HIGH COURT OF GUJARAT

PATEL DAHYABHAI RAMJIBHAI
Versus
MANAGER, RANUJ NAGRIK SAHAKARI BANK LTD AND ORS

Date of Decision: 12 January 2010

Citation: 2010 LawSuit(Guj) 207

Hon'ble Judges: Jayant Patel

Eq. Citations: 2010 AIR(Guj) 54, 2010 3 GLR 2339, **2010 2 GLH 1**, 2010 3 BankCas 641

Case Type: Spl Civil Appln

Case No: 13181 of 2004 and 16879 of 2005

Subject: Civil

Editor's Note:
(A) Securitisation & Reconstruction of Financial Assests & Enforcement of Security Interest Act, 2002 - Sec. 17 - Provincial Insolvency Act, 1920 - Sec.61 - Gujarat Co-Operative Societies Act,1961 - Secs. 101 & 103 - Transfer of Property Act, 1882 - Secs. 58(f) & 68 - The property of the deceased, who was the principal borrower, which has been sold by the receiver under the provisions of the Provincial Insolvency Act was mortgage with the respondent-Bank. - Therefore, proceedings on the basis that there was valid mortgage in favour of the Bank executed by the deceased pertaining to the property, which has subsequently vested to the legal heirs of the deceased, the resultant effect would be that the insolvents were holding the property subject to the right of the mortgagee. - Even if the property is held by the insolvent, but once the mortgage is proved, such property would be available to the extent minus the rights of the mortgagee in the property as available under the T.P.Act. - The Bank in the capacity as secured creditor was entitled to have the payment of its outstanding amount of the Award of the Nominee from the money realized by sale of property & the balance, if any, available could be distributed amongst other debtors which may include the decree-holder

(B) Provincial Insolvency Act, 1920 - Sec.61 - Gujarat Co-Operative Societies

Act,1961 - Secs. 101 & 103 - Transfer of Property Act, 1882 - Secs. 58(f) & 68 - The councel appearing for the creditors contended that the decree in favour of the creditors was earlier than the decree by the Nominee in favour of the Bank. - Held. - The claim of the petitioner as mere decree-holder could not be said as marching over the claim of the secured creditor. - Hence, the said contention cannot be accepted

(C) Securitisation & Reconstruction of Financial Assests & Enforcement of Security Interest Act, 2002 - Sec. 17 - Gujarat Co-Operative Societies Act,1961 - Secs. 101 & 103 - In absence of any security interest created in favour of the Bank by the petitioners, the Bank could not have resorted to the provisions of the Securitization Act. - The Bank will still remain as the judgment-creditor under the Award & the recovery may be effected as per the provisions of the Gujarat Co-Operative Societies Act read with the Rules & such may extend to the stay against transfer of properties to the petitioner in accordance with law

Acts Referred:
Provincial Insolvency Act, 1920 Sec 61
Insolvency Act, 1955 Sec 41, Sec 60

Final Decision: Petition allowed

Advocates: Gaurang H Bhatt, J A Adeshara, Mehul Sharad Shah, R C Jani

Cases Referred in (+): 1

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[1] The short facts of the case appear to be that both the petitioners are the guarantors to the transaction of loan given by one Ranuj Nagrik Sahakari Bank Ltd. (hereinafter referred to as 'the bank' for the sake of convenience) to one Naranbhai Govindbhai Patel for the principal amount of Rs. 3 lacs. As per the petitioners, the house of Naranbhai Govindbhai Patel situated at 9 Rameshwar Society, Mahesana was mortgaged in favour of the bank at the time when the transaction of loan was entered into and both the petitioners stood as the guarantor. The said Naranbhai had expired but the amount of loan was not fully paid, therefore Lavad Suit No. 726 of 2001 was preferred by the respondent bank for the amount of Rs. 3,18,639 with the interest and in the said suit the award was passed on January 30, 2001. It appears that there were other creditors also and therefore the wife of the deceased Naranbhai Govindbhai Patel filed Insolvency Petition No. 7 of 2001 before the learned Civil Judge (S.D.) Mahesana and in the said insolvency proceedings the receiver was appointed and the house which was mortgaged with the respondent bank also came to be sold by the receiver and the

amount realized was of Rs. 8,01,000/-. It appears that the respondent bank submitted an application for disbursement of the payment on priority basis as the house was mortgaged with it. However, the other creditors who were holding decree in their favour for recovery of the amount resisted the same. The learned Civil Judge in the proceedings of insolvency petition ultimately passed the order on 21.01.2004 whereby he ordered for proportionate distribution of the amount amongst all creditors including the respondent bank and the said order is one of the basis for approaching before this Court by the present petitions.

[2] As per the petitioners in respect to the decree which was passed in the proceedings of Summary Suit in favour of the other creditors against the legal heirs of deceased Naranbhai G. Patel as was ex parte the matter was carried in appeal before this Court being First Appeal No. 4042 of 2001 and in the said proceedings of the appeal, on 07.09.2001, the Division Bench of this Court in Civil Application No. 9823 of 2001 in First Appeal No. 4042 of 2001 granted stay of execution of the decree on condition to deposit the entire amount in the trial Court together with the cost and the interest within 8 weeks. It was also observed that as and when such is deposited by the respondent original plaintiff shall be at the liberty to withdraw the same by furnishing security to the satisfaction of the trial Court. It appears that the First Appeal No. 4042 of 2001 is still pending but as stated by the learned Counsel for the petitioner it has been transferred to the District Court on account of the enhancement of the jurisdiction of the District Court for entertainment of the appeal. As the Civil Court in the proceedings of insolvency, ordered for proportionate distribution, the bank could realize the amount of Rs. 1,98,810/-. But, as the bank was holding the award in its favour including against the petitioners who were guarantors, it appears that the notice has been issued under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (hereinafter referred to as 'the Securitization Act' for short) qua the immovable property of the petitioners for attachment. The perusal of the said notice further shows that the same is based on the earlier notice dated 5-10-2004 which has been issued under the Gujarat Cooperative Societies Act read with Rules 96 to 133 and also under the Securitization Act for the attachment of the said property. It is under these circumstances both the petitioners have approached to this Court by the present petitions.

[3] I have heard Mr. Mehul S. Shah as well as Mr. R.C. Jani for the respective petitioners and Mr. Gaurang Bhatt for the respondent bank and Mr. Adeshra is also heard.

[4] Two aspects deserve to be examined in the present proceedings. One is the priority for payment to a secured creditor by the Insolvency Court at the time of

distribution or disbursement; and the second is the exercise of the powers by the bank against the personal properties of the petitioners under the Securitization Act.

[5] In order to verify the factual aspect as to whether the property was mortgaged with the respondent bank by way of equitable mortgage or otherwise. Mr. Bhatt, learned Counsel for the respondent bank has placed on record the copy of the equitable mortgage executed by the deceased Patel Naranbhai Govindbhai in favour of the bank for deposit of the title deeds for creating equitable mortgage in connection with the transaction of loan of Rs. 3 lacs. Therefore, it appears that the property of the deceased Patel Naranbhai Govindbhai, who was the principal borrower, which has been sold by the receiver under the provisions of the Provincial Insolvency Act (hereinafter referred to as the Insolvency Act) was mortgaged with the respondent bank.

[6] Had it been a case of two creditors claiming the amount on the basis of the priority and proportionate distribution, it may stand on different footing. However, it appears that in the present case the bank put forward the claim as mortgagee of the property coupled with the circumstance of having award passed by the learned Nominee in its favour. It appears that the learned Civil Judge exercising the powers under the Insolvency Court Act has not examined the priority for claiming payment by the mortgagee under the Transfer of Properties Act and has only referred to the provision of Sections 41 and 60 of the Insolvency Act which also appears to be a typographical error inasmuch as Section 41 refers to the discharge whereas Section 60 refers to special provision regards immovable property. But, the discussion made by the learned Judge in the impugned order is on the basis of the contents of the provisions of Section 61 of the Insolvency Act.

[7] The relevant aspect in the present case is that whenever any property of the person who is declared insolvent is taken over by the Receiver or the officer of the Court appointed for such purpose, the same would be available to the extent of the interest held by the insolvent in such property. If the rights of any third party exists in the property or a bar or a clog is operating over the title of the insolvent in such property, such would be required to be taken care of by the Court at the time when the money is to be appropriated. As per the provisions of the Transfer of Properties Act, once a mortgage is created by any person in favour of the mortgagee, interest in the property to that extent is created and the rights of the owner in the property to that extent shall vest with the mortgagee subject to the provisions of the Transfer of Properties Act. If such insolvent who is mortgagor has to sell the property, he will have the rights to sell the property subject to the mortgage or the rights of the mortgagee and such rights in the property to that extent would be available to the Insolvency Court for realization of the property of the insolvent unless the transaction of such mortgage is declared as fraudulent or void or set aside by the Insolvency Court in such

proceedings. It is not the case of any parties to the proceedings that the transaction of mortgage was by way of fraud or the transaction was fraudulent or void or otherwise. Therefore, proceedings on the basis that there was valid mortgage in favour of the bank executed by the deceased pertaining to the property, which has subsequently vested to the legal heirs of the deceased, the resultant effect would be that the insolvents were holding the property subject to the rights of the mortgagee. Under such situation, the Receiver though might have taken possession of the property and though might have sold the property of the insolvents, the money available for distribution as per the provisions of Section 61 would be after satisfying the encumbrances or the rights of the mortgagee to the extent created in the property prior to the requisite period for which the bar operates against the insolvent and in any case on the date when the person is declared insolvent and his property is taken over by the Receiver of the Insolvency Court.

[8] The aforesaid appears to be the position as per the Transfer of Properties Act and for the rights in the property of the insolvent. If the provisions of Section 61 is examined in light of the aforesaid position of law, to be considered as per the provisions of Transfer of Properties Act, it would appear that the distribution of the property as provided under Section 61 on the basis of the priority of the debt is to be considered qua the absolute property or qua the rights under the Transfer of Properties Act. To say in other words, even if the property is held by the insolvent, but once the mortgage is proved, such property would be available to the extent minus the rights of the mortgagee in the property as available under the Transfer of Properties Act. Further, the pertinent aspect is that Section 61 of the Provincial Insolvency Act is not with a non-obstacle clause or the legislature did not intend to have the overriding effect over any other law for the time being in force which may include Transfer of Properties Act. Therefore, in view of the aforesaid position, the question of priority in payment would be required to be considered from the money realised of the property of the insolvent minus the rights of the mortgage in such property. As such, the interest created in favour of the mortgagee by the insolvent prior to the declaration as insolvent unless the transaction is held to be fraudulent or void, voidable, cannot be equated with the word debts fully. The mortgagee is having a secured interest in the property and the amount payable by the insolvent to the mortgagee cannot be only termed as debt. But the rights are additionally available to the mortgagee having created secured interest for which the property as per the provisions of the Transfer of Properties Act. Therefore, the net effect of the aforesaid is that the amount recoverable by such mortgagee will be above the priority contemplated under Section 61 of the Insolvency Act.

[9] At this stage, the reference may be made to the provisions contained in the Companies Act, 1956, for availability of the rights of the secured creditors as per the provisions of Section 529 and over the preferential payments available under Section 530. This Court in the case of Textile Labour Association v. The Official Liquidator of Rajpur Mills Ltd.,2010 CLC 267 (in Lqn.) in Company Application No. 358/08 and allied matters, decided on 4-8-2009 reported in, 2010 CLC 267, the debt of the workers in addition to the pari passu and if yes, to what extent, at para 7 in the said decision observed thus--

> Therefore, it appears that as per Section 529, rights of secured and unsecured creditors as in force for the time being under the law of insolvency with respect to the estates of persons adjudged insolvent, are required to be observed. If the matter is considered for the respective rights of the secured creditors, they would be entitled to foreclosure of the mortgage and the Company in liquidation would be entitled to redemption of the mortgage by payment of the full amount. It is by now well settled that the rights of the secured creditor would stand above the rights of the preferential creditors under Section 530 as well as unsecured creditors. It is only by way of statutory provision of Section 529A of the Act which begins with the non-obstante clause, the workers' dues are to be treated at par with the secured creditors and for such pari passu payment, the debts of the workers' dues and all the secured creditors as per Section 529A of the Act are given priority above all other debts. It is not in dispute that the debt under Section 529A of the Act are not satisfied. Therefore, in the present group of matters, the Court may not be required to examine the aspects of priority of the workers' dues and secured creditors under Section 529A of the Act over the other debts falling in the category of Section 530 of the Act and also of other unsecured creditors. It appears from the conjoint reading of Section 529 read with Section 529A of the Act that Section 529A is carving out an exception to the rights of secured and unsecured creditors under Section 529. Therefore, if the provisions of Section 529A of the Act is to be implemented, Section 529 would not operate as a bar. However, after the satisfaction of the debts under Section 529A of the Act, the effect is required to be given to the provisions of Section 529 of the Act. As observed earlier, Section 529 of the Act saves the rights of the secured and unsecured creditors as are for the time being in force. To say in other words, the rights of the secured creditors are above the unsecured creditors as they have interest in the property of the Company in liquidation for which the security is created. It is only between the rights of secured and unsecured creditors. Section 530 may have role to play for preferential payment amongst the unsecured creditors. Therefore, the creditors who may fall in the category of secured creditors would be to the extent of their security, above the creditors falling under Section 530 of the Act and other

unsecured creditors. Therefore, it appears that if on account of the implementation of the provisions of Section 529A of the Act, if the secured creditors have not been able to realise the full money from their security, after payment to the workers at pari passu, if the surplus/balance amount remains, which is realised from the security of the secured creditors the same may be claimed by the secured creditors in the capacity as secured creditors who otherwise could not recover the amount from their security in view of the provisions of Section 529A of the Act. To say in other words, if the secured creditors have to recover the amount of Rs. 100/- for satisfying their outstanding dues and on account of the inclusion of the claim of the workers for pari passu payment under Section 529A, they have received lesser amount, such amount would be available to the secured creditors, provided there is surplus/ balance after compliance to the provisions of Section 529A of the Act and such remaining amount is a part of the amount realised from their security. Therefore, the first question shall stand answered accordingly. The aforesaid shall hold good for realisation of the amount by the secured creditor upto the date of winding up of the Company in liquidation.

[10] Therefore, in view of the aforesaid observations and discussions, the conclusion would be that the Bank in the capacity as secured creditor was entitled to have the payment of its outstanding amount of the Award of the learned Nominee from the money realised by sale of the property and the balance, if any, available could be distributed amongst other debtors which may include the decree holder who are respondents in the present proceedings, but the premise on the basis of which the learned Judge has passed the order of not at all considering the claim of the priority for availability of the payment to the secured creditor who is Bank in the present case, could be said to be an error apparent on the face of the record committed by the learned Civil Judge in the Insolvency Proceedings. It was required for the learned Judge to consider the aforesaid aspects and to make the fund available for satisfaction of the interest of the secured creditor who is Bank in the present case and thereafter, the balance if any available could be distributed amongst the other creditors, which includes the creditor holding decree who are respondents in the present case.

[11] Mr. Adeshra, learned Counsel appearing for the creditors holding decree in their favour contended that the decree in favour of his client was earlier than the decree by the learned Nominee in favour of the Bank. He therefore submitted that the debt of his client who were decree holder would stand above the amount recoverable by the Bank as the secured creditor.

[12] I am afraid such contention can be accepted on the face of the mortgage executed in favour of the Bank and the status of the Bank having been found as that of the secured creditor. It may be that such secured creditor, if not holding the award or

the decree, the amount may not be crystallised at the relevant point of time, but it is not possible to accept the contention that such recoverable by the secured creditor would be after the satisfaction of the decree holder who hold no interest in the property by creation of mortgage or otherwise. In any case, when the learned Judge passed the order for distribution, the amount recoverable by the respondent Bank in capacity as secured creditor stood crystallised. Therefore, when such amount was already crystallised, to be termed as the interest of the secured creditor on the date when the learned Judge passed the order, the other aspects would not assume much importance. The only observation deserves to be made is that on such contention, the claim of the petitioner as mere decree holder could not be said as marching over the claim of the secured creditor. Hence, the said contention cannot be accepted.

[13] Mr. Adeshra. learned Counsel for such decree holders contended that in the event this Court takes the view that the secured creditor could claim amount first in comparison to the decree holder who are his clients, the question of liability of interest for the period on which the payment has been received by them till it is redeposited, may not arise since such persons were holding decree in their favour and had to recover the amount from the insolvents. He also contended that the Bank did not challenge the order of the learned Judge for distribution of the amount to the decree holder by not accepting the claim as secured creditor having a priority in payment.

[14] In my view, such aspects as was not before the Court below nor is required to be considered at this stage in the present proceedings and the said aspect as such, may be in the realm of restitution, if ultimately, any benefit is enjoyed by any parties to the proceedings. Hence, no further observations deserves to be made in this regard.

[15] The next aspect deserves to be considered is the action by the Bank under the Securitization Act qua the properties of the petitioners who are guarantors of the loan transaction.

[16] It appears that the respondent Bank has not been able to show this Court that any of the petitioners who stood as the guarantor to the loan transaction had executed any equitable mortgage in favour of the Bank. Under these circumstances, in absence of any security interest created in favour of the Bank by the petitioners, the Bank could not have resorted to the provisions of the Securitization Act. Consequentially, the action of the Bank under the Securitization Act cannot be said as with the authority under the law and can rather be said as ultra vires to the provisions of the Act and the action under the Securitization Act qua the properties of the petitioner could be said as illegal and without there being any authority under the Act.

[17] However, it would not be a case where the Bank will have no remedy available for recovery of the amount from the petitioners in capacity as the guarantor even if the action of the Bank is found as not authorised under the Securitization Act. The bank will still remain as the judgment creditor under the Award and the recovery may be effected as per the provisions of the Gujarat Cooperative Societies Act read with the Rules and such may extend to the stay against transfer of properties to the petitioner in accordance with law. But, at the same time, it deserves to be recorded that it would be dependent upon the amount as may be realised by the Bank as the secured creditor from the property of the insolvent, which has been sold by the receiver in the insolvency proceedings and the balance amount, if any, if could not be recovered by the respondent Bank so as to satisfy the Award of the Nominee, could be recovered by the Bank from the petitioners under the Co-operative Societies Act read with Rules. As in the present case, the action taken by the Bank is under the Securitization Act, as per the second notice dated 20-10-2004, the same can be said as illegal, but the order for attachment of the property to the extent under the Gujarat Cooperative Societies Act could not be said as without any authority in law since the proceedings are yet to be finalised on the said aspects, and as observed earlier, is also dependent upon the final recovery may be made available to the Bank in capacity as secured creditor from the insolvency proceedings, no further observations deserve to be made in this regard.

[18] In view of the aforesaid, the concerned impugned orders dated 21-1-2004 passed by the learned Civil Judge in the proceedings of Insolvency Applications Nos. 7/01 below Exh. 68, 76 and 85 (common order) is quashed and set aside with the direction to the learned Judge to consider the applications in light of the observations made hereinabove in the present judgment and shall pass appropriate orders. The prayer of the petitioners to quash and set aside the action of the Bank for recovery of the amount under the Securitization Act is granted, but with the observation that the Bank may exercise the power for recovery of the amount in accordance with law under the provisions of the Gujarat Co-operative Societies Act read with the relevant Rules.

[19] The petitions are allowed to the aforesaid extent. Rule made absolute accordingly.

No order as to costs.