

(1979) 11 KAR CK 0013

In the Karnataka High Court

Case No : Company Application No. 37 of 1975

Official Liquidator, Karnataka High Court

APPELLANT

Vs

R.C. Marathe and Others

RESPONDENT

Date of Decision : 26-11-1979

Acts Referred:

Companies Act, 1956 — Section 543 (1)

Citation : (1982) 52 CompCas 125

Hon'ble Judges : M.P. Chandrakantaraj, J

Bench : Single Bench

Advocate : S. Vijayashankar, for the Appellant;

Judgement

Chandrakantaraj Urs, J.—This application is filed by the official liquidator of this court under s. 543(1) of the Companies Act, 1956 (hereinafter referred to as "the Act"), alleging against five of the former directors of M/s. Coaram Chemicals Private Ltd. (in liquidation) for acts of misfeasance. One of the five directors, who is the 1st respondent in the application, was the managing director up to February 8, 1969. The 4th respondent was the administrative director with effect from February 8, 1969, on which date, the 1st respondent-managing director was designated as technical director. The other respondents, who were ordinary directors, did not have direct concern in the matter of day-to-day administration of the company in liquidation.

2. The official liquidator has alleged that the company in liquidation was originally incorporated on 5th May, 1966, with an authorised capital of Rs. 2,00,000 divided into 200 equity shares, each valued at Rs. 1,000. The said capital was at all material times issued and stood subscribed and credited in the books of the company as fully paid. Thus, there was no difference between the authorised capital and the subscribed capital. By an order dated January 22, 1971, in Company Petition No. 21 of 1970, the company was ordered to be wound up by this court and the official liquidator was appointed as the liquidator of the company in liquidation. On July 13, 1973, in Company Application No. 168 of

1973, this court appointed M/s. K. V. Narasimhan and Company as special auditors to complete the books of accounts of the company and also to examine and report whether there had been any acts of misfeasance, misapplication, retainer or breach of trust in relation to the company by the 1st respondent-managing director and other respondents-directors. This application under s. 543(1) of the Act is the result of the report of the auditors so appointed by this court.

3. The official liquidator has made the allegation of misfeasance against all the respondents depending on the report of the auditors, which is extracted here below.

"(a) The auditors in page 7, paragraph 2 of their report, submitted that on 31st March, 1968, the managing director affixed his signature in the cash book in token of the accuracy of the cash balance of Rs. 5,773.26 disclosed in the cash book, whereas the said cash balance was brought forward as Rs. 25 on 1st April, 1968, as opening balance, thereby not accounting for the cash balance of Rs. 5,748.26. Thus the first respondent is liable to account for the above sum to the company along with interest at the rate of 12 per cent. which comes to Rs. 7,708.26.

(b) The respondents herein did not take necessary steps to take out an inventory of stock-in-trade kept under lock and key by the State Bank of India from March, 1969, for valuation purpose and failed to maintain proper books of accounts for the period from 1st April, 1968, to 22nd January, 1971. Thereby the speedy realisation of outstandings was obstructed and unnecessary incidental expenses had to be defrayed by the official liquidator. Thus the respondents herein who were aware of the critical financial position of the company were equally negligent in not calling upon the bank to sell away all the pledged assets forthwith and adjust the proceeds towards the loan. In the result, the respondents caused loss indirectly in the realisation of good sale price for the stock and fixed assets which are estimated at least in a sum of Rs. 91,000 and interest thereon at the rate of 12 per cent. from 15th December, 1968, the actual date of stoppage of production, in all comes to Rs. 1,13,760."

4. In the circumstances stated above, the official liquidator has prayed that the 1st respondent-managing director has been guilty of misfeasance and breach of trust in relation to the company in having misappropriated the cash balance amounting to Rs. 7,708.26 and, therefore, liable to make good that loss to the company. Similarly, there is a prayer against all the respondents that they jointly and severally contribute to the company in liquidation in the sum of Rs. 1,21,468.26 together with interest on the aforesaid sum at the rate of 6 per cent. per annum from the date of winding up till the date of payment.

5. All the respondents have entered their appearance and filed their written statements. It is unnecessary to set out in detail the respondents' defence. It may be stated that they have denied the allegation of any act of misfeasance on

their part while discharging their duties as directors of the company in liquidation at all relevant times. After the pleadings were complete, draft issues were filed on behalf of respondent No. 1 and by respondents Nos. 2 to 5. But no formal issues were framed by the court. Therefore, at the time of passing this order, I have determined the following points for consideration.

"(1) Whether respondent No. 1 was liable to account for the cash balance of Rs. 5,748.26 claimed by the official liquidator in accordance with the report of the auditors appointed by this court together with interest thereon ?

(2) Whether respondents Nos. 1 to 5 jointly and severally caused loss directly or indirectly in a sum of Rs. 91,000 by not instructing the State Bank of India to whom they had pledged the stock-in-trade and raw materials which they had handed over to the bank without specific instructions in March, 1969, to sell the said stock-in-trade and raw materials and realise the maximum price available ?

(3) Whether the official liquidator has proved any act or acts of misfeasance against the respondents ?"

6. In support of the case of misfeasance by the respondents, the official liquidator has examined two of the directors, namely, respondent No. 1 - managing director, R. C. Marathe - and respondent No. 4 - Radhakrishna Reddy - who was director-in-charge of administration with effect from February 8, 1969.

7. At the trial, as many as 10 documents have been marked for the applicant, and for the respondents at the enquiry and after, by consent. The aforementioned two witnesses have been cross-examined by the learned counsel for the official liquidator and answers also had been elicited by their own counsel.

8. On the facts of this case, it is unnecessary for me to go into the merits of the case in detail.

9. So far as issue No. 1 is concerned, it is concluded by an order passed by Venkatachaliah J. in Company Application No. 37/1975 on June 16, 1978, by which order the official liquidator entered into a settlement with the 1st respondent - Marathe - and gave up all claims against him having received the sum of Rs. 10,942.26. In those circumstances, Venkatachaliah J. ordered release of respondent No. 1 from the enquiry and the enquiry was continued against respondents Nos. 2 to 5 only. In this view of the matter, the allegation of misfeasance against the 1st respondent contained in para. (a) extracted above does not survive for consideration at all and the loss to the extent of Rs. 10,942.26 got reduced from the total loss of Rs. 1,21,468.26 claimed by the official liquidator.

10. On the second point for consideration, the only argument advanced on behalf of the official liquidator by the learned counsel has been that the 4th respondent being the director-in-charge of administration did not act promptly and in the manner he ought to have done to get the pledged stock-in-trade and raw materials sold by the bank and adjusted towards the debt, which, in turn, would

have reduced for the company the estimated loss Rs. 91,000. This is founded on the fact that having regard to the evidence adduced, the value of the stock-in-trade and raw materials was estimated at Rs. 91,000 and this was put in the custody of the bank by handing over the key of the room where the stock-in-trade and raw materials were stored, to the State Bank of India in the month of March, 1969, by the 4th respondent. The said articles were not sold by the bank at all. It was only on April 16, 1971, in Company Application No. 80/1971, that this court ordered custody of those articles of stock-in-trade and raw materials to the official liquidator. Thereafter, the official liquidator got them sold on April 29, 1972, realising a sum of Rs. 13,000 and the said sale was confirmed by this court on August 4, 1972. Thus, the loss claimed by the official liquidator stands further reduced by the aforementioned sum of Rs. 13,000.

11. Sri S. Vijayashankar, learned counsel for the official liquidator, has fairly conceded that no case is pleaded nor proved against respondents Nos. 2 to 5 except respondent No. 4. Even as against respondent No. 4, the only case ought to be made out is that he did not give suitable instructions to the bank to dispose of the stock-in-trade and raw materials in time. In this behalf, it is necessary to notice that, as is evidenced by the testimony of R-4, he became a resident-director on February 8, 1969, he handed over the custody of the stock-in-trade and raw materials to the state Bank of India, to whom they were pledged, in March, 1969, itself. Thereafter, the company went into liquidation. But a specific question put by the learned counsel for official liquidator whether or not he had instructed to sell the same after it was given over to the custody of the bank, the witness, respondent No. 4, has answered in the affirmative and asserted that he said given such instructions and this court cannot ignore the same.

12. However that may be, the Supreme Court in the case of *Official liquidator v. Raghawa Desikachar* [1975] 45 Comp Cas 136 has held as follows :

"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 nonfeasance rests on the official liquidator."

13. In the instant case, there is no specific pleading against any of the respondents except the first one. The extraction of a portion of the auditors' report which in turn has been extracted above, in the course of this order, does not satisfy the requirements laid down by the Supreme Court in the aforementioned case to bring home the charge of misfeasance.

14. I do not think that in the case the official liquidator has made out a case for this court to foist the liability on respondent Nos. 2 to 5 for any loss that may have been incurred by the company in liquidation. Even if negligence or act of misfeasance were to be inferred, then it is impossible to quantify the liability

when is there is a total lack of evidence as the part played by one or the other the directors. Therefore, on point No. 2, I hold that the official liquidator has not made a case of misfeasance against respondents Nos. 2 to 5.

15. As a result of my ruling on points 1 and 2, point No. 3 should also be held in favour of the respondents.

16. In the result, this application is dismissed. But, in the circumstances of the case, there will be no order as to costs.