

**HIGH COURT OF BOMBAY**

**BENCH : B.P. Colabawalla and Somasekhar Sundaresan, JJ.**

**Date of Decided : 18-03-2024**

Writ Petition No. 1673 of 2005

**ASSETS RECONSTRUCTION COMPANY (INDIA) LTD.**

**Vs.**

**UNION OF INDIA AND OTHERS**

**Legislation:**

Recovery of Debts Due to Banks and Financial Institutions Act, 1993

Transfer of Property Act, 1882

Maharashtra Co-operative Societies Act, 1960

**Subject:** Challenge against DRAT's order upholding DRT's approval for the sale of a mortgaged apartment below the approved reserve price - Consideration of rights of a mortgagee and a licensee.

**Headnotes:**

Mortgagee vs. Licensee Rights Dispute – Petition challenging the approval of sale of mortgaged property at a price below the reserve price set by DRT, treating a licensee as a secured creditor over the mortgagee. [Paras 2, 14-15, 32-34]

Procedural and Factual Background – Mortgage created by Karias in favor of ARCIL (Petitioner), license agreement between Karias and SCB. DRT and DRAT treated SCB as having a "charge" on the property, overlooking the superior rights of the mortgagee. [Paras 3, 7-11, 26-27]

Principle of Law – Emphasis on established legal principles prioritizing the rights of mortgagees over licensees, highlighting misinterpretation in the Impugned Orders. [Paras 5, 14-15, 21-24, 28-29]

Erroneous Consideration by DRT and DRAT – Incorrectly treating SCB, a licensee, as a secured creditor with a "charge" over the property, resulting in the wrongful sale of the mortgaged asset. [Paras 7, 15, 23, 32]

Legal Precedents – Reference to cases establishing priority of mortgagee's rights over those of a licensee or lessee, and the ineffectiveness of a license in overriding mortgage rights. [Paras 18-19, 23]

Equitable Considerations – Discussion on SCB's knowledge of the mortgage and initiation of separate recovery proceedings, with the court finding no equities favoring SCB. [Paras 25-28]

Directions and Conclusions – Quashing the Impugned Orders, directing a fresh auction in accordance with the law, affirming the mortgagee's priority, and instructing a refund to the Purported Acquirers with interest. [Paras 33-35]

**Referred Cases:**

- Sumikin Bussan (Hong Kong) International Limited Vs. Manharlal Trikamdass Mody & Anr. [(2006) SCC OnLine Bom. 506]
- LKP Finance Ltd. vs. International Asset Reconstruction Co. Pvt. Ltd. [2013 (1) Mh.L.J. 743]
- Goldie Sud vs. Punjab National Bank & Ors. [2011(2) Mh.L.J. 944]

**Representing Advocates:**

- Ms. Vinodini Srinivasan for Petitioner

- Mr. Cherag Balsara for Purported Acquirers

**JUDGMENT**

**Somasekhar Sundaresan, J.** - With the consent of the parties, writ petition is taken up for final disposal.

2. This writ petition challenges an order passed by the Debt Recovery Appellate Tribunal ("DRAT") upholding an order passed by the Debt Recovery Tribunal ("DRT"), allowing the sale of a mortgaged apartment at below the approved reserve price in an auction. For the reasons set out by us in this judgement, the orders of the DRT and the DRAT deserve to be quashed, with a direction to conduct the auction afresh in accordance with law, as declared in this judgement. The fundamental fallacy in them is that they have treated an unsecured creditor as a secured creditor and that too with priority over the secured creditors (beneficiaries of a mortgage over the secured asset).

**Factual Matrix:**

3. In a nutshell, the following core facts are relevant to adjudicate the petition:

(a) The Petitioner, Asset Reconstruction Company (India) Ltd. ("ARCIL"), is the beneficiary of a mortgage over Flat No. 61, 6th Floor, Basant Apartment, Navrang Basant Cooperative Society, 101, Cuffe Parade, Backbay Reclamation, Colaba, Mumbai 400 005 ("Secured Asset");

(b) The mortgage had been created on 15th May, 1998; by way of deposit of title deeds by Respondent Nos. 4 and 5; Mr. Kirit Karia and Ms. Nirupama Karia (collectively, the "Karias"); and the promoters of Respondent No. 3, Eastern Overseas Ltd. ("EOL"); to secure borrowings by EOL from a consortium of banks led by Indian Overseas Bank ("IOB");

(c) On 28th June, 2000, upon default by EOL, the Petitioner initiated proceedings to enforce the mortgage by filing Original Application No. 2458 of 2000 ("Original Application") before the DRT under the Recovery of Debts Due to Banks and Financial Institutions Act, 1993;

(d) About two months after the Original Application was filed and proceedings were underway, the Karias executed a leave and license agreement dated 20th August, 2000 ("LLA"), over the Secured Asset purporting to grant Respondent No. 6, Standard Chartered Bank ("SCB"), a bare license to use and occupy the Secured Asset as a residence for 24 months, retaining legal possession over the Secured Asset;

(e) The LLA entailed SCB placing a security deposit of Rs. 80 lakhs with the Karias, with a clause that if the security deposit was not repaid by the Karias

at the expiry or termination of the LLA, then SCB would have an irrevocable license to remain in occupation of the Secured Asset until the deposit is repaid with interest at the rate of 3% per month (36% per annum);

(f) SCB was unable to occupy the Secured Asset immediately since the housing society in which the Secured Asset is situated, refused SCB entry on the premise that approval of IOB (as the mortgagee) would be necessary (although the society had approved the execution of the LLA on 22nd August, 2000). The housing society wrote to SCB on 8th September, 2000, explicitly putting SCB to notice that the Secured Asset stood mortgaged;

(g) Owing to the housing society's stance, the Karias moved the First Co-operative Court at Mumbai constituted under the Maharashtra Co-operative Societies Act, 1960, with Case No. CCI/315/2000, behind the back of IOB, complaining about the society obstructing SCB from entering the property, and obtained an interim order dated 19th September, 2000, pursuant to which, SCB was allowed to occupy the Secured Asset;

(h) The LLA was subsequently registered by the Karias and SCB on 12th December, 2000;

(i) On 29th May, 2002, in proceedings in the Original Application, the DRT appointed a receiver with a power to sell the Secured Asset;

(j) SCB moved the DRT contending that the order dated 29th May, 2002 compromised SCB's right to receive a refund of its security deposit and its right to occupy the premises until refund of the security deposit;

(k) On 3rd September, 2002, the DRT passed an order recording an explicit finding that the mortgagee had superior rights. In the same order, the DRT ruled that the Secured Asset may be sold either after evicting SCB, or by leaving it to the purchaser of the Secured Asset to evict SCB. SCB was directed to pay its arrears of license fees. The latter option (of selling the Secured Asset leaving it to the purchaser to evict SCB) was pursued for sale of the Secured Asset;

(l) SCB filed a suit against the Karias for recovery of the security deposit, being Suit No.1925 of 2003 ("SCB Recovery Suit"), and the same is pending in this High Court;

(m) On 6th February, 2004, the terms and conditions were set by the DRT Receiver for an auction of the Secured Asset on an as-is-where-is basis,

including a term that the auction may not be at a price lower than a reserve price to be fixed;

(n) A public notice for the auction was given on 17th February, 2004, and the bidders were all informed about the LLA with SCB;

(o) Based on an independent valuation report dated 8th March, 2004, the DRT, on the same date, fixed the reserve price for sale of the Secured Asset at Rs. 1.17 crores. The reserve price was naturally not made public but it was a benchmark by which the success of the auction would be assessed by the DRT;

(p) The auction was thereafter conducted on 9th March, 2004. Two offers were received. Respondents No. 7 and 8, Mr. Satindernath Khanna and Ms. Vandana G ("Purported Acquirers"), made a bid of Rs. 31 lakhs for the Secured Asset, and another offer of Rs. 20 lakhs was received. The Purported Acquirers raised their bid to Rs. 33 lakhs at the suggestion of the DRT Receiver;

(q) The DRT Receiver declared the auction as having failed, stating that there was a "vast difference" between the reserve price fixed by the DRT and the bid by the Purported Acquirers. A report declaring such failure was prepared for consideration by the DRT;

(r) The Purported Acquirers asserted by a letter from their advocates, dated 15th March, 2004, sent to the Receiver, that their offer was effectively for an amount of Rs. 1.70 crores (Rs. 33 lakhs being the bid amount; Rs.90 lakhs being the amount of security deposit payable to SCB; Rs. 45 lakhs being the accumulated interest payable to SCB; and a sum of Rs.2.93 lakhs being arrears payable to the society);

(s) Surprisingly, and even though the price offered by the Purported Acquirers was way below the reserved price of Rs.1.17 crores, the DRT, vide an order dated 19th March, 2004 ("DRT Order"), overruled the failure report filed by the DRT Receiver and declared the auction a success in favour of the Purported Acquirers. The DRT approved the sale of the Secured Asset to the Purported Acquirers, by ruling that SCB had a "charge" for Rs. 90 lakhs. The DRT ruled that the bid amount of Rs. 33 lakhs was proper, taking into account the attendant liability and the outgoings payable to the society, and asked the Purported Acquirers to settle the dues of SCB independently. The DRT did

not rule what the amount payable to SCB was, and did not seek a deposit of any amount that, in its view, was payable to SCB;

(t) On appeal, the DRAT, vide an order dated 5th November, 2004 ("DRAT Order"), approved the DRT's order in near-identical terms, effectively treating SCB as a secured creditor with a charge, and approving the sale of the Secured Asset at below the reserve price;

(u) The writ petition was filed on 25th February 2005. After the filing of the petition, the debt of the IOB-led consortium eventually came to be assigned to the Petitioner and the petition came to be amended, replacing IOB with ARCIL on 22nd March, 2012; and

(v) On 28th March, 2005, a status quo order was passed by this Court. On 26th September, 2005, rule was issued and the status quo has continued since then.

#### **Core Issue and Approach:**

4. We are conscious of our jurisdiction being that of a writ court, and have accordingly examined the material on record from the perspective of whether due process and the foundational elements of law have been complied with. We are faced with considering the rights of a mortgagee (Petitioner), the rights of a licensee (SCB) and those claiming derived benefits from such rights of the licensee (Purported Acquirers). The Karias did not participate in the proceedings. Counsels who have appeared before us for the other parties, suggest that the Karias are absconding, but as will be seen, that need not detain us from considering and disposing of this writ petition.

5. In our opinion, the DRT Order and the DRAT Order (collectively, "Impugned Orders") are perverse and are manifestly contrary to law. The Impugned Orders turn on the head, well-established principles of law governing priority of security interests, the rules governing the auction that was conducted, and indeed the core principles of the Transfer of Property Act, 1882 ("ToP Act").

#### **Contentions of the Parties:**

6. We have heard at length the learned counsel appearing on behalf of the Petitioner, the Purported Acquirers and SCB. Each of them has also filed written submissions to summarize their stance, which has been helpful in crystallising the issues to be dealt with.

7. Ms. Vinodini Srinivasan, the Learned Counsel appearing for the Petitioner, lucidly underlined the foundational errors in law that undermine the validity of the Impugned Orders. Fundamentally, the error in the Impugned Orders lies in the fact that the sale in the auction was approved for a value of Rs. 33 lakhs, far below the reserve price of Rs. 1.17 crores, for no evident reason other than treating SCB's interests as being a "charge" and that too with a right to receive from the proceeds of the sale, in full, and in priority over the other creditors. Effectively, Ms. Srinivasan would argue, the DRT and the DRAT have decreed the SCB Recovery Suit filed by SCB for recovery of the security deposit that is pending in this High Court, assuming SCB had been able to successfully conduct trial and prove that the amount was payable to it in full. Worse, the said suit has effectively been executed against the mortgagees by the outcome in the DRT Order and the DRAT Order.

8. Mr. Cherag Balsara, learned counsel on behalf of the Purported Acquirers, essentially argued that the Petitioner (the successor in interest to IOB) can be said to have acquiesced to the rights enjoyed by SCB. He would argue that the LLA was a registered document and the consequences of non refund of the security deposit viz. the entitlement of SCB to remain in possession until it receives a full refund with interest, indeed constituted a "charge" or "encumbrance" in favour of SCB. According to Mr. Balsara, despite being aware of the existence of the LLA, IOB did not initiate any steps to evict SCB. Instead, IOB agreed to the option of a sale of the Secured Asset, leaving it to the purchaser to deal with SCB (contained in the DRT's order dated 3rd September 2002) and that position has "attained finality". Consequently, he would argue, IOB (and therefore the Petitioner) is estopped from raising any dispute over the validity of the auction price, which had been approved by not only the DRT but also the DRAT. Mr. Balsara would further emphasise that the terms and conditions for the auction had been finalized by the officers of IOB, and therefore, there has been a complete acquiescence to the position the Petitioner finds itself in. As regards the deep discount of the auction price to the reserve price, Mr. Balsara would assert that the valuation had not factored in the effect of SCB being in occupation of the Secured Asset and therefore the reserve price of Rs.1.17 Crores was merely an indicative price for market value between a willing buyer and a willing seller without regard to the problems posed by SCB's rights under the LLA.

9. Therefore, Mr.Balsara would argue, the effective price offered by the Purported Acquirers should be considered as Rs. 1.23 Crores (the sum of



Rs.33 lakhs bid in the auction being enhanced by the amount of Rs.80 lakhs or more payable to SCB). In conclusion, Mr.Balsara would argue that the DRT and the DRAT have exercised judicial discretion in a non-arbitrary manner to confirm the sale of the Secured Asset at Rs.33 lakhs, since in their view, it would have been grossly unreasonable and illogical to expect full market value for the Secured Asset in the absence of the ability to deliver vacant and peaceful possession of the Secured Asset. Mr.Balsara would further suggest that the Purported Acquirers were willing to deposit a sum of Rs.90 lakhs in the SCB Recovery Suit, subject to the outcome of such suit, in which, SCB was seeking to recover the deposit amount.

10. In its written submissions, SCB has argued that it was unaware of the mortgage created by the Karias in favour of the Petitioner, and it was unaware of the Original Application to enforce the mortgage. Towards this end, SCB would purport to rely on the representations made by the Karias in the LLA that there were no proceedings in any Court which would prejudicially affect the licensee's right to use the Secured Asset. Since the Karias now appeared to be absconding, SCB, as a counter party to the LLA in good faith, without notice of the mortgage or its enforcement, should not be considered to be a trespasser to the Secured Asset. Upon becoming aware of the proceedings pursuant to the Original Application to enforce the mortgage, SCB would argue, it chose to intervene in those proceedings.

11. SCB also argued that it had a right to remain in occupation of the Secured Asset until the security deposit with interest thereon as contracted with the Karias is refunded, on the premise that the license in SCB's favour is irrecoverable and such license could not be extinguished by reason of a transfer of the Secured Asset. The transferee would merely step into the shoes of the Karias and would need to adopt eviction proceedings to remove SCB from the premises. Curiously, SCB would also argue that the LLA cannot be equated with a lease in order to attract Section 65-A of the ToP Act particularly since the memorandum of deposit of title deeds did not contain an explicit restriction on execution of such a license agreement. To summarize, SCB would argue that it is a bonafide licensee for value, without notice of the mortgage, and its right to use and occupy the Secured Asset would override any other interest in the Secured Asset unless and until the security deposit along with interest is refunded.

#### **Findings and Conclusions:**



12. We have given our anxious consideration to the material on record and to the pleadings and contentions of the parties. The bid by the Purported Acquirers being below the reserve price, is adequate reason to set aside the outcome in the auction. However, we have examined the material on record to deal with the argument that despite the yawning gap between the reserve price and the auction price, the auction outcome was fair, considering that the Impugned Orders have sought to reconcile the competing interests of the Petitioner and of SCB, and thereby justified the bid of the Purported Acquirers.

13. In a nutshell, SCB is a creditor of the Karias and may have a cause of action to recover its dues from the Karias, for which it has instituted the SCB Recovery Suit, which would be eventually adjudicated. Should SCB succeed, the decree therein would have to be executed against the Karias.

14. The issue at hand is not whether SCB may have a legitimate right to recovery of the security deposit under its LLA which was admittedly entered into not only after the creation of the mortgage in favour of the Petitioner, but also after the Original Application was filed. Instead, the issue at hand is whether SCB has any right over the Secured Asset to recover its dues from the Karias. The Petitioner being a prior mortgagee in whose favour the Karias created the mortgage over the Secured Asset, it is the Petitioner who has the foremost and highest priority over recovery of proceeds of sale of the Secured Asset. SCB does not have a charge over the Secured Asset, and even if one were to treat its rights under the LLA as a fetter of some kind over the Secured Asset (and thereby an "encumbrance"), such fetter cannot in any manner rank superior to the rights of the mortgagee over the Secured Asset.

15. In our opinion, the Impugned Orders deserve to be set aside on the following compelling counts, each of which undermines the validity of the Impugned Orders:-

(a) SCB, a mere unsecured creditor of the Karias, which would have to stand in queue behind the secured creditors of the Karias in a bankruptcy event, has been treated in the Impugned Orders as a holder of a "charge". Thereby, the Impugned Orders have elevated SCB's status to that of a secured creditor;

(b) The LLA itself contained provisions stating that (i) legal possession of the Secured Asset would not vest in SCB; (ii) the license was a bare license to use the Secured Asset as a residence; and (iii) no other right, title or interest

would vest in SCB by reason of the LLA. Yet, the Impugned Orders have treated SCB as a beneficiary of a "charge" and that too as a secured creditor with the highest priority, ahead of the consortium of banks led by IOB, which had the highest security interest in the Secured Asset;

(c) Therefore, not only was the unsecured creditor i.e. SCB treated as a secured creditor, the amount of unsecured debt claimed by SCB has effectively been treated as being payable to SCB, from the proceeds of sale of the Secured Asset, in priority to the mortgagees of the Secured Asset. Effectively, the DRT and DRAT have accepted the Purported Acquirers' depiction of their bid amount of Rs. 33 lakh as being far higher than that amount (the Purported Acquirers had claimed that the effective bid was for Rs. 1.70 crores). By taking the unsecured debt owed to SCB as being payable in full and with first priority, the secured creditors with a mortgage over the Secured Asset, have been made to take a hair-cut in what they can get from the sale of the Secured Asset;

(d) In the process, the Secured Asset is being sold for a value far lower than even the reserve price, which in itself, is a ground for interference by reason of the sale being in direct conflict with a core condition applicable to the auction;

(e) Under Section 65-A of the ToP Act, no lease of a mortgaged property may be made for a period exceeding three years, and no clause for renewal may be contracted. The agreement with SCB is a mere leave and license agreement and not even a lease, and it purports to contain a perpetual license pending repayment of security deposit with 36% interest - provisions that must necessarily yield to the mortgage being enforced;

(f) Despite a licensee being a position inferior to a lessee, and despite even a lessee not having any right to retain possession beyond three years in such property, the Impugned Orders effectively endorse SCB as having a superior right - only because of the foundational error of treating SCB's rights as a "charge" or "encumbrance", when it did not even have a contractual right to possession, being a recipient of a bare license to use the Secured Asset;

(g) Worse, the manner in which the LLA was executed and SCB entered upon the premises, does not even point to any equities being available either to SCB or to the Purported Acquirers, who derive benefit on the premise of SCB's rights. The LLA was created on 20th August, 2000, well after the institution of the Original Application on 28th June 2000. Besides, in the teeth

of objection from the housing society, SCB gained access to the premises of the Secured Asset by the Karias having adopted proceedings behind the back of IOB, when SCB had full notice that IOB's mortgage interests were the reason for the society not permitting access;

(h) It is the DRT that had the power to enforce the mortgage and hand over the Secured Asset to the Petitioner. SCB would have had to vacate the Secured Asset upon enforcement of the mortgagee's rights. It is SCB that would have to stand in queue as an unsecured creditor in the bankruptcy of the Karias. However, the Impugned Orders treat SCB as having a "charge" and an "encumbrance" over the Secured Asset and over the proceeds of the sale of the Secured Asset;

(i) SCB's occupation of the Secured Asset, with full knowledge of the mortgage, was subject to the outcome of the proceedings in enforcement of the mortgage, which had been initiated even before the LLA was executed. Strangely, the DRT has indeed ruled that SCB's rights are inferior to the rights of the mortgagees, and yet, on the premise that due process for eviction would have to be taken, SCB's dues have been treated as having priority over the dues payable to the mortgagee. This is the only means to justify the bid of the Purported Acquirers in the sum of Rs. 33 lakhs, which is way below the reserve price of Rs. 1.17 crores;

(j) On the face of it, the bid having been way below the reserve price, the auction ought to have been declared a failure - a position that the DRT Receiver rightly set out for acceptance by the DRT, which, inexplicably, and in gross error, overruled and confirmed the sale to the Purported Acquirers; and

(k) Under Section 52 of the ToP Act, where any right to immovable property is directly and specifically in question in a suit, the property cannot be dealt with by any party to the suit so as to affect the rights of any other party to the suit, except under the authority of the court. This position would obtain from the date of instituting the proceedings and remain until disposal by a final decree. The LLA was evidently created well after the presentation of the Original Application before the DRT. The DRT ought to have dealt with this factual position, and ruled on the same as a matter of law. The DRT did recognise that the rights of the secured creditors were superior and yet adopted a stance that some other proceedings would be necessary to evict SCB, and thereby ruled that SCB had a charge. Therefore, the DRT justified

the approval of the Purported Acquirers' bid amount of Rs. 33 lakhs, in the teeth of the reserve price of Rs. 1.17 crores, treating the amount purportedly payable to SCB as being added to the bid amount.

16. To put it in a nutshell, SCB, the unsecured creditor was now, by virtue of the Impugned Orders converted into a secured creditor, and worse, in preference to the consortium of banks led by IOB, the secured creditors, whose interest is now owned by the Petitioner. Even if we were to assume for the sake of argument that the LLA created any sort of "charge" in favour of SCB, it would make no difference for the simple reason that the LLA executed with SCB was way after the mortgage created in favour of IOB (now assigned to the Petitioner) and even after the Original Application was filed by IOB in the DRT. Therefore, any so-called "charge" of SCB would in any event be subservient to the charge of IOB (now the Petitioner). Yet, the effect of the Impugned Orders are that SCB will get priority over and above IOB.

17. The LLA having been executed after initiation of the proceedings for enforcement of the mortgage, and the entry of SCB into the premises of the Secured Asset behind the back of the mortgagee, inexorably lead to even equities not being in favour of SCB, on whose strength, the Purported Acquirers seek to justify that their bid was made at a deep discount to the reserve price. SCB having been treated as a holder of a "charge" and such charge being effectively treated as superior to even a mortgagee, we are left with no option but to set aside the Impugned Orders and direct the DRT to conduct the auction afresh.

**Sumikin Bussan and its implications :**

18. Both SCB and the Purported Acquirers sought to press into service a judgment by Division Bench of this Court, in the case of Sumikin Bussan (Hong Kong) International Limited Vs. Manharlal Trikamdas Mody & Anr. [(2006) SCC OnLine Bom. 506] ("Sumikin Bussan") to argue that parties who have contracted that a license would become irrevocable, would have conferred on the licensee the right to use the premises until the security deposits were refunded. Sumikin Bussan is of no assistance to them to argue that such right of a licensee would rank superior to the rights of a mortgagee and thereby give an unsecured creditor priority over secured creditors.

19. To begin with, the mortgage over the Secured Asset was created as security from the Karias in favour of the consortium of banks led by IOB for loans advanced to EOL, well prior to the execution of the LLA. The LLA was

executed by the Karias in favour of SCB subsequently. In other words, the Karias gave SCB a license to use the mortgaged property. We are not concerned with the interpretation of the contractual terms of the LLA and we are not resolving a dispute between the parties to the LLA - that would be the subject matter of the SCB Recovery Suit. In *Sumikin Bussan*, the Division Bench was essentially dealing with a dispute between a licensor and a licensee in that case. *Sumikin Bussan* has nothing to do with giving an unsecured licensee priority over a secured mortgagee.

20. As stated earlier, at the heart of this writ petition is the question of whether (as ruled by the DRT and DRAT) the conflict between the rights of a licensee under the LLA and the rights of a mortgagee can be resolved by giving primacy to the unsecured licensee, making the secured mortgagee, subservient to the unsecured creditor. *Sumikin Bussan* is of no assistance in resolving this conflict of rights in a manner that places the unsecured licensee above the secured mortgagee.

21. In any case, the LLA was nothing but a mere bare license to use the mortgaged asset as a residence. Even a bare perusal of the LLA would show that under Clause 22(b) of the LLA, it is the Karias who are in "in legal possession and full charge and control of" the Secured Asset at all times. It is an explicit provision in the LLA that the LLA was "a mere license" and SCB shall at no time be deemed to have "exclusive possession" of the Secured Asset.

22. Clause 15 of the LLA also explicitly provided that neither SCB nor any person claiming through SCB would be entitled to put up any claim of tenancy, sub-tenancy or any other adverse right or title in the Secured Asset. This clause would bring the Purported Acquirers within its sweep. This clause explicitly provided that the LLA would create no such right or title over the Secured Asset in favour of SCB, which had "a bare license with a mere limited rights of user for the residence purpose only".

23. A decision by another Division Bench of this Court states that the law on the subject in succinct terms, is the one rendered in **LKP Finance Ltd. vs. International Asset Reconstruction Co. Pvt. Ltd. [2013 (1) Mh.L.J. 743]**. Dealing with rights of a person with possessory lien in comparison with the rights of a mortgagee, the following extracts are noteworthy:-

"7. In the instant case, the petitioner admittedly is neither a tenant nor a lessee of the mortgage premises and only claims to have right over the mortgaged

premises on the basis of promissory lien. It is also not in dispute that the original borrower had created mortgage of secured premises in favour of the respondent bank (consortium) while the petitioner has been or was permitted by the original borrower to occupy the mortgage premises. The short question which arises for consideration is.....

"Whether the mortgagor can permit the petitioner to occupy the mortgaged premises after creating mortgage in contravention of provisions of section 65-A of the Transfer of Property Act? "

It is brought to the notice of this Court that the said issue is considered by the Division Bench of Madras High Court in the case of **Sree Lakshmi Products Rep. by its partner vs. State Bank of India, AIR 2007 Madras 148** in the backdrop of provisions of section 65-A of the Transfer of Property Act. Relevant observations made in paragraph 8 of the said decision, reads thus:

"8. In **Sanjeev Bansal v. Oman International Bank SAOG, 2006 (4) BC 299 (DB)** Delhi High Court, a similar contention was raised by the petitioner therein that he being a tenant and in physical possession of the mortgaged property is protected under the provisions of the Delhi Rent Control Act and cannot be dispossessed without taking recourse to the provisions of the Delhi Rent Control Act. Repelling this contention the Court held that the protection afforded by the Rent Control Act to a tenant is from the landlord of the premises and the landlord of the premises cannot recover possession from the tenant unless he takes recourse to any of the grounds as available to him under Rent Control Act and the right of the tenant is fully protected notwithstanding anything contrary contained in any other law or contract. This protection is however not available against the mortgagee who seeks to enforce his right under the SARFAESI Act against the principal borrower who had mortgaged the property in question by duly and validly executing the memorandum of mortgage in favour of the mortgagee. The Court further held that section 65-A of the Transfer of Property Act clearly mandates that the duration of lease to be executed by the mortgagor cannot exceed 3 years. The Court therefore, concluded in paragraph 6 as follows:

"Manifestly the said unregistered lease was created for the alleged unlimited period through unregistered lease deed in complete contravention of section 65-A of the Transfer of Property Act as per the said provision of section 65-A, the lessee can enjoy the protection if the lease is created by the mortgagor in conformity with the mandate of requirements laid down in section 65-A of



Transfer of Property Act and not otherwise. Neither the mortgagor nor the lessee can defeat the right of mortgagee and no lessee can claim any protection unless his tenancy is as per the requirements of section 65-A of Transfer of Property Act. "

8. In the present case, the claim of the respondent bank stands on a much better footing since the petitioner is neither a tenant nor lessee of the mortgaged premises and claims its right over the mortgaged premises on the basis of possessory lien. In view of the facts and circumstances involved in the present case it is evident that the mortgagor though in a given case can let out the mortgaged premises which will be binding on the mortgagee, however, it must be as per the mandate of section 65-A of the Transfer of Property Act the duration of such lease cannot exceed three years and therefore the observations made in paragraph 8 of the decision makes it implicitly clear that neither the mortgagor nor the lessee can defeat the right of mortgagee and no lessee can claim any protection unless its tenancy is as per the requirement of section 65-A of the Transfer of Property Act. In the instant case the original borrower has not let out the mortgaged premises to the petitioner nor the petitioner claims possession over the mortgaged premises on the basis of any lease deed but claims the promissory lien over the premises on the basis of the letter dated 1-11-2011 issued by the Authorised Signatory, without there being any document of lease or tenancy created in its favour. Therefore, in view of requirement laid down in section 65-A of the Transfer of Property Act, the petitioner cannot claim any protection only on the basis of promissory lien. We answer the question in negative. [Emphasis Supplied]

24. Applying the aforesaid articulation to the case at hand, it is evident that SCB may be a protectee against the Karias on terms reduced to writing in the LLA. SCB would have recourse to the Karias to enforce its protection. However, SCB would simply be unable to claim any protection against IOB and the Petitioner, and those claiming through such mortgagee. SCB cannot claim to have any recourse to the proceeds of the sale of the Secured Asset, and towards this end, the DRT and the DRAT failed to apply their mind to this vital facet of the matter, and instead, perhaps thinking of their decision as a practical matter, permitted the sale in the auction at a price below the reserve price, justifying such sale by alluding to SCB having a "charge" and taking into account the amount they believed would need to be paid to SCB for SCB to give up possession.



**Equitable Considerations do not arise:**

25. The submission by the Purported Acquirers and by SCB, that SCB became a party to the LLA without notice of the mortgage does not inspire confidence of a degree that could alter our view that the Impugned Orders deserve to be set aside. It is a matter of record that the LLA was executed after the proceedings pursuant to the Original Application were underway. It is also a matter of record that on 13th September 2000, the housing society informed SCB about the mortgage over the Secured Asset, insisting that permission from IOB should be obtained. By this time, SCB obtained knowledge of the mortgage or at least that of a purported mortgage. Worse, the Karias initiated litigation in the Co-operative Court constituted under the Maharashtra Co-operative Societies Act, 1960, without making the mortgagee a party, to obtain an interim order granting SCB entry into the premises.

26. Even at this stage, SCB, itself being a commercial bank, and therefore, fully conversant with the law on security interests, incredibly, chose to avail of the benefit of access to the Secured Asset obtained from the Co-operative Court by the Karias behind the back of the mortgagee, and that too with full knowledge that the Secured Asset was mortgaged. SCB and the Karias went on to register the LLA on 12th December, 2000, despite SCB too being aware by this time, about the existence of the mortgage, and having knowledge of the Original Application.

27. It is inexplicable that in these proceedings SCB should seek to differentiate between a license and a lease as a matter of law, particularly when the right under a license would be inferior to the right under a lease. The mere bare license to use the Secured Asset as a residence is not even on par with a lease. Even if one were to argue that the LLA got converted into a lease by reason of the irrevocable license pending refund of the security deposit with security interest, the provisions of Section 65-A of ToP Act would stare SCB (and indeed the Purported Acquirers) in the face. In that event, the statutory cap on the lease period would have been three years (it could not be irrevocable and perpetual), and the interest of the mortgagee would override the interest of the lessee.

28. It would hardly lie in the mouth of the Purported Acquirers who were bidding on an as-is-where-is basis to canvass SCB's case to get around the fact that they were bidding for a property that had been mortgaged and which

mortgage was in the process of being enforced even before the LLA had been executed, to somehow justify the deep discount to the reserve price and justify the Impugned Orders as being a product of equitable and fair exercise of judicial discretion. While SCB's conduct does not give rise to equities, even if it did, in our opinion, equity considerations cannot undermine the explicit position in law, to give an unsecured creditor a march over a mortgage in access to the proceeds of sale of a mortgaged asset. Equity supplements the law and it cannot supplant the law.

29. As a matter of fact, considering that proceedings before the DRT and DRAT were proceedings dealing with enforcement of a mortgage, both these forums have erred in not appreciating the evident position discernible from a bare perusal of the material on record and the applicable law. The LLA, pointing towards being a contrivance devised to undermine the enforcement of the mortgage over the Secured Asset, the DRT and DRAT ought to have applied their minds to the core issue of whether a bid below the reserve price could be justified by resort to treating SCB as enjoying a charge with a right to get the value ascribed to the Secured Asset. In effect, both forums ended up granting primacy to an unsecured licensee over the secured mortgagee, by highlighting that some separate eviction proceedings would have to be undertaken, instead of ruling upon the law and applying to the facts, which would have rightly declared the right of a licensee to be inferior to the right of a mortgagee, leaving it to SCB to prosecute recovery against the Karias in the SCB Recovery Suit, rather than enabling recovery against the Secured Asset.

30. The vital nature of the element of the reserve price in auctions in security enforcement is well summarised by a Division Bench of this Court in **Goldie Sud vs. Punjab National Bank & Ors. [2011(2) Mh.L.J. 944]** in the following words:

"8. In the present case, the terms and conditions of sale provided that the property would not be sold at a price less than the reserve price. There was, therefore, in this case a clear indication by the first respondent that it would not agree to any amount less than the reserve price. No bidder was therefore entitled to assume that a bid at an amount less than the reserve price would possibly meet the consent of the secured creditor. The secured creditor had in advance clearly set forth its intent not to accept any bid below the reserve price. [Emphasis Supplied]

31. The DRT and the DRAT ought to have been mindful of the fact that the reserve price was one of the core features of the auction. Just as the Purported Acquirers submit that IOB had agreed to the approach of the DRT to auctioning the Secured Asset (for the element of leaving it to the buyer to evict SCB after the acquisition), it must also be remembered that an integral feature of the terms of the auction was that the sale would not be at below the reserve price. Be that as it may, both forums have erred by wishing away the relevance of the reserve price fixed during the auction. It is true that the reserve price was not publicly disseminated - obviously, because dissemination of such price could have led to the auction process being rigged with cartelisation, frustrating the discovery of the best price. However, the DRT Receiver, upon receiving the bids and comparing them with the DRT-approved reserve price, rightly concluded that the auction deserved to be declared as a failure. The only means for the DRT over-ruling this obvious position was the treatment of SCB as a beneficiary of a "charge" and that too superior to the mortgagee, which aspect has been dealt with extensively by us earlier.

32. We are surprised that SCB, itself a commercial bank that must have multiple enforcement proceedings against those who borrow from it, and therefore conversant with the law on asset recovery and priority of charges, has conducted itself in the aforesaid manner. SCB has indeed instituted the SCB Recovery Suit against the Karias for refund of the security deposit. Effectively, the Impugned Orders have not only granted relief on issues that form the subject matter of the SCB Recovery Suit, but also execute the same against the Secured Asset (the execution would have had to be against the Karias). We say nothing more, particularly since we are relegating the matter to the DRT to conduct the proceedings afresh and to auction the Secured Asset in accordance with law and to rule on the same in accordance with the law declared by us in this judgement.

33. We must record that we enabled the parties to engage with one another in a commercial and practical manner to see if they could work out a resolution with a formulation that would resolve their disputes by mutual consent. However, the parties could not resolve their disputes and differences, perhaps each of them sanguine about their respective positions.

**Directions Issued:**

34. Consequently, in these circumstances, we allow the writ petition in the following terms:

(a) The DRT Order upholding the sale of the Secured Asset to the Purported Acquirers, and all consequential actions such as issuance of the sale certificate and other formalities flowing from the DRT order are hereby quashed and set aside;

(b) The DRT is directed to conduct and oversee an auction afresh in accordance with law, treating the mortgagee as the only secured creditor with a charge in the form of the mortgage over the Secured Asset;

(c) SCB is free to pursue recovery proceedings against the Karias to recover the amount so deposited, which is in fact, the subject matter of the SCB Recovery Suit;

(d) Since the non-compliant auction was conducted way back in 2004, we request the DRT to endeavour to complete the auction and dispose of the Original Application as expeditiously as possible, and endeavour to do so within a period of six months from today;

(e) The Purported Acquirers shall be entitled to refund of any amounts deposited by them towards the purchase of the Secured Asset with interest that would have been earned thereon from the date of the payment by them until the date of the refund. We direct such refund to be effected within a period of four weeks from today.

35. Rule is made absolute in the aforesaid terms and the writ petition is also disposed of in terms thereof. In the peculiar circumstances of the case, we have persuaded ourselves to make no order as to costs in these proceedings. Parties are at liberty to pursue applications for costs before the DRT.

36. This judgment/order will be digitally signed by the Private Secretary/ Personal Assistant of this Court. All concerned will act on production by fax or email of a digitally signed copy of this judgment/order.

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