
(1958) 03 MAD CK 0029
In the Madras High Court

Syed Mahomed Ali

APPELLANT

Vs

M.R. Sundaramurthy and Others

RESPONDENT

Date of Decision : 20-03-1958

Acts Referred:

Companies Act, 1956 — Section 397, 398

Citation : AIR 1958 Mad 587 : (1958) ILR (Mad) 838 : (1958) 2 MLJ 259

Hon'ble Judges : Ramachandra Iyer, J

Bench : Single Bench

Judgement

Ramachandra Iyer, J.—This appeal filed at the instance of Syed Mahomed Ali, a shareholder, arises from the judgment of Subrahmanyam,

J., in O.P. No. 159 of 1956 giving certain directions under Sections 397 and 398 of the Indian Companies Act. That petition was filed by

Sundaramurthy the first respondent supported by 42 shareholders of the Neptune Studios, Ltd., complaining of several prejudicial acts and

breaches of trust on the part of respondents 2 to 8, the directors, alleging oppression of the minority by them and praying for regulating the conduct

of the company's affairs in future. Neptune Studios, Ltd., which will hereafter be referred to as "the company" is a public limited company with a

subscribed share-capital of Rs. 3,15,000 consisting of 6,150 shares, 4,000 founder-shares of Rs. 25 each and 2,150 ordinary shares of Rs. 100

each. The company owns a studio and an equipment for the production of cinematograph pictures. The company hires out the premises and the

equipment and affords facilities to producers of pictures for monetary consideration. The fortunes of the company do not depend on the success or

failure of the pictures produced by it as it does not itself produce any picture. Such being the nature of the business of the company there is no

scope for loss if its affairs were properly managed. The directors of the company, viz., respondents 2 to 8, were interested either as directors or as partners or proprietors in several picture-producing concerns like the Jupiter Pictures (Private) Ltd., Saravanabhava Pictures, Manohara Pictures, Unity Pictures and Jyothi Pictures. These producing concerns will hereafter be referred to as the ""Jupiter group."" The second respondent who had interest in more than one concern in the group became a director of the company in 1951. In course of time respondents 2 to 8 and their relations in all about ten shareholders acquired and held 3,652 founder shares and 1,098 ordinary shares of the total value of Rs. 20,1100. According to the petitioners, the directors having obtained this large volume of shares misused their position as a result of which the company sustained loss year after year. Although it appears that even before the advent of the second respondent and his friends on the directorate the company showed loss, the mounting losses in succeeding years after 1951 was a matter of concern to the shareholders. By a resolution of the general body at a meeting held on 25th December, 1956, a committee of five shareholders including Sundaramurthy and Syed Mahomed Ali Was appointed to investigate and report about the affairs of the company. The committee submitted its report on 29th January, 1956, wherein quite a good number of irregularities and breaches of trust on the part of the directors were mentioned. No action appears to have been taken on the report of the committee. Thereupon Sundaramurthy with the consent of 42 shareholders filed an application under Sections 397 and 398 of the Indian Companies Act for the regulation of the future conduct of the company's affairs. In that petition various charges were made against the directors. One of the main charges was that the directors of the company purporting to give rebate to producers gave a rebate of a sum of Rs. 1,35,000 to the Jupiter group whereas for an equal number of pictures produced for outsiders the amount of rebate given was only Rs. 12,800. There was thus illegal profit of Rs. 1,20,000 made by the directors to the detriment of the interests of the company. The second charge was that the directors have been creating mortgages and charges over the properties of the company in favour of their close relations, respondents 9 to 13 with the object of having a ""stranglehold"" over the company. The mortgages were alleged to be fraudulent transactions unsupported by consideration. It was further

alleged that the accounts of the company were not maintained properly nor were they passed at any general body meeting of the shareholders. The accounts were written for about five months in 1955. Besides these charges a number of instances of the directors, using their position to the detriment of the company were pointed out. It was alleged that the directors were paying nominal rents for the machinery or the premises of the company used by them in connection with the business of the Jupiter group; that they were debiting the company with exorbitant charges whenever the machinery or other equipment belonging to the Jupiter group were utilised for the purposes of the company; that the wages of the employees working under the Jupiter group were being paid out of the funds of the company; unserviceable articles belonging to the Jupiter group were sold to the company at high prices, such articles being of no use resulted in loss; that the company's moviola and sound-recording equipment were kept in disrepair and were not used while the moviola belonging to the Jupiter group was being lent to the company at an unconscionable rate of hire. Other charges of a minor nature such as consumption of electric current, etc., were also made. The directors were also charged with having closed the main entrance of the company at the Adyar Bridge Road and of having made an opening to the company's premises through the property of the Jupiter group so that anyone coming into the company must of necessity pass through their premises. Another charge was that they gained personal advantage by virtue of their position as directors in the company by obtaining contracts from the Ceylon Theatres, Ltd., Colombo, the benefit of which was taken by the Jupiter group which resulted in a loss of profit of about Rs. 1,20,000 to the company. Soon after the filing of the petition certain interlocutory applications were also filed. Application No. 1353 of 1956 was filed by Sundaramurthy for the appointment of a receiver. Application No. 1421 of 1956 was filed by him for the purpose of putting up a separate entrance to the property of the company and to re-open the entrance facing the Adyar Bridge Road. The respondents filed counter-affidavits to the applications and on 23rd October, 1956, the parties agreed to an interim order in terms of the memorandum of consent filed into the Court. Balakrishna Iyer, J., accepted the consent memo, and passed an order directing the existing directors to resign their office and also directing the affairs of the company to be managed by a

committee of management consisting of three persons from the petitioner's group and two from the group of the directors, namely, Sundaramurthy,

Syed Mahomed Ali, Natesa Mudaliar Balasubramaniam and S.K. Habibullah, pending disposal of the main petition, O.P. No. 159 of 1956. Syed

Mahomed Ali was to be the member-in-charge of the management having control over the administration, production business, etc. It is

unnecessary to refer to the other clauses of the order of the learned Judge. After this order of Balakrishna Iyer, J., Syed Mahomed Ali got into the

management along with the other members of the committee. In the meantime O.P. No. 159 of 1956 was posted at the preliminary stages for

hearing before the Master and as there appeared to have been an unanimous desire for a compromise in regard to the outstanding disputes,

counter-statement on behalf of the respondents was not filed and the petition was adjourned from time to time for reporting settlement. Syed

Mahomed Ali having got into the management began, in the opinion of the other members of the committee, to abuse his position and indulge in

various activities highly detrimental to the interests of the company. Whether that was true or not, the fact remains that he became unpopular with

the remaining four members, of the committee. Meanwhile proposals for the adjustment of the disputes were taking concrete shape. It was stated

in the counter-affidavit of the first respondent in Applications Nos. 2133 and 2134 of 1957 that the compromise proposals emanated from Syed

Mahomed Ali himself and that there had been numerous sittings of the parties at which there were elaborate discussions. No objections were taken

to the correctness of this statement by means of any reply affidavit by Syed Mahomed Ali and having regard to the other affidavits filed in the case

we can take it that Syed Mahomed Ali himself sponsored the compromise up to the stage when it became clear that he would not be included in

the committee of management proposed to be set up under the compromise. This exclusion disappointed Syed Mahomed Ali and he filed

Applications Nos. 2133 and 2134 of 1957 complaining that the committee of management appointed by the High Court as an interim arrangement

did not function properly and that another officer should be appointed to act with him in the conduct of the affairs of the company and also praying

for an order restraining the other members of the committee from interfering with his management. In the affidavit in support of the application he

repudiated the compromise which by then appears to have taken some shape. The sponsors of the compromise were, however, more thorough.

They put the terms of the compromise in the form of a memorandum and circulated it to all the shareholders. Forty of the shareholders signed the

memo, of compromise with the result that by including the directors group 50 shareholders holding shares to the value of Rs. 2,85,600 supported

the compromise. 19 shareholders holding shares of the value of Rs. 18,900 were neutral and the opposition was confined to Syed Mahomed Ali,

his brother and one Joseph Pallipat owning shares of the value of Rs. 10,500 only. Application No. 2179 of 1957 was then filed by Sundaramurthy

for approving the compromise. Applications Nos. 2196, 2197 and 2198 of 1957 were filed by one Joseph Pallipat to come on record as a party

in O.P. No. 159 of 1956, to reject the compromise and to file the report of the committee, dated 29th January, 1956. Briefly the terms of the

compromise were: (1) that the directors should give up their claim to a sum of Rs. 1,38,000 entered as a credit in their favour in the company's

accounts by way of rebate; (2) the company was to have no claim whatsoever against respondents 2 to 8 in respect of the various allegations and

the claims made against them in the original petition; (3) the loan transactions in favour of respondents 9 to 13 should be accepted as genuine; (4)

that the management of the affairs of the company should be vested in a committee of management consisting of five members, three to be

nominated by the 43 shareholders on the side of the petitioner and two to be nominated by the directors and one among the former to be the

member-in-charge. This committee of management was to function for a period of three years at the end of which the management of the affairs of

the company shall vest in a board of directors to be elected by the shareholders of the company. (5) In consideration of the directors' giving up

their claim for rebate all agreements between the company and the Jupiter group with regard to production of films, etc., should stand cancelled.

2. The petition and all the applications including those filed by Syed Mahomed Ali were heard by Subrahmanyam, J. The learned Judge did not,

however, accept the whole of the compromise. He adopted the clauses relating to the deletion of the credit of Rs. 1,38,000 in favour of the Jupiter

group in the books of the company and exoneration of the directors from all liability in respect of the various allegations and claims made against

them in the original petition. He refused to decide the genuineness of the transactions under which respondents 9 to 13 were claiming to be the creditors of the company and left their claims to be agitated in a proper suit. He disallowed the provision for management of the affairs of the company by a committee but directed the shareholders to elect their directors under the Articles of Association of the company at a meeting to be held on 6th January, 1958, but disqualified the persons who were directors or partners or proprietors of the various concerns in the Jupiter group from standing for election as directors for a period of one year. Provision was also made for the retirement of the directors in rotation and also for the appointment of a receiver pending the taking over of the management by the newly elected directors and for the conduct of the election of the directors. The applications filed by Joseph Pallipat and Syed Mahomed Ali were dismissed except to the extent of making Joseph Pallipat a party to Application No. 2179 of 1957.

3. Syed Mahomed Ali feeling aggrieved by the acceptance of the compromise has filed this appeal against the judgment of the learned Judge. Mr.

V.C. Gopalaratnam, appearing for the appellant, has criticised strongly the procedure adopted by the learned Judge and also the propriety of the

disposal of O.P. No. 159 of 1956 on the basis of the compromise memo. His main complaint was that the serious charges which were the subject-

matter of the petition have not been investigated but the directors were even without any enquiry completely exonerated from any liability to the

company. There is great force in the criticism of the learned advocate for the appellant in regard to the disposal of the petition. No notice was given

of the application to record compromise to Syed Mahomed Ali and his supporters. It is true that Syed Mahomed Ali, in his applications,

repudiated the compromise and those applications were also heard along with the main O.P. No. 159 of 1956. But it must not be forgotten that

Syed Mahomed Ali was constructively a party to the main petition and Sundaramurthy having supported the compromise, he was the only person

who could carry on the petition and notice of the application to record the compromise should have been given to him. A singular feature of this

case is that Sundaramurthy who was one of the committee that investigated and reported on 29th January, 1956, on the affairs of the company and

who solemnly subscribed to the petition containing serious charges against the directors made on the basis of the committee's report should have agreed to the compromise without any investigation of the charges. Nothing is mentioned in his affidavit in support of the compromise petition as to why he came to an opposite conclusion and agreed to the directors being completely exonerated. Such conduct on his part justifies to a great extent the suspicion and criticism that he was actuated by motives other than the welfare of the company in supporting the compromise. There is another feature of the proceeding which is not the less unfortunate. Although the petition was pending for nearly 18 months no counter-statement or affidavit was filed by the directors denying the serious charges that were made against them. There was no material placed before the Court which would show even prima facie that the charges were not justified. The learned Advocate-General has stated from the Bar that the respondents had practically prepared a counter-statement but they did not proceed with the same as there were talks for compromise in which even Syed Mahomed Ali participated. While we accept that statement it must be pointed out that in a matter of this kind where the complaint is one of oppression by a powerful majority it was essential that the directors should have filed their counter-statement and even tendered some prima facie evidence by affidavit, auditors' report or otherwise to show that there was no substantial basis for the charges and that the matter could be disposed of by compromise. The omission of the respondents even to deny the charges had given rise to a not wholly unjustified criticism that the compromise might have been a maneuver to prevent the Court from investigating the state of affairs. Proceedings under Sections 397 and 398 of the Indian Companies Act are not like suits between private parties which could be compromised in any manner they choose. The interests of the, company are paramount. u/s 406, there is jurisdiction in Court to assess damages against delinquent directors. In such circumstances the Court should have given an opportunity to the dissentient shareholders to become parties to the petition or should have disposed of the matter after due notice to them. Joseph Pallipat sought to come on record in the Original Petition but by some mistake the learned Judge did not make him a party to that petition but merely made him a party to the Application No. 2179 of 1957. As pointed out already, there are certain unsatisfactory features

in the management of the company which required explanation. It is rather strange that the company should incur loss year after year. Accounts were admittedly not properly kept. Rebates and debits required a detailed scrutiny. The charges against the directors were sufficiently serious to require an explanation from them at least to provide for safeguards against future malfeasance. The learned Judge considered that even if the charges were true the giving up of the credit in their favour by the Jupiter group to the extent of Rs. 1,38,000 was a substantial gain which would warrant the abandonment of any further investigation. We regret that we cannot share that view. The learned Advocate-General argued that Sections 397 and 398 should be worked with a view to make the company function and not to wind it up and that if the minority which complains of the oppression is satisfied, there is no need to further investigate the matter. We cannot agree. Both under Sections 397 and 398 the interests of the company are of paramount importance and the proceedings should not be conceived as a mere dispute between individuals. Any compromise suggested should be acceptable to the Court whose powers are set out in Section 402. Even accepting the argument, the compromise which has not been agreed to by Syed Mahomed Ali, one of those represented in the petition, cannot be used to stifle the enquiry of the petition in the absence of a finding that the compromise was entered into bona fide in the interests of the company as a whole. The learned Advocate-General 1 referred to the decision *In re Antingen Laboratories, Ltd.* (1951) All. E.R. 110, and a passage from Buckley's "Company Law", page 1091, in support of the proposition that a petitioner seeking relief u/s 210 of the English Companies Act which corresponds to Section 397 of the Indian Companies Act should state in the prayer in clear terms the general nature of the relief sought whether it be for the appointment of a director or of some other kind. His contention was that in the petition the only relief prayed for was regulation of the conduct of the affairs of the company in future and not in regard to any action against the director for the alleged malfeasance and misfeasance. That may be so; but the petition contains an elaborate statement of the charges against the directors and an investigation into those charges would be necessary even for the purpose of regulating the affairs of the company. We do not think that the absence of any formal prayer in the petition u/s 397 would entitle the Court to

refrain from investigating into the various charges levelled against the directors. In Gower's "Modern Company Law", 2nd edition, at page 513, the

scope of Section 210 of the English Act which corresponds to Section 397 of the Indian Companies Act is discussed and referring to Cohen

Report on which the section in the English Act was based the learned author says:

that it was the intention that the Court should "have power to impose upon the parties whatever settlement the Court considers just and equitable".

While recognising that the Court could not be expected in every case to find and impose a solution it was thought that its discretion must be

unfettered for it is impossible to lay down a general guide in the solution of what are essentially individual cases.

Referring to the decision In re Antingen Laboratories, Ltd. (1951) All. E.R. 110, the learned author says:

that it has been held that the petitioner cannot just ask the Court to exercise its discretion but must indicate the nature of the relief wanted. This

decision though perhaps inevitable seems regrettable and inconsistent with the intention that the Court should have power to find and impose a

solution.

The decision of the English Court was, as pointed out by the learned author, the result of the procedure of the English High Courts:

which was ill adapted for the exercise of the inquisitorial and constructive role thus imposed upon the Court.

We are not hampered by such rigid technicalities of procedure and if the minority in a company complains of an oppression and discloses certain

grounds of complaint in the petition which are made the basis for the reliefs, we would have that the Court should ordinarily investigate the charges.

Such investigations may in certain cases be necessary even to regulate the future conduct of the company for providing against recurrence of such

abuses of power by the majority. We are, therefore, of opinion that notwithstanding the omission in the petition to pray for relief against the

delinquent directors, and enquiry into the charges against them was properly within the scope of the petition. Sections 402 and "406 of the Indian

Companies Act give ample jurisdiction to the Court to dispose of the matter in the larger interests of the company. The question then is whether it

would be in the interest of the company and even of the disappointed minority to

set aside the compromise and start an enquiry on the petition. Mr.

V.C. Gopalaratnam has conceded that it was not his client's intention that the company should be wound up. As the learned Advocate-General

rightly pointed out any order that may be made u/s 402 should be to facilitate the working rather than the destruction of the company. Discussing

the nature of the jurisdiction under the corresponding section of the English Act, Mr. Gower in his book on ""Modern Company Law"", says at page

513:

Nevertheless the section is of undoubted value. Despite the paucity of reported cases it has been extensively and effectively invoked as a threat to

induce those in control to behave reasonably towards all interests and as a weapon in the investor's armoury it will probably always prove more

efficacious when brandished in terrorem than when actually used to strike.

4. In regard to the regulation of the future conduct of the company's affairs the learned Judge's order would be quite sufficient. The only persons

who could be dissatisfied with it are the persons belonging to Jupiter group who are disqualified from standing for election for one year but they

have gracefully accepted the direction. The learned Judge has, if we may say so with respect, made a correct approach to the question by

considering the compromise put before him on the merits and adopting only such portions of it which were in the interests of the company, We are

then left with the only question which was pressed before us with great insistence by Mr. V.C. Gopalaratnam as to the desirability or expediency of

remanding the case for disposal after giving an opportunity to the appellant to prove the charges against the directors. Though the charges required

investigation, it does not appear that any shareholder was anxious to have them investigated. The directors denied the charges in the counter-

affidavits filed by them to the various interlocutory applications. We have already said that a counter-affidavit to the main petition was practically

ready to be filed but was not filed in view of the unanimous desire for settlement. Syed Mahomed Ali too was participating in the talks for

settlement. He had since his appointment in the managing committee, complete access to the accounts and other papers of the company. He was

familiar with the charges as he was one of the committee of shareholders that investigated and made a report to the general body on 29th January,

1956. He could have, during the pendency of the petition, initiated proceedings u/s 406 if he really believed in the charges. Instead he was willing to compromise and broke off only when it was plain that he was not to get a share in the management. We agree entirely with the learned Judge that the opposition from Syed Mahomed Ali and his small group were actuated by personal motives. It is unfortunate that the parties in the case viewed the matter-as a mere game for getting into power rather than serving the interests of the company. This is evident from the fact that immediately after the order of Balakrishna Ayyar, J., negotiations were started for settlement and positions of power. The conduct of Syed Mahomed Ali in the managing committee appointed under Balakrishna Ayyar, J.'s order does not appear to have satisfied the others. The result is that but for the opposition by a small group under Syed Mahomed Ali who undoubtedly is actuated by reasons other than the welfare of the company, no other shareholder wants the proceedings to be continued. There is no doubt, that rehearing of the petition at this stage would only lead to acrimony and bitterness and perhaps invest in the hands of Syed Mahomed Ali an increased bargaining power. That would lead to an undesirable state of affairs in the working of the company and far from the majority oppressing the minority, the minority would become the masters of the situation. We consider, therefore, in the circumstances, particularly after the order of the learned Judge regulating the future affairs of the company, it is inexpedient to start an enquiry into the charges. We cannot, however, sustain the direction contained in para. 4 of the decretal order (schedule) under which the directors are exonerated from all liability in respect of the various allegations against them. We delete that clause from the decretal order. In doing so we also modify the Clause 3 under which respondents 2 to 8 give up their claim to Rs. 1,38,000 by declaring that if at any time proceedings are taken against respondents 2 to 8 in respect of the charges mentioned in O.P. No. 159 of 1956, their giving up of this claim of Rs. 1,38,000 will not disentitle them from pleading a discharge of their liability to the extent of that sum. This right would be without prejudice to the right of the company to show that the credit entry of Rs. 1,38,000 was itself not binding on it. Subject to these modifications we dismiss the appeal. There will be no order, as to costs. C.M.P. No. 523 of 1958 dismissed. No costs.