

P.K. Nedungadi vs The Malayalee Bank Ltd. (In ... on 9 February, 1971

Equivalent citations: AIR1971SC829, [1972]42COMPCAS120(SC), (1971)3SCC598, AIR 1971 SUPREME COURT 829

Author: A.N. Grover

Bench: A.N. Grover, K.S. Hegde

JUDGMENT

A.N. Grover, J.

1. This is an appeal by certificate from a judgment of the Madras High Court.

2. In October, 1950 the Malayalee Bank Ltd., hereinafter called the "Bank" was ordered to be wound up. On that date there were only two Directors i.e., respondent No. 3 and the appellant P. K. Nedungadi. The second respondent P. S. Mannadiar hereinafter called "M" was appointed as the Managing Director on March 4, 1945. He continued to work as such till December 25, 1948. Afterwards he was a Director till the date of his resignation on June 14, 1950. The third respondent T. Eronanunrd was Director from November 15, 1943 onwards. The fourth respondent V. K. Thirumalpad was a Director from 1940 till March 13, 1949. The appellant P. K. Nedungadi was a Director from October 8, 1948 till the date of the winding up order. The fifth respondent V. Venugopalan Thampan was a Director from June 22, 1946 till October 8, 1948.

3. In September, 1953 the Official Liquidator filed a petition under Sections 183(3) and 235 of the Indian Companies Act together with Rule 9 of the Companies Rules and Section 45, A, B and F of Act IX of 1950 and Rule 6 of the Banking Companies Rules for an order determining and fixing the liability of the respondents jointly and severally in respect of the acts of misfeasance, misapplication of monies, breach of trust etc., and to declare their liability to contribute Rs. 2,11,998.04 or such other sum as might be determined. In September, 1954 the High Court directed the Official Referee to record the evidence. Two charges were framed out of which so far as the appellant is concerned, the material portion of the following charge may be reproduced:

In contravention of the resolution of the Board of Directors dated 27-10-1946. No. 1 (P. S. Mannadiar) amongst you took away and Nos. 2 to 5 (T. Eromanunni, V. K. Thirumalpad and V Venugopal Thampan) permitted No. 1 to take away a sum of Rs. 14,623-4-2 from the Bank under the guise of an overdraft.

That No. 1 amongst you obtained and Nos. 2 to 5 amongst you sanctioned to No. 1 loan, aggregating to Rs. 34,863-6-0 (wherein the aforesaid sum of Rs. 14,623-4-2 was merged) on the supposed security of the Mannadiar Saw and Oil Mills Ltd., Palghat.

That at the time the transaction was put through you knew or could with reasonable diligence have known that the security was wholly illusory and that was only a device to circumvent the provisions of Section 20 of the Indian Banking Companies Act That by this and other connected wrongful devices you caused loss to the aforesaid bank of a sum of Rs. 49,608-4-3.

A learned Single Judge took the view that all the Directors left everything in the hands of respondent No. 2 and that was the reason why the transactions which had been brought about had taken place. According to the learned Judge any criminal prosecution in the circumstances disclosed would have failed and therefore he dismissed the application of the Official Liquidator. On appeal by him a Division Bench of the High Court held that the appellant and respondent No. 2 had been guilty of acts of misfeasance etc. and directed that they should jointly and severally pay to the Official Liquidator a sum of Rs. 46,616 together with interest on a sum of Rs. 34,541.31 from 1953 to the date of realisation. It is unnecessary to refer to the liability of the other respondents which was determined. Respondent No. 2 has not filed any appeal and we are concerned with the appeal of Nedungadi.

4. Now what the High Court found from the evidence was as follows: Respondent No. 2 was carrying on business under the name of Mannadiar Saw & Oil Mills. He had three loan accounts with the Bank. The first was a current account and the second an overdraft account and the third an account in the name of the Mills. Large sums of money were drawn by him without security from the various accounts exceeding limits sanctioned to him by the Board of Directors. The affairs of the Mills became very unsatisfactory and its business fell on evil days. M formed a public limited company and sold the Mills and its property at an inflated price to the said company. This company was incorporated by the name of Mannadiar Saw & Oil Mills Ltd. on January 31, 1948, hereinafter referred to as the "Mills." The appellant was one of the Directors of that Company. This company was ultimately wound up in 1950. The Bank had certain deposits to the extent of Rs. 50,000/- with the Palghat Branch of the Indo-Mercantile Bank. In the beginning of 1948 the Indo-Mercantile Bank got into difficulties and it closed its business from February 10, 1948. M had an overdraft account with Indo-Mercantile Bank at its Palghat Branch. The agent of that Branch was the appellant. M purporting to act on behalf of the Bank drew a cheque on the Indo-Mercantile Bank Ltd. on February 8, 1948 for a sum of Rs. 13,000/- and with the help of the appellant that amount was adjusted against his overdraft account. In the accounts of the Indo-Mercantile Bank this sum was debited against Rs. 50,000 standing to the credit of the Bank. M however did not debit himself with the sum of Rs. 13,000/- in any of his accounts with the Bank. The amount was shown only in the suspense account. On October 8, 1948 the appellant, who was formerly the agent of Palghat Branch of Indo-Mercantile Bank, was appointed a Director of the Bank. On taking charge he discovered that M had not brought to account the sum of Rs. 13,000/- which he had taken away from the Bank in the manner stated before, M thought of a scheme by which his obligations to the Indo-Mercantile Bank

were to be consolidated with certain other sums and for the total indebtedness a mortgage was to be got executed by the Mills thereby discharging, completely his indebtedness to the Bank. A fourth mortgage of the property of that company was consequently executed for a sum of Rs. 34,541-5-0. This amount which was the consideration for the mortgage was in satisfaction of the claim which the Indo-Mercantile Bank had against M and certain other amounts. Now these other amounts were made up in this way. The Indo-Mercantile Bank had a claim against one Ravi Verma who was a Director of the Mills. He was perfectly solvent and that amount could have been realized from him but instead of doing that M was given a credit to the extent of Rs. 12,083/-with a direction to him to realize Ravi Verma's dues to the Bank himself. M was also indebted to Rukmini, the sister-in-law of the appellant. For wiping out this liability a fixed deposit account for Rs. 6,000/-was opened in the Bank in the name of Rukmini. Cash money was not deposited and the consideration for the deposit was an undertaking by M to pay to the Bank and that liability was included in the total liability covered by the mortgage executed by the Mills. Subsequently the fixed deposit amount of Rs. 6,000/-was withdrawn by Rukimini. Thus, the High Court found that the three items of consideration for the mortgage which had been created on a defunct company like the Mills were, (1) the wiping out of the liability of M to the Bank to the extent of Rs. 14,623-4-2 which consisted of a sum of Rs. 13,000/-and interest; (2) wiping out of liability of Ravi Verma a solvent debtor of the Indo-Mercantile Bank to the extent of Rs. 12,083/9/7 and (3) the creation of the fixed deposit for the benefit of the fourth respondent for a sum of Rs. 6,000/-. The appellant obviously got the benefit for bringing about this transaction because of his relationship with Rukimini.

5. The High Court found that the assets of the Mills were worth not even Rs. 10,000/-and to obtain a fourth mortgage of the property of that company could not be an error of judgment on the part of the Directors but it was designed and calculated arrangement made with a view to benefit, at the expense of the Bank, M, the appellant and Ravi Verma. It was not possible to believe that the Directors were not aware of the financial condition of the Mills. The security which was thus taken was merely illusory and when the transaction was approved at the meeting of the Directors held on July 22, 1949 the Directors present were M, the appellant and respondent No. 2 before the High Court. The Division Bench quite rightly did not agree with the learned Single Judge that all these transactions which were tell tale were the result of an error of judgment. On the contrary there was a clever plan and design behind the creation of the mortgage. As regards the appellant this is what was observed:

The fourth respondent P. K Nedungadi, was undoubtedly the guiding spirit for the fraud perpetrated by the first respondent. He obtained a benefit on opening a fixed deposit in favour of his sister-in-law, and realising the same while he was in active management, as the Managing Director of the Bank. But scruples were not amongst his virtues is plain from the fact that he who engineered the mortgage transaction described the same within the few months thereof in his report to the Directors. He should be made liable to the entire extent. But for his help, the first respondent could not have avoided his liability or been permitted to realise the unpaid purchase money from the Mannadiar Saw and Oil Mills Ltd., which he had no hopes of realising. He should be made liable to the entire amount decreed against the first respondent Under Section 235 of the Indian Companies Act, 1913 which was in force at the

material time the Court has been given the power to assess damages against the delinquent Directors, etc. If the money or the property of the Company has been misapplied or there has been misfeasance or breach of trust in relation to the company by a Director, an officer or other persons mentioned in the section the Court, after examining the matter, can compel him to repay or restore the property with interest at such rate as the court may think fit or to contribute such sums 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 fit. It has been expressly declared that the section shall apply notwithstanding that the offence is one for which the offender may be criminally responsible. In Halsbury's Laws of England, 3rd Edition, Volume 6, it has been stated at page 623 that misfeasance and breach of trust include a breach by a Promoter, Director etc. of a duty to the Company the direct consequence of which has been a misapplication or loss of its assets for which he could be made responsible in an action. Allegations or proof of fraud are not essential and it is immaterial that the offence is one for which the offender may be criminally liable.

6. In the present case the High Court has found and that finding has not been shown to be wrong or erroneous in any manner that it was the appellant who enabled M to perpetrate the fraud which apparently resulted in loss to the Company. The appellant himself also derived a certain benefit from the fraudulent acts of M. He would thus be clearly liable to repay or restore to the Bank the amount in respect of which there was misapplication, misfeasance and breach of trust resulting in loss to the Company. The appellant cannot escape liability for the entire amount for which an order has been made against him by the High Court.

7. In the result this appeal fails and it is dismissed with costs.