
(1957) 09 KAR CK 0002
In the Karnataka High Court
Case No : Appeal No. 81 of 1952-53

Srikantiah Setty and Others

APPELLANT

Vs

Abdulla Basha Saheb and Co. and Another

RESPONDENT

Date of Decision : 06-09-1957

Acts Referred:

Provincial Insolvency Act, 1920 — Section 5, 53, 54

Citation : AIR 1958 Kar 35 : (1957) ILR (Kar) 147

Hon'ble Judges : Somnath Iyer, J;Sadasivayya, J

Bench : Division Bench

Advocate : S. Rangaraj, for the Appellant; Venkataramiah, for the Respondent

Judgement

Somnath Iyer, J.—On 18-3-1942, four creditors of one S. M. Zackria whom I shall hereafter refer to as the insolvent, made an application to the District Judge, Bangalore, u/s 9 of the Mysore Insolvency Act for getting him adjudged insolvent. On that application he was so adjudged insolvent on May 29, 1942.

On July 7, 1942, the Official Receiver made an application (I. A. 2) under the provisions of Sections 5, 53 and 54 of the Act for a declaration that transfer made by the insolvent of his properties in favour of respondents 1 to 4 on January 5, 1942, and a subsequent transfer of those properties by respondents 1 to 4 in favour of the fifth respondent was voidable and should be annulled. He also added a further prayer to his application that the Court should direct the said properties or their value to be handed over to him by the respondents.

2. Respondents 1 to 5 opposed that application and the learned District Judge allowed it. Respondents 1 to 4 have appealed and respondent 5 has not.

3. It is admitted that on January 5, 1942, by a document of sale which is not exhibited in this case the insolvent transferred to respondents 1 to 4 who were some of his creditors, all his assets belonging to a business which he was conducting. It is stated, although it is not admitted by the Official Receiver, that the consideration for the transfer was a sum of Rs. 3,300.

On the next day, i.e., on January 6, 1942, respondents 1 to 4 in their turn transferred all those assets which they had purchased from the insolvent to respondent 5 and it is stated that the consideration for that transfer was a sum of Rs. 5,500. The case for the Official Receiver is that both these transfers were neither made in good faith nor for valuable consideration but were made for the purpose of defrauding the other creditors of the insolvent.

As I have mentioned above, a little more than two months after the dates of these transfers some other creditors of the insolvent presented the application for getting Zackria adjudged insolvent. In the meanwhile, the insolvent himself had issued a notice (Ex. III) on January 29, 1942, twenty-five days after he had transferred his assets to respondents 1 to 4, repudiating the transaction of transfer and also alleging that a document in that regard had been fabricated by respondents 1 to 4. I. A. 2 filed by the Official Receiver for getting these transfers annulled, was made as I have mentioned above, on July 7, 1942.

4. The alienation in favour of respondents 1 to 4 by the insolvent and that in favour of respondent 5 by respondents 1 to 4 were within two years from the date of the presentation of the petition for getting Zackria adjudged insolvent. It is therefore not disputed that this was a case to which Section 53 of the Insolvency Act applied and under which the transfers could be annulled provided it was established by the evidence that those transfers by them were found to be not made in favour of the purchasers in good faith and for valuable consideration. It is now settled law that in proceedings u/s 53 of the Insolvency Act the onus of proving that the impugned transactions were not entered into in good faith and for valuable consideration is on the Official Receiver. The question to be decided in this appeal is whether the learned District Judge was right in coming to the conclusion that these two transfers assailed by the Official Receiver were not entered into in good faith and for valuable consideration.

5. It is undisputed that Zackria who was adjudged insolvent on May 29, 1942, was in extremely difficult financial straits at the time when he transferred all his assets in favour of respondents 1 to 4 as stated above.

Schedule A to the application presented by his creditors for getting him adjudged insolvent, enumerates as many as twenty-two persons who were his creditors. Respondents 1 to 4 are only a few of them and it will be seen from that Schedule that the debt due to respondent 1 was only Rs. 300 while that due to respondent 4 was only Rs. 400 and it is not clear how much was due to respondent 2 or to respondent 3.

6. It appears from the evidence of P.W. 3 that some time before the presentation of the application for the adjudication of Zackria as insolvent, there was a panchayat in the shop of one Appajiah & Sons, in the course of which the creditors came to an understanding that the insolvent should continue to conduct his business in his shop and pay his creditors, the amounts due to them, in easy instalments. He also gives evidence that respondents 1 to 4 and another Abdul

Wahab were appointed trustees as they are described, for the supervision of the business which the insolvent was so permitted to conduct. His evidence is that sometime after the arrangement was so reached, some of the creditors of the insolvent discovered that a transaction had been surreptitiously entered into between respondents 1 to 4 on the one hand and the insolvent on the other, as a result of which the entire stock-in-trade and assets of Zackria had been sold to respondents 1 to 4.

Having felt disconsolate at the transfer of those assets in that clandestine manner, they arranged for the presentation of an application for getting Zackria adjudged insolvent, and this they appear to have done after they made an unsuccessful attempt through the good offices of P.W. 4 Kota Kamakshiah Setty for getting the transfer cancelled by consent of parties.

It is therefore clear from this evidence and also from the other evidence to which I shall refer in the course of my judgment, that Zackria on the date he transferred all his assets to respondents 1 to 4, was undoubtedly in insolvent circumstances and that his creditors were putting pressure upon him for the payment of their debts.

Although there is some variation between the story told by P.W. 3 Narayana Setty and what is stated in Ex. III, the notice issued by the insolvent himself on January 29, 1942, to which I have made reference above, as to who were the trustees appointed, there does not appear to be any doubt that some understanding was reached between the insolvent and his creditors as a result of which the insolvent had to continue to conduct his business and pay off his creditors from out of the profits he would make from it.

It is not difficult to hold that respondents 1 to 4 were fully aware of not only of the insolvent circumstances of Zackria but also of the above arrangement entered into between him and his creditor. While that was so, the question is whether it was proper for respondents 1 to 4 to have purchased from the insolvent soon after the arrangements reached in that way all his stock-in-trade and assets and as to what would be the proper inference to be drawn if they did enter into that transaction in that way.

The answer to that question would depend upon whether respondents 1 to 4 paid any money for what they purchased from the insolvent and if so, whether they entered into the transaction of sale in good faith.

7. On the question as to whether respondents 1 to 4 paid any consideration at all to the insolvent, it must be pointed out at the outset that it is one of the most curious features of this case that the document evidencing the sale by the insolvent in favour of respondents 1 to 4 is not produced before the Court nor is the document recording the sale by respondents 1 to 4 in favour of respondent 5 produced either.

When P.W. 1 who is no other than respondent 5 was, by what I consider a most

unusual procedure quite often discountenanced, examined by the Official Receiver as his own witness, it was elicited in his cross-examination that there was only one document evidencing both these sales and that that piece of paper on which the sale transaction had been recorded, was handed over to the advocate who appeared for respondents 1 to 4 in this case, that learned advocate who was conducting the cross-examination of P.W. 1 promptly denied that he had received that piece of paper and P.W-1 in another part of his cross-examination admitted that when the Official Receiver made the application (I. A. 2) to the Court below he was in possession of that piece of paper.

Whatever might be the truth of the story told by P.W. 1 about his having handed over the document of sale to the hands of the advocate for respondents 1 to 4, what is material for the purposes of this case is that the sale chit is not forthcoming and therefore it is impossible for the Court to know what that sale chit recited, how much consideration it mentioned and how it was paid.

To my mind, the story of respondents 1 to 5 that on the very document executed by the insolvent in their favour recording the transfer to them, a further endorsement was made by respondents 1 to 4 for the purpose of transferring those very assets to respondent 5 and that they retained in their possession no evidence in respect of the payment of Rs. 3,800 which they claim to have paid to the insolvent on that date, is utterly incredible.

While respondents 1, 2 and 4 who have examined themselves as R. Ws. 1, 4 and 2 respectively have given evidence that they paid the sum of Rs. 3,800 towards the consideration for the first sale to the hands of the insolvent on January 5, 1942, the evidence of respondent 3 who has been examined as R.W. 5 is materially different from the evidence given by the other respondents.

According to him no money was paid to the hands of the insolvent on the date of the sale by him but that it was only on the next day, after respondents 1 to 4 had in their turn made a sale to respondent 5, that a sum of Rs. 3,800 was so paid to the insolvent out of a sum of Rs. 5,500 paid by respondent 5 to respondents 1 to 4.

To my mind it appears that the circumstance that although the insolvent purports to have sold all his assets for Rs. 3,800 on January 5, 1942, the fact that respondents 1 to 4 were able on the very next day to sell the same assets to respondent 5 for a sum of Rs. 5,500 making a profit of Rs. 1,700 overnight, is itself a circumstance which has been rightly regarded by the Court below as one that should excite the suspicion of the Court.

But the more important question is whether it is true that when the insolvent sold his properties to respondents 1 to 4, the transferees made any payment at all to the insolvent. It appears to me that the answer to that question should be against respondents 1 to 4.

8. As I have mentioned above, they have not retained in their possession any

evidence of any such payment. R.W. 1 who is the first respondent in the case admits that there is no entry in his accounts to show that he paid any part of the sum of Rs. 3,800 to the insolvent. The second respondent R.W. 4 and the third respondent R.W. 5 also give similar evidence and admit that their accounts also do not evidence any payment of any portion of the purchase money for that transfer.

What is even more awkward for the respondents is that the fourth respondent Subramanya Setty when he gave evidence as R.W. 2 made a very curious admission that the consideration for one of the sales -- although it is not clear to which sale he was making reference -- was really Rs. 5,500 but was nominally mentioned as Rs. 3,800. If the transaction was free from all taint and was quite above board, it is difficult to understand why an artificial figure should have been mentioned in the sale chit as the consideration.

The insolvent himself is dead and therefore the only evidence available to prove the payment of the consideration for the first sale is the evidence of the respondents who have given evidence as stated above. It is admitted that no other creditor of the insolvent was present at the time of the transaction. Having regard to the unsatisfactory character of the evidence given by the respondents, it would not be proper for us to differ from the finding of the learned District Judge that the sale by the insolvent to respondents 1 to 4 was not for valuable consideration.

That this would be a proper inference would be clear from the evidence of P.W. 4 Kota Kamakshiah Setty which appears to my mind to be quite trust-worthy evidence that on his intercession in connection with the controversy relating to the disputed sales during which he advised respondents 1 to 4 to return the pronotes and the cash they had taken from P.W. 1, respondent 4 returned the pronote executed in his favour.

9. The next question is whether the purchase made by respondents 1 to 4 was one made in good faith. If as I have mentioned above, it was within the knowledge of respondents 1 to 4 that Zackria was in insolvent circumstances at the time of the sale and there was pressure from his creditors for the payment of the moneys due to them and respondents 1 to 4 purchased from him his entire stock-in-trade and assets without making any substantial contemporaneous payment and without undertaking to make any such payment in future in order that he might be able to continue his business so that he would be in a position to pay off his creditors, it would be very difficult to hold that the transfer was one entered into in good faith. The law on this question is contained in the well-known rule of law enunciated in the judgment of Lord Hobhouse in *Khoo Kwat Siew v. Wool Talk Hwat*. ILR 19 Cal 223 (PC) (A), at p. 231, which is as follows:--

"The well-known rule of law is that if a trader assigns all his property, except on some substantial contemporaneous payment, or some substantial undertaking to make payment in future, that is an act of bankruptcy and is void against the

creditors and the assignee simply because nothing is left with which to carry on his business, whereas if he receives substantial assistance, something is left to carry on the business."

So tested, the conclusion is irresistible that the transfer to respondents 1 to 4 was one which was not entered into in good faith,

10. Sri Rangraj, learned counsel for the appellants, has argued before us that the learned District Judge was in error in recording a finding that the transaction was not for valuable consideration, or was one not made in good faith for the reason that according to him, the evidence in the case establishes that out of the consideration paid to the insolvent by respondents 1 to 4 a large number of creditors were paid, as a result of a composition between the creditors and the insolvent, their debts pro rata, calculated at the rate of 0-4-6 in the rupee. I must state at once that in the first place, it would not be open to respondents 1 to 4 to urge a contention of this type by way of an answer to an application u/s 53 of the Act as they had not opposed the application for the adjudication of Zackria as insolvent on that ground. The explanation offered by Sri Rangraj that his clients were not aware of the insolvency proceedings and had no opportunity to put forward any such contention before the insolvency Court is thoroughly unconvincing.

The simple answer to that argument is that the insolvency application having been duly advertised and published, it would not lie in the mouth of respondents 1 to 4 to plead that they had no notice of it. Assuming for & moment that it would shall be open to them to urge that contention on its merits, it appears to me that the evidence in this case relating to this composition is neither satisfactory nor adequate. The witnesses who have spoken to that composition have given evidence that the dividends paid to the creditors were paid at four annas in the rupee whereas in the statement of objections presented by respondents 1 to 5 they stated that it was at 4-1/2 annas in the rupee.

Secondly, no evidence has been adduced that all the creditors of Zackria were paid in that way. The only witnesses who have spoken about it are P. W. 1 and R, W. 4. P. W. 1, as I have mentioned above, is none other than the 5th respondent himself and he admitted in the course of his cross-examination that he received towards his debt the amount mentioned in Ex. 1(a), a note-book containing an entry to that effect and which represented a fraction of what was due to him.

I am not disposed to attach any importance to that admission made by him remembering that he was vitally interested in supporting the impugned alienations. R.W. 4 is another witness who gives evidence that he was paid a sum of Rs. 3-1-6 which represented the amount due to him towards his debt of Rs. 10-14-6 calculated at 0-4-6 in the rupee.

He did not produce his accounts to support his evidence and having regard to the extremely small sum of money said to have been paid to him, it is difficult to believe that he received that sum of money as a result of a composition to which

all the creditors of Zackria were parties. The other creditors who are said to have received their dividends in that manner are not examined by the respondents and the receipts said to have been executed by them are therefore not proved.

Respondents 1 to 4 who according to them received towards their debts similar sums, admitted in cross-examination that their accounts do not contain any entries to evidence such receipts. I am, therefore, of opinion that the proper inference to be drawn from the above circumstances is that the story of respondents 1 to 4 that any such composition as pleaded by them between the insolvent and all his creditors took place, is not established.

The result of the discussion of the evidence to which I have referred above is that the transfer by the insolvent to respondents 1 to 4 must be held to fail within the ambit of Section 53 of the Insolvency Act and was therefore, rightly annulled by the Court below.

11. Although respondent 5 has not appealed from the order annulling the transfer in his favour, the next question is whether the alienation by respondents 1 to 4 in favour of respondent 5 was also similarly liable to be annulled and whether the Insolvency Court had jurisdiction to so annul it. Sri Rangraj has argued before us with great emphasis that Section 53 of the Insolvency Act can have no application to a transfer of that description.

In my opinion, it is difficult to accept that contention. The case for the Official Receiver was that the alienation in favour of respondents 1 to 4 and that in favour of respondent 5, both formed part and parcel of one fraudulent scheme and that they had been entered into for the purpose and with the intention of defeating the other creditors of the insolvent. It may be that respondent 5 paid a sum of Rs. 5,500 towards the transfer in his favour upon which it is very difficult to express any definite opinion.

But there can be no doubt that when respondent 5 purchased the entire assets and stock-in-trade of the insolvent from respondents 1 to 4, he was aware of all the facts relating to the financial difficulties of the insolvent and also of his insolvent circumstances and it is difficult to escape the conclusion that he must also have been aware of the fraudulent character of the alienation by the insolvent in favour of the respondents 1 to 4 and must have been a party to a scheme to defraud the other creditors of the insolvent.

There is some evidence that in respect of the promissory notes executed by respondent 5 in favour of respondents 1 to 4 towards a portion of the consideration for the transfer to him, suits were filed against him for the recovery of the amounts due under them and that he had to discharge those debts. It may be that the evidence establishes the existence of some consideration for the transfer to respondent 5 although it is difficult to find how much it really was.

But that does not to any extent establish that the transaction between

respondents 1 to 4 and respondent 5 was one entered into in good faith. For the reasons for which I have held that respondents 1 to 4 were not transferees in good faith, it has to be held that respondent 5 was not a transferee in good faith either.

12. If therefore it can be said that Section 53 of the Act controls a transfer like the one in favour of respondent 5, his transfer would similarly have to be annulled. I have no doubt in my mind that Sri Rangraj, learned counsel for the appellants, is not right when he contends that Section 53 of the Insolvency Act does not apply to a transfer by a transferee from the insolvent.

If the transfer to a transferee from the insolvent is declared invalid and not binding on the Official Receiver and if the later transfer by the transferee from the insolvent is held to form only a link in the chain of a fraudulent scheme to defraud the other creditors of the insolvent, the Insolvency Court has, to my mind, clearly the power to annul the second transfer as not [finding on the Official Receiver not only u/s 53 of the Act, but also, if necessary, by the exercise of its powers u/s 4 of the Act. (Vide: *Isamoddin Ajmuddin Vs. Ajmuddin Shamsoddin*, ; *Kandaswamy Goundan v. Rangaswamy Goundan* AIR 1038 Mad 370 (C) ; and *Amir Ahmad v. Syed Hasan* ILR 57 All 900 : (AIR 1035 All 671) (D).) In my opinion the transfer in favour of respondent 5 was also rightly annulled.

13. The only question that survives for determination is as to what really is the scope and effect of the order made by the learned District Judge. All that he stated was that he allowed I. A. 2, the application filed by the Official Receiver holding that the sales were not made in good faith and for valuable consideration. But it does not appear to have been noticed by him that one of the prayers made by the Official Receiver in I. A. 2 was that the respondents should be directed to hand over to the Official Receiver the properties sold to the respondents or their value.

Although the prayer in the form in which it was made by the Official Receiver was somewhat clumsily worded, there is no doubt that what he wanted the Court to direct was that the respondents should render an account to the Court of all their dealings with the insolvent under the impugned sales in respect of what they had purchased under them so that the Court might eventually pass appropriate orders after taking into account all the circumstances in the case and after making necessary adjustments which the equities of the case demanded.

What exactly is the relief granted by the District Judge is not clearly formulated. Anyhow, having regard to the manner in which he made his order, it must be taken that there is a direction made by the District Judge as prayed for in I. A. 2. It appears to me that that direction is not an appropriate one.

Respondents 1 to 4 if they took possession of the assets of the insolvent and handed them over to respondent 5 and respondent 5 has in his turn dealt with those assets and stock-in-trade in the course of his business, the proper direction

to be given in those circumstances would be a direction like the one which appears to have been given by the learned Judges of the High Court of Calcutta in *The Official Assignee of Bengal Vs. Yokohama Specie Bank Ltd.*, .

The proper direction to be given therefore is that the respondents and each of them shall deliver to the Official Receiver all the assets and stock-in-trade purchased by them and that they should also render an account to the Official Receiver and to the Court of all their dealings with the insolvent in respect of the impugned transfers and also of all their dealings in respect of the assets, stock-in-trade which they purchased and also in respect of the proceeds of those assets and stock-in-trade.

Any amounts found due by respondents after such an accounting shall be paid by them to the Official Receiver for distribution by him among the creditors of the insolvent. In my opinion, we should substitute a direction on the above terms for the direction which must be deemed to have been given by the District Judge. This is the only modification that we need make in the order of the District Judge.

14. The order annulling the transfers in favour of respondents 1 to 4 and in favour of respondent 5 is therefore confirmed and this appeal, except for the modification made above, is dismissed with costs. SADASIVAYYA, J.:

15. My learned brother has discussed at length the facts and the evidence in the case. In most of the cases in which parties come forward before the Court u/s 53 of the Insolvency Act attacking alienations by the debtor on the ground that the transferee is not a transferee in good faith, it will be very difficult to prove by direct evidence the lack of good faith on the part of the transferee. It is essentially from the circumstances surrounding the transaction that the Court has to gather as to whether the transferee is a transferee in good faith.

In the present case the evidence, through which we have been taken by the learned counsel in the case, shows that the transferees-are not transferees in good faith. Respondents 1 to 4 are some of the creditors of the debtor who has effected the alienation of all the properties in his shop in their favour. The fifth respondent is a transferee of the same properties from respondents 1 to 4.

The evidence in the case shows that at the time when the transfer was effected by the debtor in favour of respondents 1 to 4, the alienor was under the pressure of debts which he was unable to discharge. All the respondents were, at that time, aware of the plight in which the debtor had been placed. Though respondents 1 to 4 have made an attempt to show that the purchase by them was something in the nature of a public auction, they have not succeeded in establishing the same.

That the debtor must have been in very bad circumstances at that time can be gathered from the fact that in less than five months thereafter he was adjudged an insolvent. That the respondents 1 to 4 could not have paid the full value of the goods which they purchased from the debtor, is also clear from the

circumstance that almost overnight they were able to sell these goods for a profit of Rs. 1,700 to the 5th respondent. Having regard to these and the other circumstances in the case the conclusion reached by the learned District Judge that these transferees were not transferees in good faith, must be supported.

16. Having reached this conclusion, it has to be seen as to whether the Court has not the power to ensure that the properties which were the subject-matter of these alienations would be made available to the Receiver for being dealt with in accordance with law. It was contended by the learned counsel for respondents 1 to 4 that the Court, while acting u/s 53 of the Insolvency Act is not competent to make an order in respect of the properties which have been subsequently sold away in favour of a second or a subsequent transferee by the original alienee from the debtor.

I am unable to accept the proposition that in a case where the Court is satisfied that the original alienation and the subsequent alienations are all in favour of transferees who are not transferees in good faith, the Court is powerless to make such appropriate orders as may be necessary in the interests of justice.

When once the alienations are found to be not sustainable, the benefits which had accrued to the alienees by such transfers should be made available to the Receiver for being dealt with in accordance with the provisions of the law of Insolvency. Section 4 of the Insolvency Act gives very wide powers to the Court.

I agree with my learned brother that this is a fit and proper case in which the Court should not hesitate to have recourse to the powers that are available u/s 4 of the Insolvency Act. It is only just and proper that those alienees who have purchased the goods from the debtor should render accounts into Court. I agree with the judgment which has been just now delivered by my learned brother.

17. Appeal dismissed.