
(1985) 03 KAR CK 0038

In the Karnataka High Court

Case No : Company Application No. 102 of 1983 in Company Petition No. 7 of 1981

K.S. Shivappa

APPELLANT

Vs

State Bank of Mysore and Others

RESPONDENT

Date of Decision : 07-03-1985

Acts Referred:

Companies Act, 1956 — Section 171, 231, 439, 536, 537 (1)

Citation : (1988) 63 CompCas 135 : (1985) ILR (Kar) 2040 : (1985) 2 KarLJ 220

Hon'ble Judges : P.P. Bopanna, J

Bench : Single Bench

Advocate : Tukaram S. Pai, for the Appellant; C.B. Srinivasan, S.V. Krishnaswamy, S. Vijayashankar and N. Santosh Hegde, for the Respondent

Judgement

P.P. Bopanna, J.—Heard the learned counsel for the parties.

2. This application is taken out by one of the guaranties for the secured debt in favour of first respondent herein owed by the company (in liquidation), namely, Mr. Leaf Tobaca Development Co. P. Ltd., represented by the official liquidator, who is the third respondent herein. It is not in dispute that the first respondent, the State Bank of Mysore, had obtained a mortgage of the properties of the company (in liquidation) as security for the payment of certain amounts loaned by it to that company. The company having failed to pay the said amount, a suit was instituted by the first respondent bank in O.S. No. 78 of 1977 on the file of the Civil Judge, Davangere. The suit was decreed on March 23, 1979, and in Execution Case No. 1341 of 1980, which was filed on December 10, 1980, the first respondent sought for the sale of the mortgage properties in satisfaction of the decree against the company (in liquidation). Accordingly, the properties were brought to sale on August 25, 1981, the sale was confirmed on August 29, 1981, and the sale certificate was subsequently issued in favour of the second respondent auction purchaser. The auction purchaser purchased these properties for a sum of Rs. 1,75,000, though it is the case of the applicant that the

properties measuring three and a half acres of vacant land and two factory sheds as also a guest house situate therein could have easily fetched Rs. 5 lakhs at the market value prevailing then. The grievance of the applicant is that he was deputed as an official to work for the company (in liquidation) and he had no personal interest in the loan transaction between the first respondent and the company. On account of his official position as an office deputed to work for the said company, he had to sign as a guarantor and as guarantor, there is a decree against him in the original suit and thus he is now saddled with the liability to pay the balance amount due to respondent No. 1 after part satisfaction of the decree by the sale of the properties. According to the learned counsel for the applicant, the court sale in favour of respondent No. 2 is void u/s 537(1) of the Companies Act, 1956 (in short "the Act"), as in Company Petition No. 7 of 1981 filed by respondent No. 4 for the compulsory winding-up of the third respondent company, a winding-up order by this court had been made on April 15, 1982. But the proceedings for winding-up had commenced u/s 441 of the Act when the winding-up petition was presented before this court and, therefore, for the purpose of section 537(1) of the Act, the winding-up of the company by the court was deemed to have commenced at the time of presentation for winding-up. In the circumstances, the sale effected without leave of this court after the commencement of the winding-up proceedings was void u/s 537(1) of the Act. The facts relating to the presentation of the winding-up petition and sale of the properties in the court auction sale are not in dispute.

3. However, it is contended by the learned counsel for the first respondent that the petitioner being a guarantor has no locus standi to invoke the provisions of section 537 of the Act. Secondly, even assuming that the official liquidator did not take leave of the court for the sale of the properties in question, he should be deemed to have waived to have waived such leave u/s 537 of the Act on the facts and circumstances of this case, since he did not raise any objection before the executing court for the sale of the properties. Thirdly, such leave could be given even now by this court by making an order granting ex post facto leave for the sale effected by the civil court.

4. I will consider the second contention first. The learned counsel for the first respondent placed reliance on the provisions of section 446 of the Act to drive home the point that the failure to obtain leave of this court is not fatal to the sale of the properties through the executing court. He relied on the decision of the Madras High Court in *S. Krishnamachariar Vs. The Hanuman Bank Ltd. (in liquidation) and Others*, on this point. In that decision, a Division Bench of the Madras High Court was called upon to interpret the meaning of the word "leave of the court" which occur in section 446(1) of the Act. Section 446 of the Act corresponds to section 171 of the earlier Act, namely, the Indian Companies Act, 1913. In that case, the decree holder-plaintiff had obtained a mortgage decree on a mortgage executed by defendants Nos. 1 to 4 for a sum of Rs. 7,600. After this mortgage, defendants No. 1 to 4 had sold the equity of redemption to defendants Nos. 5 and 6 with a direction to redeem the mortgage.

Defendants Nos. 7 to 11 in the suit were alienees of the half share of the acquit of redemption sold to the sixth defendant. The fifth defendant had created an equitable mortgage in favour of the Hanuman Bank in 1946 over the half share sold to him by defendants Nos. 1 to 4. In the year 1947, Hanuman Bank went into liquidation. The suit on the mortgage was filed on March 1, 1950, and Hanuman Bank got itself impleaded as the sixteenth defendant in that suit by reason of the equitable mortgage in its favour. Among the many contentions raised by the Hanuman Bank, there was a prayer that the properties over which it had an equitable mortgage should be sold last. A decree was passed for Rs. 19,546 odd on July 11, 1952, and by this decree the order in which the properties were to be sold was also settled. As these properties were the properties in which the Hanuman Bank was interested by reason of the equitable mortgage, an application was filed by one of the defendants to declare the sale as void on the ground that leave of the liquidation court had not been obtained for proceeding against the properties over which the bank had security. The defendants invoked the provisions of section 171 of the Indian Companies Act and also section 231 of the said Act which corresponds to section 537 of the present Act. The lower court declared the sale as void, but the High Court set aside the order on the ground that there was an effective waiver of want of leave. On facts, the Madras High Court found that the suit itself was instituted with the leave of the company court. Therefore, the decree was binding on the company. The official liquidator had on more than one occasion taken into time to deposit the decree amount to satisfy the claim of the first mortgagee. In its view, "section 237 really should be read jointly with section 171."

5. It should be noticed that section 446(1) applies to a proceeding where a winding-up order has been made or the official liquidator has been appointed as provisional liquidator. In such a case, no suit or other legal proceedings shall be commenced or if pending on the date of winding-up order shall be proceeded with against the company except by leave of the court and subject to such terms as the court may impose. But section 537(1) makes a specific provision declaring any attachment or execution put in force without leave of the court against the estate or effects of the company after the commencement of the winding-up or any sale held without leave of the court of any of the properties or effects after such commencement shall be void. Section 537(2), however, makes it clear that section 537(1) shall not apply to any of the proceedings for recovery of any tax, impost or any dues payable to the State Government. That is, as it should be, because the State Government always has the first charge on any of the properties for the recovery of its due notwithstanding the fact that any liquidation proceedings are pending in any court under the Companies Act. If this distinction between the scope of section 446 and the scope of section 537 is kept in view, the decision of the Madras High Court does not appear to be a correct view on the interpretation of section 537 of the Act.

6. In my view, the provisions of section 446 and the provisions of section 537 operate in different fields. Section 446 is a general provision dealing with all suits

and legal proceedings which are yet to commence or pending on the date of the winding-up order. Whereas, section 537 deals with a limited class of cases where the attachment or the sale of the properties of the company is made without leave of the court when that company is being wound up subject to supervision of the court. So the next point for consideration is, what is the meaning of the words, "commencement of winding-up" in section 537(1) of the Act. This does not present any difficulty in view of the statutory definition found in section 441 of the Act. It is not in dispute in this case that the winding-up order was made u/s 433(e) of the Act read with section 439 of the Act. Therefore, it is a case of winding-up of a company by the court. The relevant provision u/s 441(2) of the Act reads as under :

"In any other case, the winding-up of a company by the court shall be deemed to commence at the time of the presentation of the petition for the winding-up."

7. On the plain language of section 441(2) of the Act, the third respondent-company was being wound up when the court auction sale in favour of the second respondent bank took place on August 25, 1981.

8. The learned counsel for the official liquidator has also supported the application and he has invited my attention to the two decisions of the other High Courts, namely, the Patna High Court and the Kerala High Court in *Bhagwati Devi Bubna v. Dhanraj Mills P. Ltd.* [1969] 39 Comp Cas 1023 (Pat) and *Sebastian Vs. Rubber Board and Another*,

9. The decision of the Patna High Court brings out the difference between the provisions of section 446 and section 537 of the Act. The Patna High Court has observed that leave to proceed with the suit u/s 446 is not similar to leave u/s 537 of the Act. In section 537, the legislative intention is quite clear that in the circumstances indicated therein, if no leave is obtained from the court, any action taken shall become void; but no such word "void" is used in section 446. That also indicates that non-compliance of the provisions contained u/s 446 will not result in the suit or the decree being void but it will be merely voidable at the instance of the liquidator.

10. The distinction made by the Patna High Court on the facts of that case is equally applicable to the facts of this case. Here we are only concerned with the validity of the sale effected in contravention of section 537 of the Act.

11. The Kerala High Court in *Sebastian Vs. Rubber Board and Another*, has noticed the scope of section 446 and section 537 of the Act. P. T. Raman Nayar, Actg. C.J., while dealing with the two provisions, observed as follows (at p. 121) :

"Were sections 446 and 537 designed to operate in the same field, the latter setting out the consequences of a disregard of the former - even so it will be noticed that section 537 concerns itself only with a particular class of proceedings falling within section 446, namely, attachment, distress or execution - then there might have been some substance in the contention that if, by reason

of sub-section (2) of the latter section, proceedings in attachment, distress or execution taken without leave of the court for the recovery of any tax or impost or any dues payable to the Government are not on that account void, the former cannot be regarded as requiring leave of the court for the commencement or the continuance of such proceedings. But then the two provisions are really designed to operate in different fields : section 537 is an entirely independent section not merely a section setting out the consequences of a disregard of section 446 and sub-section (2) of section 537 only saves the proceedings mentioned therein from sub-section (1) thereof, not from the operation of section 446. Section 537 is really complementary to section 442 and not to section 446. u/s 442 the appropriate court may, at any time after the presentation of the winding-up order has been made, stay or restrain proceedings against the company. But, in the absence of such stay or restraint, the court seized of the proceedings would have jurisdiction to proceed with it and to decide it. Where, however, a winding-up order follows, any attachment, distress or execution (but not other legal proceedings) put in force, without leave of the court, against the assets of the company, after the commencement of winding-up, in other words, after the presentation of the winding-up petition, is rendered void by section 537 notwithstanding that there was no stay or restraint ordered u/s 442. But once a winding-up order has been made, the commencement or the continuance thereafter of any legal proceeding (including proceedings in attachment, distress or execution) can be only by leave of the court, and any proceeding without such leave would be without jurisdiction and, therefore, altogether void. That is the result of section 446 itself, and it is not section 537, which, as we have noticed, applies only to a particular class and not to all proceedings falling within section 446, that render it void. And hence there can be no question of sub-section (2) of section 537, which only excludes the application of sub-section (1) thereof, excluding the application of section 446 in respect of any proceeding whatsoever. Section 537, it seem to me, is really designed to cover proceedings of the kind described therein taken during the interval between the presentation of the winding-up petition and the winding-up order in case where a winding-up is ordered, although its language is wide enough to cover proceedings taken even after the winding-up order. But, with regard to proceedings taken after the winding-up order, these would be void u/s 446 itself, unless taken with leave of the court, and the assistance of section 537 would not be necessary."

12. The first contention of Sri Srinivasan is that the applicant being a guarantor of the company (in liquidation) is not entitled to present this application. He relied on the provisions of sections 433 and 439 of the Act. According to him, the company may be wound up persons who are mentioned in section 439. The circumstances under which the company could be wound up are found in section 433. He contends that both these provisions do not make any reference to the guarantor of a secured loan and if the guarantor has no right to make an application u/s 439, he has no right to set at naught the sale u/s 537. This submission of Srinivasan overlooks the plain language of section 537 as also the

scheme of the Act.

13. The provisions of section 433 and 439 come under Chapter II of the Act relating to winding-up by the court. The provisions of section 539 come under Chapter V. This chapter relates to proof and ranking of claims in the course of winding-up.

14. The provisions of section 528 to 536 make it clear that the Act has prescribed provisions for proving debts of all descriptions, for the application of insolvency rules in winding-up of insolvent companies, preferential payments, provisions relating to preferential creditors, avoidance of fraudulent preference, and voluntary transfer and avoidance of transfer of shares after the commencement of winding-up. etc. Section 537 is one such provision which gives protection to any aggrieved person to avoid any attachment or execution or sale effected by the civil courts without the leave of the company court when the company is being wound up. In the circumstances, the provisions of section 537 have no bearing at all on the provisions of sections 433 and 439 of the Act. If that be so, the language of section 537 gives room for no doubt that any person who is affected by any attachment or sale of the property of the company in liquidation without the leave of the company court can invoke the said provisions. The applicant as a guarantor of the loan due to the first respondent-bank is greatly prejudiced by the court auction sale. He is now saddled with the liability of paying the balance of the decretal amount due to the first respondent-bank. In the circumstances, he is an aggrieved person who can invoke the provisions of section 537 of the Act.

15. The second contention of Srinivasan need not detain me for long. On the plain language of section 537, the ex-post facto sanction of this court granting leave for the sale in question does not arise. When the sale is void u/s 537, the same cannot be validated by a subsequent order of this court.

16. In view of the aforesaid discussion, this application is allowed, and the sale in favour of respondent No. 2 is set aside as being void, reserving liberty for the second respondent to work out his rights against respondent No. 1 in a properly constituted civil suit, if so advised.

17. The applicant will be entitled to the consequential relief also. There shall be a direction that the second respondent shall deliver the properties in question to the official liquidator of this court within four weeks from the date of receipt of this order.

18. It is made clear that the second respondent shall have the liberty to work out his rights against the first respondent and also against other parties in the civil court in accordance with law.

19. Parties to bear their own costs.