

(1968) 10 KL CK 0014

In the High Court Of Kerala

Case No : A.S. No's. 105, 124, 125, 133, 134, 137, 139 and 140 of 1963 and 426 of 1964

In Re: Popular Bank Ltd. (In Liquidation)

Date of Decision : 29-10-1968

Acts Referred:

Companies Act, 1956 — Section 542

Citation : AIR 1970 Ker 120

Hon'ble Judges : V.P. Gopalan Nambiar, J; V. Balakrishna Eradi, J

Bench : Division Bench

Advocate : K.V. Suryanarayana Iyer, C.M. Devan, N.N. Venkitachalam, C. Ravi Namboodiri and C.K. Balan, in A.S. Nos. 137, 139 and 140 of 1963, V. Rama Sehnoi and R. Raya Shenoi, in A.S. No. 105 of 1963, S. Narayanan Potti, in A.S. Nos. 124 and 125 of 1963, P.C. Chacko, in A.S. No. 133 of 1963, T.N. Subramonia Iyer, P.C. Chacko and P. Krishnamoorthy, in A.S. No. 134 of 1963 and C.C. Sivasankara Panicker, P.G.P. Panicker and K.S. Parameswara Iyer, in A.S. No. 426 of 1964, for the Appellant; P.C. Chacko, in A.S. No. 426 of 1964 and Mani J. Meenattoor, for the Respondent

Final Decision : Dismissed

Judgement

Gopalan Nambiar, J.—The Popular Bank Ltd., now in liquidation, was incorporated in 1944 with head office in Alleppey. It established three branch offices at Vaikom, Shertalai and Kuthiathode respectively. The bank suspended business on the 16th August, 1956. A petition for winding up the bank was presented in this court and was ordered on the 19th December, 1956. Thereafter, two applications were made by the official liquidator of the bank. Application No. 1 of 1959, from which these appeals arise, was u/s 542(1) of the Companies Act, 1956, read with Rules 260 to 262 of the Companies (Court) Rules, 1959. Application No. 2 of 1959, from which the connected appeals heard along with these arise, was u/s 543 of the Companies Act, read with Section 45H of the Banking Companies Act, 1949. These were disposed of by our learned brother, Raghavan J.

2. Except where expressly indicated, reference hereinafter would be to the ranks of the parties as in Application No. 1 of 1959 which appears to have been treated

as the main application by the learned judge, and a copy of the judgment in which was ordered to be appended to the judgment in Application No. 2 of 1959. Respondents Nos. 1 to 8 and the deceased Damodara Pai were the directors of the Popular Bank Ltd. Of these, respondents Nos. 1 and 8 were in Trivandrum and the rest were in Alleppey. The 1st respondent was the chairman of the board of directors. The 9th respondent was appointed general manager of the bank on November 21, 1955, in pursuance of a resolution dated November 10, 1955. The 10th respondent was the manager of the bank from its inception till the appointment of the 9th respondent, after which he was made to work as secretary under the 9th respondent. The 11th respondent was a clerk under the 10th respondent. The 8th respondent is the son-in-law of the 1st respondent; the 5th respondent is the brother-in-law of the 1st respondent being the 1st respondent's wife's brother.

3. The learned trial judge, Raghavan J., found that the business of the bank was carried on with intent to defraud the creditors of the banking company, and, at any rate, for other fraudulent purposes as contemplated by Section 542(1) of the Companies Act, that respondents Nos. 1 to 8 and 10 and 11 were knowingly parties to the carrying on of the said business in the manner aforesaid, and that the 9th respondent was not a knowing party to such carrying on of the business. He further held that respondents Nos. 1 to 8 and 10 were personally liable without any limitation of liability for the debts of the company. The learned judge found that the Popular Bank is an insolvent company and the deficiency in its assets to pay the creditors in full is Rs. 6,50,000. He directed that the liquidator may sell by public auction or otherwise the assets belonging to the company which are considered unrealisable and that the amounts realised will be applied in reduction of the decree amount and in proportionate reduction of the liability of the directors as settled by the decree. Subject as above the learned judge found respondents Nos. 10 and 11 jointly and severally liable for the entire amount of Rs. 6,50,000. This was apportioned between the various respondents as follows :

The 3rd respondent was found liable for a sum of Rs. 2,00,000. Respondents Nos. 1, 4, 5 and 7 were made liable for a sum of Rs. 75,000 each, and respondents Nos. 2, 6 and 8 were held liable for a sum of Rs. 50,000 each. The liquidator was held entitled to his costs from the respondents in proportion to their liabilities.

4. Respondents Nos. 1, 6 and 8 through a common counsel have preferred A. S. Nos. 140 of 1963, 137 of 1963 and 139 of 1963 respectively, against the order. A.S. No. 105 of 1963 is by the 7th respondent; A.S. No. 125 of 1963 and A.S. No. 124 of 1963 are respectively by respondents Nos. 4 and 5 ; A.S. No. 133 of 1963 is by the 2nd respondent; and A.S. No. 134 of 1963 is by the 3rd respondent. A.S. No. 426 of 1964 is by the present Joint Commercial Tax Officer, Tirunelveli, who is not a party to Application No. 1 of 1959, but who feels aggrieved by certain directions made by the learned judge, and who has filed the

appeal with the leave of the court. A.S. No. 426 of 1964 is dealt with separately at the end of this judgment, and all the other appeals by the directors are treated together.

5. No appeals were preferred by respondents Nos. 10 and 11. The 10th respondent did not file any defence and was examined as P.W. 22, on the side of the liquidator. The whereabouts of the 11th respondent were unknown and substituted service was ordered and effected on him.

6. The official liquidator has accepted the order of the learned judge and has not filed any appeal, nor any memorandum of cross-objections. In each of the appeals preferred by the various respondents, the official liquidator alone has been made a party. In A.S. No. 426 of 1964, in addition to the official liquidator, the 3rd respondent is also a party.

7. The 1st respondent and the 6th respondent died subsequent to the order of the learned judge and after the filing of the appeal their legal representatives have been impleaded. After arguments in these appeals and the connected appeals against Application No. 2 of 1959 were closed on July 4, 1968, and judgment was reserved, the 3rd respondent died on July 10, 1968, C.M.P. No. 7081 of 1968 was filed on July 16, 1968, to declare the proceedings initiated by the liquidator as having ended with the death of the 3rd respondent as far as he is concerned, and to record that the claim against him had abated. On this petition the appeals were reposted and arguments on the matter raised by the petition alone were heard on July 25, 1968. At the request of counsel the matter was adjourned to July 31, 1968, and after further submissions and arguments on the C.M. P., orders thereon were reserved.

8. We shall proceed to consider at the outset certain preliminary questions, generally affecting all the appeals, and which, do not depend on the facts. It was contended that Section 542 of the Companies Act, 1956, introduced for the first time on and from April 1, 1956, cannot be given retrospective operation so as to permit of an enquiry into the fraudulent trading of the company or the fraudulent acts of its directors during a period prior to the coming into force of the section. The argument seems to us to proceed from a misunderstanding of the provisions of the section and the rule of retrospectivity. Section 542 of the Act reads :

" 542. (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 court, 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 in 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 court 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 court 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 court 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 on his behalf, or any person claiming as assignee from or through the person liable or any person acting on his behalf.

(c) The court 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 five 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. "

9. We are clear that in order to attract Sub-section (1) of Section 542 it is enough, if, as stated therein, it "appears " that any business of the company has been carried on with the requisite intent or for the requisite purpose mentioned in the sub-section. Once it is so made to "appear" in the course of winding up of a company subsequent to April 1, 1956, to make the facts and circumstances prior to that date the foundation of the proceeding or order," does not amount to giving retrospective operation to the section. Conduct in the past is made the cause or the reason for the action subsequent to April 1, 1956. We may contrast the expression " has been " used in relation to carrying on of the business of the company in subsection (1) of Section 542 with the expression "is" occurring in Sub-section (3) thereof.

10. The ambit of the liability sketched by the section was next debated before us. The section has been copied from Section 275 of the English Companies Act, 1929, corresponding to Section 332 of the English Act, 1948. It has its parallel in Section 281 of the Western Australia Companies Act of 1943. There was no

similar provision in the Indian Act of 1913,

11. Our attention was called to the decision in *In re William C. Leitch Brothers Ltd.* [1933] 3 Comp. Cas. 97 KER : [1932] 2 Ch. 71. and *In re Patrick and Lyon Ltd.* [1933] Ch. 786 : [1933] 3 Comp. Cas. 449 KER, rendered with respect to the provision of the English Act and to *Hardie v. Hanson*, 105 Commonwealth Law Reports 451, rendered with respect to the Australian section. The section appears to make the directors liable in disregard of the principles of limited liability. It leaves the court with a discretion to make a declaration of liability, in relation to " all or any of the debts or other liabilities of the company ". The English case, *William C. Leitch Brothers Ltd.*, *In re*, itself recognises that the order would, in general, be limited to the amount of the debts of those creditors proved to have been defrauded by the acts of the directors in question. In the Australian decision Dixon C.J. more explicitly stated the position thus :

"To me it seems difficult to suppose that it was intended that the court should, in exercising this power of direction go outside the debts and liabilities, the existence of which was in some way attributable to the carrying on of the business with the requisite intent to defraud."

12. According to the above view the section seems to postulate some nexus between the fraudulent trading or purpose and the extent of the liability of the directors or other persons.

13. In the English case, *In re William C. Leitch Brothers Ltd.* [1958] 28 Comp. Cas. 246; AIR 1958 Mad. 583, Maugham J, laid down the dictum that:

"if a company continues to carry on business and to incur debts at a time when there is to the knowledge of the directors no reasonable prospect of the creditors ever receiving payment of those debts, it is, in general, a proper inference that the company is carrying on business with intent to defraud."

14. It was argued before us that the proposition in the above terms has been stated too widely, and that it has been dissented from in the Australian case. Neither of these submissions is justified. The proposition in the English case has been put guardedly. It is one of proof or evidence, not of substantive law. Even so, it is one of inference regarded as proper, generally, and not universally. In the Australian case Dixon C.J. said nothing against the dictum. Kitto J. stated that the generalisation ought not to be sustained as a valid starting point for consideration of the evidence arising under the section. But the learned judge did not proceed to elaborate why it should not, at least generally, be so treated. Menzies J., the third learned judge in the Australian case, with whose reasons Dixon C.J. concurred, said nothing about the dictum of Maugham J. We see nothing in the Australian case to whittle down the dictum of Maugham J. in the English case. As an exposition of the parent section from which our provision has been copied, we feel, it is entitled to respect. We further feel that it lays down a safe working rule to go by, in applying the provisions of the section. We shall here deal with the objection raised by the counsel for the 3rd respondent--the

appellant in A. S. No. 134/1963--that the proceedings initiated by the official liquidator u/s 542 of the Companies Act terminate and abate with the death of the 3rd respondent. It has been recognised in a number of authorities that proceedings u/s 235 of the Indian Companies Act, 1913 (corresponding to Section 543 of the Act of (1) [1932] 2 Ch. 71 : [1933] 3 Comp. Cas. 97, terminate with the death of the person sought to be proceeded against and cannot be continued against his legal representatives. It is enough to refer to the decision in *In re Peer dan Juharmal Bank Ltd.* [1958] 28 Comp. Cas. 246 : AIR 1958 Mad. 583, where previous decisions have been reviewed. It was accepted before us that the same principle applies to proceedings u/s 542. The decisions to which our attention was drawn were all cases where the proceedings had not crystallised into an order or decree against the delinquent party. Once this has happened, as in the present case, and the delinquent party dies thereafter, it appears to us that his liability under the decree or order cannot stand automatically vacated. Abatement, if at all, in such circumstances, can only be of the proceedings by way of appeal, but not of the original proceedings, which have merged in the decree or order. The distinction in this respect has been clearly pointed out by Mulla in his 13th edition of the CPC (see volume 2, page 1231).

15. Besides, the death of the 3rd respondent occurred on July 10, 1968, after the hearing was concluded and judgment was reserved on July 4, 1968. Such a situation is provided for in Order 22, rule 6, of the Civil Procedure Code, which reads as follows :

" Notwithstanding anything contained in the foregoing rules, whether the cause of action survives or not, there shall be no abatement by reason of the death of either party between the conclusion of the hearing and the pronouncing of the judgment, but judgment may in such case be pronounced notwithstanding the death and shall have the same force and effect as if it had been pronounced before the death took place."

16. We entertain no doubt that the above provision is applicable to these proceedings by reason of Section 488 of the Companies Act read with rule 8 of the Companies (Court) Rules, 1959, and rule 44 of the Rules framed by the Travancore-Cochin High Court under the Banking Regulation Act, 1949. The result is that our judgment in the appeal preferred by the 3rd respondent would have the same force and effect as if it had been pronounced before the death of the 3rd respondent. But to say this is not to state that, should any re-investigation into the liability of the 3rd respondent become necessary by reason of any order of remand, the proceedings to the extent remanded would still be open. It was admitted before us that in such a case, the proceedings, to that extent, would lapse as against the deceased respondent.

17. Before leaving this aspect of the case, we wish to record that, although respondents Nos. 1 and 6 are in the same position as the 3rd respondent, no arguments were addressed on their behalf at any time, that the proceedings

initiated by the official liquidator would stand terminated by their death, pending appeal, and after the decree or order passed against them by the learned trial judge. On the other hand, they were strenuously seeking to get rid of the liability imposed on them by the decree or order under appeal.

18. We may also observe that, as a petition, C.M.P. No. 7081 of 1968 can have no legal existence, as it purports to have been filed by a party who is dead. We have dealt with it as a memo intimating to us the death of the 3rd respondent.

19. We may then note the argument advanced by some of the counsel that, unless the persons sought to be proceeded against u/s 542 of the Act had the "primary" intent to defraud creditors, liability u/s 542 would not be attracted. We are unable to see any warrant for introducing this refinement into the terms of the section. The section speaks of the business of the company having been carried on "with intent to defraud creditors of the company, or for any fraudulent purpose". If, on an assessment of all the facts and circumstances, the fraudulent intent or the fraudulent purpose is made out, liability must follow, as much as a contrary conclusion should result, if neither the intent nor the purpose could be said to be fraudulent.

20. We have so far cleared some of the general arguments addressed to us and the particular argument addressed in A. S. No. 133 of 1963. We may now get down to brass tacks and proceed to deal with the concrete facts and details of the various claims against the respondents. In doing so, we may conveniently refer to a few land-marks in the history and management of the bank. From the inception of the bank in 1944 there was in existence an executive committee to sanction loans, etc., in the bank. Some of the powers of the board of directors had been delegated to the committee. In 1951, there was an intimation or advice by the Reserve Bank that the advances of the bank showed an over-extended position. The directors of the bank would disclaim knowledge of this directive or advice from the Reserve Bank (except after seeing the later inspection report of the Reserve Bank in 1954), and there is no clear evidence that they had been apprised of it, although it is highly probable that they were. On September 6, 1953, the executive committee was reconstituted with respondents Nos. 4, 5 and 7 as its members. By proceedings of the board of directors of the same date, the manager was directed to call a meeting of the committee at least once a month and act only on its orders in all matters of advances and credits (vide exhibit P-58). Some time in January, 1954, there was an inspection of the bank by the Reserve Bank and the inspection report (exhibit P-62) was received in the bank in May, 1954, and placed before the executive committee in July of the same year. One of the points made in the inspection report was that the board of directors did not appear to have sufficiently interested itself in the working of the bank and, although it had constituted committees from time to time for the purpose of sanctioning and reviewing the advances, these committees did not function properly. Nor did the Board either define the powers of the manager or review the advances granted at his discretion. The report also pointed out that

the head office did not obtain periodical statements from the branches regarding full particulars of advances outstanding in the names of individual borrowers such as the nature and value of the securities, the worth of the parties, etc. On August 20, 1954, the post of a separate agent was sanctioned for the Alleppey office and the 11th respondent was appointed to the post to enable the manager to concentrate on the recovery of monies advanced. On December 26, 1954, one of the members of the executive committee (4th respondent) was appointed supervisory director and his written consent had to be taken in all urgent cases where it was difficult to get at the members of the executive committee. This step was consequent on the discovery of a few transgressions of the directions of the executive committee. On August 20, 1955, when the cash position of the bank became acute, the 10th respondent reported the same to the directors. They called for a report from the 10th respondent, and certain changes in the organisational set up of the bank followed (consequent on the admission of their irregularities by the 10th and 11th respondents), resulting in the demotion of the 10th and 11th respondents and the appointment of the 9th respondent as general manager by a resolution of the board dated November 10, 1955. On the same date, the executive committee was re-constituted to consist of respondents Nos. 2, 4 and 5. These will be referred to in detail later.

21. We shall next refer to certain orders passed in the course of these proceedings. By order dated June 13, 1955, public examination of respondents Nos. 10, 11 and another was directed by Raman Nayar J. Exhibits P-55 and P-71 are certified copies of the depositions of respondents Nos. 10 and 11 in public examination. After their examination, on the further report of the official liquidator for public examination of respondents Nos. 1 to 9, the learned judge by order on C.M.P. No. 113 of 1958 dated October 19, 1959, directed their public examinations. Appeals against the said judgment were allowed by a Division Bench, [1960] 30 Comp. Cas. 501, Madhava Naik and Others Vs. Popular Bank Ltd., Alleppey, of this court, on the ground that the order for public examination was, in the circumstances, violative of Article 20(3) of the Constitution. Further appeals--C.As. Nos. 603 to 608 of 1961, Offi. Liq., Official Liquidator, Popular Bank Ltd. Vs. Madhava Naik and Others, --were preferred by the liquidator and these were allowed by the Supreme Court by its judgment dated August 17, 1964, restoring the order of Raman Nayar J. By that time, applications Nos. 1 and 2 of 1959 had been heard and disposed of on the merits by the learned trial judge. The liquidator then filed statements in these applications that the order for public examination restored by the Supreme Court would be availed of, if necessary, in the event of any possible remand by any order passed in the appeals preferred.

22. With the background thus sketched, we may proceed to examine the various heads of claim made by the official liquidator against the respondents. After formulating the points for determination, the learned judge set down nine heads under which counsel for the liquidator had arranged and presented his case. We shall refer to these heads of claim as noticed by the learned judge, and with

respect to which arguments were advanced before us.

23. The FIRST HEAD of claim relates to withdrawal by the bank of several amounts from its accounts with other banks without accounting for them in the books of the bank, and misappropriation of these amounts by the officers of the bank. Schedule III of the points of claim gives details of 18 items of such withdrawals totalling, in all, Rs. 1,60,500. The withdrawals range from 3rd August, 1954, to 22nd July, 1955. That the monies were thus withdrawn and were not brought into the accounts of the bank was not disputed either before the learned trial judge or before us. The points stressed on this aspect of the claim were that the directors had no knowledge of these withdrawals and misappropriations; and, assuming they had, as the liquidator's specific case was that the directors had such knowledge only in 1955, and as the trial judge himself found such knowledge only from 1955, they cannot be saddled with liability for the entire claim. As this defence is common to this, and to the third, fourth and fifth heads of claim, we shall discuss the same after noticing the said heads.

24. The SECOND HEAD of claim relates to misappropriation of a sum of Rs. 10,000 being the fixed deposit amount of Sri N. Narayanaswamy, the uncle of the 9th respondent. The learned trial judge found that this amount received on 19th June, 1955, was not brought into the accounts of the bank when received, and that it was misappropriated and was credited only on 2nd September, 1955. The said Narayanaswamy has now proved his claim for the amount as a creditor of the bank. The learned judge held in the judgment in the connected Application No. 2 of 1959 that the misappropriation of this amount " probably.....may not be the direct result of the misfeasance of the directors ". Our finding to be noticed presently, regarding the requisite knowledge of the directors, cannot make them liable for the misappropriation of the amount when received on June 19, 1955. Taken along with the learned judge's finding on this aspect of the claim in the connected Application No. 2 of 1959, we feel we shall not be justified in finding the directors liable on this head of claim. We hold accordingly.

25. The THIRD, FOURTH and FIFTH HEADS relate respectively to: (1) misappropriations by manipulating the bills purchased and negotiated accounts and profit and loss accounts of the bank ; (2) concealment of those misappropriations by false and fictitious entries made in the books of the bank by respondents Nos. 10 and 11 with the knowledge and approval of respondents Nos. 1 to 8, showing the amounts involved as advances to different customers; and (3) the ratification of the fictitious advances by the board of directors at their meeting held on 10th November, 1955. The misappropriations and manipulations complained of are admitted. The defence to these heads of claim is also identical with that noticed under the first head, viz., that the directors had no knowledge about the misappropriations or manipulations or about the fictitious nature of the advances, and, in any event, such knowledge cannot be predicated throughout the entire gamut of the claim. A list of bills entered in the bills negotiated

accounts of the company and in respect of which no bills appear to have been actually negotiated was furnished in schedule II attached to the points of claim. The period covered by these bills ranges from August 17, 1954, to November 19, 1955, and the total amount covered is Rs. 2,64,700. A list of the entries of fictitious advances has been given in schedule I of the points of claim. The period ranges from 13th August, 1955, to 5th September, 1955, and the claim aggregates to Rs. 1,99,000. Schedule III and the extent of liability and the period covered by the same have already been referred to under the first head of claim.

26. We shall now consider the defence of the directors to heads 1, 3, 4 and 5. They disclaim knowledge of the misappropriations, falsification of accounts, etc., till after C.M.P. No. 113 of 1958 (exhibit P-74) was moved by the liquidator for their public examination. We have referred to the Reserve Bank's intimation in 1951, and also to its report after inspection in January, 1954, of which the directors had clear knowledge by July, 1954. We have also referred to a few transgressions of the directions of the executive committee which, admittedly, led to the appointment of the 4th respondent as a supervisory director on December 26, 1954. Against this background we may refer to the evidence of P.Ws. Nos. 1 to 3 and P. Ws. Nos. 13 to 16 and 22 to which our attention was called by the counsel for the liquidator.

[Their Lordships referred to the evidence and proceeded].

27. We have given the gist of the relevant evidence of P. Ws. Nos. 1 to 3, 13 to 16 and 22. It was pressed before us that their evidence is unacceptable and has not been accepted by the learned trial judge. Giving the matter our careful attention, neither of these submissions appeal to us. The learned trial judge referred to the evidence of P. Ws. Nos. 1 to 3 and 13 to 16 at page 14 of the judgment in Application No. I of 1959 in the printed book supplied to us. Discussing the question of the knowledge of the directors the learned judge observed :

" The learned advocates for the directors vehemently attack the evidence of P. Ws. 1 to 3, besides, of course, attacking the evidence of P. W. 22. P. Ws. Nos. 1 and 2 were employees of the Kuthiathode branch and P. W. 3 was a clerk in the Shertallai branch. If the evidence on this question was only the evidence furnished by these witnesses, probably I would have agreed with the contention of the directors. P. Ws. Nos. 13 to 16 may by themselves also be not quite believable. But there are several circumstances in the case driving me to the conclusion that respondents Nos. 1 to 8 must have known the real situation regarding the entries in schedule 1..... .. "

28. However, on page 24 of the same judgment the learned judge recorded:

" I place respondents Nos. 1, 4, 5 and 7 who were the chairmen of the board of directors and members of the executive committee respectively, and who were also present when some of the hundi forms and promissory notes were taken to

manipulate the accounts of the bank, on a par and direct them to pay Rs. 75,000 each..... "

29. These observations of the learned judge seem to us to indicate that the learned judge was accepting the evidence of P. Ws. Nos. 13 to 16 who spoke to the presence of the directors at the time of the execution of the hundi forms and promissory notes, taken to manipulate the accounts of the bank. The learned judge in more than one place freely referred to the evidence of P. Ws. Nos. 1 to 3, and notwithstanding his awareness which we also share that P. W. No. 22's evidence had to be viewed with caution, he did not reject it.

30. Besides, we have carefully scanned the evidence of these witnesses. We find no cross-examination worth the name on the side of the directors to discredit the testimony of P. Ws. Nos. 1 to 3 regarding the information conveyed in July, 1955, to the 4th respondent of the defalcations and the irregularities in the bank, and the subsequent meetings of the directors at the residence of the 4th respondent. P. W. No. 1 was not cross-examined about his presence, as stated, at most of these meetings. Nor have any reasons been made out before us to discredit the evidence of P. Ws. Nos. 13 to 16. There is hardly any cross-examination of these witnesses in regard to the part attributed by them to the directors in obtaining the bills, cheques and pronotes from them in the manner spoken to. The evidence of P. Ws. Nos. 1 to 3 (that of P. W. No. 3 in particular) fix the directors with the knowledge of the irregularities and defalcations in the bank on the last Friday in July, 1955 (July 29, 1955). The evidence of P. Ws. Nos. 13 to 16 would show that the directors, with the knowledge of the fictitious nature of the advances and borrowings, suffered entries to be made in the books of the bank and were parties to the manipulations therein. The evidence of P. W. No. 22 lends support to the evidence of these witnesses and we see no reason to reject it. On a review of the evidence of these witnesses we are satisfied that the directors had knowledge of the defalcations and irregularities committed by respondents Nos. 10 and 11 at least on the last Friday in July, 1955, and that they were parties to covering up the defalcations by causing false entries to be made in the books of the bank.

31. We shall then consider the case regarding the ratification of the advances specified in exhibit P-61 at the meeting of the board of directors held on November 10, 1955. It is undisputed that on August 20, 1955, the 10th respondent reported to the directors acute cash shortage in the bank. By the board's resolution on August 31, 1955, the 10th respondent was asked to report on the cause for the stringency. On September 14, 1955, an office order was issued by the 10th respondent calling upon the 11th respondent to explain why certain specified advances were made by him without proper authority, and why disciplinary action should not be taken against him for having done so (vide exhibit P-59). On the evidence of P. Ws. Nos. 1 to 3, and 22, which we accept, we entertain no doubt that the resolution of August 31, 1955, was in pursuance of the directors having been alerted about the irregularities and defalcations in

the bank, as spoken to by these witnesses and not merely on the report made on August 20, 1955, about the stringency. Exhibit P-59 was submitted to the board of directors on November 10, 1955, with an explanation of the same date appended to it by the 11th respondent, in which the 11th respondent admitted the charge against him. On the same day, the 10th respondent submitted a detailed report (exhibit P-60) to the board as to the cause for the stringency of funds in the bank and the steps to be taken to ease the situation. The report referred to the unauthorised advances. The explanation of the 11th respondent appended at the foot of exhibit P-59, and the report of the 10th respondent were nothing but unabashed confessions of their culpability. The board of directors in its resolution dated November 10, 1955, fretted and fumed at the conduct of respondents Nos. 10 and 11, demoted the 10th respondent, cancelled the powers of attorney of the 10th and 11th respondents, and docked the emoluments of both. Even before the board's resolution of August 31, 1955, calling for a report on the stringency, we find from the minutes of the proceedings of the executive committee (exhibit P-63), that the matter of some unauthorised advances had been engaging its attention, at least from December 25, 1954. On that day, the 10th respondent was asked to submit his explanation in respect of a series of unauthorised advances made by him. His explanation was considered at the subsequent meeting of the executive committee on February 13, 1955, and a decision thereon was postponed to the next meeting. The explanation was further discussed at the next meeting on June 11, 1955, and action and decision thereon were deferred to the next meeting. After all these, and after the Reserve Bank's comments in exhibit P-62, it was a tame showdown that on November 10, 1955, the very date on which the 10th respondent submitted his report and the 11th respondent his explanation, the board ratified the whole list of a series of unauthorised advances. Exhibit P-61 is the list so ratified. It includes (according to P. W. No. 22 and D. W. No. 3) the advances in respect of which explanation was called for by exhibit P-59 and comprises all the advances in Schedule III of the points of claim in Application No. 2 of 1959 (which is the same as schedule I herein). Exhibit P-58 records that the board of directors scrutinised all the advances and limits shown in exhibit P-61 list and ratified the same. And yet we are told by D. W. No. 1 (1st respondent) that scrutiny was impossible, and that the directors "just went through" the list and by D. W. No. 3 (5th respondent) that there was no use considering these advances because they had already been made without sanction. The feverish haste and the supreme indifference with which the ratification was made cannot be too strongly condemned. Their explanation that this was done to satisfy the 9th respondent who was being inducted into the bank and on his insistence, appears to us to be hardly acceptable. The action of the directors in ratifying exhibit P-61 list seems to strengthen the case of the liquidator that the calling for explanation from the 11th respondent and report from the 10th respondent, the purported consideration of the same, the approval of the list of advances, and even the appointment of the 9th respondent as general manager, were all pre-arranged. P. W. No. 22 deposed to that effect in

his public examination (exhibit P-55). He repeated the same in his evidence in the present proceedings. This was repudiated by the 1st respondent as D. W. No. 1. The learned judge" appears to have been inclined to accept this part of the liquidator"s case, for, he observed :

" But the circumstances already discussed by me inevitably make me feel that the directors knew about the situation and probably the suggestion of the liquidator that the whole thing was pre-arranged, is also justified."

32. We have no hesitation in more firmly and clearly endorsing these observations of the learned judge and in finding that exhibits P-59 and P-60, and the ratification of exhibit P-61 list--not to go further--were prearranged as claimed by the liquidator and spoken to by P. W. No. 22. We also find that the directors had knowledge of the defalcations and falsifications and of the fictitious nature of the advances and entries in the bank accounts, when they ratified exhibit P-61. In the absence of even elementary scrutiny of exhibit P-61 list, their contention that they only knew that the advances were unauthorised, but not that they were fictitious, is hardly acceptable. We cannot accept also the argument that the defalcations and misappropriations having been already effected, the subsequent manipulation of entries as to fictitious advances, cannot be said to be an act done with " intent to defraud " or for " other fraudulent purpose " within the meaning of Section 542. The manipulation of entries and the creation and the ratification of fictitious advances were with intent to cover up the misappropriations, and were an integral part of the fraudulent intent or purpose; no less so, for the one having followed the other.

33. The learned judge at page 16 of the printed judgment stated that the directors knew about the real position on 30th November, 1955. At the top of page 17 he recorded that they knew about the bogus advances mentioned in schedule I and ratified the same by resolution dated November 10, 1955, knowing their real nature. At page 18 the learned judge stated that the insolvent condition of the bank started, at any rate, to show itself from August, 1955, and it was clear that the directors and respondents Nos. 10 and 11 knew about this also. In his judgment in the connected Application No. 2 of 1959, the learned judge stated :

" I have already held in the other application that the directors must have known by the end of July or the beginning of August, 1955, about the misappropriations made by respondents Nos. 9 and 10." (See page 14 of the printed judgment in Application No. 2 of 1959).

34. Accepting the evidence of P.Ws. Nos. 1 to 3 we would fix the knowledge of the directors at least on the last Friday in July, 1955.

35. It was pressed on us that the third respondent"s position was different and that he cannot be saddled with knowledge in the same way as the other directors, either on the basis of the resolution dated 10th November, 1955, or on the basis of the evidence of P.Ws. Nos. 1 to 3 and 13 to 16 and 22. He was not a

party to the resolution of the board of directors dated November 10, 1955, and did not attend that meeting of the board. P.W. No. 1 generally speaks about the directors at Alleppey having been informed and their contacting the outside directors, namely, respondents Nos. 1 and 8. The 3rd respondent is one of the local directors. P.W. No. 3 in chief-examination deposed to the 4th respondent calling the other local directors and contacting the 1st respondent on the telephone and meeting at the residence of the 4th respondent. In cross-examination by the 3rd respondent he stated that the 5th respondent and the 7th respondent were the directors present in the 4th respondent's house on the last Friday of July, 1955. P.Ws. Nos. 13 to 16 do not implicate the 3rd respondent. But in spite of these infirmities, we feel from the conduct of the 3rd respondent, to which we shall refer, and from the attendant circumstances that the 3rd respondent must have had the requisite knowledge of the affairs of the bank at the same time as the other directors, if not earlier. His place of business in Alleppey was only 200ft. away from the bank, and it is inconceivable that he would not have known, and would not have been informed, about the information conveyed by P.Ws. No. 1 and 3 regarding the defalcations in the bank and the meeting subsequently in the 4th respondent's house. P. W. No. 3 deposed that in 1954-55 the 3rd respondent and his sons used to come to the bank and ask P.W. No. 22 for money. As D. W. No. 3, the 3rd respondent was cross-examined about these aspects, he merely stated that he does not "remember" the 4th respondent telling him regarding the complaint about the misappropriations of large amounts from the bank by the 10th and 11th respondents and that he further does not know and does not remember a discussion having taken place in the house of the 4th respondent among the directors including himself, about these misappropriations. These hesitant answers of his in cross-examination are not sufficiently pointed and we are inclined to think that the 3rd respondent also did have knowledge of the defalcations and irregularities in the same way as the other directors.

36. Counsel for the liquidator sought to fasten knowledge on the 3rd respondent also from the fact that, although he was not present at the meeting of the board of directors on November 10, 1955, when exhibit P-61 list was ratified, he was present at the next meeting of the board on March 30, 1956, where the minutes of the previous meeting were read and passed and approved. If the liability of the 3rd respondent were to be rested merely on his adoption at the subsequent meeting of the proceedings of the board of directors dated November 10, 1955, we would have hesitated to endorse the claim of the liquidator. The decision in *Burton v. Bevan*, [1908] 2 Ch. 240, cited by counsel for the 3rd respondent seems to be against spelling out liability by mere adoption at a subsequent meeting of the proceedings of a previous one. But, for reasons noticed earlier, and from his conduct to be noticed presently, we are of the view that the 3rd respondent also had the requisite knowledge of the true position of the bank.

37. We shall now refer to certain features proved in evidence against the 3rd respondent. His conduct, as disclosed by the same, leaves us in no doubt that he

must have been aware of the true state of affairs of the bank. The 3rd respondent was a director of the bank from its inception. He was a member of the executive committee for about three years from 1944. He was doing business in piece-goods and also in the production and distribution of films. The case of the liquidator as spoken to by P.W. No. 22 is that the 3rd respondent had a large amount of what the witness described as "unaccounted money " or " black-market money ". Such money to the tune of about Rs. 1,40,000 was entrusted by the 3rd respondent on several occasions from 1949 onwards to the 10th respondent to be secretly lent on interest. The 10th respondent used to lend these amounts to constituents and customers of the bank, taking cheques as security from them, and returning the cheques when the amounts were repaid by the parties. Exhibit P-56 is a series of 35 cheques issued by the customers of the bank to secure such advances of the 3rd respondent's money by the 10th respondent. These cheques had not been presented for encashment and were recovered from the 10th respondent's table. The 10th respondent as P.W. No. 22 deposed that the amounts covered by some of these cheques are still outstanding. P.W. No. 22 was having satta transactions which landed him in a loss oi about five or six thousand rupees in 1954, and another ten thousand rupees in 1955. According to the witness the 3rd respondent must have known about his financial position and that of the parties to whom the monies were lent, all of whom were in Alleppy, and none of whom was in a position to repay the monies in 1954 and 1955. The 3rd respondent pressed for repayment and the witness's only source was to draw amounts from the Popular Bank and pay the 3rd respondent, which he did. In spite of this, he stated in one place that the 3rd respondent did not know that the witness drew money from the bank, in the sense that the 3rd respondent did not enquire, and the witness did not volunteer the information. From the evidence and the circumstances to which we shall refer, it seems to us that neither enquiry nor volunteering of information was necessary, and the whole thing was patent enough. Exhibit P-57, an acknowledgment receipt given by the 3rd respondent to the 10th respondent on January 19, 1955, shows the amount due that day to the 3rd respondent as Rs. 20,000. Out of this, a sum of Rs. 13,000 was paid by 26 cheques of Rs. 500 each, issued by the 10th respondent. (Vide exhibits P-88, P-90 series and P-92 series and the credit entry in favour of the 3rd respondent in exhibit P-89). The balance then stood at Rs. 7,000. On February 11, 1956, the 10th respondent submitted exhibit P-64 petition to the chairman of the executive committee of the bank for a loan of Rs. 7,500 from the bank. Exhibit P-64 contains the endorsement " yes " with the counter-signature of the 3rd respondent (in Tamil) and of the 5th respondent, below the same. P.W. No. 22 deposed that the 3rd respondent at any rate, knew that the purpose of the loan was to pay off the balance amount due to him. The evidence of the 5th respondent as D.W. No. 3 is also to the effect that he was told by the 3rd respondent and the 10th respondent that the purpose of exhibit P-64 was for repayment of a loan advanced by the 3rd respondent to the bank. The 3rd respondent then was not even a member of the executive committee and we can find no reason for his

signature sanctioning the loan, except that he was a party to the scheme of advancing bank's money to the 10th respondent for repayment to himself. The 10th respondent executed a pronote for the loan amount sanctioned, which was paid to him by his own cheque as manager as seen from exhibit P-28. He discharged his debt due to the 3rd respondent on 13th February, 1956, by exhibit D-37 cheque for Rs. 7,000. Exhibit P-13, the current account of the 3rd respondent, shows a credit entry of Rs. 7,000 by cheque or transfer. Exhibit P-4 shows a corresponding debit in the 10th respondent's account and a credit of his cheque as manager for Rs. 7,500. The balance amount of Rs. 500 was credited to the 10th respondent's savings bank account, and, as seen from exhibit P-47, utilised to meet the expenses of discounting cheques. Exhibit P-89 the current account ledger, shows the credit of Rs. 13,000 to the 3rd respondent by cheques. Exhibit P-88(a), exhibit P-91 and exhibit P-93 are the transfer credit slips in respect of twenty-three of the twenty-six cheques by which payment of Rs. 13,000 was made. P.W. No. 22 deposed that when on a complaint by some of the employees in July, 1955, he was called by the directors, he told them that a part of the amounts drawn from the bank and not brought to account, was used to pay off the 3rd respondent, a good portion to finance the speculative transaction of the 11th respondent, and some to meet his own losses in the satta transaction.

38. The 3rd respondent's case was one of complete denial of the transactions attributed to him. As D.W. No. 5, he denied the possession of any "black-market money " or its entrustment to P.W. No. 22, for being lent on interest. He denied his account having been credited with cheques issued by the 10th respondent. He relied on the entries in exhibits D-80 and D-82, his Ledger and Day Book, to show that the payments of Rs. 500 each evidenced by exhibit P-90 series, etc., and the payment of Rs. 7,000 on February 13, 1956, were all payments in cash. Regarding exhibit P-64 he stated in chief examination that he signed the same without knowing that it was a loan application. In cross-examination he was obliged to admit that his accountant (D.W. No. 6) told him that exhibit P-64 was a loan application by the 10th respondent for Rs. 7,500. The learned trial judge recorded that the 3rd respondent did not impress him at all as a witness of truth. On a perusal of his evidence as a whole, we record our concurrence. The 3rd respondent in cross-examination admitted that he must be having in his possession pass-books issued by the bank regarding his current account and savings bank account and that these would show whether the payments were in cash or otherwise. At one stage of his cross-examination he expressed willingness to produce them. On the same day he deposed that the bank used to issue receipts (pay-in-slips) against payment of monies disclosing whether the payments were in cash or by cheque, and undertook to produce them. Yet, the next day when his cross-examination continued, he stated that the pass-book relating to the 26 payments was with the Popular Bank Ltd. and the receipts for payments could not be found. He admitted that neither the entries in the cashier's scroll (P-I 1) nor the agent's scroll (D-7) would bear out his case of cash payment.

39. The chain of documents produced by the liquidator is connected, and fairly complete ; and the evidence of P.W. No. 22 on this aspect of the case is in keeping with the same. u/s 45F of the Banking Regulation Act, entries in the bank's books of accounts or other documents are, in the circumstances, prima facie evidence against the directors of the truth of all matters therein recorded. Supporting evidence as to these entries is supplied by P.W. No. 3 and D.W. No. 2. There is no satisfactory evidence on the side of the 3rd respondent to rebut the case of the liquidator.

40. It was argued for the 3rd respondent that it was inconceivable that there was no document to evidence the entrustment of the alleged large sum of money to the 10th respondent or its discharge. P.W. No. 22 deposed that the 3rd respondent used to take letters of acknowledgment as and when money was entrusted and that these used to be got back when the money was repaid. The non-production of these letters of acknowledgment was commented on. P.W. No. 22's answer in his deposition was that most of the other letters, like exhibit P-57, had been destroyed then and there, and he disclaimed knowledge as to the rest. Comment was also made that P.W. No. 22's version about informing the directors in July, 1955, that part of the defalcated funds of the bank was utilised to pay off the 3rd respondent was untrue, and that there was no mention of it on two earlier occasions when it could have been disclosed, viz., the exhibit P-60 report and the public examination evidenced by exhibit P-55. We do not feel persuaded by any of these alleged infirmities. If, as stated, the genesis of the transaction between the 3rd respondent and P.W. No. 22 was unholy, and related to " unaccounted money " or " black-market money ", the absence of any document relating to it, the secrecy or clandestine character of the dealings, and the non-mention of it in exhibit P-60 are all understandable. From the cross-examination of P.W. No. 22 by the 3rd respondent it was brought to light that certain enquiries were started against the 3rd respondent and P.W. No. 22 was examined before the Income Tax Officer. Exhibit D-38 is a certified copy of the deposition of the 3rd respondent before the said officer. P.W. No. 22 explained his omission to refer in public examination about the use of the bank's funds to pay off the 3rd respondent, on the ground that he was never asked about the same. In the circumstances, we are not inclined to attach any importance to the non-production of letters of acknowledgment, if any, similar to exhibit P-57, or to the non-disclosure of the entrustment and repayment of the 3rd respondent's monies either in exhibit P-60 report or subsequently. We see no reason to discredit the testimony of P.W. No. 22 that in July, 1955, at the residence of the 4th respondent, while confronted with his irregularities and the difficult position of the bank, he had stated to the directors that a portion of the defalcated amounts had been used to pay off the 3rd respondent. The time at which the 3rd respondent put pressure on P.W. No. 22, and secured repayment, is significant. The 23 cheques produced (exhibits P-88, P-90 series and P-92 series) range from February 7, 1955, to July 20, 1955. The conclusion appears irresistible that while the bank was burning, the 3rd respondent was engaged in pulling out the

chestnuts and that he did so with full knowledge of the affairs of the bank.

41. The learned trial judge perused the 3rd respondent's account books, exhibits, D-80 and D-82, which showed that the twenty-six payments of Rs. 500 each and the payment of Rs. 7,000 on February 13, 1956, were all in cash. It was the opinion of the learned trial judge that these accounts are false and written up for the purpose of the case. We see no reason to dissent from this finding. From the cogent and convincing evidence produced on the side of the liquidator, to which we have referred, we have no hesitation in holding that the payments in question were by cheques, and that exhibits D-80 to D-82 are untrustworthy and cannot be relied upon. About one other account book of the 3rd respondent, exhibit D-87, we shall refer while dealing with A.S. No. 426 of 1964.

42. The learned trial judge, after referring to the evidence of P.Ws. 1 to 3 and 13 to 16 in the passage cited, referred to two circumstances in support of his conclusion that respondents Nos. 1 to 8 had knowledge regarding the fictitious advances in schedule I. The first of them was that in exhibit P-63, the minutes book of the executive committee, a large number of pages have been left blank and the last of the proceedings is dated 11th June, 1955. The learned judge referred to the evidence of the 5th respondent as D.W. 3, that the committee functioned till the bank suspended business, that it met five or six times after June 11, 1955, and to his inability to explain why the minutes of the meeting after 11th June, 1955, were not recorded in exhibit P-63. Counsel for the various appellants attacked this circumstance relied on by the learned judge and pointed out to the evidence of P.W. 22 and D.W. 3 himself in re-examination. P.W. 22's evidence is unhelpful and is only to the effect that the proceedings of the last meeting of the executive committee held on June 11, 1955, appear at page 14 of exhibit P-63. Likewise, the statement of D.W. 3 in re-examination relied on for the purpose is also inconclusive. There is intrinsic evidence, that the executive committee did transact some business after June 11, 1955, In its proceedings dated August 31, 1955, the board of directors recorded that an office note for sanction of a loan of Rs. 47,000 was placed before the executive committee. There is also evidence that after stringency in the bank was reported by P.W. 22 in August, 1955, the executive committee sanctioned the raising of a loan of Rs. 47,000 by repledge of jewels. In the circumstances, we do not think that the reliance placed by the learned trial judge on the absence of record of the proceedings of the executive committee subsequent to June 11, 1955, was unjustified.

43. The second circumstance relied on by the learned judge is the conduct of the directors in having accorded wholesale approval to the list of advances in exhibit P-61, without scrutinising the same or going into details regarding the nature and particulars of the advances. We have already adverted to this circumstance and we are in agreement with the learned judge that the conduct of the directors in ratifying the advances in exhibit P-61 list in the most perfunctory fashion is

consistent only with their knowledge of the real position.

44. We shall now refer to an aspect of the case, which has caused us some anxiety and uneasiness. We have accepted the evidence of P. Ws. 1 to 3 and 22, and have endorsed, in more certain and emphatic terms, what the learned trial judge was inclined to accept as probably justified, namely, the case of the liquidator, that the calling for the report and explanation from respondents Nos. 10 and 11, the acceptance of the same and ratification of the advances were all part of a pre-arranged plan. According to their evidence--or at least that of P.Ws. 3 and 22--the appointment of the 9th respondent as the manager of the bank was also pre-arranged. We are reluctant to say anything bearing on the liability of the 9th respondent, as he is not before us in any of these appeals, and as the liquidator has not appealed against the order exonerating him from liability. But in the face of the evidence of P.Ws. 1 to 3 and 22 which we have accepted, and which the learned judge also accepted, we have found it not easy to accept the learned judge's reasoning in support of the exoneration of the 9th respondent from liability. Were the matter open, we would have had second thoughts on the question of the 9th respondent's liability. There is enough in the evidence of P.Ws. 3 and 22 and D.Ws. 1 and 3 and the resolution dated August 31, 1955, recorded in exhibit P-58 to make it appear that the 9th respondent was either anxious to enter the service of the bank, or offered his services to it, although the evidence of the 9th respondent himself as D. W. 2 is to the effect that he was inducted into the bank. His insistence on the ratification of all advances in exhibit P-61, including those made prior to his entering the service of the bank, is a telling circumstance. P.W. 22 deposed that even before November 10, 1955, the 9th respondent was coming to the bank and he kept him informed of the regularisation of the defalcations. We have found it not easy to square these aspects with the exoneration of the 9th respondent and the finding of his absence of knowledge of the affairs of the bank. Before us the liquidator attempted the unenviable task of supporting the decree against the respondents-directors even by showing under Order 41, Rule 22, of the Civil Procedure Code, that the finding recorded against the 9th respondent was unsustainable, without asking for a reversal of this part of the learned judge's order. Neither the objectivity and dispassionateness expected of the liquidator as an officer of court, nor the high standards expected of him in not pursuing a vindictive or frivolous appeal--which were the explanations attempted on his behalf--appear to us to be sufficient to justify the liquidator's omission to file an appeal against this part of the judgment, which is inextricably bound up with certain other parts of the claim. In view of the obvious limitations, and the unfairness in our dilating further on this part of the case, we leave the matter there.

45. As a result of the foregoing discussions, we hold on heads 1, 3, 4 and 5 that respondents Nos. 10 and 11 were guilty of misappropriation of the bank's funds and that the directors were parties to covering up the fraud thus committed by causing false and fictitious entries to be made in the books of the bank, and by the ratification of exhibit P-61 list in the manner detailed earlier. The extent of

liability of the directors under these heads will be discussed separately.

46. The SIXTH HEAD of claim relates to two matters, namely, issuing false balance-sheets for the years 1954 and 1955 showing profits and thus inducing the depositors not to withdraw the deposits; (2) the canvassing for and receiving fresh deposits, without disclosing the true position of the bank. Schedule IV appended to the points of claim is the list of 165 deposits canvassed for and secured by the directors and employees of the bank. The learned judge found that the liquidator had no case that the directors had knowledge of the misappropriations in 1954 and therefore it was too much to conclude that the balance-sheet of 1954 was false to the knowledge of the directors. Against this part of the learned judge's order there is no appeal. As far as the 1955 balance-sheet (vide exhibit P-66) is concerned, by the time of its preparation, the fictitious advances in schedule I had been made. The 9th respondent in the draft proposals made by him, for consideration by the board of directors (exhibit D-47) suggested that in view of the small profits and uncertain times no dividend should be recommended for the year. The same was scored out by the 1st respondent, the chairman of the board of directors, who suggested payment of dividend for the year. On these facts the learned judge observed that the conduct of the 1st respondent in overruling the suggestions made by the 9th respondent indicated that he knew that the bank was not working on profit. Exhibit P-58 shows that the balance-sheet was passed at a meeting of the board of directors dated March 30, 1956, attended by all except the 7th respondent. There is the evidence of D.W. 2 (9th respondent) that the board of directors passed the balance-sheet, and notwithstanding his protests and unwillingness to sign, the 1st respondent insisted on his doing so. He has also deposed that the corrections to his draft proposals were made after discussion by the board and in accordance with the opinion of the board. Clause 120 of the memorandum and articles of association of the bank (exhibit D-39) declares that no dividend will be paid otherwise than out of the profits of the year or any other undistributed profits. In the face of this provision, and on the authorities, there can be little doubt that a declaration of dividend otherwise than out of profits, and at a time when the bank was, to the knowledge of the directors, working at a loss, was an act ultra vires the directors. On the materials we hold that all the respondents-directors except the 7th respondent were parties to the preparation and passing of false balance-sheet for the year 1955, showing profits, knowing that the position of the bank was such that it could not show any profit or declare dividends for that year.

47. The evidence in regard to the canvassing of deposits is afforded by P.Ws. 2, 12, 19, 20, 22, 23 and D.W. 2 and by exhibits P-67 to P-70, P-85 and P-86. Exhibits P-67 to P-70 are circulars issued by the 9th respondent (D.W. 2) to the branches calling upon the staff-members to canvass deposits. D.W. 2 deposed that while in the employ of the Travancore Bank before he joined the Popular Bank, he used to get such circulars from the head office of the Travancore Bank and that he followed the practice after joining the Popular Bank. He further

deposed that the directors instructed him to issue such circulars and requested him to canvass deposits. He stated that the directors were also canvassing deposits to his knowledge. Exhibits P-85 and P-86 written by the 1st respondent to D.W. 2 afford clear indication of the 1st respondent's eagerness to canvass deposits. Exhibit P-86 dated April 26, 1956, indicates that the 1st respondent and 5th respondent wanted to go over to canvass deposits. D.W. 2 offers evidence about the reference to the 5th respondent in exhibit P-86, and that in pursuance of exhibit P-86, the 1st respondent actually canvassed deposits. As far as the directors are concerned, P.W. 19 implicates the 4th respondent, and P.W. 23, the 5th respondent, in the matter of canvassing deposits. The 1st respondent as D.W. 1 denied having canvassed deposits, or having known other directors having done so. The first part of his denial cannot be accepted in the face of exhibits P-85 and P-86. Strangely enough, these documents were not put to the 1st respondent or proved through him when he was in the box, but were proved only through the 9th respondent as D.W. 2, in the course of his cross-examination by the liquidator. The explanation on behalf of the liquidator is that these documents were made available only when D.W. 2 stepped into the box. Whatever that be, there is no denial either by cross-examination or by further evidence on behalf of the 1st respondent of these letters. There is also the fact that when the 1st respondent was examined as D.W. 1 he was asked in cross-examination by the liquidator whether he had not sent a letter dated March 23, 1956, to the 9th respondent asking him to canvass deposits, and he replied " I do not remember" (the date of exhibit P-85 is March 24, 1956, and not March 23, 1956, if the suggestion was about the said letter). In these circumstances, we find no reason to reject the evidence afforded by exhibits P-85 and P-86. There is no reason also to disbelieve the evidence of D.W. 2 that the circulars, exhibits P-67 to P-70, were issued under the instructions of the directors and that the directors requested him to canvass deposits and were doing so to his knowledge. There is no effective cross-examination on these aspects. No reasons have been made out to discredit the evidence of P. Ws. 19 and 23. We hold that, in pursuance of the circulars, exhibits P-67 to P-70, issued at the instance of the directors, there was canvassing for deposits ; that, some at least of the directors, namely, respondents 1, 4 and 5 are shown to have canvassed deposits ; and that the directors requested D.W. 2 to do so; all at a time when they knew that the affairs of the bank did not justify the canvassing for or the making of deposits in it. The action of the directors here summarized amounts to carrying on the business of the bank with the requisite fraudulent intent or purpose required by Section 542 of the Companies Act. Such intent or purpose appears to us to be a reasonable inference, in the circumstances, from the financial" state of the bank as known to the directors. (Vide *In re William C. Leitch Brothers Ltd.* [1932]Ch. 71 : [1933] 3 Comp. Cas. 97.).

48. The EIGHTH HEAD of claim relates to payment by the respondents to certain creditors in fraudulent preference over others at or about the time of the suspension of business of the bank, with knowledge of the insolvent position of

the bank. The learned judge's finding under this head is that the directors, who knew about the insolvent position, were making at least some payments to some of the creditors in fraudulent preference over the others. The range of controversy before us under this head of claim was considerably narrowed, as counsel for the liquidator admitted that, except in respect of two payments, there was no evidence to show that the payments were made under the directions or to the knowledge of the directors. We shall therefore consider only the two excepted items. The first of them is item 12 of Schedule VI of the points of claim and relates to withdrawal of Rs. 8,500 on August 8, 1956, from the account of the 3rd respondent and the transfer of the same to the overdraft account of Ramanatha Reddiar, a nephew of the 3rd respondent. Exhibit P-13 is the cheque issued by the 3rd respondent containing endorsement on the reverse that the amount was credited to Ramanatha Reddiar's account. There is the evidence of P.W. 3 and P.W. 22 regarding the transaction to the effect that the cash position of the bank did not warrant the payment on August 8, 1956. It seems unnecessary to discuss this item in detail in view of certain prior proceedings to which we shall immediately refer. The liquidator filed C.M.P. No. 144 of 1958, claiming repayment of several amounts lost to the bank on the ground that they amounted to fraudulent preference. The 1st respondent to the said application was the 3rd respondent and item 6 in the said application was item 12 of Schedule VI herein. The other directors were not parties. The claim of the liquidator was upheld by Raman Nayar J. in exhibit P-72 judgment. The 1st respondent and another appealed by A.S. No. of 620 of 1961 to a Division Bench of this court. Appeals were filed by others also. It is enough to notice that, as far as this part of the official liquidator's claim is concerned, the Division Bench confirmed the finding that the transaction relating to the payment of Rs. 8,500 by transfer to the overdraft account of Ramanatha Reddiar amounted to a fraudulent preference. A.S. No. 620 of 1961, in so far as the same had been preferred by the 1st respondent in C.M.P. No. 144 of 1958, was dismissed with costs. The liquidator filed C.M.P. No. 6106 of 1968 to receive the appellate judgment as additional evidence. The said judgment was delivered only on 6th December, 1965, long after the judgment now under appeal. We have allowed C.M.P. No. 6106 of 1968. The additional document will be marked as exhibit P-96. In view of this judgment, we have no hesitation in holding that the transfer of Rs. 8,500 referred to above amounted to a fraudulent preference.

49. The second excepted item is item 15 of Schedule VI relating to the withdrawal of a sum of Rs. 2,000 from the savings bank account of Smt. Premalatha Bai, wife of the 5th respondent. The withdrawal was on August 11, 1956, and there is the evidence of P.Ws. 3 and 22 that the cash position on the date did not warrant the withdrawal. The amount was withdrawn and transferred to the overdraft account of G.S. Mallayya. From the absence of the requisite notice of withdrawal (vide P.W. 3) and from the close relationship of the depositor with the 5th respondent (who, besides being a director, was also the legal adviser of the bank), and the latter's knowledge at the time of the withdrawal of

the insolvent position of the bank, the learned judge was of the view that the payment amounted to a fraudulent preference. We endorse the said findings.

50. The NINTH HEAD of claim as stated by the learned trial judge is only that respondents Nos. 1 to 8, as directors, and respondent Nos. 9 to 11 as officers or employees of the bank, were knowingly parties to the carrying on of the business of the bank with intent to defraud the creditors or other persons or for any fraudulent purpose. This does not call for any separate discussion.

51. The SEVENTH HEAD of claim was found against the liquidator and there is no appeal or cross-objection by him. It is unnecessary to refer to this further.

52. From our discussion, of heads (1) to (6) and (8), we have no hesitation in holding that the business of the bank was carried on with intent to defraud creditors or other persons, and certainly, with a fraudulent purpose within the meaning of Section 542 of the Companies Act. We also have no hesitation to hold that the directors (respondents Nos. 1 to 8) were knowingly parties to the carrying on of the said business.

53. The defence to these proceedings that has been relied on by all the directors generally, and by those of them who were not in the executive committee at the relevant period, was that they placed implicit trust and confidence in respondents Nos. 10 and 11 and in the members of the executive committee to whom the power of managing the affairs of the bank, and of granting and reviewing loans and advances had been delegated, and that they cannot be held responsible if things went wrong. The defence is based on, and inspired by, the decision in *Dovey v. Cory* [1901] A.C. 477.. We are unable to endorse the broad submission that irrespective of the size and standing of the bank, the volume of business transacted therein, and the efficiency and trustworthiness of the persons to whom responsibilities were entrusted, a delegation of functions would per se carry with it a denudation of responsibility. In the present case, we have noticed that as early as 1954 the Reserve Bank in exhibit P-62 report commented on the laxity of supervision of the board of directors and of the committees constituted for the purpose of sanctioning and reviewing the advances, and the impropriety of leaving these matters to the uncanalised discretion of the manager. The resolution of the board of directors on September 6, 1953, by which the manager was directed to call a meeting of the committee at least once in a month and to act only on its orders in all matters of advances and credits was hardly adhered to especially after 1954. The laxity of supervision and the uncanalised powers of the manager were allowed to continue. Even after their knowledge on the last Friday in July, 1955, that the affairs of the bank had been brought to a sad impasse by reason of the defalcations and malpractices of respondents Nos. 10 and 11 the directors still continued them in the service of the bank. They connived at, and were parties to, covering up the misappropriations by manipulation of entries in the accounts of the bank. Even after the confession of guilt by respondents Nos. 30 and 11 in exhibits P-59 and P-60, the directors had no hesitation in ratifying exhibit P-61 list, without any scrutiny or check-up.

There was no effort and no attempt on the part of the directors at any time to see that respondents Nos. 10 and 11, or the executive committee, functioned properly and discharged their functions satisfactorily. In the circumstances, we cannot accept the defence of the directors that they should be excused from liability by reason of the trust and confidence reposed in respondents Nos. 10 and 11 by all of them, and in the members of the executive committee of the board, by the rest of the directors.

54. It was argued that the conduct and course of dealing of the directors coupled with their respectability and status were quite inconsistent with the acts of fraudulent trading and the fraudulent purpose attributed to them, and that they had acted only with the bona fide object of helping the bank to tide over its difficulties. It was stressed that the majority of the shares and deposits in the bank were, at the relevant time, held by the directors and their near relations and it was hardly conceivable that they would bring the bank to grief by the action attributed to them. We need not dwell on these aspects at length, as the improbability of a course of action or conduct seems to us of no avail against the proved facts. As a circumstance it cannot outweigh the proved facts to which we have fully adverted.

55. Some complaint was made before us that the pleadings were not sufficiently clear and specific. The substance of the case was contained in the points of claim. Its elaboration in matters of detail was attempted in the evidence. We see no complaint before the learned trial judge of deficient pleading nor do we see any case of prejudice by evidence sprung unsuspectingly by the liquidator.

56. We may now sum up our findings regarding the liability of the directors on the various heads of claim. On the first head we find that amounts were withdrawn by the bank from its accounts with other banks without accounting for them in the books of the bank, and had been misappropriated by the officers of the bank. These withdrawals, as listed in Schedule II, range from August 3, 1954, to July 9, 1955. As the directors had knowledge of the misappropriation only on the last Friday of July, 1955, they cannot be said to be " knowingly parties" to these withdrawals and misappropriations when they were made. On the second head of the claim, we find that the directors cannot be held liable for the fixed deposit amount of Rs. 10,000 by Sri Narayanaswamy, received on 19th June, 1955, and not brought into account in the books of the bank till September 2, 1955. On the third and fourth heads we find that misappropriations were covered up by manipulating the bills purchased and negotiated accounts and by false and fictitious entries in the books of the bank as advances to different customers, and that these fictitious entries were made by respondents Nos. 10 and 11 with the knowledge and approval of respondents Nos. 1 to 8. On the fifth head we find that the directors ratified exhibit P-61 list with knowledge of the fictitious nature of the advances in Schedule I of the points of claim. The entries in Schedule I range from August 30, 1955, to September 3, 1955, and total Rs. 1,99,000. The entire period covered is subsequent to the knowledge of the

directors and they are responsible for the entire claim. On the sixth head of the claim, we hold all the directors, except the 7th respondent, responsible for passing the balance-sheet of 1955, and the declaration of dividend for that year, at a time when the bank could not, to their knowledge, have made any profit. We further find that the directors had issued instructions to D.W. 2 for canvassing deposits and that at least some of them, viz., respondents Nos. 1, 4 and 5, actually canvassed deposits, and that they requested the 9th respondent to do so--all at a time when they knew the affairs of the bank did not justify their action. On the eighth head of claim we find that there was fraudulent preference in regard to items 12 and 15 of Schedule VI of the points of claim, amounting in all to a sum of Rs. 10,500.

57. The apportionment of liability made by the learned trial judge between the directors, as such, was not attacked before us except by the 3rd respondent, who complained against his being debited with the major share of the liability. We do not think that the learned judge was wrong in debiting the 3rd respondent with the major share of liability. As we are ultimately remanding the matter to the trial judge further discussion of this aspect is not called for.

58. What then, is the decree or order to be passed ? Section 542 of the Companies Act makes the directors who are knowingly parties to the carrying on of the business of the company with intent to defraud creditors or any other person or for any fraudulent purpose personally responsible for all or any of the debts or other liabilities of the company as the court may direct. That raises two questions : First: What is the totality of the debts or other liabilities of the company ? and Second: Should the directors be made liable for the totality of such debts or other liabilities, and if not, for what portion of them ? On these matters we have found the pleading and the evidence deficient and we are unable to record any definite finding. In paragraph 3 of the points of claim the liquidator alleged that the estimated deficiency of the company according to information gathered by him is Rs. 6,50,000. In paragraph 6(d) the liquidator prayed :

" (1) a declaration that the respondents are liable without any limitation of liability for all the debts of the company amounting to the sum of Rs. 13,97,300.

(2) A declaration that the respondents are jointly and severally liable to pay to the official liquidator sums amounting to Rs. 6,50,000 being the balance amount required to pay the creditors of the company in full after realising the available assets of the company.

(3) If necessary, an account of the debts of the company be taken.

(4) Payment by the respondents to the official liquidator of the company the said sum of Rs. 6,50,000 or such other sum for which the respondents may be found liable on the taking of accounts.

(5) An order that the respondents do pay to the applicant costs of and incidental

to the application.

(6) Such other order in the premises as the court shall think fit to make."

59. In traversing this, in paragraph 33 of the 1st respondent's defence, he stated:

" It is not even known how and why a declaration of liability to the extent of Rs. 13,97,300 has been claimed which has later been limited to Rs. 6,50,000."

60. In paragraph 21 of the defence this was repeated, and the liquidator was put to strict proof of establishing the deficiency and its quantum. The points of defence of many of the other respondents followed on the same lines.

61. There is not even formal evidence on the side of the liquidator, either as to how the deficiency was estimated at Rs. 6,50,000 or as to the totality of the debts or liabilities of the company. Nothing was said in the liquidator's evidence as P.W. No. 24, or on his behalf, in support of the quantification of all the debts of the company in the points of claim at Rs. 13,97,500. As P.W. No. 24 the liquidator only stated that he has claimed Rs. 6,50,000 as deficiency for paying creditors in full.

62. The learned trial judge while rightly noticing that the court had a discretion in assessing and fixing the liability of the persons concerned, recorded his opinion that respondents Nos. 1 to 8 are liable " for all the liabilities of the bank " (vide page 22 of the printed judgment). At that stage there was no attempt by the learned judge to quantify " all the liabilities " of the bank. At pages 24 and 25 of the judgment the learned judge recorded that the liquidator claimed a sum of Rs. 6,50,000 to meet the deficiency in the assets of the company to pay the creditors in full. On issue No. 1, the learned judge found without any consideration or discussion that the deficiency in the assets of the company is Rs. 6,50,000.

63. With respect, we are unable to accept this finding. We have already posed the aspects which appear to us to be germane to the question. We are not to be understood as saying that if the nature and extent of the fraudulent trading was responsible for all the debts and liabilities of the company, a decree for the same cannot follow. But these matters have neither been adverted to nor found. The extent of the fraudulent trading of the directors in regard to the claim made in the various schedules of the points of claim will have to be reassessed in the light of our finding as to the directors' knowledge of the true position of the bank. Again, in Schedule VI, the liquidator pressed before us, and we have found the liability of the directors only for items 12 and 15. In the light of these, and the other findings that we have recorded, the extent of liability of the directors will have to be re-estimated and appropriate orders passed.

64. We therefore set aside the decree of the learned trial judge in so far as respondents Nos. 1 to 8 are concerned, and remit Application No. 1 of 1959 back to the trial judge for the limited purpose of : (1) deciding the extent of all the

debts or liabilities of the bank ; and (2) considering and deciding in the light of our findings whether the respondents-directors should be made liable for the totality of such debts, and if not for what portion of the same. The parties are at liberty to adduce additional evidence limited to these points. As the appellants-directors have substantially failed in their contentions, we direct that they pay one-half of the costs of the liquidator in Appeals Nos: 137, 139, 140, 105, 124, 125, 133 and 134 of 1963, and bear their own. Costs before the learned trial judge both before and subsequent to this remand will be provided for in the final order to be passed by the learned judge.

A. S. No. 426 of 1964.

65. This is an appeal by the present Joint Commercial Tax Officer, Tirunel-vely, who was the Sales Tax Officer, 1st Circle, Alleppey, till July 2, 1955. He was not a party to Application No. 1 of 1959, but feels aggrieved by certain observations made by the learned judge about some writing, signature and seal made and affixed by him as Sales Tax Officer in two of the account books produced by the 3rd respondent, namely, exhibits D-81 and D-87. In effect, he seeks to expunge the observations made by the learned judge.

66. Discussing the case of the liquidator and of the 3rd respondent regarding the alleged entrustment of the latter's "unaccounted money" to the 10th respondent and its repayment, we have had occasion to refer to the 3rd respondent's case that no payments by cheque were made to him by the 10th respondent and that there were payments in cash on the relevant dates, as seen entered in the 3rd respondent's account books, exhibits D-80 to D-82. Exhibit D-87 is a ledger of the 3rd respondent for the year 1130 and was tendered for the only purpose of showing that it bears the signature, writing and seal on October 13, 1955, of the same Sales Tax Officer, as the one whose signature, writing and seal are to be found in exhibit D-81. The only purpose in producing exhibit D-87 seems to have been to add authenticity to exhibit D-81 by reason of the presence in the latter of the same signature, writing and seal, and of the same date as in exhibit D-87. The learned judge discussed the matter and recorded his conclusion thus :

" The 3rd respondent has produced another account book, exhibit D-87, to prove the genuineness of the accounts. Page 739 of this book contains the seal of the Deputy Commercial Tax Officer, Special Circle

Madras, with the date 30th January, 1957. A little below that appears " Checked " with initials underneath and date : " 26-7-1957, A.C.T.O., Madras". In between these two, I mean the seal of the Deputy Commercial Tax Officer, and the endorsement and initials of the A.C.T.O., there is a little space and therein appears the seal of the Sales Tax Officer, 1st Circle, Alleppey. About this seal and below the seal of the Deputy Commercial Tax Officer already referred to, there appear " Examined " and the signature of the S.T.O. with the date " 13-10-55 ". The same seal of the Sales Tax Officer and the word " Examined " with his signature and dated " 13-10-55 " appear on page 374 of exhibit D-81. The case

of the 3rd respondent is that exhibit D-81 is genuine because the same seal of the Sales Tax Officer and the same signature and date 13-10-55 as appearing in exhibit D-87 appear in Exhibit D-81 also. In other words, the argument is that since exhibit D-87 is undoubtedly genuine as the seal of the Deputy Commercial Tax Officer and the initials of the A.C.T.O., Madras, will indicate and since the same seal and signature of the Sales Tax Officer, Alleppey, as contained therein appear in exhibit D-81 also, exhibit D-81 must be genuine too.

I have closely examined the word " Examined " with the signature of the S.T.O. and dated "13-10-55" under a magnifying glass. It is very clear that the word " Examined" overlapping the seal of the Deputy Commercial Tax Officer, Madras, bearing the date 30th January, 1957, is on or above the seal. From my examination under the magnifying glass, it is clear to me that the seal of the Deputy Commercial Tax Officer with the date 30th January, 1957, was affixed earlier and the word " Examined " was written above it after the seal was affixed and the date " 13-10-55 " and the signature of the S.T.O. were also put subsequently. It appears to be clear that this alleged examination by the S.T.O. is a subsequent invention, subsequent to 30th January, 1957, with an earlier date put thereon. Therefore, I have no hesitation in holding that exhibit D-81 is an account subsequently written up and the seal and the signature of the S.T.O. with an earlier date produced for the purpose of this case. The same seal and signature, etc., of the same S.T.O. have been procured on page 739 of exhibit D-87 also.

(This is a matter for the Government to take up and it is for the Government to decide what action they should take against the Sales Tax Officer responsible for this. A copy of this judgment may be sent to the Government. The Registrar will keep exhibits D-81 and D-87 in safe custody and these account books will not be returned without orders of this court)."

67. In pursuance of these observations of the learned judge it appears that on January 23, 1964, the Board of Revenue, Commercial Taxes, Madras, served on the appellant in the above appeal, a notice calling upon him, to explain the irregularity committed in his capacity as the then Sales Tax Officer, 1st Circle, Alleppey. The show-cause notice is stated to have quoted the first two out of the three paragraphs of the learned judge's order, which we have extracted above. Thereupon the appellant filed this appeal.

68. We have examined the two account books, exhibits D-81 and D-87, and also the signature, writing and seal, and the juxtaposition of these. In spite of the challenge made by counsel for the appellant and for the 3rd respondent from specimen demonstrations before us, that it was impossible to be dogmatic in any given case from mere examination with the naked eye or with a magnifying glass, as to whether the seal is over the writing, or the writing over the seal, we are not satisfied that the observations made by the learned judge are unjustified. Our own examination of the seal and writing only confirmed the learned judge's impression and observations.

69. The appellant before us has only been issued a show-cause notice in pursuance of the observations made by the learned judge in his judgment. He would hereafter have sufficient opportunity to explain, as he has attempted to do before us, that he was not a party to Application No. 1 of 1959, nor even a witness therein and had no occasion to explain the nature of the writing, signature and seal, or the circumstances under which they happened to be made and affixed.

70. We dismiss this appeal, but without any order as to costs.