K. Joseph Augusthi and Two Ors

Vs

M. A. Narayanan, Official Liquidator, Palai Central Bank Ltd.

Civil Appeals Nos. 254 to 256 of 1963

(CJI P. B. Gajendragadkar, K. N. Wanchoo, J. C. Shah, N. Rajgopala Ayyangar S. M. Sikri JJ)

11.03.1964

JUDGMENT

GAJENDRAGADKAR, C.J. –

Two questions of law have been raised before us by Dr. Seyid Muhammad on behalf of K. Joseph Augusthi, the appellant in Civil Appeal No. 254/1963. Both of them are related to section 45G of the Banking Companies Act, 1949 (No. X of 1949) (hereinafter called the Act). The first question raised has reference to the validity of the said section and the second to its true scope and effect. Dr. Seyid Muhammad contends that the answers given by the Kerala High Court to both these questions are erroneous. According to him, s. 45G is unconstitutional inasmuch as it contravenes the fundamental right guaranteed to the citizens of this country by Art. 20(3) of the Constitution. He also argues that in making an order for the public examination of the appellant, the High Court has misconstrued the scope and effect of the relevant provisions of the said section.

The appellant, Joseph Augusthi, was the Managing Director of the Palai Central Bank Limited from 26-1-1927, to 8-8-1960; K. George Thomas and George Joseph who are the appellants in the two other appeals Nos. 255 and 256 of 1963 respectively, were the Directors of the said Bank; the first of them was the Director from 14-1-1935 to 8-8-1960 and the latter from 26-1-1927 to 8-8-1960.

An application for the winding up of the said Bank was made before the Kerala High Court by the Revenue Bank under section 38(3)(b)(iii) of the Act. The said provision justifies the making of an application by the Reserve Bank in case in the opinion of the Reserve Bank, the continuance of the banking company in question is prejudicial to the interests of the depositors. On the 8th August, 1960, an order was passed on the said application appointing the Official Liquidator of the High Court the Provisional Liquidator of the Bank. The order of winding up then followed on the 5th December, 1960, and on the 8th December, 1960, an Official Liquidator was appointed under section 39 of the Act. After the Official Liquidator came on the scene, he made three reports to the High Court - report No. 192 on the 17th August, 1961; report No. 242 on 29th September, 1961; and report No. 350 on the 4th December 1961. All these reports were made under s. 45G(1) of the Act. The appellants filed their objections on the 23rd November, 1961, to the first two reports. The matter was then considered by the learned single Judge of the Kerala High Court and after hearing the parties, he made an order directing the public examination of the three appellants under s. 45G(2).

This order was challenged by the appellants by preferring three appeals before a Division Bench of the High Court. The Division Bench agreed with the view taken by the learned single Judge and dismissed the three appeals. The appellants then applied for and obtained certificates from the High

Court and it is with the said certificates that they have come to this Court by the present three appeals.

The first point which has been argued before us by Dr. Seyid Muhammad is that s. 45G is unconstitutional because it contravenes the fundamental rights guaranteed by Art. 20(3). In order to appreciate this argument, it is necessary to read s. 45G(1) and (2).

> "(1) Where an order has been made for the winding up of a banking company, the official liquidator shall submit a report whether in his opinion any loss has been caused to the banking company since its formation by any act or omission (whether or not a fraud has been committed by such act or omission) of any person in the promotion or formation of the banking company or of any director or auditor of the banking company.
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> (2) If, on consideration of the report submitted under sub-section (1), the High Court is of opinion that any person who has taken part in the promotion or formation of the banking company or has been a director or an auditor of the banking company should be publicly examined, it shall hold a public sitting on a date to be appointed for that purpose and direct that such person, director or auditor shall attend thereat and shall be publicly examined as to the promotion or formation or the conduct of the business of the banking company, or as to his conduct and dealings, in so far as they relate to the affairs of the banking company :

Provided that no such person shall be publicly examined unless he has been given an opportunity to show cause why he should not be so examined."

The other sub-sections of this section need not be cited, because it would be enough for our purpose to notice, in substance, what their effect is. Sub-section (3) allows the Official Liquidator to take part in the examination and to employ such legal assistance as may be sanctioned by the High Court, if he is specially authorised by the High Court in that behalf. Sub-section (4) permits the creditor or contributory to take part in the examination either personally or by any person entitled to appear in the High Court. Sub-section (5) gives authority to the High Court to put questions to the person who is being examined; sub-section (6) empowers oath to be administered to the said person and compels him to answer questions as may be put to him by the High Court, or as the High Court may allow to be put to him. Under sub-section (7), such a person is entitled to appear by a lawyer and the lawyer so appointed shall be at liberty to put to him such questions as the High Court may deem fit just for the purpose of enabling him to explain or qualify any answer given by him; there is a proviso to this sub-section which authorises the High Court to make an order for costs in its discretion in case the person under examination is exculpated from any charges made or suggested against him. Sub-section (8) deals with the procedure to be followed in keeping a record of the examination. Sub-section (9) provides that where after the examination of the person, the High Court is satisfied that a person, who has been a Director of the banking company, is not fit to be a director of a company, or an auditor, or a partner who has been acting as such auditor, is not fit to be such an auditor or partner, the High Court may make an order that that person shall not, without the leave of the High Court, be a director of, or in any way, whether directly or indirectly, be concerned or take part in the management of, any company, or, as the case may be, act as an auditor of, or be a partner of a firm acting as auditors of, any company for such period not exceeding five years as may be specified in the order.

Thus, it will be clear that the scheme of s. 45G is first to decide whether, prima facie, there is a case for the public examination of a person; then in deciding this question, give an opportunity to the person concerned; if it is decided to hold a public examination of the said person, proceed to hold that examination; if suggestions made against the person examined are found to be unwarranted, make an order of costs in his favour; and if the person concerned is found to have been responsible for acts or omissions which caused loss to the banking company, to make a penal order disqualifying such person from acting as a director or an auditor as indicated by sub-section (9). It is in the light of this scheme that the argument about the contravention of Art. 20(3) falls to be examined.

> Article 20(3) provides that no person accused of any offence shall be compelled to be a witness against himself. It may be conceded that when a person is compelled to submit to a public examination, that itself, prima facie, looks like pillorying him in the public gaze. It is also true that s. 45G(6) compels the person to answer questions which the High Court may put to him, or which the High Court may allow to be put to him, and it is quite likely that in cases where public examination is ordered to be held, some suggestions and even some charges may be levelled against the person examined by reference to his acts or omissions in relation to the promotion, formation or conduct of the banking company of which he was a director or an auditor. Therefore, there is no difficulty in holding that a person examined publicly under s. 45G may, in some cases, be compelled to be a witness against himself. Thus, one element of Art. 20(3) is satisfied; but the question still remains whether the other essential element is satisfied or not.
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> Article 20(3) guarantees to every citizen the fundamental right not to be compelled to be a witness against himself, provided the person who is being compelled in that way, is accused of any offence. In other words, it is only when a person can be said to have been accused of any offence that the prohibition prescribed by Art. 20(3) comes into operation. If a person who is not accused of any offence, is compelled to give evidence, and evidence taken from him under compulsion ultimately leads to an accusation against him, that would not be a case which would attract the provisions of Art. 20(3). The main object of Art. 20(3) is to give protection to an accused person not to be compelled to incriminate himself and that is in consonance with the basic principle of criminal law accepted in our country that an accused person in entitled to rely on the presumption of innocence in his favour and cannot be compelled to swear against himself. Therefore, unless it is shown that a person ordered to be publicly examined under s. 45G is, before, or at the time when the order for examining him publicly is passed, an accused person, Art. 20(3) will not apply.

What then is the position with regard to a person against whom an order for public examination is made by the High Court against the appellants ? All that has happened at the relevant time is that the official liquidator has submitted reports indicating that in his opinion, loss has been caused to the banking company under liquidation by the acts or omissions of the appellants, and the High Court, on considering the reports and taking into account the explanation given by the appellant, has come to the conclusion that, prima facie, a case has been made out for their public examination. In such a case, how can it be said that the appellants have been accused of any offence ? The whole object of the enquiry is to collect evidence and decide whether any acts or omissions caused loss to the banking company. It may be that as a result of the enquiry, the court may reach the conclusion that

the alleged acts or omissions did not cause any loss; in such a case, nothing further has to be done. On the other hand, it is likely that the opinion formed by the liquidator may be vindicated and the court may come to the conclusion that some or all of the acts or omissions on which the liquidator's opinion was based did cause loss to the banking company; and in that case, some action may conceivably be taken against the persons examined in addition to the action contemplated by s. 45G(9). That, however, only means that after the examination is over and the material adduced before the court has been examined by the court, an occasion may or may not arise to take any action. In such a case, what may conceivably follow cannot be said to be existing before the order is passed under s. 45G; an accusation may follow the enquiry, but an accusation was not in existence at the time when the public examination was ordered; and so, the appellants cannot contend that they were accused of any offence at the time when the order for their public examination was passed by the High Court. The accusation of any offence which is an essential condition for the application of Art. 20(3) is a condition precedent for the application of the principle prescribed by the said Article, and since this essential condition is lacking in all cases covered by section 45G, it is difficult to sustain the argument that the said section contravenes Art. 20(3). Therefore, we do not think Dr. Seyid Muhammad is right in contending that s. 45G is invalid on the ground that it contravenes Art. 20(3) of the Constitution. It appears that in the case of Mallala Suryanarayana v. The Vijaya Commercial Bank Ltd. [Civil Appeal No. 286 of 1959 decided on 26-10-1961], the same view has been expressed by this Court, though it may be added that this question does not appear to have been then elaborately argued.

In this connection, we may refer to a decision of this Court in Raja Narayanlal Bansilal v. Maneck Phiroz Mistry and Anr. [A.I.R. 1961 S.C. 29], where a somewhat similar provision contained in s. 240 of the old Companies Act fell to be considered and it was held that it did not contravene Art. 20(3) of the Constitution.

That takes us to the question of the construction of s. 45G. Dr. Seyid Muhammad contends that s. 45G requires that the acts or omissions alleged against a person should be acts which are prohibited by law, or omissions in relation to acts the performance of which is enjoined by law, and he suggested that if this interpretation is put on the words "acts or omissions", it would appear that the reports made by the liquidator in the present case have not made out any case for the public examination of the appellants. We are not impressed by this argument. It is significant that the acts or omissions to which s. 45G(1) refers need not be fraudulent acts or omissions, because, in terms, the section provides that the act or omission would attract s. 45G(1) if it has led to any loss to the banking company even though fraud may not have been committed by such act or omission. The context also shows that what the court has to consider, is whether any act or omission on the part of the director or the auditor of the banking company has caused any loss to the company. Now, such an act or omission need not necessarily be criminal; it may even include acts or omissions which are commercially unsound or unwise. In this connection, it may be recalled that s. 478 of the Companies Act which deals with a similar problem, requires that the report of the Official Liquidator should disclose his opinion that a fraud has been committed. To the same effect is the provision contained in s. 268 of the English companies Act (11 and 12 Geo. 6, c. 38). Therefore, it would, we think, be unreasonable to put a narrow and restricted construction on the words "acts or omissions" used by s. 45G(1).

Dr. Seyid Muhammad has then contended that in dealing with the reports made by the liquidator in the present case, the High Court has not given effect to the provision contained in the proviso to s. 45G(2). The said proviso requires that no person shall be publicly examined unless he has been given an opportunity to show cause why he should not be so examined, and Dr. Seyid Muhammad

argues that unless the matter is fully examined and an opportunity is given to him to show that the facts alleged in the reports are untrue, the requirements of the proviso will not have been satisfied and his grievance is that no such opportunity was given to the appellants in the present case. There is no substance even in this argument. What the Court has to do in exercising its power under s. 45G(2) is to consider the report made by the liquidator and decide whether it can reasonably entertain the opinion that any person who has taken part in the promotion or formation or conduct of the banking company should be publicly examined. In other words, it is a preliminary stage of the enquiry and the point which the Court has to consider is whether, prima facie, a case has been made out to hold a public examination of the person concerned. It cannot be the object of s. 45G(2) read with the proviso that the Court should allow the appellants to lead evidence rebutting the allegations made by the liquidator in his reports, for if such a course was adopted, it would itself develop into a full-fledged enquiry and the very object of a limited enquiry at the initial stage would be defeated. What the Court can and should do in such cases is to read the report submitted by the Official Liquidator, consider whether the opinion expressed in the report appears to be, prima facie, reasonable; hear the explanation of the person concerned; and find out prima facie whether the explanation tendered by the person is sufficient to reject the liquidator's request for such person's public examination and whether, on the whole, it is just and beneficial to the interest of the banking company that public examination should be held. The subject-matter of this preliminary investigation is not the whole of the enquiry on the merits; it is an enquiry as to whether the director or the auditor should be publicly examined. Therefore, we do not think Dr. Seyid Muhammad is justified in contending that the High Court has ignored the safeguard afforded to the appellants by the proviso s. 45G(2).

The question about the construction of s. 45G(1) & (2) does not present any serious difficulty. What must be disclosed by the report of the Official Liquidator is the act or omission of the person there specified which has led to loss to the banking company since its formation. The acts or omissions to which s. 45G(1) refers, when considered in the light of s. 45G(2), are acts or omissions "as to the promotion, or formation, or the conduct of the business of the banking company, or as to his conduct and dealings in so far as they relate to the affairs of the banking company", so that after the report is made, the court takes a broad and overall view of the state of affairs disclosed by the report and considers prima facie whether a case has been made out for the public examination of the director or the auditor. We are satisfied that the High Court has dealt with the matter precisely in this way, and no grievance can be made against its decision on the ground that the provisions of the proviso to s. 45G(2) have been ignored.

In support of his argument that the High Court has misconstrued the effect of the provisions of s. 45G(1), Dr. Seyid Muhammad referred to two decisions which may be mentioned at this state. The first of these is the decision of the House of Lords in Ex parte George Stapylton Barnes [[1896] A.C. 146 at p. 152]. In that case, the question which fell to be considered was the scope and effect of s. 8(3) of the Companies (Winding-up) Act, 1890; Lord Halsbury observed that he entertained not the smallest doubt that the meaning of this legislation is that, in order to give the Court jurisdiction to make an order for public examination, there must be a finding of fraud, and a finding of fraud against an individual who is thereby made subject to being summoned before the Court, and is compelled to answer, whether the answer incriminates him or not, but, being exculpated, receives his costs. He further observed : "I confess I am unable, looking at the whole of the legislation on the subject, to entertain the least doubt that that was what the Legislature intended, and I am a little surprised, I confess, that there should have been any doubt that fraud must be found." In our opinion, this passage is hardly relevant for our purpose, because as we have already indicated, s. 45G(1) expressly provides that the act or omission complained of need not necessarily

be fraudulent, and so, there can be no question, under s. 45G(1), of coming to a conclusion that fraud has been committed before directing public examination of a person.

The other decision on which Dr. Seyid Muhammad has relied is the judgment of the Bombay High Court in Sir Fazal Ibrahim Rahimtoola v. Appabhai G. Desai [A.I.R. 1949 Bom. 339]. In that case, dealing with the provisions contained in s. 196 of the old Companies Act, Chagla C.J. disapproved of the practice of ordering ex parte public examination of persons. In that connection, he quoted with approval the warning sounded by Sir Lawrence Jenkins in the Ahmedabad Advance Spinning and Weaving Company v. Lakshmishanker [I.L.R. 30 Bom. 173], that the practice of passing ex parte orders involving the person affected in serious liability is much to be deprecated. In that case, the Bombay High Court was called upon to consider whether the allegations made against the director were vague and indefinite. As we will presently point out, that difficulty does not arise in the present appeals. The allegations made by the liquidator in his reports against the appellants are clear, precise and definite.

Let us now refer to the reports submitted by the liquidator in the present case. In his first report, the liquidator has stated that in carrying out the affairs of the bank, the Directors, with the help of officers appointed by them out of their own relatives, have not properly conducted the affairs of the bank. He has also stated that in his opinion, loss had been caused to the bank since its formation by the acts and omissions of the Directors and of the auditor of the bank. The report then proceeds to specify the extent of the loss and the causes for the said loss. It appears from the report that loans were advanced by the bank without regard to the question of any adequate security. In many cases, loans were advanced without any security at all and the inevitable consequence has been that a large number of debts have become barred by time long before the winding up proceedings were started. The bank appears to have paid dividends without earning profits. Similarly, though it did not earn any profits between 1936 to 1958, it submitted reports showing substantial amounts as net income and so, it has paid income-tax on the said amounts. A large amounts of advances appears to be irrecoverable. At the end of his report, the liquidator has mentioned 10 persons, including the three appellants before us, whose acts and omissions, in his opinion, contributed to loss to the banking company. Two further reports were made by the liquidator and they support the opinion expressed by him in his first report. The third of these reports was filed after this matter was heard by the learned Single Judge but the first two reports themselves fully justify the order made by him, and so, the third report can well be left out of consideration.

When we turn to the objections filed by the appellants, it is clear that some of the facts are not seriously disputed. Take, for instances, the allegation that dividends were declared without earning profits. The appellant Joseph Augusthi contended before the High Court that the bank used to treat interests accrued on advances, though not received, as income, and so, income-tax and super-tax were paid on such income and dividends were also paid on the same basis. He suggested that the Reserve Bank had noticed these facts and had waived its objection. In other words, he relied on a practice which is obviously unsound in a commercial sense and pleaded that at this stage the Reserve Bank cannot challenge the correctness or propriety of the said practice. This practice has been described by the appellant as mercantile system of accounting. It would thus be seen that some of the facts alleged by the liquidator in his report are not disputed; the effect of those facts was a matter of argument between the parties before the High Court. In such a case, we do not see how the appellants can successfully challenge the correctness of the view taken by the High Court that a case had been made out for the public examination of the appellants. That is why we do not think there is any substance in the argument urged before us by Dr. Seyid Muhammad that on the facts, an opportunity had not been given to the appellants to show that their public examination should not be

ordered. We are satisfied that in dealing with the facts of this case, the Courts below have taken into account the reports made by the liquidator and after considering the objections raised by the appellants, they have come to the right conclusion that the appellants should face a public examination.

The result is the appeals fail and are dismissed with costs. One set of hearing fees.

Appeal dismissed.

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