SUPREME COURT OF INDIA

Pankaj Mehra

Vs.

State of Maharashtra

(K Thomas and A Misra JJ.)

15.02.2000

JUDGMENT

K.T. THOMAS, J.

1. Can a company escape from penal liability under Section 138 of the Negotiable Instruments Act (for short "the NI Act") on the premise that a petition for winding up of the company has been presented and was pending during the relevant time? A Division Bench of the Bombay High Court held that the company cannot avert its liability on the mere ground that such a petition was presented prior to the company being called upon by a notice to pay the amount of the cheque. By holding so, the Division Bench dismissed a batch of writ petitions filed by different companies challenging the criminal proceedings initiated against them in different criminal courts for the offence under Section 138 of the NI Act. We have now to deal with the same question in this batch of appeals filed by special leave.

2. Though different cases now before us have differing facts we are not bothering ourselves with such differences. The common features in all the appeals, which alone are relevant for dealing with the aforesaid question, can be culled out from one of the appeals. The company involved in the said sample appeal will be referred to as "the Company". The cheque which the company issued bore the date 30.10.1996 and the amount covered by the cheque was Rs. 5,72,432/-. (There is a contention that the cheque was actually drawn much before that date). When the cheque was presented for encashment the drawee bank dishonoured it on 26.12.1996. The payee of the cheque issued a notice to the Company on 21.12.1996 calling upon it to pay the amount. As the Company failed to pay the amount a complaint was filed before the magistrate on 29.1.1997 against the Company and two of its directors for the offence under Section 138 of the NI Act.

3. The magistrate who took cognizance of the offence issued process to all the accused. It was then that the accused challenged the criminal proceedings by means of a writ petition filed before the Bombay High Court, on the premise that a petition for winding up of the Company has been filed on 27.5.1996 before the court concerned and a Provisional Liquidator was appointed by that court two years later i.e. on 21.4.1998.

4. As the facts stated above were not substantially disputed the Division Bench of the High Court

proceeded to hear the writ petition along with the other writ petitions in the batch, on the limited question whether the Company can avert the penal liability on that premise. The main footing on which the Company resisted the prosecution was that under Section 536(2) of the Companies Act any disposition of the property of the Company shall be void if it was made after the commencement of winding up proceedings by the court. To bolster up the said ground the Company relied on Section 441(2) of the Companies Act which says that winding up of a company by the court shall be deemed to commence at the time of presentation of the petition for winding up. The Division Bench of the High Court noticed the common features in all the cases in the following sentences:

In all these matters, a petition for winding up had been filed either before the cheques were issued (in some cases) and (sic or) in any event before the period of 15 days, after receipt of notice, expired. Thus the question for consideration is whether merely by reason of a winding up petition being presented there was a bar or legal disability in making payment.

5. Learned Judges proceeded to consider the question on the aforesaid admitted premise and, therefore, examined the contention whether disposition of any property by the company would become "void" immediately on presentation of the petition for winding up, or it would become void only when an order of winding up has been passed, or at least when a provisional liquidator has been appointed. Section 536(2) of the Companies Act was sought to be interpreted in a wide dimension so as to render all transactions void merely because a petition for winding up was presented - whether or not it was succeeded by an order of winding up or appointment of a provisional liquidator. The Division Bench of the High Court repelled the said contention on the following reasoning:

If this argument is accepted, persons who purchased shares in the open market through the Stock Exchange without any knowledge of a petition for winding up having been presented, would also get affected as all such transactions would be void. Therefore, if this wide propositions were to be accepted then once a petition for winding up is presented, even without an order for winding up, there would be for all practical purposes closure of the company. All activities of the company would have to come to a standstill. If this were the law then unscrupulous parties could

blackmail/pressurise all companies to succumb to unjustified demands by merely threatening to or presenting petitions for winding up. Conversely unscrupulous companies could avoid payment/discharge of its (sic their) liabilities by having their own parties present bogus petitions for winding up. After one is dismissed another could be filed. In this manner, the company could avoid discharging its liabilities indefinitely if not permanently. If the law was that merely on the filing of a petition for winding up all dispositions were void, it would lead to absurd or catastrophic results. In our view that can never be the legal position.

6. It was then argued before the Division Bench that the words "in the winding up" appearing in Section 536(2) of the Companies Act, should mean "during winding up proceedings". Reliance was placed on the decision in Kamani Metallic Oxides Ltd. v. Kamani Tubes Ltd. (1984 Company Cases page 19) wherein it was held that the words "in the winding up" do not mean "after or upon the passing of the winding up order". Learned Judges of the Division Bench of the High Court pointed out the distinguishing context in the said case in which such a view was taken and then expressed the view that merely because a petition for winding up has been presented all transactions or dispositions undertaken during the period cannot become ab initio void. The following reasoning of

the Division Bench for repelling the said contention is worthy to be extracted:

If they were to be void ab initio i.e. immediately on their being entered into, then on the petition being withdrawn or dismissed, they would not revive. It is clear that if the petition is withdrawn or dismissed then the transactions would never have been void. This clearly shows that the transactions/dispositions are not void ab initio but become void on the passing of an order for winding up or on appointment of a Provisional Liquidator. What Section 536(2) read with Section 441(2) provides for is to convert what was otherwise valid into void by virtue of the legal fiction. Thus the voidness takes effect on the passing of the order of winding up or appointment of Provisional Liquidator. By virtue of the legal fiction, in Section 441(2), it then relates back to the date of presentation of the petition for winding up.

7. We will presently consider the effect of Section 536(2) of the Companies Act. The entire Section is quoted below:

Avoidance of transfers, etc., after commencement of winding up.- (1) In the case of a voluntary winding up, any transfer of shares in the company, not being a transfer made to or with the sanction of the liquidator, and any alteration in the status of the members of the company, made after the commencement of the winding up, shall be void.

(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.

8. Contextually Section 441(2) of the Companies Act is very relevant and hence that is also extracted here:

441. Commencement of winding up by Court.-Where, before the presentation of a petition for the winding up of a company by the court, a resolution has been passed by the company for voluntary winding up, the winding up of the company shall be deemed to have commenced at the time of the passing of the resolution, and unless the Court on proof of fraud or mistake, thinks fit to direct otherwise, all proceedings taken in the voluntary winding up shall be deemed to have been validly taken.

(2) In any other case, the winding up of a company by the Court shall be deemed to commence at the time of the presentation of the petition for the winding up.

9. Three modes of winding up have been prescribed in Part VII of the Companies Act, (vide Section 425). First is, winding up by the court, next is voluntary winding up and the third is winding up by subjecting to the supervision of the court.

10. We need not bother ourselves with the first sub-section of Section 536 of the Companies Act as it deals with a case of voluntarily winding up of the company, because none of the companies in the present batch of appeals is involved in such a contingency. Sub-section (2) deals with the other two types of winding up. Section 439 of the Companies Act contemplates an application to the court for the winding up of the company. It can be done by presenting a petition by any one of the persons enumerated in Sub-section (1) of Section 439. Such persons include, any creditor, including any

prospective creditor.

11. Once a petition for winding up is presented it is not a necessary concomitant that the winding up would follow. This position is made clear in Section 440(2) which says that "the court shall not make a winding up order on a petition presented to it under Sub-section (1), unless it is satisfied that the voluntary winding up or winding up subject to the supervision of the Court cannot be continued with due regard to the interests of the creditors or contributories or both."

12. So a judicial exercise is called for to reach the satisfaction of the court that winding up has to be continued with due regard to the interest of the creditors or the contributOrs. Section 443 of the Companies Act is important in this context. Sub-section (1) of that Section says that on hearing a petition for winding up the court may either (1) dismiss the petition or (2) make any interim order as it thinks fit or (3) make an order for a winding up. Sub-section (2) says that "where the petition is presented on the ground that it is just and equitable that the company should be wound up, the Court may refuse to make an order of winding up, if it is of opinion that some other remedy is available to the petitioners and that they are acting unreasonably in seeking to have the company wound up instead of pursuing that other remedy."

13. Two more provisions are relevant in this context. Section 450 says: "At any time after the presentation of a winding up petition and before the making of a winding up order, the Court may appoint the Official Liquidator to be liquidator provisionally". Before appointing a Provisional Liquidator the court has to give notice to the company and reasonable opportunity to make his representation. Section 449 enjoins that "on a winding up order being made in respect of a company the Official Liquidator shall, by virtue of his office, become the liquidator of the company."

14. In the above backdrop alone we can consider the impact of the legislative direction in Section 536(2) that any disposition of the property of the company made after the commencement of the winding up (i.e. after the presentation of a petition for winding up) shall be void. There are two important aspects here. First is that the word "void" need not automatically indicate that any disposition should be ab initio void. The legal implication of the word "void" need not necessarily be a stage of nullity in all contingencies. Black's Law Dictionary gives the meaning of the word "void" as having different nuances in different connotations. One of them is of course "null, or having no legal force or binding effect". And the other is "unable in law, to support the purpose for which it was intended". After referring to the nuances between void and voidable the Lexicographer pointed out the following:

The word 'void' in its strictest sense, means that which has no force and effect, is without legal efficacy, is incapable of being enforced by law, or has no legal or binding force, but frequently the word is used and construed as having the more liberal meaning of 'voidable'. The word 'void' is used in statutes in the sense of utterly void so as to be incapable of ratification, and also in the sense of voidable and resort must be had to the rules of construction in many cases to determine in which sense the Legislature intended to use it. An act or contract neither wrong in itself nor against public policy, which has been declared void by statute for the protection or benefit of a certain party, or class of parties, is voidable only.

15. For discerning the legislative idea in employing the word "void" in the context set out in Section 536(2) of the Companies Act the second aspect to be noticed is that the provision itself shows that the word void is not employed peremptorily since court has power to order otherwise. The words

"unless the court otherwise orders" are capable of diluting the rigor of the word "void" and to choose the alternative meaning attached to that word.

16. In Chittoor District Co-operative Marketing Society Ltd. v. Vegetols Ltd. and Ors. (1987 (Suppl.) SCC 167) a two Judge Bench of this Court considered a plea for validation of payments made by a company after presentation of a petition for winding up. One set of payments were made before the passing of the winding up order and the other set of payments were made thereafter. This Court declined to validate such payments on the ground that "there is no evidence to show that those payments were made either under compulsion of circumstances in order to save or protect the property of the company or that there was any commercial compulsion to enable it to run its business". The decision only indicates that such payments could have been made valid if evidence was adduced to show that there was compulsion of circumstances. In fact, this decision lends support to the interpretation that the payments which were made after the commencement of winding up proceedings, would not become ab initio void.

17. An early decision of a Division Bench of the Bombay High Court in Tulsidas Jasraj Parekh v. Industrial Bank of Western India (AIR 1931 Bombay 2) was sought to be relied on by most of the learned Counsel who argued for different appellant. The question which the Court considered therein pertained to Section 227(2) of the old Companies Act, 1913 which was identical to Section 536(2) of the present Act. Certain payments made by a company after commencement of the winding up proceedings were questioned and the Division Bench considered the scope of the sub-section and noticed that the principle had been borrowed from the English Companies Act. Hence some of the English authorities were also referred to by Marten C.J., who spoke for the Division Bench. Learned Judges stated thus:

Now here as regards Section 227(2) the Court has to steer a middle course between two extremes. On the one hand the words of the section are wide enough to include any sale or payment that a company may make after the date of the winding-up petition. On that basis any business would practically have to be stopped if a petition was presented, because it would be unsafe to dispose of any of the company's assets. For instance, a mill company might not be able to buy a ton of coal for the use of its furnaces, or, on the other hand, it might not be able to sell any of its goods in the ordinary course of business. Consequently, the Court has very properly laid down that, speaking generally, any bona fide transaction carried out and completed in the ordinary course of current business will be sanctioned by the Court under Section 227(2). On the other hand it will not allow the assets to be disposed of at the mere pleasure of the company, and thus cause the fundamental principle of equality amongst creditors to be violated. To do so would in effect be to add to the preferential debts enumerated in Section 230 a further category of all debts which the company might choose to pay wholly or in part.

18. It is useful to refer to the reasoning adopted by a Division Bench of the Gujarat High Court in Navjivan Mills Ltd., In re 1986 (59) Company Cases 201 in favour of adopting a pragmatic attitude when a Company Court was approached for approval of certain dispositions which a company made after presentation of a petition for winding-up. A clear distinction was drawn by the Division Bench between the period till the passing of the order for winding-up and thereafter, so far as dispositions are concerned. The following reasoning is useful for consideration of the issues involved:

The court can exercise the jurisdiction under Section 536(2) of the Companies Act, 1956, of giving directions validating proposed transactions pending a petition for winding up but before the winding

up order is made for the obvious reason that unless these transactions are saved from the consequence which may ensue, if at all, on an order of winding up being made, the company might find it difficult to keep itself going and its business might be paralysed. The purpose underlying the investment of the power in court is for the benefit and the interest of the company so as to ensure that a company which is made the subject of a winding-up petition may nevertheless obtain the money necessary for carrying out its business and so as to avoid its business being paralyzed. If that is the purpose and object of the section, it would hardly be proper and just to stultify the power and restrict its operation since otherwise it is bound to be counter-productive in the sense that the very purpose of keeping the company as a going concern so as to ensure the interest of the shareholders and creditors would be defeated.

19. In Re Grays Inn Construction Company Ltd. (1980 (1) All E. R. 814) the Court of Appeal (Civil Division) considered the principle on which discretion of the court to validate the dispositions of property made by a company, during the interregnum between presentation of a winding up petition and the passing of the order for winding up, has been dealt with. Section 227 of the English Companies Act, 1948 is almost the same as Section 536(2) of the Indian Companies Act. Dispositions which could be validated are mentioned in the decision. The said decision was cited before us in order to emphasis the point that courts would be very circumspect in the matter of validating the payments and the interest of the creditors as well as the company would be kept uppermost in consideration. Be that so, the said decision is not sufficient to support the contention that disposition during the interregnum would be irretrievably void.

20. It is difficult to lay down that all dispositions of property made by a company during the interregnum between the presentation of a petition for winding up and the passing of the order for winding up would be null and void. If such a view is taken the business of the company would be paralyzed, for, the company may have to deal with very many day-to-day transactions, make payments of salary to the staff and other employees and meet urgent contingencies. An interpretation which could lead to such a catastrophic situation should be averted. That apart, if any such view is adopted, a fraudulent company can deceive any bona fide person transacting business with the company by stage-managing a petition to be presented for winding up in order to defeat such bona fide customers. This consequence has been correctly voiced by the Division Bench in the impugned judgment.

21. If the payment is not ab initio void the company cannot contend that it is legally forbidden from making payment of the cheque amount when notice was issued by the payee regarding dishonour of the cheque. To circumvent this hurdle an endeavour was made by some of the appellants' counsel to show that the very issuance of a cheque would amount to disposition of property. We are unable to accept the said contention particularly in view of the definition of "cheque" in the Nl Act. "A Cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand."

22. Bill of exchange is "an instrument in writing containing an unconditional order, signed by the maker, directing certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument". The cheque, therefore, can be an order on the banker to pay the amount to the holder thereof and no disposition of property would take place until the payment is made by the banker pursuant thereto. At the most, drawing of a cheque can be considered as a step towards disposition of property, but that is insufficient to amount disposition of property.

23. It was next contended that since one of the conditions to constitute the offence of Section 138 of the Nl Act is that a cheque should have been drawn for the discharge of a legally enforceable "debt or other liability" no such cheque can possibly be conceived in a situation such as this because the creditor would be disabled from legally enforcing the debt with the commencement of winding up proceedings. Section 138 of the Nl Act, no doubt, contemplates only when the cheque is drawn by a person "for the discharge, in whole or in part, of any debt Or other liability". Explanation to Section 138 says that "for the purposes of this Section 'debt or other liability' means a legally enforceable debt or liability". Therefore, the first limb of the contention is forceful that for the offence under Section 138 the cheque should have been drawn for discharging a legally enforceable debt or other liability. But the second limb of the contention is tenuous as the debt would not cease to be legally enforceable merely because some body has filed a petition for winding up.

24. In this context a reference to Section 138 of the Nl Act is indispensable. It reads thus:

139. Presumption in favour of holder. - It shall be presumed, unless the contrary is proved, that the holder of a cheque received the cheque, of the nature referred to in Section 138 for the discharge, in whole or in part, of any debt or other liability.

25. Thus, when a cheque is received by a holder the court has to presume that (1) it is a cheque of the nature referred to in Section 138; and (2) such cheque was received for the discharge of a legally enforceable debt or liability. It is a legislative mandate that the court should proceed with the assumption that such cheque was received for the discharge of a legally enforceable debt or other liability until the drawer proves that it is not so. Learned Counsel contended that the burden of proof cast on the drawer of the cheque would stand discharged and the presumption would stand rebutted when it is shown that the company has been brought into winding up proceedings, as then no debt can be legally enforced against the company.

26. There is no provision in the Companies Act which prohibits enforcement of the debt due from a company. When a company goes into liquidation, enforcement of debt due from the company is only made subject to the conditions prescribed therein. But that does not mean that the debt has become unenforceable altogether. Perhaps due to want of sufficient assets for the company the realisation of a debt would be difficult. But that is no premise to hold that the debt is legally unenforceable. Enforceability of a debt is not to be tested on the touchstone of the modality or the procedure provided for its realisation or recovery. Hence the contention that the special provision incorporated in the Companies Act regarding the debts and liabilities due from the company will render the debt unenforceable, cannot be accepted.

27. The alternative approach is this: Even assuming that any disposition of the property made by a company after commencement of the winding up proceedings is null and void, how that is an escape ground from the offence under Section 138 of the Nl Act? That section created a statutory offence which on the confluence of the various factors enumerated therein, commencing with the drawing of the cheque and ending with the failure of the drawer of the cheque to pay the amount covered by it within the time stipulated, ripens into a penal liability.

28. The last factor for constituting the offence under Section 138 of the Nl Act is formulated in clause (C) of the proviso to the Section which reads thus: "the drawer of such cheque fails to make the payment of the said amount of money to the payee or as the case may be, to the holder in due

course of the cheque within fifteen days of the receipt of the said notice."

29. The words "the drawer of such cheque fails to make the payment" are ostensibly different from saying "the drawer refuses to make payment". Failure to make payment can be due to the reasons beyond the control of the drawer. An illustrative case is, if the drawer is not a company but individual who has become so pauper or so sick as he cannot raise the money to pay the demanded sum, can he contend that since failure to make payment was on account of such conditions he is entitled to be acquitted? The answer cannot be in the affirmative though the aforesaid conditions can be put forth while considering the question of sentence.

30. We therefore feel that legislature has thoughtfully used the word "fails" instead of other expressions as failure can be due to variety of reasons including his disability to pay. But the offence would be complete when the drawer "fails" to make payment within the stipulated time, whatever be the cause for such failure.

31. The drawer of the cheque can have different explanations for the failure to pay the amount covered by the cheque. But no such explanations would be sufficient to extricate him from the tentacles of the offence contemplated in the Section. Perhaps some kind of explanations would be sufficient to alleviate the rigor of the offence which may be useful to mitigate the quantum of sentence to be imposed. But that is no ground for consideration at this stage.

32. For all the above reasons, we are not inclined to interfere with impugned judgment of the Bombay High Court. However, learned Counsel who argued for one of the appellants in this batch of appeals (M/s. Atash Industries (India) Ltd.) pointed out that an observation made by the Division Bench in the impugned judgment would cause prejudice to that company when the case proceeds to the trial. We noticed that the following observation in paragraph 59 of the impugned judgment has the potency of creating a prejudice against them:

The conduct of Atash Industries (India) Limited in suppressing facts and obtaining orders from Courts without pointing out correct facts must be deprecated. In our view this conduct precludes the Company from getting any equitable reliefs.

33. We make it clear that the observation was made only for the Writ Petition pending in the High Court and that will not be counted against the said company during the remaining stages of trial.

34. All the appeals are accordingly dismissed.