1940 *Present :* **Howard C.J. and Keuneman J.**

THE CHARTERED BANK *v.* RODRIGO.

68—D. C. Colombo, 8,482.

Insolvency—Fraudulent preference—Deposit of scrip by insolvent with Bank—Authority to sell—Claim by assignee to proceeds of sale—Right of Bank.

Where the plaintiff Bank, with whom scrip relating to shares in a company was deposited by the first defendant by way of security for an overdraft with written authority to dispose of the shares, sold the shares and appropriated the proceeds in reduction of the overdraft,—

Held, that there was no fraudulent preference of the Bank, and that the Bank was entitled to the proceeds of the sale as against the second defendant, the assignee of the insolvent estate of the first defendant who claimed them for the benefit of the insolvent estate.

APPEAL from a judgment of the District Judge of Colombo.

N. Nadarajah (with him *E. B. Wikremanayake*), for second defendant, appellant.

H. V. Perera, K.C. (with him *N. K. Choksy* and *Miss Metha*); for the plaintiff, respondent.

[1] *(1928) 21 B. W. C. C. 32.*

[2] *(1929) 22 B. W. C. C. 451.*

March 6, 1940. HOWARD C.J.—

This is an appeal by the second defendant who is the assignee of the insolvent estate of the first defendant from a judgment of the District Judge of Colombo, dated December 12, 1938, in favour of the plaintiff for the sum of Rs. 108,631.98 with costs. The facts so far as material to this appeal are as follows:—By a bond or obligation No. 747 dated December 20, 1934, the first defendant gave to the plaintiff a floating security to secure the payment of sums then owing and of future overdrafts over certain immovable property set out in the schedule. As further and additional security to the plaintiff for the payment of moneys owing under bond No. 747 the first defendant deposited with the plaintiff by way of pledge and hypothecation the share certificates specified in the second schedule to the plaint together with relative transfers executed by the first defendant. In the District Court the appellant did not contest the whole of the plaintiff's claim. He maintained (1) that the deposit of the share certificates and transfers specified in schedule "A" to the amended answer amounted in law to a fraudulent preference of the plaintiff by the first defendant and (2) that as assignee in insolvency he was entitled to a declaration as against the plaintiff that a sum of Rs. 6,709.09 specified in schedule "B" to the amended answer should be paid to him for the benefit of all the creditors of the insolvent estate of the first defendant. It was also claimed by the appellant that the goods and property specified in schedule "B" of the amended answer were surrendered by the first defendant to the plaintiff in circumstances amounting to a fraudulent preference of the plaintiff by the first defendant. The learned District Judge has answered all the contentions of the appellant in favour of the plaintiff. So far as the question of fraudulent preference is concerned it appears from the evidence of the first defendant that from 1934 onwards his financial condition was getting progressively worse. On December 1, 1937, he states that his liabilities far exceeded his assets, that his condition was hopeless and that the plaintiff Bank was financing him. It was in these circumstances that he visited the plaintiff Bank, saw the Manager and handed over the share certificates, his only unencumbered assets apart from his existing stocks of tea. The deposit of these certificates was made by the first defendant with a two-fold purpose. Firstly because the Bank had informed him that his overdraft had increased beyond the authorised limit and it required further security. And secondly—and on the evidence it is transparent that this was the main purpose—to secure a further advance of Rs. 2,500. On handing over the scrip the first defendant was accommodated by the plaintiff Bank by the cashing of his cheque for Rs. 2,500.

The facts with regard to the goods and property specified in schedule "B" of the amended answer are as follows:—The arrangements with regard to the disposal of the proceeds derived from the sale of the Tripoli tea are contained in the documents 10, 10A, 10B, 10C. From these documents it would appear that on December 14, 1937, the first defendant informed the plaintiff Bank that he had instructed his agent in Tripoli and his associates in Paris and the Banco di Roma, Tripoli, to hold the

balance proceeds of sale arising from a consignment of tea sent to Tripoli at the disposal of the plaintiff Bank. The latter was also authorized by the first defendant to collect these proceeds which, so it would appear from 10A, 10B, and 10c, were then lying in the Banco di Roma, Tripoli. the balance amounting to Rs. 2,476.84 from the sale of the Tripoli tea was eventually received by the plaintiff Bank on April 9, 1938, and went in reduction of the first defendant's overdraft.

The amount of Rs. 17.60 referred to in schedule "B" of the amended answer represented a dividend from the Forest Hill Tea Company shares transferred to the plaintiff Bank on December 1, 1937. This dividend was paid on April 19, 1938, and went in reduction of the first defendant's overdraft.

The transaction with regard to 43,467 lb. of tea was arranged about January 17, 1938, with a certain Mr. Henry of the plaintiff Bank who on that day visited the first defendant's store. In consequence of an agreement reached on that day the first defendant sent R. Gordon & Company 43,467 lb. of tea. The Manager of the plaintiff Bank states that the tea was handed over to R. Gordon & Company to be held by them for the Bank because the latter was afraid it might disappear if it remained in the first defendant's hands. The instructions given by the first defendant to R. Gordon & Compnay are contained in P 11 and are to the effect that they should receive the tea into their godown and hold it for the account of and at the disposal of the plaintiff Bank. This tea was eventually sold and credited to the account of the first defendant on April 22, 1938.

The Manager of the Bank explains the handing over of the 2,525 tea coupons as being in response to a request made to the first defendant in January, 1938, by the Bank who wanted to get as much security as possible into their hands. These coupons were sold and the proceeds credited to the first defendant's account on April 5, 1938.

The learned District Judge has held that neither in the case of the shares specified in schedule "A" nor in the case of the goods mentioned in schedule "B" of the amended answer do the circumstances in which they became vested in the plaintiff Bank amount to a fraudulent preference. In order to constitute a fraudulent preference four conditions must be satisfied. (1) The debtor at the date of the transaction must be unable to pay from his own money his debts as they fall due, (2) the transaction must be in favour of a creditor or of some person in trust for a creditor, (3) the debtor must have acted with the view of giving such creditor or a surety or guarantor for the debt to such creditor a preference over his other creditors and (4) the debtor must be adjudged bankrupt on a bankruptcy petition within three months after the date of the transaction sought to be impeached. In this case conditions (1), (2), and (4) have been satisfied. The question that arises for decision is whether the learned Judge was right in holding that these various transactions were not made with a view to giving the plaintiff Bank a preference over other creditors. The English cases lay down the principle that the whole question turns on the intention of the trader in disposing of his goods to a particular creditor. Turning to the present case the intention of the first defendant

in handing the shares over to the plaintiff Bank was not to give a preference to the latter but to obtain more credit. So far as the tea coupons and stocks of tea handed over to R. Gordon & Company and the proceeds of the sale of the Tripoli tea are concerned, the placing of them at the disposal of the plaintiff Bank was at the instance of the latter and in view of the fact that the overdraft had exceeded the authorised limit. If the first defendant had not taken this step, there was a danger of his credit being stopped by the plaintiff Bank with grave danger to his business. In these circumstances the second defendant did not prove that the intention of the first defendant was to give a preference to the plaintiff. The learned District Judge was, therefore, correct in holding that there was no fraudulent preference.

There remains for consideration the question as to whether the goods specified in schedule "B" of the amended answer vested in the second defendant by virtue of section 70 of the Insolvency Ordinance (Chapter 82) and, therefore, the plaintiff Bank received the proceeds of the sale of such goods including the dividend from the Forest Hill Tea Company as agents of the second defendant. Counsel for the plaintiff Bank has claimed that the title to (*a*) the tea coupons, (*b*) the tea, (c) the Tripoli debt passed to the Bank on the dates when the various arrangements were made for placing this property at the Bank's disposal. Alternatively, then, goods were given by the first defendant to the Bank by way of security, that is, as a pledge. In my opinion the evidence does not prove that full title in the goods passed to the plaintiff Bank. It is, however, established that they were allocated by the first defendant to the Bank by way of security against the overdraft. In this connection it is material to consider the form in which the various transactions took place. The tea coupons were handed over to the plaintiff Bank, while the tea itself was delivered to R. Gordon & Company on behalf of the Bank. In these circumstances under section 18 (*a*) of the Registration of Documents Ordinance the transaction was complete without being in writing and without registration. The Tripoli debt was a "chose in action" and hence exempted from the provisions of the Registration of Documents Ordinance by virtue of section 17 (2). The right to take the dividend from the Forest Hill Tea Company passed to the plaintiff Bank when the shares themselves vested in the latter. The form in which the various deals with regard to the property specified in the amended answer were transacted was therefore in accordance with the law.

The remaining question now requiring elucidation is whether those transactions conferred on the plaintiff Bank the right to sell this property on the insolvency of the first defendant. The matter is discussed in *Wille on Mortgage* at pages 175-183. Generally speaking, it may be said that the pledgee on default may not sell the secured property unless the pledgor consents. In *Hongkong & Shanghai Bank v. Krishnapillai*[1] it was held that 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

[1] *33 N. L. R. 249.*

in insolvency objects to such a course. In the present case the plaintiff Bank had the written authority of the first defendant to dispose of the goods. Their sale has been effected by the plaintiff and is not impugned by the second defendant who merely claims that the proceeds should be applied for the benefit of the insolvent's estate. In these circumstances I think the plaintiff Bank is entitled to show that it had a preferred claim to apply those proceeds in reduction of the first defendant's overdraft.

For the reasons I have given, the appeal is dismissed with costs and the judgment of the District Court affirmed.

KEUNEMAN J.—I agree.

Appeal dismissed.