

Life Insurance Corporation Of India vs Devendrappa Bujjappa Kadabi And Others on 17 October, 1986

Equivalent citations: [1990]69COMPCAS404(KAR)

Author: M.N. Venkatachaliah

Bench: M.N. Venkatachaliah

JUDGMENT

K.A. Swami, J.

1. This plaintiff's appeal is preferred against the judgment and decree January 31, 1972, passed by the learned District Judge Dharwadi, in Civil Appeal No.290 of 1964 reversing the preliminary decree dated September 29, 1964, passed by the learned Civil Judge, Dharwad, in Special Suit No.4 of 1962. The trial court passed a preliminary decree for recovery of a sum of Rs.18,591 together with interest and costs. The lower appellate court has set aside the decree passed by the trial court and dismissed the suit as brought by the plaintiff corporation.

2. The appeal is referred to a Division Bench having regard to the importance of the question of law arising for consideration,

3. The appellant Life Insurance Corporation of India ("Corporation" for short), is the plaintiff in the suit. Respondents are the defendants. Respondent No. 1 died during the pendency of the appeal. His legal representatives are brought on record on record as respondents Nos.1 (a) to 1(e) The parties will hereinafter be referred to which reference to their array in the trial court.

4. The suit was brought by the Corporation as the successor-in- interest of the United Karnataka Insurance Co. Ltd. ("company", for short). Plaintiff's case is that the late defendant No.1, who was the father of defendants Nos.2 to 4 along with his major son, defendant No.2, executed a simple mortgage deed dated April 1, 1952 for a sum of Rs.30,000 in favour of the company, both as the "karta" of the joint family and also as the guardian of the minors defendants No.3 and 4 ; that all the assets and liabilities of the controlled business of the company statutorily stood transferred to and vested in the plaintiff corporation consequent upon the coming into force of the Life Insurance Corporation Act. 1956 (hereinafter referred to as "the Act"); that defendant No. 1 even after admitting the amount due under the suit mortgage failed to pay the same. It was alleged that defendant No.1 unjustly sought to repudiate his liability in his letter dated August 6, 1959 sent through his advocate, necessitating the institution of was instituted for recovery of the sum of Rs.18,591.59 said to be due under the simple mortgage dated May 1, 1952, with future interest till

payment and costs of the suit and in default payment of the sum, an order for sale of the mortgaged properties for recovery of the aforesaid amount with interest till realisation, and for a personal decree in the event of insufficiency of the security. The alleged securities were : (1) the storyed building with open site and backyard bearing G P No.679, situated at Akkipet, Kalghatgi, Taluk Kalghatgi, District Dharwad ; (2) the rice mill bearing G P No.273 (new No.109), situated in Bhagwan Galli at Kalghatgi with the open space ; (3) Life Insurance Policy No.6966 with the company dated December 31, 1951 for Rs.10,000 the yearly premium of which was Rs.948.12 and five yearly premiums were paid and the policy was paid-up for Rs.3,846 only the date of maturity being December 31, 1964.

5. The defendants contested the suit on several grounds contending inter alia, that the plaintiff-corporation has no locus standi to institute the suit; that the benefit of the mortgage in question had not vested in the plaintiff corporation because it did not form part of the controlled business of the company ; that on March 1, 1952, the company's registration to carry on life insurance business was cancelled under the Insurance Act, 1938 ; therefore, the company could not have carried on the business of lending money ; that the transaction itself was void and inoperative ; that the civil court had no jurisdiction to entertain and decide the suit ; that when the defendants entered into the transaction, the company had exercised fraud upon the defendants ; that the entire amount of consideration of Rs.30,000 had not been paid ; that a sum of Rs.12,000 which was retained by the company as interest-free deposit could not be held to constitute good and valid consideration and that the defendants has paid back Rs.18,000 received by way of consideration with interest, fully discharging their obligation. It was further contended that the alleged purchase of shares of the value of Rs.12,000 was not out of their own volition and free will and was not binding on the defendants.

6. There was a counter-statement filed by the plaintiff corporation with the permission of the court as per exhibit 23 ; and the defendants also filed a rejoinder as per exhibit 30. It is not necessary to refer to the same.

7. On the pleadings, the trial court framed as many as 19 issues. The trial court negated the contentions of the defendants and decreed the suit as aforesaid. In the appeal preferred by the defendants, the learned District Judge has reversed the decree and dismissed the suit. In the appeal before the learned District Judge, only issues Nos.1,3,4,5,6,10,11,12 and 15 were pressed.

8. The learned District Judge, inter alia, held that the mortgage transaction did not form part of the controlled business of the company and consequently, the right of action in regard thereto did not vest in the plaintiff corporation under section 7 of the Act; that the consideration of Rs.30,000 mentioned in the mortgages deed (exhibit 75) in so far it included the sum of Rs.12,000 retained by the company as interest free deposit to be used subsequently for allotment of shares in favour of defendants Nos.1 and 2 failed. In regard to the sum of Rs.12,000 originally taken as interest-free deposit and later transferred to the shares account, the learned District Judge held that the adjustment of the deposit for allotment of shares in favour of defendant No 1 and his two brothers was tainted and that it was the duty of the company to have disclosed the fact of cancellation of the licence and the notice issued in that connection by the Controller, before bringing pressure on the

defendants to purchase shares on incurring the debt from the company. It was also held that the company was in a position to dominate and to influence the defendants in respect of the consideration of the mortgage to the extent of Rs.12,000 and as such, it stood vitiated ; therefore the defendants were entitled to avoid the transaction in question to that extent. Accordingly, the learned District Judge allowed the appeal set aside the preliminary decree passed by the trial court and dismissed the appellant's suit.

before us, the defendants sought for amendment of the written statement. By the order dated June 8, 1984, we have allowed the application I A III filed by the defendants seeking amendment to the written statement. As a result thereof, the following plea has been permitted to be raised :

"17A. The mortgaged transaction between the plaintiff and defendant No.1 and others is illegal and void and since it contravenes the provisions of sections 23 and 24 of the Contract Act read with section 54 of the Indian Companies Act, 1913, inasmuch as its object and consideration consisted of the prices of shares of the Karnataka United Insurance Co. the defendants on credit basis. The plaintiff cannot therefore enforce the said mortgage claim against these defendants who are the mortgagors."

9. The defendants have also filed a memo dated June 8, 1984 which reads thus :

"The advocate for the respondents submits as under :

The respondents submit that the payments made by them towards the mortgage amount would not be claimed back by way of refund or restitution from the plaintiff appellant corporation as a result of the plea allowed to be taken by this hon'ble court."

10. It is, no doubt, contended on behalf of the plaintiff corporation that the findings recorded by the learned District Judge are not correct and are opposed to law and the preliminary decree passed by the trial court is entitled to be restored. However, it is not disputed before us and it also a finding of fact recorded by the learned District Judge -that out of the consideration amount of Rs.30,000, a sum of Rs.12,000 was not paid in cash but was retained as interest-free deposit to be adjusted towards the share certificates were issued to the first defendant and his two brothers for the aforesaid sum of Rs.12,000.

11. It is also not disputed before us that the remaining sum if the consideration amount for Rs.18,000 and the interest thereon had been paid by the defendants before the suit and that the suit claim relates wholly to this disputed sum of Rs.12,000 and interest thereon .

12. In view of these undisputed facts, we do not consider it necessary to go into the other questions raised by the plaintiff- corporation bearing on the correctness of the findings recorded by the learned appellate judge except the following points :

(1) Whether the entire mortgage transaction in question between the company and the defendants was in contravention of the provision contained in section 54A of the Indian Companies Act, 1913 and as such it was null and void having regard to the provisions contained in section 23 and 24 of the Indian Contract Act?

(2) If not whether the mortgage transaction in question was void only to the extent of the consideration amount of Rs. 12,000?

(3) What order ?

13. Points Nos 1 and 2.- These two points can conveniently be considered together. The company was a limited company. It was not a subsidiary company of a public company. At the relevant point of time, the Indian Companies Act, 1913, was in force. Article 2 of the Articles of association (exhibit 156) of the company provided that none of the funds of the company shall be employed in the purchase of or lent on shares of the company Sub-section (2) of section 54A of the Indian Companies Act, 1913 was as follows :

"54A Restrictions on purchase by company or loans by company for purchase of its own shares.- (2) No company limited by shares other than a private company not being a subsidiary company of a public company shall give whether directly or indirectly and whether by means of a loan guarantee, the provision of security or otherwise any financial assistance for the purpose of or in connection with a purchase made or to be made by any person of any shares in the company :

Provided that nothing in this section shall be taken to prohibit where the lending of money is part of the ordinary business of a company, the lending of money by the company in the ordinary course of its business."

14. Thus, article 2 of the articles of association of the company and the aforesaid sub-section (2) of section 54A of the Indian Companies Act, 1913 prohibited the company from giving directly or indirectly any financial assistance by any means for the purpose of or in connection with a purchase made or to be made by any person of any shares in the company. It is not the case of the plaintiff-corporation that lending money was part of the ordinary business of the company in the ordinary course of its business. No doubt para 7 of the memorandum of association permitted the company to grant loans in general on mortgages or otherwise to approved company to grant loans in general on mortgages or otherwise to approved individuals..... as are carried on by purely loaning and investment companies and in particular without prejudice to the generality of the words contained in the said paragraph. But a mere provision in the memorandum of association to enable the company to do the business of lending money is not sufficient to attract the proviso to sub-section (2) of section 54A of the Indian Companies Act, 1913 unless it is shown that lending of money was part of the ordinary business of the company and the loan in question was made by the company in the ordinary course of its business. Therefore, in this case, there is no scope for applying the proviso to sub-section (2) of section 54A of the Indian Companies Act 1913 as that part of the loan was clearly intended to enable purchase of the shares of the lender-company itself.

15. In view of the prohibition to lend money or give any financial assistant in any manner by the company to purchase its shares the adjustment of Rs.12,000 being a part of the consideration of the suit mortgage by the company was clearly to increase its own share capital. The adjustment of the part of the consideration of the mortgage towards the share capital was forbidden by law. In the instant case, as already pointed out the entire consideration of the suit mortgage was not unlawful. It was only to the extent of Rs.12,000 out of the consideration of Rs.30,000 that the consideration was not lawful as it was forbidden by law, i.e section 54A (2) of the Indian Companies Act 1913. Therefore we are now required to see whether the entire suit mortgage was void or it was void only to the extent of Rs.12,000 which was adjusted towards share certificates of the company issued to defendant No.1 and his two brothers. The answer to this question depends upon the effect of section 24 of the Indian Contract Act on the mortgage in question.

16. Sections 23 and 24 of the Indian Contract Act, are as follows :

"23. The consideration or object of an agreement is lawful, unless-

it is forbidden by law; or is of such a nature that, if permitted, it would defeat the provisions of any law ; or is fraudulent ; or involves or implies injury to the persons or property of another or the court regards it as immoral or opposed to public policy In each of these cases the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful is void.

24. If any part of single consideration for one or more objects or any one of part of any one of several consideration for a single object is unlawful the agreement is void."

17. There is a distinction between an agreement and transfer of property Sections 23 and 24 of the Indian Contract Act, deal with consideration and object of an agreement. The provision of the Indian Contract Act do not, as a matter of course apply to transfer of property. Section 4 of the Transfer of Property Act provides thus :

"4. The chapters and sections of this Act which relate to contracts shall be taken as part of the Indian Contract Act, 1872.

And section 54, paragraphs, 2,3,59,107 and 123 shall be read as supplemental to the Indian Registration Act, 1908."

18. From the aforesaid provisions contained in section 4 of the Transfer of Property Act, it is clear that all the provisions of the Indian Contract Act are not made applicable to transfer of immovable properties. Therefore the provisions of the Indian Contract Act, as a whole cannot be read as part of the Transfer of Property Act. It is only such parts or provisions of the Transfer of Property Act which relates to contract alone that are to be read as part of the Indian Contract Act. Therefore, such of the provisions in the Transfer of Property Act, which relates to contracts shall have to be interpreted in the light of the provisions contained in the Indian Contract Act. Transfer of ownership of immovable property is effected by compliance with certain legal formalities, in accordance with the provisions

contained in the Transfer of Property and Registration Acts. Once there is a completed conveyance the matter does not remain in the domain of contract and the consequences of the distinction between an agreement which is normally executory and a completed conveyance are attracted. A mortgage is both a debt and a conveyance. Section 6(h) of the Transfer of Property Act, provides that :

"No transfer can be made (1) in so far it is opposed to the nature of the interest affected thereby, or (2) for an unlawful object or consideration within the meaning of section 23 of the Indian Contract Act, 1872 or (3) to a person legally disqualified to be a transferee."

19. Thus, section 6 of the Transfer of Property Act, which deals with the topic of "what may be transferred" provides that no transfer can be made for an unlawful object or consideration within the meaning of section 23 of the Indian Contract Act. The result is that the validity of a transfer of property must be tested in the light of section 23 of the Indian Contract Act. Apart from section 6(h) of the Transfer of Property Act, which makes only section 23 of the Indian Contract Act applicable to transfer of property there is no other provision in the Transfer of Property Act, which makes section 24 of the Indian Contract Act applicable to transfer of property.

20. In *Dip Narayan Singh v Nageshwar Prasad*, AIR 1930 All [FB] the question as to whether section 24 of the Indian Contract Act was applicable to transfer of immovable property was considered. The principal question that was considered by the Full Bench was as to the legal effect of including non-transferable occupancy land along with other properties which were transferable occupancy land along with other properties which were transferable in a registered mortgage deed it was held by Sulaiman J as follows (at page 2) :

"There can be no doubt that there is a clear distinction between a contract which still remains to be performed and specific performance of which may be sought and a conveyance by which title to property has actually passed. Cases of mere contract are governed by the provisions of the Contract Act. Cases of the transfer of immovable property are governed by the Transfer of Property Act. A mere contract to mortgage or sale would not amount to an actual transfer of an interest in the immovable property (section 54, Transfer of Property Act), but a deed of sale or mortgage, if duly registered would operate as a conveyance of such interest. Once a document transferring immovable property has been registered the transaction passes out of the domain of a mere contract into one of a conveyance. Such a completed transaction would be governed by the provisions of the Transfer of Property Act, and only so much of the Contract Act as are applicable thereto.

It is significant that the whole of the Contract Act has not been made applicable to transfer of immovable properties. Section 4 Transfer of Property Act, merely makes certain provisions of the Transfer of Property Act, relating to contracts as part of the Contract Act and not vice versa.

It is section 6(h) Transfer of Property which lay down that no transfer can be made for an unlawful object or consideration within the meaning of section 23 Contract Act. Sub-clause (i) further provides that nothing in that section would authorise a tenant having an untransferable right of occupancy to assign his right as such tenant.

Thus an attempted transfer of an untransferable right of an occupancy tenant is merely declared to be unauthorised and therefore void and ineffectual. Similarly a transfer for an unlawful object or consideration is declared to be void and ineffective. So far as these sections go they do not lay down the law that if such a non-transferable interest is included among other transferable properties the whole transaction is illegal. It is noteworthy that in order to bring in the operation of section 6(h) the object or consideration for the transfer should be unlawful. The section would be inapplicable where the object of the consideration for the transfer is itself not unlawful but the transfer may be ineffective on some other ground...

Coming back to the question as to how much of the provisions of the Contract Act are to be deemed to have been incorporated in the Transfer of Property Act, I must point out that what has in some cases been overlooked is that section 24, Contracts Act has not been made applicable to transfers of immovable property. There is therefore no justification for stating broadly that even if the transfers of several items of properties can be split up and separated the whole transaction is void because one part of it may be vitiated. Of course, where the object of the consideration of the transfer is unlawful, as that word is defined in section 23, Contract Act the transfer is not effective... If the effect of enforcing the contract would necessarily be to defeat the provisions of any law, the contract would undoubtedly be void, but if it consists of several distinct parts which can be separated the whole transaction would not be bad unless the provisions of section 24, Contract Act, are applicable to it."

21. The decision in *Dip Narain Singh* AIR 1930 All [FB] was followed in *Gappu Singh v. Har Charan* AIR 1935 Oudh 501 by a Division Bench of the Oudh Chief Court and it was held that section 24 of the Indian Contract Act did not apply to the transfers under Transfer of Property Act ; therefore, where a transfer of several items of properties could be split up and separated, the whole transaction was not void because one part of it was vitiated. A Division Bench of the same court again in *Lal Bhagwat Singh v. Harikishen Das*, AIR 1942 Oudh 1, reiterated the same view following the decision in *Dip Narain Singh*, AIR 1930 All 1 [FB] and distinguished the decision in *Muhammad Khalilur Rahman Khan v. Mohammad Muzammilullah Khan*, AIR 1933 All 468 as being not applicable to the case of a mortgage deed under which some transferable and non-transferable properties were mortgaged . In *Muhammad Khalilur Rahman Khan*, AIR 1933 All 468 no opinion different from the view of the Full Bench in *Dip Narain Singh* AIR 1930 All 1 [FB] it was held that in a case where the terms of the deed contained two separate contracts in the first part of which the debtor admitted a sum of Rs.20,000 as due by him and undertook to pay the same on demand, the debtor was quite competent to enter into that contract. In the second part the debtor mortgaged certain property by way of security. This part was invalid. The two parts could be separated. Therefore, it was held that the plaintiff was entitled to maintain the suit on the basis of the personal covenant to pay as per the

first part of the deed, which the debtor had agreed to pay on demand. It was further held that the right of the plaintiff to recover the amount due on the basis of the agreement was perfectly valid as it was not dependent on the failure of the debtor to perform the contract of mortgage; therefore it was held that section 24 of the Indian Contract Act did not apply. thus the decision in Mohd. Rahman AIR 1933 All 468, also rested on the severability of the valid portion of the contract. This was also the principle which was adopted in Dip Narain Singh AIR 1930 All 1 [FB].

22. It may also be noted that in Eastern Mercantile Bank Ltd. v N T Philip, the entire mortgage deed has been held to be void, applying section 24 of the Indian Contract Act. That was a case where an agreement to stifle the prosecution was the consideration for the mortgaged in the mortgage deed that a sum of Rs.2,400 was misappropriated by the son of the mortgagor and as a compromise, the police prosecution pending against the son of the mortgagor was to be withdrawn. As the whole consideration for the mortgage was opposed to public policy inasmuch as it was for stifling prosecution and as there was no question of severance of any part of the mortgage deed from the invalid portion, as such the entire transaction was vitiated, consequently section 23 of the Contract Act itself was attracted to the case ; therefore there was no question of application of section 24 of the Indian Contract Act. Hence the decisions in Eastern Mercantile Bank Ltd., , cannot be held as laying down the law that section 24 of the Indian Contract Act applies to the completed conveyance.

23. Similar is the position in Soundatti Yellamma Municipality v. Shripadbhat Seshbhat Joshi, AIR 1933 Bom 132. In that case, the Municipality leased the levy of toll on pilgrims though it has no power to levy toll on pilgrims which was in the nature of tax. The lessee failed to pay the amount due under the lease. The Municipality filed a suit for recovery of the amount. One of the contentions raised by the defendant was that the Municipality was not competent to levy toll on pilgrims; therefore the contract granted to him by the Municipality to levy on and collect the toll from the pilgrims was altogether void. It was held that the Municipality had no power to impose the toll. Consequently, it was held that the contract itself was void. As such there was no question of application of section 24 of the Indian Contract Act. Nevertheless, it observed in that case that where a part of the consideration was unlawful, the general rule was that when a valid part could not be severed from the illegal part of the contract, the contract was altogether void.

24. It follows from the above discussion that section 24 of the Indian Contract Act does not apply to a completed transaction of a transfer of property ; the provisions of the Indian Contract Act apply to the transfer of property only to the extent they are made applicable. Section 6(h) of the Transfer of Property Act makes applicable the provisions of section 23 of the Indian Contract Act to transfer of property. Section 23 of the Indian Contract Act does not prohibit enforcement of the valid portion of the transfer of property or debt, if it is severable from the invalid portion. Applying the aforesaid conclusions to the facts of the present case, it is seen that the suit transaction is a mortgage. The mortgage is both a debt and a transfer of interest in immovable property. The mortgage debt in question was valid to the extent of Rs.18,000. The remaining portion of the debt amounting to Rs.12,000 was invalid because it was hit by sub- section (2) of section 54A of the Indian Companies Act, 1913 read with section 23 of the Indian Contract Act. The invalid portion of the debt is severable. The valid portion has already paid.

25. It is an established principle, rooted in public policy, that the courts of law do not aid or do not become instrumental in enforcing transactions *ex turpi causa*. We may usefully refer to the observations made in *Selangor United Rubber Estates Ltd. v. Cradock (No. 3)* [1968] 2 All 1073, 1150 (Ch D) : "It is not disputed by the plaintiff company that if a contract or consensual arrangement is illegal *ex facie*, or made for illegal purpose then the court will not assist in enforcing the contract or consensual arrangement' (whether, eg, by specific performance, money judgment or damages) or to recover property (including money) passed in pursuance of it. The plaintiff company contends, however that such refusal of the court to assist is limited to cases of contract or consensual arrangement' and does not extend in particular to claims based on breach of trust.

26. The ambit, within which such consequences of the illegality operate, has by no means been clearly defined. This amply appeared from the arguments before me. The usual field of its operation is certainly contract ; but then contract is the field which gives most scope for its operation.

27. The principle governing such consequences of illegality is not however, just a twig of any particular branch of the law but is rooted deeply in public policy - that the courts are not to be instruments for aiding illegality in contract, but may be instruments for aiding illegality in other branches of the law. It is accordance with this substantial public policy nature of the courts' refusal of aid to illegality that such illegality is not treated as a matter of pleading or a matter merely as between the parties but as a matter of which the court will, of its own initiative take cognisance irrespective of pleadings or wishes of the parties. The objection to aiding illegality is thus not limited in its origin in public policy to any particular form of action."

28. This being the position the plaintiff corporation is not entitled to recover the suit claim as it represents the invalid portion of the consideration of the mortgage.

29. For the reasons stated above, points 1 and 2 are answered as follows :

The entire mortgage transaction between the company and the defendants was not in contravention of the provisions contained in section 54A of the Indian Companies Act, 1913 ; as such, the entire mortgage transaction was not invalid. The mortgage transaction in question in so far as it included Rs.12,000 as part of the consideration which was adjusted towards the share capital of the company was invalid.

30. Having regard to the fact that the amount claimed in the suit under the suit mortgage admittedly represented the sum of Rs.12,000 adjusted towards the share capital of the company and the interest thereon, and as it is held that it was invalid, the plaintiff corporation is not entitled to recover the same. Hence, the ultimate conclusion reached by the learned appellate Judge that the suit has to be dismissed, is correct and it is accordingly affirmed. Consequently, the appeal has to fail.

31. For the reasons stated above, the appeal is dismissed. However, there will be no order as to costs.

32. At the end, we consider it necessary to clarify that the dismissal of the suit does not come in the way of the United Karnataka Insurance Co. Ltd., Dharwad, calling upon the defendants to surrender the shares.