

V. Ramachandran, Professor Dr. Moolamattom Varkey Paily and K.V. Rajan "Sangeetha" Vs Official Liquidator

Court: High Court Of Kerala

Date of Decision: April 1, 2008

Acts Referred: Companies (Court) Rules, 1959 " Rule 260

Companies Act, 1956 " Section 446, 542, 543, 543(1)

State Financial Corporations Act, 1951 " Section 27(1)

Hon'ble Judges: K. Hema, J; J.B. Koshy, J

Bench: Division Bench

Advocate: M. Pathrose Mathai, for the Appellant; K. Moni, for the Respondent

Final Decision: Allowed

Judgement

J.B. Koshy, J.

A company, namely, M/s.Velton Prefan Elements Limited was under liquidation. The official liquidator filed company

application u/s 542 and 543(1) of the Companies Act read with Rule 260 of the Companies (Court) Rules, 1959 for recovering Rs. 47,637.25

from all the directors of the company (appellants in these appeals) contending that the above debts became time-barred due to the inaction on the

part of the ex- directors. The above debt became time-barred before winding up proceedings started. According to the official liquidator, if proper

action was taken, this amount would not have become time-barred. Hence, the above amount should be realised from the ex-directors together.

The company court after detailed consideration found that the managing director did not bring to the notice of this fact to the director board and

found that the debt amounting to Rs. 48,137.25 became time-barred due to the negligence or omission on the part of the board of directors for not

taking proper steps for recovering the same and one-half of the liability was cast on the managing director and the other half amount in equal

proportion from other directors, respondents 2 to 5 in the company application. Therefore, first respondent managing director was directed to pay

Rs. 24,068.63 and other directors were directed to pay an amount of Rs. 6,017.18 to the company. The managing director (first respondent) filed

Company Appeal No. 38 of 2003 and respondent Nos. 3 to 5 filed M.F.A. No. 237 of 2002. Appellants in M.F.A. No. 237 of 2002, apart from

contending that the order of the company court is illegal as no allegation was alleged for taking action against the directors jointly u/s 542 and

543(1) of the Companies Act. It was also argued that they are directors nominated by the Financial Corporation u/s 27(1) of the State Financial

Corporation Act for protecting the interests of the Financial Corporation and securing that the accommodation granted by it is put to the best

interest of the industrial concerned. It was argued that no action can be taken against them u/s 543(1). If they are not doing their duties in not

conducting the interest of the Financial Corporation, only the Financial Corporation which nominated them can taken action. The learned Counsel

for the official liquidator argued that even though the Financial Corporation can nominate any person notwithstanding the provisions in the

Memorandum of Articles of Association or Companies Act, but, they are also accountable once they are in the Board. If amounts from the

company are advanced to others and no proper action is taken to recover the same, the repaying capacity will be lost and in that way, the

Financial Corporation also will be interfered and also cited the decision of the Calcutta High Court in A. Stock and Co. (In Liquidation) and

Official Liquidator Vs. Dilip Kumar Chakraborty and others, . wherein it was held that nominee directors can also be held liable depending upon

the role which they played in the conduct of affairs, i.e., whether they performed their statutory duties in good faith. It was held in Official

Liquidator v. Ram Swarup (1997) 88 Comp. Cas. 569 that nominee director cannot be permitted to defend themselves against liability just by

saying that they only knew that the directors were withdrawing heavy amounts from the company free of interest. If action taken u/s 542 and 543

are not maintainable on the facts of this case, this legal question need not be considered for academic interest.

2. Sections 542 and 543 of the Companies Act reads as follows:

542. Liability for fraudulent conduct of business:- (1) If in the course of the winding up of a company, it appears that any business of the company

has been carried on with intent to defraud creditors of the company or any other persons or for any fraudulent purpose, the Tribunal, on the

application of the Official Liquidator, or the liquidator or any creditor or contributory of the company, may, if it thinks it proper so to do, declare

that any persons who were knowingly parties to the carrying on of the business to the manner aforesaid shall be personally responsible, without any

limitation of liability, for all or any of the debts or other liabilities of the company as the Tribunal may direct.

On the hearing of an application under this sub-section, the Official Liquidator or the liquidator, as the case may be, may himself give evidence or

call witnesses.

(2) (a) Where the Tribunal makes any such declaration, it may give such further directions as it thinks proper for the purpose of giving effect to that

declaration.

(b) In particular, the Tribunal may make provision for making the liability of any such person under the declaration a charge on any debt or

obligation due from the company to him, or on any mortgage or charge or any interest in any mortgage or charge on any assets of the company

held by or vested in him, or any person liable or any person acting on his behalf.

(c) The Tribunal may, from time to time, make such further order as may be necessary for the purpose of enforcing any charge imposed under this

sub-section.

(d) For the purpose of this sub-section, the expression "assignee" includes any person to whom or in whose favour, by the directions of the person

liable, the debt, obligation, mortgage or charge was created, issued or transferred or the interest was created, but does not include an assignee for

valuable consideration (not including consideration by way of marriage) given in good faith and without notice of any of the matters on the ground

of which the declaration is made.

(3) Where any business of a company is carried on with such intent or for such purpose as is mentioned in Sub-section (1), every person who was

knowingly a party to the carrying on of the business in the manner aforesaid, shall be punishable with imprisonment for a term which may extend to

two years, or with fine which may extend to fifty thousand rupees or with both.

(4) This section shall apply, notwithstanding that the person concerned may be criminally liable in respect of the matters on the ground of which the

declaration is to be made.

543. Power of Tribunal to assess damages against delinquent directors, etc. (1) If in the course of winding up of a company, it appears that any

person who has taken part in the promotion or formation of the company, or any past or present director, manager, liquidator or officer of the

company

(a) has misapplied, or retained, or become liable or accountable for, any money or property of the company; or

(b) has been guilty of any misfeasance or breach of trust in relation to the company;

the Tribunal may, on the application of the Official Liquidator, or the liquidator, or of any creditor or contributory, made within the time specified in

that behalf in Sub-section (2), examine into the conduct of the person, director, manager, liquidator or officer aforesaid, and compel him to repay

or restore the money or property or any part thereof respectively, with interest at such rate as the Tribunal thinks just or to contribute such sum to

the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust, as the Tribunal thinks

just.

(2) An application under Sub-section (1) shall be made within five years from the date of the order for winding up, or of the first appointment of

the liquidator in the winding up, or of the misapplication, retainer, misfeasance or breach of trust, as the case may be, whichever is longer.

(3) This section shall apply notwithstanding that the matter is one for which the person concerned may be criminally liable.

3. Section 543 empowers the court to assess damages and requires the delinquent officer or director to pay the amount to the company, if by

sheer inaction, claims of the company is allowed to become barred, it can be recovered from the concerned officer u/s 543. The section is not

creating any new right or offence, but, only provides a summary and cheap remedy for enforcing the rights as are otherwise enforceable by law.

But, for enforcing such right, there should be breach of trust and an act or omission which results in loss to the company. Gross negligence on the

part of directors will amount to misfeasance. Misfeasance was held to be inferable where large amount of money is withdrawn by the directors of

the company or their relatives when the company was grinding in loss. If the money is lent in contravention of the Memorandum of Association, the

officer or director who is responsible for the same is also liable for action u/s 543, but, no liability can be granted if the company itself had written

off the claims as bad debts. Mere vague and general accusations will not be sufficient to find a liability u/s 543. There should be an act of

commission or omission. It is true that the court is vested with jurisdiction to examine the conduct of the past or present directors, manager or

liquidator or any of the officer, if he was guilty of misfeasance or breach of trust in relation to the company's property. All depends upon the facts

of each case. Conduct of the directors has to be looked into. Only two items in the general charge alleged against all the directors and the charges

are as follows:

As per the schedule II attached to the Statement of Affairs submitted by the Ex- Directors of the company it is seen that a sum of Rs. 11,413.54

due by Incos Marketing Services, Incos House, Anpal Building, Ernakulam to the above company which has been furnished as good. Demand

notices were issued to the above firm in the address furnished by the Ex-Directors of the company which was returned by the postal authorities

with remark "not known". The Ex-Managing Director had also furnished four different addresses of the above debtor and the Official Liquidator

issued demand notices again to the said debtor for realisation of the above debt together with interest which was also returned unserved with postal

remark "not known". As per the ledger for the year 1986-87, folio 13, book No. 21, it is seen that the last transaction made by the company with

the above debtor was on 10.2.87. As such the aforesaid debt is barred by limitation before the commencement of winding up. Therefore no claim

could be filed against the above debtor u/s 446 of the Companies Act, 1956 in this case.

As per the Statement of Affairs submitted by the Ex-directors of the Company a sum of Rs. 33,770.25 shown as due to the company. The said

debt shown as bad debts. Demand notice was issued by the official liquidator in the available address viz. Silver Trading Company, 6-Rajdeep,

Gokhale Road, Near Telephone Exchange, Bombay furnished by the Ex-directors of the company for realisation of the above debt together with

interest at 12% per annum from the date of default till the date of realisation. The said demand notice was returned unserved with postal remark

left". As per the latest ledger for the year 1987, Book No. 21, Folio 13, it is seen that the said amount is only a carry forward figure from 1.7.86

and thereafter no transaction has been made by the company. Therefore the said amount has been barred by limitation and hence the Official

Liquidator could not take any steps to file claim against the above debtor.

4. The company was incorporated in 1980 with authorised capital of Rs. 50 lakhs and invested capital of Rs. 20lakhs in the year 1980. Trial

production was started in the year 1983. The unit became financially unviable, in view of the fire in Cochin Port Trust which destroyed some

machineries which were imported and for various other reasons beyond the control of directors and the company was referred to B.I.F.R. and in

the year 1988, B.I.F.R. declared the unit as a sick unit and proposed liquidation. The B.I.F.R. appointed a special director when the company

when the company was declared as a sick unit. Two items of amount due to the company mentioned above were not barred at that time when the

matter was pending before the B.I.F.R. The special director appointed by the B.I.F.R. also did not take any action as the debts were written off

by the company as it was not feasible to get the amount returned. In the manufacturing and trading of the company, there will be some amounts

which may not be returnable. There is no allegation that the directors gave advances to themselves or their relatives. The amounts were due in bona

fide commercial transaction. The only allegation is that no case was filed before it was time-barred. With regard to the amount of Rs. 33,770.25

due from Silver Stone Trading Company, the Silver Stone Trading Company was an agent appointed by the company in Bombay unit which was

appointed for marketing company's products at Bombay. A consignment was sent. They paid an advance of Rs. 12,000/- and a promissory note

was taken for the balance amount. Balance amount was not paid. Earnest attempt was made by the then directors and officers for getting the

amount. A representative was sent from the company to Bombay. Lawyer notice was also issued to the above proprietary company. Owner of the

company fell ill. Wife of the proprietor requested for more time. That company also requested by letter dated 27.2.1986 asking for 35 days to

settle their liability as can be seen from Ext.R1 (e). The letter sent by the wife of the proprietor of that company is Ext.R1(f). The company sent

registered letters again. Again, lawyer notice was sent on 21.4.1987. These letters are proved by Exts.R1 (g) and (h). Acknowledgment card is

Ext.R1 (i). Therefore, earnest efforts were made by the directors. It is not an advance made. It is balance received amount of a consignment. It

was not practicable to recover the amount. On the facts of the case, there is no gross negligence on the part of the directors. Even though B.I.F.R.

appointed a special director, he also did not take any action as it was not feasible or viable to file a suit. It was already declared as a bad debt.

5. With regard to the amount of Rs. 11,413.54 due from M/s.Incos Marketing Services, Incos House also they had several transactions with them

and they were making payment. But, in the accounts, the balance due from them is Rs. 11,413.54. All attempts were made to get the amount, but,

finally, it was found that it is not possible to get the amount. It is also an amount of money to be received due to bona fide commercial transaction.

The consignment was sent after complying with the procedure fully. But, last transaction was on 10.2.1987. Since the company was not able to

send any further material due to shortage of production, there were no further transaction with them and they also changed their address and after

making various efforts, it was found that the above is not returnable and if money was spent for realising it will be a futile exercise and the company

will incur further loss. A company with an authorised capital of more than Rs. 50 lakhs and with a good turn over and when it was running, such

small amounts with regard to value of consignments may not be received, but, it cannot be stated that the directors were grossly negligent with

regard to these transactions. It is proved that due care and caution was taken by the directors and directors are not personally responsible for the

same as there is no material to hold that they together are responsible for the above as alleged in the charge sheet. These are transactions in the due

course of business and merely part of the value of the consignment was not able to be recovered, it cannot be stated that there is misfeasance.

Further, even after the matter was referred to B.I.F.R. and the B.I.F.R. appointed a technical director, he also did not take any proceedings for

getting these amounts. Merely because appellants are director board members they cannot be held liable. No specific allegation against any

individual director or manager was also raised. In these circumstances, it is not a fit case for taking action u/s 542 and 543(1) of the Companies

Act. Hence, we allow the appeals and the impugned order is set aside.