing bank, SBI. As already noted earlier, after the date of the first winding up petition, i.e., February 24, 1983, the company

entered into the following disposition of properties in favour of SBI :

18. The agreement for extension of hypothecation charge on the company's movable machinery and assets dated June 6, 1983, is annexure ""A"" to

Company Application No. 236 of 1984. Para 1 of the agreement clearly recites that by a deed of hypothecation of machineries dated July 15,

1982, in respect of the company's cash credit and other facilities made by the borrower, the borrower had created a hypothecation charge on the

whole of the borrower's machineries and machinery spares to cover the company's liability in respect of the cash credit and other facilities to the

extent of Rs. 9,48,75,000. By the date of the document, there was an over-run of Rs. 95,59,891.58 in the case of some of the facilities and

consequently, the extent of hypothecation charge was by the document in question in question to cover not only the then existing secured loans of

Rs. 9,48,75,000 but in addition, it was to cover the order-run as aforesaid and this the total loan secured worked up to Rs. 10,44,34,891.38. By

the second document, annexure ""B"", to Company Application No. 236 of 1984, of even date, a further hypothecation agreement covering stocks, stores and book debts of the company was executed. In para 1 thereof, it was recited that at the request of the company and the guarantors by an agreement for hypothecation dated September 15, 1982, executed by the company and guarantors in favour of the bank, the letter granted to the company a demand cash credit against hypothecation of stocks, stores and book debts required by the company in the ordinary course of its business and for the purpose of carrying on the same which the company and the guarantors expressly submitted and acknowledged and that at the request of the company, the bank by an agreement for hypothecation dated December 29, 1982, executed by the company and the guarantors in favour of the bank, the letter granted to the company an additional limit of Rs. 20,00,000 for establishing letters of credit on its behalf from time to time in respect of their import purchase of raw materials required by the company in the ordinary course of business and for the purpose of carrying on the same. It was further recited that the company and the guarantors had requested the bank to continue the various facilities aggregating to Rs. 9,48,75,000 and the present overrun of Rs. 85,59,891.38 and for securing the same, the document in question was executed.

The aforesaid two documents clearly indicate that in those days, the company was a going concern. Its manufacturing unit was on stage. But it required more and more finance for carrying on its manufacturing activities. The SBI was also a secured creditor to the tune of Rs. 9,48,75,000 so far as its charge on all the movable properties of the company was concerned. This charge was extended to cover overrun on various facilities. It is easy to visualise that overrun of certain facilities would clearly postulate the ordinary course of business in which these facilities given to the company got overrun. When the company which was heavily indebted to the tune of more than Rs. 8 crores was to be given any more finance by the financing bank, SBI, it would be in the fitness of things and quite natural that the bank would insist that the company for being given any more facility for financial assistance, must adequately secure the financier and that assistance obviously would go a long way in keeping the company on rails as a going concern providing employment facilities to 2,500 workers. Be it noted that the company, a losing concern over years, actually got

derailed and closed its manufacturing activities months later in December, 1983. Prior to December, 1983, the company was a going concern and

if more and more finance was needed by the company to make both ends meet and to keep its head above water, if the financing bank insisted on

extension of hypothecation and mortgage on company's movable and immovables, it cannot be said that the said insistence was in any way not

bona fide one or that the transactions entered into by the company for that purpose were not bona fide transactions effected for keeping the

company as a going concern.

19. The next two documents recite equitable mortgagees in favour of SBI. By a document, annexure ""C"" dated August 5, 1983, the then directors

of the company entered into an extension of equitable mortgage of its immovable properties in favour of SBI. Annexure ""C"" which is a measure

sum of deposit of title deeds, recites that deposit of title deeds was made on behalf of the company by its director with intent to create a security

by way of a mortgage of title deeds on all the company's immovable properties together with all buildings and structures thereon to the extent

permitted to be a mortgage by the Industries Commissioner and Secretary, Revenue Department, as per post, Ahmedabad, vide order dated

February 22, 1983, in favour of SBI made u/s 27 of the Urban Land (Ceiling and Regulation) Act, 1976, and that this equitable mortgage was to

secure repayment, discharge and redemption by the company to SBI, the various facilities aggregating to Rs. 9,48,75,000 and the present overrun

to the extent of Rs. 1,20,12,462.36. Now, it must be kept in view that various financial facilities afforded to the company by SBI amounted to Rs.

9,48,75,000 even prior to the filing of the winding up petitions. It is only the overrun of various facilities which had increased from time to time.

That overrun obviously showed that the manufacturing activities of the company required more and more finance which came through various

facilities and that overrun was made available to the company by SBI with a view to seeing that the company went on as a going concern and did

not come to a grinding halt. The learned counsel for the objecting creditors invited my attention to the fact that by 1981-82, the company had

sustained a loss of Rs. 2.50 crores as seen from the profit and loss account and the balance-sheet and that even in the earlier years, the company

was a losing concern. This is no doubt true. But that itself shows that the company's financial and economic positions were running downhill. But they had not reached rock-bottom. Under these circumstances, when the company was gasping for breath and was struggling to keep itself out of a total mess, if more and more finance was supplied by SBI by way of providing the company finance beyond the limits of facilities which resulted in the granting of the overrun, it cannot be said that this accommodation given by SBI to the company was in any way mala fide or was not bona fide given with a view to keeping the company on the rails. In my view, the overrun of the relevant facilities which went on mounting month by month clearly shows that the company's finances were in a very bad shape and for keeping the company as a going concern, more and more finance had to be sunk by the financing bank so that the company may not ultimately stop its manufacturing activities. However, unfortunately, the efforts proved to be in vain and ultimately the company's manufacturing activities crashed down by the end of December, 1983, rendering about 2,500 workers unemployed and on an average of three members per family, about 7,500 souls became destitute. But that does not mean that so long as rock bottom was not reached, the company on the one hand and the financing bank on the other were not justified in seeing to it that more and more financial assistance was made available to the company so that it could avoid doomsday. All efforts made in that connection must be held to be bone fide efforts made for the purpose of keeping the company as a going concern and consequently, dispositions effected by the the company in favour of SBI by way of extension of hypothecation of movables and extension of equitable mortgages must be treated to be bona fide transactions entered into in the ordinary course of business of the company. Before parting with the document at annexure ""C"" dated August 5, 1983, it must be noted that as seen from the second schedule attached to the document, 27,690 sq. mts. of land of the company were sought to be brought within the sweep of equitable mortgage for securing the aforesaid loans given by the bank on various facilities. It appears that by a later document dated October 3, 1983, annexure ""B"", which is a memorandum of entry by extension, equitable mortgage of all the immovable properties was effected in favour of the bank secure the loans given by the SBI under various facilities amounting to Rs. 9.48.75.000 and also to

cover the then overdraft amounting to Rs. 1,72,53,791.98. Thus, by October, 1983, the overrun had shot up to Rs. 1,72,53,791.98 from the original overrun of Rs. 85,59,891.38 which was noticed at the time when the document (annexure "A") dated June 6, 1983, was executed. By the document at annexure "C", all immovable properties of the company, viz., buildings and lands were brought within the net work of equitable mortgage for securing both the aforesaid dues of the bank which by October 3, 1983, worked out to Rs. 11,21,28,791.98 This clearly shows that by October, 1983, the company which was carrying on its manufacture activities was hopelessly a losing concern and it was practically a drowning enterprise. It was a sinking ship. But in order to see that it did not actually sink, SBI went on extending various financial facilities under different heads and poured more and more money into the company with the result that the overrun shot up on the concerned items of facilities to Rs. 1,72,53,791.98 by October, 1983. It must be kept in view that the original facilities granted by bank to the company even prior to the filing of the first winding-up petition stood at Rs. 9,48,75,000, SBI was a secured creditor for this amount from the very beginning. After the first winding-up petition, all that has happened is that as the company in order to keep its head above water was in need of more and more finance, certain limits of facilities were exhausted and that resulted in an overrun which went on galloping and skyrocketing and reached the highest figures of Rs. 1,72,53,791.78 by October, 1983, and in December, 1983, the manufacturing activities of the company died down. It must, therefore, be held that all the aforesaid documents, annexures A, B, C and D have been entered into by the company during the time it was facing an acute financial crisis and was quickly moving down the hill of economic progress and was hitting rock bottom. During that time, more and more financial facilities were made available by the bank to the company to see that it may not ultimately meet its end. With that end in view, large overruns were permitted under various heads of facilities and they had to be secured so that the company which was otherwise a sick unit may not die. The SBI as a financing bank and as a secured creditor with whom all movables and immovables of the company were under charge and being the sole financing agency, pumped in more and more finance by way of overruns with a view to seeing that the company may not die down. If, with that

end in view, more finance was made available during the closing stages of the company's manufacturing unit's existence which went on giving

employment to a large number of workmen being 2,500, and for that purpose, if the company had executed these documents in favour of the

financing agency, it cannot be said that these transactions were in any way mala fide or were not transacted in the ordinary course of business of

the company, may be, a losing concern. The transactions, therefore, must be held to be valid and bona fide transactions not hit by section 536(1)

of the Act and must be validated u/s 536(2) of the Act. So far as other documents dated August 27, 1984, are concerned, they are as under :

20. By a document dated August 27, 1984, which is an agreement for extension of hypothecation charge on the company's movable machinery

and assets, hypothecation charge is sought to be extended to cover rehabilitation loans of Rs. 118 lakhs which are to be given by SBI by way of a

package deal for the revival of the unit. The said document is annexure ""E"". By a second document dated August 27, 1984 (annexure ""F""), seeks

to hypothecated stocks, stores and book debts of the company which were already hypothecated with SBI for covering additional rehabilitation

loan facilities which are to be given by SBI under the package deal, viz., Rs. 118 lakhs. The last document (annexure ""G"" of the same date seek to

extend the equitable mortgage to cover the additional rehabilitation loan of Rs. 118 lakhs which is ought to be given by SBI under the package deal

for reviving the unit. It must, therefore, be held that all the aforesaid documents (annexure A to C) have been entered into with a view to seeing that

the company revives and continues to be a going concern and have been bona fide entered into in the ordinary course of business of the company.

The documents (annexures A to D) have been executed during the time when the company was practically sinking and they reflect a heroic attempt

to pull out the company from its bad shape when large overruns of various facilities were being provided during the day to day working of the

company, while the last three documents (annexures E, F & G) have been executed as a part of the package scheme by which rehabilitation

assistance of Rs. 118 lakhs has been offered by SBI with a view to seeing that the company whose manufacturing activities have died down may

revive and may again become healthy and start kicking. It must be noted that even though the company's manufacturing activities came to a

grinding halt in December, 1983, after issuance of relief undertaking notifications, manufacturing activities have been partially resumed from

September 8, 1984, and as the record shows, about 400 employees who were otherwise unemployed have been re-employed and if the entire

rehabilitation loan of Rs. 118 lakhs as offered by SBI and Rs. 65 lakhs as offered by the IDBI and IRCI are made available to the company on the

company executing necessary further documents in favour of the concerned financiers, as part and parcel of the package deal, the entire unit is

likely to be resurrected and after retrenchment of 600 workmen, the balance of 1,900 workmen will get reemployment and the company would be

once again put on rails full steam and both its departments, viz., spinning and weaving, would get revitalised and effectively commissioned into

action. When the company seeks to come out of the present doldrums, it is absolutely necessary that the company should be permitted to draw

upon the rehabilitation loan by executing the necessary documents which may have been left out and which may be required to be executed. Under

these circumstances, it is not possible to agree with the pessimistic objection raised on behalf of the objectors that there is no possibility of the

company getting rehabilitated and that again it may come to the doldrums. It must be kept in view that under the present package deal,

rehabilitation finance is made available to the company subject to the condition that on the board of directors of the company, there will be a

Government director as well as the bank's representative as observers. Under these circumstances, there is an even chance for the company to

revive and to go full steam and for that purpose, all efforts have to be made with a view to seeing that the company turns the corner and gets a fair

chance of being put on rails. There is no reason why such positively healthy efforts should be allowed to get frustrated.

21. It must be kept in view that the present objectors are unsecured creditors. They sold their goods on credit to the company before its

manufacturing activities ceased in December, 1983. May be, these creditors have suffered. But, for these creditors, the company was one of the

customers. If their dues ultimately do not get paid, they would become bad debts for these creditors, whose sole livelihood does not depend upon

the profits earned from the transactions with the company. They can turn their sails in other directions. They have many customers to fall back

upon. If these creditors are pushed to the background by secured creditors like SBI which by extension of mortgage and hypothecation can very well be visualised as displacing all other creditors, even then, the petitioning creditors who are objecting to those applications cannot be said to have suffered irreparably in the sense that they were otherwise also unsecured creditors while SBI was a secured creditors worth at least more than Rs. 9 crores even before the filing of the first winding up petition. SBI was a wholly secured creditor having all the movable and immovable properties of the company in its charge. Objecting creditors were at the end of the queue being essentially unsecured creditors. They were already displaced by SBI. If they are displaced any more, it would not substantially alter their position which ever otherwise was bleak and it would remain the same while if the applications are granted and the company gets a fair chance of revival, at least 1,900 workers who are otherwise unemployed would get their livelihood. On an average of three members per family of workman, at least 5,700 souls who are otherwise starving and who have nothing else to fall back upon, may get a fair chance of survival. For these unemployed workers, there is no other alternative. For these unemployed, the mill is the only source of livelihood. Once they are thrown out of employment, they are nowhere. Under these circumstances, it is difficult to appreciate the grievance made by the objecting creditors against granting of these applications. If by granting of these applications, the prospects of the company improve, it is much better for even unsecured creditors like the objecting creditors. They may get a better for even unsecured creditors like the objecting creditors. They may get a better chance of ultimately getting some amount of their dues. But, if on the other hand, the present precarious condition of the company continues and the company is wound up, the objecting creditors would not get even that chance of getting back their dues which would be available to them in case fortunately the company gets revived and is put on the rails pursuant to the present package deal becoming effective and getting fully implemented. The fifth objection of the directors, therefore, must be overruled.

* * * *

22. So far as the seventh objection was concerned, it was submitted that by granting these applications, this court will permit the directors who

might have misconducted themselves to escape their liabilities. But to say the least, this objection is more out of frustration and pessimism. It must be kept in view that by the granting of the present applications, all that is being done is that various transactions entered into between the company on the one hand and the financing bank on the other after February 24, 1983, viz., the transactions reflected by exhibits A to G, are held to be entered into for the bona fide purpose of enabling the company to survive as a going concern and for reviving the same in future. That would protect the secured creditor. But if the concerned directors having brought these monies are shown to have misappropriated any part thereof, they would still be liable to face the music of misfeasance proceedings. Section 538(1) (d) and (e) clearly laid down that if any person being a past or present officer of a company which, at the time of the commission of the alleged offence, is being wound up, whether by or subject to the supervision of the court or voluntarily, or which subsequently ordered to be wound up by the court or which subsequently passes a resolution for voluntary winding up, within the twelve months next before the commencement of the winding up or at any time thereafter, conceals any part of the property of the company of the value of one hundred rupee or upwards, or conceals any debt due to or from the company or within the twelve months next before the commencement of winding up or any time thereafter, fraudulently removes any part of the property of the company of the value of one hundred rupees or upwards, he shall be punishable in the case of any of the offences mentioned above with imprisonment for a term which may extend to two years or with fine, or with both. Section 542 of the Act deals with liability for fraudulent conduct of business by the concerned persons in charge of the company's affairs. Section 543 deals with the power of the court to assess damages against delinquent directors, etc. It is, therefore, obvious that if in any future proceedings, it is found that the concerned directors had misapplied the company's funds and had incurred liabilities, both criminal and civil, as laid down by the aforesaid provision, they will have to face the music and they cannot escape the same, merely because the present applications are granted u/s 536(2) of the Act. Mr. G. N. Shah for the company rightly agreed to this legal position. He stated that despite the grant of these applications, if it is ultimately shown that the concerned directors misapplied the funds which

were supplied by SBI for running the company and had misconducted themselves in conducting the affairs of the company, they would remain

liable to be proceeded against under the aforesaid relevant provisions of the Act. The aforesaid stand taken by Mr. Shah is in consonance with the

legal position as emanating from the aforesaid provisions. Even otherwise, it stands to reason. I may take a simple illustration to highlight this point.

If a guardian of a sick patient purchases medicine on credit from a chemist who supplies medicine on credit with a view to seeing that the sick ward

recovers and if instead of utilising the medicine for the patient for whom it is meant, the guardian sells it off at profit in the market and pockets this

amount, it cannot be said that the chemist who supplied the medicine on credit should not be paid his dues or that his transaction was in any way

vitiated. The guardian who has misconducted would remain liable for his own misconduct but so far as the chemist who supplied the medicine on

credit is concerned, there is no reason why he should not be paid his dues treating his dues to be legal and valid. Consequently, so far as the

directors are concerned, if they have misapplied the funds which were supplied by SBI under various facilities to run the company, the directors

will remain liable to be proceeded against in accordance with law and the present order obviously cannot come in the way of such legal

proceedings against the concerned alleged delinquents. This order obviously cannot shield such personal misconduct of the alleged delinquent

directors. It only shield the transactions in favour of the financing banker and nothing more. The seventh objection, therefore, also fails.

23. That takes me to the last contention by the objecting creditors. It was contended by Mr. R. H. Mehta for some of the creditors that by granting

the present applications, negligent bank officers would get protected. It is difficult to appreciate this type of objection. Strictly speaking, such an

objection is outside the periphery of section 536(2) of the Act and it would be an irrelevant objection. If on evidence, it is found that the company

which is sought to be wound up had disposed of the property in favour of the creditor with a view to seeing that its ordinary course of business

does not get disrupted, the matter ends so far as section 536(2) proceedings are concerned. This court is not concerned with the disciplinary

jurisdiction which the SBI may exercise over its delinquent officers. It is entirely their domestic matter. If some of the bank officer allowed certain

facilities given to customers to get overrun, it would be open to the bank to take proper steps against the concerned officers. This court is not concerned with the same. Even if these transactions between the company and the bank get validated in the present proceedings, the alleged default and the negligence of the concerned bank officers for allowing the overrun to grow would still remain a matter for inquiry by the concerned bank against its officers. Whether the bank should inquire into the same or not is entirely a domestic question of the bank. This court is not concerned with the same. The objecting creditors are not holding a brief on behalf of the employer bank with a view to upholding discipline and proper working of various branches of the bank. Under these circumstances, even the last objection put forward by the objecting creditors must be repelled offhand both on the ground that it is irrelevant as well as on the ground that it is beside the point and does not have any impact on the moot question as to whether these applications should be granted u/s 536(2) or not. Even otherwise, there is no substance in the said objection as seen above.