
(1928) 09 BOM CK 0007

In the Bombay High Court

Case No : O.C.J. Appeal No. 55 of 1927 and Suit No. 639 of 1924

Krishna Chinnoo and Sons

APPELLANT

Vs

Matubhai Kasanbhai

RESPONDENT

Date of Decision : 12-09-1928

Acts Referred:

Presidency Towns Insolvency Act, 1909 — Section 62(2)

Citation : (1929) 31 BOMLR 35 : (1929) ILR (Bom) 290 : 117 Ind. Cas. 440

Hon'ble Judges : Kemp, J;Fawcett, J

Bench : Division Bench

Final Decision : Dismissed

Judgement

Kemp, J.—This is an appeal by certain opposing creditors against the order of Mr. Justice Daver sitting in Insolvency allowing the claim of respondent Nos. 1 to 2 (whom I shall call the claimants) in the insolvency of Evans. The material facts are as follows;-

2. Evans and on Kaderbhoy carried on business as joint building contractors and as such entered into an indenture of lease for 999 years, dated July 26 1920, with J.R. patel and B.S. Shroff, of certain land situated at Tardeo in Bombay at a monthly rent of Rs. 694-7-2 and subject to certain conditions one of which was that the lessees should build upon the land buildings to the value of Rs. 50,000 within 1 1/2 year from July 26, 1920. The lessees (sic) the deed of surrender for the Official Assignee's inspection. The Official Assignee took inspection of the deed on March 10, 1927. On April 8, 1927, the Official Assignee wrote asking for a reply to his letter of February 24, 1927. It is not clear what he meant by this letter as he had seen the deed of surrender and had disclaimed the lease, but it may have been that he had in his mind that the claimants must elect what position they were going to adopt under Rules 9, 10, and 11 of the second schedule.

3. Then on April 29, 1927, the Official Assignee declared a first and final

dividend. The only intimation before us of his intention to declare a dividend is the notice of January 26, 1927, published in the press on February 5, 1927. On July 21, 1927, the claimants wrote to the Official Assignee saying they had replied to his letter of February 24, 1927, on March 7, 1927, and asking if he admitted their claim. On July 23, 1927, the Official Assignee rejected the proof on the ground that the deed of surrender operated to extinguish the whole debt against the insolvent.

4. Davar J. decided in favour of the claimants on September 20, 1927, and admitted the proof and ordered the Official Assignee to recover from the creditors who had participated in the distribution on April 29, 1927, a proportional share of their dividend. Subsequently, on other claimants coming forward he ordered the whole dividend to be opened up. Those other claimants are respondents in Appeal No. 69 of 1927. Davar J. gave no reasons for his decision but intimated he would give them should an appeal be preferred. Subsequently, on January 19, 1923, after the memo, of appeal had been filed on October 10, 1927, and more than three months after the decision, he gave his reasons. This is unfortunate as it has been contended before us that some of the points taken by counsel in this appeal were not taken by his client in the lower Court. Nor had counsel any reasons for the finding before him when he drafted the memorandum of appeal.

5. The rules in the first schedule to the Presidency Towns Insolvency Act, which I shall hereafter refer to as "the Act, 11 relating to the proof of debts are, by virtue of Section 48, statutory rules. Section 48 is imperative in its terms. Similarly the rules framed by the High Court under Sections 112 and 114 of the Act and the forms annexed thereto must be strictly followed. Section 112(p) refers specially to the forms to be used in proceedings under the Act. Section 114 enacts that such rules shall have the same force and effect as if they had been enacted in the Act.

6. It is contended that when the claimants lodged their proof with the Official Assignee on February 23, 1927, they claimed as unsecured creditors although they had a security which they incorrectly regarded as worthless. In their letter of March 7, 1927, they say they have surrendered the security which was "unremunerative." Rule 5 of the rules in the schedule requires the creditor to state in the affidavit in support of his proof whether he is or is not a secured creditor. Rule 3 of the rules made under the Act lays down that the forms in the appendix I to the rules "shall" be used with such variations as circumstances may require. Rule 116 of the same rules requires in imperative terms that a proof shall be in the form No. 45 in the appendix to the rules with such variations as the circumstances may require. The deponent in his proof whilst mentioning the mortgage failed, if he were a secured creditor, to comply with Rules 9, 10, and 11 in the schedule; for he did not assess his security nor surrender it nor state that it had been realised, These particulars should have been stated on oath and it is not sufficient to merely show the Official Assignee the deed of surrender

after the proof had been lodged. Rule 16 of the rules in the schedule says that if a secured creditor does not comply with the rules in the schedule for secured creditors, he shall be excluded from all share in any dividend.

7. But I am of opinion the form of their proof shows they were and claimed as unsecured creditors in this case; for, as a matter of fact, they were not "secured creditors" within the meaning of that term under the insolvency law. The definition in Section 2, Clause (g), of the Act is not exhaustive and as the Act largely adopts the wording of the English Bankruptcy Acts, we may accept the definition of "secured creditor" in those Acts as intended equally to apply under our Act. That definition requires that the mortgage, charge, or lien should be on the debtor's property. See also our Provincial Insolvency Act V of 1920, Section 2, Clause (e), which is an exact copy of the definition in Section 167 of the English Act of 1914. In the present case the Official Assignee having properly disclaimed the lease and the mortgagees not having obtained a vesting order u/s 66(1), there was no interest of the insolvent with the mortgagees and, therefore, at the date of the proof no security on the debtor's property. That this is the effect of the disclaimer is, I think, clear from Sections 62(2) and 66 of the Act. No vesting order was made in respect of the disclaimed property and by the proviso to Article 66(1) the mortgagees failing to take advantage of the subsection were excluded from all interest in and security upon the property. I have had the advantage of perusing my brother Fawcett's judgment on this point and with respect agree with his conclusions.

8. There was property burdened with onerous covenants for the Official Assignee to disclaim. In India the equity of redemption in a mortgage is immovable property (*Parashram Harlal v. Govind Ganesh* I.L.R (1895) Bom. 226, *Vithal Narayan v. Shriram Savant* I.L.R (1905) Bom. 391,; 7 Bom. L.R. 313. and Section 108(j) of the Transfer of Property Act preserves for the lessee the liabilities under the lease of a lessee who transfers by way of mortgage or sub-lease the whole or part of his interest in the property.

9. The Official Assignee was bound under the proviso in Rule 119 of the rules made under the Act to admit or reject the proof and in case of a disputed proof to retain u/s 73(1)(c) and Rule 122(2) sufficient assets in his hands when distributing the dividend to meet what would be due if the proof were ultimately allowed. He did not adjudicate on the proof until long after the distribution of the dividend on April 29, 1927. The claimants were entitled under Rule 119 to an adjudication on their proof by the Official Assignee within seven days of the latest date mentioned in the notice of dividend as the latest date for lodging proofs, This was imperative, as by Rule 122(2) of the same rules a right of appeal is given to a creditor whose proof has been rejected and provision is made by that rule for retaining sufficient assets to meet the dividend on his claim. This is a constitutional right of which the creditor cannot be deprived. The Court has since allowed the claim but the Official Assignee has distributed the assets available for dividend.

10. Before considering what should now be done I wish to refer to the form of notice of intention to declare a dividend in this case. The dividend in this case was the first and final dividend. Section 73(1) provides that the Official Assignee before declaring a final dividend "shall give notice in manner prescribed to the persons whose claims to be creditors have been notified to him but not proved" to prove their claims within the time limited by the notice. Rule 122 of the rules made under the Act lays down the form and contents of this notice. The notice must be in the forms Nos. 81 and 83 in the appendix to the rules (see Rule 122(4)). It must be published not more than two months before the declaration of the dividend and a special notice must be given in addition to such creditors in the schedule as have not proved their debts, It must also state the latest date up to which proofs must be lodged which shall not be less than fourteen days from the date of such notice.

11. In the present case the insolvent did not file his schedule. The claimants, therefore, were not entitled to a special notice but they were "persons whose claims to be creditors have been notified" to the Official Assignee u/s 73(1) of the Act because before the notice of February 5, 1927, there had been correspondence and negotiations regarding the sale of the security and the disclaimer of the lease by the Official Assignee (see the Official Assignee's letter of July 17, 1924, and the affidavit of the claimants dated August 18, 1924, para 6). But even if the claimants cannot be regarded as persons who "before the notice to declare dividend were entitled to the benefit of a notice u/s 73(1), there is nothing in the Act or the rules that I can see which prevents any creditor coming in or proving before the latest date fixed in the notice and published as required by Rule 122. The notice as a matter of fact did not comply with Rule 122. It was published more than two months before the declaration of dividend and it did not state the latest date within which creditors could prove. The necessity of giving such a date is important because it limits the time for proof and dates the rejection of the proof within that time as the starting point for an appeal against the Official Assignee's decision. As a matter of fact the notice merely stated that creditors were to prove "as soon as possible" which is indefinite and in conflict with the requirement in the rule that the latest date for proof must be "not more than fourteen days from the date of the notice".

12. We have been informed by the Official Assignee that the practice is for the notice calling upon the creditors to prove their claims "as soon as possible" to be followed up by a further notice requiring them to prove within a fortnight from the date of the notice; but though we have had enquiries made as to such a second notice having been issued in this case, the solicitors of the parties have been unable to find any trace of it.

13. The fact that the claimants had entered into possession of the mortgaged premises has, in my opinion, no bearing on the claimants' rights because there is nothing to show that by doing so they waived their right to prove for the balance of the mortgage debt. They did not do so in extinction of the debt.

Indeed it is scarcely credible they would considering what they realised on the security, notwithstanding their assertion at first that it would amount to 75 per cent, of the mortgage debt.

14. We, therefore, hold the dividend should be disturbed as the claimants' claims should have been taken into account, and as the Official Assignee failed to comply with the rules; but we will pass our final order after our judgment in the connected Appeal No. 69 of 1927.

Fawcett, J.

15. My learned brother has in the judgment he has just read, fully stated the facts out of which this appeal arises.

16. The main contention of the appellants is that stated in paragraph 6 of the memorandum of appeal. It was alleged by Mr. Munshi for the respondents that this was a ground that had not been urged in the lower Court, and that respondents Nos. 1 and 2 are prejudiced by their not having had an opportunity of putting in all relevant evidence upon this point. In the view, however, that we take, the question of their being allowed to put in any additional evidence becomes unnecessary.

17. The contention of Mr. Coltman for the appellants is briefly as follows:—

18. He says that the disclaimer of the insolvent's interest in the lease by the Official Assignee in October 1924 did not operate to extinguish the security, which respondents Nos. 1 and 2 had by the mortgage of the insolvent's interest in the leased property in their favour;

(2) that any surrender or release of the equity of redemption in regard to the insolvent's interest in the property under the deed of March 20, 1926, was invalid and did not operate to put the respondents Nos. 1 and 2 in the position of unsecured creditors of the insolvent; and

(3) that, as they were really secured creditors, the proof that they submitted on February 23, 1927, being on the basis of their being unsecured creditors, did not comply with the Rules 9 to 15 in Schedule II of the Presidency Towns Insolvency Act, 1909, and that accordingly under Rule 16 they should be excluded from all share in the dividend declared by the Official Assignee.

19. Mr. Munshi, on the other hand, contends that the disclaimer put an end to all rights and liabilities of the insolvent, that the respondents ceased to be secured creditors, and that the proof submitted was a valid one. He also raised other contentions which need not be considered at present.

20. The first question, therefore, is what was the effect of the disclaimer by the Official Assignee in regard to the position of the respondents as mortgagees. Mr. Coltman argued that the deed of March 20, 1926, purported to be a release and surrender not only of the interest of the deceased Kaderbhoy Mulla Noorbhai in the property and a full discharge of his liability to pay the mortgage money, but

also of the interest and liability of the insolvent Evans. I do not, however, think that the document is really open to this interpretation, having regard to the definition of the expression "the Mortgagors" in its preamble. This definition confines that expression to the legal representatives of Kaderbhoy. Moreover, the final clause about the right being reserved to the mortgagees to rank as creditors to the full extent of the estate of the insolvent and to receive dividends which might be declared in regard to it, is against such a construction. The deed was drawn up by solicitors, respondent No. 1 being himself a solicitor, and he would presumably be aware that the last clause would be open to objection, if his deed purported to deal with any part of his security so far as the interest of the insolvent was concerned. Therefore, the main ground on which Mr. Coltman put his contention that the respondents remained secured creditors is not, in my opinion, made out. On the other hand, Mr. Munshi's contention that Sub-section (2) of Section 62 of the Presidency Towns Insolvency Act, 1909, in itself made the disclaimer operate so as to extinguish the insolvent's equity of redemption and the security that the mortgagees had in respect of Evans's interest in the mortgaged land, ignores the closing words of the sub-section, viz., "but (such disclaimer) shall not, except so far as is necessary for the purpose of releasing the insolvent and his property and the official assignee from liability, affect the rights or liabilities of any other person." Prima facie, those words would cover such rights of the mortgagees as could be enforced without affecting the liability of the insolvent and the Official Assignee under the terms of the lease in the insolvent's favour. I was at first inclined to think that some security remained, so that in February 1927 the respondents were secured creditors of the insolvent. But a consideration of the provisions of Section 66 of the Act, and of the English authorities in regard to corresponding provisions in Section 55(6) of the Bankruptcy Act, 1883, (46 & 47 Viet, c. 52), from which Section 66, Sub-section (1) was taken verbatim, has led me to a different opinion, Sub-section (2) of Section 86 is similarly based on Section 13 of the Bankruptcy Act, 1890 (53 & 54 Vic. c. 71); and both of these are now reproduced in Sub-section (6) of Section 54 of the Bankruptcy Act, 1914 (4 & 5 Geo. V. c. 59). These provisions put any under-lessee or mortgagee of a lease-hold property burdened with onerous covenants, &c., in rather an awkward position; in fact, such under-lessee or mortgagee is liable to lose his interest in or security upon the property, unless he accepts a vesting order making him either (a) subject to the same liabilities and obligations as the insolvent was subject to under the lease at the date when the insolvency petition was filed, or (b) subject to such liabilities and obligations as arise on or after the date of the filing of the petition, *In re Finley. Ex parte Clothworkers' Company* (1888) 21 Q.B.D. 475. it was pointed out by Lindley L.J. that the effect of the proviso corresponding to that in Sub-section (1) of Section 66 was that, if an application for a vesting order is made by the under-lessee or mortgagee (hereinafter called the sub-lessee) (p. 486):

the vesting order can only be made in favour of the sub-lessee, subject to the covenants and conditions of the original lease, and, if the sublessee will not take

the property of those terms, which, of course, he need not do, then these consequences appear to follow : First, the sub-lessee will be excluded from all interest in the disclaimed property. Whether the latter part of the proviso in Clause 6 (i.e., sub-s. (1) of Section 66 of the Indian Act) will apply will depend upon whether there is any such person as is there referred to. There may or may not be. If no vesting order is made, the lease will be determined under Sub-section 2 (i.e., Sub-section (2) of Section 62 of the Indian Act), the sub-lease will be determined under Sub-section 6 (i.e., Sub-section (1) of Article 66), and the lessor will take the property freed from both lease and sub-lease.

He pointed out that this was a very startling result and would very seriously affect the old practice of taking securities on leasehold property by way of sub-demise, the whole object of which was to prevent the mortgagee from becoming liable to the rent and to the covenants and obligations of the original lease. It appears to have been in consequence of this that Section 13 of the Bankruptcy Act, 1890, was enacted. But, as pointed out in *Garter & Ellis, In re, Savill Brothers, Ex parte* [1905] 1 K.B. 735. that provision did not (p. 749):

give the Court any power to put the mortgagee back in his old position. The sole choice is between taking a vesting order " subject to the same liabilities and obligations as the bankrupt was subject to under the lease in respect of the property at the date when the bankruptcy petition was filed," and taking the order " subject only to the same liabilities and obligations as if the lease had been assigned to him at that date.

21. In *In re Smith. Ex parte Hepburn* there had been a disclaimer of a lease granted to the bankrupt by the trustee in the bankruptcy with the permission of the Court. One day prior to the Court's order the mortgagees executed a deed by which they absolutely assigned the mortgage debt and all interest therein to a clerk of the mortgagees, who, admittedly, was a man of small means. It was held that this was a sham assignment and that the original lessor was entitled to an order that unless the mortgagees would, within a certain time, accept an order vesting in them the mortgaged property, subject to the same liabilities and obligations as the bankrupt was subject to in respect thereof under the original lease at the date when the bankruptcy petition was filed, the mortgagees would be excluded from all interest in, and security upon, the mortgaged property. This decision gave effect to the provisions of the law corresponding to Sub-section (1) of Section 66. The question is whether the fact that the lessor has not, in the present case, obtained an order excluding the mortgagees from all interest in and security upon the insolvent's property makes any difference.

22. The record shows that the mortgagees applied to the Commissioner in Insolvency for an order inter alia that the equity of redemption of the insolvent in the property comprised in the lease was extinguished and that the right, title and interest of the insolvent in the said lease and the property built in pursuance thereto vested in the applicants. (See the affidavit of August 18, 1924, by respondent No. 1). The minutes of the Court's order of September 3, 1924,

shows that the mortgagees were represented before it, but the Court passed no vesting order of the kind applied for. It merely sanctioned the disclaimer of the Official Assignee. The reasons for this are not on record, but I think it is a safe presumption that that was mainly due to the terms of Sub-section (1) of Section 66 and the unwillingness of the mortgagees to accept a vesting order upon the terms laid down in that sub-section or in Sub-section (2) of that section. Sub-section (1) says that any under-lessee or mortgagee declining to accept the vesting order upon such terms shall be excluded from all interest in and security upon the property. That is a positive provision, which does not depend upon any actual order of the Court. It seems to me, therefore, that the effect of the proceedings before the Commissioner in Insolvency in 1924, is that the security of the mortgagees in the leasehold property in question, so far as regards the interest of the insolvent in the property, was extinguished.

23. I may add that this agrees with the view taken by Lindley L.J. in *In re Finley*, in the passage I have already cited. He there says (p. 486):?

If no vesting order is made, the lease will be determined...the sub-lease will be determined...and the lessor will take the property freed from both lease and sub-lease.

This was followed by this Court in *Abubaker, In re I.L.R (1924) Bom 580: 26 Bom. L.R. 628*. though in that case there were no complications of an under-lease or mortgage.

24. Accordingly, I think that the respondents were in law entitled to say that in February 1927 they were unsecured creditors of the insolvent. I was at one time inclined to think that, in so far as they had further security by virtue of the lessor J.R. Patel having been a surety under the mortgage of December 21, 1921, they still were secured creditors. This was because the definition of the expression "secured creditor" in Section 2(g) of the Act of 1909 is not the same as the definition of that expression in Section 168(1) of the Bankruptcy Act of 1883. Under the latter definition a "secured creditor" means a person who holds a mortgage, charge or lien on the debtor's property or any part thereof, as a security for a debt due to him from the debtor;" whereas the Indian definition only says the expression "includes a landlord who under any enactment for the time being in force has a charge on land for the term of that land." But I think that there is no reason to suppose, that the Legislature intended the expression to have a different meaning from that which it has in England, having regard to the closeness with which the Indian Act follows the provisions of the English Bankruptcy Act of 1883. That view is further strengthened by the fact that in the Provincial Insolvency Act of 1920, the definition of "secured creditor" follows the English definition instead of the one in the Presidency Towns Insolvency Act of 1909, which was also contained in the Provincial Insolvency Act of 1907.

25. It follows that upon the disclaimer there was no property of the bankrupt and a third party jointly, which was security for the debt due from the insolvent to

the mortgagees, so that the test about the property, if given, augmenting the bankrupt's estate would not come into operation: cf. Halsbury's Laws of England, Vol. II, p. 224, Article 368.

26. It is unnecessary to consider whether the disclaimer by the Official Assignee was unnecessary in view of what was held in *In re Gee, Ex parte Official Receiver* (1889) 24 Q.B.D. 65. As pointed out by Mr. Munshi, this case does not apply in India for reasons which are set out in *Vithal Narayan v. Shriram Savant* I.L.R (1905) Bom. 391: 7Bom. L.R. 313. The affidavit actually filed as proof in the insolvency recited that the respondents had not had or received any manner of satisfaction or security whatsoever in respect of the debt due under the deed of mortgage. That statement is open to criticism. It would, I think, have been better if it had said, as the form contemplates. "save and except the following, viz,, the security provided by the mortgage deed dated December 21, 1921, which has been extinguished by virtue of the disclaimer of the Official Assignee of the insolvent's interest in the lease to the insolvent and Kaderbhoy Mulla Noorbhai and its consequences," This does not, however, substantially affect the validity of the proof. It is at the most an irregularity falling under Rule 197 of the Bombay Insolvency Rules, 1910.

27. I, therefore, think that Rules 9 to 15 do not apply in this case and that Rule 16 accordingly does not come into operation.

28. In regard to 8. 72 of the Act the respondents had lodged their proof in accordance with the Rules 1 to 4 in the second schedule of the Act, and they are not, therefore, creditors, who had not proved their debt before the declaration of a dividend, so as to fall under the bar against disturbance of a distribution of dividends contained in Section 72. The fact that the Official Assignee had not accepted the proof in accordance with the provisions of Rule 119 under the Presidency Towns Insolvency Act cannot be allowed to prejudice the rights of the respondents. It is true that they should have used more expedition in bringing to the notice of the Official Assignee that they had already replied to his letter of February 24, 1927; but they had sent the deed of March 20, 1926, to his office for inspection and the Official Assignee had access to the documents under which the disclaimer had been made by him. I think, therefore, there is adequate ground for disturbing the distribution as one not validly made, and agree with my learned brother on this point, as well as to the irregularities in the action taken by the Official Assignee in this case that he has stated in his judgment.

29. Our orders in the appeal can best be passed, after our judgment in the connected Appeal No. 69 of 1927 has been delivered.

30. As regards the question of costs we have heard counsel in this case. Respondents Nos. 1 and 2 have succeeded and would ordinarily be entitled to their costs either from the appellants or from the insolvent's estate. We certainly do not think that this is a case where the insolvent's estate should be made further liable in respect of costs. There is also the consideration that respondents

Nos. 1 and 2 are in some way to blame for the Official Assignee not recognising them as creditors who had proved their claim; first of all because they did not show due expedition in answering his reminder about the letter he had sent them, secondly because of their negligence in not fully stating the circumstances under which they contended that they were not secured creditors; and even in the appeal before us, these respondents have really succeeded mainly upon a view taken by up in regard to Section 66 which was not, so far as I remember, even referred to by either of the learned Counsel, while the appeal was being argued. We, therefore, think that the proper order to pass would be that the appellants must bear their own costs of the appeal and half the respondents' costs. Respondents Nos. 1 and 2 must bear their remaining costs. We do not think that this is a case where we can properly certify for two counsel.