HON'BLE SRI JUSTICE CHALLA KODANDA RAM

WRIT PETITION No.9370 OF 2006

ORDER:

Heard learned Senior Counsel Sri A. Satya Prasad for the petitioners, Dr. P.B. Vijay Kumar, learned counsel for the 3rd respondent and Sri V.V. Narayana Rao, learned counsel for the 4th respondent and learned Government Pleader for the official respondents 1 and 2.

The present writ petition is filed assailing the orders dated 25.01.2006 in O.A.No.57 of 2005 passed by the A.P. Cooperative Tribunal, Visakhapatnam (in short "the Tribunal") in confirming the Orders dated 07.05.2005 in ARC No.11/2004-05 passed by the 1st respondent-Assistant Registrar-cum-Arbitrator, Office of the Dy. Registrar of Cooperative Societies, Visakhapatnam.

The 3rd respondent-The FCI Employees Cooperative Society Ltd., invoked the provisions under Section 62 of the A.P. Cooperative Societies Act (in short "the Act") against the petitioner-society for recovery of a sum of Rs.20,00,000/- with interest. The 2nd respondent arbitrator passed an Award in A.R.C.No.11/2004-05, dated 07.05.2005 rejecting the defence raised by the petitioner society that it had not received the sum of Rs.20,00,000/- and in fact the 4th respondent, who was the officiating secretary, had played fraud on the society as well as on the 3rd respondent and misutilised a sum of Rs.20,00,000/- and thus there is no liability on the part of the petitioner society to refund the money to the 3rd respondent society. The Award was challenged before the Tribunal, which also confirmed the Award by an order dated 25.01.2006 passed in O.A.No.57 of 2005. Assailing the Award made under Section 62 of the Act as confirmed in appeal by the Tribunal, the present writ petition is filed.

Sri A. Satya Prasad, learned senior advocate for the petitioner, by copiously taking this Court through the orders of the Arbitrator as well as the orders of the Tribunal, contends that both the authorities have grievously erred in appreciating the facts on record, particularly the fraud played by the 4th respondent in opening a separate account in the Post Office in the name of the petitioner-Society and depositing the cheques issued by the 3rd respondent society in that account and thereafter drawing the money for his personal gains. Further learned senior counsel contends that the 4th respondent had forged the board resolutions and other documents for misappropriating the amount and inasmuch as, the petitioner-society had never received the money, the arbitrator as well as the appellate tribunal had erred in fixing the liability on the petitioner society and thus erred in appreciating the said facts. Learned senior counsel would submit that it is well settled that fraud vitiates everything from the beginning and as the record revealed that the 4th respondent has played fraud, there is no liability on the petitioner society. Learned Senior Counsel Sri A. Satya Prasad also contends that the fact that the 4th respondent played fraud on the petitioner society and misutilised the society's funds, now stands confirmed by the surcharge orders passed by the 2nd respondent against the 4th respondent and other Directors on 24.05.2008. In that view of the matter, learned counsel for the petitioner prays for dismissal of the surcharge proceedings.

On the other hand Dr. P.B. Vijay Kumar, learned counsel appearing for the 3rd respondent, supports the orders of the Arbitrator as well as the Tribunal and contends that there is a collusion between the office bearers of the petitioner and the 4th respondent and at any rate the amounts were deposited into the petitioner society's account and thus it is the Society who is responsible for the monies received from them. He further contends that petitioner society may have recourse to the 4th respondent, but that by itself does not absolve the petitioner society to refund the money, which is found to have been received by the petitioner society.

The contention of Sri V.V. Narayana Rao, learned counsel for the 4th respondent, is that for the first time 4th respondent was made as a party respondent before the Tribunal without his being a party in the arbitration proceedings and as such the order passed by the Tribunal shall not bind his client.

Learned Government Pleader supports the orders of the Tribunal.

Having considered the crux of the matter, the controversy in issue raised in a narrow compass and certain facts are not in dispute. The fact that the 3rd respondent society was approached by the 4th respondent seeking money to be deposited in the petitioner society, is not in dispute. The petitioner society originally had its bank account at Andhra Bank, Woodpeta Branch, Anakapalle, in which Rs.5,00,000/- cheque was deposited and a parallel account was opened at Head Post office and the cheques worth of Rs.15,00,000/- were encashed and credited to the accounts in the name of the petitioner's society. Upto this aspect there is no dispute. The contention urged by the petitioner society is that it was the 4th respondent, who had played fraud. In the enquiry proceedings it was categorically found that the Board of Management virtually was always being guided by the 4th respondent had reposed great trust in him. The 4th respondent specifically contended that there was Board resolutions to open account and in fact the books of accounts were maintained properly and further the amounts received were utilised for disbursement of loans, repayment to District Central Cooperative Bank, Anakapalli and advances payments to members of society. All these transactions have been recorded in the society's books of account and signed by them.

The argument of the petitioner society that the 3rd respondent had given Rs.20,00,000/- is highly irregular and by violating the byelaws of the petitioner society and the GOs governing the same, would made the deposits good as *non est* in law, was also rejected. On appreciation of evidence that was brought before the petitioner society as well as the 4th respondent society, the arbitrator came to the conclusion that both the petitioner society as well as the 3rd respondent society had violated various norms in collecting the deposits and giving deposits. However, the fact of the matter is that the petitioner society had received Rs.20,00,000/- is confirmed. As a matter of fact, the arbitrator found that both the petitioner and respondent societies had given a goby to various practices and strictly did not follow the procedures prescribed. As the petitioner society failed to produce the minutes books, the contention of the petitioner society that there was no resolution in favour of the 4th respondent to collect the deposits and open account with the Post Master, Anakapalli was not believed. Even assuming for argument sake the 4th respondent Secretary had opened the parallel bank account without proper resolution, the said aspect does not disentitle the 3rd respondent society to recover the money on the principle of indoor management. In similar circumstances in a matter arising under the Companies Act when a plea is raised that the creditor ought to have verified whether the proper authorization for the company to borrow the money before lending the same, the Allahabad High Court had after referring to various precedents both English as well as Indian on subject had held in **Lakshmi Ratan Cotton Mills Co. Ltd., Kanpur Vs J.K. Jute Mill Co. Ltd., Kanpur**[1] as follows:

> In view of the above provisions, there can be no doubt that Sri Gulab Chand Jain who was the director of the defendant company, the director of the managing agency and also a delegate of the managing agency could be authorised to enter into this transaction. Under the above circumstances, <u>even supposing that there was no actual resolution authorising him to enter into this transaction on behalf of the defendant company either by the Board of Directors or by the Board of Managing Agents, the claim of the plaintiff who was a creditor cannot be affected. A creditor dealing with a trading company is required by law to be conversant with the terms of its Memorandum and Articles of Association and no more. If it is found that the transaction of loan into which the creditor is entering is not barred by the charter of the Company or its Articles of Association, and could be entered into on behalf of the Company by the person negotiating it, then he is entitled to presume that all the formalities required in connection therewith have been complied with.</u> If the transaction in question could be authorised by the passing of a resolution, such an act is a mere formality. <u>A bona fide creditor, in the absence of any suspicious circumstances, is entitled to presume its existence. A transaction entered into by the borrowing company under such circumstances cannot be defeated merely on the ground that no such resolution was in fact passed. The passing of such a resolution is a mere matter of indoor or internal management and its absence, under such circumstances, cannot be used to defeat the just claim of a bona fide creditor. A creditor being an outsider or a third party and</u>

[1] 1956 SCC OnLine ALL 370 : AIR 1957 ALL 311

<u>an innocent stranger is entitled to proceed on the assumption of its existence; and is not expected to know what happens within the doors that are closed to him.</u> Where the act is not ultra vires the statute or the company such a creditor would be entitled to assume the apparent or ostensible authority of the agent to be a real" or genuine one. He could assume that such a person had the power to represent the company, and if he in fact advanced the money on such assumption, he would be protected by the doctrine of internal management.

The Supreme Court held in **MRF Limited Vs. Manohar Parrikar and others**[2] as follows:

> "110. The doctrine of indoor management is also known as the *Turquand rule* after *Royal British Bank V. Turquand*. In that case, the Directors of a company had issued a bond to Turquand. They had the power under the articles to issue such bond provided they were authorised by a resolution passed by the shareholders at a general meeting of the company. But no such resolution was passed by the company. It was held that Turquand could recover the amount of the bond from the company on the ground that he was entitled to assume that the resolution was passed.
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> 111. The doctrine of indoor management is in direct contrast to the doctrine or rule of constructive notice, which is essentially a presumption operating in favour of the company against the outsider. It prevents the outsider from alleging that he did not know that the constitution of the company rendered a particular act or a particular delegation of authority ultra vires. The doctrine of indoor management is an exception to the rule of constructive notice. It imposes an important limitation on the doctrine of constructive notice. According to this doctrine, persons dealing with the company are entitled to presume that internal requirements prescribed in the memorandum and articles have been properly observed. Therefore, doctrine of indoor management protects outsiders dealing or contracting with a company, whereas doctrine of constructive notice protects the insiders of a company or corporation against dealings with the outsiders.

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[2] (2010) 11 Supreme Court Cases 374

The above principle has been followed in several judgments.

Considering the fact that the office bearers of the petitioner society had addressed letters to the Postmaster about the transactions of the 4th respondent, the arbitrator came to conclusion that the office bearers of the petitioner society were aware of the transactions being carried out by the 4th respondent and as such the society cannot disown the transactions of the 3rd respondent society with the petitioner society. The arbitrator has also taken into consideration had noted that the petitioner society did not take any steps to impeach the Secretary by moving no confidence motion and thus came to conclusion that there was a connivance of the office bearers of the petitioner society with the 4th respondent. By over all appreciation of the material placed on record, the arbitrator had considered other material facts placed before him and came to conclusion that the petitioner society was aware of the transactions in the post office, particularly receipt of money from 3rd respondent society and withdrawal of the same. While it is the contention of the 4th respondent that the monies have been used for the society, the society by not producing the relevant records and not making any effort has failed to substantiate their claim. Apart from that, inasmuch as, the money was received into the account of the petitioner society without prejudice to the rights of the petitioner to recover the money from the 4th respondent, if otherwise they are entitled to so far as their application to the 3rd respondent as fag end by the Arbitrator, cannot be found fault. Before the Tribunal the main trust of argument was alleged misdeeds of the 4th respondent. Even by the time of the Tribunal considering the case, there was no action initiated by the petitioner society against the 4th respondent. The Tribunal *prima facie* came to conclusion that in the absence of any complaints from the members about non-receipt of loans etc., the argument of the petitioner society that the money was misutilised by the 4th respondent was *prima facie* not accepted. However, the said aspect was left open by the Arbitrator as well as the Cooperative Tribunal. In the light of the facts as found by the Arbitrator and Tribunal practically there being no other material the writ petition does not deserve any consideration and the orders of the Arbitrator as confirmed by the Tribunal does not call for any interference in exercise of the Certiorari jurisdiction of this Court under Article 226 of the Constitution of India.

Accordingly, this Writ Petition is dismissed. There shall be no order as to costs. As a sequel, miscellaneous petitions pending, if any, shall also stand closed.

CHALLA KODANDA RAM, J

Dated:09.09.2016
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