
(1968) 10 KL CK 0007

In the High Court Of Kerala

Case No : A.S. No's. 370, 381, 382, 395, 396, 399, 400 and 412 of 1963

K. Madhava Nayak

APPELLANT

Vs

Popular Bank Ltd. (In Liquidation)

RESPONDENT

Date of Decision : 29-10-1968

Acts Referred:

Banking Companies Act, 1949 — Section 45H
Companies Act, 1956 — Section 543, 543(1)

Citation : (1969) 39 CompCas 711

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

Bench : Division Bench

Advocate : V. Rama Shenoi and R. Raya Shenoi, in A.S. No. 370 of 1963, P. Krishnamoorthy, in A.S. No. 381 of 1963, P.C. Chacko and P. Krishnamoorthy, in A.S. No. 382 of 1963, K.V. Suryanarayana Iyer, C.M. Devan and N.N. Venkitachalam, in A.S. No. 396 of 1963, S. Narayana Potti, in A.S. Nos. 399 and 400 of 1963, K. Suryanarayana Iyer and C.M. Devan, in A.S. No. 412 of 1963, for the Appellant; Mani J. Meenattor, for the Respondent

Judgement

1. These appeals were heard along with, and in continuation of Appeals Nos. 137, 139 and 140 of 1963, etc., in which we have just delivered judgment. They arise from Application No. 2 of 1959 filed by the official liquidator of the Popular Bank Ltd., u/s 543 of the Companies Act. The parties to this application are, with one difference, the same as the parties to Application No. 1 of 1959 against which A.S. Nos. 137, 139 and 140 of 1963, etc., were directed, the only difference being that the 9th respondent in Application No. 1 of 1959 is not a party hereto. The result is that respondents Nos. 10 and 11 in Application No. 1 of 1959 are respondents Nos. 9 and 10 in Application No. 2 of 1959. Save where expressly indicated, reference would hereinafter be made to the ranks of the parties as before the trial judge.

2. Application No. 2 of 1959 sought to make the respondents liable for misfeasance and breach of trust, in relation to the company, and for misapplication and retainer of the money and property of the company, and as

being accountable for such money and property. The misfeasance, misapplication, retainer, breach of trust and accountability were claimed under six principal heads. Firstly, it was complained that respondents Nos. 1 to 8, the directors of the company, did not exercise adequate control in the matter of advances of the company's funds, and, in consequence, respondents Nos. 9 and 10 advanced large amounts to various parties without taking adequate securities for the advances and from whom it was not possible to recover the whole or a substantial portion of the advances. Not only were steps not taken to recover the amounts covered by the advances, but the board of directors ratified the advances on November 10, 1955. A list of such advances made, together with the amounts likely to prove unrealisable, was furnished in Schedule I. The unrealisable amounts aggregate to Rs. 4,76,746. Secondly, it was alleged that several amounts were withdrawn by respondents Nos. 9 and 10 from other banks, and were wrongfully retained and misappropriated. Respondents Nos. 1 to 8, who had knowledge of the said withdrawals, did not take any steps to recover the amounts withdrawn. The withdrawals thus made were covered up by false entries, made by respondents 9 and 10 with the knowledge of respondents Nos. 1 to 8, of advances to different customers of the company. These fictitious advances were also ratified on November 10, 1955. The list of the withdrawals from other banks was furnished in Schedule II aggregating to Rs. 1,60,500. A list of the false and fictitious entries of advances made to cover up the misappropriations was shown in Schedule III. The amount covered by such entries comes to Rs. 1,99,000. Thirdly, it was contended that respondents Nos. 1 to 8 prepared and published false balance-sheets for the years 1954 and 1955 showing profits when the bank had actually incurred heavy loss. The amounts paid as dividends for the said two years was shown in Schedule IV. Rs. 12,311-8-10 was claimed under this head. Fourthly, it was alleged that there were manipulations and falsification of accounts in the bills negotiated account of the company. Several bills have been entered as negotiated, which were actually not so negotiated. A list of bills in the bills negotiated account, in respect of which no bills have been actually negotiated, was shown in Schedule V. The amount covered thereby totals to Rs. 98,700. Fifthly, respondents Nos. 3 and 5 sanctioned and caused to be paid to the 9th respondent a sum of Rs. 7,500 in February, 1956, on a demand promissory note without any security, knowing that the 9th respondent had no means to repay the loan. A sum of Rs. 10,000 deposited by Sri N. Narayanaswamy was also misappropriated. Sixthly, it was alleged that there were manipulations in the profit and loss account of the company. The defences raised will be referred to in the course of the judgment. On these heads of claim, the learned trial judge formulated fifteen points for determination and recorded his findings which may be summarized thus :

(1) That the directors did not exercise adequate control in the matter of advances, and, in consequence, respondents Nos. 9 and 10 advanced large amounts to various parties without adequate security. The directors did not take effective steps to recover those advances ; (2) that the amounts mentioned in

Schedule II, were withdrawn and misappropriated ; that the directors did not take appropriate steps to recover the said amounts from respondents Nos. 9 and 10; and that the misappropriations were covered up by making false entries of fictitious advances, as indicated in Schedule III, with the knowledge and consent of the directors; (3) that the liquidator had not established any manipulations in the profit and loss account; (4) that the fixed deposit amount of Rs. 10,000 of Sri Narayanaswamy was misappropriated but probably this may not be the direct result of misfeasance of the directors as it could be discovered only if the directors looked into the account books item by item ; and that respondents Nos. 3 and 5 had sanctioned a loan of Rs. 7,500 to the 9th respondent without security ; (5) that there were manipulations in the bills negotiated account, as a result of which the bank must have lost at least Rs. 61,800 as shown in Schedule V ; (6) that as far as the balance-sheet for 1954 was concerned, respondents Nos. 1 to 8 might not have known that it was false ; but regarding the balance-sheet for 1955, the same was false and incorrect to the knowledge of respondents Nos. 1 to 8, and they had not established that the dividends covered thereby were not disbursed ; (7) that the loss sustained by the bank can be fixed at Rs. 6,50,000 being the amount claimed in Application No. 1 of 1959 ; (8) that the respondents are guilty of misfeasance and breach of trust in relation to the bank and are liable to contribute the following sums by way of compensation in respect of the misapplication, misfeasance and breach of trust, namely, respondents Nos. 9 and 10, jointly and severally liable for the entire sum of Rs. 6,50,000; the 3rd respondent liable for Rs. 2,00,000 ; respondents Nos. 1, 4, 5 and 7 liable for Rs. 75,000 each; and respondents Nos. 2, 6 and 8 liable for Rs. 50,000 each. The respondents were made liable for the costs of the liquidator in the same proportion. It was made clear by the learned trial judge that the liquidator will not in any event be entitled to realise more than the amount of Rs. 6,50,000 and one set of costs by executing either of the decrees or both the decrees in Applications Nos. 1 and 2 of 1959 from respondents Nos. 1 to 8 in the proportion directed. A copy of the judgment in Application No. 1 of 1959 was directed to be appended to the judgment in Application No. 2 of 1959.

3. Against this order of the learned judge, A.S. No. 370 of 1963 has been preferred by the 7th respondent; A.S. No. 381 of 1963 by the 2nd respondent; A.S. No. 382 of 1963 by the 3rd respondent; A.S. No. 395 of 1963 by the 8th respondent; A.S. No. 396 of 1963 by the 1st respondent; A.S. No. 399 of 1963 by the 4th respondent; A.S. No. 400 of 1963 by the 5th respondent; and A.S. No. 412 of 1963 by the 6th respondent. Respondents Nos. 9 and 10 have not filed any appeal. Nor has the official liquidator filed either any appeal, or memorandum of cross-objections.

4. Since the filing of these appeals, respondents Nos. 1, 3 and 6 died. The legal representatives of respondents Nos. 1 and 6 have impleaded themselves as appellants in the appeals filed by them.

5. On behalf of the 3rd respondent C.M.P. No. 7082 of 1968 was filed on July 16,

1968, after arguments on the appeals were closed and judgment was reserved on July 4, 1968. It was prayed that the entire proceedings initiated by the liquidator be declared to have abated. The cases were re-posted to argue the subject-matter of the petition alone. Arguments on the same were heard on July 25, 1968, and adjourned at the request of counsel to July 31, 1968. After further submissions made on that day on the subject-matter of the C.M.P., orders thereon were reserved. We have repelled a similar argument addressed to us in A.S. No. 134 of 1963 in the judgment just delivered in that appeal and other connected appeals. For reasons recorded in paragraphs 12 to 14 therein, we have no hesitation in rejecting the contention that the proceedings initiated by the liquidator terminate on the death of the 3rd respondent after decree and pending appeal. We further hold that, as the 3rd respondent died after conclusion of arguments and before delivery of judgment in his appeal, this judgment of ours would have effect as against him as if it were pronounced while he was alive.

6. The learned trial judge by his order directed that the liquidator will not in any event be entitled to realise more than Rs. 6,50,000 and one set of costs by executing either or both of the decrees in Applications Nos. 1 and 2 of 1959 from respondents Nos. 1 to 8 in the proportion of their liabilities as determined by the judge. The liquidator has not appealed from this part of the learned judge's order. For that reason we say nothing about this aspect of the order. We shall now proceed to consider the various heads of claim. The relevant facts have been stated by us in our judgment in A.S. Nos. 137, 139 and 140 of 1963, etc. As we are directing a copy of the said judgment to be appended to this, it is unnecessary to traverse the same ground over again. The facts stated in the said judgment will serve as a background to these appeals also. The evidence given in Application No. 1 of 1959 was treated as evidence in Application No. 2 of 1959 also.

7. Section 543(1) of the Act may conveniently be quoted :

" 543. (1) If in the course of winding up a company, it appears that any person who has taken part in the promotion or formation of the company, or any past or present director, managing agent, secretaries and treasurers, manager, liquidator or officer of the company-

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

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

the court may, on the application of the official liquidator, or the liquidator, or of any creditor or contributory, made within the time specified in that behalf in Sub-section (2), examine into the conduct of the person, director, managing agent, secretaries and treasurers, manager, liquidator or officer aforesaid, and compel him to repay or restore the money or property or any part thereof respectively, with interest at such rate as the court thinks just, or to contribute such sum to

the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust, as the court thinks just. "

8. Considerable discussion centred round the meaning of the expression " misfeasance " and the scope of liability sketched by the section . Copious references were made to the English and Indian decisions. We do not think it necessary to survey the entire gamut of these decisions. As we understand them, certain propositions appear to be well settled. Before liability can be attracted under the Section it must be shown that the person proceeded against has been guilty of misapplication, retainer, misfeasance, etc., resulting in loss to the company as a direct consequence of the act complained of. It was argued that mere nonfeasance would not be included within the purview of the Section . The observations in some cases seem to countenance such a view. But the view of Jessel M.R. in *Ex parte Pelly* [1882] 21 Ch. D.492 the views expressed in *In re Kingston Cotton Mills Company (No. 2)* [1896] 2 Ch. 279 and the decision of Maugham J. in *re Etic Ltd.* [1928] Ch. 861 are sufficiently clear that the English Section --on which the Section in the Indian Act has been modelled--covers a breach of trust in the wide sense, including a breach of trust by negligence or something of that kind. The same view has been taken in some of the Indian decisions also. (See *Rao Sahib V. Subbayya and Others Vs. C.T. Machayya and Another*, and *M.A. Malik v. V.S. Thiruvengadaswami Mudaliar*, [1949] 19 Comp. Cas. 311). The facts presented here and the conclusions that we have formed do not warrant any greater elaboration or a more detailed examination of the legal position.

9. We shall first take up the second head covered by schedules II and III. Schedule II herein is identical with Schedule III in Application No. 1 of 1959, and Schedule III is identical with Schedule I in Application No. 1 of 1959. In our judgment in Appeals Nos. 137, 139 and 143 of 1963, etc., we have held, on the evidence of P.Ws. 13 to 16 and 22 and other circumstances that the advances shown in Schedule I of Application No. 1 of 1959 (Schedule III herein) were fictitious and that the directors with the knowledge of their fictitious nature suffered entries to be made in the books and were also parties to the borrowings and manipulations. The facts proved and accepted by us are that the bank's monies were withdrawn and utilised to pay off the " unaccounted money " of the 3rd respondent entrusted with the 9th respondent, to finance the speculative transactions of the 10th respondent, and to meet the losses from satta transactions of the 9th respondent; and that the losses thus incurred by the bank were covered up by making false and fictitious entries of advances having been made to certain customers of the bank. The total liability under Schedule III comes to Rs. 1,99,000. It is the evidence of the 9th respondent as P.W. 22 and of the 5th respondent as D.W. 3 that exhibit P-61 list which was ratified by the board of directors on November 10, 1955, comprised all the advances in Schedule III hereto. In our judgment in A.S. Nos. 137, 139, 140 of 1963, etc., we have commented on the perfunctory way in which the list was ratified without the least scrutiny. On the facts briefly referred to above, and noticed in detail in

our judgment in those appeals just delivered, we hold that in being parties to covering up the misappropriations effected by respondents Nos. 9 and 10, by causing entries to be made relating to the fictitious advances shown in Schedule III and in ratifying these advances without the least care or scrutiny, the directors have been guilty of misapplication of the bank's funds and misfeasance u/s 543 of the Act.

10. As far as the withdrawal of the amounts and misappropriations mentioned in Schedule II are concerned they range from August 3, 1954, to July 9, 1955. In our judgment in the appeals from Application No. 1 of 1959 we have held that the directors had knowledge of the unsatisfactory state of affairs in the bank and of the defalcations and misappropriations of those funds only on July 29, 1955. The withdrawals shown in Schedule II are all before this date. There is no evidence to connect any of the directors with these withdrawals when they were effected.

11. A claim has, however, been made against the directors on the ground that they did not take appropriate steps to recover the amounts withdrawn from respondents Nos. 9 and 10. On the other hand, when they were apprised of these withdrawals--as we have held they were, on July 29, 1955--far from taking steps to recover the amounts from respondents Nos. 9 and 10, they were privies to covering up the misappropriations by causing false and fictitious entries to be made in the books of the bank showing these misappropriated amounts as having been advanced to customers of the bank. This conduct of theirs constitutes misfeasance and would attract liability u/s 543 of the Act. But we do not think any fresh or independent loss on this account has been caused to the bank, in addition to the loss occasioned by the misappropriations resulting from the withdrawals mentioned in Schedule II. Having found the directors liable in regard to these entries in Schedule III, we do not feel justified in duplicating their liability, by surcharging them for the amounts covered by Schedule II as well. The fictitious entries in Schedule III and the withdrawals in Schedule II were all parts of the same transaction. The learned trial judge noticed the liquidator's attempt, through the evidence of P.W. 2, to connect the withdrawals in Schedule II with the bogus and fictitious entries in Schedule III, and recorded that he was inclined to think that the advances shown in Schedule III were made for the purpose of accounting for the earlier misappropriations shown in schedules II and V. We agree, and hold that the directors are responsible u/s 543 of the Act for the amounts withdrawn from other banks and misappropriated by respondents Nos. 9 and 10 as shown in Schedule II which were covered up by the entries of fictitious advances in Schedule III.

12. It would be convenient next to take up the fourth head of claim which relates to manipulations in the bills negotiated accounts, resulting in a loss of Rs. 61,800 to the bank, as shown in Schedule V. We have difficulty in holding the directors, or any of them, responsible for the entries in the bills negotiated accounts of the company, as furnished in Schedule V. The period covered by these entries ranges

from August 17, 1954, to November 19, 1955. A good part of it is prior to the knowledge of the directors about the state of affairs of the bank. There is no evidence to show the complicity of the directors in the matter of the entries in the bills negotiated accounts. Further, if, as stated by the learned trial judge, the amount shown as advances in Schedule III were made for the purpose of accounting for the earlier misappropriations in Schedules II and V, we do not think that the loss sustained by the bank under this head can be surcharged against the directors in addition to their liability for the amounts in Schedule III. We, therefore, hold that the directors are not liable in respect of the amounts mentioned in Schedule V of the claim.

13. The third head of claim relates to the preparation and publication of false balance-sheets for the years 1954 and 1955, showing profits when the bank had actually incurred heavy loss. The amounts thus paid as dividends for the two years shown in Schedule IV of the points of claim total to Rs. 12,311"8l. The learned trial judge held that the balance-sheets for the years 1954 and 1955 were both false; but that the respondents Nos. 1 to 8 might not have known the real position that the bank was working at a loss during the year 1954. As far as the 1955 balance-sheet is concerned, the learned trial judge held that the directors (respondents Nos. 1 to 8) must have known about the misappropriations prior to November, 1955, and therefore the balance-sheet for 1955 was false and incorrect to the knowing of the directors. The learned judge noticed that there was no contention on behalf of the directors that the dividends declared in 1955 balance-sheet were not actually paid to, or received by, the shareholders, and that the onus was on the directors to prove that the dividends were not actually paid. We are relieved from considering the liability, if any, of the directors, in respect of the 1954 balance-sheet, as there is no appeal by the liquidator. But in respect of the 1955 balance-sheet, which alone is the subject-matter of the appeal before us, we are of the opinion that liability u/s 543 of the Act is attracted.

14. Exhibit D-39 is the memorandum and articles of association of the bank. Clause 120 of the articles of association 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 the above provision in exhibit D-39, and on the authorities, there can be little doubt that a declaration of dividend otherwise than out of the profits, and at a time when the bank was, to the knowledge of the directors, working at a loss, is an act ultra vires the directors. It was a case of misapplication of the bank's capital resulting in loss to the bank. For reasons we have elaborately discussed in the appeals against Application No. 1 of 1959 there can be little doubt that the directors were aware by the 2nd of July, 1955, of the financial bankruptcy of the bank. They were fully aware that on account of the misappropriations the bank had suffered heavy loss and that it was not in a position to declare profits or pay dividends. There is also evidence that Nilakanta Iyer (D.W. 2) who was the general manager of the bank since November 21, 1955, had recommended against the declaration of dividends for 1955 in his

draft proposals (exhibit D-47), that the 1st respondent corrected the draft proposal, and, contrary to it, proposed a declaration of dividend, which was accepted and passed by the board of directors. We agree with the learned trial judge that the liquidator having shown that there was a declaration of dividend, the burden is on the directors to show that the dividend thus declared had not actually been paid. This is so by reason of Section 45H of the Banking Companies Act, according to which, on the liquidator making out a prima facie case, the burden shifts to the directors (in this case) to disprove liability. We shall advert to the Section and to the arguments based on it later.

15. But, as already noticed by us in our judgment in the appeals against Application No. 1 of 1959, the 7th respondent was not present, and did not participate in the meeting of the board of directors held on March 30, 1956, at which the 1955 balance-sheet was passed and dividend was declared. We therefore hold that all the directors except the 7th respondent are liable u/s 543 of the Act for the declaration of dividend for the year 1955.

16. The fifth head of claim relates to the payment of Rs. 7,500 on February 13, 1956, to the 9th respondent on a promissory note and to the misappropriation of Rs. 10,000 being the fixed deposit amount of Sri Narayanaswami. The first of these relates to the last phase of repayment to the 3rd respondent by the 9th respondent of the " unaccounted money " of the former entrusted with the latter. We have discussed this transaction in detail in paragraphs 39 to 41 of our judgment in A. S. Nos. 137, 139, etc., of 1963. From the circumstances disclosed, which we have detailed in the said judgment and which we need not repeat, we hold that there is a clear misapplication of the bank's funds to the extent of Rs. 7,500 which was paid to the 9th respondent by his own cheque as manager of the bank. The payment was sanctioned by respondents Nos. 3 and 5. We have discussed the evidence in A. S. No. 137 of 1963, etc., and there is little doubt that this amount was paid to the 9th respondent at a time when the bank was in distress and the 9th respondent had landed himself in loss as a result of his satta transactions and was not in a position to repay. Rs. 7,000 out of this amount went in repayment of the dues of the 3rd respondent and the remaining Rs. 500 was credited to the account of the 9th respondent. The learned trial judge held the 3rd respondent liable for Rs. 7,000 as the said amount went directly into his pocket; and that the balance of Rs. 500 was liable to be paid by respondents Nos. 3 and 5 in equal motives as they were responsible for the loan. We see no reason to disturb the learned judge's finding on this account.

17. Regarding the fixed deposit amount of Sri. Narayanaswami, the learned judge recorded that the amount was misappropriated but the directors were not probably responsible for the same. As no appeal has been preferred by the liquidator, we need not canvass the finding any further.

18. The sixth head of claim regarding manipulations in the profit and loss account of the bank was found against by the learned trial judge, and, there being no appeal by the liquidator, we need not consider the matter any further.

19. This leaves us only with the first head of claim. The same relates to what has been described as irrecoverable advances, shown in Schedule I of the points of claim, and stated to have been made by respondents Nos. 9 and 10 to various parties. The pleading relating to this head of claim is contained in paragraph 5 of the points of claim which may usefully be extracted:

" The respondents Nos. 1 to 8 both inclusive and S. Damodara Pai, now deceased, who were the directors of the company did not exercise adequate control in the matter of advances of the company's funds to parties as they ought to have done. Consequently respondents Nos. 9 and 10 advanced large amounts to various parties without taking adequate securities for the advances and from whom it was and is not possible to recover the whole or a substantial portion of the said advances. Most of the said advances had become sticky. Yet the respondents did not make any enquiries as to the financial soundness of the persons to whom large amounts were advanced or the means of those people to repay. They did not take immediate action to recover the amounts. On the other hand, the board of directors ratified the aforesaid advances in their meeting held on November 10, 1955. By the aforesaid acts and omissions of the respondents loss has been caused to the company. A list of some of such advances together with the amounts likely to be unrealised out of the said advances is given in Schedule I hereto annexed. The respondents are jointly and severally liable to make good the loss to the company by way of compensation in respect of the misapplication, misfeasance and breach of trust. "

20. To the same effect are the recitals in paragraph I(a) of the summons. These were traversed by the various respondents, of which paragraphs 22 and 23 of the points of defence of the 1st respondent may be taken as representative. There was a general denial of the allegation that the Directors did not exercise adequate control in the matter of advances of the company's funds, followed by the plea that an executive committee had always been functioning for the purpose of sanctioning loans and that several loans sanctioned by the committee or by the supervisory director after his appointment had been granted only after a careful consideration of the circumstances. It was also pleaded that the 9th respondent was a person of large experience in banking business and the directors had no reason to distrust him. There was no specific denial of the allegations that the advances were irrecoverable or had been made without taking proper security. The learned judge noticed the liquidator's case that the advances in Schedule I were made without the sanction either of the board of directors or of the executive committee, and observed :

" It is not contended by the directors that any of these advances enumerated in Schedule I was made with the sanction of the board of directors or the executive committee. The directors did not make any such averment in their defences. In fact the 7th respondent admits in paragraph 4 of the points of defence that these advances were without proper authorisation. There is also no indication either in exhibit P-63, the minutes and proceedings of the board of directors, or exhibit

P-68, minutes of the executive committee, that these advances were made with the sanction either of the board of directors or of the executive committee. Therefore the liquidator's case that they were made without sanction appears to be justified. "

21. We may add that, in addition to the pleading of the 7th respondent, the 5th respondent as D. W. 3 deposed that practically all the advances made prior to the Reserve Bank's Report (exhibit P-62) were made without sanction. We have already noticed in our judgment in the appeals against Application No. 1 of 1959, that by proceedings of the board of directors dated September 6, 1953, the manager was to call a meeting of the executive committee at least once a month, and to act only on its orders in all matters of advances and credits. Counsel for the liquidator stated before us that all the advances in Schedule I except items I and 37 were made before the Reserve Bank's Report, exhibit P-62. Item 1 is an advance of Rs. 7,400 to the 9th respondent, and item 37 is an advance of Rs. 400 to P.W. 15. Both these were made when Nilakanta Iyer was the manager. Strictly, therefore, these would not be covered by the pleading which takes in only advances made by respondents Nos. 9 and 10 and not by Nilakanta Iyer. Leaving out these two items, as far as the remaining advances are concerned, it is clear from the pleadings, the evidence, and the stand taken by the directors before the learned trial judge, to all of which we have referred, that, one of the essential requirements to guarantee the prudence of the transactions, namely, the sanction of the executive committee, was wanting in regard to the Schedule I advances. Being so, the question whether the advances were made without proper scrutiny and whether the whole or any portion of them had become irrecoverable--apart from their bearing on the imprudence or impropriety of the transactions--seems to us to be more germane to the question of loss sustained by the bank. Counsel for the directors were at pains to point to us that the executive committee had reviewed many of these advances and directed that suitable action be taken in regard to them from time to time. For instance, attention was called to the minutes recorded in exhibit P-63, regarding the action taken by the committee on August 19, 1954, August 20, 1954, and October 26, 1954, in regard to item 3 of Schedule I; the proceedings dated January 14, 1954, in regard to item 4 ; the sanctioning of limits on February 4, 1954, regarding items 32 and 33 ; to the issuance of directions regarding items 8, 9, 10 and 11 by the proceedings of the executive committee on January 24, 1954; to the proceedings dated September 26, 1954, reviewing various items of advances, and such other matters. It was complained that these had escaped the attention of the learned trial judge. None of these, however, establish that the executive committee had initially sanctioned the advances or that the manager had acted on its orders in granting advances as required by proceedings of the board of directors, dated September 6, 1953, to which we have called attention. Whether these further steps taken by the executive committee to review the advances would go to mitigate the liability of the directors or to exculpate them altogether would be considered separately.

22. Even if the conduct of the directors in allowing the Schedule I advances to be made without proper sanction by their lack of effective supervision and control were to amount to misapplication or misfeasance, we find it impossible on the materials available on record to quantify the loss sustained by the bank on this account and to evaluate the liability of the directors. The loss under this head has been estimated by the liquidator at Rs. 4,76,747. The learned trial judge was of the view that the advances mentioned in Schedule I were not on adequate and proper security, were made by respondents Nos. 9 and 10 by reason of want of proper and adequate control by the board of directors, and that it did not appear that the directors took any effective steps to recover the advances even when they were told that some of them revealed sticky tendencies. We shall consider each of these aspects.

23. We have extracted the pleading in the points of claim about the absence of adequate control by the directors in the matter of advances of the bank's funds. The plea of the directors is that the executive committee had been authorised to sanction and review the loans, that the committee functioned effectively, and that the directors were on that account relieved from responsibility. It is also pleaded that the directors placed trust and confidence--as they were entitled to--in the 9th respondent, and therefore again they cannot be held liable for these advances. Neither of these contentions appear acceptable to us. It was accepted before us that by reason of Clause 105 of the articles of association (D-39), no less than by reason of regulation 71 of Table A of the Indian Companies Act, 1913 (the provision in the Travancore Act was also similar) the responsibility of managing the business of the bank is laid upon the directors. We do not think that the said responsibility can be got rid of altogether by a mere delegation in favour of an executive committee, or by blindly reposing confidence and trust in the 9th respondent. In our judgment in the appeals against Application No. 1 of 1959 we stated that 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 delegate, a delegation of powers would per se carry with it a denudation of responsibility. The least that the responsibility placed on the directors by statute and by the articles of association would require and expect them to do, is to see that the delegate or the confidant functioned properly and effectively. In the present case, we find that although it was recorded in exhibit P-58 that a meeting of the executive committee shall be called at least once a month to consider and review the advances, this was not followed in actual practice, especially at the later stages after 1954, We find again that early in 1954 the Reserve Bank had commented in exhibit P-62 report about the lack of supervision and control by the board of directors in the matter of granting advances and about the passivity of the committees constituted from time to time for sanctioning and reviewing the advances. It had also commented upon the undefined powers granted to the manager in the matter of advances and credits. The directors were aware of this report at least in July, 1954, and their action in not seeing that their resolution of

September 6, 1953, was properly implemented and that the manager was not given a free hand in the matter of advances amounts to a grave dereliction of duty on their part, and, in our opinion, to misfeasance. Our conclusion is strengthened by the fact that even when the irregularities and defalcations were disclosed to them in the end of July, 1955, the directors in the most perfunctory fashion, which we have detailed in our judgment in the appeals against Application No. 1 of 1959, ratified the whole series of advances in exhibit P-6I list. To a situation such as this, and to the facts disclosed here, we have held in our judgment referred to supra, that the principle in *Dovey v. Cory* [1901] A.C. 477 has no application.

24. The learned trial judge was satisfied from Schedule I and from exhibits P-73 and P-75, that the advances listed in Schedule I were not made on proper security. Exhibit P-73 dated December 19, 1961, is a statement made by the liquidator regarding the realisations made. The 7th respondent in appendix D to his points of defence showed the probable amounts that may be realised from the parties mentioned in Schedule I. This was answered by the official liquidator in exhibit P-75 statement. In the light of these, the learned judge held that he was inclined to hold that the advances were not on proper and adequate security. This finding has been assailed before us, and, as noticed earlier, our attention was called to the proceedings of the executive committee recorded in exhibit P-63, which showed that in the case of some at least of these advances, the executive committee had called for securities at a certain stage and had also directed action to be taken at a certain stage. For instance proceedings of the executive committee dated January 14, 1954, and September 17, 1954, were relied on to show that in respect of item 18 in Schedule I a limit of Rs. 10,000 was directed to be continued and an equitable mortgage of properties was probably taken. In regard to item 26 again, the insistence on title deeds from the party, as seen from the proceedings of the executive committee dated September 26, 1954, and October 26, 1954, were stressed. In addition to these, on the aspect of irrecoverability of the advances, it was pointed out that a detailed cross-examination had been directed of P.W. 3 and P.W. 22 and D.W. 3 to show that many of the advances mentioned in Schedule I cannot be regarded as irrecoverable. Above all, the liquidator's affidavit dated June 4, 1968, filed before us was relied on to show that a sum of Rs. 41,225 had been thus far realised by the liquidator out of what he characterised as irrecoverable advances.

25. On these aspects, which bear on the loss caused to the bank, the learned trial judge expressed himself thus :

" Last I come to the amount of loss sustained by the bank and the respective liabilities of the respondents. According to the liquidator, who is examined as P.W. 24, the loss comes to over Rs. 7,00,000, namely, the aggregate of the unrealisable advances shown in Schedule I of Rs. 4,76,746, the amounts withdrawn from other banks and misappropriated of Rs. 1,60,500 shown in Schedule II, the sum of Rs. 12,311 being the dividends declared, Rs. 61,800

being items 22 to 24 in Schedule V and the sum of Rs. 10,000 being the fixed deposit of Narayanaswami. Probably the last item may not be the direct result of the misfeasance of the directors because that amount could be discovered only if the directors looked into the accounts item by item. Similarly, the dividend declared for 1954 might also be excluded on my finding that the directors did not know that the bank was working at loss in 1954. All the other amounts, I am inclined to hold, are the result of the misfeasance and breach of trust committed by the respondents. In this case the misfeasance of the directors ultimately resulted in fraud as I have already indicated in Application No. 1 of 1959. Considering all the circumstances, I am inclined to think that the amount of loss be fixed at Rs. 6,50,000 being the amount claimed in Application No. 1 of 1959."

26. In our judgment in the appeals against Application No. 1 of 1959 we have already held that we cannot accept the finding of the learned judge quantifying the deficiency in the assets of the company to pay creditors in full at Rs. 6,50,000. Much the less can we accept the figure as a correct estimate of the loss caused to the bank by reason of the misfeasance, misapplication, etc., of the directors who are the appellants before us. It is a regrettable fact that there is not even formal evidence on the side of the liquidator of the loss occasioned to the bank, as a result of the acts of misapplication, misfeasance, breach of trust, etc., of the directors. The loss had not been estimated even in the pleading. On the pleading and the evidence, we cannot assess the loss caused to the bank as a result of the grant of irrecoverable advances specified in Schedule I.

27. We may also advert, in this connection, to an argument that has been advanced to us regarding the scope of Section 45H of the Banking Regulation Act. The Section reads :

" 45H. Special provisions for assessing damages against delinquent directors, etc.--(1) Where an application is made to the High Court u/s 543 of the Companies Act, 1956 (1 of 1956) against any promoter, director, manager, liquidator or officer of a banking company for repayment or restoration of any money or property and the applicant makes out a prima facie case against such person, the High Court shall make an order against such person to repay and restore the money or property unless he proves that he is not liable to make the repayment or restoration either wholly or in part :

Provided that where such an order is made jointly against two or more such persons, they shall be jointly and severally liable to make the repayment or restoration of the money or property.

(2) Where an application is made to the High Court u/s 543 of the Companies Act, 1956 (1 of 1956), and the High Court has reason, to believe that a property belongs to any promoter, director, manager, liquidator or officer of the banking company, whether the property stands in the name of such person or any other person as an ostensible owner, then the High Court may, at any time, whether before or after making an order under Sub-section (1), direct the attachment of

such property, or such portion thereof, as it thinks fit and the property so attached shall remain subject to attachment unless the ostensible owner can prove to the satisfaction of the High Court that he is the real owner and the provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to attachment of property shall, as far as may be, apply to such attachment. "

28. The words of Section 45H of the Act may be co-related to those occurring in Section 543(1) of the Companies Act, which may also be extracted:

" 543. (1) If in the course of winding up a company, it appears that any person who has taken part in the promotion or formation of the company, or any past or present director, managing agent, secretaries and treasurers, manager, liquidator or officer of the company-

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

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

the court may, on the application of the official liquidator, of the liquidator, or of any creditor or contributory, made within the time specified in that behalf in Sub-section (2), examine into the conduct of the person, director, managing agent, secretaries and treasurers, manager, liquidator or officer aforesaid, and compel him to repay or restore the money or property or any part thereof respectively, with interest at such rate as the court thinks just, or to contribute such sum to the assets of the company by way of compensation in respect of the mis-application, retainer, misfeasance or breach of trust, as the court thinks just....."

29. Based on these, the argument addressed to us was that the obligation of the liquidator to make out only a prima facie case and the burden thereafter on the delinquents proceeded against to disprove the liability can arise only when the relief claimed is repayment or restoration of any money or property of the company, and not compensation in respect of the misapplication, retainer, misfeasance or breach of trust. Going purely by the language of Section 45H of the Banking Regulation Act, the juxtaposition of the words occurring therein, and co-relating them with the words in Section 543 of the Companies Act, we are free to admit that the Section has not been artistically drafted. A plainer and simpler drafting was certainly possible. But, on the facts found by us, the argument appears quite academic. On the 2nd, 3rd and 5th heads of claim, we have found the directors, or such of them as are liable, guilty of mis-application of the bank's funds. We have also expressed, while dealing with the first head of claim, that it is not possible to assess the loss. On the 4th head of claim, we have held that the directors are not liable. On the 6th head of claim again, the trial judge found against the liquidator and there is no appeal before us. The result is that to the extent to which we have found the liability of the directors, the same can be rested on the ground of mis-application of the funds of the bank. Even on the argument of counsel for the directors, the special provision in

Section 45H of the Banking Companies Act is applicable to a case of mis-application of the bank's funds. Having regard to the conclusion that we have come to in these appeals that the directors to the extent to which they or any of them are liable are guilty of mis-application of the funds of the bank, Section 45H is attracted. It is therefore unnecessary for us to consider in these appeals whether Section 45H covers only the cases covered by Section 543(I)(a) of the Companies Act 1956, and does not cover the cases contemplated by Clause (I) (b) thereof.

30. In the result, we record our findings as follows :

(1) On the first head of claim we find that the liquidator has not proved the loss caused to the bank by reason of the irrecoverable advances listed in Schedule I and therefore is not entitled to succeed on this head of claim ; (2) On the second head of claim we find that the directors were parties to the falsification of the bank's accounts by making entries relating to the fictitious advances shown in Schedule III for the purpose of covering up the misappropriations effected by withdrawal of the bank's monies from its account with other banks as shown in Schedule II. We find the loss caused to the bank under this head to be, as stated in Schedule III, a sum of Rs. 1,99,000. Respondents Nos, 1 to 8 will be jointly liable for this amount. Having regard to all the circumstances, and to the proviso to Section 45H of the Banking Regulation Act, we fix the several liability of these respondents for this head of claim at Rs. 40,000 each. We make it clear that the total amount recoverable under this head of claim will in no event exceed Rs. 1,99,000 ; (3) On the third head of claim, we find that all the directors except the 7th respondent are responsible for the preparation and acceptance of the false balance-sheet for the year 1955 showing profit and declaring dividends when the bank was, to their knowledge, working at a loss. The loss incurred by the bank under this head as shown in Schedule IV is Rs. 6,155-12-5. We hold respondents Nos. 1 to 6 and 8 jointly and severally liable for this amount; (4) On the fourth head of claim, we find that the directors are not liable for the manipulations in the bills negotiated accounts, shown in Schedule V ; (5) On the fifth head of claim, we find that the 3rd respondent and the 5th respondent are liable for the total amount of Rs. 7,500 given as loan to the 6th respondent on February 13, 1956, of which the 3rd respondent is liable for Rs. 7,250, and the 5th respondent for the balance amount of Rs. 250,

31. In the result, in modification of the decree passed by the learned trial judge, there will be a decree in the following terms:

(1) That respondents Nos. 1 to 8 do jointly contribute to the assets of the bank a sum of Rs. 1,99,000 in respect of the second head of claim ; and that each of them be severally liable under this head for Rs. 40,000, the liquidator not being in any event entitled to recover more than Rs. 1,99,000 under this head of claim.

(2) That respondents Nos. 1 to 6 and 8 be jointly and severally liable to contribute to the assets of the bank Rs. 6,155-12-5, being the dividend

wrongfully declared for the year 1955.

(3) That the 3rd respondent be liable to contribute a further sum of Rs. 7,250 to the assets of the bank under the fifth head of claim, and the 5th respondent be similarly liable to contribute Rs. 250 under the same head of claim.

(4) That in other respects the decree of the learned trial judge in so far as the same is against respondents Nos. 1 to 8 do stand vacated.

(5) That the parties do bear their respective costs throughout.