

**Madras Metropolitan Development Authority Vs. Sears Electronics Limited (In Liquidation) and ors.**

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**Court :** Chennai

**Decided On :** Apr-21-2003

**Reported in :** [2005]128CompCas545(Mad)

**Judge :** A.K. Rajan, J.

**Acts :** Companies Act; Original Side Rules - Order 4, Rule 1

**Appeal No. :** Civil Suit No. 500 of 1993

**Appellant :** Madras Metropolitan Development Authority

**Respondent :** Sears Electronics Limited (In Liquidation) and ors.

**Advocate for Def. :** Ramesh, Adv. for Official Liquidator for Respondent No. 1, ;R. Shankara Narayanan, Adv. for Respondent No. 2 and ;K. Mani, Adv. for Respondent No. 3

**Advocate for Pet/Ap. :** N. Sampath, Adv.

**Judgement :**

**A.K. Rajan, J.**

1. Suit for recovery of a sum of Rs. 62,94,520.50 with further interest on Rs. 50,00,000 from March 16, 1993, till the date of realisation.
2. The plaint averments are as follows : The plaintiff is the Madras Metropolitan Development Authority (hereinafter referred to as 'M.M.D.A.'), represented by its member-secretary. The first defendant is a company registered under the Companies Act; it was ordered to be wound up by order of this Court, dated November 26, 1993. Hence, the official liquidator is substituted in place of the first defendant. The second and third defendants are the non-rotational whole time directors of the first defendant-company. On December 21, 1990, the first defendant wrote a letter to the chairman of the Electronics Corporation of Tamil Nadu Limited to forward a letter of request to M. M. D. A. for placing an inter-corporate deposit of Rs. 50 lakhs for interest and the same was forwarded to the plaintiff by the chairman of M/s. Electronics Corporation of Tamil Nadu Limited (hereinafter referred to as 'ELCOT'). The plaintiff considered the request of the first defendant and since it was a joint venture with Elcot, the plaintiff agreed to make the deposit. The cash management committee of M. M. D. A. decided to deposit a sum of Rs. 50 lakhs with the first defendant-company on a 45 day roll-over short term deposit with interest at the rate of 15 per cent, per annum. The first defendant by letter dated December 24, 1990, accepted the short-term deposit and the interest rate. The second and third defendants have executed personal guarantees in their capacity as non-rotational directors in whole time employment of the company for prompt repayment on demand. The first defendant also gave a true copy of resolution of the board meeting held on December 21, 1990, by which the second and third defendants were authorised to execute necessary documents and to do all such acts necessary for availing of short-term deposit from the plaintiff. On December 26, 1990, the first defendant executed a promissory note and received a sum of Rs. 50 lakhs on the above terms. After expiry of 45 days, the first defendant executed fresh promissory notes, taking back the old promissory notes and finally on June 24, 1991, the first defendant executed the suit promissory note. The first defendant paid interest at the rate of 15 per cent up to June 24, 1991, only. Thereafter, the first defendant failed to pay the interest, in spite of repeated demands. The principal amount has also not been repaid. Therefore, the defendants are liable to pay a sum of Rs. 50 lakhs towards principal

and a sum of Rs. 12,94,520.50 towards interest from June 24, 1991, till the date of the plaint, totally aggregating to a sum of Rs. 62,94,520.50. The first defendant as the borrower and defendants Nos. 2 and 3 as guarantors are jointly and severally liable to pay the amount. The defendants are liable to pay interest at 15 per cent per annum as it is a commercial transaction.

3. Though by the order of this Court, the first defendant is in liquidation, the plaintiff moved the High Court for leave to proceed with the present suit and the same was permitted by order dated November 7, 1997. Therefore, the plaintiff prays for a decree for the plaint amount together with interest at the rate of 15 per cent, per annum till the date of payment and for costs. The written statement filed by the third defendant and adopted by the second defendant, is as follows : There is no cause of action against these defendants to file a suit. They have not executed any personal guarantee in respect of the promissory note dated June 24, 1991. They were appointed as whole time managing director in the joint venture of Elcot. In the year 1983, the name of the company was changed as Sears Electronics Limited. It is a joint venture company wherein 50 per cent, of the equity shares belong to Elcot. The first defendant-company approached Elcot on November 21, 1990, requesting to recommend to the plaintiff to provide inter-corporate deposit for a short-term period. Thereafter, Elcot recommended to M. M. D. A. to sanction the short-term deposit. Then, the first defendant requested by their letter dated December 19, 1990, to provide Rs. 50 lakhs as short term deposit. In turn, M. M. D. A. called upon the first defendant to execute a promissory note for Rs. 50 lakhs. Accordingly, a promissory note was executed by the first defendant. The promissory note was for a period of 45 days from the date of execution. The said amount was repayable to the plaintiff at the expiry of 45 days together with interest. It is not correct to say that it was provided for a period of 45 days as rollover call deposit. The first defendant received the said deposit only for a specific period of 45 days. At the time of disbursement of the amount, the plaintiff also requested the first defendant to arrange for personal guarantee from the directors. These defendants were full-time employees and were only paid directors. In order to improve the production of the first defendant-company, these defendants agreed to give personal guarantees only for the specific loan covered by the promissory note for the limited period of 45 days. Thereafter, they have not

extended the personal guarantee, nor did the plaintiff call upon them to execute a fresh personal guarantee. The guarantee given by them ceased on the expiry of the 45th day, i.e., on January 8, 1991. These defendants cannot be called upon to pay the amount on the failure of the first defendant. The plaintiff never informed these defendants about the renewal of the loan nor the subsequent execution of the promissory note of the first defendant. The plaintiff cannot rely upon the earlier letters executed by these defendants, in respect of the promissory note executed subsequent to that date. There is no consideration for any guarantees being given by these defendants, subsequent to the expiry of 45 days. The plaintiff has not taken any action against the first defendant after November 26, 1990. The plaintiff cannot proceed against these defendants. The execution of the promissory note by the first defendant on June 24, 1991, amounts to granting of a concession or benefit to the first defendant without the consent or approval of these defendants and hence, there is no liability for these defendants for the promissory note dated November 26, 1990, also. These defendants are discharged of their obligations even in respect of the letters executed by them. Due to various reasons including labour unrest and refusal of the bank to grant working capital, the first defendant-company declared lock-out. Even SIPCOT, one of the long term-lending institutions of the Tamil Nadu Government proceeded against the first defendant-company for its dues and it took possession of the factory at Thiruvannamiyur. Therefore, the first defendant-company's production was completely stopped. The creditors of the company filed winding up petition and the High Court ordered winding up of the company with a direction to the official liquidator to take charge of the company and its factory and the said order was passed on November 26, 1993. As such, the entire assets are with the official liquidator. The plaintiff has to proceed only against the estate of the company. The first defendant-company submitted the statement of affairs wherein the assets of the company was shown at Rs. 4,71,87,000 including the liability of the plaintiff. In the circumstances, the suit is liable to be dismissed.

4. On these pleadings, the following issues were framed :

(1) Whether the plaintiff is entitled for a money decree against the defendants jointly and severally for the suit claim ?

(2) Whether the second and third defendants had guaranteed the payment of loan borrowed by the first defendant as stated in the plaint ?

(3) Whether the guarantee given by the second and third defendants had ceased to operate as contended by the said defendants ?

(4) Whether the second and third defendants are liable to pay the suit claim as guarantors ?

(5) Whether there is cause of action for the suit ?

(6) To what other relief the plaintiff is entitled to ?

5. On the side of the plaintiffs, P. W. 1 has been examined and D. Ws. 1 to 3 were examined on the side of the defendants.

6. (a) The senior accounts officer in the plaintiff Corporation, P. W. 1, has stated in his evidence that the first defendant is a registered company and the second and third defendants are the directors of the first defendant-company. Exhibit P1, dated November 21, 1990, is the xerox copy of the letter sent by the second defendant to chairman of Elcot to forward the letter of request to M. M. D. A. for placing an inter-corporate deposit; exhibit P2 is a letter written by the first defendant-company to the plaintiff. Exhibit P3 is another letter written by the first defendant-company to the plaintiff whereby the resolution passed by the board of directors of the first defendant was informed ; exhibits P4 and P5 are the letters of personal guarantee in their capacity as non-rotational directors in whole time employment of the company for the prompt repayment of the short-term deposit of Rs. 50 lakhs sanctioned by the plaintiff. Exhibit P6 is a certified copy of the resolution of the board meeting of the first defendant-company on December 21, 1990. Exhibit P7 is the promissory note dated June 24, 1991, executed by the first defendant to the plaintiff; exhibit P8 is the demand made by the plaintiff; exhibit P9 is another letter written by the plaintiff. Exhibits P10 and P11 are the replies. P. W. 1 has stated in the cross-examination that there is no personal guarantee executed by the third defendant in respect of exhibit P3 promissory note dated December 26, 1990, as it was not necessary.

7. (b) The second defendant was examined as D. W. 1. He has stated that he worked in various electronics companies before promoting the joint venture company with Electronics Corporation of Tamil Nadu ; he was the managing director and the third defendant was the joint managing director of Sears-Elcot T.V. Electronics Corporation of Tamil Nadu ; Electronics Corporation of Tamil Nadu, a Government of India undertaking has 50 per cent, share in Sears-Elcot; the chairman of the first defendant board is the ex-officio chairman of Elcot ; both Elcot and Sears-Elcot have equal representation in the board ; on December 24, 1990, he wrote a letter exhibit P4 undertaking as the director of Sears-Elcot to repay the amount; no time limit was specified in the letter ; one P. N. Kumar gave a similar undertaking ; on December 24, 1990, neither the company, nor anyone received any consideration from the plaintiff; on June 24, 1991, exhibit P7 was sent by D. W. 1 in his capacity as managing director of Sears Elcot ; after December 24, 1990, he has not written any letter or undertaking or guarantee similar to exhibits P4 and P5 ; Sears-Elcot has gone into liquidation in November, 1993. At that time, the company had 18 grounds of land in an industrial place together with a built-up area of 16,000 sq. ft; the company also had a flat in Andheri, Bombay; all these properties are in the possession of the official liquidator ; at that time, the company had assets worth Rs. 50 lakhs. In the cross-examination, he stated that he gave a letter dated December 24, 1990, to M. M. D. A. stating that personal guarantees are enclosed ; for giving such personal guarantees, the company passed a resolution on December 21, 1990, under exhibit P6 ; personal guarantees were given in the capacity as whole time directors ; he also admits that the company executed exhibit P7. Further, he has stated that on February 8, 1991, and again on May 9, 1991, the first defendant paid a sum of Rs. 92,465.75 for the accrued interest up to May 9, 1991 ; he also admits that exhibit P8 letter was given by the plaintiff demanding repayment and that was not paid. But, he states that it is the company which is liable to pay the amount and not the second defendant.

8. (c) The third defendant has been examined as D. W. 2. He has stated that he was one of the full-time employees in the joint venture company; the chairman, Elcot is the deciding authority for any borrowal of the first defendant; he was only a joint managing director getting salary. But, he fairly admitted that exhibit P5 letter was signed by him as non-rotational director of the first defendant-company in full-

time employment. According to him, he has not signed any promissory note under exhibit P7. He was not called upon to give any guarantee letter for exhibit P7. Sufficient assets of the company are available with the official liquidator. In the cross-examination, he has admitted that on December 24, 1990, he gave a letter, exhibit P5 ; he admitted that it is the letter of guarantee and no time limit has been mentioned. Initially, the promissory note has been given by the company for 45 days ; on June 24, 1991, a fresh promissory note was executed. He has stated that he is not personally liable to pay the suit claim.

9. Learned counsel for the plaintiff, Mr. N. Sampath submitted that the payment by way of deposit of Rs. 50 lakhs initially for a period of 45 days by the plaintiff is to be repaid with interest at 15 per cent, per annum is admitted by the second and third defendants and promissory note, exhibit P7, was executed on June 24, 1991, uptill that date interest was paid ; subsequently, interest was not paid and therefore, on March 5, 1992, a demand was made in exhibit P8 ; therefore, the plaintiff has proved that the suit amount is due and payable by the first defendant; exhibits P3 and P4 are letters of personal guarantee executed by the second and third defendants guaranteeing the repayment of Rs. 50 lakhs ; therefore, the plaintiff has proved his case that defendants Nos. 2 and 3 are personally liable to repay the amount and hence the plaintiff is entitled for a decree, as prayed for.

10. Learned counsel Mr. R. Shankara Narayanan appearing for the second defendant and Mr. K. Mani, for the third defendant argued that the first defendant is a joint venture company and that according to the plaint, the cause of action arose only on June 24, 1991; but, exhibit P4, letter of guarantee is dated December 24, 1990 ; this was executed only in accordance with the board's resolution, dated December 21, 1990 ; inasmuch as the guarantee letter was prior to the date of cause of action, this letter cannot be construed as the guarantee for the promissory note, exhibit P7 ; therefore, defendants Nos. 2 and 3 cannot be fastened with liability on the basis of the personal guarantee letters, exhibits P3 and P4. In support of his contention, they relied upon the decision in State of Maharashtra v. Dr. M. N. Kaul, : AIR 1967 SC1634 , wherein the Supreme Court observed that (head note of AIR) :

'Whether a guarantee is enforceable or not depends upon the terms under which the guarantor bound himself. To this there are some exceptions. In case of ambiguity when all other rules of construction fail, the courts interpret the guarantee contra proferentem that is, against the guarantor or use the recitals to control the meaning of the operative part where that is possible. But whatever the mode employed, the cardinal rule is that the guarantor must not be made liable beyond the terms of his engagement.'

11. They also referred to a decision in Seth Pratap Singh Moholalbhai v. Keshavlal Harilal Setalwad, , where the Privy Council held (headnote) :

'The surety, like any other contracting party, cannot be held bound to something for which he has not contracted. If the original parties have expressly agreed to vary the terms of the original contract, no further question arises. The original contract has gone, and unless the surety has assented to the new terms, there is nothing to which he can be bound, for the final obligation of the principal debtor will be something different from the obligation which the surety guaranteed. Presumably he is discharged forthwith on the contract being altered without his consent, for the parties have made it impossible for the guaranteed performance to take place.'

12. They referred to another judgment in M. S. Anirudhan v. Thomco's Bank Ltd. for the same proposition.

13. Relying on these decisions, learned Counsel submitted that exhibits P3 and P4 are limited guarantees ; therefore, they are limited only to the first period of 45 days immediately after December 26, 1990. Therefore, the limited guarantee ends when it is extended to any other amount other than the agreed one. Inasmuch as exhibit P7 is a promissory note dated June 24, 1991, and exhibits P4 and P5 are prior to that, there is no liability fastened on the second and third defendants ; hence, the plaintiff is not entitled to get a decree against defendants Nos. 2 and 3.

14. The Supreme Court in the case of State of Maharashtra v. Dr. M. N. Kaul, : AIR 1967 SC1634 , has held that whether the guarantee is enforceable or not depends upon the terms under which the guarantor bound himself. Further, the

cardinal rule is that the guarantor must not be made liable beyond the terms of his engagement. From this, it is clear that the guarantor is liable on the basis of the terms by which he agreed to be bound and he is not liable beyond those terms. The judgment of the Privy Council is to the effect that if the terms of the contract are varied subsequent to the guarantee and unless the guarantor expressly agrees to vary the terms of the original contract, the guarantor would not be liable for the new terms of the contract. The contents of exhibits P4 and P5 are identically worded which are as follows :

Exhibit P4 : 'From : 24th December, 1990 A. K. Bhattacharya, 23, 22nd Cross Street, Besant Nagar, Madras-600 090. To : Madras Metropolitan Development Authority, Thalamuthu Natarajan Bldg., 8, Gandhi Irwin Road, Madras-600 008. Dear Sirs, With reference to the above, the undersigned hereby undertake a personal guarantee in their capacity as non-rotational directors in whole time employment of the company for prompt repayment on demand these short term deposit of Rs. 50 lakhs sanctioned to M/s. Sears Electronics Limited in full. Thanking you, Yours faithfully, (Sd.) A. K. Bhattacharya. 'Exhibit P5 : 'From : 24th December, 1990 P. N. Kumar, 45, Rukmani Salai, Kalakshetra Colony, Madras-600 090. To : Madras Metropolitan Development Authority, Thalamuthu Natarajan Bldg., 8, Gandhi Irwin Road, Madras-600 008. Dear Sirs, With reference to the above, the undersigned hereby undertake a personal guarantee in their capacity as non-rotational directors in whole time employment of the company for prompt repayment on demand these short term deposit of Rs. 50 lakhs sanctioned to M/s. Sears Electronics Limited in full. Thanking you, (Sd.) P. N. Kumar. '

15. From this, it is seen that the second and third defendants have written these letters in their individual capacity and undertook a personal guarantee for prompt repayment of the entire amount of the short term deposit of Rs. 50 lakhs sanctioned to the first defendant-company when demanded. This letter presumably refers to the earlier letter, exhibit P2 written by the plaintiff on December 19, 1990 ; referring to exhibits P2, D2 and D3, they have given a personal guarantee for the prompt payment of Rs. 50 lakhs 'sanctioned'. Admittedly, this amount was sanctioned on December 26, 1990 and thereafter, only interest for two periods of 45 days till June 24, 1991, has been paid; the

principal was never repaid. This fact is admitted by D. Ws. 1 and 2 before the court. It is not the case of D. Ws. 1 and 2 that the principal amount had been that the principal amount of Rs. 50 lakhs had been repaid. Exhibits P4 and P5 have no time limit. By these letters, D.W. 2 and D.W. 3 guarantee personally for the repayment of Rs. 50 lakhs paid to the first defendant ; therefore, the second and third defendants are also personally liable to repay the balance amount.

16. Learned counsel appearing for the defendants referred to the cause of action stated in the plaint and submitted that cause of action according to the plaintiff arose on June 24,1991. Therefore, any letter of guarantee executed prior to that date will not bind the guarantors, as the cause of action arose subsequent to such letters of guarantee. This argument though attractive is not sound and it does not help the defendants. The guarantee letters exhibits P4 and P5 mention that it is executed for the amount of Rs. 50 lakhs 'sanctioned' already. Though it is true that in the plaint the cause of action refers only to the date of the promissory note, June 24, 1991, yet the averments contained in the plaint refers to all the happenings and correspondence right from November, 1990. The plaintiff under Order IV, rule 1 of the Original Side Rules, have filed the documents dated from November 21, 1990, to March 5, 1992. Therefore, it is clear that the plaintiff based their claim not on the promissory note, but on the earlier cause of action. It is not the case of either the plaintiff or the defendants that there was any other amount other than the Rs. 50 lakhs sanctioned on December 26, 1990. Admittedly, that amount was never repaid ; only the interest was paid on two occasions. Therefore, the Rs. 50 lakhs referred to in exhibits P1 to P6 is the amount that was sanctioned on December 26,1990. The plaintiffs unnecessarily have obtained fresh promissory notes including exhibit P7, returning the promissory note executed by the first defendant earlier. Getting fresh promissory notes does not affect the case of the plaintiff; the consideration for the fresh promissory note was the amount paid on December 26, 1990. Therefore, the personal guarantees, exhibits P4 and P5 are for the Rs. 50 lakhs borrowed by the first defendant (sanctioned by the plaintiff on December 26, 1990).

17. The contention of D. Ws. 1 and 2 is that they executed personal guarantees only as per the resolution passed by the board of directors ; exhibits P4 and P5 do

not reflect that the guarantees were executed only in pursuance of such resolution. Further that will not have any bearing in the suit because that is an internal matter concerning the first defendant-company and its directors. Therefore, the contention that exhibits P4 and P5 were executed in the capacity as managing director and joint managing director and it cannot be construed as the personal guarantees, is not acceptable. As per the decision relied upon by the defendants themselves of the Supreme Court, the enforceability of the guarantee depends upon the terms under which the guarantor bound himself. Exhibits P4 and P5 have been executed in the personal capacity only; not as a managing director or joint managing director respectively. Therefore it is proved that D. W. 2 and D. W. 3 stood guarantee only in their personal capacity and not in the capacity as the managing director of the first defendant-company. Therefore, D. W. 2 and D.W. 3 are personally liable.

18. Finally learned Counsel for the defendants argued that the company is now under liquidation and all the properties are vested with official liquidator and the first defendant-company had valuable immovable properties and that can be sold and the amount can be recovered. Therefore, it cannot be held that they can be proceeded against only after proceeding against the properties of the first defendant-company. Inasmuch as the plaint prayer is for a decree against the defendants to pay the amount jointly and severally, this Court cannot grant a different decree. Therefore, it cannot be held that defendants Nos. 2 and 3 can be proceeded against only after proceeding against the properties of the first defendant-company. Therefore, the suit is decreed, as prayed for.

19. It is needless to point out that defendants Nos. 2 and 3 have a right to step into the shoes of the plaintiff to recover the amount from and out of the assets of the first defendant which is now under the control of the official liquidator.

20. The official liquidator, it appears, has not taken any steps so far to sell the immovable properties of the first defendant. The official liquidator shall take real and effective steps to sell the property in accordance with the rules and disburse the amount to the creditors, so that all the creditors as well as the first defendant may get their due.

21. In the result, the suit is decreed, as prayed for.

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