

(1964) 05 SC CK 0012
In the Supreme Court Of India
Case No : Appeal (civil) 113 OF 1960.

Naini Gopal Lahiri and Others

APPELLANT

Vs

State of Uttar Pradesh

RESPONDENT

Date of Decision : 08-05-1964

Acts Referred:

Companies Act, 1913 — Section 77(2)
Penal Code, 1860 (IPC) — Section 120B, 34, 406, 408, 409

Citation : (1965) 35 CompCas 30

Hon'ble Judges : P. B. Gajendragadkar, C.J.; Raghubar Dayal, J.; M. Hidayatullah, J.; K. C. Das Gupta, J.; J. C. Shah, J

Bench : Full Bench

Final Decision : Allowed

Judgement

Shah, J.—On November 13, 1946, the United Hindustan Films Ltd. was incorporated as a public limited company with its head office at Calcutta, " to carry on the business of cinematographic trade and industry and particularly the film industry both silent and talkie, ... to manufacture and deal in educational films, commercial and agricultural pictures and to purchase films or to take on hire films from other film producers." By Clause 31 of the memorandum of association, the company was authorised to employ brokers, commission agents and underwriters for sale of shares and debentures and to provide for their remuneration. The articles of association provided that the company may pay a commission for subscribing or agreeing to subscribe for any shares or agreeing to procure subscribers for any shares, but so that the commission in respect of the shares shall not exceed ten per cent. of the shares subscribed or to be subscribed. The articles also provided that " Messrs. Eastland Trust"--a firm--will be appointed managing agents for a period of twenty years with authority, inter alia, to appoint underwriters on a commission of ten per cent. on sale of shares of the company sold directly or through brokers or agents appointed by them.

2. On November 30, 1946, the prospectus of the company was filed with the

Registrar, Joint Stock Companies, West Bengal. On December 2, 1946, Ram Kishore Chatterji, the third appellant in this appeal, applied to the managing agents of the company offering the services of Messrs. Chatterji and Co. of which he was a partner as underwriters of the company. By letter dated December 9, 1946, Messrs. Chatterji and Co. were informed that the application had been placed before the board of directors and it had been decided to appoint Messrs. Chatterji and Co. as underwriters of the company. A formal contract was then executed. At a meeting of the board of directors held on June 21, 1947, the appointment of Messrs. Chatterji and Co. as underwriters of the company with a commission of ten per cent. on the face value of the shares sold by them was confirmed.

3. The activities of the company were restricted to the area of the District of Benaras and neighbouring districts. Sheo Prasad Sharma, appellant No. 2, was appointed managing director of the company's branch at Benaras. He also worked as branch manager of the Bengal Express Bank at Benaras. Ram Kishore Chatterji, appellant No. 3, was a part-time clerk of the company at Benaras and also worked as accountant of the Bengal Express Bank at Benaras. The first appellant, Naini Gopal Lahiri, was working as a clerk in the Traffic Accounts Office, East Indian Railway, at Benaras during the period 1946-47.

4. Many persons residing in the District of Benaras purchased shares of the company. In a complaint addressed to the Home Minister, Uttar Pradesh, some time in the year 1951, it was alleged that office-bearers of the company including the appellants had made false representations to the public that the company intended opening a cinema house at Benaras and that the venture was likely to yield large profits, and relying upon the representations the public were induced to purchase shares of the company. Investigation was directed into this complaint and a police report was submitted against the three appellants and eight others in the court of the Magistrate, Ist Class, Benaras, charging them with offences of conspiracy to commit cheating, criminal breach of trust, falsification of accounts and alternatively of committing those offences in furtherance of the common intention of the accused. The case was tried before the Court of Session on charges against the accused for offences u/s 420 read with Section 34 of the Indian Penal Code and also for offences under Sections 406, 408, 409, 417, 465, 471, 477A read with Section 120B of the Indian Penal Code. The Sessions Judge, Benaras, convicted the appellants and two others, B. B. Biswas and R.C. Moitra, of offences under Sections 417, 420, 409, 465, 471 and 477A read with Sections 120B and 34 of the Indian Penal Code and sentenced them to suffer imprisonment for various terms.

5. In appeal to the High Court of Allahabad, the order of conviction and sentence passed against B. B. Biswas and R. C. Moitra was set aside. The High Court also set aside the conviction of the appellants, Naini Gopal Lahiri, Sheo Prasad Sharma and Ram Kishore Chatterji for offences under Sections 417, 465, 471, 477A and 409 read with Section 120B and Section 34 of the Indian Penal Code,

but maintained the order of conviction for offences u/s 420 read with Section 34 of the Indian Penal Code on the charge of cheating in a sum of Rs. 6,680 paid by the company to Messrs. Chatterji and Co. as commission under the underwriting agreement. The High Court confirmed the sentences passed by the Court of Session for that offence. With special leave, the three appellants have appealed to this court.

6. The only question which falls to be determined in this appeal is whether, on the findings recorded by the High Court, the appellants are proved to have committed, in furtherance of their common intention, the offence of cheating the company, and thereby inducing it to part with Rs. 6,680 as commission under the underwriting agreement. By the ninth head of charge framed by the Court of Session the appellants, Sheo Prasad Sharma, R. K. Chatterji and R. C. Moitra (who was acquitted by the High Court), were charged with having dishonestly or fraudulently induced the company to pay share commission in the sum of Rs. 6,630 with the knowledge that by that act wrongful loss was likely to be caused to the shareholders on the basis of a fictitious " deed of underwritership " which those three persons knew or had reason to believe to be fictitious. Separate charges were also framed against the appellants for criminal breach of trust in respect of Rs. 6,989-6-0, which included Rs. 6,680 paid as underwriting commission. The foundation of the charge for the offence u/s 420 read with Section 34 of the Indian Penal Code was that Sheo Prasad Sharma, R. K. Chatterji and R. C. Moitra had by setting up a " fictitious deed of underwritership " dishonestly or fraudulently induced the company to pay underwriting commission and had thereby caused wrongful loss to the shareholders. The three named accused were called upon to meet the case that by setting up an underwriting agreement in favour of Messrs. Chatterji and Co., which was a sham or " fictitious deed ", the company was induced to pay Rs. 6,680 as underwriting commission to Messrs. Chatterji and Co., which was not payable to that firm.

7. The High Court, for reasons, which we will presently set out in detail, held this charge proved. But somewhat inconsistently the High Court, instead of convicting R. C. Moitra who was named in the charge as a person concerned in the offence of cheating in the matter of the underwriting commission with the two appellants, R. K. Chatterji and Sheo Prasad Sharma, convicted the appellant, Naini Gopal Lahiri, of the offence punishable u/s 420 read with Section 34 of the Indian Penal Code. The High Court acquitted R. C. Moitra and B. B. Biswas, and convicted the appellants of the offence of cheating. In so recording its judgment, the High Court appears to have fallen into some error : there was no charge against B. B. Biswas for the offence punishable u/s 420 read with Section 34 of the Indian Penal Code, nor was there any charge against N. G. Lahiri for that offence.

8. Apart from this infirmity, the judgment of the High Court is otherwise unsustainable. The material findings recorded by the High Court in the light of the evidence may be set out. The High Court declined to place any reliance upon

the testimony of Dr. S. K. Moitra, the approver, on whose testimony apart from some documentary evidence the prosecution primarily relied for establishing its case generally. The High Court held that the evidence did not establish the case of the prosecution that the funds of the company were misused and that the State had failed to establish that the real purpose for the formation of the company was to finance the Bengal Express Bank, which it was alleged was a moribund company. The High Court also held that the story about the fraudulent representations alleged to have been made in pursuance of a criminal conspiracy in the prospectus of the company so as to induce shareholders to subscribe to the share capital was not established, and that the charge for the offence u/s 417 of the Indian Penal Code in respect of certain shares alleged to have been purchased by three ladies, Shaila Bala, Sabita Devi and Surja Bala, was also not made out. The only charge, which, in the view of the High Court, was proved was one relating to fraudulent and dishonest inducements made to the company to pay Rs. 6,680 as commission pursuant to the underwriting agreement. But the High Court found that the case of the State, that the underwriting agreement was a " sham or fictitious " agreement, was not made out. By the memorandum of association Messrs. Eastland Trust were appointed as managing agents and power was conferred upon them to appoint underwriters. Such an appointment was, in the view of the High Court, made by a written agreement. The Court of Session held that this was a sham document brought into existence to support a fraudulent claim for commission which the company was not bound to meet. The underwriting agreement was in the view of that court a sham transaction which was never intended to be operative : it was merely used as a cloak by the three appellants with a view to induce the company to pay commission which the company was not bound to pay. On this view, the Court of Session convicted the three appellants of the offence of cheating u/s 420 read with Section 120B of the Indian Penal Code and also for the offence u/s 409 read with Sections 120B and 34 of the Indian Penal Code.

9. But the High Court took a different view. The High Court held that the underwriting agreement was not " sham or fictitious ". They pointed out that under the articles of association, Messrs. Eastland Trust had been specifically mentioned as managing agents of the company for a period of twenty years, that the managing agents were authorised to carry on the business of the company subject to the supervision and control of the board of directors and they were empowered to pay underwriting commission of ten per cent. on sale of shares sold directly or through agents appointed by the underwriters. It could not be said that Messrs. Eastland Trust--the managing agents--had not come into existence on the date of incorporation of the company ; in fact Messrs. Eastland Trust had started functioning as managing agents from the date on which the company was incorporated as a joint stock company. The managing agents had full authority to appoint underwriters, and they did in fact appoint Messrs. Chatterji and Co. as underwriters. Therefore, there was nothing illegal or improper about the appointment of Messrs. Chatterji and Co. as underwriters.

There was also no evidence led by the State showing that R. K. Chatterji was connected with Messrs. Eastland Trust or their partners, nor had the managing agents any "oblique motive in making their appointment". The High Court inferred from these circumstances that the agreement was not a "fictitious" agreement. But the High Court still held that R. K. Chatterji was a person of no means and under the cloak of his appointment Lahiri, the first appellant, and Sharma, the second appellant, exploited the underwriting agreement to their own advantage, by selling the shares themselves and manipulated things in such a way that, although underwriting commission was debited as paid to Messrs. Chatterji and Co., a substantial part thereof was received by them. The High Court relied in support of this argument that the appellants, Lahiri and Sharma, and one Banerjee were canvassing for sale of shares and were receiving share application money on behalf of the company and the evidence disclosed that out of 1,100 applications for shares not one bore the signature of R. K. Chatterji as agent of the underwriters, nor were any other applications shown to have been made in which Messrs. Chatterji and Co. had acted as underwriters. The High Court observed that the shareholders who were examined as witnesses had deposed that they had purchased shares from Lahiri, Sharma and K. L. Banerji and that R. K. Chatterji had not negotiated the sale of the shares to them. From this the High Court inferred that in reality shares were sold by Lahiri and Sharma and not by Chatterji. The High Court also relied upon two documents, exhibits Ka-989 and Ka-534, recovered in the course of investigation which recorded that the underwriting commission paid to Messrs. Chatterji and Co. was divided as recorded in the account head " P/L Account Commission. " In the view of the High Court the two documents disclosed that Lahiri, Sharma and Chatterji were sharing the share commission. On this evidence, the High Court recorded its findings as follows :

" I have no doubt in my mind that R. K. Chatterji was merely acting as a conduit pipe for the purpose of enabling S. P. Sharma and N. G. Lahiri to make unlawful gains by realising commission from the company. It is conceded that both S. P. Sharma and N. G. Lahiri could not have directly taken part in the sale of shares so as to earn share commission from the company. Both of them were directors of the company, and, as such, could not have participated in the business transactions of the company. As directors they stood in fiduciary relationship with the shareholders and the public and, therefore, they could not directly and openly earn profits on the sale of shares. It was to obviate this difficulty that they employed a camouflage and took advantage of the existence of the underwritership agreement in favour of Chatterji and Company. The evidence in the case makes out that not only S. P. Sharma and Lahiri but even some of the shareholders of the company had been participating in the sale of shares and thereby earning commission on their own account. All this could have been possible only with the concurrence and connivance of S. P. Sharma and Lahiri who were the brain trust of the company at Benaras, which was the main center of activity of the company."

10. The High Court inferred that the illegal acts committed by the three appellants were committed by them in furtherance of their common intention to cheat the company of the share commission, and convicted them of offences punishable u/s 420 read with Section 34 of the Indian Penal Code. The High Court also observed that the Court of Session had recorded the order of conviction against the appellants, Sharma, Lahiri and Chatterji and also Moitra, for the offence punishable u/s 420 read with Section 34 of the Indian Penal Code in that they were proved to have committed the offence of criminal breach of trust in respect of underwriting commission obtained by cheating the company, but once a conviction was recorded for the offence of cheating, it would be anomalous to convict the same person of the criminal breach of trust on the same facts.

11. As we have already observed the foundation of the charge u/s 420 read with Section 34 of the Indian Penal Code was that relying upon the fictitious underwriting agreement the company was made to part with the underwriting commission. The High Court reached that conclusion in three steps: first, that the directors of the company were not entitled to participate in the sale of shares; second, that even though there was a genuine agreement in favour of Messrs. Chatterji and Co. appointing them as underwriters of the company, in fact nothing was done by Chatterji and Co.; and third, that the shares were sold by Lahiri, Sharma and others and the commission which was nominally paid over to the underwriters was shared between Lahiri, Sharma and R. K. Chatterji:

We may usefully refer to the terms of the underwriting agreement:

" Name of underwriter--Messrs. Chatterji and Co. Address 6/8/48, Sonapura, Benaras. Place of business. Throughout India.

Date of appointment. (Nil).

Terms and conditions are as below :

- (1) that you guarantee a business worth Rupees one lakh within a year,
- (2) that you will receive a commission of ten per cent. on the face value of shares,
- (3) that you will receive your commission from time to time when the allotment money due on your business have been received by the company,
- (4) and that you are authorised to appoint any number of ordinary, special and district agents to procure business. "

12. It is clear from these terms that Messrs. Chatterji and Co. had agreed to underwrite business of Rs. 1 lakh " within a year ", i.e., to procure other persons to subscribe for shares of the value of Rs. 1 lakh or to purchase the shares of that value. The underwriters were expressly authorised by the underwriting agreement to appoint ordinary, special and district agents to procure business. An underwriter is a person who agrees with the company in consideration of a

commission payable to him, that if all or a particular number of the company's shares are not taken up by the public, he will make up the deficiency and make up the total number of shares underwritten by him. Underwriting is in the nature of an insurance against the possibility of inadequate subscription. A public company cannot proceed to allot shares offered to the public, unless the amount specified in the prospectus as the minimum subscription is raised by the issue of shares. It is therefore usual for a new company to enter into an underwriting agreement. An underwriter is entitled to enter into subsidiary agreements with which the company is not concerned. They are not required to be disclosed in the prospectus.

13. It is recorded by the High Court that it was conceded that the directors were not entitled to canvass " directly " for sale of shares of the company. We think that such a concession can have no value. Counsel appearing on behalf of the State very fairly did not contend that the concession is based on the true legal position. We fail to appreciate why a director is not entitled to participate in canvassing the sale of shares. There is nothing in the underwriting agreement which prevented the directors or others from acting as agents for Chatterji and Co. in canvassing the sale of shares. The underwriting agreement being a contract that the underwriter will either himself purchase or procure purchasers for the shares underwritten by him, it is no concern of the company as to how the underwriter procures the purchasers. On the findings recorded by the High Court it is clear that the underwriting agreement was genuine, and commission was in fact debited to Chatterji and Co. for shares subscribed by the public. It is true that according to the High Court, in the applications for shares submitted by the public the underwriters did not figure, and the work of canvassing was mainly done by Lahiri, appellant No. 1, Sharma, appellant No. 2, and others. This may give rise to two alternative inferences consistent with probabilities:

(1) that the canvassers acted as agents of the underwriters who were expressly authorised to appoint agents;

(2) that the underwriters after obtaining the agreement for some reason remained supine, and other persons independently of them canvassed shares, and then the underwriters made a fraudulent representation that the shares purchased by the public were covered by the underwriting agreement, and obtained payment.

14. If the first be a legitimate inference, no offence of cheating can be deemed to be made out. The High Court, it appears, raised the alternative inference and convicted the appellants. But it must at once be noticed that there was no charge against the appellants or any of them, that they made a representation that the shares sold by the efforts of the directors were sold through the agency of the underwriters, and thereby they induced the company to pay to Chatterji and Co. commission which they were not entitled to. The charge, it may be recalled, was that the company was induced to pay the underwriting commission on the faith of an agreement which was " fictitious. "

15. Section 415 of the Indian Penal Code, which defines "cheating", provides:

" Whoever, by deceiving any person, fraudulently or dishonestly induces the person so deceived to deliver any property to any person, or to consent that any person shall retain any property, or intentionally induces the person so deceived to do or omit to do anything which he would not do or omit if he were not so deceived, and which act or omission causes or is likely to cause damage or harm to that person in body, mind, reputation or property, is said to ' cheat'. "

16. The definition consists of two parts. A person who induces another to deliver any property to any person, or to consent that any person shall retain any property, is said to cheat, if he does so fraudulently or dishonestly. Similarly a person who deceives another and intentionally induces that person to do or omit to do something, which he would not have otherwise done or omitted to do is also said to cheat, if the act or omission causes or is likely to cause damage to him. In the first, the offender may induce the victim to deliver any property to another, or to consent that any person shall retain property. In the second, the offender may induce the victim to do or omit to do something which, but for deception, he would not do or omit to do. Under the first part the inducing must be fraudulent or dishonest ; under the second, it must be intentional. But the gravamen of the offence common to both the parts is the deceiving of the victim, that is, the victim must by representation be made to believe as true, what is not true, and which the offender knows or has reason to believe is not true. The representation may be express, or may be inferred from conduct. But mere deception is not sufficient: the victim in consequence of the deception must be induced to act to his prejudice, and the offender must, in offering the inducement, have the specified mens rea.

17. The charge of fraud, by the Court of Session, apart from the infirmity set out earlier, does not refer to any deception of the company. There is no mention of any representation made to the company; and these defects are not technical, but of substance. Our attention is not invited to any specific evidence of representation, express or by conduct, which deceived the company, nor has the High Court recorded any finding in that behalf. The vouchers submitted by Messrs. Chatterji and Co., claiming payment of underwriting commission, have not been produced before the court. Only receipts for payment of commission made to Chatterji and Co. are produced. Unless there was a representation which deceived the company, and the company was induced fraudulently or dishonestly to part with property, the offence of cheating could not be deemed to be committed. Chatterji and Co. had undertaken to procure purchasers for shares of the value of Rs. 1 lakh within one year. Assuming that they claimed commission in respect of the shares which were sold by other persons, it could not be said merely on that account, that the company was deceived and it was induced dishonestly or fraudulently to part with the amount of commission.

18. The view expressed by the High Court that the directors were incompetent to act for the purpose of canvassing for sale of shares is wholly unsustainable, and

proof of the mere fact that under an existing binding agreement between Messrs. Chatterji and Co. for underwriting the shares, commission was paid to them for shares in the sale of which Lahiri and Sharma were concerned, will not establish the case of cheating, for there is complete lack of evidence both about the deception practised and the inducement of the company with the requisite intention to pay commission to Chatterji and Co.

19. Counsel for the State sought to contend that deception was practised by the managing agents by submitting a statutory report u/s 77(2) of the Indian Companies Act, 1913, mentioning that no appointment of underwriters was made. No such case was, however, set out in the charge, nor at any stage in the trial court or even before the High Court, and we cannot go into that question. This, if established, would be a charge of cheating entirely different from the one found in the charge, and may necessitate enquiry on several matters of fact which has not been made.

20. Counsel for the State also sought to contend that the High Court was in error in concluding that the underwriting agreement was a genuine agreement, and not fictitious as found by the Court of Session. The High Court has, however, marshalled in its judgment evidence which shows that the agreement was genuine and we do not think, in an appeal by the accused under Article 136 of the Constitution, we would be justified in interfering with the conclusion of the High Court on that point.

21. Counsel for the State finally contended that in any event this court may on the findings recorded by the High Court convict the appellants of the offence u/s 509 read with Section 34 of the Indian Penal Code i.e., of the offence of committing criminal breach of trust of the company's funds in furtherance of their common intention. But in relation to the payment of commission on the shares underwritten a charge u/s 409 read with Section 34 of the Indian Penal Code was expressly framed and all the three appellants were convicted of that offence by the Sessions Judge. The High Court acquitted the appellants of that offence and no appeal has been filed by the State challenging the correctness of that decision. It was open to the State to apply for leave to appeal against the order of acquittal passed by the High Court, but they took no steps in that behalf. We will not, in the circumstances, be justified in entertaining the plea of the State and in calling upon the appellants to answer at this date a charge of criminal breach of trust for which they have already been tried and acquitted. Without considering, therefore, whether in an appropriate case the appellate court may have the power in an appeal against an order of conviction of cheating to convert it into one for the offence of criminal breach of trust, we are definitely of the view that this is not a case in which, assuming that we have the power, it may be exercised.

22. The appeal is therefore allowed and the three appellants are ordered to be acquitted of the offence u/s 420 read with Section 34 of the Indian Penal Code, The fine if paid is to be refunded.