
(1940) 05 MAD CK 0013
In the Madras High Court

G. Samuel

APPELLANT

Vs

Cyril Gill and John Stanley Goodwin, Official Liquidators

RESPONDENT

Date of Decision : 03-05-1940

Acts Referred:

Companies Act, 1956 — Section 229

Citation : (1941) 1 MLJ 818

Hon'ble Judges : Venkataramana Rao, J

Bench : Division Bench

Judgement

Venkataramana Rao, J.—This application raises a question of set-off. The Travancore National and Quilon Bank hereinafter called the Bank, lent a sum of Rs. 2,000 to the applicant herein, Mr. G. Samuel, on a promissory note dated 7th October, 1936. The Bank was not willing to lend this sum to him without security. His mother-in-law Mrs. G. P. Sathanantham Srinivasan offered to give the necessary security. On the date of the loan she had a sum of Rs. 4,300 in fixed deposit covered by the Fixed Deposit Receipt bearing the same date. She gave that amount as security. In her affidavit Mrs. Srinivasan states that she gave the said security on the definite understanding that the Bank should adjust the amount due by Mr. Samuel from and out of the money due to her under the said deposit at the time of maturity. The terms on which she gave the said security were reduced to writing and is evidenced by a letter written by Mrs. Srinivasan to the Bank and it runs thus:

I beg to hand you herewith Fixed Deposit amount Receipt No. 116 for Rs. 4,300 dated 7th October, 1936, as security for the pronote loan of Rs. 2,000 you have granted to Mr. G. Samuel. I hereby authorise you to set-off at any time the whole or any portion of the said deposit and interest accrued thereon towards the said loan whenever you deem it necessary.

2. It appears from the affidavit of the Official Liquidators that along with the said letter a duly Receipted Fixed Deposit Receipt in blank was also lodged with the Bank. The Fixed Deposit was for a period of two years and on the date when the

Bank went into liquidation it had not matured. Mr. Samuel . has not paid anything towards the promissory note but he claims that he is entitled to have the amount due "by the Bank to Mrs. Srinivasan set-off against the amount due by him. Mrs. Srinivasan has also filed an affidavit stating that she is willing to have the amount set-off. The question is not whether she is willing, but whether a set-off can be allowed in law. Mrs. Srinivasan has not personally undertaken to repay the debt except giving security as aforesaid. There are no mutual dealings in this case which would entitle the applicant to claim a set-off u/s 229 of the Indian Companies Act, under which in the winding up of an insolvent company the same rules should prevail and be observed as are in force for the time being under the law of insolvency with respect to the estates of persons adjudged insolvent.

3. Mr. G. Ramakrishna Aiyar who appears for the applicant has not been able to put before me any authority in support of the contention that he" can claim a set-off under the said section. His contention however is that Mrs. Srinivasan was a surety for Samuel though her liability is limited to the extent of her security and a surety can claim to have the debt due to her by the Bank set-off against the debt due by the principal. In support of this contention he relied on a ruling of my learned brother Gentle, J., in Application Nos. 841 and 815 of 1939. In that case both the principal and the surety were severally liable to pay the debt due to the bankrupt creditor. Therefore the learned Judge following the rule that if a surety being severally liable has money in the hands of the creditor who became a bankrupt, he was entitled before the trustee sues the principal to have the amount applied in satisfaction of the debt. To put it concretely, A, owes a debt to B, B, owes a debt to C, C also agrees to stand surety for A, and becomes liable in respect of A's debt; C is entitled to have the amount due to him set-off against the amount due from the debtor and in respect whereof he is liable. The reason is there is a demand by A, against C, and there is a cross demand by C, against A. In this case the Bank cannot call upon Mrs. Srinivasan to pay the debt; all that they are entitled to is to realise the security and pay themselves off. I do not see how the said decision of my learned brother Gentle, J., supports him.

4. Mr. Ramakrishna Aiyar then contends that an agreement to set-off was entered into by the Bank at the time of the contract and the said agreement is binding on the Bank. He also raises another contention, namely, the Bank by reason of having gone into liquidation has impaired the security and is not in a position to return the security unimpaired on payment of the debt by Mr. Samuel and the Bank is therefore not entitled to enforce the debt; in any event, it must give credit for the full value of the security. In opposition to this contention, the counsel for the Official Liquidators relies on the decision of my learned brother Gentle, J., reported in *D. Sundaravaradan Vs. M.K. Mani Iyer*, , Ex parte Caldicott, In re Hart (1884) 25 Ch. D. 716 and *Commercial Bank of Australia v. Official Assignee of the Estate of John Wilson & Company* (1893) A.C. 181. The case decided by Gentle, J., appears to be a case in point. In that case the applicant was a subscriber for one ticket in a chit fund conducted by the

Travancore National (Subsidiary) Company and was a successful bidder for a sum of Rs. 940 at the auction held. Under the Rules of the Company he could only draw the amount of Rs. 940 on giving sufficient security for the due payment of the future instalments of the chit. Two of the brothers of the subscriber who were also subscribers to other chit funds conducted by the company offered to give the amount that might be due to them in respect of their tickets in the said chit funds as security for the amount that might be due in respect of future instalments if defaults were committed by their brother. The learned Judge held that no set-off could be allowed. He distinguished two cases on which reliance was placed and held they were not applicable to the facts of that case. One was a case reported in *Ellis and Co.'s Trustee v. Dixon-Johnson* (1925) A.C. 489 and the other, a decision of Leach, J., (now my Lord the Chief Justice) in *Official Assignee v. M. C. Harikrishna & Sons* AIR 1935 Rang. 201. As Mr. Ramakrishna Aiyar laid considerable emphasis on these two cases, I shall proceed to deal with them. In *Ellis and Co.'s Trustee v. Dixon-Johnson* (1925) A.C. 489 as pointed out by Viscount Cave no question of a cross claim or set-off really arose. The question that actually arose there was whether the defendant, who was indebted to the bankrupt firm and deposited certain rubber shares with them as security, was not entitled to a return of the said shares in specie on making a payment. It arose in this way. Before the firm became bankrupt, the firm sold the said shares without the knowledge or authority of the defendant who was not aware of such a sale till the bankruptcy. The trustee in bankruptcy claimed the balance of the debt due from the defendant after giving credit to the value of the shares. Lawrence, J., before whom the matter came up was of the opinion that the bankrupt firm was guilty of wrongful conversion and that "the principle that a mortgagee will not be permitted to sue his mortgagor for the mortgage debt, if he has parted with the mortgaged property otherwise than in exercise of a power of sale" would apply to the case. But the principle is not inflexible and some modification was required in the circumstances of that case. He was of the opinion that justice could be done in that case by ascertaining the market value of the shares on the date of the receiving order and by setting off the amount so ascertained against the amount found due from the defendant and the balance directed to be paid by the defendant. When the matter went up before the House of Lords, Viscount Cave, L. C., was of the opinion that bankruptcy could not modify the application of the rule that if a creditor holding security sues for his debt, he is under an obligation on payment of the debt to hand over the security, and if, having improperly made away with the security, he is unable to return it to his debtor, he cannot have judgment for the debt. However he was not prepared to disturb the order made by Lawrence, J., but he was emphatically of the opinion that there was no mutual credit within the meaning of Section 31 of the Bankruptcy Act and he gave his reason thus. "The right of the defendant was not to a money payment present or future, but to a return of his shares in specie as and when he paid off his debt". It is thus clear that there is no question of a set-off in that case. Mr. Ramakrishna Aiyar contends that the principle of that case ought to be applied to the present case on the ground that the Bank was

unable to return the security by reason of the liquidation and in support of his contention he relied on the ruling of the Rangoon High Court reported in *Official Assignee v. M.C. Harikrishna & Sons* AIR 1935 Rang. 201. The rule as stated by Viscount Cave L.C., is applicable to a case where a mortgagee or a pledgee has improperly made away with the security. There is no question here of the Bank improperly making away with the security or its inability to return it. The moment the debt is paid, it will release its security. The contention is, not that the security cannot be had but the value of the security has been diminished by the conduct of the Bank. It seems to me that, the rule of Viscount Cave, L.C., will not be applicable to cases of liquidation or insolvency. The security in this case takes the form of a debt due by the Bank. If that debt was owing to the debtor it will be a case of cross-demand and a case for a set-off. But the security in this case was given by a third party and by reason of the liquidation the owner of the security cannot have any cause of action against the Bank for any wrongful conversion. Under the law he cannot say that the value of his debt is impaired : he is only entitled to receive the dividend and cannot claim the full amount. While therefore the owner of the security cannot claim the full amount and there can be no cause of action against the Bank for any diminution in the value of the security, it is not possible to understand how the applicant can claim the full value of the security. No doubt the view of Mr. Ramakrishna Aiyar "derives some support in the ruling of the Rangoon High Court, but that case is distinguishable. In that case there was a joint debt by a firm of partners. As security for the payment of the debt one of the partners gave his Fixed Deposit amount with a stipulation that that amount should be adjusted against the debt. On the facts the learned Judge found there was an agreement between all the parties that there should be a set-off of this amount against the debt due by the firm. The learned Judge was very clear in stating that there was no question of mutual dealings within the meaning of the Bankruptcy Act. Apart from agreement it may perhaps be possible to justify the conclusion of the learned Judge on the ground that having regard to the fact that one of the partners was severally liable for the debt a set-off is permissible. No doubt the learned judge rested his decision on *Ellis & Co's Trustee v. Dixon-Johnson* 1925 A--C 489. With due respect I am unable to agree in the reasoning of the learned Judge in regard to this.

5. Mr. Ramakrishna Aiyar next contends that on the facts it must be found in this case that there was an agreement to set-off the amount of Fixed Deposit against the debt due by the applicant. From the terms of the letter given by Mrs. Srinivasan the Bank is authorised to set-off the whole or any portion of the said deposit and interest accrued thereon. Of course it confers a right on the Bank to set-off, if the Bank so chose to do. From the terms of the letter it appears to me that the Fixed Deposit amount is given as security with the intention that the amount when realised may be appropriated by the Bank towards the debt if they so chose to do. It is one thing to say that the Bank has a right to set-off but another thing to say that the applicant has got a right to set-off and there was an agreement to set-off. It is open to the Bank to give up the security if they like.

6. I am therefore of the opinion that no set-off can be allowed in this case but the equity of the case demands that the Bank should adjust the dividend payable under the deposit towards the amount due and recover only the balance. In the circumstances I do not direct the applicant to pay the costs of the Official Liquidators. I award Rs. 35 as and for costs of the Official Liquidators plus Rs. 35 for their counsel, Rs. 35 for Mr. Parthasarathy, counsel for the Petitioning Creditor and Rs. 35 for Mr. Vepa, the costs to come out of the assets of the Bank.