Sri Ramdas Motor Transport Ltd. And Ors vs Tadi Adhinarayana Reddy And Ors on 1 May, 1997

Equivalent citations: AIR 1997 SUPREME COURT 2189, 1997 (5) SCC 446, 1997 AIR SCW 2051, 1997 (3) COM LJ 35 SC, 1997 (4) SCALE 4, (1997) 3 COMLJ 35, (1997) 10 JT 667 (SC), (1997) 3 SCR 1160 (SC), (1997) 3 MAD LW 155, (1997) 25 CORLA 177, (1997) 5 SUPREME 29, (1997) 4 SCALE 4, (1997) 90 COMCAS 383, (1997) 2 SCJ 299

Author: Sujata V. Manohar

Bench: K.S. Paripoornan, Sujata V. Manohar

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           CASE NO.:
Appeal (civil)  3155 of 1997

PETITIONER:
SRI RAMDAS MOTOR TRANSPORT LTD. AND ORS.

RESPONDENT:
TADI ADHINARAYANA REDDY AND ORS.

DATE OF JUDGMENT: 01/05/1997

BENCH:
K.S. PARIPOORNAN & SUJATA V. MANOHAR

JUDGMENT:
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JUDGMENT 1997 (3) SCR 1160 The Judgment of the Court was delivered by MRS. SUJATA V. MANOHAR, J. Leave granted.

The first appellant company was established in 1944 as a private limited company under the Companies Act, 1913. It continued as a private limited company under the Companies Act, 1956. However, with effect from 1.2.1975, by virtue of Section 43-A of the Companies Act, 1956, it became a public limited company in view of the fact that the annual turn-over of the company was above the prescribed limit. The first appellant company, however, continues to be a closely held company consisting of only 61 shareholders including 11 employees and ex-employees, The second appellant is the Chairman and Managing Director of the first appellant company. The third appellant is the Joint Managing Director of the first appellant company. The main object of the company is to carry on the business of parcel lorry service, manufacture of automobile components and dealership of Telco.

It is the case of the appellants that there were disputes between the Managing Director i.e. second

appellant, and his son-in-law, Srihari Rao, who was a former Director of the first appellant company and a former Member of Parliament. The disputes started some time in 1993. In 1994, (according to the appellants, at the instigation of Srihari Rao) eight shareholders of the company filed before the Company Law Board, Principal Bench, New Delhi, a company petition being C.P. No. 7 of 1994 under Sections 397 and 398 of the Companies Act, 1956, on the ground of oppression of minority shareholders and mismanagement of the affairs of the company by the second and third appellants. In the said petition an injunction was sought to restrain the first appellant company from proceeding with the Rights Issue of its shares. After hearing both the parties, however, the Company Law Board declined to grant any interim order to this effect. The Company Law Board directed the company to file an affidavit with regard to the Rights Issue and to follow the procedure which it had followed earlier for the Rights Issue.

Thereafter, Srihari Rao and some others filed before the Company Law Board another Company Petition No. 15 of 1994 under Sections 397 and 398 of the Companies Act, 1956 on the ground of oppression of minority shareholders and mismanagement of the affairs of the company by the second and third appellants. This petition was filed on 7th April, 1994. An interim relief was sought from the Company Law Board for supercession of the Board of Directors of the first appellant-company and for re-constitution of the Board of Directors. An interim injunction was also sought against appellants 2 and 3 to restrain them from functioning as Managing Director and Joint Managing Director of the first appellant- company. The company petition was listed for hearing on 20th March, 1995. It was adjourned at the request of the petitioners therein and thereafter from time to time. The petitioners before the Company Law Board filed an application to receive evidence by affidavit. This application was rejected by the Company Law Board on 17th June, 1995. The main petition was thereafter heard from 16th of October 1995 onwards.

On 12th of January, 19% Shrihari Rao filed another company application for appointment of an administrator. During the hearing of this application, the petitioners in the said petition took further time for filing a better affidavit in support of their application and the application was adjourned to 4th December, 1996. The hearing of the main company petition was adjourned to May, 1997 at the instance of the petitioners therein. We have set out these facts as the grievance of the 1st respondent in his writ petition is : Company Law Board has failed to pass an order.

During the pendency of all these proceedings before the Company Law Board, on 5.10.1996 the 1st respondent filed a writ petition under Article 226 of the Constitution before the High Court of Andhra Pradesh for a writ of mandamus directing Union of India and the Secretary (Finance), Union of India (respondents 1 and 2 in the writ petition) to forthwith prosecute the present appellants 2 and 3 in accordance with law. The 1st respondent has challenged in the writ petition various transactions entered into by the first appellant company relating to purchases and sales. The 1st respondent has also challenged the correctness of the figures shown in the balance- sheet and profit and loss accounts of the first appellant-company. According to the 1st respondent there was misappropriation of the funds of the company by appellants 2 and 3. It was claimed by the first respondent that this amounts to misappropriation of public funds and that, for the alleged acts of appellants 2 and 3, the Union of India should be directed to prosecute appellants 2 and 3. There is a further prayer in the writ petition that the court should direct an inquiry by the Central Bureau of

Investigation into the alleged financial mismanagement of the company and misappropriation of funds by appellants 2 and 3; that a report should be submitted to the Court within four weeks pending the disposal of the writ petition; and on the basis of such report the Court should give further directions. There is also a prayer for the appointment of an interim administrator to take charge of the affairs of the first appellant-company. All these prayers relate to the alleged mismanagement of the affairs of the first appellant-company by appellants 2 and 3. In essence, the writ petition under Article 226 prays for an investigation into the affairs of the first appellant-company, and for action against appellants 2 and 3. The interim prayer for an administrator of the company also clearly shows that the main grievance of the first respondent in the writ petition relates to the manage-ment of the affairs of the first appellant-company.

The Companies Act, 1956 provides for dealing with such grievances against a company and its Board of Directors. Under Section 235 of the Companies Act, 1956 the Central Government may, where a report has been made by the Registrar under Section 234(6) or (7), appoint one or more competent persons as Inspectors to investigate the affairs of a company and to report thereon in such manner as the Central Government may direct. Section 234(6) requires the Registrar, in cases where he is of the view, on the basis of information or explanation furnished by the company, or on the basis of the books and papers produced, that the documents together with information and explanation disclose an unsatisfactory state of affairs, or do not disclose a full and fair statement of any matter to which the documents purport to relate, to report in writing the circumstances of the case to the Central Government. Sub-section 7 deals with the Registrar acting on the basis of material placed before him by any contributory or creditor or any other person interested in the business of the company. The Registrar, if he is satisfied that the business of the company is being carried on in fraud of its creditors or persons dealing with the company, or otherwise for a fraudulent or unlawful purpose, may, after giving an oppor-tunity of hearing to the company, by written order call upon the company to furnish in writing any information or explanation in connection with it. If he is satisfied that investigation is required, he may refer the case to the Central Government. Whereupon the Central Government could order an investigation under Section 235. The Central Government, therefore, will not readily order an investigation into the affairs of the company unless the Registrar makes a report as set out in Section 235(1) read with Section 234(6) and (7).

Under Section 235(2) a power is given to the Company Law Board in case where, inter alia an application is received from not less than 200 members, or members holding not less than 1710th of the total voting power in a company, to declare, after giving the parties an opportunity of being heard, that the affairs of the company ought to be investigated by an Inspector or Inspectors. On such a declaration being made, the Central Government shall appoint one or more competent persons as Inspectors to investigate the affairs of the company and to report thereon. The power, therefore, to appoint Inspector to investigate the affairs of a company has to be exercised by the Central Government after a proper preliminary scrutiny by the Registrar or by the Company Law Board as the case may be. It cannot be instituted simply on the basis of allegations made by one shareholder. Under Section 237, there is a further power given to the Central Government to appoint Inspectors to investigate the affairs of a company if the company, by a special resolution, or the court, by order declares that such investigation is necessary. Similarly, this may be done if in the opinion of the Company Law Board there are circumstances suggesting that the business of the

company is being conducted with intent to defraud its creditors, members or any other person or otherwise for a fraudulent or unlawful purpose or in a manner oppressive of any of its members or that the company was formed for any fraudulent or unlawful purpose. The Company Law Board may also come to a conclusion that there are circumstances suggesting that the persons concerned in the formation of the company or management of its affairs have been guilty of fraud, misfeasance or other misconduct towards the company or towards any of its members; or that the members of the company have not been given all the information with respect to its affairs which they might reasonably expect. In these circumstances, on the basis of the opinion so framed by the Company Law Board, the Central Government may order an investigation. Neither the Central Government nor the Company Law Board has been moved by the 1st respondent in accordance with law for this purpose. In the case of Rohtas Industries Ltd. v. S.D. Agarwal & Anr. [1969] 3 SCR 108 this Court examined the nature of the power conferred on the Central Government under Section 235 as well as 237(b) and held that the scheme of these sections makes it clear that unless proper grounds exist for investigation of the affairs of a company, such investigation will not be lightly undertaken. An investigation may seriously damage a company and should not be ordered without proper material gathered in the manner provided in the Companies Act. The power of investigation has been conferred on the Central Government on the faith that it will be exercised in a reasonable manner. The department of the Central Government which deals with companies is presumed to be an expert body in company law matters. Therefore, the standard that is prescribed under Section 237 (b) is not the standard required of an ordinary citizen but that of an expert.

In the present case no attempt has been made by the first respondent to get the affairs of the company investigated in the manner provided under the Companies Act. Neither the Central Government nor the Company Law Board has been moved by the 1st respondent in accordance with law for this purpose. Instead of moving the authorities prescribed under the Companies Act the first respondent has chosen to resort to the writ jurisdiction of the High Court for a direction to have the affairs of the company investigated by the C.B.I. Under Section 397 of the Companies Act any member of a company who complains that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members may apply to the Company Law Board for an order under that section. The Company Law Board has wide powers to make such orders as it may think fit to bring an end to the matters complained of. Some of the shareholders of the first appellant-company have, in fact, filed petitions under Sections 397 and 398 of the Companies Act before the Company Law Board in which they have asked for similar reliefs including the appointment of an interim administrator. The acts of mismanagement and oppression complained of are similar to those set out in the writ petition before the High Court. The only ground alleged in the writ petition for moving the High Court under Article 226 is that the Company Law Board is not moving in the matter under an excuse that the Company Law Board has not yet made an order, a shareholder cannot be allowed to bypass the express provisions of the Companies Act and move the High Court under Article 226. A shareholder has very effective remedies under the Companies Act for prevention of oppression and mismanagement. When such remedies are available, the High Court should not readily entertain a petition under Article 226.

Learned Single Judge before whom the present writ petition came up for hearing very rightly held that the Companies Act provides a forum to consider the grievances made out by the first

respondent in the writ petition. When such a forum, statutorily constituted, exists, it is but appropriate that resort to Article 226 should be discouraged There is an efficacious alternative remedy available under the statute. In fact under the Companies Act, a more satisfactory solution is available. The Single Judge was right in pointing out that some of the shareholders have initiated proceedings before the Company Law Board, The only grievance of the petitioner in the writ petition is that no orders have been passed thereon. The Single Judge has rightly held that such a grievance cannot constitute a ground for invoking the jurisdiction of the High Court under Article 226, He, therefore, dismissed the writ petition.

In appeal, however, the Division Bench of the Andhra Pradesh High Court presided over by the Chief Justice, entertained the appeal on the ground that the petition raised many serious issues as to falsification of the accounts of a public limited company. It said that the acts of the company would jeopardize public interest. Therefore, the petition involved wider "public interest" and should be entertained. In the result the Division Bench issued a direction to the Central Government to make its own verification of the allegations in the writ petition. In other words, the Division Bench of the High Court directed an investigation into the affairs of the company, bypassing the detailed provisions with inbuilt safeguards under the Companies Act, designed specially for this purpose. The only ground for intervention appears to be "public interest". We fail to see what public interest is involved in disputes of the kind referred to in the writ petition. They basically deal with mismanagement of the affairs of the company and oppression of the minority shareholders. The company in only a deemed public limited company. Its shareholding is very closely held. The only other factor referred to in the writ petition to invoke the doctrine of so called public interest, is the fact that the company had borrowed moneys from public institutions. This is no ground for not availing of the statutory remedies provided under the Companies Act before the appropriate statutory forums which are designed for this very purpose. We are distressed to find that the well-reasoned judgment of the Single Judge was interfered with in a casual manner. The impugned judgment rests on fragile foundations and reads more like an ipse dixit.

The appeal is allowed and the impugned judgment of the Division Bench of the Andhra Pradesh High Court is set aside. The first respondent shall pay to the appellants costs of the appeal quantified at Rs. 15,000.