Bombay High Court State Bank Of India vs Trade Aid Paper And Allied ... on 25 May, 1995 Author: M Pendse Bench: M Pendse, A Savant, S Kapadia JUDGMENT M.L. Pendse, Actg. C.J. 1. The State Bank of India is a banking company incorporated under the State Bank of India Act, 1955, and carries on business all over the country through its various branches. Respondent No. 1 is a private limited company and is the owner of industrial gala bearing No. 116, Shiv Shakti Industrial Estate, Ghatkopar, Bombay. Respondent No. 1 sought diverse credit facilities from the appellant-bank and the facilities were granted on November 18, 1991. The facilities granted were : (a) Demand cash credit against hypothecation of stocks for Rs. 50 lakhs. (b) Demand cash credit against hypothecation of book debts for Rs. 55 lakhs, (c) Bill discounting limit for Rs. 25 lakhs. (d) Import and inland letters of credit for Rs. 75 lakhs, (e) Bank guarantee limit for Rs. 10 lakhs. 2. Respondents Nos. 2 to 9 stood as guarantors for repayment of loan amounts by respondent No. 1. Respondents Nos. 2, 3 and 4 are individuals, while respondents Nos. 5 to 8 are companies and respondent No. 9 is a sole proprietary concern. Respondent No. 4 is the owner of industrial gala bearing No. 112, in Shiv Shakti Industrial Estate, Ghatkopar, Bombay, and also of a residential flat in Jai Jatin Co-operative Housing Society at Ghatkopar. Respondent No. 4 also owns factory land at Patalganga in Raigad district of this State. 3. In consideration of the bank granting credit facilities to respondent No. 1, the respondents executed various documents including (a) a general agreement for grant of small industrial advances and hypothecation of movables, book debts and other assets, and (b) a common letter of guarantee by defendants Nos. 2 to 9 guaranteeing repayment of amounts due and payable in respect of facilities granted by the bank. Respondent No. 2 on March 9, 1992, created an equitable mortgage in respect of gala bearing No. 116 on behalf of respondent No. 1 by deposit of title deeds. The equitable mortgage was also in respect of movables including the plant and machinery affixed in the gala. The bank prepared a memorandum of deposit of title deeds duly stamped as required by law. On March 10, 1992, respondent No. 1 confirmed by letter the fact of deposit of title deeds. Respondent No. 2 created a legal mortgage and an indenture of mortgage dated March 9, 1992, in respect of property situated at Patalganga. The respondents by another indenture of mortgage dated March 19, 1992, created a legal mortgage in respect of other immovable properties. 4. Respondent No. 1 utilised various credit facilities and by confirmation letter dated April 12, 1994, confirmed that a sum of Rs. 1,59,65,363.42 was due and payable to the bank as on March 31, 1992. Respondent No. 1 was irregular in maintaining the accounts and committed defaults in repayment. The bank thereupon by letter dated January 25, 1995, called upon respondent No. 1 to pay the outstanding amounts within four days from the receipt of the letter. The respondents sent a reply on January 28, 1995, merely demanding inspection of documents and claiming that negotiations for revival of respondent No. 1-company were pending. The bank thereafter called upon respondents Nos. 2 to 9 - the guarantors, to pay a sum of Rs. 1,89,50,616.05 along with future interest thereon at the rate of 17.75 per cent. per annum with quarterly rests. The respondents failed to repay any amount and that gave rise to the filing of

Suit No. 532 of 1995 on the original side of this court on March 15, 1995. 5. On institution of the suit, the bank took out notice of Motion No. 924 of 1995 seeking interim relief pending the disposal of the suit. The interim relief sought was appointment of a court receiver under Order 40, rule 1 of the Code of Civil Procedure, 1908, in respect of properties described in exhibits "A" to "D" to the plaint and stocks, book debts, plant and machinery described in exhibit "R" to the plaint. The bank claimed that the receiver should be directed to sell and realise the same and pay over the net sale proceeds towards the satisfaction of the claim in the suit. The bank also sought an injunction restraining the respondents from disposing of, alienating, encumbering or creating third party interest in respect of properties described in exhibits "A" to "D" and "R" of the plaint. 6. The bank moved the learned single judge on March 31, 1995, for grant of ad interim relief. The learned judge by order dated March 31, 1995, granted ad interim relief of injunction restraining the respondents from alienating or encumbering or creating any third party interest in the properties and declined to appoint a receiver. The order declining the relief of appointment of a receiver gave rise to Appeal No. 290 of 1995. The appeal came up for hearing before a Division Bench and by order dated April 18, 1995, the appeal was referred to the larger Bench in view of the conflict of decisions between the two Division Benches of this court. The appeal is accordingly placed before this Full Bench. 7. The respondents submitted that the order granting injunction restraining the respondents from alienating or encumbering the properties more than safeguards the interest of the appellants and no case whatsoever is made out for appointment of a court receiver under Order 40, rule 1 of the Code of Civil Procedure, 1908. It was urged, relying upon the decision of the Division Bench in B. D. A. Ltd. v. Central Bank of India, that a receiver should not be appointed unless it was established that the properties hypothecated and mortgaged were likely to be insufficient to satisfy the claim or that they were likely to be dissipated or wasted. The bank, on the other hand, pleaded that the decision of the Division Bench proceeds on the peculiar facts of the case and the observations made therein are erroneous. The bank further submitted that the earlier decision of the Division Bench in Podar Mills Ltd. v. State Bank of India , was not considered and which decision clearly lays down that in suits instituted by banks and financial institutions for realisation of public money, the appointment of a court receiver is a must. 8. Order 40, rule 1 of the Code of Civil Procedure, 1908, provides for appointment of a receiver, where it appears to the court to be just and convenient. The power can be exercised both before and after decree. The power conferred upon the receiver enables the receiver to manage, protect and preserve the property and to collect the rents and profits thereof and for realisation of profits. The principles to be borne in mind while exercising the powers under Order 40, rule 1 of the Code of Civil Procedure, 1908, are well-settled by a catena of decisions and as observed by the Privy Council in Benoy Krishna Mukerjee v. Satish Chandra Giri, AIR 1928 PC 49, the court has to consider whether special interference with the possession of the defendant was required, there being a well-founded fear that the property in question will be dissipated or that other irreparable mischief may be done

unless the court gives its protection. A single judge of the Madras High Court in a decision in T. Krishnaswamy Chetty v. C. Thangavelu Chetty, , set out five factors which the court must consider before concluding that it is just and convenient to appoint a receiver. The five factors are : (i) The appointment of the court receiver was a matter resting in the discretion of the court. (ii) The appointment should not be made unless the plaintiff had prima facie an excellent chance of succeeding in the suit, (iii) The plaintiff establishes some emergency or danger or loss demanding immediate action, (iv) The order would not be made if it had the effect of depriving the defendants of a 'de facto' possession, and (v) The court will look to the conduct of the party who made the application and would refuse to interfere if the conduct is not free from blame. 9. The decision of the Privy Council and of the Madras High Court and other decisions referred to during the arguments were recorded in the suits instituted by individuals and the only decision where the suit was instituted by a bank or a financial institution was the one in Podar Mills Ltd. v. State Bank of India . In this case, the State Bank of India had filed a suit for recovery of a sum of Rs. 13,59,49,986.59 and pending the suit, the trial judge appointed the court receiver to take charge of the secured properties. It was contended before the Division Bench that though a receiver can be appointed in a suit for enforcement of an equitable mortgage, it could be done in extraordinary cases and where there are allegations of waste. The Division Bench examined the judgment of the Privy Council and the Madras High Court referred to hereinabove as well as the Full Bench of the Allahabad High Court in Anandi Lal v. Ram Sarup , and the Division Bench of this court in Damodar v. Radhabai, AIR 1939 Bom 54, and thereafter came to the conclusion that a receiver should be appointed to protect the mortgaged property pending the disposal of the suit if the circumstances so warrant. The Division Bench further held that the court must bear in mind that the claim made against the company is in respect of public monies. 10. The Division Bench, which spoke through Mr. Justice Bharucha, as he then was, was fully conscious of the large number of suits filed by banks and financial institutions on the original side of this court and which involved huge stakes. The Division Bench was also conscious of the fact that suits filed by banks and financial institutions do not reach hearing for over several years for reasons which are beyond the control of the courts and the litigants. Experience clearly indicates that in almost all the suits instituted by banks and financial institutions, there is hardly any defence. The usual defences are that the documents are signed in blank, that the interest charged is excessive and the fact that the amount was secured from the bank is never seriously disputed. Indeed, the suits are resisted with the knowledge that the date of the judgment will be postponed by a few years and the monies secured from the bank and which are really the monies of the depositors can be profitably used for some more years. The Division Bench was fully conscious of all these aspects and, therefore, observed that when the claim is in respect of public monies and the amount involved is large, then the receiver should be appointed to protect the mortgaged property pending disposal of the suit. The view taken by the Division Bench is correct and is consistently followed in this court. 11. In the case

of B. D. A. Ltd. v. Central Bank of India, Central Bank of India instituted a suit for recovery of a large amount and pending the suit sought appointment of the court receiver in respect of secured properties. The learned single judge by observing that the suit is the usual bank suit appointed the court receiver in respect of the secured properties. The Division Bench, speaking through the Chief Justice Bhattacharjee, set aside the order by observing that the receiver shall not be appointed unless it appears that the sale proceeds of the property secured or other securities are insufficient to satisfy the claim. It was further observed that the appointment of the receiver is permissible only in extreme cases and in circumstances where the interest of the creditor is exposed to manifest peril. The Division Bench felt that the receiver shall not be appointed unless there is well founded apprehension that the property in suit will be dissipated or other irreparable mischief may be done. The Division Bench placed strong reliance upon the judgment of the Madras High Court in T. Krishnaswamy Chetty v. C. Thangavelu Chetty, , but did not refer to the earlier Division Bench judgment of this court. Though the Division Bench observed that, on the facts of the case, the appointment of the receiver was not warranted, it proceeded to make observations which had the effect of nullifying the earlier judgment. The Division Bench was not right in various observations made in the judgment and these observations would create untold hardships to banks and financial institutions while realising the public monies. The Division Bench was conscious that the nationalised banks and the monies belonging to such banks are of the entire nation and in the conflict between the individual and the interest of the nation, the latter should prevail. In spite of this, the Division Bench set aside the order of the learned single judge appointing the receiver by finding fault with the observation of the trial judge that the suit filed by the bank is the "usual bank suit". The expression "the usual bank suit" should have been understood as a suit filed by the bank to recover the amounts which were advanced and where the defendant has no valid defence. 12. In the Madras case, on which the Division Bench placed reliance, the plaintiff had filed more than three suits claiming a right to certain properties and which suits never went for hearing and were dismissed or withdrawn. The fourth suit was filed for a declaration that the alienations made in favour of the defendants were not valid and binding and that the suit was filed in forma pauperis. The properties involved in the suit belonged to the grandfather of the plaintiff and who had left a will and of which probate was granted. After the grant of probate, the members of the family were given definite shares and later on a family arrangement culminated in a consent decree passed by the Madras High Court. The respective branches were enjoying the properties and alienating the same. The fourth suit was filed in forma pauperis and the application for appointment of a receiver was made two years after the filing of the suit. On these facts, the learned judge came to the conclusion that the appointment of a receiver was ruled out and thereafter set down the five principles hereinabove quoted. 13. The suits instituted by banks and financial institutions for realisation of loans advanced to borrowers form a class by themselves. The amounts advanced by nationalised banks or financial institutions are out of the funds deposited by common citizens and

the loans are advanced with a view to generate more employment and creation of additional wealth. Indeed, the amount is advanced with a view to further the cause of the country and surely not for the benefit of an individual. The banks and the financial institutions secure the requisite documents and the borrower prior to obtaining loans executes deeds of mortgages and hypothecation of movables including raw materials and book debts. The refusal to return the amount compels the bank to institute suits and in case the interim relief is denied, the person who refuses to repay could continue to use the public money and make profits to the detriment of the financial institution. To hold that the receiver should not be appointed unless it appears that the sale proceeds of the properties secured or other securities are insufficient to satisfy the claim, or the receiver should be appointed only in extreme cases and where the interest of the creditor is exposed to manifest peril would lead to serious prejudice. In the first instance, the value of the property or other securities as on the date of the suit is not likely to remain the same on the date of the judgment and which in this court means more than 10 years. The assumption of the Chief Justice in B. D. A. Ltd.'s case, that the value of the property would remain the same is erroneous because even if the injunction is granted restraining the defendants from alienating or encumbering the property, that would not prevent the preferential right of the Government or corporation to bring the properties to sale for failure to pay income-tax dues or property taxes. The apprehension of the financial institution that the properties are exposed to manifest peril when the defendant is committing default in repayment of the loan amounts is perfectly just and cannot be bypassed by suggesting that the property involved will not be dissipated or otherwise irreparable mischief may not be done by not granting injunction. The assumption of the Division Bench in B. D. A. Ltd.'s case, that the properties are not likely to be dissipated, wasted or otherwise seriously damaged or injured if a receiver is not appointed is incorrect in most of the cases. Experience indicates that huge amounts are secured from banks and financial institutions and repayment is refused for no valid reason. The institution of the suit and the pendency of the suit enables the defendants to create more encumbrances on the properties and some of the encumbrances are like failure to pay income-tax, property taxes, provident fund dues of the employees, etc. All these liabilities though subsequent to the date of the institution of the suit have a preferential claim of recovery and that leaves the bank without any real relief after obtaining judgment. It is, therefore, futile to suggest that the bank or the financial institution are not exposed to manifest peril. The effect of the observations of the Division Bench in B. D. A. Ltd.'s case, with respect, is to virtually rule out appointment of a receiver in suits instituted by banks and financial institutions and consequently, the decision is incorrect and is overruled.

14. As mentioned hereinabove, the decisions referred to in the judgment as regards the ambit of the power of the court to appoint a receiver under Order 40, rule 1 of the Code of Civil Procedure, 1908, were recorded in suits filed by individuals to recover loans or to enforce mortgages. The economic policy of the Government and the nationalised banks has opened new vistas and requires the banks and the financial institutions to advance loans in many areas which were

earlier unknown. The benefit available to citizens of securing loans from banks and financial institutions cannot be misused by refusal to repay the amount and then indulging in time-consuming litigation. Indeed, it is the duty and function of the court entertaining the suits instituted by banks and financial institutions to ensure that efforts are made to dispose of the suits as early as possible and even during the pendency of the suits ensure that not only the properties are protected but the defendant is made to repay the amount, if desirous of enjoying the benefits secured by obtaining the loan. The powers of the court under Order 40, rule 1 of the Code of Civil Procedure, 1908, are to be exercised to advance the cause of justice and what is "just and convenient" depends upon the nature of the claim and the surrounding circumstances. The court should not close its eyes to the realities and blindly follow the principles laid down 50 years before when suits by banks and financial institutions were a novelty. The economic liberalisation and the policy of the Government to grant loans for various activities has increased the number of suits by banks and financial institutions and in this court every year more than 2,000 suits are instituted. It would not be difficult to imagine how much public money is involved in these suits and how long the nationalised banks and financial institutions are deprived of their dues. The court should be conscious of these facts and should be more pragmatic in exercising the powers under Order 40, rule 1 of the Code of Civil Procedure, 1908. 15. Parliament is also conscious of the importance of the claims of the banks and financial institutions and section 29 of the State Financial Corporations Act, 1951, entitles the financial corporation to take up possession of the concern when a default is committed and without resorting to a suit. Parliament had realised that taking advantage of the liberal economic policies and healthy approach of banks and financial institutions to advance loans, there is a growing tendency to misuse the facility by taking advantage of delays in disposal of cases in court. The delay in disposal of cases in the court is not due to the fault of the litigant and the banks and financial institutions should not be hampered from recovering the amounts by denial of just relief admissible under Order 40, rule 1 of the Code of Civil Procedure, 1908. 16. The courts while appointing receivers under Order 40, rule 1 of the Code of Civil Procedure, 1908, may not deprive the defendant of possession in the case of immovable properties provided that the defendant is ready and willing to continue in possession as agent of the receiver on terms and conditions to be settled. In case, the defendant is ready and willing to accept the agency then the defendant will continue to hold "de facto" possession. In case the defendant is not ready and willing to accept the agency or commits default in compliance with the terms of the agency, then it is open for the court to invite bids from outsiders for use and enjoyment of the immovable property. While inviting bids, the court should ensure that a reserve price is fixed after ascertaining the valuation from a valuation expert. In no case, should immovable property be sold by the receiver before passing of the decree in favour of the bank or the financial institution. In the case of movable property and which is hypothecated with the bank or the financial institution, the receiver should be normally appointed. In the documents executed by the defendant while securing loans from the banks, the defendant often agrees that

receiver can be appointed, in respect of hypothecated goods, if defaults are committed. The appointment of the court receiver is de hors the agreement but to refuse to appoint the receiver in respect of hypothecated goods virtually amounts to denial of relief in respect of hypothecated goods. The hypothecated goods either will not be available on the date of the judgment or would lose their value and, therefore, appointment of a receiver is necessary in respect of movable properties. In case, the defendant is willing to work as agent of the court receiver, then movables can be handed over to the defendants on such terms and conditions as the receiver can settle. In a case where vehicles or air-crafts are hypothecated, the defendants should be permitted to use them as agent of the receiver on terms and conditions to be settled. In respect of book debts, the receiver on terms and conditions to be settled. In respect of book debts, the receiver should be directed to recover the same. There is one more category, where the appointment or receiver is necessary and that is in respect of property which belongs to banks or financial institutions and which is leased out to the defendants for use and occupation. The refusal to return the property results in institution of suits and in such cases also the receiver should normally be appointed and the defendant can be permitted to use the leased property either movable or immovable on terms and conditions to be settled. 17. In Kerr on the Law and Practice as to Receivers and Administrators, seventeenth edition, it is observed that the right of appointment of a receiver is one of the rights which accrue to an equitable mortgagee, whose security has become enforceable, as one of the steps in realisation. The receiver is appointed at the instance of an equitable incumbrancer if the principal has become payable or if there is reason to apprehend that the property is in peril or insufficient to pay the charges on it. In respect of legal mortgages, the appointment of a receiver is not as a matter of course and the court has a discretion in the matter, but where an action for foreclosure is pending, the court should usually appoint a receiver at the instance of the legal mortgagee and should do so on an interlocutory motion where the mortgagor is in possession. Possession is usually directed to be given to the receiver but the mortgagor is allowed to continue as agent of the receiver. The principles set out in Kerr on the law and Practice as to Receivers and Administrators are correct and should be followed in the actions instituted by banks and financial institutions. 18. For the reasons recorded hereinabove, we are in agreement with the view of the Division Bench in Podar Mills Ltd. v. State Bank of India , and we overrule the judgment in B. D. A. Ltd. v. Central Bank of India, . The appeal now to be placed before the appropriate Division Bench for final disposal.