

**IN THE COURT OF APPEAL OF THE DEMOCRATIC
SOCIALIST REPUBLIC OF SRI LANKA**

Attorney General,
Attorney General's Department,
Colombo 12.
1st Defendant-Appellant

CASE NO: CA/145/2000/F

DC COLOMBO CASE NO: 12945/M

Vs.

1. M.S.M. Najimudeen,
No. 22,
Maitland Crescent,
Colombo 7.
2. M.L. Fouz,
No. 42A,
Hastings Road,
Melbourne,
Victoria,
Australia.

1st and 2nd Plaintiff-Respondents

2. Fairdeal Industries (Pvt) Ltd.,
No. 862,
Negombo Road,
Keranga Pokuna,
Wattala.

3. Nagaraja Kanagaraja,
No. 862,
Negombo Road,
Keranga Pokuna,
Wattala.
4. Kanagaraja Annathurai,
No. 862,
Negombo Road,
Keranga Pokuna,
Wattala.

2nd-4th Defendant-Respondents

Before: Mahinda Samayawardhena, J.

Counsel: Vikum De Abrew, Senior D.S.G., with Indula Ratnayake for the 1st Defendant-Appellant.
Riad Ameen with Rushitha Rodrigo for the Plaintiffs-Respondents.

Decided on: 23.10.2019

Mahinda Samayawardhena, J.

The two plaintiffs filed this action in the District Court of Colombo naming four defendants, but seeking reliefs only against the 1st defendant, the Attorney-General, basically challenging the order of the Sri Lanka Customs made on 22.10.1992 whereby the textile material relevant to this case

was forfeited and a penalty of Rs. 10.8 million on the 2nd defendant company and Rs. 100,000 each on the 2nd plaintiff, the 3rd and 4th defendants as directors of the said company were imposed. The forfeiture of textile material has taken place and the penalties have been paid.

This order by the Customs has been made after due inquiry, in which, during the investigation period as well as at the customs inquiry, several prominent counsel have appeared for the alleged preparators.¹

This action has been filed in the District Court by the two plaintiffs as shareholders of the 2nd defendant company in the nature of a (Common Law) derivative action for and on behalf of the company on the basis that *“the 3rd and 4th defendants have acted in their own personal interest in respect of the subject matter of this action set out hereinafter causing wrongful loss to the 2nd defendant company and its shareholders including the plaintiffs.”*² In paragraph 6 they further state that *“the plaintiffs apprehend and have reason to apprehend that the 3rd and 4th defendants who constitute the majority in the Board of Directors and have been and are in control of the 2nd defendant company will not make any claim on behalf of the 2nd defendant company*

¹ During the investigation period of this customs inquiry, Mr. D.S. Wijesinghe, P.C. (vide page 443 of the brief), and during the customs inquiry, Mr. Prasanna Jayawardena, (I assume, presently, a Judge of the apex Court) (vide page 496 of the brief) have appeared. It has also been suggested to the 1st plaintiff that Mr. Ameen, P.C. also appeared for them, which has not been denied by the 1st plaintiff (vide page 361 of the brief).

² Paragraph 5 of the plaint at page 47 of the brief.

in respect of the subject matter of this action.”³ But this alleged apprehension, in the facts of this case, is a pretence.

At the trial, the 2nd plaintiff who paid the penalty did not give evidence, but the 1st plaintiff did give evidence. But, the 3rd defendant, the alleged wrongdoer, who caused wrongful loss to the company, gave evidence for the plaintiffs.

After trial, the District Judge has granted all the reliefs to the plaintiffs. They are basically that the forfeiture and penalty imposed are illegal, the textile material and the penalty paid shall be returned to the company.

Being dissatisfied with this Judgment, the 1st defendant has filed this appeal.

The pivotal argument of the learned Senior Deputy Solicitor General for the 1st defendant is that the plaintiffs have no *locus standi* to file this action. This matter had *inter alia* been raised in the District Court by way of issues, but the learned District Judge has answered it against the 1st defendant. In my view, the learned District Judge has erred on that threshold issue. If the plaintiffs do not pass that test, consideration of merits of the case does not arise.

Although the plaintiffs have not highlighted in the plaint, as the 1st plaintiff who gave evidence at the trial admitted, at all times material to this action, the 2nd plaintiff was not only a director of the 2nd defendant company, but also the majority shareholder

³ Paragraph 6 of the plaint at page 47 of the brief.

holding nearly 60% of the shares of the company.⁴ The 1st plaintiff, who is also a shareholder of the company holds 100 shares, and also a director of the company from 05.01.1994.⁵ The 1st and 2nd plaintiffs are very close relations⁶, and are living in the same address/place.⁷ The 1st plaintiff is the Power of Attorney holder of the 2nd plaintiff.⁸

At one time, in evidence, the 1st plaintiff has admitted that, being the majority shareholder, the 2nd plaintiff controlled the affairs of the company, but thereafter, changed it and stated that the 3rd and 4th minority shareholders controlled the company.⁹

Although the plaintiffs in the plaint state that the 3rd and 4th respondents caused wrongful loss to the company, no action has been taken against them by the 1st and/or the 2nd plaintiffs as majority shareholders/directors of the company. No meeting has been called in order to pass a resolution against alleged wrongful acts of the 3rd and 4th defendants.¹⁰ No attempt has been made by the plaintiffs who have the majority shareholding to remove the errant 3rd and 4th directors by an ordinary resolution at a General Meeting of the company and to appoint new directors. They were admittedly serving as directors of the company even

⁴ Page 344, 363 of the brief.

⁵ Pages 189-291, 428 of the brief.

⁶ Page 303 of the brief.

⁷ Page 365 of the brief.

⁸ Page 304 of the brief.

⁹ Page 345 of the brief.

¹⁰ Pages 363-364 of the brief.

at the time of the 1st plaintiff giving evidence without any hindrance whatsoever.¹¹

Notwithstanding the plaintiffs in the plaint state that the forfeiture and penalty are illegal, the 1st plaintiff knows nothing about the factual matters relating to the transaction in issue.¹² All what the 1st plaintiff says is that the forfeiture of textile material and imposing fines are illegal, and what the customs could have done was to impose custom levies and not fines. Had that been done, according to the 1st plaintiff, it was lawful.¹³ Ironically, the same position was taken by the 3rd defendant, who is the alleged culprit, in his evidence given as the plaintiffs' witness.¹⁴ If the penalty was recovered as custom levies, according to them, there is no wrongful loss to the company! How can that happen, I am unable to comprehend!

If that contention is taken at its best, the wrongful act has been done not by the 3rd and 4th defendants, but by the Sri Lanka Customs. In that backdrop, I cannot understand why the company cannot take action against the alleged wrongful acts done by Sri Lanka Customs.

This position of the plaintiffs, and the 3rd and 4th defendants (who are father and son respectively) cannot be believed in view of the fact that they were fully represented by eminent lawyers at the customs inquiry.

¹¹ Page 362 of the brief.

¹² Pages 388-393 of the brief.

¹³ Pages 320, 362, 363, 323-326 of the brief.

¹⁴ Page 450-451 of the brief.

The Sri Lanka Customs has raided the bonded ware house of the 2nd defendant company on 20.07.1990 for alleged violation of Customs Ordinance. The 1st plaintiff in his evidence stated that the 2nd plaintiff knew about that incident in 1990.¹⁵ The 2nd plaintiff did not contest the matter and after the customs inquiry paid the penalty of Rs. 100,000 imposed on him as a director of the company. It is not the position of the plaintiffs that the 3rd and/or 4th defendants paid the penalty for the 2nd plaintiff against the wishes of the 2nd plaintiff.

When the 1st plaintiff was asked why the plaintiffs and the 3rd and 4th defendants did not contest the matter, his answer was that it was due to “fear”.¹⁶ Same was stated by the 3rd defendant who was called by the plaintiffs to give evidence on behalf of the plaintiffs.¹⁷ The plaintiffs in their written submissions also state that *“Evidence was also adduced with regard to the undue pressure and/or harassment and/or duress brought upon the 4th and 5th defendant-respondents (should be 3rd and 4th defendants) by certain custom officers including Gamini Rajapakshe, who gave evidence leading to the payment of the purported forfeitures imposed through fear.”*

This purported fear/pressure/harassment/duress is unbelievable, I repeat, as they were, at that time, represented by eminent lawyers.

On the other hand, if the story of “fear” is correct, the 3rd and 4th defendants have not acted fraudulently to the detriment of the

¹⁵ Page 348 of the brief.

¹⁶ 320-322, 351-355, 402 of the brief.

¹⁷ Page 449 of the brief.

company. They could have got the company to file the action to get the order made by the Customs quashed. If that argument of the plaintiffs is correct, the foundation of the plaintiffs' action is wrong.

At this stage, it is interesting to note that, the 3rd defendant, in his evidence, in fact, admitted the violation of Customs Ordinance in regard to this particular transaction. He admitted that the 2nd defendant company was obliged to store the textile material, imported under a special scheme without the payment of duty, in the bonded warehouse, and send within the given time the finished products made from the said textile material to the foreign supplier, who is the owner of the said material, but it was not done.¹⁸

It is trite law that a company is a legal person separate from its shareholders who own it and directors who run it. Therefore, if a wrong is committed against a company, only the company can sue against the wrongdoers for redress. This fundamental principle is known as 'proper plaintiff' principle.¹⁹ However, one cannot assume wrongdoing directors in control of the company would bring an action in the name of the company alleging wrongdoing against themselves. Hence proper plaintiff principle cannot be an inflexible principle.²⁰ The right to derivative actions was developed as an exception to this proper plaintiff principle. Derivative action allows a shareholder to sue on behalf of the company if the company is unwilling to sue against

¹⁸ Pages 457-460 of the brief. Vide also pages 719-723 of the brief.

¹⁹ *Foss v. Harbottle* (1843) 2 Hare 46, *Gray v. Lewis* (1873) 8 Ch App 1035, *Burland v. Earle* [1902] AC 83 (PC)

²⁰ In *Foss v. Harbottle* four exceptions were identified.

the wrongdoers because wrongdoers are in control of the company.

Are the 3rd and 4th defendants wrongdoers? According to the 1st plaintiff who gave evidence on behalf of the plaintiffs, and according to the 3rd defendant who was called by the plaintiffs to give evidence in support of the case for the plaintiffs, the 3rd and 4th defendants are not wrongdoers who acted to the detriment of the company and its shareholders. The 3rd and 4th defendants fought their case to the maximum retaining best lawyers at the customs inquiry and paid the penalty. At best, the 3rd and 4th defendants agreed to pay the penalty in fear of death threats. That does not amount to committing a fraud or wrongdoing by the 3rd and 4th defendants to the detriment of the company, which entitles the plaintiffs to sue the 1st defendant on behalf of the company.

On the other hand, if the 3rd and 4th defendants committed a wrongdoing against the company, why no reliefs are sought against them?

Are the 3rd and 4th defendants in control of the company? In the facts and circumstances of this case, it is not possible. They are in the minority. The majority shareholders are the plaintiffs.

The fact that the plaintiffs called the 3rd defendant to give evidence for the plaintiffs present ample testimony that the plaintiffs' action is misconceived in law.

In view of that conclusion, consideration of merits of the case does not arise.

For the aforesaid reasons, I answer issue No. 10 on *locus standi* of the plaintiffs to file this action in favour of the 1st defendant-appellant, and set aside the Judgment of the District Court, and allow the appeal with costs.

Judge of the Court of Appeal