
(2011) 08 CAL CK 0160

In the Calcutta High Court

Case No : C.A. No's. 14 of 2007, 466 to 468 of 2008 and 645 of 2009 in Bifr
Case No. 69 of 1999

Official Liquidator

APPELLANT

Vs

Nagin B. Parikh and Others

RESPONDENT

Date of Decision : 19-08-2011

Acts Referred:

Civil Procedure Code, 1908 (CPC) — Order 7 Rule 11
Companies (Court) Rules, 1959 — Rule 261
Companies Act, 1913 — Section 235
Companies Act, 1956 — Section 543

Citation : (2012) 2 CALLT 540 : (2011) 167 CompCas 332

Hon'ble Judges : I.P. Mukerji, J

Bench : Single Bench

Advocate : A.K. Dhandhanian and B.P. Das for official liquidator, for the Appellant; HIRAK MITRA Senior Counsel, with Deb Dutta Sen, Moloy Sil and Nilendu Bhattacharya, for the Respondent

Final Decision : Allowed

Judgement

I. P. Mukerji J.

1. The company Jamshedpur Cement Ltd., was wound up by this court on January 14, 2003. The official liquidator attached to this court is in possession of all its assets and other properties.

2. As is routine in winding up proceedings, an order was made by this court on August 31, 2007, appointing a chartered accountant to investigate the affairs of this company u/s 543 of the Companies Act, 1956 (hereafter "the Act"). The court was in contemplation of starting misfeasance proceedings against the directors and other officers of the company. It would be guided, in ordering initiation of those proceedings by the report of the auditor to be filed after investigation was complete.

3. Mr. P. K. Chatterjee who was appointed as auditor submitted his report on

December 6, 2007. On examination of the report, this court ordered misfeasance proceedings to be started. They were accordingly started and the misfeasance application came to be numbered as C. A. No. 14 of 2007. This application had ten respondents, all directors or responsible officers of the company. It appears that the statement of affairs was filed by the second, third, sixth and ninth respondents.

4. Further to leave granted by this court in the misfeasance application, points of claim were filed implicating the respondents jointly. They were accused of misapplication and misappropriation of the funds of the company aggregating to Rs. 1,52,07,388.

5. Four respondent former directors of the company have made separate applications to the court to absolve them from all the charges of misappropriation and misapplication made against them by the official liquidator. They are the second respondent who has made the application C. A. No. 467 of 2008, the sixth respondent who has made the application C. A. No. 466 of 2008, the ninth respondent who has made the application C. A. No. 468 of 2008 and the tenth respondent who has made the application C. A. No. 645 of 2009. All these applications were in the nature of demurrer. At the time of consideration of those applications I felt that the points raised therein, by themselves, could not absolve the applicant directors of their liability. The four applications had to be decided on affidavits. After affidavits were complete these four applications were to be considered along with the misfeasance application.

C A. No. 645 of 2009

6. First, I will deal with the application of the tenth respondent. This application is numbered as C. A. No. 645 of 2009. There is little or no dispute about the facts. This respondent joined the company as a non-executive director on February 12, 1999. According to him, the purpose of his induction was to maintain "liaison" between the company, State Bank of India and other financial institutions. He was posted at Patna. Then in less than two months of his joining the company, an application was made by it to the Board for Industrial and Financial Reconstruction for declaring the company sick. On September 17, 2001, he resigned as director. He says that the reason for such resignation was that the negotiations for arriving at a settlement between the company and the financial institutions failed. On November 21, 2001, Form No. 32 recording the resignation of this respondent with effect from November 16, 2001, was filed with the Registrar of Companies, West Bengal. Therefore, the resignation was a little less than one year and two months before the company was wound up by this court.

7. The misfeasance proceedings are attacked on two main grounds.

8. The first is that this respondent was only a non-executive director. He had no responsibility for and no role in the conduct of the company's business. He only looked after negotiations to forge a settlement between the company, the State Bank and other financial institutions. Therefore, he should be discharged from

the proceedings.

9. The second point is that the judge's summons and the points of claim are devoid of any particulars regarding the involvement of this respondent in the acts of alleged misappropriation and misapplication of funds assets and other properties of the company. Allegations should not only be made with all the necessary details but must be proved.

10. Common authorities Learned senior counsel arguing this application and the other applications by the respondents relied on the case of The Official Liquidator Vs. Raghawa Desikachar and Others, . He also relied on a judgment of brother Jayanta Kumar Biswas J., in Dewrance Macneill and Co. Ltd. (In Liquidation) Vs. Padam Kumar Khaitan, where the respondent director was discharged, applying the principles contained in Order 7, rule 11 of the Code of Civil Procedure, 1908. To advance this proposition reliance was also placed on Security and Finance P. Ltd. v. B. K. Bedi reported in [1991] 71 Comp Cas 101 (Del), Official Liquidator Milan Chit Fund and Finance P. Ltd. v. foginder Singh Kohli reported in [1978] 48 Comp Cas 357 (Del), Official Liquidator of John Galt Laboratories Ltd. (in Liquidation) Vs. R.B. Sangare and Others, and Official Liquidator, High Court Vs. V. Selvaraj and Others,

11. Although, Mr. A. K. Dhandhanias, learned counsel for the official liquidator disputed the date of resignation of this respondent, he could not positively show from the records that the respondent participated in the affairs of the company after the date of his resignation. Therefore, I have said that there is little or no dispute regarding the above facts. However, learned counsel added to the list of authorities placed before me by citing P.K. Nedungadi Vs. The Malayalee Bank Ltd. (In Liquidation) and Others, Comp Cas 120, paragraph 5. He submitted that (page 125) : "Allegations or proof of fraud are not essential and it is immaterial that the offence is one for which the offender may be criminally liable". He cited this part of paragraph 5 to support misfeasance proceedings against this respondent as well as the other respondents. He also showed me Official Liquidator, Supreme Bank Ltd. Vs. P.A. Tendolkar (Dead) by Lrs. and Others, (paragraph 40). He stressed on the passage which said that a director may be shown to be so closely connected with the affairs of the company that he should be made responsible for any loss caused to the company, although no specific act of dishonesty is proved against him.

Findings in C.A. No. 645 of 2009

12. I am satisfied from the evidence, for there is no contradiction of this, that the tenth respondent was a non-executive director of the company. He was taken as a director to do negotiations between the company, the State Bank of India and the other financial institutions to arrive at a settlement between them and the company. The assertion of the applicant that he tendered his resignation on September 17, 2001, has not been controverted. Neither is there any contradiction of his submission of Form No. 32 with the Registrar of Companies

on November 21, 2001. According to that form, the resignation was with effect from November 16, 2001. The auditors' report does not indicate any specific act by which it can be inferred that this respondent was involved in misappropriation or misapplication of the company's assets and other properties. Therefore, applying the ratio of all the cases enumerated above, I am of the opinion that there is no evidence to suggest involvement of this respondent in any act of misappropriation or misapplication of the properties of the company. Therefore, the proceedings against him are dismissed. This application is allowed.

C A. No. 467 of 2008, C. A. No. 466 of 2008 and C. A. No. 468 of 2008

13. The applicants in these applications are the second respondent, Dinesh B. Parikh, the sixth respondent, Mrs. Ruprani D. Parikh and the ninth respondent, Rajendra K. Chokshi, also referred to as the applicant-respondents.

14. The auditor made his report on December 6, 2007. On the basis of the report the points for claim were filed. I am amazed as to how these points of claim could be drafted, without calling for any particulars from the auditor or without asking the court to direct the auditor to make a more specific enquiry and file a more specific report against the directors.

15. The points of claim are a mere reproduction of the report of the auditor. All the respondents have been made jointly liable for any unaccounted cash and movable properties of the company like motor vehicles, generator, stock, stores, spare parts, raw materials, unpaid loans and so on. There is no detail of the assets, how they were misappropriated or misapplied and by whom.

16. The directors and other officers of the company do not become automatically liable for all the loss that the company has suffered. The loss or misappropriation or misapplication of assets and other properties of the company have to be identified in detail and responsibility fixed jointly upon those in control of the company or upon some of them or one of them, with the necessary justification for fixing such liability.

17. The hon'ble Supreme Court expressed itself in the following manner in the case of *The Official Liquidator Vs. Raghawa Desikachar and Others*, (page 142) :

It may be mentioned that misfeasance action against the directors is a serious charge. It is a charge of misconduct or misappropriation or breach of trust. For this reason the application should contain a detailed narration of the specific acts of commission and omission on the part of each director quantifying the loss to the company arising out of such acts or omissions. The burden of proving misfeasance or non-feasance rests on the official liquidator.

18. The same court pronounced the following in the case of *P.K. Nedungadi Vs. The Malayalee Bank Ltd. (In Liquidation) and Others*, (page 124) :

Under section 235 of the Indian Companies Act, 1913, which was in force at the material time, the court has been given the power to assess damages against the

delinquent directors, etc. If the money or the property of the company has been misapplied or there has been misfeasance or breach of trust in relation to the company by a director, an officer or other person mentioned in the section the court, after examining the matter, can compel him to repay or restore the property with interest at such rate as the court may think fit or to contribute such sums to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust, as, the court thinks fit. It has been expressly declared that the section shall apply notwithstanding that the offence is one for which the offender may be criminally responsible. In Halsbury's Laws of England, 3rd edition, volume 6, it has been stated at page 623 that misfeasance and breach of trust include a breach by a promoter, director, etc., of a duty to the company the direct consequence of which has been a misapplication or loss of its assets for which he could be made responsible in an action. Allegations or proof of fraud are not essential and it is immaterial that the offence is one for which the offender may be criminally liable.

19. Our court in the case of Dewrance Macneill and Co. Ltd. (In Liquidation) Vs. Padam Kumar Khaitan,), went even further and dismissed the misfeasance proceedings against the directors of the company, applying Order 7, rule 11 of the Code of Civil Procedure, 1973. The reason for application of Order 7, rule 11 of the Code of Civil Procedure, 1908, was for want of necessary details, the proceedings did not disclose a cause of action and was liable to be dismissed.

20. In a similar application Baldev Raj Taneja v. Official Liquidator, High Court, Calcutta reported in [2011] 161 Comp Cas 417 (Cal), concerning the fourth respondent I tried to embellish this principle by saying that when it can be shown that any director or officer of the company had resigned much before the date of winding up of the company, the obligation of the official liquidator to furnish details was much more than with regard to those officers who were connected with the company at or about the time of winding up. The obligation to give details of wrong doing, according to me is always there. But the time of relinquishment of the office determines the amount of details to be furnished. The details of wrong doing about a director at the time of winding up need not be as much the details of the wrong doing of the director who left the company, say, 15 years before its winding up. This is so because the longer in point of time a person has dissociated himself from the company, the presumption is stronger that he might not have been involved with the misappropriation alleged. However, in that decision I departed to some extent from the principles in the case of Dewrance Macneill and Co. Ltd. (In Liquidation) Vs. Padam Kumar Khaitan, I said that lack of details did not normally warrant dismissal of the proceedings on Order 7, rule 11 principles but could be a ground for dismissal of the proceedings at the time of final hearing. Order 7, rule 11 could only be invoked when proceedings were started, without any details, against directors who had resigned long ago. Then it could be said the application did not disclose a cause of action.

21. But there is one exception to this principle which was pointed out by the Supreme Court in the case of Official Liquidator, Supreme Bank Ltd. Vs. P.A. Tendolkar (Dead) by Lrs. and Others, . It remarked the following in paragraph 40 (page 400) :

It is certainly a question of fact, to be determined upon the evidence in each case, whether a director, alleged to be liable for misfeasance, had acted reasonably as well as honestly and with due diligence, so that he could not be held liable for conniving at fraud and misappropriation which takes place. A director may be shown to be so placed and to have been so closely and so long associated personally with the management of the company that he will be deemed to be not merely cognizant of but liable for fraud in the conduct of the business of a company even though no specific act of dishonesty is proved against him personally. He cannot shut his eyes to what must be obvious to everyone who examines the affairs of the company even superficially. If he does so he could be held liable for dereliction of duties undertaken by him and compelled to make good the losses incurred by the company due to his neglect even if he is not shown to be guilty of participating in the commission of fraud. It is enough if his negligence is of such a character as to enable frauds to be committed and losses thereby incurred by the company.

22. Applying the above principles it appears to be quite plain that when on the face of materials on record it can be shown that none except the directors and other officers in control of the company could be responsible for any act of misappropriation, then there is a presumption of guilt against the directors and these officers, which they have to rebut. I was of the opinion that nonpayment of sales tax by the company as pleaded in paragraph 13(e) of the points of claim pointed to such culpability on the part of the first nine respondents except the fourth who had been discharged in another application. So also non-payment of Rs. 1,33,144 on account of Provident Fund, ESI and EDLI liabilities. I felt that this amount was collected from the customers or employees and the company could not use these funds. The sales tax had to be deposited with the sales tax authorities; the provident fund with the provident fund authorities. When such amount had not been deposited there was a presumption of misappropriation by these respondents, who were in control of the company at the material time.

23. In those circumstances I directed the auditor to file a supplementary report. That report was brought on record by the official liquidator by his report dated July 21, 2011. Nothing was added to the original report. The auditor has in turn relied upon the report of the auditor of the company. This was for the year 2000-01. The company auditor's report was as follows :

The amount outstanding as on March 31, 2001, in respect of undisputed sales tax, income tax, wealth tax, custom duty and excise duty, which were due for more than six months from the date they became payable are sales tax Rs. 93,69,399 and income tax (TDS) Rs.500.

24. In those circumstances I called upon the applicant respondents to rebut this presumption.

25. I applied rule 261 of the Companies (Court) Rules, 1959, to dispense with oral evidence and relied upon the affidavit evidence and other materials on record like the auditor's report, the circular of the Bihar Government dated August 23, 1991 and so on, to decide these applications. I was satisfied that such procedure was adequate for the purpose.

26. The applicant-respondents have brought on record by way of a compilation a circular of the Finance (Commercial) Department of the Government of Bihar dated August 23, 1991. This circular is in Hindi and was translated by the applicant respondents. I showed a copy of this translation to the interpreting officer attached to my court on the latter day of hearing of this application. For the last part of the circular learned counsel for the applicant respondents referred to the original Hindi circular as, according to him the English translation was not correct. This was confirmed by the interpreting officer of this court. The interpreting officer further confirmed that the interpretation made by learned counsel was correct and not the English translation. This sales tax deferment circular said that payment of sales tax on the main product and its by products, produced by the company could be deferred till September 30, 1994.

27. Now if this circular is taken into account the applicant respondents have succeeded in reversing the burden of proof. It can no longer be presumed that they have misappropriated the amounts collected as sales tax. If the Government of Bihar deferred payment of sales tax there is a necessary implication that the amount collected as sales tax could be used for the purpose of the company and the tax paid later. Although such deferment was only up to September 30, 1994, still the official liquidator had the burden to prove that this sales tax amount had been misappropriated by the directors jointly or by some of them or one of them or by any other officer.

28. The report of the auditor does not mention the period for which this sales tax was not deposited by the company. It gives no details of how the collection was made and how it was kept in deposit by the company. There is also no indication of how this sales tax was utilised. Therefore, on the above decisions it was obligatory on the part of the official liquidator to state with precision the details of misappropriation and identify the person or persons associated with this. Unfortunately, there is no such detail in the points of claim.

29. So this claim fails.

30. There are no details of the involvement of the applicants or any of them in the alleged acts of misappropriation mentioned in sub-paragraphs (a), (b), (c), (d) and (g). Hence, these claims also fail.

31. But one claim against the applicant respondents is to succeed because there is no explanation for this sum. This is the sum of Rs. 1,33,144 deposited with

them by the employees on account of Provident Fund, ESI and EPLI liabilities. For this sum the same presumption will apply as with regard to sales tax, namely, that the company cannot use this money which belongs to the employees and so it is deemed to have been misappropriated, by the directors or those in, charge of the company unless suitably explained (see the case of Official Liquidator, Supreme Bank Ltd. Vs. P.A. Tendolkar (Dead) by Lrs. and Others,

32. There is no such explanation. For misappropriation of Provident Fund and other dues I would impose a high penal rate of interest, because by misappropriation of this sum, the employees of the company have been deprived.

33. It appears on consideration of the records that the applicant-respondents were the persons involved in the running of the company. Therefore, the applicant respondents are liable to compensate the company in liquidation for the loss. I compute the provident fund dues together with interest at a penal rate to be Rs. 5 lakhs.

34. Therefore, I pass an order directing the second, sixth and ninth respondents to pay a sum of Rs. 5 lakhs together with interest at 10 per cent, per annum simple interest from this date till realisation to the official liquidator. This decretal amount is to be shared equally among these respondents and realised accordingly. This order is to be executed as a decree. If these respondents or any of them prefer an appeal from this order the official liquidator is given leave to file a cross objection on such terms as he thinks fit. No claim can be sustained against the first, third, fifth, seventh and eighth respondents, for the reasons above.

35. All the above applications are allowed to the above extent.

36. No order as to costs.

37. Urgent certified photocopy of this judgment/order, if applied for, be supplied to the parties subject to compliance with all requisite formalities.