
(1988) 04 KL CK 0010

In the High Court Of Kerala

Case No : M.C.A. No. 93 of 1987 in C.P. No. 15 of 1984

Travancore Rayons Ltd.

APPELLANT

Vs

Registrar of Companies

RESPONDENT

Date of Decision : 05-04-1988

Acts Referred:

Companies Act, 1956 — Section 536(2)

Citation : (1988) 64 CompCas 819 : (1988) 2 ILR (Ker) 655

Hon'ble Judges : Varghese Kalliath, J

Bench : Single Bench

Advocate : K.A. Nair and Antony Dominic, for the Appellant; C.S. Rajan, Thomas Rajan, P. Sankarankutty Nair, George Varghese and T. Mathew Thomas, for the Respondent

Final Decision : Allowed

Judgement

V. Kalliath, J.—Travancore Rayons Ltd. is the applicant. The applicant came up before this court u/s 536(2) of the Companies Act, 1956. This section provides that in a winding up, any disposition of property of a company made, after the commencement of the winding up, shall, unless the court otherwise orders, be void. Three winding-up petitions are pending against the applicant-company. They are C.P. Nos. 15 of 1984, 21 of 1985 and 2 of 1986, All these petitions for winding up the company are on the ground that the company is unable to pay its debts.

2. In the application, the company submits that the company was registered under the Indian Companies Act, 1913, with its registered office at Rayonpuram, Perumbavoor, Kerala State. The company was incorporated on July 19, 1945, and it commenced its business in March, 1946. It was carrying on its business profitably during its early years. In 1975, there was an unprecedented strike by the workers lasting for about six months and there was also a devastating fire in the factory in 1976 in which large quantities of raw materials was gutted. After this unfortunate event, the company was industrially sick for the succeeding five

years, though it was employing over 1500 workmen. A mode of rehabilitation was earnestly desired by the company. For this purpose, a consortium of four All-India financial institutions consisting of IDBI, IFCI, ICICI and IRBI met and discussed ways and means of rehabilitating the unit. I am told that the financial consortium ultimately expressed its preparedness to advance a loan of Rs. 511 lakhs. In fact, out of this sanctioned loan, a substantial part of the loan has already been received by the company and the balance sanctioned loan amount is only Rs. 225 lakhs. I may also incidentally refer to an earlier loan granted by the above financiers to the company. As early as on September 15, 1984, this company was given Rs. 510 lakhs by the financiers. Of course, for this 510 lakhs of rupees, the financiers obtained both movable and immovable properties of the company as security. To say it plainly, the loan amount of Rs. 510 lakhs granted on September 15, 1984, is a secured debt.

3. Now, the company wants the remaining amount of the second loan sanctioned, namely, Rs. 225 lakhs. When the company approached the financiers for the said loan, the financiers insisted that they must be given security not only for Rs. 225 lakhs but also for the entire amount of Rs. 511 lakhs. Since winding-up petitions are pending before this court, the financiers also insisted that before offering movable and immovable properties as security, the company should obtain appropriate leave and sanction from this court u/s 536(2) of the Companies Act. This situation necessitated the company approaching this court with a petition u/s 536(2) of the Companies Act.

4. As I said earlier, leave was sought u/s 536(2) of the Act since three company petitions for winding up the company are pending. These petitions have proceeded to any length to reach a finale. They are in the first stage. The petitioners in two of the petitions are opposing the application filed by the company u/s 536(2). The petitioner in C.P. No. 21 of 1985 submits that an amount of more than Rs. 4 lakhs is due from the company and that out of the said amount, Rs. 2,15,000 is supposed to be an admitted amount. The petitioner in C.P. No. 15 of 1984 also submits that a little more than Rs. 20,000 is due from the company to the petitioner. This petitioner also seriously opposes the application u/s 536(2) of the Companies Act, of course, the petitioner in C.P. No. 2 of 1986 who claimed that they have to get an amount of Rs. 16 lakhs has not chosen to oppose this petition.

5. The company in question is one of the companies included in the notification under the Kerala Relief Undertakings (Special Provisions) Act, 1961. The consequential effect of enlisting the company within such a notification is really in effect a declaration of a moratorium, a hold up regarding the repayment of debts by the company. So long as the notification continues with respect to this company, this court may not order the winding up of the company. All recoveries in regard to the liabilities of the company are statutorily suspended.

6. Counsel for the petitioner submitted before me that the application is made with utmost good faith and honesty and that there are adequate and sufficient

reasons and persuasive circumstances for this court to exercise the power u/s 536(2) of the Companies Act in favour of the company. I feel that it is now apposite to quote Section 536(2) of the Companies Act.

" In the case of 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."

7. Before considering the merits of the case, I must be fully informed of my power u/s 536(2). I must know the real width, ambit, content and scope of the said provision. What is the power encapsulated in the said section ? A serious incidental question is as to whether it is open to me to make an order granting leave for the disposition by the company of its assets as sought for at the present stage, when no order has been made in the winding up proceedings which is still pending. This secondary question is raised on the wording of Section 536(2). This doubt is not a new one. It is created on the lingo and formulation of the section to wit "in the case of winding up by or subject to the supervision of the court, any disposition of the property (including actionable claims) of the company.....shall, unless the court otherwise orders, be void." Whether the power u/s 536(2) is exercisable only when an actual winding up order is passed and only when the court can examine whether the creation of a security on immovable property is justified or valid, since it is done when winding up petition/petitions is/are pending. Though this is a point of difficulty, I feel that there is no great ado to answer this question. The provision in the Indian Companies Act is almost identical with the provision in the English Companies Act. In English Law, two poles of judicial opinion existed, but now it is settled. As early as in 1948, a direct question came up for consideration before Vaisey J. regarding the jurisdiction of the company court to exercise the power to grant leave for disposition of assets of a company against which a winding-up petition was pending in *Miles Aircraft Ltd., In re* [1948] Ch 188; [1948] 18 Comp Cas 250 (Ch D). When the petitioning creditors opposed the making of the order, Vaisey J., after saying that the question raised before him was whether he had jurisdiction in those circumstances to make the order, read with Section 173 of the Act of 1929 and Section 153 of the Act of 1862, said (at page 252 of 18 Comp Cas): "In my judgment, the object of the section both in its original form and in its present form was this, that if a winding-up order is made any transaction which has been entered into since the commencement of the winding-up--which, of course, in the present case, if the winding-up order is made is the date of the presentation of the petition--is subject to review by the liquidator..... All that we have now is a contingent future possible winding-up and I do not think the section is so framed as to give me jurisdiction to adjudicate on this matter, so to speak, in advance. I must, therefore, dismiss this summons with costs."

8. The matter came up again before Buckley J. In *A.I. Levy (Holdings) Ltd., In re*

[1964] 1 Ch 9; [1964] 34 Comp Cas 720 (Ch D), considering Miles Aircraft's case [1948] Ch 188 ; [1948] 1 All ER 225 ; [1948] 18 Comp Cas 250 (Ch D), and other cases including the decision of Chitty J. and Pennycuik J. in *Garden v. Albert Palace Association* [1887] 56 LJ Ch 166; and *In re Douglas Griggs Engineering Ltd.*, [1963] Ch 19; [1962] 2 WLR 893 ; [1962] 1 All ER 498 Buckley J. said (at page 727 of 34 Comp Cas):

"I think I am bound to look at Vaisey J.'s decision in Miles Aircraft's case [1948] Ch 188 ; [1948] 1 All ER 225 ; [1948] 18 Comp Cas 250 (Ch D) with considerable care to see whether it is in fact an authority which I ought to feel myself bound to follow to the conclusion that I have no jurisdiction to make the order asked for in the present case. "

9. An elaborate consideration is made by Buckley J. on this question and he finally said (at page 728 of 34 Comp Cas):

"In these circumstances, with greatest respect to Vaisey J., from whose view as to jurisdiction, I think I am, in the circumstances, at liberty to differ, I hold that I have jurisdiction and that on the facts of this case, I should exercise my jurisdiction here and now, notwithstanding that no winding-up order has yet been made. "

10. This decision has been approved by Slade J. in *Burton and Deakin Ltd.*, *In re* [1977] 1 All ER 631 (Ch D).

11. In my view, the animus of the sub-section is to forbid malapropos and objectionable disposition or dissipation of property which would ultimately fall to a low ebb or tail off the assets otherwise available for distribution among the creditors of the company in the event of winding up. But the section leaves a reserve power of discretion to justify and uphold all genuine and proper transactions, exercising a sound discretion normally validating transactions which are benign and honest; transactions which have been done in the best interest of the company and in the ordinary course of the company's business. The legislative intent is plainly manifested by the use of the select expression "unless the court otherwise orders" which mandates silently but eloquently a duty on the judge to examine each case on its peculiarities, facts and circumstances, special bearing being given to the question of good faith and honest intention aimed at the best interest of the company. The omission to indicate any special guiding principles in the matter of discretion to be exercised by the court, makes it clear that it is not left entirely at large, but controlled only by the general principles which apply to every kind of judicial discretion.

12. In *Burton and Deakin Ltd.*, *In re* [1977] 1 All ER 631 (Ch D), the court of Chancery Division observed (head note):

"If on an application u/s 227 relating to a solvent company, its directors placed before the court evidence that they considered that a particular disposition falling within their powers was necessary or expedient in the interests of the company,

and if the court considered that the reasons given were such as an intelligent and honest man could reasonably hold, the court would normally sanction the disposition notwithstanding the opposition of a contributory, unless the contributory had adduced compelling evidence which proved that the disposition is likely to injure the company. The court would not, except in the case of proven bad faith or other exceptional circumstances, interfere with the discretion conferred on the directors by a company's articles of association at the instance of a contributory, even if a winding-up petition had been presented. "

13. The special Bench of the Rajasthan High Court considered the question in *B. Gopal Das v. Kota Biran (P) Ltd.* [1972] Tax LR 2285. The court held thus (head note...):

" In the absence of any prohibition in the law, there is no reason why the court should be precluded from examining the propriety of a proposed disposition during the pendency of a winding-up petition if the company has a genuine case requiring early consideration. The High Court has, therefore, jurisdiction u/s 536(2) to authorise a disposition of a company's property during the pendency of a winding-up petition notwithstanding that a winding-up order has not been made. "

14. The same conclusion has been reached by the Bombay High Court in the decision in *Kamani Metallic Oxides Ltd. v. Kamani Tubes Ltd.* [1984] 56 Comp Cas 19. Though the conclusion was identical with the conclusion of the Rajasthan High Court, the reasoning was slightly different. This is clear from the following observation (at page ...):

The "expression "In the case of winding-up " means " during winding-up proceedings " and not " after winding-up order is passed", or "upon passing such order". Hence, the court can authorise disposition of the company's assets u/s 536(2) even before the winding-up order is passed."

15. The obvious purpose of the petitioner-company in approaching this court perhaps is to avoid future challenge of the security offered. If a security is offered and if the same is accepted at a time when winding-up petition or petitions were pending, in the event of winding-up, the liquidator has got the power to challenge the correctness or the genuineness of the security. The lender wants to avoid this contingency before it decides to grant the loan. The borrower is in need of the loan in the best interest of the company. This heteromorphic position can pass muster only if previous sanction is obtained by the company u/s 536(2) of the Companies Act. If I decline to grant sanction on a narrow interpretation of the section, viz., that I can exercise the power u/s 536(2) only in the event of an order of winding-up, in certain genuine cases where disposition should be necessary in the best interest of the creditors of the company, it will be made impossible. I do not think that such an interpretation is intended by the Legislature and the court should not limit the scope of the section to that extent, and so, necessarily, the company court should possess jurisdiction and protect

the interest of the creditors if such transactions are genuine and bona fide and are for the purpose of promoting the interest of the company. When I say "it is for the purpose of promoting the interest of the company", I am bound to remember realistically the interest of the creditors and particularly the interest of the creditors who have come up before me with the winding-up petitions.

16. Now, I turn to consider the facts which are highlighted by the company for the relief and the facts placed before me by the respondents who opposed the petition. I first consider the possible and potential advantages to the creditors who are opposing this petition. Certainly, they want this petition to be dismissed. In case I dismiss the petition, I put to myself a question with two points what immediate or mediate benefit or advantage the creditors are obtaining. Certainly, no immediate advantage. By dismissing the petition, no progress will be made in the matter of winding up either. No immediate payment of the alleged debts can be ordered by this court. This is prevented by a statutory stay under the Relief Undertakings Act. The only advantage that can be envisaged is an advantage of a potential nature. In the event of passing an order of winding up, the creditors' distributive share in the assets of the company will be affected, if the loan amounts received with sanction of this court from the financiers are not utilised for reviving the company or augmenting the assets of the company. Certainly, this is so because an additional secured debtor is emerging in the fray of creditors. . Now, I turn to consider the reverse side of the picture, namely, if I grant sanction, what would be the effect ? First and foremost my concern in this aspect is to examine the honesty and good faith spotlighted in the petition on which the reliefs in the petition are founded. If the request of the company is allowed and leave for disposition is granted, certainly, there is a well-grounded hope of reviving or rehabilitating the company and if the company succeeds, the company may be in a position to pay all its debts including the debts of the respondents who are opposing this petition.

17. I have to decide this question on the materials available before me, facts disclosed and the circumstances developed in the case. One illuminating fact which is relevant and pertinent is that very renowned and well-established financiers have offered to grant considerably large amounts as loan to the company. This is not disputed and the financiers have appeared before me. They told me that they have studied the situation of the company carefully and scientifically with the help of their technical experts. This is one of the circumstances which very much persuades me to grant the relief sought for. Again, it is also plain and clear that this company has been included in the notification under the Kerala Relief Undertakings (Special Provisions) Act, 1961. So, this circumstance leads to a fact of secondary importance in assessing the merits of the respective cases that it is not possible for this court to pass an order of winding up immediately or at least within a reasonable time.

18. No material, substantial in character, has been placed before me to consider seriously the honesty and good faith of the company. The company is not hiding

the fact that it is in financial difficulties and that has been placed before this court as an open book. But the company tells me that it is attempting to revive and rehabilitate the company where over 1,500 employees are working. Now, I turn to the final question. I can say definitely that no limits are placed by the section on the court's discretion to grant or refuse an application u/s 227 (here Section 536(2)) and such a discretion will, of course, have to be exercised in every instance having regard to the particular circumstances of the particular case (vide *Burton and Deakin Ltd., In re* [1977] 1 All ER 631 at page 637 (Ch D)). Certainly, if I refuse sanction, it will be a great setback to the honest and genuine attempt of the company to rehabilitate itself. I do not think that this court should hold back the company from making an attempt to rehabilitate itself. I feel that the leave for disposition sought for is necessary and expedient in the interest of the company and I hold that the reasons given are such that an intelligent and honest man could reasonably hold, and the court will normally sanction the disposition, notwithstanding the opposition.

19. In the result, I would allow the petition. I permit the applicant company, Travancore Rayons Ltd., Rayonpuram, Perumbavoor, to create a charge of Rs. 511 lakhs over the movable properties of the company in favour of IDBI, ICICI, IFCI and IRBI.