1924

Present : Bertram C.J. and Ennis J.

SOOSAIPILLAI *v.* FERNANDO

307—D. C. Colombo, 4,133.

Insolvency—Fraudulent preference—Fraudulent alienation—Prescription—Concealed fraud—Action for accounting by assignee of partner—Must plaintiff show that there had been profits to ask for an accounting?

W and the defendant entered into a partnership as from January 1, 1914, for three years by P 1. On December 11, 1914, W assigned his interest in the partnership to the defendant by deed P 2. By an informal document P 4A of the same day, the defendant agreed to give W one-third of the profits "that may be earned by. . . . the business carried on under deed P 1." W filed his petition of insolvency in October, 1915, and the assignee brought this action on February 21, 1922, against the defendant, praying that the defendant should be ordered to furnish an account of the profits of the business from December 11, 1914, to December 31, 1921, and subsequently added a further prayer that the deed of assignment P 2 and the agreement P 4A be set aside, and the plaintiff declared entitled to half of the entire business in terms of the deed of partnership P 1.

The District Judge held that P 2 was not a fraudulent alienation; that the agreement P 4A was binding on the defendant; that it terminated on December 31, 1916, when the partnership deed ceased to have any effect; that the claim up to February 20, 1916, was prescribed; and as the existence of any profits had not been proved, he dismissed the action.

Held, that the creditors were entitled to the profits between February 21, 1916, and December 31, 1916, when the partnership expired under P 1; and that plaintiff was entitled under P 4A to an account of the profits of the business carried on under P 1.

An assignment by an insolvent may be impeached on several grounds. It may be impeached as a fraudulent preference under section 58 of the Insolvency Ordinance, or as a voluntary settlement under section 51. It may also be impeached if it can be shown that apart from these sections it is in effect a fraudulent conveyance executed within twelve months prior to the filing of the petition. If it was of an earlier date, the only remedy of the creditors is by a Paulian action.

THE facts are set out in the judgment.

Elliott, K.C. (with him *H. V. Perera* and *C. W. Perera*), for plaintiff, appellant.

H. J. C. Perera, K.C. (with him *Samarawickreme, R. L. Pereira*, and *D. P. Fernando*), for defendant.

February 4, 1924. BERTRAM C.J.—

This is an appeal raising issues both of fact and law, but is in the main a case turning upon facts, and the difficulty that we have in the case is that it seems impossible to accept either of the conflicting stories told by the two principal witnesses. There is a further difficulty in that another witness, whose evidence would have been decisive on all the aspects of the case, has not been called at all. We are left to piece together the truth of the stories of witnesses whom we cannot believe.

The case originates out of the insolvency of Peter de Silva Wijeyeratne, who was declared an insolvent in October, 1915. The orignator of the case is the insolvent himself, and the costs of the action are being defrayed by his wife.

The insolvent's story is as follows: He and the defendant were partners, and had for some time been associated in a landing and shipping business. A few months after they had entered into a formal partnership, his circumstances became embarrassed. At the time he was approached by his partner, the defendant, and pressed to put more money into the business. He declared his inability to do so, and was thereupon pressed to assign his share to his partner. They consulted a well-known proctor, Mr. J. A. Perera, and the insolvent alleges that upon this gentleman's advice, with a view to preventing the boats and other assets of the business being seized by the creditors of Wijeyeratne, they made an arrangement under which Wijeyeratne was to assign his share of the partnership to the defendant, and so to all appearances terminate his connection with the business, but that at the same time what is described as a "secret document" should be executed, reserving to Wijeyeratne an interest in the business to the extent of one-third of the profits.

The deed of assignment was prepared by Mr. J. A. Perera, and was to be executed not at his office or at the house of the partners, but, for some reason unexplained, at the house of a relation of Wijeyeratne. Mr. A. J. Perera did not attend to attest the document, but handed it to a junior proctor of good position. Mr. W. J. C. Fernando, to get it attested for him. This circumstance is not explained, but, of course, the explanation may be that Mr. Perera had other business to attend to. When the parties met, Wijeyeratne refused to sign the deed of assignment, unless at the same time a document was drawn up and executed securing him the one-third of the profits which had been promised him. Mr. W. J. C. Fernando had received no instructions on this point from Mr. Perera, but on the defendant's admitting that there was such an undertaking, he drew up, in a very informal way, a document to give effect to the undertaking, and this was signed by the defendant.

This is the first part of the story as told by the insolvent. We have now to follow the second part of the story which is concerned with

1924.

BERTRAM C. J.

Soosaipillai v. Fernando

the fortune of the so-called "secret document." Later on in the evening of the same day Mr. J. A. Perera called upon the bankrupt and learnt, apparently with some surprise and embarrassment, of the execution of this document. He asked to see it, and had some difficulty in doing so, owing to the objection of the insolvent's wife. He saw it, however, and then, according to the insolvent, persuaded the latter to let him take it away with a view to getting a more formal document executed. Such a more formal document never was executed. Very soon after this a dispute arose between defendant and Wijeyeratne with regard to three promissory notes, amounting to Rs. 25,000, which, under the arrangement between the partners at the time of the partnership deed, were to have been discharged by Wijeyeratne, but had not been discharged in accordance with the arrangement. There seems every reason to believe that the defendant's complaint was just, and I understand the District Judge so to think, but on this point there has been no issue. Mr. J. A. Perera appears to have been asked by the defendant not to surrender the "secret document" until this question was settled. A letter requesting the return of the document P 4 was drafted by Mr. W. J. C. Fernando for Wijeyeratne, who at this time was insolvent. Various evidence adduced shows that the document was at this time still in the possession of Mr. J. A. Perera. Afterwards it was found in the possession of the defendant. This in its main lines is the story of the insolvent.

The story of the defendant is entirely irreconcilable with this. According to him the impending insolvency of Wijeyeratne had nothing to do with the assignment. Wijeyeratne left the business as he had no time to manage it. Nothing was said about his financial affairs. The consideration for the transfer was calculated simply upon the basis of the financial position of the business. There was no stipulation at the time for any secret collateral agreement, but after the arrangement had been made and a few days before the execution of the assignment, Wijeyeratne came to him and pressed him to promise him, notwithstanding the assignment, a share of the profits. The defendant yielded to his importunities, and promised this share as "something extra." He declared that he regarded it as a "santosum." When the parties assembled to execute the assignment, Wijeyeratne reminded him of the promise, and said that life was uncertain and that he would like to have the promise in writing. Defendant admitted that he had made the promise, and Mr. Fernando accordingly reduced it into writing, and the defendant signed it. He did not attach any great importance to the promise, because up to that time on the statement of accounts which the partners had made, there had been no profits, and he regarded the promise as having relation simply to the duration of the partnership which had a little more than two years to run, and it might well be that no profits would

be earned. At first defendant said that he knew nothing about the instructions for drawing the deed of assignment, and that Mr. Perera was not his proctor for the purpose, but he subsequently explained that in this he was mistaken, and that he paid Mr. Perera's charges. This is the defendant's story upon the first part of the case. His story as to the second part, namely, that relating to the "secret document," is equally irreconcilable with the story of the insolvent. As I have said the document ultimately got into defendant's hands. According to the evidence called by the insolvent, it must have reached him through Mr. J. A. Perera. According to the evidence of the defendant, sworn first in answer to an interrogatory, the document was handed to him by the insolvant himself upon a settlement of the dispute about the Rs. 25,000, and it was surrendered to him as being discharged by that agreement.

We now come to the findings of the learned District Judge. With regard to the first part of the story, the learned Judge, except on one point—a point of great importance—decisively rejects the story of the defendant. He says : "The conclusion that P 4A was signed with the object of concealing that fact from Mr. Wijeyeratne's creditors is irresistible." The learned Judge thus apparently means that the document was to be kept secret. He proceeds "If not, there was no reason why Wijeyeratne should not have assigned over one-sixth instead of half by the deed of assignment, No. 448. The seizure of the boats by Wijeyeratne's creditors would have been disastrous to defendant." The learned Judge thus appears to think that the arrangement contained in the deed of assignment was not the real arrangement between the parties, but only a disguise ; that according to the real terms between them, Wijeyeratne was to retain an interest in the business to the extent of one-third of the profits, and that this interest was to be concealed from the creditors. If this is really the meaning of the District Judge, I think he ought to have given judgment for the plaintiff, but he adds a qualification of some importance, namely, that it is possible that Wijeyeratne, knowing defendant's position, "instead on P 4A being signed as a condition precedent to his executing the transfer, and defendant had no choice, but to agree to save the business from being at the mercy of Wijeyeratne's creditors." He here seems to imply that this document was executed after the preparation, but before the execution of the assignment. With regard to the second part of the case, the learned Judge rejects the story of the defendant with equal decisiveness. He accepts the evidence of Mr. W. J. C. Fernando, and it seems to me that he could not do otherwise than accept it. He disbelieves the story that the document was surrendered to the defendant as a result of a compromise, and he holds that it is entitled to any effect which may belong to it.

1924.

BERTRAM C. J.

Soosaipillai v. Fernando

As I have said the learned Judge's finding would seem to imply a verdict in favour of the plaintiff. The reason why the learned Judge does not give such a verdict is that he thinks that the defendant had no desire to defraud Wijeyeratne's creditors, but only looked to make his position safe. The learned Judge appears to have overlooked the fact that his language implies that one of the terms of the agreement was that Wijeyeratne should retain an interest in the business, and that this interest was to be given him in such a form as to conceal it from the creditors. The real question in the case is whether this was the intention of the parties. It may be convenient at this point to state the law. Under our antiquated Insolvency Ordinance, which is a discredit to the Statute Book and the occasion of constant scandals, we are in effect administering the English principles as embodied in the Bankruptcy Act of 1849. An assignment by an insolvent may be impeached on several grounds. It may be impeached as a fraudulent preference under section 58, and here the law applicable is the English law for the time being, or as a voluntary settlement under section 51, but it may also be impeached if it can be shown that apart from these sections it is in effect a fraudulent conveyance. This is nowhere expressly declared by the Ordinance, but it follows from the fact that by section 7 any fraudulent conveyance by an insolvent is an act of insolvency. All acts of insolvency being offences against the bankruptcy law are themselves void, but according to the principles which have been followed in England, such a conveyance cannot be declared void on this ground unless the act of insolvency is an " available " act of insolvency (that is to say, unless, under our own law, it was committed within twelve months prior to the filing of the petition). If it was committed at an earlier date, the only remedy of the creditors is by a paulian action (which in our law corresponds to an action under the Statute of Elizabeth) with all the difficulties which that action involves. See on this point *Williams' Bankruptcy Practice, 9th ed., p. 18,* and *Mercer v. Peterson* [1] *Shrubsole v. Sussam* [2], *Allen v. Bonnett* [3], *Jones v. Harber* [4], and *Exparte Games* [5].

To return to the facts. As I have said the real question is whether it was a secret term of the assignment of the insolvent's interest that he should retain a right to one-third of the profits which should be put in such a form that it could be kept concealed from the creditors. If this was the real intention, then, under whatever pressure that intention was formed, its object was to defraud the creditors . . . . Nevertheless, on a careful consideration of the evidence, I am not satisfied that there was any secret term in the arrangement for the assignment, nor am I satisfied that it was

[1] *L. R. 2 Ex. 304.*
[2] *16 C. B. N. S. 452.*
[3] *L. R. 5 Ch. 577.*
[4] *L. R. 6 Q. B. 77.*
[5] *12 Ch. D. 314.*

the intention of the defendant that the document P 4A should be kept as a secret document.

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I have very little doubt that the defendant gave the document because he wished at all costs to avoid the seizure of his boats by Wijeyeratne's creditors, but I am not satisfied that there was any fraudulent arrangement between him and Wijeyeratne that the document should be kept secret.

This brings us to the question of the effect of the document and, in particular, as to the point from which its operation begins and the point at which its operation ends. The document was executed on December 11, 1914, and the action was instituted on February 21, 1922. It is agreed that in the absence of concealed fraud any claim must be prescribed to profits which were earned earlier than February 21, 1916. Concealed fraud, in my opinion, is not made out. The right to profits then must start from February 21, 1916, but to what period does it extent? This is a question of the interpretation of the document, and it is by no means an easy question. The promise is to give one-third share of the profits that may be earned by the Colombo Landing and Shipping Agency in the business carried on under deed No. 740 dated January 30, 1914, attested by Mr. J. A. Perera, Notary Public. Does the reference to the partnership deed in this document import a limitation to the period during which the deed or partnership was to run? Or, do the terms of the document give to the insolvent an unrestricted right to a share of the profits as long as the actual business, from which he was retiring, was carried on? We cannot, unfortunately, ask ourselves what the parties must have intended, because we must judge by the terms of the document which they executed. It is highly probable that neither of them fully thought out what their intention was, and it is singular that Mr. Fernando, who drew it up for them, did not ask them further to define their intention. Certainly it would be a singular promise to make on the part of the defendant that for a wholly indefinite period as long as he carried on the business from which his partner was retiring, the latter would receive a one-third of the profits, and not be responsible for any of the losses. On the whole, I have come to the opinion that the reference to the partnership deed imports a reference to the duration of the partnership under that deed. On this view of the case the creditors are entitled to any profits between February 21, 1916, and December 31, 1916, when the partnership would have expired.

On the question of this right to the profits, the learned Judge has given certain rulings which I am unable to follow. He has ruled that inasmuch as the insolvent is not an actual partner, the assignee cannot claim an account of the profits unless he shows

1924.

BERTRAM C.J.

Soosaipillai v. Fernando

that profits were in fact earned. He further rules that inasmuch as the plaintiff obtained discovery of the defendant's books for certain purposes not defined in the record, he had an opportunity of ascertaining whether profits were in fact earned, and that the onus of proving profits consequently lay upon him, and as he has not proved the existence of profits, and as there are certain circumstances which suggest that there were no profits, his claim to an account must be dismissed. I am entirely unable to follow this reasoning. The assignee, as representing the insolvent, is entitled under this document to any profits earned by the business for a specified period. In my opinion he is entitled under that document to an account of the profits of the business carried on under the partnership deed from February 21, 1916, to December 31, 1916, and the case should be sent back to the learned District Judge to enable that account to be rendered, and to enable the plaintiff, if he so desires, to surcharge and falsify, and judgment should be ultimately entered up on the footing of that account.

The plaintiff has asked for any directions as to the manner in which the account should be taken, and, in particular, as to whether in taking the account the allowance of 12 per cent. of interest on capital, which under the practice in force between the partners had been made before the assignment, should be continued. I think that it would be convenient that we should give a direction on this point. I do not myself see how it can be left out of account that as between the partners it had been customary to allow 12 per cent. for interest on capital before estimating profits. I think that in taking the account, the learned Judge should follow the same practice.

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ENNIS J.—His Lordship stated the facts, and after discussing other issues continued:—

With regard to the claim for an account on the learned Judge's finding, the plaintiff was entitled to an account from February 21, 1916, to December 31, 1916, and I am of opinion that the learned Judge was wrong in holding that the plaintiff had to prove that there was a profit. It is true that there was an issue as to the amount of the profits, if any, and there is general evidence that there were no profits. The Judge has answered the issue holding that there were no profits, and that the business resulted in a loss up to the end of 1921. The defendant does not appear to have been in any way reluctant to let the assignee see his books. He appears to have allowed, at the request of the plaintiff, an accountant to see the books, but we are told by the counsel for the appellant that the books for 1914 only were seen. The petition of appeal

says that the issue was regarded at the trial as a preliminary one which could be gone into only when it was decided that the plaintiff was entitled to an account.

I would uphold the learned Judge's findings in all other respects, and, while setting aside the decree, direct, using the terms of the prayer in the plaint, the defendant to furnish an account of the profits of the business from February 21, 1916, to December 31, 1916. It is possible that no further proceedings will be necessary, as the assignee and the defendant may agree as to whether there were any profits, and if so, what.

As to costs I agree with the order proposed by my Lord the Chief Justice.

Set aside.