APPELLATE CIVIL.

Before Sir Murray Coutts Trotter, Kt., *Chief Justice, and Mr. Justice Anantakrishna Ayyar.*

THE OFFICIAL ASSIGNEE OF MADRAS (APPELLANT), 1929. March 15.

v.

THE DEVAKOTTAH NAGARATHAR SRI MINAKSHI VIDYASALAI PARIPALANA SANGAM (RESPONDENT).*

Indian Trusts Act (II of 1882), sec. 66—Trustee wrongfully mingles trust property with his own—If beneficiary entitled to charge on whole fund for amount due—Trustee of endowed school—Money belonging to endowment entrusted to him by co-trustees—Money put into his own business without the knowledge or consent of co-trustee—Trustee adjudicated insolvent—If co-trustees entitled to charge on whole estate in priority to other creditors.

Where a trustee wrongfully mingles trust property with his own, the beneficiary is entitled to a charge on the whole fund for the amount due to him.

Where a banker, who was one of the trustees of an endowed school, had a sum of money belonging to the endowment entrusted to him by his co-trustees, and he put that sum into his own business without the knowledge or consent of his co-trustees, and his business came to a standstill, and he was adjudicated an insolvent, *held*, that the bankrupt's co-trustees were entitled to a charge on the whole estate in the hands of the Official Assignee in priority to other creditors, on the basis of following moneys which have been misappropriated to the fund in which they must be supposed to have been sunk. *In re Hallett's Estate, Knatchbull* v. *Hallett*, (1879) 13 Ch.D., 696, *Sinclair* v. *Brougham*, [1914] A.C., 398, and *Pennell* v. *Deffell*, (1853) 4 De G.M. & G., 372, followed.

ON APPEAL from the judgment of Mr. Justice WALLER, dated 20th September 1927, and passed in the exercise

* Original Side Appeal No. 82 of 1927.

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of the Insolvency Jurisdiction of the High Court in Petition No. 278 of 1925, Application No. 418 of 1927.

M. A. R. N. Ramanathan Chettiar, a Nattukottai Chetti, was carrying on a money-lending business under the firm name of M. A. R. N. Ramanathan Chettiar. He was a member of the committee of the Nagarathar Sri Minakshi Vidyasala Paripalana Sangam, and also the treasurer of the Sangam. As treasurer, Ramanathan Chettiar collected various sums subscribed for the upkeep of the school conducted by the Sangam. He paid these sums into his own business without the knowledge or consent of his co-trustees, and in 1925, the firm was adjudicated insolvent. At the time of adjudication, a sum of over Rs. 40,000 stood to the credit of the Sangam in the firm's books. The committee of the Sangam claimed that the said amount should be paid in full by the Official Assignee in preference to the debts due to the other ordinary creditors. The Official Assignee passed an order rejecting the claim, stating that "the relationship between the governing body and the insolvent was that of debtor and creditor. Assuming for the purpose that he was in a fiduciary relationship and that he acted improperly in investing the moneys of the school in his firm, the same cannot be thus identified or earmarked. When the firm was adjudicated insolvent, there was no cash and no part of the assets could be followed by the beneficiary." Against that order of the Official Assignee, the committee appealed to the Judge sitting in Insolvency, who allowed the appeal and gave the committee a first charge for the full amount of their claim on the assets of the firm of the insolvent.

S. Duraiswami Ayyar (*V. Varadaraja Mudaliar* with him) for appellant.—The committee, not having shown that its money was traceable to any fund vested in the Official Assignee, was entitled to rank only as a simple unsecured creditor, *In re*

Hallett & Company, ex parte Blane(1), judgment of LOPES, L.J., at 244: "If trust money can be traced, it is liable to be followed by the trustee, and will not pass to the trustee in bankruptcy; but if it has been mixed up with other money so as not to be distinguishable, it cannot be followed."

[CHIEF JUSTICE.—No money really passed into the hands of Hallet. It was a mere book adjustment.]

The rule as to following trust property requires that there must be something specific which is capable of being identified as that into which the money has been converted. Lewin on Trusts, 12th Edn., p. 1155; 13th Edn., p. 934. See also Godefroi on Trusts and Trustees, 5th Edn., p. 575, and Halsbury's Laws of England, Vol. 28, p. 207.

V. V. Srinivasa Ayyangar (*S. G. Sadagopa Mudaliar* with him) for respondent.—There is no dispute as to the facts. On the admission of the appellant's counsel at the trial the respondent is entitled to a charge on the entire fund. "If a trustee pay trust money into a bank to the account of himself not in any way earmarked with the trust, and also keep private money of his own to the same account, the Court will disentangle the account, and separate the trust from the private money and award the former specifically to the *cestui que trust.*" Lewin on Trusts, 13th Edn., p. 933, and *Pennell* v. *Deffell*(2); see also *Sinclair* v. *Brougham*(3), *In re Hallett's Estate, Knatchbull* v. *Hallett*(4), and Halsbury's Laws of England, Vol. 28, p. 208.

JUDGMENT.

COUTTS TROTTER, C.J.

COUTTS TROTTER, C.J.—I have so little confidence in my own ability to decide correctly a case involving wide principles of Equity, that I am relieved to find that the amount here at stake is sufficient to enable an appeal to be taken to a higher tribunal. I approach this case with much more than the diffidence expressed by Lord SUMNER in *Sinclair* v. *Brougham*(3), and feel myself under the ban expressed by THESIGER, L.J., in Hallet's

(1) [1894] 2 Q.B., 237.
(2) (1853) 4 De.G.M. & G., 372.
(3) [1914] A.C., 398.
(4) (1879) 13 Ch.D., 696.

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case (13 Ch. Dn., 696 at p. 722), as to the unlikelihood of Common Law judges even of the eminence of Lord BRAMWELL being able to understand any but the simplest and most firmly established of Equity doctrines.

My duty is simply to set out the facts which are practically undisputed, and to apply to those facts the principles I conceive to be laid down by the decided cases as best I can.

[His Lordship then stated the facts.] The sole question before us is whether the bankrupt's co-trustees are relegated to the position of ordinary creditors in the insolvency, or are entitled to say that they stand on a higher footing and are entitled to a charge on the whole estate in priority to other creditors, on the basis of following their moneys which have been misappropriated, to the fund in which they must be supposed to have been sunk.

I have most carefully perused the cases that the diligence of counsel has placed before us; and I wish to express my indebtedness for the assistance they have given us. The guiding principles, as I conceive them to be, are laid down in two great judgments—that of JESSEL, M.R., in *In re Hallett*(1), and that of Lord HALDANE in *Sinclair* v. *Brougham*(2). I do not propose to examine the early Common Law cases, though they have been cited to us, because, as JESSEL, M.R., points out, the judges were then dominated by the idea that, money being unidentifiable, it could in no case be followed, a doctrine eliminated by "modern equity," to use his own language. I take these propositions to be indisputable; and in stating them, I use throughout for brevity the term "trustee" to cover all cases of persons who stand in a fiduciary position and "*cestui que*

(1) (1879) 13 Ch. D., 696.

(2) [1914] A.C., 398.

trust" to cover the cases of all those towards whom the persons I have called "trustees" stand in that position :—

(1) That if the trustee keeps the sums entrusted to him entirely separate from his own moneys, as by putting them in cash in a bag, to use Sir G. JESSEL's instance, or by putting them into a separate account at a bank, the *cestui que trust* can follow them.

(2) That if the trustee can be shown to have converted the trust money into a specific thing, such as a piece of land, or a definite parcel of goods remaining in his possession, the *cestui que trust* can take that land or those goods as representing his money or claim a lien on them for the money expended on the purchase.

(3) Then comes the more common case where the trustee has mixed up the trust money with his own. I think here it is clear that, if the trustee has bought land or goods out of moneys which are partly his own and partly those of the *cestui que trust*, the *cestui que trust* can claim a charge on the property for the amount of his funds which was expended in the purchase. That is not always easy of ascertainment, and the working rule appears to be that if the trust moneys have disappeared and no residue is left, the *cestui que trust* will be entitled to a charge on the whole until it is ascertained what portion of the purchase money was contributed by the trustee out of his own funds and not out of the trust money, the onus being cast on the trustee to prove what portion came from his own funds. When that is ascertained, the *cestui que trust* will only have a lien on the property for the amount ascertained to be due to the misuse of the trust moneys.

Then arises the case where the trust moneys have not only been mixed with the trustee's moneys, but

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where there is no tangible asset which could be alleged to have been acquired with the trust funds—wholly or partially. That is the case before us, because here what the trustee did was to put the trust moneys in his hands into his own business and subject them to all the fluctuations of that business, and it is clear that the business was so unsuccessful that the actual funds in the hands of the Official Assignee as at this date realized amount to nothing. It was strenuously argued by Mr. Doraiswami Ayyar that in such circumstances the Court could not give a preferential charge over prospective as distinct from actually tangible assets of the business. That argument ultimately seems to me to imply that a trustee has only to put trust moneys into a business, and then and there the *cestui que trust* is debarred from invoking the equitable doctrine, and sinks to the position of an unsecured and unpreferred creditor of the estate. That view seems to me to have been negatived so long ago as 1853 by the judgment of TURNER, L.J., in *Pennell* v. *Deffell*(1). At pages 388 and 389, the learned Lord Justice takes the very case we have to consider as a clear illustration of a case to which the equitable doctrine would apply.

We were much pressed with the case of *In re Hallett & Co., ex parte Blane*(2). After a careful consideration of that case, I think it decides no more than this:—that a paper adjustment cannot be treated as a passing of moneys of the *cestui que trust* into the hands of the trustee. On page 242, the point is first and emphatically taken by DAVEY, L. J. Mr. Muir Mackenzie in argument had said: "The £1,600 was in fact received by Hallett & Co." DAVEY, L. J., then said; "No; all that happened

(1) (1853) 4 DeG.M. & G., 372. (2) [1894] 2 Q.B., 237.

was that they got a credit for that amount." I read the judgments which follow as proceeding on those lines, viz., that while you can follow money, you cannot follow a mere book adjustment.

I think that the learned Judge came to the right conclusion and that this appeal should be dismissed with costs payable by the Official Assignee out of the estate. Certificate for two counsel. Official Assignee to take his costs out of the estate.

COUTTS TROTTER, C.J.

ANANTAKRISHNA AYYAR, J.—(After stating the facts):—The school authorities appealed to the learned Judge sitting in Insolvency against the order of the Official Assignee. The learned Judge (Mr. Justice WALLER) allowed the appeal and gave the school authorities a first charge for the full amount of their claim, on the realization of the debts due to the firm of the insolvent.

ANANTAKRISHNA AYYAR, J.

The Official Assignee has preferred this appeal against the order of the learned Judge, and contends that the school authorities are not entitled to rank higher than the ordinary unsecured creditors of the insolvent.

Before discussing the question of law raised by Mr. S. Doraiswami Ayyar, the learned Counsel for the appellant, I think it is better just to refer to the finding of fact arrived at by the learned Judge. In the course of the judgment, the learned Judge has recorded the following admission made before him by the Counsel who appeared for the Official Assignee. "Mr. S. Doraiswami Ayyar for the Official Assignee concedes that he is unable to support the view that the relation between the insolvent and the trust was one of debtor and creditor. He admits that Ramanathan Chetti was a trustee and received the trust funds as a trustee and mixed it with the funds of his own business." As a trustee of the Nagarathar school, the insolvent was

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entirely in the wrong in utilizing the trust funds in connexion with his own business. As the learned Judge remarks, "there can be no question as to the wrongful nature of Ramanathan Chetti's action, for the mingling itself was wrongful."

The question then is whether the beneficiary (the school) is entitled to a first charge on the trade assets of Ramanathan Chetti's firm. Section 66 of the Indian Trusts Act (II of 1882) enacts as follows:—

> "Where the trustee wrongfully mingles the trust property with his own, the beneficiary is entitled to a charge on the whole fund for the amount due to him."

The learned Counsel for the appellant contends that the beneficiary is entitled to a charge for the trust money, only if he can trace it to a specific fund. The trust funds have been admittedly utilized by the insolvent in connexion with his money-lending business. It is not now possible to say which particular asset due to the firm represents the trust moneys. In these circumstances, it is argued for the Official Assignee that the beneficiary is entitled only to rank as an ordinary creditor along with the other creditors of the insolvent. In support of his contention, the learned Counsel strongly relied on *In re Hallett, ex parte Blane*(1). The following passage on page 244 in the judgment of Lord Justice LOPES was relied upon:—

> "If trust money can be traced, it is liable to be followed by the trustee and will not pass to the trustee in bankruptcy; but if it has been mixed up with other money so as not to be distinguishable, it cannot be followed."

This case however has been understood by text-writers as authority for the proposition "that in the case of *money*" there must be in fact a payment, since "the doctrine of following" depends upon identification

(1) [1894] 2 Q.B., 237.

of the subject matter; and where money not actually received was credited to an account, the doctrine was held inapplicable. Godefroi on Trust and Trustees, 4th Edition, pages 564 and 565. In Lewin on Trusts, 12th Edition, page 1155, it is stated as follows:—

"In order, however, that the rule as to following trust money should apply, there must be something specific which is capable of being identified as that into which the money has been converted, and where a transaction has been carried out by a set-off in account so that no cheque, note, coin or credit has ever passed or existed in specie, the doctrine is inapplicable."

Turning to the judgments delivered in *In re Hallet & Company's* case, we find that Lord ESHER (Master of the Rolls) says at page 244:—

"Hallett & Company did not in truth receive any money; they entered into a transaction with Hewitt & Company, the result of which was that no money passed . . . Hallet & Company did not in fact receive any money or tender of money or anything tangible which it would be possible to follow or to lay hands upon; . . . all that can be shewn is a settlement of account; and a settlement of account cannot be followed."

Similarly, LOPES, L.J., says:—

"So far as regards the following of this sum of £1,600, the attempt fails at the first stage, for that particular £1,600 was never received by Hallett & Company; no money had passed; there had been a mere settlement with Hewitt & Company. Then, again, this specific sum never passed on to Cocks & Company; and the second stage fails too."

Similarly, at page 245, DAVEY, L.J., also makes similar remarks:—

"This money was not received by them (Hallett & Company) in any sense which is material to the present purpose. Nothing was received by them in specie, notes, cheques or coin; there was no credit existing in specie; nothing which the *cestui que trust* could follow and say that the property had been converted into."

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Therefore, the case *In re Hallett & Company, ex parte Blane*(1) could be distinguished on the ground that in that case it was found that the very first step that the beneficiary should prove in such cases, namely, that the trustee received moneys of the beneficiary was not proved. On the other hand, authority seems to be fairly clear that where a trustee wrongfully mingles the trust property with his own, the beneficiary is entitled to a charge on the whole fund for the amount due to him. (See section 66 of the Indian Trusts Act, Halsbury's Laws of England, Vol. 28, page 207, sections 415 and 416.) It was admitted that where trust money is wrongfully laid out in the purchase of specific real or personal property, the beneficiary can elect to have a charge upon it for the amount of the trust money. (See authorities referred to in paragraph 415 of Halsbury's Laws of England, Volume 28.) If therefore the trustee in this case had purchased a going concern of another with the trust funds, then the beneficiary would have an option either to take the purchased property or elect to have a charge upon it for the amount of the trust money. If, instead of purchasing a going concern, the trustee wrongfully utilizes the trust money for starting a business, or for carrying on a business of his own, then it would seem that the beneficiary is entitled equally to elect to have a charge upon the assets of the business for the amount of the trust money.

It was, however, contended by the learned Counsel for the appellant that the doctrine of following trust property is not applied, and could not in the nature of things apply, when the trust funds are wrongfully applied by the trustee in a trade or business. If the doctrine is not confined in its application to cases of

(1) [1894] 2 Q.B., 237.

mingling of trust moneys with the trustee's own money where there is a mingled fund available, if the doctrine also applies to cases where with the money of the beneficiary the trustee wrongfully buys other property, and if the beneficiary could in such cases claim to have a charge on such property to the extent of the trust money utilized wrongfully by the trustee, I am not clear why the doctrine should not apply when the trustee, instead of utilizing the trust money for the purchase of property, utilizes it in a trade or business of his own. Having regard to the findings in the present case and to the admission made on the Official Assignee's behalf, as recorded by the learned Judge, there is no difficulty as regards the facts in the present case; for, as already mentioned, it was admitted before the learned Judge on behalf of the Official Assignee that "Ramanathan Chetty was a trustee and received the trust fund as a trustee and mixed it with the funds of his own business." The learned Counsel for the respondent cited to us the case of *Pennell* v. *Defell*(1). Lord Justice TURNER observed as follows :—

"It is, I apprehend, an undoubted principle of this Court that as between *cestui que trust* and trustee and all parties claiming under the trustee otherwise than by purchase for valuable consideration without notice, all property belonging to a trust, however much it may be changed or altered in its nature or character, and all the fruit of such property, whether in its original or in its altered state, continues to be subject to or affected by the trust; and from this principle I do not understand the Master of the Rolls to have in any degree dissented. Several cases illustrating the principle were cited in the argument, but perhaps it cannot be better illustrated than by referring to a case of familiar, almost daily, occurrence, the case of trust-moneys employed in trade. An executor of a deceased partner continues his capital in the trade with the concurrence of the surviving partners, and carries on the trade with them.

(1) (1853) 4 De G.M. & G., 372 (43 E.R., 551 at 558).

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The very capital itself may consist only of the balance which at the death of the partner was due to him on the result of the partnership account. That capital may have no existence but in the stock-in-trade and debts of the partnership. The stock-in-trade and debts may undergo a continual course of change and fluctuation, and yet this Court follows the trust capital throughout all its ramifications and gives to the beneficiaries of the deceased partner's estate the fruits derived from that capital, so continually altered and changed. We have here, I think, the most perfect instance of the extent to which the doctrine of following trust property has been carried by the Court, an instance, too, which exemplifies the difficulties with which the Court has felt bound to grapple for the purpose of carrying out that doctrine, for nothing can be more difficult, nothing more inconvenient, than to follow out such a case to its results."

We were also referred to *In re Hallett's Estate, Knatchbull* v. *Hallett*(1), to the Judgment of JESSELL (Master of the Rolls) at page 707, *et seq.* The decision of the House of Lords in *Sinclair* v. *Brougham*(2), was also referred to, and several passages from the speeches of the learned Lords who took part in that case were read to us. For example, at page 438, in Lord DUNEDIN'S speech, the following passage occurs:—

"Now there are certain situations, of which Hallet's case is an example, where the one sharing party has a right to say to the other, it is not in your mouth to say that the assets are not all mine, to the extent of my full claim. I do not think this is one of those positions. Neither party is here in any fiduciary position to the other."

Similarly, passages at page 418 in the speech of the Lord CHANCELLOR (Viscount Haldane) were also read to us.

I think that some of the passages occurring in the above case could be construed as laying down the principle contended for by the respondent, though it may be said that the point for decision before the House was quite a different one, and that the learned Lords

(1) (1879) 13 Ch. D., 696. (2) [1914] A.C., 398.

were not considering the exact point now before the Court.

In Perry on Trusts, 6th edition, Volume II, paragraph 828, page 1364, it is said that

"to entitle the trust oreditor to preference, it must at least appear that the fund remaining for distribution contains the proceeds of the trust."

Again in paragraph 838, it is mentioned that

"if the executor of a deceased partner is also the surviving partner, and he continues the deceased partner's capital without authority in the business and changes the property many times over, the Court follows the trust fund through all these changes and gives the beneficiaries of the deceased partner's estate the capital and all its proceeds or gains in the business in which it has been employed."

The only Indian case I am aware of, which is somewhat similar to the present case, is *Mulraju Lakshmi* v. *Official Assignee of Madras*(1), decided by SADASIVA AYYAR and NAPIER, JJ.

"Where a jeweller who was entrusted by the claimant with sovereigns and gold to be made into a jewel for him converted the same into cash and subsequently became bankrupt, and after the Official Assignee took charge of his estate, the owner of the sovereigns and gold put forward a claim that he was entitled to a preferential treatment and to get out of the estate the full value of the sovereigns and gold entrusted by him to the bankrupt,"

the Court held

"that the transaction between the claimant and the jeweller amounted to a bailment and that the jeweller became in consequence a trustee for the claimant in respect of the sovereigns and gold entrusted to him."

But as there was no evidence in that case, that the sovereigns and gold formed a portion of the estate taken possession of by the Official Assignee and as there was nothing to identify the same, the Court held that

(1) (1915) 29 I.C., 37.

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"the claimant was not entitled to the benefit of the doctrine of tracing and quasi-charge, and therefore to any preferential payment."

Justice SADASIVA AYYAR at page 41 says

"If in this case I could have found my way to decide that the assets taken possession of by the Official Assignee did include, or must have included, the gold or the value of the gold contained in the sovereigns and the bar given by the petitioner to the insolvent, I would be inclined to apply the doctrine of tracing and the doctrine of a *quasi-charge* even to the full limits indicated by Lord DUNEDIN in his judgment in the recent House of Lords case; but I do not see my way to differ from the findings of Mr. Justice BAKEWELL that the petitioner has failed to show that the gold or the price of that gold was invested in or formed part of any of the assets taken possession of by the Official Assignee."

Again the learned Judge adds:

"On the finding then that none of the assets found with the insolvent is proved, directly, or even by a remote fact from which a reasonable inference could be drawn, to have contained any portion of the petitioner's gold or could have been acquired with the use of the proceeds of that gold, I must and do confirm the order of the learned Judge."

The principle would seem to be that a wrong doer cannot be permitted to take advantage of his own wrong, and that no wrongful act of the trustee could prejudice the rights of the beneficiaries, in cases like the present.

I am, therefore, of opinion that the learned Judge was right in holding that the principle of following trust property applied to the facts and circumstances of the present case. I would therefore dismiss the appeal with costs. Costs to be realized from the estate. Certificate for two Counsel. The Official Assignee is entitled to take his costs from out of the estate.

B.C.S.