

(1965) 04 KL CK 0001

In the High Court Of Kerala

Case No : Application No. 247 of 1963 in B.C.P. No. 11 of 1960

Official Liquidator, Palai Central Bank Ltd. (in liquidation),
Ernakulam

APPELLANT

Vs

K. Joseph Augusti, Kayalackakam House, Palai and Others

RESPONDENT

Date of Decision : 02-04-1965

Acts Referred:

Banking Companies Act, 1949 — Section 45H(1), 450(2)
Companies Act, 1913 — Section 235, 235(1)
Companies Act, 1956 — Section 205, 291, 543
Limitation Act, 1908 — Section 3

Citation : AIR 1966 Ker 121

Hon'ble Judges : P.T. Raman Nayar, J

Bench : Single Bench

Advocate : K.V. Surianarayana Iyer and C.M. Bevan, for the Appellant; T.S. Krishnamoorthy Iyer, (for No. 1), K.T. Thomas, (for No. 2), Joseph Vithayathil, George Vadakkal, M.A. Joseph and Varghese Kalliath, (for No. 3), K.P. Abraham, George Kurian, K.P. Pathrose, E.M. Jacob, K.K. Poullose and M. Pathrose Mathai, (for No. 4), P.K. Kesavan Nair, K.N. Narayana Pillai, (for No. 5), V. Rama Shenoi, K.R. Raya Shenoi, (for No. 6), M. Ramanatha Pillai, (for No. 7), N. Parameshwaran Moothathu, v.N. Subramania Iyer and G.R. Menon, (for No. 8), S. Narayanan Potti, N.K. Varkey, (for No. 9) and V. Sankara Menon, (for No. 10), for the Respondent

Judgement

P.T. Raman Nayar, J.—By this application, brought u/s 543 of the Companies Act read with Section 45H of the Banking Companies Act, the Official Liquidator of the Patal Central Bank Ltd. seeks to recover about Rs. 250 lakhs from the ten respondents, former directors and officers of the banking company.

2. The company was incorporated in 1927; on the 5th of December 1960 it was ordered to be wound up on an application made by the Reserve Bank of India on the 8th August 1960 (on which very day a provisional liquidator was appointed) u/s 88(3) (b) (iii) of the Banking Companies Act; and it was on the 4th April 1963, that the liquidator Instituted the present application. The company is an

insolvent company. Its paid up capital amounts to nearly Rs. 25 lakhs; its outside liabilities to about Rs. 1007.50 lakhs; the realisations up to date to a little over Rs. 700 lakhs; future realisations are estimated at about Rs. 40 lakhs; and so, allowing for the expenses of the liquidation, the expected deficit, leaving out of account the share liability, is in the neighbourhood of Rs. 265 lakhs.

3. Respondents, 1, 2, 3, 4 and 7 were directors of the hank when the provisional liquidator took charge on the 8th August 1960. The 1st respondent was the managing director from the very beginning, i.e., from the 26th January 1927, till the 1st April 1960 when he ceased to be the managing director and continued as an ordinary director. The 2nd respondent was a director from the beginning till the end; and from 1987 to 1951 he was also functioning as the manager of the Madras Branch of the bank, as a paid manager till the 1st January 1955 and thereafter in an honorary capacity. The 3rd respondent was a director from the 23rd December 1938, and the 4th respondent from the 14th January 1985, both till the end. The latter was also a salaried officer of the bank under the designation, Special Attorney, from 1938 to 1955. The 5th respondent was a director of the hank from the 30th March 1940 till the 12th August 1943, and again from the 10th July 1947 till the 29th December 1954. He was, in addition, a salaried officer of the bank from 1933 till the end--he was attached to the head office of the bank from 1949 till the end, from the 1st January 1956 onwards as office manager. The 6th respondent was a director of the bank from the 12th August 1943 till the 28th March 1956. He was also a as salaried officer from the 18th August 1948 till] the end. The 7th respondent was a director of the hank from the 5th February 1955 till the end while the fifth respondent was its auditor from the 8th January 1947 till the end. The 9th and 10th respondents were salaried officers of the bank, the former from the 22nd October 1937 till the 1st August 1958 and the latter from the 16th May 1949 till the end.

4. Respondents 2 and 4 are brothers and the former is the son-in-law of the 1st respondent. The 7th respondent is the 1st respondent's brother's son. Respondents 5, 6 and 10 are brothers. They are the first cousins of the 1st respondent, being the sons of the 1st respondent's father's brother.

5. The claim is brought under four heads A, B, C and D. Claim A which accounts for over Rs. 240 lakhs is in respect of bad and irrecoverable advances; Claim B which amounts to over Rs. 21.6 lakhs is in respect of taxes and dividends paid for the years 1936 to 1949 as income and profits not really earned but made to appear as earned by falsifying the balance sheets and profit and loss accounts, fictitious entries being made in the books for this purpose; Claim C amounting to nearly Rs. 25.fi lakhs is in respect of similar payments for the years 1950 to 1658, the only difference being that the false income and profits were made to appear by debiting interest, which there was no prospect of ever realising, on the bad and irrecoverable advances in Claim A, credit being taken in the profit and loss account; and claim D which is for Rs. 15,000/- is in respect of unauthorised appropriation of the company's assets.

6. Points of claim have been delivered setting out with great particularity the charges levelled against each of the respondents and the allegations in support of the charges. The respondents have submitted points of defence and the liquidator has filed a replication.

7. Apart from an affidavit filed by the liquidator showing the steps taken by him for the recovery of the advances in Claim A and the results thereof, the evidence in the case consists exclusively of the books of account and other documents of the bank. These documents numbering over 2000 have all been marked by consent; in fact, many of them were produced at the instance of the respondents to whom all the books and records of the bank in the hands of the liquidator were made available for inspection; the facts stated in the documents marked are not controverted; and hence there seems to be no necessity for recourse to Section 45-F of the Banking Companies Act.

8. The liquidator, it is said, has no information apart from what he has been able to gather from the books and other documents of the bank, and in any case, he has been unable to find any witness to speak to any facts other than those disclosed by these documents. The respondents have not thought it necessary to get into the box or even to file affidavits in order to explain away or otherwise meet the charges levelled against them.

9. Claim B being in no way dependent on the remaining claims I have taken it up for adjudication first--See my order dated 2-12-1964. I thought that advisable having regard to the magnitude of the case. The hearing in respect of claim B has been completed and I am proceeding to pronounce on it; the hearing in respect of the remaining claims is continuing.

10. The respondents have taken the plea of limitation and I shall consider that plea first, The facts complained of, namely, the payment of taxes and dividends for the years 1936 to 1949 which are the subject-matter of claim B took place between 1937 to 1960. The defence is two-fold. First, that since a suit for recovery of the amounts in question was completely barred under Article 36 of the Indian Limitation Act, 1908 (which it is assumed is the proper article to apply) and the corresponding article of the Travancore Act before Section 45-0 of the Banking Companies Act, giving a longer period of 12 years, came into force on 30-12-1953, the present application for the same relief is necessarily barred; and the second, in case the first fails to gain acceptance, that since an application of the present nature had become barred in respect of acts committed before 1-10-19-17, at any rate so far as the director-respondents are concerned, under the old Section 45-0 of the Banking Companies Act, before it was replaced by the new Section 45-0 on 1-10-1959, and there being nothing in the new Section 45-0 giving it retrospective application so as to revive a barred claim, the application to that extent, remains barred. A like argument is advanced (on behalf of all the respondents) in respect of the earlier portions of the claim which, it is said, had become barred by the law of limitation for the time being in force.

11. I shall begin by stating and examining three related and familiar propositions of the law of limitation so familiar as to be almost commonplace, and for that very reason, in danger of being overlooked or misapplied. The first is the elementary proposition that, except by the operation of provisions like Section 28 of the Indian Limitation Act, 1908, I shall for purposes of illustration refer to the more familiar provisions of that Act which have repeatedly come before the courts rather than to those of the new Act of 1963--limitation does not extinguish the right but only bars the remedy. Here the word, "right" is used to mean a primary or substantive right, and the proposition is true only if the word is understood in that limited sense. For, a remedy is also a right in the wider sense of the word, a sanctioning or secondary right, a remedial or procedural right as it is often called, and limitation does undoubtedly extinguish such a right, though, subject to the qualification already mentioned, leaving the substantive right unaffected of course, the remedy can be revived -- re-created, would perhaps be the better word to use--by a law for the purpose, just as any other right, including a substantive right, can be so created.

But, in so far as the particular remedial right to which it applies is concerned, limitation undoubtedly extinguishes the right. It is, however, important to remember that limitation extinguishes only the particular remedial right which is its victim and that, since it leaves the substantive right unaffected, that right can still be enforced in other ways, if other ways are available, not merely indirectly by the enforcement of lien or by obtaining a fresh promise, or by reason of payment notwithstanding the bar being safe from recall, but also in a positive and direct manner. Thus, it might well be that there is more than one legal remedy available for the enforcement of the same substantive right. There must be many examples of this, but the example that occurs to me readily is the right of a purchaser in execution to obtain possession of the property bought by him. That is a substantive right for the enforcement of which two different remedies are available. He can either make an application under O. XXI Rule 95 of the Code or institute a suit for possession. (I shall assume that he is a stranger purchaser so as to avoid the possibility of Section 47 of the Code being a bar to a suit).

The application would fall within Article 180 of the Limitation Act--I am as I have said, referring to the provisions of the 1908 Act, not the 1963 Act--and would have to be made within three years of the sale becoming absolute. But the suit falling as it does under Article 138, could be brought within 12 years of the sale becoming absolute, and, if brought after three years, would not be barred by reason of the other remedy for the enforcement of the same substantive right, namely, an application under Order XXI Rule 95, being barred. Nor (forgetting for the moment Article 28 of the Limitation Act which is not relevant to the argument) would an application be barred because a suit had become barred, the period of limitation for a suit expiring earlier as well might have been if the starting point for limitation under Article 138 were, as in the Act of 1887, the date of the sale and if, by reason of the tendency of an application under Order

XXI Rule 90 or some other cause, the sale was confirmed only more than nine years after it was effected.

12. The second proposition has already been stated by me in examining the first. It is that, if a remedy becomes barred under the law of limitation in force at the time, a subsequent change in the law giving a longer period of limitation will not by itself, in the absence of provision for the purpose, revive, or rather, re-create the remedy. (Section 2 of the Limitation Act of 1877 and Section 31 (a) of the Act of 1963 recognize and declare this principle deducible, I think, from Section 6 of the General Clauses Act, when they expressly disclaim any intention to revive any remedy already barred under the statutes which they replaced). The particular remedial right is extinguished and can be re-created only by a law for the purpose. But the substantive right and other remedial rights, if any, for its enforcement remaining unaffected, these remedial rights can be exercised so long as they are not barred by time.

13. The third proposition is that the law of limitation to apply is the law in force at the time the proceeding in question is instituted. This, I think, is because limitation is something which fastens on the exercise of the remedy, not on the substantive right or on the cause of action, although the accrual of the latter, in other words, of the right to sue is (rather, should be, for that is not always the case, the attempt made in the third column of the schedule to the Limitation Act to apply the general principle, stated against Article 120 for example and specify for each particular case the date when the right to sue accrues, is not always successful) its starting point. It is on this principle that Section 3 of the Limitation Act, which says that, subject to certain qualifications, every proceeding instituted after the period of limitation prescribed therefore shall be dismissed, is based. What attracts the injunction is the institution of the proceeding. If that is after the period of limitation prescribed therefor, the proceeding shall be dismissed, and it necessarily follows that the period of limitation is that prescribed at the time of the institution. What is relevant therefore is the law of limitation in force at the time the proceeding is instituted; the law in force at an earlier (or later) point of time is irrelevant except for purposes of ascertaining whether the substantive right itself has been extinguished under provisions like Section 28 of the Limitation Act, or whether the particular remedial right sought to be exercised had already become barred under the previous law before the current law came into force. It is not as if the birth of a substantive right, or the accrual of a cause of action to a party, attracts the law of limitation in force at the time so as to give the party under liability a vested immunity from action once time in accordance with that law has run out. Subject to the qualifications already mentioned, the only question is whether the proceeding, when it is instituted, is within time, or out of time, in accordance with the law then in force.

14. It is sometimes said that, "the law of limitation being a procedural law its provisions operate retrospectively in the sense that they apply to causes of

actions which arose before their enactment" -- the quotation is from *Km. Kr. Ramanathan Chettiar Vs. N.M. Kandappa Goundan (died) and Others*, , para. 3. That might well be so, although the qualification must be added--qualification expressly declared by Section 31(b) of the Limitation Act of 1963--that the provisions cannot operate retrospectively so as to apply to proceedings instituted before their enactment, unless, of course, the statute so provides. However, I prefer to deduce the proposition which I have stated from a consideration of the subject-matter to which the law of limitation applies. It is, as I have said, and as Section 3 of the Limitation Act makes plain, the exercise of the remedial right, and, in relation to that it is not retrospective, although, in relation to matters which are not its real subject-matter, such as the accrual of the substantive right or of the cause of action, it might be.

A statute is truly retrospective only if we have to regard it as having come into force at a point of time earlier than when it was actually enacted. That would ordinarily require express words in the statute itself and, if strict regard be had to the subject-matter to which the statute applies, it is very rarely indeed that, in the absence of such words, considerations such as whether the law enacted is procedural or substantive, or whether vested rights are affected (are themselves not matters easy to decide), can be of assistance in deciding whether or not the statute is of retrospective operation. Thus, if a statute says that a decree shall be passed only if a certain condition is satisfied, we are not really giving it retrospective operation if we apply it to a suit pending at the time the statute came into force, although in relation to the institution of the suit or the accrual of the cause of action, it can be said that the statute is being given retrospective operation. The subject-matter of the statute is the making of the decree, not the accrual of the cause of action or the institution of the suit, and, in relation to that matter, the statute is being given only prospective operation.

And, if a statute were to say that a particular transaction can be effected only in a particular way, I should think that the real reason for not applying it to transactions effected before the statute came into force, is not so much that that would affect vested rights as that the subject-matter of the statute being the making of the transaction, it cannot, unless it says so expressly or by necessary implication, apply to a transaction already effected before its enactment. In relation to its real subject-matter it is rarely, if at all, that a statute is to be given retrospective operation unless, of course, it is so expressed as to operate from a point of time prior to its enactment. Even procedural statutes are not given retrospective effect in the true sense of that expression, for, we do not reopen things already done and do them again in the new way; only things done after the enactment of the statute are done in the new way and it is only to them that the statute is applied; and the statute is retrospective only if we have regard to the institution of the proceeding or the accrual of the cause of action, neither of which, but the thing to be done, is its real subject-matter.

15. Up to 11-12-1938 the period of limitation for an application like the present

was that prescribed by Sub-section (3) of Section 237 of the Travancore Companies Act. 1 of 1092, which is in the same terms as the old Section 235 of the Indian Companies Act, 1913, (the 1913 Act for short) until its amendment by Act 22 of 1936:

"237. Power of Court to assess damages against delinquent directors, etc. (1) Where, in the course of winding up a company, it appears that any person who has taken part in the formation or promotion of the Company or any past or present director, manager or liquidator or any officer of the Company has misapplied or retained or become liable or accountable for any money or property of the company or been guilty of any misfeasance or breach of trust in relation to the Company the Court may on the application of the liquidator, or of any creditor or contributory, examine into the conduct of the promoter, director, manager, liquidator or officer, 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.

(2) xxx (3) The Travancore Limitation Act for the time being in force, shall apply to an application under this Section as if such application were a suit."

16. From 11-12-1938 up to 1-4-1951, when the Indian Companies Act 1913 replaced, it the law in force was Section 291(1) of the Travancore Companies Act, IX of 1114. This provision is identical with the new Section 235 (1) of the 1913 Act (introduced by Act 22 of 1936) which came into force on 15-1-1937:

"291 Power of court to assess damages against delinquent directors etc.--(1) Where, in the course of winding up a Company, it appears that any person who has taken part in the formation or promotion of the Company, or any past or present director, manager or liquidator, or any officer of the company has misapplied or retained or become liable or accountable for any money or property of the Company, or been guilty of any misfeasance or breach of trust in relation to the company, the Court may on the application of the liquidator, or of any creditor or contributory made within three years from the date of the first appointment of a liquidator in the winding up or of the misapplication, retainer, misfeasance or breach of trust, as the case may be, whichever is longer, examine into the conduct of the promoter, director, manager, liquidator or officer, 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. "

17. From 1-4-1951 till 1-4-1966, the new Section 235(1) of the 1913 Act which, as I have said is in the same terms as Section 291(1) of Travancore Act IX of 1114, was in force. And from 1-4-1966 Section 543 of the Companies Act has been in force:

" 543. Power of Court to assess damages against delinquent directors, etc. --(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, of the liquidator, or of any creditor or contributory, trade 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

(2) An application under Sub-section (1) shall be made within five years from the date of the order for winding up or of the first appointment of the liquidator in the winding up or of the misapplication, retainer, misfeasance or breach of trust, as the case may be whichever is longer.

(3) x x x x

It will be noticed that the only material change made from the new Section 235(1) of the 1913 Act was to give a longer period of limitation five instead of three years, two of the alternative starting points remaining the same and a third namely the date of the order for winding up being added

18. On 30-12-1953. Section 45-0 of the Banking Companies Act which makes special provision in respect of banking companies notwithstanding anything contained in any other law for the time being in force including the Indian Limitation Act and Section 235 of the Indian Companies Act (now Section 543 of the Companies Act 1956) came into force, and it remains in force, the words underlined (here into") by me in sub Section (2) thereof having been added with effect from 1-10 1959 by Act 33 of 1959

"45-0. Special period of limitation (1) Notwithstanding anything to the contrary contained in the Indian Limitation Act. 1908, or in any other law for the time being in force, in computing the period of limitation prescribed for a suit or application by a banking company which is being wound up, the period commencing from the date of the presentation of the petition for the winding up of the banking company shall be excluded.

(2) Notwithstanding anything to the contrary contained in the Indian Limitation Act, 1908, or Section 543 of the Companies Act, 1956. or in any other law for

the time being in force, there shall be no period of limitation for the recovery of arrears of calls from any director of a banking company which is being wound up or for the enforcement by the banking company against any of its directors of any claim based on a contract, express or implied, and in respect of all other claims by the banking company against its director, the period of limitation shall be twelve years from the date of the accrual of such claims "or five years from the date of the first appointment of the liquidator, whichever is longer."

(3) The provisions of this Section, in so far as they relate to banking companies being wound up shall also apply to a banking company in respect of which a petition for the winding up has been presented before the commencement of the Banking Companies (Amendment) Act. 1953"

Both sides are agreed that Sub-section (2) of this section is the provision applicable to a misfeasance application like the present. For reasons I have already stated in *The Bank of Meenachil Ltd. Vs. Chacko Chacko Kalayakkathil and Others*, -- see also *In re Supreme Bank of India Ltd.* (1964) 34 Comp Cas 34 (Mys) --I am of the same view, and I should think that the express reference to Section 543 of the Companies Act in the non obstante clause with which the sub-section opens, puts the matter beyond doubt. Further, that Sub-section (1) of Section 45-0 can have no application whatsoever to cases falling under Sub-section (2). Sub-section (2) provides for two classes of claims For the first, namely, claims based on contracts express or implied, there is no period of limitation at all so that the question of computing the period of limitation, which is what Sub-section (1) provides for does not arise For the second, namely, other claims, one of the two alternative starting points for limitation is the date of the first appointment of the liquidator which can only be after the presentation of the winding up petition, so that if the period from the date of the presentation of the winding up petition were to be excluded by applying Sub-section (1), no such claim could ever be barred by limitation as pointed out by me in 1962 Ker L.T. 166 : (AIR 1962 Ken 333) and the provision for limitation in Sub-section (2) would be meaningless

The position therefore is that while limitation in respect of the non-director respondents was governed by the new Section 235(1) of the 1913 Act from 1-4-1951 to 1-4-1956 and is now, since 1-4-1956, governed by Section 543 of the Companies Act, that in respect of the director respondents was governed by the un-amended or old Section 45-0(2) of the Banking Companies Act from 8-12-1958 up to 1-10- 1959 and is since governed by the amended or new Section 46-0(2). .

19. As we have seen, the law of limitation to apply is the law in force at the time the proceeding in question is instituted. For this proceeding, instituted on the 4th April 1963, that law, so far as the non-director respondents are, concerned, is to be found in Sub-section (2) of Section 543 of the Companies Act. There, the period of limitation prescribed is five years. But there are three alternative starting points: (1) the date of the order for winding up, (2) the date of the first

appointment of the liquidator in the winding up, and (3) the date of the act complained of. It was contended on behalf of the 8th respondent-- to what purpose it is difficult to appreciate since the acts complained of in this case would fall both under Clause (a) and (b) of Sub-section (1) -- that the first and second starting points which in this case are later than the third (though not necessarily in all cases since the section is applicable to a liquidator as well) are applicable only to the acts mentioned in Clause (a) of Sub-section (1) and that the third alone applies to the acts mentioned in Clause (b).

Apparently it is assumed, wrongly as I have already indicated, that the acts complained of in this case fall only under Clause (b). But, even if that assumption were correct, I can see no way of reading Sub-section (2) in that manner so as to make the contention of any avail. All the three starting points are applicable equally to Clauses (a) and (b) of Sub-section (1) and the choice of the starting point depends not on whether the acts complained fall under Clause (a) or Clause (b), but on the words, "whichever is longer" occurring in Sub-section (2) which obviously mean whichever five year period from the three different starting points expires later. So far as this case is concerned, the first and second starting points fall on the 5th December 1960 on which day the winding up order was made and the liquidator was first appointed in the winding up and that is much later than the third, the acts complained of having been committed between 1937 and 1950. The institution of this application on the 4th April 1963 is well within five years of the first and second starting points, and, although it is more than five years after the third, it is clearly in time since the starting point to be chosen is that giving the longest time for making the application.

20. The law of limitation applicable to the director respondents is that contained in the new Section 45-0(2) of the Banking Companies Act, that being the law in force when this application was brought. For the liquidator it has been contended on the strength of *City Equitable Fire Insurance Co., In re* (1925) Ch. 407 *Govind Narayan Kakade Vs. Rangnath Gopal Rajopadhye*, *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.* at p. 792 (FB) and *Karachi Bank Ltd. v. Shewaram* AIR 1933 Sind 103 that a claim in an application u/s 543 of the Companies Act is a claim based on a contract and that therefore such a claim comes within the first class of cases in Section 45-0(2) for which that section says that there shall be no period of limitation, and not within the second class of cases namely, other claims, for which the section prescribes a period of limitation.

I do not think that a claim u/s 543 of the Companies Act can be said to be a claim based on a contract. It is a claim based on a breach of duty, and, although it might be that that duty is one arising out of a relationship created by contract, it can scarcely be said that the claim is one for breach of that contract. All that the decisions referred to have said, for, it may be noted, the purpose of excluding the operation of Article 36 of the Limitation Act at a time when, under the old Section 235(2) of the 1913 Act, the period of limitation for an application under that section was the same as that for a suit, was that the claim in such an

application was not independent of contract which is an entirely different thing from saying that the claim therein is based on a contract. Indeed, in providing for a period of five years from the date of the first appointment of the liquidator, it would appear that the Legislature had Section 543 of the Companies Act in mind and did not consider that such a claim was a claim based on a contract for which there was to be no limitation.

I consider that an application u/s 543 comes within the "other claims" of Section 45-0(2), the second class of claims therein for which the period of limitation prescribed is 12 years from the date of the accrual of such claims or five years from the date of the first appointment of the liquidator whichever is longer. Here also the words, "whichever is longer" really mean whichever expires later, for, of the two periods of limitation mentioned, namely, 12 years and five years, there can be no doubt that the former is longer. But the starting point for the longer period of 12 years is the date of the accrual of the claims while that for the shorter period of five years is the date of the first appointment of the liquidator. Since the Sub-section applies only to directors it necessarily follows that the latter starting point must necessarily be the later since there can be no question of directors committing any acts of misfeasance after the appointment of the liquidator. But, since the appointment of the liquidator may be more than seven years after the acts of misfeasance, the shorter period of five years, starting from the first appointment of the liquidator, may expire later than the longer period of 12 years starting from the date of the accrual of the claims, thus giving a longer time for making the application.

21. The liquidator referred to in Section 45-0(2) is the liquidator of the banking company which is being wound up and obviously means the liquidator in the winding up (c.f. Section 543(2) of the Companies Act) appointed u/s 38-A or Section 39 of the Banking Companies Act. The first appointment of the liquidator in this case was on 5-12-1960 and this application was brought well within five years of that date. (Even if the provisional liquidator appointed on 8-8-1960 can be regarded as a liquidator within the meaning of the Section, this application is well within five years of that date). Since, of the two alternative periods of limitation, the second, namely, five years from the date of the first appointment of the liquidator expires later, that is the period to be chosen, and it follows that the application is in time as against the director respondents as well.

22. I shall now consider the two main contentions advanced on behalf of the respondents in the light of the propositions I have already stated. The first contention is that a misfeasance application like the present becomes barred the moment a suit for the same relief is barred. It is urged on the authority of decisions such as *Coventry and Dixon's Case* (1880) 14 Ch D. 660 *Cavendish Bentinck v. Fenn* (1887) 12 A C. 652 *City Equitable Fire Insurance Co., In re*, (1925) 1 Ch 407 at pp. 507 and 527 and a number of more recent cases both English and Indian the most recent English case referred to being *Re. B. Johnson and Co. Ltd.* (1955) 2 All E.R. 775 at pp 780, 781, 791 and the Indian cases

being *V. Narasimha Aiyangar, Official Liquidator of the City Hygienic Milk Supply Co. Ltd. Vs. The Official Assignee of Madras and Others*, , *Hukam Chand v. Bank of Multan, Ltd.* AIR 1924 Lah 285. *Govind Narayan Kakade Vs. Rangnath Gopal Rajopadhye*, and *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.* following these older cases that Section 543 is only a procedural Section creating no new rights or liabilities and merely providing a summary remedy for enforcing, in the liquidation of a company, such liabilities as might have been enforced by the company itself or by its liquidator by means of an ordinary suit.

It is true enough that the section creates no new rights if by the word "right" is meant a substantive right, and I have no doubt that it is in this limited sense, excluding what might be called remedial rights, that the decisions referred to use the word. The substantive right enforced u/s 543 of the Companies Act is the right of the company to recover any loss sustained by it from those responsible for the loss. That is a right which it would ordinarily have to be enforced by suit. But", once it winding up intervenes, a new remedy is given by Section 543 to the liquidator and the creditors and contributories of the company a remedy they did not have before the winding up order, for the enforcement of the substantive right. The section does undoubtedly confer a new remedial right for the enforcement of such substantive rights as the company itself could have enforced by way of suit. It also provides a remedy for the enforcement of such rights as may be created by the winding up itself. (See Buckley, Thirteenth Edition, page 672 under the head "Section does not create new rights" and Palmer. Company Law, Twentieth Edition, pp. 574 and 575 under the head, "Misfeasance summons" the comment in Palmer begins with the statement that the section (Section 333 of the English Act) gives the liquidator the right, inter alia, to apply to the court to examine into the conduct of a director or past director.

Therefore, it is fallacious to argue that, whenever the right to institute a suit is barred by limitation, the right to make an application u/s 543 of the Companies Act is lost since that section creates no new rights. The section does confer a new remedial right, entirely different from the right of suit although for the enforcement of the same substantive right, and, since this is not a case to which Section 28 of the Limitation Act has any application, the fact that the remedy by way of suit has become barred by time cannot have the effect of taking away the entirely different remedy of an application u/s 543 the substantive right being still extant. I might also point out that when the liquidator, or a creditor, or a contributory makes an application u/s 548 he does not do so as representing the company but in his own independent right--see the observations of Jessel M. R. in *In re National Funds Assurance Co.* (1878) 10 Ch. D. 118 at pp. 124 and 125--although for the benefit of the company. (His position, it seems to me, is analogous to that of a junior member suing in respect of joint family property). In making an application u/s 548 the liquidator is not exercising the power conferred by Section 547(1). He does not apply in the name and on behalf of the company, but, as Forms Nos. 120 and 121 of the forms in the Companies (Court) Rules rightly set out, in his own name. I would add that he applies in his own

behalf although, in the terms of Section 543, the order can only be for payment or restoration to the company.

23. Great reliance is placed on behalf of the respondents on the decisions in *Abdullah Ashgar Ali v. Ganesh Das*, AIR (20) 1933 PC 63 and *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.*. In the former it was held that an application u/s 186 of the Companies Act, 1913, was barred because a suit for the money claimed was barred, and, in the latter that an application under the old Section 235 of the same Act was barred because a suit for the same relief was barred: But this was not on the principle sought to be deduced from these decisions, namely, that whenever a suit is barred, the entirely different remedy of an application for the same relief must be barred. It was on entirely different grounds. In the former case it was because the words, "any money due from him" occurring in the section were construed as meaning, "any money due and recoverable in a suit by the company" and as not including "any monies which at the date of the application could not have been so recovered".

In the latter case *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.*. It was because, under the old Section 235(3) of the 1913 Act, the Limitation Act applied to an application under the section as if such application were a suit. And, applying Article 120 as the proper article to apply, it was thought that the starting point for limitation under the third column was the point of time when the right to institute a suit accrued, although, with great respect, I should have thought that Section 236 (3) would have required the entry in the third column to be read as, "When the right to apply accrues". For if the application is to be regarded as a suit, the right to sue must be the right to make the application. That was the view taken in cases such as *In the Matter of the In Re: The Union Bank*, (also by Mukerji J. in his dissenting judgment in *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.* which overruled *In Re: The Union Bank*, and in which he adhered to the view he took in that latter case) and, the amendment of 1936 which provided as a starting point, the point of time when a liquidator is first appointed, in other words, when the right to apply as against directors and officers accrues, must read in accordance with the rule in *Heyden's* case, be regarded as intended to set aside the judicial error in *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.* and therefore as declaratory in effect.

It is also to be observed that the effect of that decision would, in many cases, be to bar the right given by section to the Liquidator and to creditors and contributors to make a misfeasance application, even before it accrues, In many perhaps, in most cases the acts complained of would include acts done more than six years before the making of the winding up order which confers the remedy, a remedy they did not possess before, on the liquidator and on creditors and contributories, and in respect of such act, the effect would be that the remedy is not merely still born but is contravened by the provision for limitation in the very Section that creates the remedy: This is opposed to common sense

and to the general principle that time begins to run only when there is a person to sue, capable of suing, a person to be sued and all the necessary facts have come into existence. (See *Srimati Sarat Kamini Dasi Vs. Nagendra Nath Pal*, at pp. 71 and 72 and *A.N.C.T. Subbiah Thevar, Trustee of Sree Vedapuriswaraswami Koil and Others Vs. N.R. Samiappa Mudaliar and Others*, at p. 356 (FB) following AIR 1930 270 (Privy Council) and *Chara Chandra Pramanik v. Nahush Chandra Kundu* ILR (1923) Cal 49 : (AIR 1923 Cal)). Also the dictum of Seshagiri Ayyar J. in *Muthu Korakki Chetty v. Nadar Ammal*, ILR (1920) Mad 185 : (AIR 1920 Mad 1) approved by the Supreme Court in *Sita Ram Goel Vs. The Municipal Board, Kanpur and Others*, paragraph 23)

"that the language of the third column of the Schedule to the Limitation Act is to be so interpreted as to carry out the true intention of the Legislature that is to say, by dating the cause of action from a date when the remedy is available to the party".

However that might be, what was held in *Shiam Lal J. Dewan Vs. Official Liquidators of the U.P. Oil Mills Co., Ltd.* was that, since both the starting point and the period of limitation for an application under the old Section 235 of the 1913 Act was the same as those for a suit for the same relief, such an application is barred when such a suit is barred. Neither case is therefore authority for the proposition advanced on behalf of the respondents that, when the remedy by way of suit is barred, any other remedy for the same relief in enforcement of the same substantive right, must likewise be barred. *Benares Bank Ltd. Vs. Shri Sri Prakasha Bhagwan Das and Others*, and in the matter of *In Re: The Companies Act and S.S.R.S. Nidhi Ltd.*, are authority for the proposition that, under the new Section 235 of the 1913 Act (and hence u/s 543 of the 1956 Act) the question whether a suit would be barred by limitation is irrelevant for the purpose of deciding whether an application under the section is barred.

24. It is true that at a time when there was no limitation prescribed for a misfeasance application, English Judges, as a rule, declined such an application if an action (suit) would not lie by reason of the bar of time. But that was only a refusal, in exercise of the discretion given by the section, on the score of belatedness, a matter which when provided for by statute can scarcely, by itself, be a ground for the exercise of discretion. It does not mean as is wrongly assumed by the respondents, that whenever a suit is barred by time, all other remedies for the enforcement of the same substantive right are likewise barred.

25. The second contention, based on the authority of AIR 1942 54 (Privy Council) and cases like *Mangapathi Naidu Vs. M.K. Krishnaswami Naidu and Others*, and *Km. Kr. Ramanathan Chettiar Vs. N.M. Kandappa Goundan (died) and Others*, following these decisions, is that the remedy now presented had become barred under the previous laws in force before those laws were replaced. Therefore, it remains barred and cannot be revived by the new Section 45-O (2) which is not retrospective in operation. This contention is raised specifically with reference to the old Section 45-O (2) of the Banking Companies Act which did not contain the

words, "or five years from the date of the first appointment of the liquidator whichever is longer" and prescribed only one period of limitation with one starting point, namely, 12 years from the date of the accrual of the claim. With the proposition laid down in the decisions, that a remedy once barred by the law of limitation in force at the time is not revived by a new law giving a longer period of time in the absence of provision in that new law to that effect, I have of course, no quarrel.

But I wish to emphasise, what I have already said, namely, that the decisions apply only where it is the very same remedy--that is sought to be prosecuted and that the fact that one remedy has become barred does not mean that other remedies, if there are other remedies, for the enforcement of the same substantive right, are also barred. And, even assuming that a misfeasance application u/s 543 of the Companies Act, 1956 is the same remedy as an application under the corresponding provisions of the 1913 Act and the Travancore Acts that preceded it, I do not think that, so far as the present claim is concerned, this remedy was at any time, barred by the previous laws of limitation in force.

26. Up to 11-12-1938, the law in force was Section 237 of the Travancore Companies Act of 1902. When this law was replaced on that date by Section 291(1) of the Travancore Companies Act 1914 no part of the present claim had become barred. The earliest act complained of took place in 1937 and even if it be that it was the article of the Travancore Limitation Act corresponding to Article 30 of the Indian Limitation Act, 1908 and not as the majority of the High Courts in India have held and, I think with great respect rightly the article corresponding to Article 120 and even if it be that the starting point for limitation was the point of time when the right to institute a suit accrued and not when the right to make an application accrued, no part of the claim could have been barred by 11-12-1938.

27. After 11-12-1938, the laws in force have been Section 291(1) of the Travancore Companies Act 1914, the new Section 230(1) of the Indian Companies Act, 1913, and Section 543 of the Companies Act 1956, leaving aside for the moment Section 460 of the Banking Companies Act applicable only to the director respondents. All these sections it will be noticed, come into play only in the course of a winding up so that there can be no question of the remedy provided by them coming into being or becoming barred under then before a winding up order is made. The winding up order in this case was made only on 5-12-1900, and hence there can be no question of the remedy that is now being prosecuted having been barred by any of the previous laws in force.

28. So far as the director-respondents are concerned the new Section 236(1) of the 1913 Act was replaced on 13-12-1953 by the old Section 45-0(2) of the Ranging Companies Act, and the latter by the new Section 45-0(2) on 1-10-1950. The principal contention on the part of the director respondents is as we have seen that an application of the present kind had become barred under

the old Section 45-O (2) in respect of acts committed before 1 10 1947, when the new Section 46 O(2) came into force on 1 10-1959 The argument is that the word, "claim" is used in Section 45-O(2) old as well as new to mean the substantive right that is being enforced, and that the Section applies in respect of all remedies for the enforcement of that substantive right Thai being so an application of the present nature had become barred by 1-10-1950 in respect of acts committed before 1-10 1947, and there is nothing in the now Section 45 O(2) In indicate that it is to operate retrospectively so as to review this barred remedy

29. I am inclined to accept the argument that I be word, "claim" is used in Section 45-O (2) to denote a substantive right and that in relation to its subject matter the provision for limitation contained in the section is not retrospective. The word "claim" is of wide import. It can mean the substantive right that is asserted; it can also mean the remedy invoked in enforcement of the substantive right. In the clause of the section speaking of the enforcement of any claim based on a contract ! suppose the word, "claim" means the substantive right, for, one scarcely enforces a suit or an application or other remedy. Now, would it be quite correct to say that remedy is based on a contract? And, in the clause which speaks of ""the date of accrual of such claims" the word, "claims" must refer to the substantive rights that are being enforced, for here again, it would be scarcely correct I o speak, of the accrual of a suit or application or other remedy, although it would he quite correct to speak of the accrual of a right to sue or to make an application. If the word, "claims" in the phrase, "such claims" moans substantive rights, then it should follow that the claims referred to in the opening words of the second part of the sub-section prescribing a period of limitation "and in respect of all other claims", must likewise be substantive rights. And it is only in that sense that a claim in a misfeasance application can be said to be a claim by a banking company so as to attract the section. The application, as we have seen, is. not by the company though for its benefits; but, the substantive right sought to be enforced is a right belonging to the company and may therefore be said to be a claim by the company. The period of limitation prescribed in the Sub-section therefore applies to the exercise of all manner of remedies in respect of the substantive right a covered by the sub-section.

30. There is nothing la the sub-section to indicate that, so far as the provision for limitation is concerned, the sub-section--I am of course referring to the new Section 45-O(2) ,is to apply so as to revive remedies that had become barred before it came into force. Sub-section (3) of the section has relation only to the clauses in Sub-sections (1) and (2) which speak of a banking company which is being wound up and it only makes it clear that the section applies not only to companies the winding up of which commenced after the section was first enacted by the Banking Companies (Amendment) Act 1953, but also to banking companies the winding up of which commenced earlier. If the sub-section gives the section any retrospective application it is only in relation to the date of presentation of the winding up petition, not in relation to the prosecution of

claims against the banking company concerned

31. Where the argument fails is, however, in assuming that the old Section 45-0(2) was applicable at any time before the winding up order was made so as to have barred an application like the present. As in the case of Section 235 of the 1913 Act and Section 453 of the 1960 Act, it is obvious that the sub-section applies only in the case of a banking company which is being wound up. The provision for limitation contained therein can apply only when the company is being wound up and there can be no question of its operating at any time before the winding up order so as to bar the enforcement of any claim, no matter when the claim might "have accrued. The right to apply under Section 543 of the Companies Act comes into existence only when a winding up order is made, and although it might be possible to think of instances where, as for example by reason of the defective wording under the third column of the Schedule to the Limitation Act, it is not possible to synchronise the starting point for limitation with the accrual of the cause of action, so, that as under Article 138 of the Limitation Act of 1887 (or if, for example, the third column against Article 66 read, "the date of the bond" and a bond gave five years" time for payment) a remedy can conceivably become barred before it is born, it would be startling if limitation were to so operate as to bar a remedy even before it comes into existence.

As observed by Courts-Trotter J. in *Seen Kutti v. Kunhi Pathumma* ILR (1917) Mad 1040 at p. 1055 : (AIR 1919 Mad 972 at p. 981 FB) such a startling result can be permitted only if the words of the statute are too plain to be evaded. Here, on the contrary, the language of the section, the old Section 45-0(2), clearly shows that the provisions for limitation therein can come into play only after there has been a winding up order and there can be no question of its operating so as to bar a claim before that.

32. It has been contended that both Sub-sections (1) and (2) of the new Section 45-0(2) of the Banking Companies Act apply to misfeasance applications like the present, that Sub-section (1) is of no avail to revive a claim barred at the commencement of the winding up; with the latter proposition no one can quarrel and that despite all appearances to the contrary Sub-section (2) is really in the nature of a proviso to Sub-section (1) prescribing a period of limitation for claims not barred at the commencement of the winding up and therefore kept alive by Sub-section (1). I have been quite unable to follow this argument or see what it leads to and must therefore be content with stating it as best I can.

33. I hold that no part of the claim is barred by limitation as against any of the respondents.

34. I shall now proceed to consider whether it is true that the bank was paying income tax and dividends on income and profits not really earned but made to appear as earned by falsifying its books; and, if it is what loss was occasioned to the bank thereby. Next, if loss is established, to what extent, if at all, each of the

respondents concerned, respondents 1 to 6, 8 and 10 (so far as Claim B is concerned there is no claim against respondents 7 and 9) is liable in respect of the loss.

35-89. The charge of falsification of the balance sheets and profit and loss accounts and the payment of taxes and dividends otherwise than on income and profit really earned (in other words, out of capital, whether subscribed or borrowed) seems to me amply established by the books of the bank---who was responsible for the falsification is, of course, another matter which I shall deal with later. We are at present concerned only with the taxes and dividends paid for the years 1936 to 1949, (His Lordship dealt with these matters and proceeded).

90. That the facts disclosed by the entries, or the want of them, in the books of the bank and by the other documents of the bank marked in the case are as set forth above is not disputed--only the inference therefrom that the books were falsified so as to show fictitious income and fictitious profits is denied, and, of course, hotly denied. But I fail to see what other inference is possible. The respondents have given no evidence whatsoever either on affidavit or from the box to explain or rebut the evidence furnished by the books. (I notice, on going through the record, that respondents 2 and 7 have stated their points of defence in the shape of an affidavit and that the affidavit of the former contains a prayer that it may be permitted to be read as evidence. But I was not moved for the grant of leave and no attempt was made to read it as evidence). Nor have they made the least attempt to show with reference to the books of the head office or of the several branches (all of which were open to them for inspection) that the impugned credit entries in the profit and loss accounts for the several years represented income actually earned, if not actually realised.

In their points of defence they have largely contented themselves with the bare denial that the credits in question were fictitious and will) the bare assertion that the credits were in respect of income actually earned and that the balance sheets and profit and loss accounts were correctly drawn up. Respondents 1, 5 and 6 have stated that the credits, and the corresponding debits to the branches and the interest receivable account, were on account of some of the branches having charged less than the stipulated rates of interest or none at all in the years prior to 1949. This resulted in a fall in the profits for those years, and, to cover this, the shortfall was estimated, and, credit taken thereof in the profit and loss account as interest received, by raising corresponding debits in the branch account and the interest receivable account. (This seems to me perilously close to an admission of manipulation to cover up losses).

Respondents 5 and 6 have added that the branch accounts for the several years remained unrecognised. The auditor, the 8th respondent, has taken shelter under the fact that the branch accounts were not reconciled and has added that the reserves would cover the intangible assets. How this, even if true, can be of any assistance if in fact the income and the profits shown are fictitious is not clear and I might add that if the liquidator's case is true the reserves themselves are

fictitious being transfers from fictitious profits. And, as is only to be expected when trouble is afoot, the remaining respondents have generally tried to throw the blame ,if blame there is, which they deny) on the 1st respondent who they say was in complete charge as the managing director.

91. So far as the debits to the branches were concerned his Lordship held: Taking all the circumstances mentioned above into consideration there can be no doubt whatsoever that the debits against the branches during the years in question which were balanced by corresponding credits to the profit and loss account were fictitious.

92. So far as the debits in the interest receivable account of the head office are concerned, as I have already said, these debits must be imaginary, for there is nothing in the books to disclose from whom the interest was due and on what account.

93. It follows that the credits during the years in question to the profit and loss account by debit to the branch account and interest receivable account were fictitious credits and that there were no such items of income earned. These fictitious items entered into the total of assessable income for purpose of Income Tax and were taken into account in working out the profit for the year

94. It is the law, and that is expressly embodied in Article 89 of the Articles of the Company, that no dividend shall be paid otherwise than out of profits. It follows that the payment of dividend out of fictitious profits shown by falsifying the books of the company amounts is a misapplication of the money of the company and it is not necessary that the persons responsible for the payment should have personally profited thereby. Likewise, the payment of Income Tax, not really due ,on fictitious income shown by falsifying the books of the company.

95. The statement in Appendix II (net reproduced here) to this order works out the loss suffered by the company for each of the years 1936 to 1949 on account of the misapplication of its money by the payment of tax and dividends on income and profits not actually earned. It is self-explanatory, but I might mention that the amount entered under column 3 is not the total of all the false credits to the profit and loss account but only the total of such credits raised by debits to the branch account and the interest receivable account. As we have seen, credits have been raised by debits to other accounts in some years, but the amounts are comparatively small and their addition would not affect the result, since, even without that, there would be no divisible profit or taxable income during the years concerned. They have therefore been ignored. The total loss for the years 1936 to 1949 works out to Rs 16,52,295/-, Rs. 9,24, 986/- on account of the payment of dividend otherwise than out of profits, and Rs. 7,27, 309 by reason of payment of Income Tax not really due.

96. It is said that Article 90 of the articles requires only 16 per cent of the profits of each year to be set apart as reserve and that therefore in working out the divisible profit under column 6 of the table only 15 p.c. of the actual profit shown

under column 8 and not the amount shown under column 5 should be deducted. But, what the article says is that not less than 15 per cent shall be set apart as reserve; it is open to the board to set apart more; it is not for us to speculate what sum the Board would have set apart had it kept true accounts without magnifying the profits; and in arriving at the divisible profits we must deduct the amount actually set apart as reserve or for other purposes.

97. Before proceeding to determine how far each of the respondents is responsible for the misapplication of this sum of Rs. 16,52,295/-, I shall say a word or two about the liability of the director--respondents, 1 to 6, in their bare capacity as directors. The following are the articles of the company having a bearing on the matter: [after reading Articles 60, 65, 76, 82, 89, 94, 97, 98, 99, and 109 his Lordship proceeded.]

98. We have seen how, year after year income tax was paid on fictitious income and dividends out of capital, on fictitious profits. These payments were ultra vires and amounted to a misapplication of the money of the company, a misapplication rendered possible by the falsification of its books and its balance sheets and profit and loss accounts. The article squarely lay the responsibility for the proper keeping of the books of the company and for the proper preparation of its balance sheets and profit and loss accounts on the shoulders of the Directors. The auditor only comes between the Directors and the general meeting, and it is no part of his duty to see to the keeping of the books or the preparation of the balance sheets and profit and loss accounts. Although the circumstance that the accounts have been certified by a competent and qualified auditor would naturally lend assurance to the directors in placing them before the general meeting, as I have already said, the responsibility is essentially the responsibility of the directors.

The auditor in no way relieves them of the responsibility and it is no excuse to say as some of the director respondents have done that the auditor had examined the books and certified that the balance sheets exhibited a true and correct view of the state of the company's affairs. I am not for a moment suggesting that the directors must attend to these matters personally or that they are bound to examine the entries in the company's books and satisfy themselves that the balance sheet is a true balance sheet. But, as men of business, they must at least show that they took reasonable steps to ensure that the books were properly and truly kept and the balance sheets and profits and loss accounts properly and truly prepared. This the respondent Directors have not made the least attempt to do--they devised no system, they constituted no committee for the purpose, they framed no standing instructions, and beyond saying that the bank had competent and qualified staff to attend to these matters they have not chosen to "say anything as to how these things were done and how they discharged their responsibility with regard to them--and I think it clear that the misapplication was the result of a breach, I would add a wilful breach, of their duty as directors.

99. The word, "misapplication", by itself involves no mens rea. It imports no mental element such as dishonesty or fraud, not even negligence. It only means wrong or incorrect application, not necessarily a wrongful application, and there can be a perfectly innocent misapplication. But it is well settled by decisions both English and Indian that liability u/s 643 of the Companies Act can be imposed only if there has been dishonesty or fraud or at least negligence, not ordinary negligence but gross and culpable negligence. (Eminent judges have criticised the use of phrases such as gross negligence and have said that the addition of a vituperative epithet to the word, "negligence" signifies nothing. But, equally eminent Judges have unblushingly continued to use such expressions, and it would be pedantry to deny that the phrase does convey a definite meaning as importing an element of recklessness or wilfulness negligence which is the equivalent of fraud, or constructive or equitable fraud as it is some times called).

Whether the statutory basis for this is to be found in Section 543 itself which requires the court to examine into the conduct of the alleged delinquent before making an order against him and thereby implies that his conduct must be found to be blameworthy, or whether it is to be found in Section 633 I do not know, although the way in which some decisions cast the burden on the alleged delinquent seems to suggest that the basis is the combined result of these two sections. If u/s 543 standing by itself, at least gross negligence has to be found before liability can be imposed it is difficult to see how Section 638 can afford relief from such liability since, if a person has been grossly negligent, it can scarcely be said that he has acted reasonably. Yet Section 633, expressly refers to liability on account of breach of trust and that, it seems to me, points to the statutory basis being the combined effect of the two sections. If that be so it would appear that once misapplication is proved, the burden of proving that he acted honestly and reasonably lies on the alleged delinquent. Indeed Section 633 has been invoked by some of the respondents, vainly for, as we shall see, they have not made the least attempt to show that they acted honestly and reasonably.

It might however be that these decisions do not regard the onus of proof in respect of the mental element u/s 543 as ever being thrown on the alleged delinquent as u/s 688 and only regard that the burden of adducing further evidence shifts on him once the applicant makes out a prima facie case. I am prepared to assume that that is so, but, once that stage is reached, so far as directors of banking companies are concerned, Section 45-H(1) of the Banking Companies Act comes into play and it expressly requires the alleged delinquent to prove that he is not liable. (Whether the section applies, as it was probably intended to apply, to all kinds of misfeasance falling u/s 543 of the Companies Act or only to those described in Clause (a) thereof where an order for repayment or restoration of money or property can properly be made, it is not necessary for me to decide, for, as I have already shown, the misfeasance complained of in this case docs fall under Clause (a)).

100. Now, what have the respondent directors done to show that they had taken reasonable steps, such as businessmen in their position would take, to ensure that the books of the company were properly and correctly maintained and the balance sheets and profits and loss accounts properly and correctly prepared. As I have already said, nothing whatsoever. They have offered no evidence on the point. In the points of defence (which of course are not evidence) they have stoutly denied that there was any falsification of the books or any misapplication of the money of the company, a denial which, as we have seen, can scarcely bear scrutiny. Some of them have said that they placed reliance on the 1st respondent, some that they placed reliance on the auditor. The 1st respondent has said that he placed reliance in the conduct of the affairs of the bank on the 4th respondent and another director, Jacob Cherian, now deceased, who were well versed in such affairs, lie himself being comparatively ignorant, while the 3rd respondent has pleaded ignorance of the English language as an excuse.

Beyond stating that the company had competent staff to see to the proper maintenance of its books and the proper preparation of its balance sheets and profit and loss accounts not one of them has cared to disclose who were the persons in actual charge of these matters, what exactly were the duties imposed on them and what scrutiny there was over their work in order to ensure that it was properly done. At best, the plea of the respondents can amount only to a plea of complete ignorance born of a complete inadvertence to their duties as directors, a reckless indifference or otherwise put, a wilful shutting of their eyes. The liquidator has shown that the books, and balance sheets and profit and loss accounts were falsified and deliberately falsified; it was the duty of the director respondents to see to it that these books and accounts were truly kept and prepared; they do not say that they did anything at all in discharge of this duty, nor does the evidence (consisting solely of the records of the company) disclose that they did anything; in the circumstances there is nothing more that the liquidator can do; and no question of further proof of culpable negligence arises.

A bare statement that the directors did not know what was going on is no defence. To borrow the language of Lord Simonds in *Morris v Kanssen*, 1946 A.C.459 at p. 476, though in a different context, their duty as directors was to know; their interest is to disclaim knowledge; and such a conflict can be resolved in only one way. And that is to require them to show that they were not guilty of fraud or culpable negligence. They cannot be allowed to throw up their hands and say. "We knew nothing and believed that everything was all right."

101. I would go further and say that, in this case, an inference of fraud can reasonably be drawn against the director respondents. The deliberate falsification of the books of the company year after year for the purpose of showing fictitious income and fictitious profits could not have been the handiwork of the staff of the company; it could only have been under the specific instructions of those at the helm of affairs. In a company, the directors are at the helm of affairs, and although the rudder might be in the hands of the managing director, it is the

duty of the directors to keep an eye on him and see that he steers a proper course Here the directors do not say what control they exercised: it is difficult to imagine that over this long period they were completely ignorant of the systematic fraud that was being carried on from year to year; not one of them has dared to get into the box to assert his ignorance and face a cross-examination regarding his complicity; and the inference seems to me legitimate that they were privy to the fraud

102. Of the very large number of decisions both English and Indian that have been cited at the bar, I think it necessary to make reference only to one, namely. *Dovey v Cory* 1901 A.C 477 the decision on which the strongest reliance is placed on behalf of the respondents. There *Cory*. the alleged delinquent director was exonerated, but the only resemblance that that case bears to the present case is that "that also was a case where dividend was paid otherwise than out of profits There *Cory* filed an affidavit and faced a long and searching cross-examination regarding the part played by him in the matter It was conceded that there was no question of any moral obliquity and it was not suggested that there was neglect or default by reason of the absence of some system under which: if honestly carried out, the interests of the company would have been secured. The evidence showed that, having regard to the magnitude of the work the directors entrusted the general manager and their chairman with the duty of scrutinising the returns received from the several branches and bringing to their notice any matter which required their attention. It also appears from the evidence that the branches of the bank were regularly visited and their books examined by the chairman and by the general manager and by two inspectors.

It was found, indeed it was conceded, that *Cory* had acted upon the representations made to him by the Chairman and the general manager, representations which were in fact false but which he honestly believed to be true. It was held that, in the circumstances he was entitled to rely upon the judgment, information and advice of the chairman and the general manager as to whose integrity, skill and competence he had no reason for suspicion and that he was not guilty of negligence in not examining the returns for himself. He was himself deceived by those whom, having regard to the ordinary course of business, he was justified in trusting. But, in the present case, there is nothing to show that the director respondents were misled or deceived by anybody into laying fraudulent balance sheets before the general meeting and into paying taxes not due and dividends not payable. They have not chosen to disclose how they discharged the duty cast upon them as directors and to whom they entrusted the work of seeing that the books were properly kept and the balance sheets properly and truly prepared

103. The law upon the subject has been fully set out in the speech of Lord Davey in the above mentioned case:

"My Lords, I need only refer to three cases, which seem to me to contain the whole law upon the subject In *Stringer's Case*, (1869) 4 Ch. A. 475 the business

of the company in question was of an extremely speculative and hazardous character, and the directors had paid a dividend on their estimated value of assets which were afterwards totally lost. It was held that the estimate, having been made bona fide, and without any intention to defraud anybody, a director could not be made liable when the company was wound up to replace the money. In *Rance's Case* (1870) 6 Ch. A. 104 Lord Romilly laid down the principle which he thought governed cases of this description thus: "When an improper payment has been made, if it be a mere error of judgment it cannot be recovered; if it be a fraudulent payment then it can" The learned judge explained what he meant by a fraudulent payment: "I mean once where the person who makes it or is concerned in making it is at the time aware of the impropriety of making it, but does so in order to obtain a benefit for himself" and he adds: "The director may be ignorant of [his fact, but if his ignorance arises from his wilfully shutting his eyes to the facts which are before him he is equally guilty."

I think that this statement of the law is very nearly but not quite, accurate. In my opinion it is not necessary that the motive of the improper payment should be to obtain a benefit for the director himself. I also understand Lord Romilly to include in the expression "wilfully shutting his eyes," culpable negligence or reckless indifference by the director in the performance of his duties. Lord Romilly decided that case in favour of the director. The Court of Appeal took a different view of the facts from that taken by Lord Romilly, and held that the directors in the preparation of the so-called balance-sheet had not followed the directions in their articles of association, and the balance-sheet did not in fact purport to show a profit out of which a dividend could be paid. In such a case there can be no doubt of the liability of the director who is proved to have, in fact, paid a dividend. The case of *Leeds Estates and Co. v. Shepherd* (1887) 36 Ch D 787 before Stirling, J. was a case of the same description. The directors had not followed the directions contained in the articles of association. The learned Judge, in the course of his judgment, states the law thus: "It seems to me that the views expressed by the learned judges who decided *Ranee's Case* (1870) 8 Ch. 104 are consistent with the proposition that directors who are proved to have, in fact, paid a dividend out of capital fail to excuse themselves if they have not taken reasonable care to secure the preparation of estimates and statements of account, such as it was their duty to prepare and submit to the shareholders, and have declared the dividends complained of without having exercised thereon their judgment as mercantile men on the estimates and statements submitted to them".

My Lords, I agree in this statement of the law, and I do not think it inconsistent with that of Lord Romilly, properly understood, and subject to the observation which I have already made upon it. It is by this standard that the conduct of the respondent must be judged in this case".

. Judged by this standard the respondents have miserably failed.

104-112. I shall now examine the case against each respondent separately with

a view to ascertain to what extent he is liable, and, in doing so, shall consider what incriminating circumstances there are against him apart from the circumstance that he was a director when the misapplications took place. After so examining the order concluded.

113. In the result there will be an order directing respondents 1 to 6 and 8 to repay the company the sum of Rs. 16,52,295/- misapplied by them. They will be jointly and severally liable to make the repayment, but, while the several liability of respondents 1, 2 and 4 will extend to the entire sum of Rs. 16,52,295 the several liability of the 3rd respondent will be limited to the sum of Rs 15,07,470/ that of the 5th respondent to Rs. 8,96,848/- of the 6th respondent to Rs. 12, 96,409 and that of the 8th respondent to Rs. 9,69,180/-. It seems to me only just that interest should be paid on the sums misapplied from the date of each misapplication but the liquidator has claimed interest only from 8-8-1960, the commencement of the winding up. Therefore I direct that the above sums will bear interest at six per cent per annum from 8-8-1960 until realisation.

114. Respondents 1 to 6 and 8 will pay the Liquidator his costs in respect of this claim, namely, claim B.