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Court : Karnataka

Decided On : Nov-19-1957

Reported in : AIR1958Kant126; AIR1958Mys126; ILR1957KAR333;
(1958)36MysLJ57

Judge : K.S. Hegde, J.

Acts : [Provincial Insolvency Act, 1920](#) - Sections 45, 46, 47, 48, 49 and 50;
[Negotiable Instruments Act, 1881](#) - Sections 9

Appeal No. : Civil Revn. Petn. No. (M) 13 of 1956

Appellant : Paschal Nazereth

Respondent : Denis Lobo

Advocate for Def. : G.K. Govinda Bhat, Adv.

Advocate for Pet/Ap. : P. Nazereth, Adv.

Judgement :

ORDER

1. The petitioner is the plaintiff in Small Cause Suit No. 2 of 1955 on the file of the Court of the District Munsiff, Mangalore, South Kanara. His suit has been dismissed and he has come up in revision to this Court. This revision petition raises some interesting questions of law. In order to properly appreciate the

questions of law that arise for consideration it is necessary to state the facts of the case briefly.

2. In the Town of Mangalore a Chit Fund was being run which was known as the New Kerala Daily Auction Chit Fund which will be hereinafter called the 'Fund'. The defendant was a member of the said 'Fund'. He executed a demand promissory note on 28-1-1952 in favour of the 'Fund' for a sum of Rs. 500/- security for the due payment of the future instalments of the chit purchased by him. The practice of this 'Fund' seems to have been that whenever a member was a successful bidder in any of the chit auctions, he will have to execute a pro-note as security for the payment of future instalments of the chits purchased by him.

3. The proprietor of the said 'Fund' seems to have disappeared and the transactions of the 'Fund' came to a sudden end sometime in 1953. On the application of the creditors, insolvency proceedings started and the Official Receiver took charge of the assets of the 'Fund'. The Official Receiver assigned the suit pronote in favour of the plaintiff as per endorsement dated 13-8-1954 and the plaintiff filed the present suit on the basis of the said demand promissory note.

Prior to the filing of the suit, the plaintiff had issued a registered notice demanding a sum of Rs. 440/- as balance due under the pronote. The defendant in his reply notice stated that only 11 instalments are due from him under the chit in question. Hence his liability under the chit was only Rs. 55/- He claimed certain bonus deductions. He also Claimed a set off of Rs. 185/- in respect of the 37 instalments paid by him to the same 'Fund' under a separate chit.

The plaintiff confined his suit only to a sum of Rs. 66-9-3 i. e., Rs. 55/- as admitted arrears of 11 instalments of Rs. 5/- each, Rs. 8-9-3 as interest thereon from 28-1-1952 at 6 per cent, per annum upto date and Rs. 3/- as the cost of demand. The learned District Munsiff dismissed the suit holding that the defendant was entitled for set off of Rs. 185 due to him under Section 46 of the Provincial Insolvency Act as mutual dealings between the insolvent and the creditor. The learned counsel for the petitioner challenges the correctness of the decision of the trial Court.

4. The first contention raised by him is that Section 46 of the Provincial Insolvency Act has no application to the facts of the case. According to him the said section relates only to insolvency proceedings and its benefit cannot be availed of in proceedings other than insolvency proceedings. It is further contended that the suit is based on a negotiable instrument; the plaintiff is a holder in due course without notice of the defendant's claim, hence the plea of set off is not open to the defendant.

5. The argument of the petitioner proceeds thus:

Section 46 of the Provincial Insolvency Act is in part III of the Act which relates to the administration of the property of the insolvent. The provisions of Part III are intended to provide for the proof of debts etc. According to him on analysis of the sections grouped under that head it would be clear that the benefit of Section 46 could be availed of only in an Insolvency proceeding.

Section 45 relates to the proof of certain debts which had not become due. Section 46 provides for the adjustments of mutual dealings; Section 47 sets out the rights of the secured creditors; Section 48 provides for the payment of interest under certain circumstances; Section 49 speaks of the mode of proof of debts; Section 50 provides for the disallowance and reduction of certain entries in the schedule.

So much for the scheme of the Act. He further contends that Section 46 itself very specifically lays down that the creditor can take the benefit of that section when he proves or claims to prove his debt.

6. But on the other hand the learned Advocate for the respondent contends that Section 46 embodies a rule of equity. Its application is not confined to Insolvency Proceedings only. He relies on the history of the section in support of his argument. This section is more or less copied from Section 39 of the English Bankruptcy Act, 1869. Section 39 of the English Bankruptcy Act is as follows:

'Where there have been mutual credits, mutual debts or other mutual dealings, between the bankrupt and any other person proving or claiming to prove a debt under his bankruptcy an account shall be taken of what is due from the one party

to the other in respect of such mutual dealings, and the sum due from the one party shall be set off against any sum due from the other party and the balance of such account, and no more, shall be claimed or paid on either side respectively

Section 46 of the Provincial Insolvency Act reads as follows :

'Where there have been mutual dealings between an insolvent and a creditor proving or claiming to prove a debt under this Act, an account shall be taken of what is due from the one party to the other in respect of such mutual dealings, and the sum due from the one party shall be set off against any sum due from the other party, and the balance of the account, and no more, shall be claimed or paid on either side respectively.'

From a perusal of these two sections it is clear that Section 46 of the Provincial Insolvency Act is more or less a copy of Section 39 of the English Bankruptcy Act. Mr. Govinda Bhat, the learned counsel for the respondent contends that the English courts have uniformly held that the benefit of Section 39 of the English Bankruptcy Act could be availed of not merely in the Bankruptcy Court but also in common law Courts and that there are no good reasons to depart from the practice of the British Courts.

Mr. Nazereth for the petitioner urges that the decision of the English Courts were not founded on the wording of the Section but on the basis of the practice prevailing in those Courts, and according to him no such practice is established in so far as Indian Courts are concerned. In *Peat V. Jones & Co.*, (1881) 8 QBD 147 (A), the learned Judges of the Court of Appeal held that the plea of mutual dealings under Section 39 of the Bankruptcy Act is also available in Ordinary Civil Courts. *Jessel M. R.* enunciates the position as follows:

'The statutes, however, contemplate the set off being allowed in the Bankruptcy court. This being so, if the debtor were sued in a common law court he could apply to the court of Bankruptcy for an injunction to restrain the assignee from suing him. Then the Courts of common Law, having regard to the equity of the statute, went a step further, and allowed the debtor to plead the set off in the Court of common

law it self without being under the necessity of applying for an injunction.

This practice has been recognised in a series of decisions. The legislature must be taken to have been aware of the effect of those decisions when it passed the Bankruptcy Act, 1869, and not to have intended to alter the law. We are therefore bound to hold that the defendant was entitled to have the benefit of the set off.'

The same was the opinion of Brett L. J. and Cotton L. J. The Indian Legislature when it enacted the Provincial Insolvency Act of 1920, more or less bodily lifted this section from the English Act and introduced it in the Indian Statute. The Legislature must have been familiar with the practice prevailing in the English Courts and the import of Section 39 of the English Act as interpreted by the English Courts.

Hence it is proper to presume that the Indian Legislature intended to give section 46 the same import. The rule embodied in Section 46 aforesaid is a rule of equity and there are no legitimate grounds to limit its benefits solely to actions in insolvency Courts. If that be not so it is bound to give rise to fraudulent practices with a view to evade the law.

In the case reported in *Official Assignee v. Ma Yait*, AIR 1931 Rang 25 (B), the learned Judges referred to the case of *Dickson v. Evans* reported in (1794) 3 RR 119 (C), wherein Lord Kenyon Ch. J. in the course of his judgment made the following observations:

'But it would be most unjust indeed if one person, who happens to be indebted to another at the time Of the bankruptcy of the latter, were permitted by any intrigue between himself and a third person so to change his own situation as to diminish or totally destroy the debt due to the bankrupt by an act ex post facto. In cases of this sort the question must be considered in the same manner as if it had arisen at the time of the bankruptcy, and cannot be varied by any change of situation of one of the parties.'

These observations are helpful in deciding the scope of Section 46. If we are to limit the benefit of Section 46 only to proceedings in the Insolvency Courts then it

would be easy for parties to prejudice the opposite side by acts ex post facto. No Indian decision on the subject has been brought to my notice. The American courts have taken the same view as that of the British Courts. I am reluctant to depart from the literal meaning of the words of the Section. But in the instant case I am convinced that I shall be carrying into effect the true intention of the legislature by following the English decisions.

7. Next contention urged before me is that the plaintiff in this case has sued on the basis of a negotiable instrument. He has taken the assignment for valuable consideration Without noticing any defect in the instrument. He is a holder in due course and hence his rights cannot be prejudiced. This contention has been countered by the learned Counsel for the respondent on two grounds: (1) the petitioner is not a holder in due course and (2) that the mutual dealings between the insolvent and the creditor respondent got themselves adjusted as on the date Of the insolvency. Hence there was no debt to be assigned by the Official Receiver.

8. It is clear from the facts of the case that the plaintiff even on the date of assignment knew that the said pro-note has been executed by the defendant as a security for the due payment of future instalments. He was aware that the pronote was supported by the consideration only to the extent of the arrears of payment. That was the reason as to why he claimed only Rs. 440/- in his registered notice.

In fact he filed the suit for a much lesser sum. So he knew that the negotiable instrument was not what it looked. He got the assignment from the Official Receiver. He is likely to have known the circumstances under which the insolvency proceedings had started. Hence it was his duty to make the necessary enquiries and find out the real state of affairs.

He was put on notice of the defect in the instrument. In order to become a holder in due course, the holder should have taken the assignment without having sufficient cause to believe that any defect existed in the title of the person from whom he got the assignment. It is contended for the respondent that the petitioner had sufficient information to put him on enquiry.

The learned counsel for the petitioner contends that his client's duty was to investigate only about the defect in so far as it related to the transaction on the basis of which the suit instrument had been executed, and he had no duty to enquire into all the dealings between the insolvent and his creditor. I am unable to accept this contention. As stated by Lord Blackburn in *Jones v. Gordon*, (1877) 2 AC 616 (D):

'that in order to make such a defence it is necessary to show that the person..... was affected with notice that there was something wrong about it when he took it. I do not think it is necessary that he should have notice of what the particular wrong was.'

9. In this case the plaintiff knew at the time he got the assignment that the insolvent was running the 'Fund' and the defendant was having dealings with the insolvent. He also knew the circumstances under which the said pronote was executed. He was taking the assignment from the Official Receiver and it is proper to presume that he was acquainted with the circumstances relating to the insolvency.

He had a duty to find out the nature of the defect in the suit instrument. Hence it is not possible to come to the conclusion that the plaintiff is a holder in due course.

10. In this connection the learned Counsel for the petitioner has brought to my notice a case reported in *Ramamurthi v. Nukayya*, 1941 Mad WN 775: (AIR 1042 Mad 30) CE). Undoubtedly the facts of this case are somewhat similar to the facts of the present case. But in the Madras case the learned Judge was not required to interpret the effect of Section 46 of the Provincial Insolvency Act. The decision rested on other considerations and hence is of no assistance.

11. It is unnecessary for me to decide finally the last contention raised by the learned counsel for the respondent that the mutual dealings between the insolvent and the respondent got themselves adjusted as on the date of insolvency. It is true that the relevant date for working out the mutual dealings is the date of insolvency. But it is difficult to accept his contention that there was any adjustment on the date of the insolvency. There is no support for this contention either from the wording of

the section or from any decided case. In the result this revision petition fails and is dismissed with costs.

12. Revision petition dismissed.

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