

State Bank of India Vs. Machine Well Industries and Others

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Court : Delhi

Decided On : Nov-18-1980

Reported in : [1983]53CompCas830(Delhi)

Judge : G.R. Luthra, J.

Acts : Indian Contract Act - Sections 2, 25, 33, 133, 134, 135, 139 and 141; Indian Companies Act, 1913

Appeal No. : Suit No. 461 of 1969

Appellant : State Bank of India

Respondent : Machine Well Industries and Others

Advocate for Pet/Ap. : Mr. H. R. Sahni

Judgement :

G.R. Luthra, J.

1. The present suit is for recovery of Rs. 1,51,717.39 on the assertions which are briefly as follows :

M/s. Machine Well Industries, defendant No. 1, is a partnership firm. The said firm on February 27, 1963, through its partners, defendants Nos. 2 and 3, approached National Bank of Lahore Ltd., for grant of cash credit facility against the pledge of

movable properties and overdraft facility against documentary bills. That request was accepted and defendants Nos. 1 to 3 were afforded the aforesaid facilities at the Jangpura branch of the said bank, on execution of loaning documents.

2. On May 1, 1964, defendants Nos. 2 and 3 executed fresh loaning documents in favor of the said bank because the balance in the account of the defendants exceeded original sanctioned limit. On July 8, 1964, the plaintiff bank gave fresh overdraft facility to defendants Nos. 2 and 3 to the extent of Rs. 30,000 on the hypothecation of machinery and stocks in trade belonging to the said defendants and lying in their factory at Gurgaon. On account of the enjoying of the aforesaid facilities, the defendants aforesaid had become liable to pay the amount for which suit was brought.

3. According to the plaintiff, defendant No. 4 is liable because he executed a guarantee deed dated February 1, 1964, in favor of the bank whereby he undertook to become liable for the amount payable by defendants Nos. 1 to 3.

4. Liability is sought to be fastened on defendant No. 5 on the ground that in accordance with the inter se arrangement between defendants Nos. 2, 3 and him, he undertook the liability of the firm, defendant No. 1, and also addressed a letter dated July 23, 1968, to the plaintiff to the effect that he was liable to pay the amount payable by defendants Nos. 1 to 3.

5. Later on, the National Bank of Lahore Ltd. was amalgamated with the State Bank of India, and originally the former was the plaintiff and the latter became the plaintiff after the amalgamation.

6. Defendants contested the suit. Defendants Nos. 1 to 5 filed a joint written statement and stated that defendant No. 5 was the sole proprietor of the concern, defendant No. 1. Defendant No. 5 denied that he was liable to pay the amount in question. He admitted that he did write a letter dated July 23, 1968, to the plaintiff but stated that the said letter was completely ignored and not acted upon by the plaintiff and that the same could not be a basis of making him liable.

7. Defendant No. 2 admitted that she was partner of defendant No. 1 and enjoyed credit facilities given by the plaintiff. She, however, stated that on October 3, 1964, the partnership was dissolved, that she retired and that defendants Nos. 3 and 5 continued the partnership. She pleaded that since defendants Nos. 3 and 5 undertook the liability for the payment of the debts to all the creditors with the knowledge and agreement of the plaintiff, she was not liable.

8. Defendant No. 3 admitted that defendant No. 2 and he were partners of defendant No. 1. He stated that he signed a few forms in favor of the National Bank of Lahore Ltd., that the loan amount was used by defendant No. 5 who was the managing partner of the firm. He added that hence defendant No. 5 alone was liable, and that he was also not liable - because the firm was first of all dissolved on April 26, 196 - when Smt. Thikho Rani, defendant No. 2, retired from the firm and, subsequently, on April 1, 1968, when he retired from the firm. He pleaded that even otherwise he was a partner to the extent of ten paise in a rupee and he was drawing a fixed sum of Rs. 500 per month while the business was being actually carried on solely by defendant No. 5, Shri K. P. Seth, who alone was liable to the creditors.

9. Defendant No. 4 admitted that he was the guarantor, vide agreement of guarantee dated February 1, 1964. He, however, pleaded that his liability as guarantor stood discharged by virtue of s. 133 of the Contract Act. He explained that the bank got new loaning documents executed, from the defendants on May 1, 1964, which was subsequent to his agreement of guarantee, that there was thus a novation and variance of the contract between the creditors and defendants Nos. 1 to 3 without his consent which discharged him from the liability. He stated that the firm, defendant No. 1, consisted of defendants No. 3 and 5, that defendant No. 2 was originally a partner but she retired on or about October 31, 1964.

10. Following issues were framed on May 12, 1970 :

1. Whether the plaint has been properly signed and verified and instituted by a duly authorized person ?

2. Whether defendant No. 1 has ceased to be a partnership firm and has become a sole proprietorship concern of defendant No. 5
3. Whether there was a privity of contract between defendant No. 5 and the plaintiff
4. Whether letter dated July 23, 1968, written by defendant No. 5 to the plaintiff was acted upon by the plaintiff
5. Whether the liability of defendant No. 4 stands discharged by virtue of section 33 of the Contract Act
6. Whether the relief against defendant No. 4 is barred by limitation
7. Whether the plaintiff is precluded from claiming any relief against defendant No. 4 because of its unwillingness to enforce its rights against defendants Nos. 2 and 3
8. Is the plaintiff bound to sell the pledged goods before filing a suit on the basis of the loan
9. Is defendant No. 4 not liable to pay the amount in suit till the pledged goods have been sold
10. Is the liability of defendant No. 4 limited to the extent of originally sanctioned limit and not to the extent of the amount advanced by the plaintiff in the cash credit account which is the basis of the suit
11. Is the liability of defendant No. 4 in any manner affected by the alleged internal arrangement between defendants Nos. 1, 3 and 5
12. Whether the plaintiff is prevented from recovering dues from defendant No. 4 because of the allegations made in paras. 1 and 2 of additional pleas in the written statement
13. Has the proprietorship of Machine Well Industries changed If so, does this relieve the defendants Nos. 2 and 3 from their liability to the plaintiff

14. To what amount the plaintiff is entitled and against whom

11. Originally the suit was instituted by the National Bank of Lahore Ltd., which was a company registered under the Indian Companies Act, 1913. It was that banking company which had advanced the loan to defendants Nos. 1 to 3. It was the case of the National Bank of Lahore Ltd., that the suit was instituted, vide resolution No. 16 passed by its board of directors on October 6, 1969, and that the resolution authorized Mr. Raj Kumar Kapoor, a manager of that bank at Jangpura branch, New Delhi, to institute the suit. It was afterwards that the said bank was amalgamated with the State Bank of India.

12. Shri Kailash Nath, staff officer, State Bank of India, local Head office, New Delhi, P.W. 1, stated that he was the secretary of the National Bank of Lahore Ltd., which was amalgamated with the State Bank of India. He brought a minute book of the Board of Directors of the National Bank of Lahore Ltd. He produced the minute book of the Board of Directors of the National Bank of Lahore Ltd., inter alia, containing resolution No. 16, dated October 6, 1969, authorising Shri Raj Kumar to file the present suit. Shri Kailash Nath stated that he was present at the time when the resolution was passed. He placed on record a copy of the resolution which is ex. P.W. 1/1. He also brought the original power of attorney in favor of Raj Kumar Kapoor executed by the board of directors of the National Bank of Lahore Ltd. Shri Kailash Nath testified that he signed as attesting witness of the power of attorney. He filed a copy of that power of attorney which is ex. P.W. 1/2.

13. Shri Raj Kumar Kapoor also appeared as a witness, P.W. 2. He stated that he was authorised to institute the suit by a resolution of the board of directors (copy of which was ex. P.W. 1/1) and that he held the power of attorney in his favor, copy of which was ex. P.W. 1/2. He added that he signed and verified the plaint and appointed Miss Raj Kumari Puri and Mr. H. R. Sahni as counsel for the plaintiff.

14. thereforee, it stands proved that Raj Kumar who signed and verified the plaint was authorised to do so, that he was also authorised to institute the suit and that he held a power of attorney from the board of directors. Issue is decided accordingly in favor of the plaintiff.

Issue No. 2 :

15. It is common ground between the defendants that ultimately defendant No. 5 became the sole proprietor of the business of the partnership firm. It is not specifically denied in the replication to the written statement of defendant No. 5 that the said defendant became the sole proprietor of the business of defendant No. 1. Rather the plaintiff wants to fasten defendant No. 5 with the liability on the ground that the latter had so become a proprietor. During arguments also it was taken for granted that defendant No. 5 became the sole proprietor of the partnership business of defendant No. 1. Issue is decided accordingly in favor of the defendants. However, as to what is the effect of defendant No. 5 becoming the sole proprietor is to be decided while deciding the other relevant issue.

Issues Nos 3 & 4 :

16. Both the issues are inter-connected and, therefore, they are being taken up together. It is common ground between the parties that defendant No. 5 never executed any loaning documents in favor of plaintiff or its predecessor, the National Bank of Lahore Ltd. The plaintiff does not claim any privity of contract on the basis of any loaning documents. Reliance of the plaintiff is solely on a letter dated July 23, 1968. There is no denial by defendant No. 5 about having written the said letter but his contention is that no liability can be fastened on him on account of said letter. therefore, we have to examine the contents and effects of that letter.

17. The aforesaid letter is ex. P.W. 2/1 and reads as under :

'I have to inform you that a cash credit account in the name of Machine Well Industries was opened by you on April 26, 1963, with the partnership of Smt. Thikho Rani and Shri D. D. Khosla. Later on Smt. Thikho Rani left the firm and there was partnership deed between the undersigned and Shri D. D. Khosla but the same is not traceable at present. I and Shri D. D. Khosla entered into an agreement with Shri K. S. Choudhary and Shri J. L. Khanna, both of them as financiers. This agreement has already been lodged with you.

Again on April 10, 1968, I dissolved the partnership deed with Shri D. D. Khosla and took over the complete charge of the firm from April 1, 1968, with the same terms and conditions as contained in the agreement dated October 28, 1966, with Shri K. S. Choudhry and Shri J. L. Khanna as financiers. The copy of the relative dissolution deed is enclosed. In terms of this deed, I have become the sole proprietor of the said firm. Please advise the documents that you want to get executed by me to safe-guard your interest.'

18. There is no doubt that the aforesaid letter indicated that there was a voluntary offer on the part of defendant No. 5 to be clothed with all liabilities of the firm, defendant No. 1. But we must not forget that that was simply an offer or 'proposal' and it could ripen into a contract only if there was an acceptance of that proposal on the part of the plaintiff. This is clear from the definition of the words 'proposal', 'acceptance', 'agreement of contract under s. 2 of Contract Act.' So it is to be seen if there was any acceptance or not on the part of the plaintiff, whether expressly or impliedly. The essential features of the offer were, firstly, that the plaintiff should recognise defendant No. 5 as the sole proprietor of defendant No. 1, secondly, that defendant No. 5 alone should be called upon to discharge all the liabilities of the said firm and, thirdly, as a necessary consequence, defendants Nos. 2 and 3 were discharged from liability of the business of the defendant No. 1. There is no document on record and in fact never alleged that the plaintiff expressly accepted all the aforesaid essential features of the offer. There was no acceptance by implication even. Plaintiff never discharged defendants Nos. 2 & 3 from the liability. On the other hand in the suit itself, relief is being claimed very actively against defendants Nos. 2 and 3 as partners of defendant No. 1, as executants of the loaning documents. As such no contract ever came into existence between the plaintiff on the one hand and defendant No. 5 on the other hand which means that there was neither any privity of contract between them nor the letter dated July 23, 1968, was acted upon.

19. There is another aspect of the matter too. As already stated the essential condition of clothing defendant No. 5 with the liability was to recognise him as the sole person liable for the acts of defendant No. 1 and thereby discharge defendants Nos. 2 and 3 from liability. thereforee, the consideration for entering

into contract between the plaintiff on the one hand and defendant No. 5 on the other hand was that defendants Nos. 2 and 3 should not be fastened with any liability. That consideration was never accepted because the plaintiff still wants to make defendants Nos. 2 and 3 liable along with defendant No. 5. It may be mentioned at this stage that defendant No. 3 died during the pendency of the suit without his legal representatives being brought on record and the suit against him has abated on that account. But the fact remains that the plaintiff never wanted to free him from liability. thereforee, even if it is taken for granted the offer contained in the aforesaid letter matured into a contract, the said contract was without consideration. According to s. 25 of the Contract Act any agreement made without consideration is void.

20. The learned counsel for the plaintiff relied upon a judgment in *Dodson v. Downey* [1901] 2 Ch 620. The proposition of law laid down is that the purchaser of shares in a partnership must personally indemnify the vendor against the partnership liabilities. The learned counsel contended that defendant No. 5 purchased the entire partnership business and that, thereforee, he must personally indemnify the vendors i.e., defendants Nos. 2 and 3, against the partnership liability and that, hence, he could be caught hold of by the plaintiff in respect of the liability of defendants Nos. 2 and 3.

21. But the aforesaid authority does not help the plaintiff : That decision is not to the effect that any creditor of the vendors of a partnership firm can hold the vendee directly responsible in respect of the partnership liabilities. The aforesaid decision is only to the effect that if after sale, the original partners are made to pay anything in respect of the liability of the partnership firm they can afterwards call upon the purchaser to indemnify them and not that that a creditor can enforce a liability of the partnership business directly against the purchaser. That decision talks of the ultimate rights of the original partners against the purchaser of the partnership business and has no bearing on the rights of the creditors of the partnership business as against the purchaser of the said business.

22. thereforee, in view of what has been discussed above, I decide both the issues in favor of defendant No. 5 and against the plaintiff.

Issue No. 5 :

23. It appears that it is on account of typographical mistake that s. 33 of the Contract Act has been mentioned in the issue instead of s. 133. It is only s. 133 which deals with the discharge of liabilities of a guarantor in certain circumstances. That provision reads as under :

'Any variance, made without the surety's consent, in the terms of the contract, between the principal debtor and the creditor, discharges the surety as to transactions subsequent to the variance.'

24. In the present case, there is no dispute about the facts. The agreement of guarantee, ex. PW-2/13, which is surety to be enforced against the defendant No. 4, was executed on February 1, 1964. Vide that agreement, defendant No. 4 undertook to pay up to the extent of Rs. 1,50,000 principal, interest, costs, charges and expenses due or which might at any time become due to the National Bank of Lahore on account of the operation of the cash credit account by defendants Nos. 1 to 3. Before that date cash credit facilities were already available to defendants No. 1 to 3. After that agreement of guarantee, the National Bank of Lahore Ltd. raised the cash credit limit to Rs. 2 lakhs and got the following loaning documents executed from defendants Nos. 2 and 3 on May 1, 1964 :

(a) Promissory note, ex. PW - 2/2.

(b) Letter of continuity, ex. PW -2/3.

(c) Letter, ex. PW -2/4, assuring payment of the amount mentioned in the promissory note.

(d) Letter, ex. PW -2/5, regarding interest payable on the loan.

(e) Agreement for cash credit/overdraft, ex. PW -2/6.

25. In addition to the said documents, defendants Nos. 2 and 3 on behalf of themselves and defendant No. 1 executed an agreement of pledge of goods, ex. PW -2/7, on April 26, 1964.

26. It is apparent from the above that there was a variance in terms of the contract between principal debtors, defendants Nos. 1 to 3 on the one hand, and the creditor being the National Bank of Lahore on the other hand and inasmuch as, firstly, the limit of over drafting was increased from Rs. 1,50,000 to Rs. 2 lakhs and, secondly, the original contract was substituted by a fresh one by getting fresh loaning documents executed. It may be emphasised that the aforesaid variance took place three months after the execution of the agreement of guarantee. There is no dispute that the aforesaid variance was without the consent of defendant No. 4. On that account s. 133 of the Contract Act discharges the surety, i.e., defendant No. 4.

27. The learned counsel for plaintiff, however, relied upon clause 4 of the agreement of guarantee, which reads as under :

'The guarantors hereby consent to the bank making any variance that it may think fit in the terms of the contract with the borrower, to the bank determining, enlarging or varying any credit to him or making any composition with him or promising to give him time or not to sue him and to the bank parting with only security it may hold for the guaranteed debt. The guarantors also agree that they shall not be discharged from their liability by the bank releasing the borrower or by any act or omission of the bank the legal consequence of which may be to discharge the borrower or by any act of the bank which would, but for their present provisions, be inconsistent with their rights as guarantors or by the bank's omission to do any act which but for their present provision the bank's duty to the guarantors would have required the bank to do. Though as between the borrower and guarantors they are guarantors only, the guarantors agree that as between the bank and the guarantors they are debtors jointly with the borrower and, accordingly, they shall not be entitled to any of the rights conferred on guarantors and surety by sections 133, 134, 135, 139 and 141 of the Contract Act.'

28. The learned counsel for the plaintiff contended that the said clause clearly indicated that defendant No. 4 undertook that he would not claim benefit of the provisions of s. 133 of the Contract Act and that, therefore, he was not exonerated or discharged from liability. The learned counsel relied upon a

judgment of the Madras High Court in A. R. Krishnaswamy Aiyar v. Travancore National Bank Ltd. [1940] 10 Comp Case 162 (Mad); AIR 1940 Mad 437, in support of his contention that a surety could waive his rights available to him under the provisions of the Contract Act. The following was held responsible by the Madras High Court [at p. 438 of AIR's head note].

'Although a composition bond between the principal debtor and the creditor extinguishes the debt to the principal debtor it does not absolve the sureties from their liability under surety bond, where the surety had expressly contracted to remain liable notwithstanding the discharge of the principal and, therefore, the discharge of the principal cannot be said to be implied discharge of the surety.'

29. It is not mentioned in the judgment of the Madras High Court as to the interpretation of which provision of the Contract Act was involved in that case. But it was not a case of variance of the terms of the contract which was before that court. The case before the Madras High Court was of composition of a debt by a creditor with the principal debtor. Such a situation is dealt with by s. 135 and not s. 133 of the Contract Act. Sec 135 of the Contract Act reads as under :

'A contract between the creditor and the principal debtor, by which the creditor makes a composition with, or promises to give time to, or not to sue, the principal debtor, discharges the surety, unless the surety assents to such contract.'

30. As such the authority has no application on the provisions of s. 133 of the Contract Act.

31. But the question still remains as to whether a surety can waive his rights under s. 133 or 135 of the Contract Act and give consent in advance to the future acts in contravention of the provisions of those sections. The language those sections indicates that a consent in advance could not be given. The language of s. 133 debars a creditor from making a variance in the terms of the contract without the consent of the surety. That means that if there is a variance, the surety must consent to the same simultaneously and not in advance. The words 'without the surety's consent' clearly indicate that the consent should be given along with or at the time of variance and there could not be any such consent when no variance

had been made or even though the same was not in contemplation. Similarly, words 'unless the surety assents to such contract' occurring in s. 135 also indicate that the consent should exist at the time of the acts mentioned in the said provision. The word 'assent' suggests present tense which is indicative of the fact that the assent should be simultaneously with the composition, etc., mentioned in s. 135. In fact the statutory rights of a surety or guarantor cannot be abridged by a contractual provision in the deed of guarantee unless it had been specifically provided in s. 133 or s. 135 of the Contract Act that such rights were subject to a contract.

32. Under these circumstances not only the judgment of the Madras High Court has no application to the facts of the present case, I even beg to differ with the view expressed by the said High Court. The view expressed by the said High Court does not take note of the reasons whatever have been mentioned above by me above and, in fact, any of the provisions of the Contract Act have not been specifically mentioned or commented upon in the judgment.

33. Hence I find that the liability of defendant No. 4 stands discharged by virtue of the provisions of s. 133 of the Contract Act. Issue is decided, accordingly, in favor of defendant No. 4.

34. Issues Nos. 6 and 7.

35. These issues were not pressed at the time of arguments. Hence they are decided in favor of the plaintiff.

Issue No. 8 :

36. The case of the plaintiff is that already all the goods which were hypothecated with it have been sold. The plaintiff filed an application being I.A. No. 2862 of 1980, in which it is stated that in pursuance of an order of this court passed on September 24, 1971, some of the pledged goods were sold for Rs. 30,798.28, and that, statement in that respect was made on February 27, 1973. Plaintiff added in the application that thereafter the remaining goods were sold for a sum of Rs. 9,000 out of which Rs. 1,600 was adjusted towards expenditure, that a sum of Rs.

7,400 was available towards payment of the debt and that hence a sum of Rs. 38,199.28 stood paid to the plaintiff which it was ready to adjust against the amount due. Hence I find that a sum of Rs. 38,199.28 is to be adjusted against the amount due to the plaintiff and the balance only is recoverable and the issue is decided accordingly.

Issue No. 9 :

37. I have already held above that defendant No. 4 is not liable to pay any amount in view of the provision of s. 133 of the Indian Contract Act. thereforee, the question of a decision of this issue does not arise. Further, it may be mentioned that the sale of goods has already been made and on that account also a decision of this issue is not necessary.

Issues Nos. 10 & 12 :

38. I have already found above that defendant No. 4 is not liable to pay any amount to the plaintiff in view of the provisions of s. 133 of the Contract Act. Hence there is no question of the liability of defendant No. 4 being limited to the extent of the original sanctioned overdraft limit, and there is no question of the plaintiff having any right to recover his dues from defendant No. 4. Issues are decided accordingly against the plaintiff.

Issue No. 11 :

39. As already held, defendant No. 4 is not liable to pay any debt in view of the provisions of s. 133 of the Contract Act. But there is no provision whereby he is discharged from liability on account of any internal arrangement between defendants Nos. 1, 3 & 5. He was bound by the guarantee given in respect of the acts of the partnership firm, defendant No. 1, and their partners, i.e., defendants Nos. 2 & 3, even when they entered into an arrangement with defendant No. 5, but for the discharge of liability under s. 133 of the Contract Act. Issue is decided accordingly against defendant No. 4.

Issue No. 13 :

40. Defendants Nos. 2 & 3 were admittedly partners of the firm, defendant No. 1. They also admittedly signed the loaning documents in favor of the National Bank of Lahore Ltd. Internal arrangement made by them whereby they transferred the entire assets and liabilities of the firm to defendant No. 5, does not absolve them from their creditors and the creditors of the firm unless and until the creditors had accepted defendant No. 5 as the sole debtor in their place.

41. Hence, both defendants Nos. 2 & 3 are liable to pay the amount. But it may be mentioned that defendant No. 3 died during the pendency of the suit and his legal representatives were not brought on record on account of which the suit against him stands abated. thereforee, it in only defendant No. 2, who is liable to pay the debt. Issue is decided accordingly.

Issue No. 14 :

42. Plaintiff has placed on record certified copy of the statement of account, ex. PA, which shows that a sum of Rs. 1,51,717.39 was due to the plaintiff.

43. The plaintiff has already received a sum of Rs. 38,199.28. Hence the amount due to the plaintiff is Rs. 1,13,518.11 which it is entitled to recover from defendant No. 2 alone. Suit is liable to be dismissed against the other defendants.

44. I, thereforee, pass a decree for Rs. 1,13,518.11 in favor of the plaintiff and against defendant No. 2 with costs and with interest at 9% per annum from the date of the institution of the suit till the date of payment of the amount. Suit against defendants Nos. 3 to 5 is hereby dismissed, but defendant Nos. 4 & 5 and the plaintiff are left to bear their own costs. There is no question of costs of defendant No. 3 because suit against him has been dismissed on account of abatement.

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