
(1970) 11 KL CK 0014
In the High Court Of Kerala
Case No : A.S. No. 380 of 1965

K.S. Raghavan and Others

APPELLANT

Vs

Iswara Pattar Gramom Parameswara Sastrigal's son
Subbarama Sastrigal and Another

RESPONDENT

Date of Decision : 27-11-1970

Acts Referred:

Contract Act, 1872 — Section 74

Citation : AIR 1972 Ker 21

Hon'ble Judges : T.C. Raghavan, J;E.K. Moidu, J

Bench : Division Bench

Advocate : T.S. Venkiteswara Iyer and R.C. Plapilly, for the Appellant; V. Bhaskaran Nambiar, C.R. Natarajan and M.K. Ananthakrishnan, for the Respondent

Judgement

Kaghavan, J.—The respondents as stake-holders started a kuri (chit fund) in September 1962, wherein the appellants took two tickets. They bid both the tickets, one at the third draw and the other at the tenth, and took the amounts. They also executed bonds to secure future instalments. However, they committed default in paying the future instalments; and the respondents brought the suit giving rise to the appeal for the realisation of the future instalments in a lump with interest. The appellants raised two contentions before the lower court: one, that the kuri vari (the rules of the kuri) contained several unconscionable and penal provisions, more particularly, the provision relating to the payment of all the future instalments in a lump with interest at 12 per cent, ignoring the claim of the appellants for their share in the reductions (the dividend); and two, that the respondents (the first respondent, to be more precise) acquiesced in the default and gave time to the appellants for the payment of the defaulted instalments, so that the suit for the realisation of all the future instalments together was not maintainable. Both the contentions were rejected by the lower court, and hence the appeal.

2. The main question argued by the counsel of the appellants is the first one mentioned above. Eight or nine decisions have been cited before us by the counsel on both sides--decisions of the Madras High Court, of the Travancore High Court and of the Cochin High Court. We shall refer only to the more important of them, they being all of the Madras High Court. The only other decision, to which we propose to refer, is the decision in Krishnan Ramen v. Ramen Aiyappen, 21 Trav LR 52, a decision of the Travancore High Court. A chitty scheme (a kuri is a chitty in Travancore) collapsed at the eighth draw; and the foreman assigned, with the consent of the non-prized subscribers, the security bond furnished by one of the prized subscribers to a non-prized subscriber. In the suit brought by the assignee for realising the future subscriptions in a lump, the contention raised was that, since the clause was penal, the benefit of the clause would not enure to the assignee. And this contention was rejected by the Travancore High Court holding that the clause was not penal.

3. Then we come to the decisions of the Madras High Court, the first being Vaithinatha Iyer v. Govindaswami Odayar. AIR 1922 Mad 67, a decision by a Division Bench. The Division Bench held that, where a chit agreement provided that in case the subscribers failed to pay their subscriptions regularly they were not only to forfeit the dividend but were also to pay the whole amount on demand with interest, the most material element to be decided was whether the terms of the agreement (the provisions in the kuri vari), as a whole, were unreasonable and whether they were so unreasonable that the parties never contemplated that they should receive effect and that the special relation of the parties justified the stringency of the conditions. And this question the Division Bench answered in favour of the stake-holder. (This decision, probably, may be the best for the respondents in this case).

4. The next decision chronologically is the decision in Ramalinga Adaviar and Another Vs. Meenakshisundaram Pillai and Others, by Srinivasa Aiyangar, J. The learned Judge considered the principle underlying the law of penalty and held that the question whether any stipulation in a kuri vari was only by way of compensation or by way of penalty depended upon the construction of that particular document or contract and on the circumstances of the case. The learned Judge referred to the leading English case in John Wallingford v. Directors of Mutual Society 1880 AC 685 and held that, if on a proper consideration and construction of the contract, the court came to the conclusion that--

"the real agreement between the parties was to the effect that the whole amount was on the date of the bond a debt due but the creditor for the convenience of the debtor allowed it to be paid by instalments intimating that if default should be made in the payment of any instalment he would withdraw the concession, then the stipulation as to the whole amount of the balance becoming payable would not be penal".

But if, on the other hand, on a proper consideration and construction of the contract between the parties the court came to the conclusion that--

"the debt itself is an instalment debt so to call it, that is to say, that the debt itself arises or becomes due and payable by the debtors on the respective dates fixed for the instalments, the stipulation that on default being made in the payment of any instalment the whole of the balance should become due and payable would be in the nature of a penalty."

Ultimately, the learned Judge held that the claim for all the future instalments in a lump was a penalty.

5. The next case is Muthukumarasamiah Pillai Vs. Subramanian Chettiar and Others, . The learned Judge who decided this case (Ramesam, J.) was one of the Judges who constituted the Division Bench in Vaithinatha Iyer's case AIR 1922 Mad 67 already referred to. Reliance was placed by one of the Parties before the learned Judge on the earlier Division Bench ruling, But, Ramesam, J, said

"I do not understand that case to lay down that the terms of a chit fund contract can never be penal It only says that in such a contract, the stakeholder undertakes extra risks and is entitled to heavier compensation than ordinary cases and such contracts should be scrutinised with less stringency and jealousy than ordinary contracts."

And Ramesam, J, agreed with Srinivasa Aiyangar. J.

6. Then we have three other decisions, all of the year 1933, the earliest being M. Kunju Nair Vs. Narayanan Nair, by Anantakrishna Ayyar. J. The learned Judge held that a particular stipulation in kuri vari might be in the nature of a penalty: but, in the opinion of the learned judge, the provision to pay all the future instalments in a lump in the case of default by a prized subscriber in the payment of any future instalment provided for by the kuri vari was by itself not a penalty. The next decision is Subbiah Pillai Vs. Muthiah Pillai and Others, , a Division Bench ruling. The Division Bench held that a provision in a kuri vari by which a prized subscriber bound himself to be liable for the future instalments and on default to have demanded from him in a lump all the future instalments was not a penal one. And the last decision of the same year is Ayyakannu Pillai and Another Vs. Doraiswami Pillai and Others, by Walsh, J. The learned Judge dissented from the decision of Srinivasa Aiyangar, J. in Ramalinga Adaviar and Another Vs. Meenakshisundaram Pillai and Others, and followed the Division Bench ruling in Vaithinatha Iyer's case, AIR 1922 Mad 67. He also referred approvingly to the decision in M. Kunju Nair Vs. Narayanan Nair, by Anantakrishna Ayyar, J.

7. These are the decisions (all of the Madras High Court) which, in our opinion, are relevant for the main question we have to consider in this appeal. As indicated already, the strongest case in favour of the respondents is the earliest Division Bench ruling in Vaithinatha Iyer's case AIR 1922 Mad 67 . But, one of

the learned Judges who constituted the Division Bench, Ramesam, J., himself subsequently interpreted that decision in his later ruling in *Muthukumarasamiah Pillai Vs. Subramanian Chettiar and Others*, . According to the learned Judge, the effect of the earlier Division Bench ruling was only that courts should recognise that the stake-holder in a kuri undertook extra risks and was entitled to heavier compensation than in ordinary cases and such cases should be scrutinised with less stringency and jealousy than ordinary contracts. And the learned Judge followed the decision of Srinivasa Aiyangar, J, in *Ramalinga Adaviar and Another Vs. Meenakshisundaram Pillai and Others*, . Therefore, the earliest Division Bench decision cannot be straightway accepted as to have laid down that, in a case where a stake-holder demands payment of all the future instalments in a lump with interest thereon without allowing the prized subscriber his share in the dividend (a case like the present one), he is entitled to a decree as the provision is not penal. The other decisions discussed by us, excepting the decision by Srinivasa Aiyangar, J. in *Ramalinga Adaviar and Another Vs. Meenakshisundaram Pillai and Others*, and the decision by Ramesam, J, in *Muthukumarasamiah Pillai Vs. Subramanian Chettiar and Others*, lay down that the stake-holder has a right to claim all the future instalments in a lump; but in those cases all the three penal provisions were not present, namely, lump payment, refusal to give share in the reduction (dividend) and interest on all the arrears.

8. The counsel of the appellants has drawn our attention to a few decisions on the question as to what is meant by a penal provision. One of the decisions cited is the Division Bench ruling of the Bombay High Court in *Burjorji Shapurji Sheth Vs. Madhavlal Jesingbhai*, , where Beaumont, C. J., who spoke for the Division Bench, laid down the test of a penal provision thus: "If there is an agreement to pay a sum of money by a particular date with a condition that if the money is not paid on that date a larger sum shall be paid, that condition is in the nature of a penalty against which a court of equity can grant relief and award to the party seeking payment only such damages as he has suffered by the non-performance of the contract. But if, on the other hand, there is an agreement to pay a particular sum followed by a condition allowing to the debtor a concession, for example, the payment of a lesser sum, or payment by instalments, by a particular date or dates, then the party seeking to take advantage of that concession must carry out strictly the conditions on which it was granted, and there is no power in the court to relieve him from the obligation of so doing". And the learned Chief Justice observed that, in the latter case, time was the essence of the contract.

9. The next decision and the only other decision we wish to refer to is again a Division Bench ruling, the decision of the Patna High Court in *Khetro Swain and Others Vs. Sri Sri Sri Padmanabha Singh Deo*, . The learned Judges of the Patna High Court referred to the Division Bench ruling of the Bombay High Court which we have just now referred to and followed it. We recall at this stage the decision of Srinivasa Aiyangar, J. in *Ramalinga Adaviar and Another Vs. Meenakshisundaram Pillai and Others*, wherein also the learned Judge laid down

the same principle after referring to the English decision in 1880 AC 085.

10. In the light of these decisions, what emerges is that the entire kuri vari, as a whole, has to be considered to see whether the transaction is unconscionable or penal. (Probably, particular provisions in the kuri vari may receive special attention in particular cases). This position appears to have been accepted even in the strongest case in favour of the respondents. The second aspect is that the provisions of the kuri vari have to be tested in the light of the principle laid down in John Wallingford's case (1880) 5 AC 685 and in Burjorji Shapurji Sheth Vs. Madhavlal Jesingbhai, by Beaumont, C. J. and followed by the Patna High Court in Khetro Swain and Others Vs. Sri Sri Sri Padmanabha Singh Deo, . The third aspect is that, in applying this test, it must be borne in mind that a stakeholder of a chit fund runs extra risks, and the unconscionable or penal nature of the kuri vari has to be tested in the light of these circumstances, viz., that he is entitled to heavier compensation.

11. We shall now examine the provisions of the kuri vari in the present case, Ex. A7. It has 13 clauses, of which we shall hereinafter refer to only the more important ones.

12. The first clause provides that the total amount of the chit be Rupees 15,000/- with 50 tickets, the price of each ticket being Rs. 300/-; and that there will be a draw every month on the 4th of the Malayalam month. The stakeholders take the first ticket; and they also take Rs. 500/- every month as remuneration for their trouble and Rupees 15/- to meet the expenses of providing refreshments to the subscribers who attend the draw. The balance of Rupees 14,485/- is the amount available for bidding at the monthly auctions; and the lowest bidder will be the winner. The reduction made in the bidding (the leladayam) is to be distributed among all the subscribers prized and non-prized, The first ticket having been taken by the stake-holders, they collect and appropriate the sum of Rs. 15,000/- for that ticket; and they need also pay at every subsequent draw only the reduced amount, reduced by their share of the dividend. Subscriptions for the earlier tickets will normally be roughly between Rs. 180/- and Rs. 250/- per month; and it will be Rs. 300/- for the last draw only, or for a ticket at the draw of which there is no bidding. The stakeholders pay this amount from the sum of Rs. 500/- they get as their remuneration; and the balance they appropriate every month. The result is that the stake-holders get Rs. 15,000/- at the beginning and about Rs. 250/- to Rs. 300/- every month thereafter.

13. The second clause makes provision that a non-prized ticket-holder should pay his subscription on the day of the chit or within a week thereof. If he does not pay the same as mentioned above, he has to pay a sum of Rs. 5/- along with the subscription on the next draw day, i.e., three weeks after. If he fails to do that also, he is a defaulter and has no right to bid his ticket and he can also be removed from the kuri. Such a subscriber who is removed from the kuri will be paid only the actual amount subscribed by him, less Rs. 515/- (the stake-

holders" remuneration plus the expenses for refreshments); and that will be done without any interest within two months of the close of the kuri. The unreasonableness of this provision is evident. The defaulter does not get his share in the reduction: he does not get any interest for his money. That is probably understandable; and his removal from the kuri is also understandable. But, we are not able to understand why he should pay to the stake-holders Rs. 515/- from the subscriptions he paid already. His ticket is not yet prized; and at every draw the stake-holders are taking Rs. 515/- from the total amount and the balance alone is available for bidding. Evidently therefore, this is a double collection; and it is impossible to justify it on any ground whatever.

14. The next clause, the third clause, provides that if any subscriber bids his ticket, he must furnish security for future subscriptions to the satisfaction of the stake-holders after a month from the bid. If he fails to give such security, the stake-holders keep the bid amount and add interest thereto at 3 per cent, per annum (note the percentage of interest); and out of the total of the principal and interest, adjustments will be made towards the future instalments payable by him without giving credit to him for his share in the reduction, i.e., the future instalments will all be the entire Rs. 300/- each. If the bid amount and interest thereon at 3 per cent, is not sufficient to meet all the future instalments, the balance will be collected from the subscriber. The money that is left with the stake-holders is the subscriber's money; and we are at a loss to appreciate why he should be denied his share in the dividend, at any rate, until the money is exhausted in being adjusted towards the future instalments. And the interest added is 3 per cent, per annum.

15. Clause 4 is, in fact, a continuation of Clause 3. In a case where a prized subscriber fails to furnish security and take the money and if the amount so left with 3 per cent, interest thereon exceeds the future instalments in full without any share in the reduction, the balance will be paid to him either then itself or at the close of the chit. Even here, the excess money is not paid immediately; and it is left to the discretion of the stake-holders.

16. Clause 5 states that if a prized subscriber fails to give security and leaves the bid amount with the stakeholders, the subscriber is not entitled to any share in the reduction (dividend). But, if he pays the future subscriptions regularly, he will be entitled to a share in the reduction. However, if he defaults payment of one instalment, he loses his claim for the share in the reduction in the future. A little surprisingly, there is not even a provision for payment of even the 3 per cent, interest in this case: probably, interest is not provided as the subscriber is getting his share in the dividend. Then, look at the unreasonableness of the provision: the subscriber leaves his money with the stake-holders and goes on paying the future subscriptions too. And the result is that he loses the interest on his money.

17. Clause 6 deals, again, with prized subscribers. A prized subscriber, who has taken the bid money furnishing security to the satisfaction of the stakeholders,

must pay the future subscriptions regularly on the day of the kuri. If "he commits default in paying any one future instalment, he must pay a sum of Rs. 10/- as penalty and pay the amount on the next draw day, i.e., a month after. If he fails to do even that, then all the future instalments without any benefit of the reduction becomes due immediately; and the said amount can be collected in a lump with 12 per cent, interest. (Note the rate of interest here). This is the provision particularly relevant in this case.

18. Then comes Clause 7, which, in our opinion, is not very material. Still, one thing strikes us. If a prized subscriber fails to satisfy the stake-holders by furnishing additional security when such additional security is demanded, his right to claim the dividend is lost.

19. The next clause, Clause 8, has struck us as a very curious provision: and we are surprised how such a provision can find place in a kuri vari. It provides that, if a subscriber owes any money on any account to either or both of the stake-holders, that is a first charge on the subscriptions paid by the subscriber and such amount can be adjusted from the subscriptions paid by him Without any suit, on a mere notice, or even on just an oral information regarding that. This is a method, evidently, to collect the other dues of the stakeholders, who, it will do well to remember, are money lenders. We cannot find any justification, cannot even imagine one, for this provision in a kuri vari.

20. The only other clause which we have to consider is Clause 10: and that again has struck us as a very unfair provision in a kuri vari. The clause lays down that, if no subscriber turns up on a draw day or those who have turned up do not bid, then lots of the non-prized subscribers will be taken and the subscriber whose ticket is drawn will be declared the winner. But, the amount payable to him is not the entire amount. As already pointed out, after making a deduction of Rs. 500/- as remuneration for the stake-holders and Rs. 15/- for providing refreshments, the balance of Rs. 14,485/- is the amount that should naturally, normally and reasonably go to the subscriber whose ticket is drawn. Still, what is provided is that he will be paid only such amount, which with 6 per cent, interest thereon, will make Rs. 14,485/- at the close of the chit. We wonder on what principle this provision can be justified! No subscriber is prepared to bid for a reduced amount; and therefore, there is no reduction which is to be distributed among the other subscribers. The entire Rs. 14,485/- is the money of the winner at the draw: and the stake-holders just take a portion out of it for no reason whatsoever. What the subscribers pay for that instalment is the full Rs. 300/-, since there was no reduction at the bid. And all these several provisions provide for all sorts of conceivable appropriations by the stake-holders.

21. Clauses 9, 11, 12 and 13 are not material.

22. If the entire kuri vari is considered as a whole to see whether the transaction embodied in the document is fair or penal, the only conclusion is that unconscionableness is writ large in the document.

23. However, it is contended that In this case we need not consider all the provisions, but need consider only Clause 6 of the kuri vari, on which alone the suit is based. Even here, we are of opinion that the stake-holders are not entitled to collect the entire future instalments in a lump without giving credit to the appellants for the dividend and that again with 12 per cent, interest. If the rate of interest is calculated on the basis of the several dates when the several instalments fall due, the 12 per cent, in this clause will easily work out to anything more than 20 per cent. Again, in the earlier draws the reductions are considerable. Naturally, in a case like this, where the prized subscriber is also allowed to share in the reduction, the tendency of the subscriber to bid at a more reduced amount is greater, because he will also get a share in the greater reduction: in other words, this provision allowing the prized subscriber to share in the reduction is, in effect, an invitation to reduce in the bids.

24. One of us had occasion to consider in *Thanuvan Velayudhan Vs. Velayudhan Mudaliar Appavu Mudaliar and Another*, the difference between a debt bond or a promissory note payable in instalments and a kuri security bond by a prized subscriber to secure the future instalments. It was held that in the former the debt became payable immediately, while in the latter the several instalments fell due only on the several future dates. (What was considered in that case was the applicability of Article 75 of the Limitation Act of 1908 to a kuri security bond). This will bring a kuri security bond giving a right to the stake-holder to claim in a lump all the future instalments if the subscriber defaults payment of one or two instalments within the mischief of the principle regarding penalty laid down by the English decision in (1880) 5 AC 685 and by Beaumont, C. J. in the Bombay case. Even if such a provision is considered to be essential to compensate the stake-holder for the extra risks he takes, we think that in a case like the one before us, where there are three penal provisions--collection of all the future instalments in a lump, the denial to the subscribers their share in the reduction or dividend and interest at 12 per cent., which, if calculated on the basis of the several due dates of the instalments, will work out to more than 20 per cent., the provision is undoubtedly penal and unconscionable. We also reiterate that this provision has to be considered in the background of the several other provisions of the kuri vari which we have already discussed.

25. The next question that was urged before the lower court was whether there was acquiescence on the part of the first respondent who gave the appellants time to pay the defaulted instalments. On this question also, the evidence and circumstances indicate an answer against the respondents. Exs. B1 and B2 are two registered notices of the same date, 15th June 1964, the first sent by the father of the first respondent and the second sent by the first respondent. The first is a demand notice for the immediate payment of two amounts covered by two promissory notes of 15th February 1964 and 8th April 1964; and the second one is a notice demanding payment of the defaulted instalments in a lump. In this connection, one more fact has to be noted. In Clause 12 of the kuri vari, provision is made that the kuri subscriptions may be paid to either of the stake-

holders or to the father of the first stake-holder, the first respondent. It was this father that sent Ex. B1 demanding the promissory note amounts; and if the appellants who received both these notices say that they went with some amount to either the father or the first respondent offering to pay the defaulted kuri instalments and the father or the son wanted the amount to be adjusted first towards the promissory note debts of the father agreeing to give time for paying the kuri money, we think we are justified in believing them. It is only natural that, in such circumstances, the father's promissory note debts would have been recovered first and the appellants been given time for paying the kuri subscriptions. This might gain strength when we look into Exs. B9 and B10, which are said to be the promissory notes executed by the appellants to the father of the first respondent. (The counsel of the respondents has suggested, at the time of arguments, that these were not the promissory notes executed by the appellants, because there were no endorsements of payment on the back of these notes. But, we find some initials on these notes regarding cash payment; and nothing has been brought to our notice to suggest that D. W. 1 (the first appellant) was asked about it when he was in the box). These promissory notes provide for very high rates of interest; and the reply notice sent by the appellants to the father of the first respondent states that the interest had already been deducted from the money when the amount was paid. This also is not unbelievable, because it is notorious that money lenders take a portion of their interest even at the time of the loan and pay only the balance. At any rate, the counsel of the appellants has not adduced any argument on this question; and the counsel of the respondents has also pointed out that this question has not been raised in the memorandum of grounds of appeal. We, therefore, desist from expressing any final opinion on this Question.

26. What is claimed in the appeal is the share of the appellants in the reductions (the dividend), which is estimated at Rs. 10,000/-. Regarding this figure, we do not find any dispute. Therefore, the amount has to be taken at Rs. 10,000/-; and we do so.

27. Ultimately, the appeal is allowed and the decree granted by the lower court is reduced by the amount involved in the appeal. In the trial court, the respondents will get costs proportionate to their success; and in the appeal, the appellants will get their costs.

28. Before we leave this case, we wish to add a few words. In our experience, we have not yet come across such 3 kuri vari which has so many unconscionable provisions. Ground No. 5 in the memorandum of grounds of appeal shows the amount payable by the appellants, the amount received by them, etc. to show the unconscionableness. The appellants received only Rs. 16,185/- (on both the tickets together); and, all told, they already paid back Rs. 5,100/- as subscriptions. The claim in the suit towards future instalments is Rs. 21,000/- with interest of Rs. 1,785/-. And all this within less than two years, the date of commencement of the kuri being 20th September 1962 and the date of suit

being 2nd September 1964--for receiving a little over Rs. 16,000/-, the appellants have to pay a little less than Rs. 28,000/-. In our considered opinion, such transactions should not be allowed, and people who carry on such transactions are really unsocial elements. We are told that the same stakeholders are carrying on such kuries even now without any hindrance, because there is no law to control the conduct of chit funds now in the Malabar area. It is time that the Government be moved in the matter and brought some legislation to control such unsocial activities.

29. A copy of this judgment will be sent to the Chief Secretary to the State Government.