

STATE OF MADHYA PRADESH

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v.

KALURAM

September 5, 1966

[K. N. WANCHOO, J. C. SHAH AND R. S. BACHAWAT, JJ.]

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Indian Contract Act, s. 141—Forest contract—Contractor allowed to remove wood without making due payment—Security for payment thus lost—Surety whether discharged.

At an auction held by the Divisional Forest Officer Hoshangabad Division for sale of 'felled trees', one J was declared the highest bidder. The amount of the bid was payable in four instalments. According to the contract the Forest Contract Rules were binding on the contractor, and the contractor could be prevented from removing the forest produce in case he made default in payment of the instalments due. One K had stood surety for J along with another surety. J paid the first instalment due under the contract but without making the subsequent payments was allowed to remove the whole forest produce contracted to be sold from the contract area. The State of Madhya Pradesh thereafter took proceedings to recover from K as arrears of land revenue the amount due from J. K commenced an auction for a declaration that he was not liable to pay the dues recoverable from J and for an injunction against the State. He contended that since the Forest Department had allowed J to remove the forest produce the security was lost and he stood discharged. The trial Court and the High Court both held in K's favour. The State of Madhya Pradesh appealed to this Court by special leave.

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HELD : (i) The expression "security" in s. 141 of the Indian Contract Act is not used in any technical sense : it includes all rights which the creditor has against the property at the date of the contract. The surety is entitled on payment of the debt or performance of all that he is liable for to the benefit of the rights of the creditor against the principal debtor which arise out of the transaction which given rise to the right or liability : he is therefore on payment of the amount due by the principal debtor entitled to be put in the same position in which the creditor stood in relation to the principal debtor. If the creditor has lost or parted with the security without the consent of the surety, the latter is by the express provision contained in s. 141, discharged to the extent of the value of the security lost or parted with. [272 E-G]

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Wulff and Billing v. Jay, L.R. (1872) 7 Q.B. 756, referred to.

(ii) The Forest Officer parted with the forest produce before receiving payment of the amount due by the contractor. Thereby the charge in favour of the State was seriously impaired and the statutory power to sell the produce for non-payment of the amount remaining due became, for all practical purposes, ineffective. Again, under the terms of the contract the Forest authorities had the right to prevent removal of the produce sold until the price was paid : that right was also lost. The right conferred by s. 83 of the Forest Act and under the terms of the contract to prevent removal and right to sell the produce for non-payment of the price, coupled with charge on the produce constituted the security of the State and that security was lost because the Forest Officers permitted removal of the produce by the contractor. [273 G-H]

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Accordingly the surety stood discharged from liability to pay the amount undertaken by him under the terms of the surety bond.

A CIVIL APPELLATE JURISDICTION: Civil Appeal No. 359 of 1964.
 Appeal by special leave from the judgment and decree dated September 29, 1961 of the Mádhya Pradesh High Court in First Appeal No. 123 of 1958.

B. Sen, J. P. Dube and I. N. Shroff, for the appellant.

B *B. C. Misra and S. S. Shukla*, for the respondent.

The Judgment of the Court was delivered by

C **Shah, J.** This is an appeal with special leave against the decree passed by the High Court of Madhya Pradesh in appeal No. 123 of 1958 confirming the decree of the Additional District Judge, Hoshangabad, decreeing the plaintiff's suit. The State of Madhya Pradesh has appealed to this Court.

D At an auction held on July 20, 1954 by the Divisional Forest Officer, Hoshangabad Division, for sale of "felled trees" in Coupe No. 66 Dhekna, Range Seoni, one Jagatram was declared the highest bidder and the trees were sold to him for Rs. 12,100. The amount of the bid was payable in four instalments of Rs. 3,025 each: the first instalment to be paid immediately on acceptance of the bid, the second on December 1, 1954, the third on February 1, 1955 and the fourth on May 1, 1955. Jagatram executed a contract in favour of the Governor of Madhya Pradesh in which were incorporated the terms and conditions of the sale. The following are the material terms of the contract:

E "2. The quantity of the said forest produce to be sold under this contract shall be the quantity which may exist at the time of executing this indenture or may come into existence thereafter in the contract area all of which forest contractor may collect and remove from it in accordance with the conditions herein contained during the period from the date the forest contractor furnishes the necessary coupe boundary certificate after inspection of the contract area to the 30th day of June, 1955,

F 3. The forest contractor shall commence his work of collecting and removing the said forest produce within one month after furnishing the necessary certificate mentioned in clause 2 above,

G 5. The said forest produce shall be removed by the forest contractor from the contract area by the routes specified in the following table and shall be presented by him for examination at one or other of the depots specified in that table:—

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6. The Forest contractor shall be subject to the Forest Contract Rules as amended from time to time.

and the Rules shall be deemed to be part of this contract in so far as they are applicable thereto :

Jagatram paid the first instalment due under the contract on July 28, 1954, and subscribed his signature to the terms of the contract. Nathuram and Kaluram stood sureties for him and executed the following bond:

“Whereas the Governor in order to secure the due performance of conditions of the above contract demanded security from the forest contractor, I

(1) Nathuram son of Kashiram resident of Chaterkheda

(2) Kaluram son of Jhandusingh resident of Pipaliya-Kalan, by occupation Agriculturists, surety on behalf of the forest contractor, undertake to discharge the liability of the forest contractor in case of any act, omission, negligence or default on the part of the forest contractor for any sum which may become payable by the forest contractor to the Governor by or under the conditions of the above contract.

I also agree that any sum which may be payable by me to the Governor under the terms of this bond shall be recoverable in the same manner as an arrear of land revenue.”

Jagatram removed almost the entire quantity of trees sold to him, but since he did not pay the remaining three instalments of the price, the State of Madhya Pradesh took proceedings to recover from Kaluram the amount due by Jagatram as arrears of land revenue.

Kaluram then commenced an action against the State of Madhya Pradesh for a declaration that he was not liable to pay the arrears of forest dues recoverable from Jagatram and for an injunction restraining the State from realising or from continuing the recovery proceedings with regard to those forest dues from him. The principal ground in support of the claim was that the forest authorities gave time to Jagatram and omitted to take steps which their duty to the surety required them to take i.e., prompt seizure and sale of the trees after the second instalment had fallen due, and since on that account his eventual remedy against Jagatram was impaired, he Kaluram stood discharged from liability as surety.

The Trial Court held that the forest officers were negligent in allowing the contractor Jagatram to remove the trees sold, and on that account the security of the surety was impaired, and the surety stood discharged for the whole amount recoverable from the contractor. The High Court of Madhya Pradesh confirmed the decree of the Trial Court.

A By virtue of cl. 6 of the terms of the contract, the relevant Forest Contract Rules were to be treated as part of the contract between Jagatram and the State. By r. 2 it was provided that all contracts whereby the Government sells forest produce to a purchaser shall be subject to the rules, insofar as they are applicable, and that those rules, shall be deemed to be binding on every forest contractor not only as rules made under the Forest Act, but also as conditions of his forest contract. By r. 6 the forest contractor is required to carry with him an "accessory licence" entitling him and his servants and agents to go upon the land specified in the contract and to do all acts necessary for the proper extraction of the forest produce purchased under the contract. Rule 8, provides:

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C "Where the consideration payable to Government under a forest contract is payable in instalments and the Divisional Forest Officer at any time before the last instalment is paid, considers that the value of the forest produce removed by the contractor exceeds the amount of the instalments already paid, the Divisional Forest Officer may stop further removal until the contractor has paid such further sum as may, in his opinion, be sufficient to cover such excess:

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Provided that, if in the opinion of any Forest Officer not below the rank of a Range Officer, it is necessary to take immediate action to prevent a breach of this rule, such Forest Officer—

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(i) may by notice in writing serve on the contractor, or his agent, if any, stating the grounds for the direction, require the contractor or his agent to stop further removal of the forest produce from the contract area; and

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(ii)"

By r. 12 a forest contractor is prohibited from removing any forest produce from the contract area, unless it is accompanied by a pass in the prescribed form signed by the contractor or his authorized agent. By r. 13 the forest contractor is required to remove forest produce only by the route or routes specified by rules under the Act, or by his forest contract, and to take all forest produce removed by him to such depots or places as may be similarly prescribed, for check and examination. Rule 16 requires the forest contractor to keep accounts of the quantity of forest produce removed by him from the contract area, and that such accounts shall be open to inspection at any time by the Divisional Forest Officer or by any forest subordinate duly authorized in that behalf. Rule 29(1) provides that a forest contract may be terminated by the Officer empowered to execute it on behalf of the Government, if the Forest

contractor makes default in the payment of the consideration for his contract or of any instalment thereof, or commits a breach of any of the other conditions of his contract. By sub-r. (2) of r. 29 it is provided that such termination shall be notified to the forest contractor by a written notice and thereupon all the contractor's rights under the contract including all accessory licences shall cease and all the forest produce remaining within the contract area or at the depots specified under r. 13 shall become the absolute property of Government. Rule 33(1) provides that all forest produce removed from a contract area in accordance with the rules and duly checked and passed at the depots established under r. 13 shall be at the absolute disposal of the forest contractor. By cl. (2) of r. 33 it is provided that the forest contractor may assign any forest produce not so removed, but such assignment shall not be valid unless it is made with the previous sanction in writing of the forest officer who executed the contract.

It is also necessary to refer to ss. 82 & 83 of the Indian Forest Act 16 of 1927. By s. 82 it is provided that all money payable to the Government under the Act or under any rule made under the Act, or on account of the price of any forest produce, or of expenses incurred in the execution of the Act in respect of such produce, may, if not paid when due, be recovered as if it were an arrear of land-revenue. Section 83 provides:

"(1) When any such money is payable for or in respect of any forest-produce, the amount thereof shall be deemed to be a first charge on such produce, and such produce may be taken possession of by a Forest-officer until such amount has been paid.

(2) If such amount is not paid when due, the Forest Officer may sell such produce by public auction, and the proceeds of the sale shall be applied first in discharging such amount.

(3)

Beside the contractual right which is conferred upon the State by r. 8 to stop removal of goods in value exceeding the amount already paid by the contractor, where the consideration is payable in instalments the statute has imposed a charge upon the goods sold, *inter alia*, for the price thereof, and has authorised the Forest Officer to take possession of the goods until such amount is paid. If the amount is not paid when due, the Forest Officer may sell the produce by public auction. The State Government has therefore under the terms of the contract and by virtue of the statute, even though the property in the goods has passed to the contractor, the right to stop removal of the goods and take possession thereof till the amount due is paid and to sell the goods if the amount is not

- A** paid when due; the State has also the power to prohibit removal of the goods when the value of the forest produce removed by the contractor exceeds the amount of instalments already paid, to check and examine the goods, and to terminate the contract in case of default in payment of the amount due and to take possession of the goods either in the contract area or in the depots of the contractor.
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The contract between Jagatram and the State was in respect of "felled trees" and the area and denomination of the coupe were set out. The trees agreed to be sold being in a deliverable state, by virtue of s. 20 of the Sale of Goods Act, the property in the goods sold passed on the production of the "coupe boundary certificate".

C It is true that because of the diverse covenants contained in the contract and the provisions of the Rules which formed part of the contract, certain restrictions were imposed upon the contractor. Rule 8 authorised the forest authorities to stop removal of the goods sold if it was found that the contractor had removed goods of value exceeding the amount of instalments already paid. Again the contractor was required to take the goods to the depots and to get the same checked and examined. But on that ground it cannot be said that the contractor did not become the owner of the goods when the "coupe boundary certificate" was produced. The "coupe boundary certificate" is not on the record, and we are unable to hold that any goods were removed or permitted to be removed without the production of the coupe boundary certificate. That is not the case of the State and we will not be justified in so assuming. The terms of rr. 29 & 33 also abundantly support the view that on the production of the "coupe boundary certificate" the contractor becomes the owner of the goods. Under cl. (2) of r. 29 when a contract is terminated for reasons mentioned in cl. (1) all forest produce remaining within the contract area or at the depots specified under r. 13 becomes the absolute property of the Government. It is implicit in the rule that till the eventuality contemplated by r. 29(1), property in the forest produce is in the contractor. The terms of r. 33(2) which authorize the forest contractor *to assign any forest produce* also support that inference. The right to assign the forest produce not removed from the contract area predicates title to the forest produce. The argument of the State that the property in the goods had not passed to the forest contractor till they were removed, and on that account the statutory charge under s. 83 of the Forest Act did not attach to the goods sold, has therefore no force. As soon as the contract was entered into and the coupe boundary certificate was produced and we assume in this case that it was so produced, the property in the goods passed to Jagatram. But for the contract price there was a first charge on such produce in favour of the State of Madhya Pradesh under s. 83(1). The Divisional Forest Officer had authority to stop removal of those goods until

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the amount of instalments payable by the contractor was paid and even to sell the goods for recovery of the amount which had fallen due. The forest authorities however allowed Jagatram to remove the goods sold before the instalments due on December 1, 1954 and thereafter were paid.

Kaluram by executing the surety bond had undertaken to discharge the liability arising out of any act, omission, negligence or default of the forest contractor. The surety Kaluram contends that because the State lost or parted with the security he stood discharged. By s. 140 of the Indian Contract Act, 1872, where a guaranteed debt has become due, or default of the principal debtor to perform a guaranteed duty has taken place, the surety, upon payment or performance of all that he is liable for, is invested with all the rights which the creditor had against the principal debtor; and by s. 141 it is provided:

“A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses, or, without consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.”

The State had as already observed, a first charge over the goods: the State was also entitled to prevent the goods from being removed without payment of the amount of instalments due. The expression “security” in s. 141 is not used in any technical sense: it includes all rights which the creditor had against the property at the date of the contract. The surety is entitled on payment of the debt or performance of all that he is liable for, to the benefit of the rights of the creditor against the principal debtor which arise out of the transaction which gives rise to the right or liability: he is therefore on payment of the amount due by the principal debtor entitled to be put in the same position in which the creditor stood in relation to the principal debtor. If the creditor has lost or has parted with the security without the consent of the surety, the latter is, by the express provision contained in s. 141, discharged to the extent of the value of the security lost or parted with.

The State had a charge over the goods sold as well as the right to remain in possession till payment of the instalments. When the goods were removed by Jagatram that security was lost and to the extent of the value of the security lost the surety stood discharged. In the present case the State has not produced the accounts furnished under r. 16 by the contractor relating to the quantity of goods removed by Jagatram. We must in the circumstances hold that the entire quantity contracted to be sold to Jagatram had been removed, and the surety is, because the State has parted with the security

A which it held, discharged from liability to pay the amount payable under the terms of the contract.

In *Wulff and Billing v. Jay*,⁽¹⁾ Hannen, J., stated the law thus:

B “.....I take it to be established that the defendant became surety upon the faith of there being some real and substantial security pledged, as well as his own credit, to the plaintiff; and he was entitled, therefore, to the benefit of that real and substantial security in the event of his being called on to fulfil his duty as a surety, and to pay the debt for which he had so become surety. He will, however, be discharged from his liability as surety if the creditors have put it out of their power to hand over to the surety the means of recouping himself by the security given by the principal. That doctrine is very clearly expressed in the notes in *Rees v. Barrington*—2 White & Tudor’s L.C., 4th Edn. at p. 1002—‘As a surety, on payment of the debt, is entitled to all the securities of the creditor, whether he is aware of their existence or not, even though they were given after the contract of suretyship, if the creditor who has had, or ought to have had, them in his full possession or power, loses them or permits them to get into the possession of the debtor, or does not make them effectual by giving proper notice, the surety to the extent of such security will be discharged. A surety, moreover, will be released if the creditor, by reason of what he has done, cannot, on payment by the surety, give him the securities in exactly the same condition as they formerly stood in his hands.’ ”

F Subject to certain variations, which are not material for the matter under discussion, s. 141 of the Contract Act incorporates the rule of English law relating to the discharge from liability of a surety when the creditor parts with or loses the security held by him.

G The Forest Officers of the State of Madhya Pradesh parted with the goods before receiving payment of the amount due by the contractor Jagatram. Thereby the charge in favour of the State was seriously impaired and the statutory power to sell the goods for non-payment of the amount remaining due became, for all practical purposes, ineffective. Again under the terms of the contract the Forest authorities had the right to prevent removal of goods sold until the price was paid: that right was also lost. The right conferred by s. 83 of the Forest Act and under the terms of the contract to prevent removal and right to sell goods for non-payment of the price, coupled with the charge on the goods constituted the security of the State, and that security was lost because the Forest Officers H permitted removal of the goods by the contractor.

(1) L.R. (1872) 7 Q.B. 756.

It was urged however on behalf of the State that mere inaction on the part of the forest authorities does not amount to parting with the security. But the terms of the statute do not apply only to cases in which by positive action on the part of the creditor the security is parted with. Even if the security is *lost* by the creditor, the surety is discharged. In any event the facts in the present case make it abundantly clear that it was on account of the conduct of the forest authorities that the security was lost. The goods sold were under the control of the Forest Officers, when they were in the coupe and even when they were in the depot of the contractor. The goods could be removed on the production of a pass from the coupe, and even after the goods were removed, unless they were examined and checked they were not at the disposal of the contractor. It is not pleaded by the State that the trees sold were not checked and examined at the depot of the contractor. Knowing that the goods were removed without payment of the instalments, if the Forest authorities checked and examined the goods and took no action for recovery of the amount payable, and did not enforce the charge, it would be difficult to say that there was mere inaction on the part of the forest authorities.

We therefore agree with the High Court that the surety Kaluram stood discharged from liability to pay the amount undertaken by him under the terms of the surety bond because the forest authorities of the State had parted with the security which they possessed for recovery of the amount due from the contractor.

The appeal fails and is dismissed with costs.

G.C.

Appeal dismissed.