

(1982) 12 KAR CK 0013
In the Karnataka High Court
Case No : Company Application No. 49 of 1977

State Bank of Mysore

APPELLANT

Vs

Official Liquidator and Others

RESPONDENT

Date of Decision : 09-12-1982

Acts Referred:

Companies Act, 1956 — Section 446 (2) (b)
Provincial Insolvency Act, 1920 — Section 47, 47 (3), 59

Citation : (1985) 58 CompCas 609

Hon'ble Judges : M.P. Chandrakantaraj, J

Bench : Single Bench

Advocate : A.N. Jayaram, for the Appellant; S. Vijayashankar, King and Patridge, Shivaramaiah and C.M. Monnappa, for the Respondent

Judgement

Chandrakantaraj Urs, J.—Company Application No. 49 of 1977 is filed by the State Bank of Mysore having its head office on Kempegowda Road Bangalore, (hereinafter referred to as "the bank"). The application is presumably under s. 446(2)(b) of the Companies Act, 1956 (hereinafter referred to as "the Act"). It is necessary to mention here that the bank has filed earlier Company Application No. 142 of 1976 seeking therein an order of this court restraining the first respondent-official liquidator therein from making payment of Income Tax in respect of M/s. Mysore Chemicals and Fertilisers Ltd., a public limited company incorporated under the Act and which was by an order dated December 14, 1973, order to be wound up by this court in Company Petition No. 15 of 1972 filed by the State Trading Corporation of India, New Delhi, a creditor, in as much as the bank was a secured creditor and was entitled to preferential payment even before the tax dues, if any, were settled. While that petition was pending, C.A. No. 49 of 1977 was filed by the bank in the circumstances hereafter to be set out.

2. In the latter application the bank has prayed :

(1) For a declaration that the official liquidator is not entitled to go into the

question of the status of the bank as a secured creditor on the date of the application;

(2) That the official liquidator be directed by an order of the court to pay to the bank the amount due to it on the basis of the claim already made including interest up to date from out of the sale proceeds of Rs. 85 lakhs realised from the sale of the assets movable and immovable of the company in liquidation as substituted security for the movable and immovable assets charged to the applicant and allowed to be sold in C.P. No. 15 of 1972;

(3) For an order or orders to grant such further or other consequential directions as may be necessary in the circumstances in the interest of justice.

3. The bank claims, to the best of its knowledge, to be the sole secured creditor of aforementioned M/s. Mysore Chemicals and Fertilisers Ltd. (hereinafter referred to "as the company in liquidation"). The bank had extended the financial facility in respect of which to the company in liquidation over a period of years. The facilities were in the nature of : (1) medium-term loan, and (2) cash credit facility in respect of which the company in liquidation had hypothecated its plant and machinery and movables to the extent of Rs. 30 lakhs and also created an equitable mortgage by deposit of title deeds with the bank on security of the immovable properties of the company in liquidation. The details of the loan transaction will be referred to later.

4. The bank has asserted that the assets of the company in liquidation over which the bank had a charge were made to the official liquidator for sale upon condition that the bank would receive from out of the sale proceeds the amounts due to it as substituted security. The assets of the company in liquidation were sold on June 27, 1975, to M/s. Gammon India Ltd. for a sum of Rs. 85 lakhs and this court by its order dated July 11, 1975, confirmed the said sale. It is asserted by the bank that when the order was made by this court on July 11, 1975, the court took into consideration the willingness of the bank to support the said in its capacity as the secured creditor and on that basis this court held that the sale price offered by M/s. Gammon India Ltd. was a reasonable price for the assets of the company in liquidation. Admittedly, the bank has claimed the amount from the first respondent-official liquidator. At some stage of the hearing before the official liquidator, the bank appear to have been called upon by the official liquidator to clarify as to how the interest claimed by the bank had been computed and the bank appears to have furnished to him the required information first by a letter and thereafter on the request of the official liquidator in the form of an affidavit sworn to by one of the officers of the bank. In spite of that, the official liquidator has not made any payment to the bank and apprehending that the official liquidator may withhold payment pending investigation by him as to whether the bank is secured creditor, the present application has been made for grant of prayers already set out earlier. The bank has further asserted in the application that it has neither surrendered nor abandoned its security over the assets of the company in liquidation. In that

behalf, the bank has asserted that in the proceedings before the court and the official liquidator, the bank took the plea that it would not come into the winding-up proceedings but would only enforce its own security. Subsequently, however, it is felt that this course of action would only involve considerable time and expenditure as well as on account of the circumstances that at one point of time the Karnataka Agro-Industries Corporation, a State Government company, was intending to purchase the assets of the company in liquidation, the bank made its position known that it would allow the assets of the company in liquidation to be sold subject to its right of receiving out of the sale proceeds the amount due to it on a preferential basis by way of substituted security. It is also asserted by the bank that when the official liquidator called upon the bank to hand over the possession of the assets, books and records in pursuance of the order of this court, the bank had written to the official liquidator on March 31, 1973, intimating the security held by it against the assets of the company and that the same were being handed over without prejudice to the rights of the bank as a secured creditor and also that the delivery of the assets was not to be construed as surrender or waiver of the security of the bank over the assets of the company in liquidation. The bank has further contended that the official liquidator made an application to this court in C.A. No. 24 of 1974 in which he, inter alia, sought the directions of the court to call upon the bank to place the asset charged to it, at his disposal for sale without prejudice to its right to receive payments out of the sale proceeds as a secured creditor. In the said application (C.A. No. 24 of 1974), the bank also made its position clear by an affidavit filed before the court stating that it would allow the assets to be sold subject to its right to receive from out of the sale proceeds the amounts due to it. Similarly, the bank has stated that in the report dated March 20, 1975 (C.A. No. 38 of 1975 connected with C.A. No. 24 of 1974), the official liquidator had sought directions of the court to hand over the assets of the company in liquidation without prejudice to the rights of the bank as a secured creditor and it was only thereafter that the assets were made available to the official liquidator. The bank has further asserted that pursuant to the circumstances stated above, the sale of the assets of the company in liquidation were advertised in reputed newspapers of India and in response to the said advertisement, M/s. Gammon India Ltd. offered the highest bid of Rs. 85 lakhs on June 27, 1975, when the court sold the same by public auction. It was subsequent to the sale that the bank by an affidavit dated July 4, 1975, supported the acceptance of the bid of M/s. Gammon India Ltd. and similarly, the official liquidator also in his report dated July 1, 1975, had indicated that the bank as a secured creditor had itself estimated the value of the assets at about Rs. 1 crore. The bank has also asserted that this court by its order dated July 11, 1975, took into consideration the affidavit filed by the bank and held that there was no reason to disbelieve the statements made on behalf of the secured creditor. The bank has also drawn other attention of the court in its application that the official liquidator was aware of the status of the bank as a secured creditor inasmuch as in Company Application No. 116 of 1974 the liquidator had filed a report in the court opposing

payment to some of the ex-employees of the company in liquidation, inter alia, on the ground that the claims of the secured creditor had yet to be discharged in full first, and thereafter only the claims of the employees could be discharged. The bank has also asserted that throughout the proceedings in company Petition No. 15 of 1972, the official liquidator never questioned the status of the bank as a secured creditor. It is, therefore, the bank's contention that the official liquidator could only determine the exact amount due to the bank and not to determine whether the bank was a secured creditor or not. The Bank also has drawn attention to the fact that the official liquidator in the revised return of Income Tax had in fact deducted a sum of Rs. 60,85,560 as the amount due to the bank in whose favour the charge had been created before the order for winding up was made.

5. Soon after the filing of the application, some of the former employees of the company in liquidation filed an application to be impleaded as respondents so that they could contest the claim of the bank to receive preferential payment as secured creditor inasmuch as their claim would be adversely affected if the bank was allowed to be paid as secured creditor preferentially. That application was followed by C.A. No. 58 of 1977 to the same effect. Similarly, M/s. E. I. D. Parry Limited, Madras, another ordinary creditor of the company in liquidation, made an application to intervene in C.A. No. 49 of 1977 and be heard as its claim against the company which had been proved before the official liquidator would adversely affected by treating the bank as a secured creditor. Much later, after some progress had been made in Company Application No. 49 of 1977, the State Trading Corporation, the original petitioner in Company Petitioner No. 15 of 1972, made Company Application No. 68 of 1980 to intervene and be impleaded as one of the respondents.

6. No formal orders have been passed on the application made by the employees, M/s. E. I. D. Parry Limited and the State Trading Corporation. Those applications should be held as having been allowed by this court inasmuch as the interveners have been heard and allowed to cross-examine the witnesses and otherwise participate in the proceedings in C.A. No. 49 of 1977. Therefore, the former employees the company in liquidation, M/s. E. I. D. Parry Ltd. and the State Trading Corporation will all be treated as respondents in C.A. No. 49 of 1977 in addition to the official liquidator.

7. It is only the respondents, viz., employees and M/s. E. I. D. Parry Ltd., who have filed formal objection to the bank's claim opposing the prayers in C.A. No. 49 of 1977. It is unnecessary to set out in details their objections. In substance, the objections of all the respondents are that the bank by agreeing to stand within the liquidation proceedings had abandoned and surrendered its security in respect of it dues from the company in liquidation and, therefore, it had to stand in the queue like any other ordinary creditor to receive payment attracting the provisions of s. 47(3) of the Provisional Insolvency Act, 1920 (hereinafter referred to as "the Insolvency act"), that the bank was further required to prove

its security in accordance with law before it could claim a preferential payment as a secured creditor, if this court were to come to the conclusion that the bank had not abandoned or surrendered its security.

8. On the rival contentions pleaded as above, Venkatachaliah J., who was the company judge at the relevant time, framed the following issues for determination after hearing the parties on February 24, 1978 :

(1) What is the amount due the State Bank of Mysore from the company (in liquidation) ?

(2) Whether the amount due to the applicant-bank or any part thereof, is secured by a mortgage by deposit of title deeds of the immovable properties of the company (in liquidation) or by hypothecation or pledge of its movable properties as claimed by the applicant-bank ?

(3) Whether the applicant-bank has surrendered or relinquished its security at any stage of the winding-up proceedings ?

9. The bank has led formal evidence and examined four witnesses and has got marked as many as 66 documents in support of its case. The respondents have not led any formal evidence. They have been content with cross-examining the witness of the bank and also raising formal objection in regard to the admissibility of certain documents marked for the applicant-bank.

10. It is convenient to take up first, the second of issues which goes to the very root of the matter.

11. The bank, as already stated, has examined four witnesses to prove the hypothecation of plant, machineries and movables as well as the creation of a mortgage of the immovable properties by deposit of title deeds,

12. P.W. 1 is one S. Rajagopalachari. On the date of tendering evidence in the court, he had retired from the service of the bank. He has, however, spoken to the fact that between December 14, 1964, and June 22, 1967, he was the manager of the main branch of the bank in Mysore City. He has stated that the company in liquidation was a constituent of the bank enjoying two types of facilities : (1) a medium-term loan, and (2) a cash credit facility. He has stated that a medium term loan is generally granted for the acquisition of plant and machinery, construction of land and buildings and acquisition of tools and accessories for the purpose of a factory. Similarly, he has stated that cash credit facility is meant for working capital. He has stated that cash credit facility is medium-term loan was Rs. 25 lakhs and the same was enhanced to Rs. 30 lakhs subsequently. Cash credit was originally up to a limit of Rs. 10 lakhs and, however, owing to periodic enhancements, it had reached Rs. 50 lakhs when he was the manager at Mysore City main branch. He has stated that the loan transaction had commenced even prior to his taking charge of the bank at Mysore. He stated that the Manager, who was in charge of the bank before him, had handed over to him the documents which the company had earlier executed.

Exhibit P-1, an on-demand promissory not dated December 24, 1962, is executed by the company in liquidation. Exhibit P-2 is a deed of hypothecation dated December 24, 1962. P.W. 1. has spoken about exhibit P-2 which is the subject-matter of hypothecation of the plant and machinery then in existence and also those that were to be acquired thereafter. He has spoken about exhibit P-3, another demand promissory not dated November 18, 1964, executed by the company in liquidation for a sum of Rs. 30 lakhs. He has made it to what was covered by exhibit P-3 was inclusive of and not in addition to what was covered by exhibit P-1. Similarly, on the same day, i.e., November 18, 1964, the witness has spoken about the company having executed another agreement of hypothecation of movables. The company in liquidation on November 5, 1964, executed, according to the witness, another deed of hypothecation of goods as per exhibit P-5. On January 21, 1965, the company executed another demand promissory note for Rs. 5 lakhs as per exhibit P-6. Exhibit P-6, according to the witness, was in relation to cash credits given. Contemporaneously with exhibit P-6, another agreement of hypothecation of goods was executed by the company in favour of the bank as per exhibit P-7. On June 29, 1966, the company executed a demand promissory note for Rs. 30 lakhs as well as a deed of pledge for the said amount of Rs. 30 lakhs as per exhibit P-9. On June 8, 1966, according to P.W. 1, the company executed in favour of the bank yet another demand promissory note for Rs. 25 lakhs and also a deed of pledge of goods as per exhibits P-10 and P-11 respectively. On December 26, 1966, the company executed in favour of the bank another demand promissory note for Rs. 50 lakhs as per exhibit P-12 as well as another deed of pledge as per exhibit P-13. On July 29, 1966, the company executed in favour of the bank another demand promissory note for Rs. 10 lakhs accompanied by a deed of pledge on the same day, as per exhibits P-14 and P-15 respectively. The witness also has deposed to the fact that on November 18, 1964, the company created a mortgage by deposit of title deeds in favour of the bank charging the lands and building as security for all the facilities granted to the company. The letter referring to the deposit of title deeds is marked as exhibit P-16.

13. The last witness for the bank, P.W. 4, is one G. S. Ramachandra, an officer of the bank at its head office in Bangalore. He has spoken to the fact of having gone to M/s. Gammon India Limited, purchasers of the assets of the company in liquidation at the court auction and having obtained from them photostat copies of certain documents marked as exhibits P-38 to P-64. He has stated that the originals were in the custody of the bank for some time and that on the request of the official liquidator after the winding-up order was made, the same were given to him. It is necessary at this stage to notice that the photostat copies of exhibits P-8 to P-64 were admitted in evidence in as much as the official liquidator who had the custody of the originals had lost the same and he had not returned the same to the bank. In cross-examination by Shri Shivaramaiah, this witness has spoken to the fact that he was informed by one Mr. Pandit of M/s. Gammon India Limited that Mr. Pandit had obtained the photostat copies in the

office of the official liquidator when M/s. Gammon India Limited were interested in purchasing the property of the company in liquidation at the court auction held in Company Petition No. 15 of 1972. He has spoken to the fact that exhibit P-65 is the letter addressed by the bank enclosing the list of title deeds as per exhibit P-66. The letter has been addressed to the official liquidator.

14. Exhibit P-2 is one of the important documents in evidence. At this stage, it is necessary to state that Shri Shivaramaiah, the learned counsel appearing for the former employees of the company in liquidation and interveners in these proceedings, had objected to receive in evidence the deed of hypothecation dated December 24, 1962, in respect of the plant and machineries in evidence exhibit P-18. His objection was that the deed of hypothecation had not been adequately stamped as it was in fact a deed of mortgage of immovable property, as the plant and machineries were permanently embedded in the factory premises of the company in liquidation. In respect of exhibit P-18, his objection was the resolution itself created the mortgage and, therefore, that was document which was required to be registered under the Registration Act as well as under the Transfer of Property Act and not having been so registered was inadmissible in evidence. The documents were, however, received in evidence subject to the ruling of the court at the appropriate time and I think this is the appropriate stage at which these matters should be dealt with. The settled law in relation to what constitutes movable property and immovable property is to see whether things embedded in the earth are so embedded with the intention of making it permanently a part of the building or land in which they are so embedded. The plant and machinery in a factory premises can by no stretch of imagination be said to have been embedded in the earth with the intention of making it permanently a part of the land or the building. It is common knowledge that plant and machineries even though embedded in the earth are liable for removal either for repairs or for replacement. Therefore, the deed of hypothecation of the plant and machinery cannot be said to be in respect of part of the immovable property of the company in liquidation. Therefore, the deed of hypothecation as per exhibit P-2 is adequately stamped and does not suffer from any defect such as want of registration as it is not required to be registered. Next, exhibit P-18 which is referred to as the resolution is nothing but a letter signed by the chairman of the company in liquidation, one of its directors and the secretary of the company merely confirming the earlier transactions with the bank. In para 4 therein it is clearly stated that on February 25, 1966, the company had deposited the remaining title deeds with the bank in accordance with the resolution of that date. In para 3, it merely states that deposit of title deeds had not been completed both as regards the nature of the title deeds as also the number and extent of the properties. In the last paragraph, the letter speaks of an earlier agreement of the company which is confirmed to the effect that the bank had the authority to hold the said title deeds by way of security till all the company's present and future debts were fully paid or satisfied. Exhibit P-18 must be construed having regard to exhibits P-16 and P-17 which are also letters written

by the company. Exhibit P-16 makes it clear that two title deeds pertaining to schedule properties contained therein were deposited as far back as November 18, 1964.

15. When a similar question arose in the case of *Murugharajendra Co. v. Chief Controlling Revenue Authority* AIR 1974 Kar 60 : [1974] 1 KLJ 177, a full Bench of this court explained as to what constituted a mortgage by deposit of title deeds in the following manner :

"A mortgage by deposit of title deeds can be created by handing over the title deeds by the borrower to the lender with the intention that the documents should constitute the security for the debt. The essential factor which determines a document is one by which an equitable mortgage is created is the intention of the parties. The existence or otherwise of such an intention can be established either by the documents produced by the parties or by oral evidence or by both. If the title deeds which were held in the possession of the mortgagee under the earlier mortgage were acknowledged by both the parties as being held by the mortgagee as security for additional loan, it has to be presumed that there has been constructive deliver of title deeds.

"A document referring to what had been done earlier by the constructive delivery of title deeds with the intention to create an equitable mortgage is not an instrument evidencing deposit of title deeds and is not liable to stamp duty under article 6 of the Schedule to the Mysore Stamp Act."

16. From the above ruling, it is clear that exhibit P-18 cannot be construed as an instrument evidencing creation of a mortgage. Therefore, the objections raised by the learned counsel for some of the respondents is not tenable and, therefore, the same is overruled. The documents in question are liable to be received in evidence.

17. P.W. 1 has further stated that on August 31, 1966, the company in liquidation deposited some more documents and that on March 10, 1966, the deposit of title deeds till then made and affirmed by a resolution of the board of directors of the company was as indicated to the bank. He has stated that the said resolution was accompanied by a complete list of documents till then deposited with the bank. The letter dated March 10, 1967, from the company in that behalf, the copy of the resolution furnished to the bank and the list of documents are marked as exhibits P-17, P-18 and P-19 respectively. The witness has then spoken about exhibits P-20, P-21, P-22 and P-23, which are certificates of the Registrar of Companies, disclosing the registration of the charges with him. He has stated that the certificates were made available to the bank by the company is in liquidation. He has stated that exhibits P-6 to P-19 were executed by the company in favour of the bank during his term of office as manager of the Mysore branch. He has emphasised in his evidence that the said documents were signed in his presence by those concerned. He has also asserted that the title deeds were deposited by the company on February 5, 1966, August 31, 1966,

and March 10, 1967, in his presence. He has spoken of other facts which have some relevance and there are that the amount of Rs. 30 lakhs in exhibit P-4 is inclusive of the amount of Rs. 25 lakhs shown in exhibit P-2. Similarly, he has stated that exhibits P-5, P-7, P-9, P-11, P-13, and P-15 related to the cash credit facility granted to the company in liquidation. He has stated that the amount mentioned in exhibit P-5 is the consolidation of the amount mentioned in exhibit P-5 and exhibit P-7. He has also stated the circumstances under which the limit of credit facility was enhanced from time to time. He has stated that by exhibits P-17 and P-18, the company confirmed the deposit of title deeds made till the deed of exhibit P-18 as security for all the limits both on account of cash credit and medium-term loan.

18. The witness has been cross-examined by Mr. Shivaramaiah, the learned counsel for the former employees of the company in liquidation. Nothing very useful has been elicited in the cross-examination except to establish that the plant and machinery have been embedded in the earth reinforced by cement concrete by the company in liquidation. The other information elicited in cross-examination has really no bearing on the issue raised.

19. This witness was, however, recalled and examined in chief by permission of the court on March 20, 1980. On March 20, 1980, the witness has stated that the documents deposited by the company in liquidation with the bank at the relevant time for the two loans granted to the company in liquidation were the original title deeds and also says that he was the person who received the title deeds, as he was in charge of the bank at that time.

20. P.W-2 is one B. C. Mallaraja Urs, who was the manager of the main branch, Mysore City of the bank for the period between June 23, 1967, and January 4, 1971. He has stated that he took over from P.W. 1. He has stated that the company in liquidation was a constituent of the Mysore branch at the time when he took charge of that branch. He has stated that as part of taking over charge, he took possession and charge of all the documents executed by the company as security in favour of the bank. He has spoken to exhibit P-26, a deed of pledge. It was executed by the company in liquidation when he was in charge of the branch at Mysore. That deed of pledge, according to the witness, was for securing a sum of Rs. 55 lakhs which had been advanced on cash credit account. He has asserted that exhibit P-26 was executed in his presence at the bank. He has spoken in exhibit P-27 being a certified copy of the registration of charge with Registration of Companies. He has spoken in exhibit P-28 being a modification of that charge. In the cross-examination, nothing very useful has been elicited by the learned counsel for the interveners in so far as it touches upon issue No. 2. However, an attempt has been made to get P.W. 2 to estimate the value of the land in 1964 and 1967. The witness has stated that he did not know what the value of the lands of the company in the year 1967 was. As a very broad estimate, he has stated that it might have been of the value of Rs. 10,000 an acre in that year. Similarly, in regards to the extent of immovable

property secured to the bank, he has stated that in cross-examination on the basis of the sale notification in Company Petition No. 15 of 1972 that the extent of land owned by the company in liquidation was 180 acres. Later, he has stated that he was not aware of the extent of the land owned by the company but it could have been 200 or 150 acres.

21. P.W. 3 is an employee of the bank at the head office at Bangalore, in charge of the credit department of the bank. He has spoken about his being familiar with the accounts of the company in liquidation with the bank as he had occasion to deal with accounts. He has stated that the company in liquidation had two accounts with the bank (1) a medium-term loan, and (2) cash credit. Exhibit P-29 is the extract of the entries in the books of account of the bank relating to medium-term loan. Similarly, the witness has stated that exhibit P-29 is the extract of the ledger entries from November 20, 1964, to September 21, 1973. This witness has stated that exhibit P-30 is the extract of the cash credit account from February 14, 1964, to December 20, 1973. He has also spoken of exhibits P-29 and P-30 having been prepared by his subordinates under his supervision. He has asserted that he has compared the contents of exhibits P-29 and P-30 with the books of accounts from which they were prepared and that he has satisfied himself about their correctness. He has asserted that books of accounts were maintained with the Mysore branch in the ordinary course of business. The witness has spoken about exhibits P-31 and P-32 being the ledgers in regard to the medium-term loan. The witness has spoken of the details of the transactions in exhibit P-31 and of the transactions of the company noted from November 20, 1964, to May 17, 1973. According to this witness, as on November 17, 1973, the medium-term loan account showed a debit of Rs. 10,28,669.88. This witness has further deposed in regard to the rates of interest charged. He has stated that in 1964 the interest charged was at 8 per cent., 10 per cent. from 1970 till December 8, 1971, and interest at 10 1/2 per cent. was charged from December 8, 1971 onwards. He has stated that the rates of interest were linked to Reserve Bank of India advances rates till January 8, 1971, and thereafter were linked to the Bank of India rates. He has also stated that no penal interest was charged to the company in liquidation even though the terms of the loans permitted the same. In cross-examination by Shri Shivaramaiah, the learned counsel for the interveners, witness has denied the suggestion that exhibits P-29 and P-30 are not true extracts of the corresponding books of account of the bank. He has, however, stated that the extracts at exhibits P-29 and P-30 did not contain all that is to be found in the ledger such as the rates of interest, etc. He has stated in cross-examination that exhibits P-31 and P-32 relate to the medium-term loan and that so far they had not produced the ledgers relating to the cash credit account. He has admitted in his cross-examination that no vouchers or cheques have been produced by the bank in favour of the company in support of the books of account. On further examination-in-chief with the permission of the court, the witness has produced exhibit P-34, the cash credit ledger pertaining to the period from February 14, 1964, to June 28, 1965, and exhibit P-35 is the

cash credit ledger from June 28, 1965, to December 22, 1971. Similarly, exhibit P-36 is a further ledger relating to the period from January 1, 1972, to June 28, 1973, and exhibit P-37 is a further ledger relating to the period from December 14, 1973. According to the witness, the balance on the date of winding up was Rs. 44,63,510.09 as per entry on page 1 at exhibit P-37(a).

22. From the summary of evidence given above, what emerges clear is that the bank had acquired a charge on the immovable and movable properties of the company in liquidation. I do not see any reason why this evidence in so far as it relates to the creation of a mortgage by deposit of title deeds by the bank in favour of the bank should not be accepted. It is useful to notice that at no point of time either the court or the official liquidator had questioned the status of the bank as a secured creditor. Normally, that should have clinched the issue but in the light of the objections taken by the interveners that the bank was required to prove its security before its claim for preferential payment, it has become necessary for the bank to adduce the evidence which it has done. No arguments have been advanced other than the objections to receive some of the documents in evidence to demonstrate that there was no mortgage by deposit of title deeds by the company in liquidation by any of the counsel appearing for the respondents. I have, therefore, no hesitation to hold that the bank has proved its security and its status as a secured creditor by the various documents produced before the court particularly exhibits P-16, P-17 and P-18 and by the admitted fact that certain title deeds listed in exhibit P-66 were indeed given to the official liquidator who has lost them. Therefore, exhibits P-38 to P-64 are the photostat copies of some of those title deeds and I accept the testimony of P.W. 4 in that behalf.

23. Before parting with this issue, it is necessary to notice one other argument advanced by Mr. Shivaramaiah, learned counsel for the intervening ex-employees of the company in liquidation. He has argued that exhibits P-38 to P-64 are not at all documents of title and, as such, their deposit could not have legally created a mortgage by deposit of title deeds in favour of the bank. According to the learned counsel, exhibit P-38 is a mere copy of the Government order sanctioning the acquisition of a small bit of land for the company in liquidation in 1941 while exhibits P-39 to P-64 are mere encumbrance certificates in respect of certain lands which by no means could be called, much less answer to the description of title deeds to immovable property.

24. Shri S. G. Sundaraswamy, learned counsel for the bank, has drawn my attention to several decisions but it will suffice it to notice a decision of the Division Bench of the High Court of Madras in the case of Angu Pillai and Others Vs. M.S.M. Kasiviswanathan Chettiar and Others, . In the said case, the learned judges had to decide whether tax receipt issued in favour of the mortgagor together with an agreement of sale to purchase the property in respect of which he had paid the tax satisfied the requirement of s. 58(f) of the Transfer of Property Act. Learned judges of the Madras High Court approving the Full Bench

decision of the Rangoon High Court in *K.L.C.T. Chidambaram Chettyar v. Aziz Meah* AIR 1938 Rang 149, came to the conclusion that it is not necessary that the most material of the document of title should be deposited in order to create an equitable mortgage, but it is sufficient if the deeds deposited bona fide relate to the property in question. This appears to be the correct legal position. As between the mortgagor and mortgagee, what is important is the intention and object of deposit of the title deeds and not whether the mortgagor has a genuine title. Genuineness of the title may assume importance only when a third person claims title to the same property. Any document which evidence of title would be sufficient to create a mortgage by deposit of title deeds and need not in itself be the title deed. Exhibits P-38 to P-64 are documents which are not in themselves title deeds but evidences that the company in liquidation was the owner of the lands mentioned in them on the relevant dates. I do not, therefore, see much merit in the argument of Shri Shivaramaiah and reject the same.

25. Shri S. G. Sundaraswamy, learned counsel for the bank, has drawn the attention of the court to the statement of affairs filed by the ex-directors of the company pursuant to the winding up order made by the court on December 14, 1973, wherein the bank has been shown as a secured creditor of the company in liquidation. No one has questioned the correctness of the statement of affairs. No director (former) has been examined by the respondents in that behalf. This fact alone should clinch the issue in favour of the bank and I have no hesitation to hold that the bank was a secured creditor as on December 14, 1973.

26. It is now convenient to deal with issue No. 3.

27. The respondent have asserted that the bank by the fact of filing the affidavit dated March 21, 1975, in C.A. No. 24 of 1974 (in C.P. No. 15 of 1972) had abandoned or surrendered its security in having agreed stand within the liquidation proceedings. It is further contended that the bank having filed its affidavit of proof of debts on August 31, 1974, should be presumed to have abandoned its security in terms of s. 47(3) of the Insolvency Act and elected to realise its credit as an ordinary creditor. The bank, of course, had resisted these contentions as untenable, not warranted and misconceived.

28. Counsel appearing for parties have drawn my attention to several High Courts in India in support of their rival contentions. I do not think it is necessary to advert to all of them. Similarly, the parties have not led any evidence in these proceedings on this issue but have relied, by consent, on the records of C.P. No. 15 of 1972 to make their points.

29. It is seen from affidavit of the then official liquidator, dated January 8, 1974, filed in C.A. No. 24 of 1974 that the bank which had intervened therein as seventh respondent had by its letter dated December 31, 1973, had furnished to him the details of its interest in the assets of the company as a secured creditor claiming a sum of Rs. 56,17,164.01 under cash credit loan as well as the medium-term loan. By his letter dated January 31, 1974, the official liquidator

requested the bank to send all the title deeds held by it in respect of the two loans advanced to the company in liquidation for purposes of verification promising to return the same after verification. The bank replied to the same by stating that they were not willing to do so unless there was an order of the court to that effect and that the representative of the official liquidator could have inspection of the same at its Mysore branch. In the report dated April 4, 1974, the official liquidator in C.A. No. 24 of 1974 prayed for an order of the court to direct the secured creditor to deposit sufficient funds towards meeting expenses in connection with taking inventory, valuation and preparation of plans, measurements, etc., of the assets of the company in liquidation. In C.A. No. 80 of 1974, the official liquidator sought several directions from the court one of which was for directing the bank to hand over all pledged and mortgaged assets to the official liquidator in the event of the bank as secured creditor surrendering its security to the official liquidator. The bank thereupon filed an affidavit dated August 23, 1974, asserting that it relied upon the security created in its favour to realise the debts due to it by the company in liquidation and would, therefore, stand outside the winding up proceedings. On that date, it is significant to notice that only some movable pledged to be bank, like sulphuric acid, had been sold. However, eight days later, the bank filed before the official liquidator on August 31, 1974, its affidavit of proof of debt as a secured creditor claiming that in terms of the security of documents executed in its favour as well as in exercise of the banker's lien under the Contract Act, the bank was entitled to have the debts due to its satisfied out of the sale proceeds of the properties charged to it. Subsequently in February, 1975, the official liquidator made a report to the court, inter alia, praying that he may be permitted to sell all the assets of the company by public auction or private negotiations as his efforts to rehabilitate the company in liquidation and reconstruct the same had not met with success. He further prayed that the bank may be directed to put him in possession of all the assets of the company in liquidation in the possession and control of the bank as well as the title deeds and securities relating thereto. That report was followed by a formal application, C.A. No. 38 of 1975, more or less to same effect of March 17/18, 1975. On the same day or a day earlier, Karnataka Agro-Industries Corporation Ltd., a Government of Karnataka company, filed an application in court praying that the official liquidator may be directed to hold an open equitable public auction of all the assets of the company in liquidation to enable it to purchase the same. It was at this juncture that the bank filed its affidavit dated March 21, 1975, indicating its willingness to stand within the liquidation proceedings subject, however, to receiving out of the sale proceeds on a preferential basis the amounts due to it as secured creditor as notified to the official liquidator on August 31, 1974. The bank further stated in the said affidavit that the official liquidator may be directed to negotiate the sale of assets with the Karnataka Agro-Industries Corporation or in the alternative to sell the assets en bloc by open auction. The bank further offered its full co-operation to the official liquidator as may be directed by the court. It was in these circumstances that the court on March 25, 1975, made the order in C.A. No. 38

of 1975 permitting the sale of the assets by public auction after proper advertisement and publicity as directed in the order. In the result, at the auction held in court on May 27, 1975, M/s. Gammon India Ltd. came to purchase the assets for Rs. 85 lakhs. This, is in spite of the fact that the valuer appointed by the court had valued all the assets at rupees one crore eighty lakhs. After hearing all parties concerned on July 11, 1975, the court confirmed the sale in favour of the auction purchaser.

30. From the above undisputed facts and events, Shri S. G. Sundaraswamy, learned counsel for the bank, has argued that the conduct of the bank at no point of time amounted to waiver of its security, abandonment of its security in favour of the other creditors or a surrender. He has argued that security of immovable property cannot be extinguished except in two ways - by an express and positive act of surrendering the security by process known to law or by an express provision of law, such as an act of the Legislature authorising such extinguishment. He has also argued that the bank stepped into the winding up proceeding only to assist the court in the sale of the assets of the company in liquidation with the express reservation that the bank's dues would be paid out of the sale proceeds by way of substituted security.

31. Relying upon the decision of the Supreme Court in the case of Basheshar Nath Vs. The Commissioner of Income Tax, Delhi and Rajasthan and Another, , the learned counsel has contended that waiver can only be expressed in respect of a legal right and such waiver cannot be implied or waived except by process known to law. In the aforementioned decision, the Supreme Court was examining the question of the scope of the fundamental right under art. 14 and whether it could be waived by a citizen. The ruling that it cannot be waived as that right is indirectly conferred on the citizen has no application to the type of waiver the bank is charged with in this case. However, in the judgment of S. R. Das C.J., it is to be seen that the learned Chief Justice discussing, on the fact of that case, described the term "waiver" as a troublesome term in law. He further ruled that to constitute a waiver, there should be an intentional relinquishment of a known right or a abandonment of a known existing legal right. That undoubtedly is the law declared by the Supreme Court and, therefore, having regard to the repeated assertion of the bank throughout the proceedings before this court in Company Petition No. 15 of 1972 after the winding up order was made, I have no hesitation to hold that bank has not waived, or surrendered or relinquished or abandoned its security in respect of the assets of the company in liquidation.

32. Shri S. G. Sundaraswamy has drawn my attention to a few other decisions of other High Courts bearing on this point which merit notice.

33. In the case of Kanniappa Mudali and Others Vs. P.V. Raju Chettiar and Others, a Division Bench of that high court deciding a question arising under s. 16(5) and s. 31 of the Provincial Insolvency Act of 1907 corresponding to s. 28(2) and 47(3) of the Insolvency Act, 1920, ruled as follows (p. 762) :

"..... sale by mortgagor without a relinquishment by the mortgagee, but merely with the consent of the mortgagee expressed in an unregistered document, cannot be valid unless the facts amount to an authorisation of the mortgagor to sell on the mortgagee's behalf or to an agreement by the mortgagee to accept such sum as may be realised in the sale in discharge of his debt."

34. All that the bank has done in the instant case is to consent to the sale of assets subject to payment of its due on a preferential basis. Mere fact of giving consent cannot have the effect of destroying its security. Similarly, in the case of *Govinda v. Abdul Kadir (Khansahib)* AIR 1923 Nag 150, Acting Judicial Commissioner, Nagpur, in deciding as to what were the available assets distribution by the receiver under s. 56 of the Insolvency Act held that where any part of the insolvent's property was subject to a mortgage, the value of the insolvent's right to redeem that property could only to be his assets available distribution and if the receiver sold the property free from mortgage and realised the purchase money, the whole of it was not assets available for distribution but only such part as remained in his hands after paying off the mortgagee.

35. Again in the case of AIR 1930 196 (Nagpur) Acting Judicial Commissioner, considering the scope of s. 47 of the Insolvency Act, 1920, held that where the mortgagee desired that the mortgaged property of the insolvent mortgagor should be sold free from the mortgaged debts and the mortgage debts should be recovered from the sale proceeds, the Insolvency Court was competent to comply with such request.

36. In the case of *Parameswaram Pillai Raman Pillai Vs. Lekshmi Pilla Kamalamma Pilla and Others*, a Division Bench of the Kerala High Court examining the scope of s. 59 of the Insolvency Act have held that if a secured creditor agreed to have the sale conducted free of his encumbrance so that he could realise his debt from the amount realised by sale and the receiver conducted the sale, such a procedure could not be said to be not warranted by law.

37. Numerous other cases have also been cited by the counsels at the Bar. But every case must be understood to have been decided on the facts of that case. But in so far as the facts of the present case of the bank are concerned, it would be useful to refer to decision of the High Court of Andhra Pradesh in the case of *Smt. Syamala Bai v. Official Receiver, Kurnool* [1967] 1 AWR 70. The learned single judge of that of High Court had occasion to consider the scope of ss. 28, 47 and 59 of the Provincial Insolvency Act. The case came up for consideration before the Andhra Pradesh High Court in exercise of its revisional jurisdiction under s. 115 of the CPC. The facts of that case may be briefly stated as follows : Three people were adjudged insolvents. Two of the properties belonging to the insolvents were mortgaged to two different people. One of them valued the property and given sum and requested the official liquidator to sell the property and give the mortgage amount. The official receiver sought permission of the court of the sub-judge and the sub-judge gave that permission, consequent upon

which the property was sold; the mortgagee claimed that the amount realised should be paid to him on a preferential basis as he had retained the lien on the mortgage amount. The official receiver accepted that plea and proceeded to pay the mortgage amount preferentially to the mortgagee. That was objected to by others and they filed an appeal before the sub-judge against the excision of the official receiver. The sub-judge upheld the decision of the official receiver rejecting the contention of the appellant that by permitting the sale of the mortgage property, the mortgagee had relinquished by any rights which had accrued to him in accordance with law. On further appeal, the District Judge confirmed that view. Therefore, a revision petition was filed before the High Court.

38. The learned judge, dealing with the questions raised before him and particularly dealing with the contention advanced that the mortgagee amount being paid to him had relinquished his right to claim preferential treatment in terms of sub-s (3) of s. 47 of the Insolvency Act, held as follows :

"In order to understand the implication of this contention, it is necessary to read sections 28, 47 and 59 of the Provincial Insolvency Act, hereinafter called the Act.

39. Section 28 of the Act gives the effect of an order of adjudication. According to sub-section (6) of that section, nothing in that section affect the power of any secured creditor to realise or otherwise deal with his security in the same manner as he would have been entitled to realise or deal with it if that section had not been passed.

40. Section 47 which relates to secured creditors enjoins that where a secured creditor realises his security, he may prove for the balance due to him after deducting the net amount realised. Secondly, where a secured creditor relinquishes his security for the general benefit of the creditors, he may prove for his whole debt; and, thirdly, where a secured creditor does not either realise or relinquish his security, he shall before being entitled to have his debt entered in the schedule, state in his proof, the particulars of his security and the value at which he assesses it and shall be entitled to receive a dividend only in respect of the balance due to him after deducting the value so assessed.

41. According to sub-section (4) of that section where a security is so valued, the court may at any time before realisation redeem it on payment to the creditor of the assessed value. Sub-section (6) states that where a secured creditor does not comply with the provision of this section, he shall be excluded from all share in any dividend.

42. Section 59 of the Act concern itself with the duties and powers of receiver. According to that provision, he has power to sell all or any part of the property of insolvent, apart from other powers mentioned in the section. He can mortgage or pledge any part of the property of the insolvent for the purpose of raising money for the payment of his debts.

43. It will be thus plain that what section 47 provides is only for the benefit of the mortgagee and not to his detriment. He can follow any one of the three procedures suggested in the section. In this case, I do not think it can be validly argued that the mortgagee has relinquished his security. Exhibit B-1 makes it clear that he had no objection if the property is sold free of mortgage but a lien is kept in so far as the value he had assessed is concerned and is preferentially paid out of the sale proceeds. There are no words in exhibit B-1 which warrant any circulation that the mortgagee had relinquished his security....

44. In fact, sub-section (3) of section 47 lends support to this method of payment to the mortgagee. If the official receiver proceeds to sell the security, the court first has to pay the amount at which the security was valued to secured creditor out of the sale proceeds. Whatever may be the position in regard to the balance in so far as the value of his assessment is concerned, he can be preferentially paid out of the sale proceeds.

45. If the sale was valid, I fail to see how the mortgagee could be deprived of his security, particularly when he had not relinquished. The property was sold with a clear understanding that the mortgagee will be paid first from the sale proceeds. This mode of realisation of security is not, in my view, derogatory either to section 47 or to section 59 of the Act ...

46. I am in respectful agreement with the reasoning of the learned single judge for reasons already stated, supported by the authority of the Supreme Court decision, that the mortgagee cannot relinquish his rights except by instrument provided for the relinquishment of rights under law. There cannot be an implied surrender in terms of sub-s. (3) of s. 47 of the Insolvency Act and the surrender referred to therein should be construed as surrender in accordance with law. On the facts of this case, which may be once again restated, the bank had first stood outside the winding up when the sale was asked for by the official liquidator. It was in that circumstance that this court gave notice to the bank and there-upon the bank expressed that the property may be sold subject to the security being transferred to the sale price received. That is clear from the affidavit filed by the bank at the relevant time in these proceedings. Therefore, the contention of the respondents must be rejected. Sub-s. (3) of s. 47 of the Act does not come in the way of the official liquidator entertaining the application of the bank for payment of secured loans in accordance with the hypothecation agreement and the mortgage by deposit of title deeds, as proved by the bank. In the result, the bank is entitled to realise that amount on a preferential basis as a secured creditor notwithstanding the fact that it filed the affidavit indicating that it stands within liquidation but subject to the reservation of its security being continued.

47. Therefore, issue No. 3 must be answered in favour of the bank and held against the respondents and other objectors.

48. Now, we have to turn to issues No. 1. What is the amount due to the State Bank of Mysore from the company in liquidation ? This does pose several

problems. There has been some amount of confusion and I would venture to hint some amount of negligence on the part of the official liquidator as well as the parties in not leading sufficient evidence or even directing cross-examination of the witness examined by the bank in this regard. From the affidavit filed by the bank in Company Application No. 80 of 1974 on August 23, 1974, as on that date, the amount claimed was Rs. 58 lakhs. In that affidavit it is also made clear that the term loan of Rs. 30 lakhs had been secured by equitable mortgage by deposit of title deeds of the land and buildings belonging to the company. The same affidavit also claimed that cash credit facility availed of by the company from the bank was up to Rs. 55 lakhs. The cash credit facilities loan had been secured by hypothecation of raw materials, other materials, stores and spares. But in the affidavit of proof of debit filed before this court by the bank as on August 31, 1974, a sum of Rs. 29,32,708.06 has been claimed against cash credit facilities and for the same period ending August 31, 1974, the term loan is claimed at Rs. 11,25,002.33. The bank has further claimed a sum of Rs. 13,925 as other expenses in the affidavit of proof. It can straightaway be said that the claim of Rs. 13,925 cannot be treated as an amount due to the bank as a secured creditor and in respect of that amount, they have to stand in the queue as ordinary creditors.

49. But, in the course of the argument it has been brought out that the bank has arrived at those figures as evidenced by annexures A and B to the affidavit of the bank filed on August 17, 1976. Unpaid interest has been treated as loan advanced and for the subsequent period, interest is charged on such interest. This is usurious in character. But no evidence has been led in regard to this matter. In fact, the counsel at the Bar were unable to submit as to which law governed the usurious nature of the transactions both in respect of cash credit facilities and the term loan at the relevant time, but brought to my notice the ruling of the Division Bench of the High Court of Kerala in the case of State Bank of Travancore Vs. C.T. George and Another, , which has disallowed charge of interest on interest as offending the provisions of the Madras Usurious Loans Act (1918).

50. In the absence of sufficient evidence and specific pleadings in that behalf, I do not think it is wise to decide that question, but leave it open for the official liquidator in the light of the direction hereinafter to be issued to decide that question after notice to all parties and after hearing them.

51. The second factor which creates a problem to determine the exact amount due to the bank as a secured creditor is the absence of sufficient evidence regarding the value of land sold to Gammon India Ltd. It is seen from the records of the Company Petition No. 15 of 1972 that a valuer as appointed to value the property after the official liquidator had taken possession of the same. Total land value was shown assuming the total extent of land to be 180 acres and after deducting 10 per cent. for roads and drainage valued the land in an extent of 162 acres at Rs. 8,000 per acre on the basis of enquires said to have

been made by him. That report is dated 12/16 November, 1974. But from the sale certificate issued by this court, it is seen that the extent of land is 214 acres. In other words, it was never in evidence properly either in the proceedings for liquidation or in these collateral proceedings as to what the exact extent of land was. This court can only take notice of the sale certificate issued by it and hold that the total extent of land is 214 acres and 11 guntas. Then the mortgage of land and buildings by deposit of title deeds in favour of the bank covers in extent of just over 91 acres, having regard to the extent mentioned in the documents marked as exhibit P-39 to exhibit P-64. This leads to the inevitable conclusion that the security available to the bank in respect of the mortgage extends only to a little over 91 acres of land and not to the rest of the land. Therefore, it can only enforce its rights as a secured creditor on account of the mortgage in its favour in respect of the value of the land and buildings to the extent of 91 acres only and not in respect of the remaining lands.

52. However, in arriving at the value of the land, this court cannot rely upon the valuer's report which, in fact, was never treated as evidence in these proceedings. But, what is evidence in these proceedings is the oral testimony of P.W. 2, B. C. Mallaraj Urs, one of the bank managers at the relevant time at the Mysore City branch. He has stated that for the period, i.e., in 1967-68 when he had occasion to deal with the company in liquidation for giving the loans, the land value was in the region of 10 to 15 thousand rupees. The valuer also in his report has mentioned 16 thousand rupees as the value of the land which had been converted but that report was after the liquidation proceedings had commenced. It is safe to rely upon the estimate made by one of the bank's own officers at the time of giving loan and add some increase to the price on the date of sale having regard to general rise in the value of land in the area and that rise in price may be taken at 25 per cent. between 1967 and 1975. Thus, the land value should be arrived at for purposes of deciding this issue at 15 thousand rupees. Giving margin for roads and wastage at 10 per cent., the value of the land would still be Rs. 13,500 per acre. Therefore, 214 acres and 11 guntas of land should be valued at Rs. 13,500 per acre by the official liquidator and the value of 123 acres and 11 guntas which forms the extent of unsecured land should be taken out of the original sale price and kept in separate account not to be hit by the security of the bank from the date of the sale. It is only out of the remainder of the sale price and the interest that may have accrued thereon till today that the bank's claim as secured creditor should be examined by the official liquidator for preferential payment. In fact, when this matter was brought to the notice of the learned counsel for the bank in the course of arguments, he did concede that the bank could not enforce its security against lands in excess of 91 acres and the buildings.

53. For the reasons I have given above, the application by the bank is allowed, notwithstanding the objections filed by the others who are either objectors, respondents or applicants themselves.

54. In the result, I give the following directions to the official liquidator :

(1) The official liquidator shall straightaway pay a sum of Rs. 50 lakhs on a broad estimate, whatever may be due to the bank, subject to mutual adjustments after proper calculations and determination in the proceedings before him as directed in the course of this order earlier.

(2) The official liquidator shall entertain the application filed by the bank for preferential payment and in that decide the exact amount that may be due to the bank in accordance with law having regard to the observations made in the course of this order regarding the usurious nature of the transactions. But he shall allow at all times up to date of filing of the winding up petition, the contractual rate of interest as evidenced by the hypothecation agreements and the agreement relating to rate of interest on the mortgage, and statutory rate thereafter at 6 per cent per annum.

(3) He shall set apart the land value in respect of the lands of the company in liquidation now sold to Gammon India Ltd., which is not covered by the security of mortgage as pointed out in the course of this order in a separate account from out of the original sale price received and credit interest accrued thereon in an separate account to be dealt with separately as not covered by the security of the bank enjoyed by equitable mortgage and the hypothecation of machinery and raw materials, etc.

(4) If there is no agreement reached as to what constitutes usury in the light of decided cases, parties including the bank may in the usual course and in accordance with law appeal to this court against the adjudication of the official liquidator.

(5) The official liquidator shall pay Rs. 50 lakhs reserving to himself the right to claim repayment of any sum which may be found to be in excess after adjudication.

(6) The claim of the bank shall be adjudicated and disposed of within three months from today and all objections in these proceedings shall also be heard in the adjudication proceedings shall also be heard in the adjudication proceedings by the official liquidator.

55. Subject to the above directions, C.A. No. 49 of 1977 is allowed. Parties will bear their own costs.