1932 *Present:* **Garvin S.P.J. and Drieberg J.**

HONG KONG AND SHANGHAI BANK *et al. v.*
KRISHNAPILLAI

78—D. C. (Inty.) Ratnapura, 60.

Pledge—Shares in Joint Stock Company pledged with bank—Security for overdraft—Insolvency of pledgor—Bank's right to dispose of shares—Order of Court to sell shares—Preferential right of bank over proceeds of sale—English law.

A bank with whom scrip relating to shares in a Joint Stock Company is deposited by way of security for an overdraft, with written authority to dispose of the shares by sale or transfer, has no right to dispose of them without the intervention of Court, where the assignee in insolvency of the pledgor objects to such a course. The bank is, however, entitled to obtain an order from Court that, upon the sale of the shares by the assignee, it should be given preference in those proceeds for so much of its claim as is charged upon and secured by such shares.

The right of a pledgee to sell his security without recourse to a Court of law is peculiar to the English law of pledge, and the Roman-Dutch law in the matter of rights of mortgage and pledge does not give place to the English law, when the mortgagee or pledgee is a bank.

The Court ordered that the bank will be further entitled, in the event of its purchasing the property hypothecated, to credit to the extent of such claim provided the purchase is made for a price not less than the current market price of the shares.

APPEAL from an order of the District Judge of Ratnapura.

This was an application by the assignee in insolvency for an order to sell certain shares alleged to be the property of the insolvent. The application was opposed by the appellant-banks so far as it related to certain shares, the scrip of which had been deposited with them as security for overdrafts with written authority from the insolvent to dispose of or transfer them. The learned District Judge ordered that the shares should be sold, the proceeds brought into Court, and that the secured creditors should bring hypothecary actions against the assignee to establish their preferential claims to the proceeds.

B. F. de Silva, for appellants.—Pledgee of shares is entitled to sell. The English law should govern banking transactions (Ordinance No. 5 of 1852). The pledge or mortgagee can sell (*Stubbs v. Slater*[1]; *Colonial Bank v. Whinney* [2]). Bankers have special lien under the law merchant (*Grant on Banking, p. 288; Rock v. Garrissen*[3]), in realizing lien on securities (*Grant, p. 296;* The Odessa case [4]). Where share certificates are deposited as security for a debt the creditor may obtain an order for foreclosure (*Grant on Banking, p. 403*). Even under Roman-Dutch law, banks are in special position, as, for example, in the case of shares held by a bank (*Wille on Mortgage, p. 183; Morice Roman-Dutch Law, p. 62*).

Counsel cited *Sankayar v. Mohamadu* [5]; *Raman Chetty v. Sarkuman* [6]; *Brand & Co. v. Assignee of Goerge Wall & Co.*[7]

Keuneman, for assignee, respondent.

January 22, 1932. DRIEBERG J.—

This is an appeal from an order directing the sale by the assignee of certain shares alleged to be the property of the insolvent. The application for sale was made by the assignee and was opposed by the appellants so far as it related to the shares in their possession.

The history of the case, so far as it relates to the matter before us, and the respective positions of the several appellants as gathered from the record and the affidavits filed by them are as follows:—

The insolvent, when he filed his declaration of insolvency on January 31, 1930, was indebted to the first appellant, the Hong Kong and Shanghai Bank, on his overdrawn current account in a sum of Rs. 13,883.90. The bank held as security 1,000 shares in Broughams, Ltd., and 650 shares in the Boscombe Tea Estates, Ltd. On October 5, 1924, the insolvent gave the bank a writing authorizing it as his attorney to dispose of the shares by sale or by transfer to a nominee of the bank if it should be found necessary to do so. The bank still holds these shares and has not dealt with them under this power. These facts appear in the affidavit

[1] *(1910) 1 Ch. 632.*
[2] *(1886) 11 App. Cases 426.*
[3] *(1860) 3 Q. L. J. Ch. 39.*
[4] *(1916) 1 A. C. 158.*
[5] *8 Times 98.*
[6] *15 N. L. R. 337.*
[7] *5 S. C. C. 86.*

of the agent of the bank dated September 19, 1930, and the application to Court of October 18, 1930, was that the Court should make order allowing the shares to be sold by a firm of brokers, Forbes & Walker, at such price as the bank should approve, that the necessary transfer be executed by the assignee, the first respondent to this appeal, that the bank be allowed credit at the sale and further, to be allowed to prove for the balance of its claim, if any, as an unsecured creditor. The writing of October 5, 1924, was not before the District Court when the order appealed from was made. It was produced before us at the argument.

The second appellant, the Eastern Bank, came into the proceedings on February 13, 1931, and on that day moved jointly with the Hong Kong and Shanghai Bank that the order made on February 7 allowing the insolvent to leave the Island be revoked " Until such time as it has been decided (1) whether the banks can realize their security, if not (2) whether they must file hypothecary actions and (3) until the question of Mr. Harrison's interest, if any, in the Uva shares now with the Eastern Bank has been decided ". The Eastern Bank had not then made any statement as to the nature or extent of its claim or what its position was regarding the enforcement of it. Mr. Harrison's claim regarding these shares is set out in his affidavit proving his claim. He there said that the insolvent purchased 500 shares in the Uva Rubber Co., Ltd., for and on his behalf, that these were made out in the name of the insolvent who held them in trust for him and paid him the dividends.

An affidavit of October 28, 1931, by the agent of the Eastern Bank was submitted to us at the hearing of this appeal. He there states that the insolvent was indebted to the bank on an overdrawn current account in a sum of Rs. 3,918.96, that as security the insolvent deposited on February 27, 1929, certificates in his name for 500 shares in the Uva Rubber Co. of Ceylon, Ltd. with a blank form of transfer signed by the insolvent; on November 8, 1928, the insolvent by a letter of lien authorized the bank to complete the transfer of all property of the insolvent in its possession and in the event of non-payment of his overdraft to sell the property and pay itself. On February 3, 1930, the bank completed the transfer of the 500 shares in the Uva Rubber Co. and received from the company amended scrip in the name of the bank's nominee. The letter of lien is not before us.

The affidavit of the agent of the Eastern Bank refers to 100 shares in the Stratheden Tea Co. deposited on June 28, 1929, with the bank as security. These were in the name of Mrs. Kennedy and there was a blank form of transfer signed by her. On July 6, 1929, Mrs. Kennedy wrote to the bank that these shares were not to be sold but were to be retained by the bank until such time as they were redeemed by Mrs. Kennedy or the insolvent. The Eastern Bank has not dealt with these shares.

The trial Judge refused the joint motion of the Hong Kong and Shanghai and the Eastern Bank and there was an appeal against the order by the Hong Kong and Shanghai Bank. The appeal was heard on February 27, 1931. The certificate meeting had previously been fixed for March 7 and the insolvent was ordered to appear at it; this Court ordered that

at that meeting the District Court should hear and determine all applications in respect of sale of shares in which notice had been given. The application referred to was one of November 10, 1930, by the assignee for leave of Court to sell through Messrs. Forbes & Walker the shares belonging to the insolvent, among them the Uva Co. shares and the Stratheden Co. shares, and that the assignee be authorized to execute the necessary transfers.

On March 7, after hearing argument only on behalf of the appellants and certain creditors, the Court ordered that the shares should be sold, the proceeds brought into Court, and that the secured creditors should bring hypothecary actions against the assignee to establish their preferential claims to the proceeds. The appeal is from this order.

The three appellants are not in the same position and it is necessary to state their claims as they were presented in the District Court.

The Hong Kong and Shanghai Bank claimed a mortgage of these shares effected by delivery, a blank transfer signed by the insolvent and a writing authorizing it to dispose of the shares. This writing however was not before the Court.

The third appellants, Bartleet & Co., had disclosed their position in their affidavit proving an unsecured debt and in their motion of January 15, 1931. They claimed to hold as security for a debt of Rs. 72,000 6,110 shares in the Etambawala Rubber Co. and 4,500 shares in the Boscombe Tea Estates Co., for which they held blank transfer forms signed by the insolvent. They do not say that they hold such an authority as the Hong Kong and Shanghai Bank has to complete the transfer if necessary in the name of the insolvent.

The claims of the Hong Kong & Shanghai Bank and Bartleet & Co. are alike. They ask for an order of Court allowing the sale of the shares by Messrs. Forbes & Walker and that they be allowed credit for their claims at the sale. The Hong Kong and Shanghai Bank asks that the sale be at a price approved by it and Bartleet & Co. ask that they be allowed to buy at a price not less than the current market rate and in the alternative that a date be fixed for inquiry and ascertaining the market value of the shares to enable them to take over the shares at that price.

The Eastern Bank had not stated its position in the District Court except what can be gathered from its motion of February 13, 1931, which is that it held as security certain Uva Co. shares to which Harrison made a claim. The amount of its claim was not stated.

From the agent's affidavit of October 28, 1931, we now know that the bank under the authority it claims had disposed of the shares and that they are now held by a nominee of the bank; I infer from the statement that the bank has received amended scrip from the company that this transfer was registered. The agent says in paragraph 9 of his affidavit that though he believes he had the right to sell these shares without reference to court doubts have arisen as to the validity of the transfer of February 3, 1930. I understand this to refer to registration being effected after adjudication and without the assent of the assignee. He says that for this reason " the Bank joined in the appeal of the Hong

Kong and Shanghai Banking Corporation and Messrs. Bartleet & Co. in order to establish its rights in the matter ". What is meant by this is not clear. If the Eastern Bank desired an adjudication on the question—for I presume this is the question that concerns it and I can only gather this from the affidavit—whether the registration of the transfer after the adjudication and without the assent of the assignee is valid, it should have been done in a proper proceeding. It may be inferred from its joining in this appeal and from what was urged on its behalf in the District Court that the Eastern Bank is prepared to assume the same position as the appellants, that is to say, that it still holds these Uva shares as security; but it is not clear that this is its position.

It was urged especially on behalf of the appellant-banks that they had the right to sell any shares pledged with them without reference to the Court. It was contended that as Ordinance No. 22 of 1866 introduced into the Colony the law of England in all questions relating to banks and banking they have the same rights in the matter of realizing these securities as they would under the law of England. But the right of a pledgee to sell his security without recourse to a Court of law is peculiar to the English law of pledge and the common law of the land in the matter of rights of mortgage and pledge does not give place to the English law when the mortgagee or pledgee is a bank.

It was contended by Mr. de Silva that the banks have the right of selling the shares independently of the Court as the writing authorizing them to dispose of the shares was an express agreement for *parate execution* which is recognized by the Courts of South Africa as valid in the case of a mortgage or pledge to a bank. He referred us to page 176 and the following pages of *Wille on Mortgage and Pledge in South Africa* and *Morice's English and Roman-Dutch Law, p. 62.* This question does not arise for decision for if the banks thought that they had this right they should have disposed of the shares without the intervention of the Court. It is suggested that they could not do so as the authority of the assignee would be needed for registration of the transfers. If they have the power to sell, they presumably also have the power to compel the assignee to do what is necessary to give effect to the sale. But what counsel urged on behalf of the appellants at the argument in the District Court was that the assignee should be authorized to sell the shares, pay the appellants, and bring the balance into Court, and that the appellants be allowed credit for the amount of their claims. It is sufficient to say that according to the Roman-Dutch law such an agreement is one which the law will not recognize, except in the case of movables of small value and in the case of shares held by a bank, in which case, the right to do so depends on custom, by which the law has been abrogated. It has not been proved that such a custom exists here and that it has been recognized in our Courts.

Voet XX., 5, 6 (Berwick's translation) says: " Whatever mode of sale of pledges has been introduced by municipal law or inveterate usage is to be observed, and this cannot be receded from, or the order changed, by private agreements between debtors and creditors. Whence, if it has been agreed by pact that it should be permissible to a creditor to sell the

pledge by private authority, nevertheless it cannot be rightly sold except by public auction under decree of the Judge, when either the debtor refuses to allow the sale to be made privately under the pact, or it concerns other hypothecary creditors that it should not be sold in this manner: for they will not lose their rights by a private sale, and the purchase will either be null, or the purchaser will take the thing subject to its encumbrances."

The law on this point in South Africa is well summarized by *Wille* on page 183: " It is submitted here that the weight of authority is against upholding an agreement for *parate execution*, except in the case of securities of small value. That the true rule is that such an agreement, if made at any time prior to the mortgagor's default, is valueless and of no effect in itself. On the default of the mortgagor, if either he or any third parties having a *jus in re* in the property, for example, a later mortgagee, raises any objection the earlier mortgagee cannot enforce the agreement except with the assistance of the Court. The only exceptions to this rule are in the case of movables of small value and, probably, in the case of shares held by a bank, for such an institution will doubtless be able to prove that by custom it is entitled to exercise the power of sale agreed upon. Apart from these exceptions, if the mortgagee wishes to avail himself of the power contained in the agreement he should apply to the Court, which will, as a rule, grant him a rule *nisi* calling on the mortgagor and third parties to show cause why the mortgagee should not be allowed to sell the property, and, in the absence of cause being shown, the rule will be made absolute (*Case of Good Hope Building Society's Liquidator v. Rodel*[1]; *Ex parte Indwe Mutual Building Society*[2]).

We were told that in the District Court of Colombo where such claims often arise, the shares so held by banks are sold with the consent of and by arrangement with the assignee; to such a course there can be no objection and it would be in compliance with the law, the assignee, representing the debtor and holders of subsequent mortgages, if any, and other creditors. In this case the assignee denies, or at any rate wishes to put the appellants to proof that they have a right of preference, for he does not consent to their getting credit for the amount of their claims.

The position of the banks therefore is that they are creditors claiming to have a mortgage of movable property. They do not seek to sell the property without the intervention of the Court and they cannot do so where the assignee, who represents their debtors, objects. It follows therefore that they must prove their claims and their right to preference. The position of Bartleet & Co. must be regarded as the same as that of the banks.

The only further question for consideration is whether such rights can be enforced in these proceedings or whether this should be done in separate hypothecary actions.

The Insolvency Ordinance, which is based on the early English Act does not allow for the fundamental difference between the English and the Roman-Dutch law of mortgage. But the practice regarding the rights of preference of creditors who hold a mortgage of immovable

[1] *(1899) 9 C. P. R. 198.* [2] *(1906) 16 C. T. R. 1137.*

property is well settled. In *Mathiah v. Markar Tamby*,[1] it was held that a mortgage creditor had three courses open to him when the mortgagor is adjudicated insolvent; he should make a formal demand of the assignee in order to allow him the opportunity of redeeming the mortgage under section 76 of the Ordinance and disposing of the property for the benefit of the creditors; if the assignee does not elect to redeem the property the mortgage creditor can prove his claim under the mortgage bond and when the property is sold he can draw the whole proceeds or so much as is sufficient to satisfy his claim, or he might bring an action on the bond against the mortgagor as debtor and against the assignee as the party in whom the property has vested under section 71 of the Ordinance, obtain a hypothecary decree and have the property sold. It does not appear from the report whether the mortgage was of movable or immovable property, but Burnside C.J. deals with this course as applicable both to a mortgage and a pledge, and Lawrie J. deals with cases where the mortgaged property has vested in the assignee under sections 70 and 71 of the Ordinance; section 70 deals with personal effects and section 71 with lands and interests in lands. The grounds on which this judgment is based are common to mortgages of movable and immovable property.

In the case of a mortgage of land there are many reasons why a creditor might prefer a sale under a hypothecary decree, for example, there may be encumbrances subsequent to the mortgage which would not affect the purchaser if the property was sold under a hypothecary decree on the first mortgage and this may lead to a better price being realized. This is what the mortgage creditor can do if he so desires, but there is nothing to prevent him from following the less formal but more expeditious course of proving his claim and asking that the property be sold in the insolvency proceedings. The mortgage creditor who adopts this course does not lose his right of preference (*In re Ingleby*[2] and *Perera v. Joseph*[3]). The latter was a case in which the mortgage was over both land and movable property. It appears from the report that the property was sold by the assignee with the consent of the primary mortgagee and the secondary mortgagee. The rulings in *Mathiah v Markar Tamby* (*supra*) and *In re Ingleby* (*supra*) were followed, and it was held that the secondary mortgagee by coming into the insolvency proceedings did not lose his right to preference.

The order appealed from is wrong so far as it directs the assignee to sell the shares and the appellants to bring hypothecary actions to establish their preferential right to the proceeds. If the appellants have hypothecary rights over these shares they are entitled to have them sold in the same way as under a hypothecary decree, and they are entitled to preference over the proceeds of the sale and to credit for the amount of their claims if they find it necessary to purchase it themselves. If they are secured creditors this cannot be denied them, but they must prove their claims and that they have a valid hypothecation.

[1] *(1884) 6 S. C. C. 83.*

[2] *(1885) 7 S. C. C. 39.*

[3] *(1912) 15 N. L. R. 327.*

Mr. Keuneman said that the assignee personally was prepared to admit the claims of the appellants but as there was opposition by some of the creditors he desired that there should be an order of the Court directing the sale and recognizing the preferential claim of the appellants. The creditors represented by Mr. Pinto and Mr. Wijetilleke apparently do not concede that the appellants have a right of preference, but for what reason they say so does not appear and the Court did not inquire.

Mr. Pinto appeared among others for T. G. Harrison who claimed the Uva Rubber Co. shares over which the Eastern Bank claims a mortgage. On March 7 the matter was discussed in a general way and the Judge refused the request made by counsel for the appellants that the assignee should be authorized to sell the shares and pay the appellants their claims on the ground that he had no power to order in these proceedings that the proceeds of sale should be paid to any particular creditor. As I have shown there is ample authority for such a course if the appellants satisfy the Court that their claims are secured by a valid mortgage. This they have not done. The Eastern Bank in particular did not put its case before the Court at all.

The order appealed from must be set aside. Any appellant who is able to satisfy the Court that shares in his possession belonging to the insolvent are validly held by him as security for the amount of his claim or any portion of it will be entitled to proceed as has been indicated and obtain an order that upon the sale of the shares by the assignee he should be given preference in the proceeds for so much of his claim as is charged upon and secured by such shares; further, he will be entitled in the event of his purchasing the property hypothecated to credit for the extent of such claim provided he purchases the same for a price not less than the current market price of such shares. The sale should be by public auction by a sharebroker approved by the Court. The appellants will be entitled to prove for the balance of their claims, if any, as unsecured creditors.

We express no opinion on the merits of the particular claims and in particular in regard to that of the Eastern Bank which as has been pointed out was not formulated in the District Court. We would merely add for the guidance of the Court that before a sale is ordered it should satisfy itself first, that the shares are the property of the insolvent or held for him and next, that they are validly pledged and hypothecated for the amount of the respective claims or any part thereof.

There will be no order as to the costs of this appeal or of the proceedings of March 7 in the Court below.

GARVIN S.P.J.—I agree.

Appeal allowed.