

(2004) 10 PAT CK 0023
In the Patna High Court
Case No : LPA No. 1210 of 2002

Bihar State Co-operative Bank Ltd. and Another	APPELLANT
Vs	
Shri Nareshwar Prasad	RESPONDENT

Date of Decision : 12-10-2004

Acts Referred:

Citation : (2004) 10 PAT CK 0023

Final Decision : Dismissed

Judgement

R.S. Garg, J.—This Appeal under Clause 10 of the Letters Patent is filed by the Bihar State Co-operative Bank Limited and another being aggrieved by the order dated 31.7.2002 passed in CWJC No. 3170 of 2001 whereunder the learned Single Judge allowed the Writ Petition filed by the writ petitioner and the appellant stands directed to pay to the original petitioner the amounts of three advances, amounting to Rs. 40,000/- and odd.

2. The writ petitioner Nareshwar Prasad filed a Writ Petition under Article 226 of the Constitution of India seeking a command against the respondents to make payment of entire amount of leave encashment and a further direction to the original respondents to pay interest on the deducted amount of leave encashment at the market rate from the date of retirement of the petitioner and a declaration in his favour that he is entitled to full amount of leave encashment.

3. The facts leading to the present dispute are that the original writ petitioner was appointed on 11.10.1965 as an Inspecting Officer in the Bihar State Co-operative Bank Ltd. and after serving the Institution for almost 34 years he stood retired on 31.1.2000 from the post of Deputy General Manager (Accounts). According to the petitioner though he was entitled to an amount of Rs. 1,58,443.76 towards leave encashment but to his shock and surprise he found that an amount of Rs. 94,875.65 only have been credited to his account and on his enquiries he was informed that the said amount has been credited in full and final settlement of his leave encashment and, as such a sum of Rs. 63,568.10 was deducted from the aforereferred amount. The writ petitioner thereafter

made a representation to the respondents on 15.12.2000 but the respondents did not respond to it. The petitioner thereafter sent a reminder but that was not replied. According to the petitioner, before deducting the amount of Rs. 63,568.10 for any good, bad or indifferent reason neither a notice to show cause was issued to him nor any reason was furnished to him for making such a deduction/cut into his entitlement. The petitioner in the aforesaid premises came to this Court with the prayer that he be held entitled to full amount under leave encashment, the respondents be asked to make full payment with interest from the date the petitioner was entitled to his salary.

4. On notice, the Respondent-Bank (now appellant) submitted its counter and took the plea that the writ petition deserves to be dismissed on the ground of suppression of material facts to the effect that petitioner-respondent stood guarantor in three Overdraft Accounts at Bankipur Branch of the Bank and due to the default of borrowers/original debtors in depositing outstanding dues, the amount has been realised from the petitioner from the leave encashment amount as the petitioner-respondent was a guarantor. It is submitted by the Bank that the overdraft facility was sanctioned on the recommendations of the Branch Manager on his personal responsibility to recover the dues in time and he also undertook that in case of default by the borrower the Manager/Petitioner in his capacity as guarantor can be held personally responsible. It is also the case of the Bank that the petitioner failed to recover the said amount and as the original debtors/ borrowers did not deposit the amount, the Bank was entitled to recover the same from the amounts to which the petitioner was entitled. It is submitted by them that most of the Officers and staff of the Co-operative Bank stood guarantors for the overdraft facilities which could be allowed in favour of their friends/close relatives. Such overdraft facilities are sanctioned on the recommendations of the Branch Manager with his personal responsibility to recover the dues in time and in case he fails to recover the dues in time and in case he fails to recover the amount such person who stands guarantor is to be held personally responsible. According to them, the petitioner stood guarantor in connection with three overdraft facilities, therefore, and certain other amounts, the detail of which are given in paragraph 12 of the counter affidavit, the Bank was absolutely justified in recovering the amount. It is submitted by them that petitioner was a guarantor in connection with the following accounts:--

(A) Sri Vishwa Mohan Prasad-A/C No. C/2243, Amount Due-Rs. 5457.01.

(B) Sri Swapanil Prasad-A/C No. C/2244, Amount Due-Rs. 7159.47.

(C) Sri Nil Ratna-A/C No. H/436, Amount Due-27.491.40.

5. According to them, if the amount otherwise also due is added to these three overdraft accounts, the Bank was justified in deducting Rs. 63,568.10. It is submitted that a sum of Rs. 19,013 which was deducted towards provident fund deduction has been refunded to the petitioner. On 27.4.2001. It is the submission of the Bank that in a meeting wherein the Branch Managers were

directed to take steps for recovering all overdraft amounts from the borrowers/debtors/defaulters, the petitioner was also asked to recover the amount but the petitioner did not do anything. They have also relied upon letter No. 192 dated 16.5.1998 to submit that the Bank has issued the aforesaid letter to the Branch Managers informing them that if the outstanding amount towards the loan amount is not recovered then the same would be recovered from the employees/officers of the Bank, who stood guarantors. It is submitted by them that in overdraft sanctioned advice it was specifically mentioned as a condition that overdraft facility had been extended to the borrower on the recommendation of the Branch Manager and it would be the personal responsibility of the Branch Manager/Guarantor to recover the dues in time. According to them, the petitioner being a defaulter in his capacity as guarantor the Bank was absolutely justified in adjusting the loan amount outstanding against the borrowers/defaulters and the petitioner was not entitled to any benefits.

6. After hearing learned counsel for the parties, relying upon a Single Bench judgment dated 21.4.2000 delivered in the matter of Md. Mahmoodul Haque Mallick v. The Bihar State Co-operative Bank Ltd. and Ors. CWJC No. 5962/1999, the learned Single Judge observed that the Bank could not adjust the amount of leave encashment towards the loan account wherein the petitioner stood a guarantor. The teamed Single Judge also observed that equity and good conscience required that the Bank should take action against both, the principal debtor as well as the guarantor. The learned Single Judge was of the opinion that if such an action is taken it would ensure that if the guarantor has any objection he may take his defence in accordance with law. The learned Single Judge was of the opinion that by not taking any action against the principal debtor the Bank, in the facts of the case, made its impugned action arbitrary and fit for interference. The learned Judge accordingly directed refund of a sum of Rs. 40,000/- and odd at its earliest. Being aggrieved by the said judgment, the Bank is before this Court in this appeal.

7. Learned counsel for the Appellant-Bank submitted that in case a particular person stands a guarantor in relation to a loan account/amount and there is a default on the part of the original debtor then the Bank has an option to proceed against either of them and even in a case where the action becomes time barred against the original debtor, the Bank if has to pay any amount to the borrower then the Bank would be entitled to adjust the said amount which is to be recovered from the borrower, from the amount to be paid to the guarantor. Learned counsel has also placed its strong reliance upon certain judgments of the Supreme Court which we shall refer in subsequent paragraphs of this judgment.

8. Learned counsel for the respondent-petitioner on the other hand submitted that if the action against the original borrower had become time barred then the liability of the guarantor which is coextensive and co-terminus with the liability of the original borrower/debtor would come to an end and in case he is required to make payment of the amount then it would become impossible for him to

recover the money from the original debtor/borrower because the amount paid by the employee guarantor was not legally payable by the original debtor on the date of adjustment as no action under law could be taken against the original debtor.

9. Section 126 of the Indian Contract Act defines "Contract of guarantee", "Surety", "Principal-debtor" and "Creditor". It says that a "contract of guarantee" is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the "surety"; the person in respect of whose default the guarantee is given is called the "principal-debtor", and the person to whom the guarantee is given is called the "creditor".

10. A guarantee is promise to answer for the payment of some debt, or the performance of some duty, in case of the failure of another party, who is in the first instance, liable to such payment or performance. A guarantee is an accessory contract by which the promisor undertakes to be answerable to the promise for the debt, default or miscarriage of another person, whose primary liability to the promisee must exist or be contemplated.

11. The word "debt, default or miscarriage" is descriptive of failure to perform legal obligations, existing or future, arising from any source, not only from contractual promises, but in any other factual situations capable of giving rise to legal obligations such as those resulting from bailment, tort or unsatisfied judgments.

12. A "contract of guarantee" covers three parties: the creditor, the surety and the principal-debtor. A contract of guarantee, therefore, involves a contract to which all those three parties are privy. Their express participation or implied assent to have such a contract must be proved by the person who wants to rely on it. The surety undertakes his obligation at the request express or implied of the principal-debtor.

13. At this stage we must observe that the Appellant-Bank has not produced the original documents to show or prove that the original writ petitioner stood guarantee in connection with those three accounts but as their assertion has not been denied by the writ petitioner by filing a rejoinder or a further affidavit, we shall presume that he in fact stood surety/guarantee in relation to those three accounts.

14. According to Section 127 of the Indian Contract Act, anything done, or any promise made, for the benefit of the Principal-debtor may be a sufficient consideration to the surety for giving the guarantee. The liability of the surety is co-extensive with that of the principal-debtor, unless it is otherwise provided by the contract.

15. Learned counsel for the Bank has placed his strong reliance upon a judgment of the Supreme Court in the matter of the Bank of Bihar Ltd. Vs. Dr. Damodar

Prasad and Another, . In the said matter, the Supreme Court has observed that u/s 128, save as provided in the contract, the liability of the surety is co-extensive with that of the principal-debtor. The surety becomes liable to pay the entire amount. His liability is immediate. It is not deferred until the creditor exhausts his remedies against the principal-debtor. In the absence of some special equity the surety has no right to restrain an action against him by the creditor on the ground that the principal is solvent or that the creditor may have relief against principal in some other proceedings. Likewise where the creditor has obtained a decree against the surety and the principal, the surety has no right to restrain execution against him until the creditor has exhausted his remedies against the principal. The Supreme Court further observed that in the matter in hand the plaintiff could obtain a decree against the surety and the principal-debtor. In the said matter, the plaintiff filed a suit and could obtain a decree against the principal-debtor so also against the surety with an embargo that plaintiff should be at liberty to enforce its dues against the surety only after exhausting its remedies against the principal debtor. The Supreme Court observed that direction for postponing the payment of decretal amount must be specific and must give sufficient reasons. It was further observed that the surety was duty bound to pay the decretal amount and on such payment he would be subrogated to the rights of the creditor u/s 140. The Apex Court was also of the opinion that such a direction would make the decree useless and would also make the surety useless. In the said matter, the creditor proceeded against the original debtor so also against the surety and in the joint action he could secure a decree against both. The Supreme Court was of the opinion that putting such a restriction on the right of the creditor would not be in accordance with law.

16. In the present matter it is to be seen that the Bank did never proceed against the original debtors within the period of limitation nor ever took any action against him within the time as prescribed under the law. The Bank even did not proceed against the surety within the period of limitation. In fact, the Bank all of a sudden abruptly of its own in a lopsided action adjusted the amount due under three loan accounts towards the leave encashment account. The said judgment in the matter of Bank of Bihar (supra), in our considered opinion, does not apply to the present case.

17. The word "co-extensive" is an adjective to the word "extent", and relates to the quantum of the principal debt. Section 128 only explains the quantum of surety's obligation when the terms of the contract do not limit it, as they often do, as against the validity of the obligation of the principal-debtor. A surety's liability depends upon the terms of his contract and he is entitled to insist on the strict adherence to the terms of his obligation by the creditor, and cannot be made liable for more than he has undertaken. Though in earlier paragraphs of this judgment we have observed that we would presume that the petitioner stood a guarantor but what were the terms of the guarantee are not known to anybody. The Bank which is supposed to possess all these official documents, for the reasons best known to it, has not produced the documents to apprise this

Court that what were the conditions appended to and agreed between the parties at the time of the agreement. In a case where the terms are not known to anybody then it cannot be said that the surety's liability would continue despite the liability of the original debtor has come to an end.

18. Limitation for filing a suit against a surety commences to run according to the terms of contract of guarantee. A debt of the surety is distinguished from that of the principal debtor. The limitation begins to run against the surety at the same time as against the principal debtor, depending upon the form of the contract entered into between the surety and the creditor, and whether or not the surety and the principal debtor are co-terminus. Section 128 is to be looked with the provisions of the Limitation Act and not in a manner so as to nullify its provisions limiting the time within which a suit must be brought after the accrual of the cause of action. Where a claim is time barred against the principal debtor, but not against the surety, the plaintiff is entitled to a decree against the surety. If the guarantee is a continuing guarantee then question of limitation would not arise against the surety so long as the Account is a levy account in the sense that it is not settled, and there is no refusal on the part of the guarantor to carry out the obligation. It is settled law that the right to recover the debt continues to exist notwithstanding that the remedy is barred by limitation. Though the remedy to recover the debt from the principal debtor may be barred by time, a creditor certainly can appropriate the accounts from the amounts which it has to pay to the surety.

19. Placing reliance upon the judgment of the Supreme Court in the matter of Punjab National Bank and others Vs. Surendra Prasad Sinha, it is submitted by the learned counsel for the Appellant-Bank that the amount which the Bank is required to pay to the surety, if is adjusted towards the money which the Bank has to recover from the debtor/surety and if such a process is allowed then the recovery cannot be held to be bad. In the matter of Punjab National Bank (Supra) the matter came before the Supreme Court in a case where process was issued against the Bank as the Bank had adjusted certain Fixed Deposit Receipts which were in its possession and which were also deposited by the guarantor by way of security. The surety filed a private complaint submitting, inter alia, that such adjustment was fraudulent and was with a criminal intention, therefore, the Bank officers be prosecuted. In the said case the Bank gave a loan of Rs. 15,000/- to one Sriman Narain Dubey on 5.5.1984 and the respondent and his wife Annapurna stood as guarantors, executed a security bond and handed over Fixed Deposit Receipts for a sum of Rs. 24,000/-, which would mature on 1st November, 1988. At the time of maturity its value would be Rs. 41,292/-, the principal debtor committed default in payment of the debt, on maturity of the FDRs. the Branch Manager adjusted a sum of Rs. 27,037.60 due and payable by the principal debtor as on December, 1988 and the balance sum was credited to the Savings Bank Account of the respondent. The original complainant alleged that the debt became barred by limitation as on May 5, 1987, the liability of the respondent being co-extensive with that of the principal debtor, his liability also

stood extinguished as on May 5, 1987. The respondent submitted that without taking any action to recover the amount from the principal debtor within the period of limitation, the Branch Manager could not have adjusted the amount and the total amount of Rs. 41,292/- at the time of maturity ought to have been refunded to the surety/ complainant. On these allegations it was submitted in the complaint that the Bank and its Officers criminally embezzled the said amount. The trial Court took cognizance of the matter and issued summons. The matter ultimately went to the Supreme Court. In the said matter, the Supreme Court observed that the rules of limitation are not meant to destroy the rights of the parties. Section 3 of the Limitation Act, 1963 (in short "The Act") only bars the remedies, but does not destroy the right which the remedy relates to. The right to the debt continues to exist notwithstanding the remedy is barred by limitation. Only exception in which the remedy also becomes barred by limitation, if the right is destroyed, the Supreme Court observed that except in such cases which are specially provided under the right to which remedy relates in other case the right subsists. Though the right to enforce the debt by judicial process is barred u/s 3 read with the relevant Article in the Schedule, the right to debt remains. The time barred debt does not cease to exist by reason of Section 3. The right can be exercised in any other manner than by means of a suit. The debt is not extinguished, but the remedy to enforce the liability is destroyed. The Supreme Court was of the opinion that such debt for which remedy has become barred under the Limitation Act continues to subsists so long as it is not paid. It is not obligatory to file a suit to recover the debt. It is settled law that the creditor would be entitled to adjust, from the payment of a sum by a debtor, towards the time barred debt. It is also equally settled law that the creditor when he is in possession of an adequate security, the debt due could be adjusted from the security in his possession and custody. The Supreme Court observed that as the original complainant and his wife stood guarantors to the principal-debtor, jointly executed the security bond and entrusted the FDR as security to adjust the outstanding debt from it at maturity though the remedy to recover the debt from the principal debtor was barred by limitation, the liability still subsist. The Supreme Court observed that again in terms of the contract express or implied is a negation of criminal breach of trust defined in Section 405 and punishable u/s 409 of the Indian Penal Code.

20. From the facts of the said case it would clearly appear that the original complainant and his wife stood guarantors in the matter and entrusted tow FDRs towards security. The Supreme Court was of the opinion that when certain amount or documents are handed over as security then even if the remedy against the principal debtor is barred by limitation under the Limitation Act, the right to recover from the security tendered by the guarantor or the surety is not lost. In the present matter undisputed the writ petitioner did not submit any documents or such valuable security towards security. He simply stood surety. He did not say at any point of time that from any amount which is payable to him in future the loan amount can be recovered. It is to be seen that on one side under

the commercial contract he stood a surety and on the other hand under a different contract he was working as an employee. The terms of contract of surety are to be seen in their true perspective and the contract of surety could not be mixed with the service contract. In a service contract, salary is to be paid to the employee monthly or as the terms are agreed. Certain leave encashments are to be given, provident fund is to be given and if the services are pensionable then pension is to be allowed in favour of such an employee. These are the consequences of service contract, these are the incidences of services, these have nothing to do with the commercial contract. However, we may not mean to say that even if an employee takes the loan then the said loan amount cannot be recovered from his salary. In such a case the loan is given to him because he is in the services and his being in services in itself is a guarantee of repayment of the loan. But in a case where an employee stands a guarantor then he stands as a guarantor in his personal capacity and not as an employee of the Bank. It is further to be seen that in the matter of Punjab National Bank (supra) the FDRs were entrusted and handed over to the Bank as security. The Bank was holder of the security. The Bank could adjust the amount on default on the part of the original debtor even before the maturity of the FDRs or could reserve its right to adjust the amount at the time of the maturity. That was not a case where the Bank was to adjust certain future deposits. The Bank was already possessed of the FDRs which in fact could be converted into cash at any point of time. When a guarantor gives the guarantee and deposits the security either in cash or in form of FDRs then on a default on the part of the original debtor, a creditor/Bank would be entitled to adjust the cash security or the Fixed Deposit Receipts either before its maturity or on the date of its maturity being in possession of the security i.e. the FDRs. The said judgment is not an authority to hold that if in future certain amounts become payable to a person then the creditor/Bank would be entitled to adjust the amount and take the surety by surprise.

21. Reliance was also placed upon the judgment in the matter of State Bank of India Vs. Messrs. Indexport Registered and others, . In the said matter, the Supreme Court again observed that if there is a composite money decree being both personally against all defendants including guarantor as well as the mortgage decree, without limitation on execution, the decree holder cannot be forced to first exhaust the remedy by way of execution of mortgage decree alone and then to proceed against the guarantor. Learned counsel for the Appellant-Bank also placed his strong reliance upon a judgment of the Privy Council in the matter of Mahanth Singh v. U Ba Yi, AIR 1939 Privy Council 110 and contended that even if there is a failure to sue the principal debtor until recovery is barred by the statute of limitation it does not operate as discharge of the surety. In the said matter a suit was filed against the original debtors and the sureties. The original debtors were the trustees. After some time an application was filed for substitution of trustees on the plea that the trustees have been changed, therefore, the new trustees be joined. Again after some time yet another application was filed that by mistake the original trustees were removed from the

array of defendants, they be again joined. The application was rejected and it was held that as on the date of their proposed rejoining the suit against them had become barred by limitation, they could be allowed to be joined. However, the suit proceeded against the surety and it was ultimately decreed. The matter was taken up to an Appellate Bench and a question was raised before them that after the principal debtors were removed from the array of the defendants the surety alone could not be sued. The learned Judges of the Bench allowed the appeal. Being aggrieved by the said judgment, the plaintiffs came to the Privy Council. The Privy Council observed that where an absolute release is given, there is no room for any reservation of remedies against the surety but in a case where there is no absolute discharge, the surety could still be sued. The Privy Council observed that in a given case where the action was brought against the debtor and the surety within the period of limitation, for one reason or the other the original debtors could not be successfully sued, the surety simply because of discharge of the debtors could not seek a discharge. The Privy Council observed that if the only result of striking out the debtors from the action was to preclude the bringing by the creditors of a fresh suit in respect of the subject-matter against them, and was not to release or discharge the principal debt, then the debt remains a debt though the creditor by reason of a rule of procedure could not himself bring an action upon it. It was also observed that the surety alone could be held liable. The said judgment, in our considered opinion, has no application to the present matter.

22. In the said matter an action was jointly brought against both and because of certain lapses or the follies committed by the plaintiff, the original defendants were discharged.

23. Learned counsel for the Appellant-Bank also placed reliance upon yet another judgment of the Supreme Court in the matter of *Bombay Dyeing and Manufacturing Co. Ltd. Vs. The State of Bombay and Others*, . After going through the said judgment, we are of the considered opinion that the said judgment has no application to the facts of the case in hand. In the said matter, the Supreme Court was required to consider the provisions of Bombay Labour Welfare Fund Act, Limitation Act, Payment of Wages Act and Contract Act (Section 56). The Supreme Court observed that the employer is no more discharged than by the operation of the bar of limitation u/s 15 of the Wages Act, or the provisions of the Limitation Act.

24. It is also to be seen from the scheme of the Act that in a case of surety/guarantee, there is a tripartite agreement. The basic agreement is between the creditor and the principal debtor, an ancillary agreement is between the creditor and the surety and then there is a unwritten statutory and subsidiary agreement between the debtor and the surety. The moment the surety is required to discharge the debts of the principal debtor the surety, upon payment of performance of all that he is liable for, is invested with all the rights which the creditor has against the principal debtor. u/s 141 of the Contract Act, a surety is

entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and if the creditor loses, or without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security. Section 145 of the Act provides that in every contract of guarantee there is an implied promise by the principal-debtor to indemnify the surety, and the surety is entitled to recover from the principal-debtor whatever sum he has rightfully paid under the guarantee, but no sums which he had paid wrongfully. The question always is that what is by the surety, can the same be held" to be legally paid. In the matter of Tarachand Lakhmichand Chuhan Vs. Gopal Lachiram Kumar, it was held that payment of a time barred debt is not a rightful payment; especially, if it has been made when the remedy against both the principal debtor and the surety had become time barred. In the present matter undisputedly on the date of the adjustment of the amount which was to fall due in future, the remedy to recover the loan amount by filing of a suit had become barred against the principal debtor so also against the surety. In the 13th report of 1958 of the Law Commission of India, the Law Commission observed that a surety paying a debt time-barred against the principal-debtor can be said to have paid it "rightfully", because the rights of the creditor arise, not from the liability of the debtor, but from the discharge of his own liability; and it recommended adding an explanation to that effect to the main Section but unfortunately the report of the Law Commission has not been translated into law. If the payment by the surety is of a time-barred debt or which otherwise could not be recovered by filing a suit against the principal-debtor or against the surety then such payment of amount cannot be held to be rightfully paid.

25. Taking into consideration the legal position, we are of the considered opinion that the Bank was absolutely unjustified in adjusting the amount from the amount payable to the petitioner which they had to recover from the borrowers.

26. It is also to be seen from the records that one of the borrowers deposited a sum of Rs. 27,000/- with the Bank on 10.7.2000 and despite that payment the amount of Rs. 40,000/- plus which included the above referred amount of Rs. 27,000/- was deducted from the retiral dues of the plaintiff on 5.12.2000. The said amount of Rs. 27,000/- had been paid to the writ petitioner almost after about 18 months. The Bank has not given any reason for not refunding the amount right in time or not paying the interest on the same. Be that as it may, though we cannot approve the Single Bench judgment of this Court in the matter of Md. Mahmoodul Haque Mallick v. The Bihar State Co-operative Bank Ltd. (supra) in the light of the judgments of the Supreme Court but on the sound legal principles we are of the opinion that in the present case the Bank was not justified in deducting the amount from the retiral dues of the petitioner.

27. The appeal is dismissed with costs quantified to Rs. 3,000/- (Three thousand).

R.N. Prasad, J.

28. I agree.