

(1939) 08 MAD CK 0001
In the Madras High Court

D. Sundaravaradan

APPELLANT

Vs

R. Narasimhachari, Official Liquidator

RESPONDENT

Date of Decision : 11-08-1939

Acts Referred:

Companies Act, 1956 — Section 229

Citation : AIR 1940 Mad 266

Hon'ble Judges : Gentle, J

Bench : Division Bench

Judgement

Gentle, J.—(Application No. 8415 of 1939): In this application the Official Liquidator seeks directions of the Court in regard to matters set

out in prayers 2 and 3. Shortly the points are these: whether a debtor in respect of whose debt there is a surety is entitled to set off against the

money owing by the debtor to the company moneys due to the debtor from the company and whether the surety is entitled to set off in respect of

his obligation to the company moneys owing to him from the company. The origin of the transactions is a liability which, arose in connexion with a

chit fund scheme conducted by the company. Every contributory to a chit fund scheme agrees that he will each month for a specified period pay to

the company an agreed amount; each month an auction is held and the successful bidder, being one of the subscribers, is entitled to receive from

the company the total amount of all his subscriptions to the fund upon furnishing security by means of a surety and also agreeing to continue to pay

each month the amount of his monthly subscription. When a debtor is placed in a position to receive from the company the total amount of his

subscriptions the company requires the debtor and a surety or two sureties to enter into an obligation to the company, a draft form of which has

been placed before me and it is on account of the obligations under this document that the matter arises in the present application. It has been contended on behalf of the liquidator that the obligation itself in regard both to the debtor and the surety first arises upon the execution of this security bond and on behalf of one of the debtors it has been on the other hand argued that the original contract between the debtor and the company subsisted throughout and continued after the execution of the security bond. Whatever the position may be, it is common ground and it is agreed that the obligations of the debtor and the surety are joint and several.

2. The claim to set-off arises in the following way: Section 229, Companies Act, provides that in the winding up of an insolvent company the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and to debts provable and other liabilities as are in force for the time being under the law of insolvency. Under that Section the provisions of Section 46, Provincial Insolvency Act, are applicable in the liquidation of a company. That Section provides that where there have been mutual dealings between an insolvent and a creditor proving or claiming to prove a debt under this Act, an account shall be taken of what is due from the one party to the other in respect of such mutual dealings, and the sum due from the one party shall be set off against any sum due from the other party, and the balance of the accounts and no more shall be claimed or paid by either side respectively. The question is whether in respect of either the debtor or the surety in the matter before me, debts owing by the company to the debtor or surety are mutual dealings within the contemplation of Section 46 mentioned above. The provisions of Section 31, English Bankruptcy Act, although, differently worded, it is conceded, do not have any different effect to those of Section 46, Provincial Insolvency Act.

3. This matter has been before two other High Courts in this country: In Trimbak Gangadhar Gokhale Vs. Ramchandra Trimbak Kirtane, , it was held in circumstances more or less similar as in this case that no right to set off arose. A decision somewhat to the same effect is to be found in Allince Bank of Simla v. Mohanm Lal AIR (1927) Lah. 228. So long ago as 1806 in Trimbak Gangadhar Gokhale Vs. Ramchandra Trimbak Kirtane, the following case is reported. At the time of the bankruptcy of two

persons two others were indebted to them in a joint bond, one as principal and the other as surety, and the principal was a creditor on a separate account. Lord Erskine, the Lord Chancellor, made an order upon

the petition presented that liberty to set off should be given. The principles laid down in that case have been referred to in modern textbooks. In 2

Halsbury (Hailsham Edition) 285, para. 377, in referring to Ex. parte Hanson (1806) 12 Ves. Jun. 345 and other cases the following appears:

In the absence of agreement, express or implied, there is no set-off between joint and separate debts; but if one joint debtor is a surety for the

other the principal debtor may set off against the joint debt a debt due to himself; and a person induced to become surety by the creditor's fraud

may set off his claim in respect of the fraud against the debt due by the principal debtor.

4. The question of fraud does not arise. I have quoted that passage for reasons which will appear in a moment. In Rowlatt on Principal and Surety,

Edn. 3, p. 140, the following appears:

If a surety, being severally liable, has money in the hands of the creditor, who becomes bankrupt, he is entitled before the trustee sues the principal

to apply it in satisfaction of the debt.

5. The trustee referred to is the trustee in bankruptcy whose position in England is analogous to that of the Official Assignee here. It is therefore to

be noticed that so far as the textbooks are concerned the principle of set off is recognized when, at any rate, the debt is a joint and several debt.

The question of set-off arose in Ex. parte Stephens (1805) 11 Ves. Jun 24. In that case a lady had placed some money in the hands of a bankrupt

firm for the purchase of stock. The bankrupts failed to make the purchase but by remitting what purported to be dividends upon the principal sum

led the lady into the belief that her instructions had been carried out. Subsequently her brother desired to borrow moneys from the bankrupt firm

and she became his surety for the amount advanced to her brother. There was a suit by the Trustee in Bankruptcy, after the firm had become

bankrupt, against the brother alone for the amount advanced and in that suit the brother and the lady were permitted to petition, and successfully

petitioned, for the amount of the debt due to the lady being the sum placed in the hands of the bankrupt to be set off or as much as was necessary

against the claim by the trustee against the brother. This was to some extent on account of the fraud of the bankrupt. That case has been explained

more fully in *Midleton v. Pollock; Ex. parte Knight and Raymond* (1875) 20 Eq. 515, in which it has been decided that there is no rule that a debt

due to joint creditors which has been contracted by fraud can be set off against a separate debt due from one of the joint creditors. Another case

was cited to me, *In re. Pennington & Owen, Ltd.* (1925) B. & C.R. 39, the effect of which is that a joint debt cannot be set off against a claim by

one of the joint debtors.

6. The privileges and rights which are given in Section 46, Provincial Insolvency Act, are based upon equity and fair dealing. It is recognized that it

would be very harsh if the Official Assignee or the Official Liquidator of a company could demand in full, moneys due by a debtor and at the same

time that person being a creditor, for an equal or a larger sum, of the company must be content with a dividend dependent on the distribution which

can be made from the assets. I have been referred to the provision of Order 8, Rule 6, Civil P.C., which deals with the position of suits against

joint debtors and the question of set-off, before any insolvency arises. The provisions of the above rule are in no way referable to matters arising in

insolvency or liquidation and in my view no help is obtained from that rule. Firstly I will consider the position of the debtor who wishes to set off. Is

it to be said that a debtor who has a cross-claim which he can set off against the company loses that right because the company has obtained a

safeguard by a surety assuring to the company the amount of the debt of the debtor to the company? That is the position which must arise if the

contention on behalf of the Official Liquidator is sound. In my view that cannot be. There being moneys which can be set off, this right is not lost

when a surety is obtained in respect of the debtor's debt to the company. The other position is that of the surety himself whose obligation is to pay

to the company the debts of another person, the surety himself having money owing to him by the company in a separate dealing or transaction. In

my view the moneys due to the surety on the one hand and from him to the company on the other are mutual dealings and he has the right to set-off

against his indebtedness to the company the moneys due to him when the obligation to the company by the debtor and surety is one which is joint

and several as admittedly it is in the present case. Both the debtor and the surety who are under an obligation to pay moneys to the company but who themselves are creditors of the company may set off one debt against the other and the balance remaining due should be paid to or by the company as the case may be. I give directions to this effect in the application by the Official Liquidator. I respectfully beg to differ from the decisions in the Indian authorities which are cited above. The Official Liquidator is entitled to his costs, Rs. 5 out of the assets.