

(1946) 12 MAD CK 0006
In the Madras High Court

P.A.R. Chandrasekhara Nadar and Others	APPELLANT
Vs	
I. Palaniappa Chettiar and Another	RESPONDENT

Date of Decision : 06-12-1946

Acts Referred:

Provincial Insolvency Act, 1920 — Section 44(2)

Citation : (1947) 60 LW 127 : (1947) 1 MLJ 134

Hon'ble Judges : Alfred Henry Lionel Leach, C.J

Bench : Division Bench

Judgement

Alfred Henry Lionel Leach, C.J.—In this appeal the Court is called upon to decide what are the rights of a secured creditor of an insolvent

when the adjudication has been annulled as the result of the Court having sanctioned a composition, the creditor not being a party to the

arrangement and having taken no steps to realize his security before the annulment.

2. On the 19th October, 1937, the first defendant in the suit out of which the appeal arises executed a promissory note in favour of the plaintiff for

Rs. 3,000. The first defendant at that time was joint with his four sons (defendants 2 to 5), all of whom are minors. As security for the advance the

first defendant executed in favour of the plaintiff what has been described as a continuing security bond. The properties covered by the bond

formed part of the family estate. On the 17th December, 1937, two creditors applied to the Subordinate Court of Madura for the adjudication of

the first defendant under the provisions of the Provincial Insolvency Act. On the 21st February, 1938, an order of adjudication was passed, and in

accordance with the provisions of Section 27, the first defendant was directed to apply for his discharge within one year. Within the year the first

defendant submitted to the Insolvency Court a proposal for a composition in satisfaction of his debts. He offered to pay ten annas in the rupee. The wife of the first defendant, as the guardian of her minor sons, consented to the arrangement. The consent was necessary because the proposal involved the transfer of properties belonging to the joint family to trustees for the purpose of realisation. There were three secured creditors. The plaintiff refused to accept the proposal, but the other two secured creditors did so. Apparently, their securities did not represent as much as ten annas in the rupee. By an order dated the 10th July, 1939, the Court sanctioned the scheme and on the 8th October, 1939, the trust deed was executed by the father and by the minors acting through their mother. In due course the trustees realised all the assets of the family, except those charged to the plaintiff and two other lots of Immovable property. The proceeds of the realisation were sufficient to pay all the consenting creditors ten annas in the rupee. The administration was closed on the 30th November, 1940, when the unsold properties were delivered back to the minors' guardian. The properties charged to the plaintiff remained, of course, subject to his charge.

3. On the 16th March, 1942, the plaintiff filed the present action in the Court of the Subordinate Judge of Sivaganga for a decree directing the realisation of the properties charged to him, and, in the event of the proceeds proving to be insufficient to pay him in full, directing the balance to be realised from the other properties of the defendants and from the first defendant personally. The Subordinate Judge held that as the first defendant had only a one-fifth interest in the properties charged, the plaintiff must, in the first place, look to the proceeds of sale of that interest. If the money realized was not sufficient to discharge the liability in full the plaintiff was entitled to have recourse to all the joint family properties in the hands of the defendants. The sons appealed to the District Judge of Ramnad who agreed with the Subordinate Judge that the first defendant was only entitled to a one-fifth share of the properties charged to the plaintiff, but he held that if the one-fifth share did not satisfy the claim, the plaintiff could have recourse to the sons' interest in the sale proceeds. Should there still be a deficiency, the plaintiff was entitled to proceed against the joint family properties in the hands of the sons but only to the extent of ten annas in the rupee with interest at six per cent per annum. The plaintiff

appealed to this Court. His appeal was heard by Rajamannar, J., who restored the decree of the Subordinate Court. The learned Judge

considered that the case fell within the judgment of the Court delivered in Chokkalinga Mudali Vs. Manickka Mudali alias Singara Mudali, . but in

view of the decision in Govindas Chathurbhujadas v. Ramadas (1924) 48 M.L.J. 252 : ILR 48 Mad. 521 he gave the first defendant's sons leave

to appeal under Clause 15 of the Letters Patent. They availed themselves of the leave and their appeal is now before us.

4. In Chokkalinga Mudali Vs. Manickka Mudali alias Singara Mudali, . a mortgagee filed a suit on his mortgage and obtained a final decree for

sale. Subsequently the mortgagor was adjudicated insolvent under the Provincial Insolvency Act, but he obtained his discharge unconditionally. The

discharge was the governing factor in the case. During the pendency of the insolvency proceedings the mortgagee took no steps to enforce his

mortgage decree, but he did so after the discharge of the insolvent and in execution proceedings he obtained an order for sale of the hypotheca.

The amount realised was not sufficient to pay off the mortgage debt and consequently the mortgagee applied for a personal decree for the balance.

It was contended by the mortgagor that in view of his unconditional discharge a personal decree could not be passed against him. According to

him Section 44(2) of the Provincial Insolvency Act stood in the way. The Court refused to accept the contention for these reasons. Section 47 in

effect says that the debt of a secured creditor is not provable until he has realised his security or has abandoned it or valued it. Until one of these

events has happened there is no debt ""provable"" in the insolvency proceedings. A secured creditor may prove, but his right is a contingent one and

until the contingency arises he is outside the Act. When a secured creditor has not during the insolvency proceedings realised his security or

surrendered or valued it, Section 44(2) does not affect him, because no portion of the debt due to him has become provable and the section only

applies to debts which are provable in the insolvency. This means that a secured creditor is entitled to a personal decree if his security has not been

realised before the discharge of the insolvent. If it has been realised during the pendency of the insolvency proceedings and there is a deficiency,

the balance of the debt constitutes a debt provable in the insolvency and in such a case Section 44(a) will operate to cancel it.

5. The difference between an unconditional discharge of an insolvent and an annulment of insolvency is of importance. When an insolvent has obtained an order of discharge he is by virtue of Section 44 released from payment of provable debts, except (a) a debt due to the Crown ; (b) a debt or liability incurred by means of fraud or fraudulent breach of trust to which he was a party ; (c) a debt or liability in respect of which he has obtained forbearance by fraud to which he was a party ; or (d) a liability under an order for maintenance made u/s 488 of the Code of Criminal Procedure, 1898. An order of annulment in itself does not release an insolvent from the payment of his debts. Section 37 states that when an adjudication is annulled, all sales and dispositions of property and payments duly made and all acts theretofore done, by the Court or receiver, shall be valid ; but, subject to this, the property of the debtor who has been adjudged insolvent shall vest in such person as the Court may appoint, or, in default of an appointment, shall revert to the debtor to the extent of his right or interest therein on such conditions (if any) as the Court may, by order in writing declare. A vesting order is intended to be for the benefit of the creditors and allows the Court to retain supervision of the administration of the assets vested. Section 39 provides that if the Court approves the proposal for a composition or a scheme of arrangement, the order of adjudication shall be annulled, the provisions of Section 37 shall apply, and the composition or scheme shall be binding on all the creditors so far as it relates to a debt provable under the Act. Section 40 states that if default is made in the payment of an instalment due in pursuance of the composition or scheme, or if it appears that the composition or scheme cannot proceed without injustice or undue delay, or that the approval of the Court was obtained by fraud, it may readjudge the debtor insolvent and annul the composition or scheme, but without prejudice to the validity of any transfer or payment duly made or of any thing duly done under or in pursuance of the composition or scheme. Therefore in the case of annulment the position is very different from the position which arises when the insolvent has obtained an unconditional order of discharge.

6. The facts in *Govindas Chathurbhujadas v. Ramadas* (1924) 48 M.L.J. 252 : ILR 48 Mad. 521 have very little in common with the facts in

Chokkalinga Mudali Vs. Manickka Mudali alias Singara Mudali, . In *Govindas Chathurbhujadas v. Ramadas* (1924) 48 M.L.J. 252 : ILR 48

Mad. 521 the respondent was adjudicated insolvent under the Presidency Towns Insolvency Act. A statutory majority of his creditors agreed to accept a composition of eight annas in the rupee. No regular scheme of composition was placed before the Court, but the insolvent filed an affidavit to the effect that his creditors had agreed to the composition. The Court accepted the statements in the affidavit and annulled the adjudication. The appellant, a secured creditor, had not realised his security or proved for the balance before the order of annulment was made. No notice had in fact been given to him of the application for annulment. Subsequently, he instituted a suit for a decree directing the sale of the securities through the Court and the payment by the insolvent personally of the balance should the sale proceeds prove to be insufficient. It was held that the annulment of an adjudication u/s 30 of the Act did not amount to a discharge or release of the insolvent in respect of debts provable in insolvency, that the secured creditor's claim for the balance after realisation of the security was a debt provable in insolvency, that notwithstanding that the secured creditor was not a party to the composition, he was bound by it in respect of the unsecured balance of his debt and that he was not restricted to an application in insolvency by way of remedy but could file a suit on the basis of the composition. The relevant provisions of the Presidency Towns Insolvency Act do not differ materially from the corresponding provisions of the Provincial Insolvency Act.

7. The judgment in *Govindas Chathurbhujadas v. Ramadas* (1924) 48 M.L.J. 252 : ILR 48 Mad. 521 has direct bearing here. When the facts in the two cases are fully understood it is manifest that there is no conflict between *Chokkalinga Mudali Vs. Manickka Mudali alias Singara Mudali*, and *Govindas Chathurbhujadas v. Ramadas* (1924) 48 M.L.J. 252 : ILR 48 Mad. 521 and we see no reason to doubt the correctness of either decision. The fundamental difference between the two is that in the former case the insolvent received an unconditional discharge before the secured creditor took action while in the latter case there was no discharge, but merely an annulment of the adjudication as the result of the acceptance of a composition. Section 33(3) says that a creditor whose debt is provable under the Act may, at any time before the insolvent's discharge, tender proof of his debt and apply to the Court for an order directing his name to be entered in the schedule. Consequently until an

order of discharge is passed a secured creditor can at any time come in and prove the balance owing to him after the realisation of his security.

8. Section 126 of the Bankruptcy Act of 1869 provided that a composition which had been accepted by a resolution of the creditors should be

binding on all those included in the statement of the debtor produced at the meetings at which the resolution was passed, but should not affect or

prejudice the rights of other creditors. Referring to this section, James, L.J., in *In re Bestwick: Ex parte Bestwick* (1876) 8 Ch. D. 485 said:

Section 126 indeed says that the composition is to be accepted in satisfaction of the debts ; it says nothing about the debts of those creditors who

may hold security, and the words, if taken literally, would compel a secured creditor to accept the composition in satisfaction of the whole amount

of his debt, but they have been always construed as meaning that he is to take the composition only on the ultimate balance of his debt which may

remain due after realising his security. When he has realised his security he has a right to say to the debtor so much remains due to me pay me the

composition upon that.

As pointed out in *Govindas Chathurbhujadas v. Ramadas* (1924) 48 M.L.J. 252 : ILR 48 Mad. 521 Section 126 of the Bankruptcy Act of 1869

was not reproduced in the Bankruptcy Act of 1883, but similar provision was made. Section 18(8) of the Act of 1883 provided that an accepted

composition should be binding on all the creditors so far as it related to debts due, to them from the debtor and provable in bankruptcy.

9. The principle laid down in *In re Bestwick: Ex parte Bestwick* (1876) 8 Ch. D. 485 has-been accepted in India. The provisions of Section 39 of

the Provincial Insolvency Act, as amended by the Provincial Insolvency (Amendment) Act, 1935, follow the provisions of Section 18(8) of the

English Act of 1883. Before the amendment, Section 39 of the Provincial Insolvency Act made the scheme binding on all creditors entered in the

schedule so far as it related to a debt entered therein. Now it expressly binds all the creditors so far as debts provable under the Act are

concerned. Therefore where there has been no order discharging the insolvent, but merely an annulment of the order of adjudication a secured

creditor is bound by a composition of which the Court has approved in so far as the balance of his debt is concerned after the realisation of his

security. The fact that he has taken no part in the composition proceedings makes no difference. He can realise his security at any time, but when

he does and there is a deficiency he can only get payment on the basis of the composition, because the unsatisfied portion of the debt is ""provable

in the Insolvency Court in the absence of an unconditional order of discharge.

10. For these reasons the appeal must be allowed and the decree of the District Judge restored with costs throughout.