(2006) 11 AHC CK 0046

In the Allahabad High Court

In Re: Danin Leathers (P.) Ltd. (In Liquidation)

Date of Decision : 02-11-2006

Acts Referred:
State Financial Corporations Act, 1951 — Section 29

Citation : (2008) 83 SCL 123

Hon'ble Judges : Sunil Ambwani, J

Bench : Single Bench

Judgement

Sunil Ambwani, J.—Heard Shri Ravi Kant, senior advocate assisted by S.N. Tiwari for the ex-directors of the company (in liquidation), namely, Smt. Alka Mahajan, wife of Shri Sanjay Mahajan, Ajay Mahajan, Shri Sanjay Mahajan and Shri Ashok Mahajan all sons of late Shri Keshav Ram Mahajan and Smt. Juhi Mahajan, wife of Shri Ajay Mahajan. Shri Rajnath N. Shukla appears for the Official Liquidator. Shri S.K. Saxena, the Official Liquidator is present. Shri Anurag Khanna appears for PICUP.

2. Danin Leathers Ltd. (in liquidation) was wound up by the court on 12-10-1999, on a creditors'' winding up petition and the Official Liquidator was appointed as the liquidator of the company. The ex-directors were required to file the ''statement of affairs'' and to handover the possession of the assets of the company (in liquidation) to the Official Liquidator. They, however, kepi on delaying the matter, in spite of full knowledge of the proceedings of liquidation, and ultimately after several summons, warrants and then non-bailable warrants issued for securing their presence they appeared and sought adjournments in the proceedings up to 14-11-2005. Initially, they made several unusual requests like providing requisite Forms for filing statement of affairs. Their counsel Shri L.K. Pandey pleaded ignorance of company law. Thereafter, Shri S.O.P. Agrawal, advocate appeared and filed an affidavit stating that the ex-directors have requested for documents from the State Bank of India for filing the statement of affairs. It was only after repeated persuasion that the statement of affairs was filed on 22-2-2006, without disclosing complete assets and liabilities. All the ex-directors except the ladies, who were exempted from personal appearance, sitting in the court for last about five dates fixed in the matter have refused to

provide complete details of the affairs of the company. At this stage PICUP, the State Bank of India and UPFC were required to file affidavits explaining the efforts made by them to recover their dues.

3. The PICUP advanced a loan of Rs. 40,21,118.02 to the company (in liquidation). At present a total amount of Rs. 2,75,38,400.09 (rupees two crores seventy five lakhs thirty eight thousand four hundred and nine paise) is to be paid by the company to PICUP. The company (in liquidation) has a sister concern M/s. Mahajan Tanners Ltd. The court prima facie found that PICUP had not taken effective steps to recover the amount. In the circumstances, the managing director, PICUP was required to file an affidavit explaining the steps that have been taken for recovery.

4. Shri Anurag Khanna, learned Counsel appearing for PICUP has filed affidavit of Shri Sudhir Garg, managing director of PICUP. This affidavit gives the details of the efforts, made by PICUP to recover the amount due from the company (in liquidation). It is stated in this affidavit that M/s. Danin Leathers (P.) Ltd., was engaged in the manufacture and export of shoes and shoe uppers at Johns Mill Compound, Jeoni Mandi, Agra, with an installed capacity of three lakh pairs of shoes/uppers per annum. They requested for financial assistance on which PICUP sanctioned loan of Rs. 100 lakhs under ''Equipment Refinance Scheme'', vide sanction letter dated 10-11-1999. The company requested for cancellation of loan as they did not want to implement the scheme. The loan was cancelled in September, 1990. Again a request was made for financial assistance of Rs. 51.80 lakhs and again the loan was cancelled in March, 1993. Once again a request of Rs. 45 lakhs was made by the company with board of directors including Shri Keshav Ram Mahajan, Shri Sanjay Mahajan, Shri Anil Mahajan and Smt. Juhi Mahajan. The composition of board of directors was changed on 16-5-1994, with Keshav Ram Mahajan, Sanjay Mahajan, Dr. Ashok Mahajan and Ajay Mahajan as directors. A loan of Rs. 45 lakhs was sanctioned, and a total amount of Rs. 43.80 lakhs was paid. The company committed defaults in November, 1995. A notice u/s 29 of the SFC Act was sent, and the bonds of guarantee were invoked on 17-1-1998. A recovery certificate of Rs. 59.53 lakhs was sent to the Collector, Agra, against which only Rs. 2.27 lakhs was realized by the Revenue Recovery Officer.

5. It was then reported that in an incident of fire on May 21,1999, the entire unit was gutted. An inspection was made on 1-6-1999, in which the unit was found to be badly damaged. The possession was taken by the district authorities on 10-6-1999, in follow up of R.C. issued by PICUP, against which an interim order was obtained on 24-3-1999, in Writ Petition No. 11903 of 1999. The PICUP lodged an FIR in which a final report was submitted, which has been set aside by this Court on the ground that the police officer did not even care to find the burnt machinery and convenient snorted that the entire properties, which included the land also was lost in fire. Another R.C. was issued on 16-10-1999. The writ petition against the notice u/s 29 of the SFC Act was dismissed on 29-7-2000.

Once again recovery certificate was issued and fresh R.C. was issued against the guarantors on 24-4-2000. The Collector, however, did not take any interest to recover the dues.

6. In pursuance of fresh recovery of Rs. 76,571.78 and Rs. 11,41,907 was recovered from the guarantors and the amount was deposited with PICUP vide Tehsildar''s letter dated 13-2-2003 and 11-8-2003, respectively.

7. In the third attempt the Tehsildar, Sadar, recovered Rs. 1,40,000 on 24-2-2004, from the guarantors. The PICUP informed ADM (F and R), Agra, by a letter that the properties of M/s. Mahajan Tanners (P.) Ltd., cannot be auctioned. The PICUP by the letter dated 6-9-2004, again sent R.C. indicating that there is no legal impediment in recovering the dues from M/s. Mahajan Tanners (P.) Ltd., and the orders of this Court dated 28-8-2003, were also sent.

8. In spite of its best efforts, PICUP has not been able to recover its dues so far.

9. The Official Liquidator has filed an application under Sections 454(5), 542 and 543 of the Companies Act, 1956, reporting that the ex-directors have not filed statement of affairs and that the chartered accountants while examining the audited accounts up to the year 31-3-1994, when a public issue of the company was offered in November, 1995, found unreasonable and unexplained accounting practice showing untrue results. The relevant part of the chartered accountant''s report is quoted as below:

Company''s latest audited accounts for the year ended on 31-3-1994, were examined by us in the light of the previous year figures and we found that:

(i) Cartage, freight and octroi paid on purchases which was shown at Rs. 26.75 lakhs on raw materials purchases of Rs. 545.57 lakhs for the year ended 31-3-1993, which works out to 4.90 percent of purchases, came down to just Rs. 3.79 lakhs on purchases of 758.57 lakhs in the year ended 31-3-1994, which works put to a mere 0.50 per cent of purchases.

Had the cartage, freight and octroi remained at the same levels as was in the year ended on 31-3-1993, it should have been Rs. 37.17 lakhs. Apparently either the accounts of the year ended 31-3-1993, or of 31-3-1994, were not showing true figures.

There does appear to be an attempt by the company to show better than actual results in the year ended 31-3-1994, as a build up towards showing better performance just before the public issue which was made in 1995, and also to show good performance to the new bankers, i.e., Indian Overseas Bank from whom working capital assistance to the tune of Re. 81 01 lakhs was taken for the first time in the year ended 31-3-1994.

(ii) Closing stock of raw materials as on 31-3-1994, appears to have been overvalued. As against average purchase price of ''chrome'' of Rs. 6.59 per sq. dcm during the year the closing stock has been valued at Rs. 7.61 per sq. dcm thus overvaluing it by Rs. 13.34 lakhs. In the same way, stock of lining'' has been valued at Rs. 4.13 per sq. dcm. whereas the yearly average purchase price is Rs. 2.59 per sq. dcm, thus this stock has also been overvalued by Rs. 6.34 lakhs.

Overall overvaluation of raw material stock comes to Rs. 19.68 lakhs.

This also shows that there was an attempt to overstate the profits to show better performance before public issue and also to the new bankers.

By overvaluation of stocks the company was also in a position to give misleading figures to bankers and thereby get the drawing power increased to get higher withdrawals from the bank for diverting the funds.

(iii) Raw material stock levels which were maintained at just 18 days of raw material consumption up to 31-3-1993, was shown instead at two months of value of raw material as at 31-3-1994, another possible way to show better performance as well as an opportunity to draw higher-amount from the bankers of the company by showing inflated value of stocks.

(iv) Efforts to make over the statement of profit can also be seen from the unreasonable fact that the company''s gross profit [sales - (raw material consumption + manufacturing and operational expenditure + increase/decrease in stocks)] rate has been shown at double, i.e., 3.83 per cent of sales as compared to G.P. Rate of 1.42 per cent for the year ended on 31-3-1993.

(v) During the year 1993-94, the company diverted funds which can be seen from the fact that Mahajan Tanners (P.) Ltd., and Keshav Sons Properties (P.) Ltd., both of which are ''associate companies'' were given advances of Rs. 74.31 lakhs and Rs. 10.80 lakhs respectively.

(vi) Land has been purchased from associate concern, i.e., Keshav Sons Properties (P.) Ltd., at Rs. 19.33 lakhs.

(vii) Land and buildings cost as at 31-3-1994, has been shown at one figure of Rs. 45,50,429 whereas the separate cost of land and buildings is required to be shown by the provisions of Schedule VI of the Companies Act, 1956.

Land purchased during the year 1993-94 at Rs. 19.33 lakhs has been shown as a separate item instead of adding the same to the existing land''s cost

(viii) Diversion of funds of the company also appears to have been done by giving advances. There is seen a very huge, unwarranted increase in the figure of advances as at 31-3-1994, as compared to the previous year as detailed hereunder:

(Rs. in lakhs) As at 31-3-1994 As at 31-3-1993 Advances to suppliers 57.06 5.16 Other advances 29.16 25.46 ________ _________ 86.22 30.72.3 ________ __________

This shows an increase of 181 per cent over the previous year. These advances apparently have been given to the associate companies only, i.e., Rs. 10.80 lakhs to Keshav Sons Properties Ltd., and Rs. 74.3 lakhs to Mahajan Tanners (P.) Ltd.

(ix) There also appears to be an unreasonable and unwarranted increase in the expenditure on entertainment. In 1993-94 it was Rs. 3.16 lakhs as compared to just Rs. 0.23 lakhs last year.

(x) As per the requirements of Schedule VI to the Companies Act, 1956, there should be mentioned the quantities of opening and closing stocks of finished goods, which is not found to be disclosed in the accounts for the year ended on 31 -3-1994.

(xi) As per 1(ix) of Schedule ''Q'' to the accounts for the year ended on 31-3-1994, retirement benefits of gratuity, etc., is accounted for on ''cash basis'' which is against the provisions of Section 20G of the Companies Act, 1956, and also of the guidance note issued by the Institute of Chartered Accountants of India on this subject. However, the auditor of the company has not made a specific mention of this fact and has not qualified his report on this matter which he ought to have done.

(xii) While examining other documents of the company, which were found on record, we gathered the following further information which may be of interest and use for you:

(a) Danin Leathers Ltd., was incorporated as a private company on 20-7-1979, and became public company on 8-11-1994.

(b) Associate concerns mentioned in the prospectus are : Mahajan Tanners Ltd.

Good Wear (India)(P.) Ltd. Good Year Shoe Factory (Firm) Bench Mark Leather Goods (P.) Ltd. Keshav Sons Properties (P.) Ltd.

(c) The company was running in a normal routine manner up to the year 1994, thereafter it appears that the management decided to change the functioning of the company. It was in April, 1994, that Dr. Ashok Mahajan and Mr. Ajay Mahajan joined the company as directors.

(d) Promoters included the following persons:

Keshav Ram Mahajan (Father) Dr. Ashok Mahajan (Son)(MBBS, MD, Doctor) Mr. Ajay Mahajan (Son) Mr. Sanjay Mahajan (Son)

All of them are shown as resident of 3/30, Khandari, Agra.

(e) Auditors of the company up to 29-12-1993, were M/s. H. Gambhir and Co., 4/6, Deshbandhu Gupta Road, Paharganj, New Delhi-110055. Thereafter, one partner of this firm only Mr. Vimal Tandon (M. No. 91985) became proprietor of M/s. Vimal Tandon and Co., 9198/5, Multani Dhanda, Paharganj, New Delhi, and became the auditor of the company.

(f)(i) Lead managers to the issue were: Prudential Capital Markets Ltd., ''Ameen

Complex'' 9, Rani Laxmi Bai Marg, Lucknow-226 001.

(ii) The Industrial Finance Corporation of India Ltd., Merchant Banking and Allied Business Department, First Floor, Core V, Scope Complex, 7, Lodhi Road, New Delhi-110 003.

(g) Advisors to the issue were: Century Consultations Ltd., 21, Ashok Marg, Lucknow-226 001.

(h) Registrars to the issue were: SRG Infotech (India) Ltd., 238, Pant Nagar, East of Kailash, New Delhi-110 065.

(xiii) As per the return of allotment found on record after the public issue made by the company following persons were allotted large No. of shares without any address or other detail:

(a) Rupinder Singh Arora 3,30,000 shares (b) Kamal Sharma 12,000 shares

10. The Official Liquidator had also pointed out the following discrepancies in the accounts spelt out from the examination of records:

(vi) During the year 1993-94, the company diverted funds which can be seen from the fact that Mahajan Tanners (P.) Ltd., and Keshav Sons Properties (P.) Ltd., both of which are ''associate companies'' were given advance of Rs. 74.31 lakhs and Rs. 10.80 lakhs, respectively.

(vii) Land has been purchased from associate concern, Le., Keshav Sons Properties (P.) Ltd., at Rs. 19.33 lakhs.

(viii) Land and building cost at 31-3-1994, has been shown at one figure of Rs. 45,50,429 whereas the separate cost of land and building is required to be shown by the provisions of Schedule VI to the Companies Act, 1956.

(ix) Land purchased during the year 1993-94 at Rs. 19.33 lakhs has been shown as a separate item instead of adding the same to the existing land''s cost.

11. Shri Ashok Mahajan filed Civil Appeal No. 4257 of 2006 in the Supreme Court against the judgment of this Court dismissing the writ petition against the recovery by PICUP in which he took a plea that unless the amount of loan is recovered from the mortgaged property, PICUP had no authority against personal guarantees given by the ex-directors. Relying upon Pawan Kumar Jain v. Pradeshiya Industrial & Investment Corporation of Uttar Pradesh Ltd. [2004] 121 Comp. Cas. 758, the Hon''ble Supreme Court allowed the civil appeal and directed the High Court to reconsider the matter in the light of the observation made in Pawan Kumar Jain''s case (supra).

12. In Pawan Kumar Jain''s case (supra), it was found that when the defaulted amount could be recovered from the properties mortgaged to secure the loan the recovering authorities should not proceed against the guarantors until they have exhausted remedies against the mortgaged properties. It is apparent that Shri Ashok Mahajan relied upon the fact that there is something to recover from the

mortgaged property, in pursuance of which the civil appeal was allowed on 26-9-2006.

13. Within a month thereafter the ex-directors have taken a plea before this Court (the Company Court) that the entire mortgaged properties under the ''Equipment Refinance Scheme'' were lost in the fire accident. Today Shri Sanjav Mahajan has filed an affidavit stating therein that the factory situate at 3, John''s Mill Compound, Jeoni Mandi, Agra, was on rented premises, and that it was returned to Gambhirmal Pandya (P.) Ltd., the landlord. The rent was paid up to 31-3-1998. This certificate appears to be signed by one Shri Dinesh, and does not bear any date, when the possession was handed over.

14. It is further stated that the property bearing 3/30, Khandari Road, Agra, of Keshav Sons Properties (P.) Ltd., Agra, was purchased by Das Friends Builders (P.) Ltd., Agra, for Rs. 40 lakhs for which Rs. 10 lakhs were paid by cheque dated 27-8-1998, and Rs. 39 lakhs by cheque dated 1-10-2002, on behalf of Danin Leathers Ltd., Agra, and that Rs. 35 lakhs was paid to the State Bank of India in March, 2003, and the account was closed.

15. It is further contended that the entire gutted machinery was sold as scrap for Rs. 67,750 to one Shri Devendra, scrap dealer at Agra.

16. It is surprising as to how the same ex-directors, who had given personal guarantees stated before the Supreme Court that the financial institutions should proceed against the mortgaged property, are now claiming before the court that nothing is left out of the mortgaged property, to recover the dues.

17. It is apparent that the ex-directors have played fraud with the court in making submissions that amount should be first recovered from the mortgaged property. They are taking inconsistent stands and seeking reliefs on making statements before the court.

18. The Official Liquidator has also placed before the court a letter of the Sales Tax Authorities No. 1174/Asstt. Commissioner, Division 8, Agra, dated 24-1-2004, signed by Shri A.K. Gupta, Asstt. Commissioner, Trade Tax, Division 8, Agra, informing him that there is liability of Rs. 64,57,000 against Danin Leathers Ltd., the company (in liquidation) from the years 1996 to 2000.

19. Further, I find that the company has taken a stand that they have bills receivable of Rs. 93,07,203 from the goods supplied to foreign buyers through S.B.I., Agra. They, however, have not been able to satisfy the court with the steps taken to recover this amount. Apart from a single letter written to the State Bank of India, there is nothing on record to show that the amount was not actually received. It is apparent that this amount was diverted somewhere else to avoid the payments to the creditors.

20. All these facts, given together show that the ex-directors have not only committed financial irregularities, defaults, they have also siphoned off the money due to the creditors. The incident of fire was not investigated. The ex-

directors did not renew the insurance of the pledged equipment and machinery. They did not file statement of affairs and sold the property even after the company was wound up and was officially in the possession with the Official Liquidator and have paid the bank.

21. Having regard to the facts and circumstances, the court is left with no option but to frame the charges against the ex-directors. All the three ex-directors namely, Shri Ashok Mahajan, Shri Ajay Mahajan and Shri Sanjay Mahajan are present in the court and the two ladies namely, Smt. Alka Mahajan and Smt. Juhi Mahajan are present through their counsel. The charges are thus framed as follows:

(i) That you, Smt. Alka Mahajan, wife of Shri Sanjay Mahajan, Shri Ajay Mahajan, Shri Sanjay Mahajan and Shri Ashok Mahajan, sons of late Shri Keshav Ram Mahajan and Smt. Juhi Mahajan, wife of Ajay Mahajan, all ex-directors of M/ s. Danin Leathers Ltd. (in liquidation) deliberately and intentionally neglected, and failed to file statement of affairs of the company as required u/s 454 of the Companies Act, 1956, within 21 days of the winding up of the company on 12-10-1999, and then filed an incomplete statement of affairs dated 21-2-2006, on 25-3-2006, with the Official Liquidator without any reasonable excuse, thereby committing offences u/s 454(5) punishable with two years imprisonment and a fine of Rs. 1,000 per day from the end of 21 days of the winding up order till 25-3-2006.

(ii) That you the ex-directors of Danin Leathers Ltd. (in liquidation) named in charge No. 1, practised an unreasonable and unexplained accounting practice in order to defraud the creditors vide report of the chartered accountants auditing accounts up to 31-3-1994, whereby the company registered losses and was ultimately wound up by the court, and thereby committed offences under Sections 541 and 542 of the Companies Act, 1956, punishable with one year of imprisonment and fine.

(iii) That you the ex-directors having full knowledge of the winding up proceedings and winding up order, continued to deal with the company properties and in fact sold the property of the company (in liquidation) in possession of the court through the Official Liquidator, and the building owned by the company and built on property No. 3/30, Khandari Road, Agra, of Keshav Sons Properties (P.) Ltd., Agra, for Rs. 40 lakhs and appropriated the amount by paying to the State Bank of India towards their dues without any information to the Official Liquidator and thereby committed misfeasance, in violation of Sections 536 and 540 of the Companies Act, 1956, punishable with two years of imprisonment and fine.

22. It will be open to PICUP to pursue his remedy by arrest of the ex-directors and attachment and sale of their properties, as on their own admission in their affidavit there is nothing left out of the mortgaged properties and further whatever was left of the company was also sold without any authority and

information to the Official Liquidator and against the provisions of the Companies Act, 1956. Since the court has taken cognizance of the offences today and has framed charges against the ex-directors and that they are on bail from the court of CJM, Agra, all the ex-directors, shall, except the lady directors appear in the court on every date fixed in defence of the charges. All the ex-directors are allowed eight weeks'' time for submitting their defence either by affidavit/ document or by person or lead any evidence. List on 9-1-2007, for prosecution evidence. The ex-directors shall be at liberty to apply and receive copies of the applications and other documents filed by the Official Liquidator from his office.