

(1965) 01 CAL CK 0001

Calcutta High Court

Case No: Civil Revision Case No. 1710 of 1961

Shri Kishan Rathi

APPELLANT

Vs

Mondal Brothers and Co.
(Private) Ltd. and Another

RESPONDENT

Date of Decision: Jan. 27, 1965

Acts Referred:

- Companies Act, 1956 - Section 292(1), 292(2), 47, 9

Citation: (1967) 37 CompCas 256 : 70 CWN 164

Hon'ble Judges: P.B. Mukharji, J

Bench: Single Bench

Advocate: Brotendra Nath Banerjee, for the Appellant; Anil Kumar Sinha and D.N. Trivedi, for the Respondent

Judgement

P.B. Mukharji, J.

This application under article 227 of the Constitution raises an important point of company law.

2. The dispute arises on a loan of Rs. 1,000 granted by the plaintiff-petitioner to the defendant company on a bill of exchange being a hundi for Rs. 1,000. On November 22, 1958, the defendant limited company drew a hundi for Rs. 1,000 on the second defendant, Ram Chandra Nag, who is also an opposite party here, payable to the plaintiff 90 days after date without grace which was accepted by the second defendant. It is the plaintiff's case that the hundi was presented to the defendants for payment but the hundi was dishonoured. The plaintiff sent letters of demand, but the money due was not paid. There was a reply by the defendant company on August 3, 1959, denying the hundi and the loan. The plaintiff filed the present suit on December 3, 1959, before the Small Cause Court, Calcutta.

3. The trial court decreed the suit of the plaintiff in full with costs. The only contestant was the first defendant, the limited company. The acceptor did not

appear. It is on record before the trial court, on the evidence of P.W. 1, Kishan Rathi, the plaintiff himself, that Naresh Chandra Mondal, director and the manager of the defendant-company, purchased the stamp for the defendant company in respect of the hundi, that Naresh wrote the hundi in his presence and affixed the company's rubber stamp on the hundi in his presence. On behalf of the defendant company, its director, Sambhu Nath Mondal, gave evidence. His evidence was that the hundi was not signed on behalf of the defendant company, that the account books of the defendant company, cash books and the balance-sheet showed that this money on the hundi, the sum of Rs. 1,000, never entered the till of the company and even the rubber stamp was not of the defendant company. This Sambhu Nath Mondal is, however, a cousin of Naresh Chandra Mondal, the maker and drawer of the hundi. Naresh was in November, 1958, when the hundi was drawn, a director and manager of the company. According to Sambhu's evidence, Naresh resigned from the company some time in February, 1959, i.e., a few months after the date of the execution of the hundi.

4. The defendant company applied for a new trial u/s 38 of the Presidency Small Cause Courts Act against this decree. The Full Bench of the Small Cause Court allowed the application and set aside the decree against the first defendant. The Full Bench found as a fact that Naresh Chandra Mondal was both manager and director of the defendant company at the time when the hundi was executed and that he had since resigned. The reason why the Full Bench of the Small Cause Court set aside the decree of the trial judge can be stated briefly.

5. According to the Full Bench, Section 9 of the Companies Act, 1956, makes a certain clause in the articles of association of this defendant company repugnant to the Companies Act and, therefore, void to the extent of its repugnancy. Section 9 of the Act provides as follows :

" Save as otherwise expressly provided in the Act:--

(a) the provisions of this Act shall have effect notwithstanding anything to the contrary contained in the memorandum or articles of a company, or in any agreement executed by it, or in any resolution passed by the company in general meeting or by its board of directors, whether the same be registered, executed or passed, as the case may be, before or after the commencement of this Act; and

(b) any provision contained in the memorandum, articles, agreement or resolution aforesaid shall, to the extent to which it is repugnant to the provisions of this Act, become or be void, as the case may be. "

6. Then the Full Bench relies on Section 292 of the Companies Act which mentions " certain powers to be exercised by the board only at its meeting " and that such act can only be done by means of a resolution passed at the meeting of the Board and that included the power to borrow money otherwise than by a debenture.

7. From these two Sections 9 and 292 of the Companies Act, the Full Bench of the Small Cause Court drew the conclusion that the articles and memorandum of this company authorising the directors to borrow money were bad and repugnant and that as the books of resolutions or the minute book of the directors has not been proved by the plaintiff, there was nothing to show that this money was borrowed in accordance with Section 292 of the Companies Act. On that finding the Full Bench of the Small Cause Court came to the conclusion that Naresh Chandra Mondal, the manager and director of the limited company had no legal authority to borrow money to bind the company. Therefore, the Full Bench set aside the trial court's decree and dismissed the plaintiff's suit.

8. The plaintiff now has applied under article 227 of the Constitution.

9. The judgment and order of the Full Bench of the Presidency Small Cause Court cannot be sustained. It is based on a number of assumptions which are wrong in law and erroneous.

10. The Full Bench failed to realise that the onus of proving that there was no resolution was upon the defendant company and not upon the plaintiff. The minute books and the book of resolution of the board of directors are books of the company and are not open to strangers and outsiders. This was also within the special knowledge of the defendant company. If the defendant company was trying to prove that its manager and director had no authority to borrow money, then it was for the company to prove from its own books of minutes and resolutions that no authority was given to Naresh Chandra Mondal, its manager and director. Section 106 of the Evidence Act says that when any fact is specially within the knowledge of any person, the burden of proving that fact is upon him. It is strange that neither the defendant company nor its witness, director Sambhu Nath Mondal, produced the minute book or the book of resolutions in this case. The only inference that can be drawn from such non-production on the facts and circumstances of this case is that, had they been produced, they would have shown that there was good authority and resolution in favour of Naresh Chandra Mondal. That presumption is irresistible in this case. Articles 103 and 114 of the articles of association of this company cast a mandatory duty upon the directors to record minutes of the proceedings of all meetings of the directors in the minute book. The defendant company or its director witness, Sambhu Nath Mondal, being in possession of such minute book and being in special knowledge of the contents of that minute book, it was their duty to produce them and not the duty of the plaintiff.

11. The next point on which the Full Bench of the Small Cause Court went wrong is concerned with the broader question of the Companies Act and the Negotiable Instruments Act. In the first place, the Full Bench was wrong in holding that articles 61 and 62 of this defendant company were inconsistent with Section 292 of the Companies Act. Articles 61 and 62 of this defendant company in material portions read as follows ;

" 61.....The directors may from time to time borrow from the members or other persons and may themselves lend any sum or sums of moneys for the purposes of the company.

62. ... The directors may raise or secure the repayment of such moneys in such manner and upon such terms and conditions.....by making, drawing, accepting or endorsing on behalf of the company any promissory notes, hundies or bills of exchange....."

12. These articles, in my view, are in no way in conflict with or repugnant to Section 292(1) of the Companies Act. Section 292(1) of the Companies Act deals with certain powers to be exercised by the board only at a meeting and lays down, inter alia :

" The board of directors of a company shall exercise the following powers on behalf of the company, and it shall do so only by means of resolutions passed at meetings of the Board :-

(e) the power to make loans."

13. Reading Section 292(1) of the Companies Act and articles 61 and 62 of the defendant company, it will be quite clear that they are not inconsistent. The articles do not say anything about the procedure by which the board of directors will act. They grant the power to the directors to borrow money on a bill of exchange. The articles deal only with the director's powers to borrow on a promissory note or a hundi. They do not enjoin any particular procedure to exercise that power to borrow. The first error of the Full Bench of the Small Cause Court was, therefore, to hold that these articles are repugnant to Section 292(1) of the Companies Act. If the articles had stated that the board of directors could exercise that power to borrow money without a resolution at a meeting of the board, then, of course, that provision would have been repugnant to this section. But articles 61 and 62 do not say so in the present case.

14. The mistake of the Full Bench lay in confusing the provision for power with the provision of the procedure for the exercise of that power.

15. The next error of the Full Bench is to overlook the proviso to Section 292(1) of the Companies Act, which says, inter alia:

" Provided that the board may, by a resolution passed at a meeting, delegate tothe manager of the company.....the powers specified in clauses (e) to the extent specified in Sub-sections (2)(3) and (4) respectively."

16. That means that the delegate may be the manager, which in this case the drawer of the hundi, Naresh Chandra Mondal, admittedly was. Whether there was resolution by the board of directors delegating such power again is a fact within the special knowledge of the defendant company and its directors. They could have easily produced the resolution book or the minute book to show that there was no

such delegation. But they had not done so and, therefore, an adverse inference must be drawn against them to the effect that, had they produced them, they would have shown such delegation to the manager, Naresh Chandra Mondal.

17. Non-production of the most vital and crucial document, the minute book and the book of resolution of the directors, is not the only point against the defendant company. The defendant company did not even call Naresh Chandra Mondal and gave no reason why the company could not or did not call him who actually executed and drew the hundi for and on behalf of the company. True it is that Naresh was no longer a director at the time of the trial, but then that is not enough. It is not said that Naresh could not be called by the company. It is not even alleged that there is any strained relationship or enmity between Naresh and the company. Indeed, the director who came to give evidence on behalf of the company at the trial, Sambhu Nath Mondal, is himself a cousin of Naresh Chandra Mondal. That being so, the failure of the defendant company to call the most important witness, namely, the drawer of the hundi in the case, can only confirm the adverse inference drawn from the non-production of the most important document, the minute book and the resolution book.

18. In that context, the fact that this money on the hundi did not find its way to the till of the company by reason of the fact that it is not shown in the company's books of account for 1958-59 marked Exts. B and B/i and the ledger of the company marked Ext. C along with the company's balance-sheet marked Ext. D of 1958-59 cannot prejudice an independent third party stranger-creditor who is advancing money to the company on a bill of exchange. If a director or a manager with ostensible authority under the memorandum and the articles of association of the company practices a fraud upon his own company by not placing the money in the coffer of the company, that cannot defeat a bona fide creditor's claim against the company.

19. This raises the important question of law relating to the internal management of the company. I shall presently deal with the law on the subject, but, before doing so, some reference to further clauses in the articles and the memorandum of the company will clear the ground. The first point to emphasise in this respect is that the director's power to borrow money for the company on a hundi or a promissory note or a bill of exchange is plainly recognised both in the memorandum and in the articles. I have already cited Article 61 of the company. I shall refer here to Clause 3 (h) of the memorandum specifying the objects of the company which include, inter alia, the object of--

"Borrowing or raising money in such manner as the company shall deem fit and in particular by the issue of bills of exchange, promissory notes or other obligations....."

20. The position of the drawer of the hundi in this case must also be emphasised. The drawer, Naresh Chandra Mondal, was at the time he was drawing the hundi, not only a director of the company but also its manager. Article 95 of the company shows that Naresh Chandra Mondal was one of the first four directors of the company and it also declares that "Naresh Chandra Mondal, B.Sc., shall be the first manager of the company". Article 98 of the company expressly recognises, *inter alia*, that:

"The directors may from time to time entrust to and confer upon a managing director or manager for the time being such of the powers exercisable under these presents by the directors as they may think fit and may confer such powers for such time and to be exercised for such objects and purposes and upon such terms and conditions as they think expedient....."

21. Article 100 expressly recognises the directors' full power to make and sign such contracts and to draw, endorse, accept and negotiate on behalf of the company all such bills of exchange, promissory notes, hundies, cheques, drafts and other instruments, etc. From a review and analysis of all these relevant articles it is indisputable on the facts of the present case that the director and the manager, Naresh Chandra Mondal, had *prima facie* authority to draw the hundi on behalf of the company. The lender who lends money to the company in those circumstances on a promissory note or a bill of exchange executed by the manager and the director after having found on inquiry from the memorandum and the articles the existence of such power to borrow, need not and cannot, and is not obliged, in my view, to look further into the internal management of the company and embark on an investigation whether a particular manager or director who is given such powers under the memorandum and the articles has nevertheless lost it or qualified or limited it by an internal resolution contained in the internal minutes book or resolution of the company's directors and if so what are the terms of such qualification or limitation? This is exactly what is meant by internal management,

22. A person taking in due course a bill of exchange or hundi signed by a director who, consistently with the company's articles, might have been, but who was not in fact authorised to sign bills or hundis is, upon the principle of *Royal British Bank v. Turquand* (1856) 6 E1. & B1. 327 entitled to assume that the director was "acting under its authority" when he signed the bill, and to recover on the bill or hundi against the company accordingly. If any authority is needed for the proposition, it is *Dey v. Puttinger Engineering Co.* [1921] 1 K.B. 77 dissenting from *Premier Industrial Bank Limited v. Carlton Manufacturing Co. Limited & Crabtree* [1909] 1 K.B. 106. In this connection a more recent decision in *British Thomson-Houston Co. v. Federated European Bank Limited* [1932] 2 K.B. 176 : [1933] 3 CompCas 106 may also be seen. No doubt, if the bill is signed by a local manager or other persons who cannot properly be assumed to have, and is not held out as having authority to sign bills for the company, then the position is different, as pointed out in *Credit-bank Cassel v.*

Schenkers [1927] 1 K.B. 826. No doubt, again, if a person has not, in fact, knowledge of the existence of the power of delegation contained in the company's articles, he cannot rely upon its suggested exercise, a point which was made clear in the decision in Houghton (J.C.) & Co. v. Nothard, Lowe and Wills Ltd. [1927] 1 K.B. 246 affirmed by the House of Lords in [1928] A.C. 1, although on different grounds. Again, if there is any collusion or fraud between the director drawing the hundi or the bill and the creditor or the lender, then, if that fraud or collusion is proved, that will vitiate certainly the transaction, and the bill or the hundi will not be binding upon the company. But be it said that there is no such case of fraud or collusion between Naresh Chandra Mondal and the plaintiff in this case. As Buckley points out in the 13th edition of the Companies Act at page 209 that, if the borrowing power of the company itself" as distinguished from that of the directors is limited, the lender cannot rely upon the principle of Royal British Bank v. Turquand, and say that he was entitled to presume that the limit was not being exceeded. But even then if a company which has power to borrow money for the purposes of its business borrows for an illegitimate purpose, the loan is good in the absence of knowledge of the lender that the borrowing was for a wrong purpose: In re Payne (David] & Co. : Young v. David Payne and Co. [1904] 2 Ch. 608 and Sinclair v. Brougham [1914] A.C. 398. The learned commentator at page 373 of the said edition of the Companies Act points out that outsiders are bound to know what Lord Hatherley called the " external position of the company " in Mahony v. East Holyford Mining Co. (1875) L.R. 7 H.L. 869 at page 893, but are not bound to know its " Indoor management ", If persons are held out as and act as directors, and the shareholders do not prevent them from so doing, outsiders are entitled to assume that they are directors, and, as between the company and such outsiders, the acts of such directors de facto will bind the company. A stranger dealing with a company has a right to assume, as against the company, that all requirements of internal management have been duly complied with. This was clearly laid down in a number of decisions beginning from Royal British Bank v. Turquand and such cases as Totterdell v. Fareham Blue Brick and Tile Co. (1866) L.R. 1 C.P. 674, In re Romford Canal Co. (1883) 34 Ch. P. 85, Montreal and St. Lawrence Light and Power Co. v. Robert [1906] A.C. 196 (P.C.) at page 222 and in the more recent decision of the House of Lords in Morris v. Kanssen [1946] A.C. 459 : 16 CompCas. 186.

23. It is exactly here that the Full Bench of the Small Cause Court went wrong in not realising that a bona fide creditor-stranger who lent money on a hundi or a bill of exchange has a right to assume as against the company that all requirements of the internal management have been duly complied with, such as, necessary resolutions are there on the directors book to make them regular and that the directors have acted according to the procedure enjoined in their board meeting. In this connection reference may also be made to the same edition of Buckley on the Companies Acts at page 83 in support of the view expressed above.

24. There is also another relevant section of the Companies Act which the Full Bench of the Small Cause Court failed to notice. That is Section 47 of the Companies Act. That section lays down that a bill of exchange, hundi or a promissory note shall be deemed to have been made, accepted, drawn or endorsed on behalf of the company if drawn, accepted, made or endorsed in the name of, or on behalf of, or on account of, the company, by any person acting under its authority, express or implied. Here, on the facts, the authority of Naresh Chandra Mondal was both express and implied. The hundi itself shows on its very face that "it is drawn for and on behalf of Mondal Brothers and Co. (Private) limited." The endorsement on the back of the hundi also shows that the stamp paper of the hundi was purchased for Mondal Brothers & Co. (Private) Limited. That being so and Section 47 making it expressly clear that it shall be deemed to have been made by the company, all the onus on the facts and circumstances of this case is upon the defendant company to show that this hundi did not bind the company at all. I must say that nothing at all has been shown to prove that the hundi does not bind the company on the face of it. Naresh Chandra Mondal's alleged lack of authority has not been proved and established in the circumstances mentioned above.

25. For these reasons this rule must succeed. A last minute effort was made by Mr. Sinha for the defendant company that there was really no presentment of the hundi. I am afraid, this point of fact about presentment cannot now be entertained. It was not taken by the company in its application u/s 38 of the Presidency Small Cause Courts Act before the Full Bench as one of the grounds to set aside the judgment. Besides, the facts are eloquent on the record. There was a demand letter mentioning the hundi and its non-payment. In fact, there was also a reply by the defendant company.

26. I, therefore, make the rule absolute with costs and set aside the order and judgment of the Full Bench of the Small Cause Court and restore the decree of the trial court. In other words, the suit will be decreed in full with costs as against the first defendant company and ex parte against the second defendant as ordered by the trial court.

27. Liberty is given to withdraw the money already deposited by the defendant company-opposite party No. 1.