

(1970) 07 GUJ CK 0001
In the Gujarat High Court

R.C. Mehta and Co. and Others

APPELLANT

Vs

Himabhai Manufacturing Co. Ltd. and Another

RESPONDENT

Date of Decision : 07-07-1970

Acts Referred:

Companies Act, 1956 — Section 2, 441(2), 531(1), 536, 536(2)

Citation : (1970) 07 GUJ CK 0001

Hon'ble Judges : D.A. Desai, J

Bench : Single Bench

Advocate : S.B. Vakil, for the Appellant; V.P. Shah, for the Respondent

Judgement

D.A. Desai, J.—Himabhai Manufacturing Company Ltd. was incorporated as a company under the Companies Act, and the company was running a textile mill. On account of straitened financial circumstances in which the company found itself in February, 1968, the mills of the company was closed on 9th February, 1968. Thereafter two company petitions being Company Petition No. 33 of 1968 and 45 of 1968 were filed by the creditors of the company for an order for winding up the company. When these petitions were pending in this court, the Government of India stepped in and appointed the Gujarat State Textile Corporation (hereinafter referred to as the "corporation") as authorised controller u/s 18A of the Industries (Development and Regulation) Act, 1951, by its notified order dated 9th October, 1969. On being appointed as the authorised controller, the corporation applied for being joined as a party to the aforementioned two company petitions; and by an order made by the company judge in Company Application No. 127 of 1969 on 13th October, 1969, the corporation was joined as a party to both the petitions. The corporation has made the present two applications for a permission to create two mortgages on the security of the immovable properties of the company, one in favour of the corporation itself for a loan of Rs. 11.85 lakhs and the other in favour of National Textile Corporation Ltd. for a loan of Rs.12.10 lakhs. These applications were made u/s 536(2) of the Companies Act. The applications are resisted by the petitioning creditors in the aforementioned two company petitions, inter alia, on the ground that this court

has no jurisdiction at this stage to grant the permission prayed for; and alternatively it was contended that even if this court comes to the conclusion that the court has jurisdiction to grant it, the corporation has not put sufficient materials on the record to decide at this stage whether the permission sought for should be granted or not.

2. A narrow but really interesting question as to the interpretation of section 536(2) of the Companies Act, 1956, arises in these applications. A few facts relevant to the point may be noticed. Company Petition No. 33 of 1968 and 45 of 1968 have been filed by the creditors of the company for an order for winding up the company on the ground that the company is commercially insolvent and unable to pay its debts. These petitions were filed on August 19, 1968, and December 4, 1968, and are pending in this court. If the company is ultimately ordered to be wound up the winding-up proceeding would be deemed to have commenced from the date of presentation of the petition in view of section 441(2) of the Companies Act, and the mortgages now sought to be created by the authorised controller would be void having been made after the commencement of the winding-up proceedings unless the court otherwise directs in view of section 536(2) of the Companies Act. The corporation has, therefore, filed these applications for protecting itself in advance by seeking a direction from the court that in the event of the company being wound up the mortgages would not be void but will be valid and binding. That necessitates examination of the scope of the court's jurisdiction to act u/s 536(2).

3. Section 536(2) of the Companies Act reads as under

" 536. (1).....(2) In the case of a winding-up by or subject to the supervision of the court, any disposition of the property (including actionable claims) of the company, and any transfer of shares in the company or alteration in the status of its members, made after the commencement of the winding-up, shall unless the court otherwise orders, be void."

4. The contention is that section 536 finds its place in Part VII of the Companies Act, styled as WINDING UP and the heading of the sections commencing from section 531(1) is : Effect of winding-up on antecedent and other transactions. In the scheme of a statute the place of the section also helps in the construction of the section. But it is well settled that the court should first look at the section and if the language of the section is precise and unambiguous, then no more can be necessary than to expound those words in their ordinary and natural sense. The place of a sub-section or section in the scheme of a statute may sometimes assist in finding out the true import of the section intended by the legislature. The language of sub-section (2) indicates that it would come into operation in respect of a company which is ordered to be wound up. The opening words of the section "in the case of a winding up", would show that the jurisdiction conferred on the court by sub-section (2) can be invoked in the event an order for winding up is made. The section provides that in the event of a winding-up order being made any disposition of property made by the company since the

commencement of winding-up shall be void unless the court otherwise orders. By operation of the section itself, any disposition of property made by the company after the commencement of the winding-up proceeding would be void unless the court otherwise orders. Therefore, before the court can order that a particular disposition of property would not be void, it must first become void by the happening of the event envisaged by the section. The power or jurisdiction is conferred upon the court to pass upon the nature of the transaction which would necessarily be void but for the direction which the court may give in respect of the transaction. By the operation of the section in the event of a winding-up order being made in respect of any particular company any disposition of property made by the company since the commencement of the winding-up proceeding would be void. But the legislature, keeping in view the fact that a winding-up proceeding commences from a date anterior to the date on which an order for winding-up a company is made, has provided that in respect of disposition of property made by a company after the day on which a winding-up petition is presented and before a winding-up order is made, shall be void unless the court otherwise orders. Section 536(2) operates for the period between the presentation of the winding-up petition and the day on which a winding-up order is made because once a winding-up order is made, the company has no power to deal with its property. Any disposition of property of a company against which a petition for winding it is filed and is pending but not ordered to be wound up, would be valid if it is done by the directors within the scope of their authority as directors. That would be a valid transaction subject to a future contingency which may or may not happen. If at a later date the company is ordered to be wound up, the transaction which was valid at its inception would become void by the operation of law. But in respect of such a transaction jurisdiction is conferred upon the court to order otherwise, namely, to declare that it is not void, in other words, to declare that it is valid and binding.

5. It has very seriously contended that the opening words in sub-section (2) "in the case of a winding-up" do not suggest any point or period of time, but they merely suggest that the consequences mentioned in sub-section (2) would ensue only on the happening of a certain event, namely, only on the order for winding up being made. It was urged that the words "in the case of a winding-up" do not refer to any particular point of time or period, but they only suggest a condition in which certain disposition of the property made by the company would become void of a particular event happens in future. It was urged that sub-section (2) only provides for consequences of winding-up order being made effective certain disposition of property made by the company prior to the exact date on which winding-up order is made. The language of sub-section (2) leaves no room for doubt that it has reference to the time lag between the presentation of winding-up petition and an order for winding-up being made. It is crystal clear that an order for winding-up made by the court would relate back to the date on which the petition for winding up the company is presented. Ordinarily, there would be some time lag between the date on which the petition for winding up is

presented and the date on which an order for winding up is made. If a petition for winding up a company is made in respect of a flourishing company or a going concern, it is natural that the company would be, day to day in its ordinary course of business, entering into transaction which can be styled as disposition of the property of the company. All these dispositions of property will be made by the directors within the scope of their power. On the date on which such disposition of the property is made they would be valid dispositions of property. But if at a later date an order for winding up the company is made, they would become void. If at all they become void, jurisdiction is conferred upon the court to decide the nature of such transaction, namely, to declare that they are not void or to declare that they are valid. But before the court would take upon itself to examine the nature of disposition of property u/s 536(2) it must be a disposition of property which has become void on the making of the winding-up order. The court would not proceed to examine the validity of a transaction which is valid at its inception any may not become void if the petition for winding up the company is dismissed. The order will be completely otiose. It would be an exercise in futility if the transaction which was valid at its inception will have to be declared valid only to save it from a remote possibility of its becoming void if the company is ordered to be wound up. Therefore, the plain language of the section clearly indicates the scope of the court's jurisdiction. The language indicates that, in the event of a company being wound up, all those dispositions of property made by the company between the date of presentation of the petition for winding up and the date on which an order for winding up is made shall be void. But the nature of the transaction which has become void can be examined by the court at the instance of a party interested in the disposition of property.

6. Mr.S.B.Vakil, learned advocate for the applicants, contended that the provision contained in section 536(2) is made not merely for protecting the interests of the creditors of the company but also for the other parties, namely, that the interest of the company is not unduly harmed. It was urged that the real object of the provision must be judged from the object sought to be achieved by the provision or the mischief intended to be arrested by the provision. It was, therefore, urged that if a very frivolous application for winding up the company is made in respect of a sound and flourishing company, it would make it impossible for the company to carry on its business during the period between the presentation of the petition and its disposal because, in the ordinary course of business, the company may have to dispose of property and in order to allay any apprehension of those intending to enter into transactions with the company, it would be open to the company to come to the court and to seek a direction that the transactions shall not be void in the event the company is wound up. If Mr.Vakil is right in his submission, the court is called upon to take an anticipatory action which ultimately may or may not become necessary. If the winding-up petition is dismissed section 536(2) would never come into play. Section 536(2) would come into play only when a winding-up petition is presented which is ultimately

granted and the company is ordered to be wound up and such company having made dispositions of the property during the period between the presentation of the petition and the date of the winding-up order. In order to see that, since the presentation of the petition, the directors of the company do not fritter away the assets of the company, a wholesome provision is made that, in the event of the company being ordered to be wound up, such disposition of property shall be void, simultaneously providing that the court may examine the nature of such disposition of the property at the instance of the liquidator or at the instance of any other person interested in the disposition of the property and declare that the particular disposition is not void or is valid. But it must be remembered that every petition presented for winding up the company would not necessarily be granted. Now, if, after presentation of the petition and till the time it is finally decided, every disposition of the property can be validated by way of anticipatory action, I am afraid, it would bind the liquidator who would not be in the picture at that stage. The liquidator steps in only after an order for winding up is made except where the provisional liquidator is appointed. But whether the assets of the company have been frittered away or not is a question which the liquidator must examine and if the permissions are granted in advance before the liquidator steps in, in my opinion, such an anticipatory action cannot be taken under sub-section (2). The condition precedent to the exercise of jurisdiction under sub-section (2) is an order for winding up of the company having already been made and disposition of the property having become void as having been made between the date of the presentation of the petition and the date on which the company is ordered to be wound up.

7. Mr.Vakil, however, urged that if two constructions are possible, namely, that the court can examine the nature of the transaction at the instance of the liquidator after the order for winding up is made as also before an order for winding up is made but after the presentation of the petition at the instance of the person seeking to enter into transaction, there is nothing in the language of the sub- section which limits the jurisdiction of the court and the court should not accept that construction by which the jurisdiction of the court is fettered. Mr.Vakil further urged that, if after an order for winding-up is made, the court can examine the nature of the transaction, there is greater reason why the court should examine the nature of the transaction at its very inception so that the apprehension of the parties, who are entering into the transactions would be fully allayed. The question, however, is "whether sub-section (2) was designed to enable the court to entertain applications which are in their very nature of anticipatory character ? Can the court consider the nature of the transaction before the transaction is entered into ? In other words, can the court say that the transaction which on happening of a future contingent event would become void should be treated as valid much before it has become void keeping also in view the fact that it may not become void if the petition for winding up the company is dismissed. It is not possible to put the other construction suggested by Mr. Vakil of sub-section (2). Even if the object sought to be achieved or the mischief

sought to be arrested is taken into consideration after putting proper construction on the language of sub-section (2), in my opinion, both can be achieved by adopting the first construction, namely, that the court will have jurisdiction to examine the nature of the transaction only in winding-up proceeding after the company is ordered to be wound up. It was also attempted to be urged that in fact there is nothing in the language of sub-section (2) to indicate one or the other stage where the jurisdiction of the court can be invoked and, therefore, it would appear that the jurisdiction of the court to pass upon the nature of the transaction can be invoked at any stage. I am afraid, as stated earlier, the condition precedent for the exercise of the court's jurisdiction under sub-section (2) is indicated by the use of the words "in the case of a winding-up" which, in my opinion, mean that in the event of the winding-up order being made, the transactions falling within before the court's jurisdiction u/s 536(2) can be invoked there must be winding-up order and the transactions must be during the specified period which must have become void on the making of the order for winding up. If these two conditions are satisfied then alone will the court have jurisdiction to pass upon the nature of the transactions.

8. I would now refer to some of the decisions relied upon by both sides. Mr.Vakil referred to in *In re A.I.Levy (Holdings) Ltd.* If that was the only authority on the subject, I must confess that it supports the construction canvassed by Mr.Vakil. Before referring to this decision, it must be made clear that the court in that case was concerned with the construction of section 227 of the Companies Act, 1948, which is in pari materia with sub-section (2) of section 536 of the Companies Act, 1956. The court proceeded to consider whether it was open to the court to make an order validating the disposition by the company of certain leasehold premises at a particular stage when in respect of that company a winding-up petition was presented and was pending though no order for winding up was made on that date. The question of jurisdiction was thus in terms raised before the court. After referring to about 5 earlier cases, one of which is the case in *In re Miles Aircraft Ltd.*, to which I am going to refer in detail, Buckley J. was of the opinion, which is expressed as under :

" In these circumstances, this being a case in which it appears to me to be manifest that the transaction is one which must benefit the unsecured creditors of the company if in due course a winding-up order is made, the reason which affected Vaisey J.'s mind, that is to say, that the liquidator should be given an opportunity to investigate the matter and bring it before the court representing the interests of all the creditors, does not affect my mind, for I do not think the liquidator could make the position clearer to me than it is at the present time on the facts."

9. It was further observed that the court has jurisdiction to entertain an application for validating the disposition of the property by the company against which an application for winding up is pending, though no order for winding up is made. While reaching this conclusion, Buckley J. differed with the judgment of

Vaisey J. in *In re Miles Aircraft Ltd.* A question of jurisdiction was again in terms raised before Vaisey J. In the case before Vaisey J. a petition for winding up Miles Aircraft Ltd. was filed on November 11, 1947. The return date was November 24, 1947. The petition came to be adjourned till December 15 when it was adjourned till 19th January. On November 12, the company entered into a contract for the sale of certain leasehold property of which the company was the registered proprietor. The debenture-holders of the company who believed that the transaction was for their benefit applied for an order u/s 173 of the Companies Act, 1929, that the contract and disposition of the property made should not be void in the event of an order for winding up the company being made. It may be noticed that section 173 of the Companies Act, 1929, is in pari materia with section 536(2) of the Companies Act, 1956. Considering the question of jurisdiction, Vaisey J. observed as under :

" In my judgment, the object of the section, both in its original and in its present form, is that, if a winding-up order is made, any transaction which has been entered into since the commencement of the winding-up -which in the present case would be the date of the presentation of the petition--is subject to review by the liquidator. If that be the true object of the section, I have great difficulty in seeing how I have jurisdiction to adjudicate on what must be an incomplete knowledge of the facts. It is not right that I should anticipate the performance of his duty by the liquidator, if a liquidator is subsequently appointed, and it seems to me that to attempt to deal with the matter, not only by implication, but also entirely conditionally, is something which the section does not enable me to do. If there is never a winding-up, my order would be without operation. It would be completely otiose if the petition now before me is ultimately dismissed or withdrawn, but, if the petition results in the making of a winding-up order, it will be, I think, for the liquidator to deal with the matter as he thinks proper."

10. It would clearly appear that in the considered opinion of Vaise J. the court has not jurisdiction to make any order u/s 173 of the Companies Act, 1929, till an order for winding-up the company is made. Now, both Vaise J. and Buckley J. referred to a judgment of Chitty J. in *Carden v. Albert Palace Association*. In that case the order has made u/s 153 of the Companies Act, 1862, before any winding up order had been made in respect of the company. But it appears that the question of jurisdiction in terms was not raised before Chitty J., though Buckley J. appeared to have culled out that Chitty J. was aware of the question of jurisdiction. There are two other cases, one being in *In re International Life Assurance Society*, and *In re Wiltshire Iron Co.: Ex parte Pearson*, which have been referred to by Buckley J. But, in my opinion, these two cases would not be of any assistance because in both the cases winding up order was already made before the court's jurisdiction was invoked for validating dispositions of property. Vaisey J. did not attach any importance to the judgment of the court in *Carden v. Albert Palace Association* on the ground that that case did not attract the attention of judges and jurists and is cited only in a casual way in Stiebel's *Company Law and Precedents*, 3rd edition, page 830, and is not referred to in

Buckley or Palmer. Apart from that, looking to the report of that case, the question of jurisdiction does not appear to have been canvassed before the court. It would thus appear that the question of jurisdiction was in terms raised before Vaisey J. in *In re Miles Aircraft Ltd.* and before Buckley J. in *In re A.I. Levy (Holdings) Ltd.* Both these decisions take exactly contrary views of almost the same section and are not reconcilable.

11. My attention was drawn to only two cases decided u/s 536(2) by the courts in India. First case on the subject is *Ramesh Chandra v. Chopasni Ice, Aerated Water and Oil Mills Ltd.* Considering the scope of the jurisdiction of the court under sub-section (2) of section 536, the Division Bench has in no uncertain terms observed that the situation visualised by the section does not arise before a winding-up order is passed by the court. Mr.Vakil, who strongly favoured the construction put upon the section by Buckley J., urged that the reasons given by the Division Bench of the Rajasthan High Court for reaching this conclusion are not borne out by the language of sub- section (2). The criticism is not justified because the language of sub-section (2) and the scheme of the Act clearly indicate that, so long as the company is not ordered to be wound up by the court, the disposition of the property made by it would be prima facie valid and would only become void after the order for winding up that company is made. When a company is a going concern any disposition of property by the company would have to be made by the directors within the scope of their powers as set out in the articles of association and as are to be found in the provisions of the Companies Act. If the construction canvassed by Mr.Vakil is to be accepted, the court would be making inroads upon the powers of other directors and there is no jurisdiction for such an intrusion and that appears to be the reason which appealed to the Division Bench of the Rajasthan High Court and which becomes manifest from the observation that the section does not contemplate any of these orders of the court about disposition of the property of the company. This decision, therefore, supports the view that no order can be made u/s 536(2) of the Companies Act, in respect of disposition of property made by the company unless an order for winding up the company is made. The second case on the subject is *Mandya National Paper Mills Ltd. v. Shreeram Durgaprasad (Private) Ltd.* Again the question of jurisdiction of the court u/s 536(2) was raised before the court and the learned judge has in no uncertain terms held that the very foundation or the occasion for the court making an order referred to in sub-section (2) of section 536 is that there is a disposition of property made by the directors which has become void, and such an effect on the disposition follows upon an order of winding-up and not earlier. No doubt in reaching this conclusion the courts seems to have taken into consideration some of the peculiar facts of that case. It was however urged that the court appears to have experienced some difficulty in putting the aforementioned construction on the section which becomes clear from the observation of the court that :

" The order of the court which could save such an alienation from becoming void, appears ordinarily to be, in the light of the section, an order made after winding

up, because until an order for winding up is made, the normal powers of the directors continue, and, unless an order for winding up is made, any disposition or alienation made by the directors does not become void."

12. The use of the word "ordinary" does not mean that the court had any doubt about the construction sought to be placed on sub-section (2). In fact the court has expressed itself most clearly and unequivocally when it said that the occasion for exercise of the power u/s 536(2) arises after an order for winding up is made.

13. It would appear that the trend of the authorities is in the direction of the court having no jurisdiction to pass upon the validity or otherwise of disposition of property by a company before a winding-up order is made in respect of the company. Therefore, both upon principle as well as on authority, it appears that the court has no jurisdiction to entertain an application for validating the transaction or put its seal of approval upon a transaction by the company before that company is ordered to be wound up. Even if it is assumed that the object of the section is to protect the interests of the creditors from the possible unfortunate results which would ensue from the presentation of a petition, which appears to have influenced the decision of Buckley J., in my opinion, the question of protecting the interests of the creditors does not arise at a stage when no winding-up order is made. In fact, if the court were to arrogate to itself the power of jurisdiction to pass upon every disposition of the property at a time when the company is not ordered to be wound up, though the company is faced with a petition for winding up, the court would be making inroads into the powers of the directors which is not contemplated by sub-section (2) of section 536. It also appears that Buckley J. was influenced by the fact that if the other view is taken, the section could be said to be ill-designed to meet a kind of risk to the creditors of the company against which one would have expected it to be intended to protect them. With respect, this aspect cannot be imported to find out the true intent of the legislature in enacting section 536(2). In my opinion, the jurisdiction u/s 536(2) can only be invoked after the company is ordered to be wound up.

14. Miss V.P.Singh, learned advocate who appeared for the petitioning creditors, urged that if the court is called upon to examine all the aspects attendant upon the transaction before a winding-up order is made there would not be sufficient material before the court to finally adjudicate upon the nature of the transaction and all the interested parties would not be before the court. It was urged that it would not be possible to bring all the interested parties before the court at this stage. The complex procedure which the court may have to adopt in order to ascertain the wishes of all concerned would not be a factor to be taken into account while deciding the scope and ambit of jurisdiction under sub-section (2) of section 536. If the court has jurisdiction, it would be open to the court to advertise the petition and to give a direction that the applicant who moves the court for approval of the disposition of the property to serve notice upon all the

creditors and members of the company and after hearing them the court can adjudicate upon the nature of the disposition. The cumbersome procedure which the court may have to adopt would not influence my mind in finding out the scope of the jurisdiction of the court under sub-section (2).

15. In view of the aforesaid discussion, these summonses are dismissed and the rule is discharged in both the applications with costs.