HON'BLE SRI JUSTICE A.RAJASHEKER REDDY

WRIT PETITION No.6967 OF 2003

ORDER:

The case of the petitioner is that he is the owner of the house and a plot bearing No.76 in Sy.No.590 admeasuring 375 sq.yards situated at Malkajgiri, Secunderabad and on the request of the 1st respondent, the petitioner offered collateral security for the amount sanctioned and disbursed in favour of the 1st respondent by the 2nd respondent and stood surety for the said amount. After the death of his wife in an accident while coming from Tirupati in a car, the petitioner was also down in bed for long period and in the meanwhile the petitioner's daughter got a medical seat at Nepal and he was shuttling from Hyderabad to Nepal. In spite of all these, the petitioner was in touch with the 1st respondent and always pressing him to clear off the loan taken from the 2nd respondent. While so, when the petitioner came to know that the 1st respondent did not clear off the loan and the 2nd respondent has already sold the plant and machinery and recovered a sum of Rs.7-00 lacs, he gave a representation dated 24.03.2003 seeking time to pay the loan amount. As he did not receive any communication, he approached the 2nd respondent on 31.03.2003 and the 2nd respondent informed the petitioner that the property was already sold on 29.03.2003. Thereafter on 10.04.2003, the petitioner received information from the 2nd respondent that the subject property was sold for Rs.3.65 lacs. The petitioner submits that he has not received any notice of sale from the 2nd respondent prior to confirmation of sale except the paper publication. In spite of giving a representation to the 2nd respondent seeking time to clear off the loan amount, the auction was held by the 2nd respondent on 29.03.2003 only to cause loss to the petitioner. Further, it is stated that the petitioner has no other property except the subject property and value of the same is more than Rs.10 lacs. Challenging the auction held on 29.03.2003, the present writ petition is filed.

Counter affidavit is filed by the 2nd respondent stating that writ petition itself is not maintainable in view of the judgment reported in ***Haryana Financial Corportion and another vs. M/s. Jagadamba Oil Mills and another[1].*** It is also stated that respondent Corporation sanctioned a term loan of Rs.10 lacs and additional loan of Rs.2.82 lacs in favour of M/S. Maruthi Dairy Products on 29.09.1994 and 04.10.1995 respectively for setting up a milk processing unit in a leasehold premises which consists of the 1st respondent and Smt T.Bhavani. The term loan was duly secured by primary security and also by the provision of collateral security of immovable property furnished by the loanee. The petitioner has offered the subject property as collateral security to enable the firm to avail the loan and executed a loan security document by way of depositing the title deeds. The respondent Corporation in terms of the loan security documents executed by the petitioner has proceeded to auction the collateral security offered by the petitioner towards arrears due and payable by the 1st respondent by serving the registered notice dated 04.03.1997 on the petitioner. Since the petitioner failed to respond to the

[1] AIR 2002 SC 834

same, the respondent Corporation published six advertisements offering the properties for sale by way of publication in various newspapers. In response to the advertisement released on 24.02.2002, the offer was received from one Sri S.V.Sudershan and others for Rs.3.65 lacs and the same was accepted on 29.03.2003 and possession was handed over to the purchaser duly exercising the power under Section 29 of the State Financial Corporations Act, 1951 (for short 'the Act'). In pursuant to the letter dated 24.03.2003 remitted by the petitioner, the respondent Corporation submits that it has informed the petitioner on 29.03.2003 about the sale of the subject property and sought for dismissal of the writ petition.

Counter affidavit is also filed by the 3rd respondent stating that in pursuant to the paper publication issued by the 2nd respondent on 24.02.2003 in respect of the subject property, he offered to purchase the same for a price of Rs.3,65,000/- by tender dated 20.03.2003. He also submits that 2nd respondent has confirmed the sale after taking all necessary steps and by following the procedure established under law, as such there is no violation of principles of natural justice as alleged by the petitioner and sought for dismissal of the writ petition.

Learned counsel for the petitioner submits that since the petitioner stood as surety and offered his property as collateral security for due performance and observing all terms and conditions in connection with additional term loan sanctioned in favour of the 1st respondent, the 2nd respondent cannot invoke Section 29 of the Act. He also submits that Section 29 of the Act can be invoked only against the principal debtor but not against the surety. In support of his contentions, he relied on judgment reported in ***Karnataka State Financial Corporation vs. N.Narasimahaiah and Others***[2]**.** He also submits that the petitioner was not issued notice before conducting auction, as such the said auction has to be set aside.

On the other hand, the learned counsel appearing for the 2nd respondent submits that the 1st respondent offered the property of the petitioner as collateral security for repayment of the loan, as such the respondents have proceeded for auction under Section 29 of the Act. He also submits that the petitioner has executed a loan security document to show that petitioner has stood as surety for repayment of loan advanced to M/s.Maruti Dairy Products. Since the surety bond is executed, it cannot be said that the respondent Corporation has no power to invoke Section 29 of the Act.

Learned counsel for the 3rd respondent submits that after the writ petition is dismissed, sale deeds were executed in favour of the 3rd respondent. Subsequently, since the writ petition is restored and that he invested the amounts for purchase of the property through auction held by the 2nd respondent, as such the same cannot be interfered with.

Section 126 of The Indian Contract Act, 1872 reads as follows:

> **Contract of guarantee', 'surety', 'principal debtor' and 'creditor'**- A 'contract of guarantee' is a contract to perform the promise, or discharge the liability, of a third person in case of his

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[2] (2008) 5 SCC 176

default. The person who gives the guarantee is called the 'surety'; the person in respect of whose default the guarantee is given is call the 'principal debtor', and the person to whom the guarantee is given is called the 'creditor'. A guarantee may be either oral or written.

Section 29 of the Act reads as follows:

"Rights of Financial Corporation in case of default: (1) Where any industrial concern, which is under a liability to the Financial Corporation under an agreement, makes any default in repayment of any loan or advance or any installment thereof [or in meeting its obligations in relation to any guarantee given by the Corporation] or otherwise fails to comply with the terms of its agreement with the Financial Corporation, the Financial Corporation shall have the [right to take over the management or possession or both of the industrial concerns], as well as the [right to transfer by way of lease or sale) and realize the property pledged, mortgaged, hypothecated or assigned to the Financial Corporation."

Xerox copy of the notice dated 04.03.1997 issued to the petitioner was placed before this Court. Further the document said to have been executed by the petitioner on 26.10.1995 is also placed before this Court which reads as follows:

"Managing Director,
A.P.State Financial Corporation
Hyderabad

Dear Sir

Memorandum of deposit of title deeds in respect of Free hold/lease hold interest in residential premises of mud walls on A.C. sheets roof bearing Municipal House No.45-92/76 in dilapidated condition on Plot No.76 in S.No.590, admeasuring 375 sq.yards, N.M.D.C.Colony, Malkajgiri Municipality, R.R.Distrcit

Vemuri Laxminarayana Sastry, S/o. Surya Narayana, Aged about 41 years H.M.45-92/1, N.M.D.C.Colony, Malkajgiri, Hyderabad, R.R.District, hereby confirm having deposited with you the undernoted documents of title relating to the properties described above, owned and possessed by me/us for the due performance and observance of all terms and conditions in connection with Addition Term Loan of Rs.2.82 lakhs sanctioned to Maruti Dairy Products for the acquisition of land, construction of buildings and acquisition of machinery and I/we confirm that the following documents will be available to you by way of collateral security for recovery of any amounts due there under from M/s. Maruti Dairy Products to you I/we further declare that I/We have no other documents of title to the said properties and the said properties have not at any time been dealt with any manner prejudicial to your interest in the matter of the above loan

LIST OF DOCUMENTS

1. Regd. Sale Deed, dated 22.01.1993 executed by N.Mallesh in favour of V.L.N.Sastry.
2. E.C.4336/94
3. Ownership certificate from Municipality

Signed and Delivered by
Sd/-
SRI V.L.N.SASTRY

Date:26.10.1995
Place:Hyderabad."

In ***Karnataka State Financial Corporation vs. N.Narasimahaiah and Others***[3] while interpreting Section 29 and 31 of the Act, Apex Court held as follows:

> **20.** Section 29 of the Act nowhere states that the corporation can proceed against the surety even if some properties are mortgaged or hypothecated by it. The right of the financial corporation in terms of Section 29 of the Act must be exercised only on a defaulting party. There cannot be any default as is envisaged in Section 29 by a surety or a guarantor. The liabilities of a surety or the guarantor to repay the loan of the principal debtor arises only when a default is made by the latter.
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> **21.** The words "as well as" in our opinion play a significant role. They confer two different rights but such rights are to be enforced against the same person viz. the industrial concern. Submission of the learned senior counsel that the second part of Section 29 having not referred to "industrial concern" any property pledged, mortgaged, hypothecated or

[3] (2008) 5 SCC 176

assigned to the financial corporation can be sold, in our opinion cannot be accepted. It is true that sub section (1) of Section 29 speaks of the guarantee. But such a guarantee is meant to be furnished by the corporation in favour of a third party for the benefit of the industrial concern. It does not speak about a surety or guarantee given in favour of the corporation for the benefit of the industrial concern.

22. The legislative object and intent becomes furthermore clear as in terms of sub-section (4) of Section 29 of the Act only when a property is sold, the manner in which the sale proceeds is to be appropriated has categorically been provided therein. It is significant to notice that sub-section (4) of Section 29 of the Act which lays down appropriation of the sale proceeds only refers to "industrial concern" and not a "surety" or "guarantor".

37. The legislative intent, in our opinion, is manifest. The intention of Parliament in enacting Sections 29 and 31 of the Act was not similar. Whereas Section 29 of the Act consists of the property of the industrial concern, Section 31 takes within its sweep both the property of the industrial concern and as that of the surety. None of the provisions control each other. Parliament intended to provide an additional remedy for recovery of the amount in favour of the Corporation by proceeding against a surety only in terms of Section 31 of the Act and not under Section 29 thereof."

A reading of the document dated 26.10.1995 clearly shows that petitioner offered his property as security for repayment of loan advanced to M/s.Maruti Dairy Products in which the 1st respondent is the partner and the said document also refers to the loan sanctioned to the 1st respondent, as such the said document definitely attracts the definition of the guarantee and the petitioner falls within the definition of surety as defined under Section 126 of Indian Contract Act.

The Apex Court in the judgment referred to above held that Section 29 of the Act refers to the property of the industrial concern, whereas Section 31 takes within its sweep both the property of the industrial concern and as that of the surety.

In view of the above, I am of the opinion that Section 29 of the Act cannot be invoked against the petitioner who is surety.

Accordingly, the writ petition is allowed and all consequential proceedings are set aside. However, this will not preclude the 2nd respondent from initiating proceedings under Section 31 of the Act. No costs.

As a sequel to the disposal of this petition, miscellaneous petitions, if any, pending shall stand closed.

A.RAJASHEKER REDDY,J

08-12-2016
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