

Dispute Resolution Hotline

July 01, 2013

EXISTENCE OF MORTGAGE IS NO BAR TO ARBITRATING MONEY CLAIMS

INTRODUCTION

The recent judgment of the Bombay High Court in *Tata Capital Financial Services Limited v. Ms Deccan Chronicle Holdings Limited*¹ gains significant importance in light of the recent spur in lending disputes. The High Court of Bombay while dealing with a petition seeking interim reliefs in aid of arbitration under Section 9² of the Arbitration and Conciliation Act, 1996 ("Act") has held that even though certain debts may be secured by a mortgage, the lender may choose to bring only a claim for recovery of the amounts due and not sue for enforcement of mortgage. Accordingly, as money claims arising under contracts are arbitrable disputes, courts are empowered to grant interim reliefs under section 9 of the Act.

FACTS AND CONTENTIONS

The case involved two separate arbitration petitions filed against Deccan Chronicle Holdings Ltd. and Mr. T. Venkatram Reddy ("**Respondent(s)**"). The petitions related to certain loans which were provided to the Respondent. Such loans had been secured by the Respondent by mortgage of immovable property. Due to the financial difficulties being faced by the Respondent, the Tata Capital Financial Services and L & T Finance Ltd. ("**Petitioner(s)**") recalled the entire loan amount with interest. The Respondent failed to repay the said amount in response to the demand from the the Petitioners. Accordingly, the two separate petitions came to be filed against the Respondents under section 9 of the Act, whereby the Petitioners sought various interim reliefs including:

1. Direction to Respondents to furnish additional security;
2. Direction for appointment of a Court Receiver;
3. Direction to Respondents to attach their properties before the final judgment;
4. Direction to Respondents to disclose on oath all the properties owned by them.

One of the principal arguments raised by the Respondents was whether the current dispute was arbitrable or not, as interim reliefs under section 9 of the Act are granted in aid of arbitration. The submission made by the Respondent was that enforcement of mortgage of immovable property could not happen by way of an arbitration. The Respondents placed reliance on the landmark judgment of the Supreme Court in *Booz Allen and Hamilton Inc. vs. SBI Home Finance Limited and Ors.*³ to substantiate their contention that the reliefs claimed in the petition filed under Section 9 of the Act are for protection of mortgaged properties, thus, rights claimed by the Petitioner are rights in rem which can only be decided by a Civil Court and not by an arbitral forum. The Respondent submitted that the notice of demand invoking arbitration clause issued by the Petitioner was for enforcement of mortgage alongwith other claims.

Further, it was argued that by the Respondent that the grant of interim measures under Section 9 of the Act would be governed by the underlying principles for grant of interim relief under Order 38 Rule 5 of the Civil Procedure Code, 1908 ("**CPC**") and that the present cases did not merit any order for interim reliefs as sought by the Petitioner.

The Petitioner's on the other hand submitted that the statement of claim was not yet filed before the arbitral tribunal and the Court in such circumstances cannot refuse to grant interim relief based on the presumption of the Respondents that the Petitioner would apply for the enforcement of mortgage against the Respondents before the arbitral tribunal. It is always open to the Petitioner to choose a claim either for enforcement of mortgage or for recovery of money simpliciter based on other securities furnished by the Respondents.

HELD

The Court appreciating the Petitioners arguments that the statement of claim had not been filed proceeded to assert that it was not up to them to presume that the Petitioner might apply for enforcement of mortgage which would be beyond the jurisdiction of arbitral tribunal. The notice of demand for enforcement of mortgage cannot be treated as a statement of claim.

Based on Order 34 Rule 14⁴ of the CPC, it was observed that there is no bar in filing a mere money claim arising under mortgage by a mortgagee. The mortgaged property could not be sold without instituting a suit for sale of mortgaged properties, however it was up to the mortgagee i.e. the Petitioners to decide in whether to file a money claim before the arbitral tribunal and file a separate suit for enforcement of mortgage after complying with the provisions of Order II Rule 2⁵. It was further held that the interim measures cannot be denied on the ground that the entire demand notice and petition filed under Section 9 of the Act was on the premise that the same was for enforcement of mortgaged properties. The Respondents had executed other securities in the nature of a guarantee

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and a promissory note and the claim could be made for enforcement of such securities.

Thus, it is for the Petitioner to decide what claims the petitioner would make before the arbitral tribunal and even if a relief by way of enforcement of mortgage was claimed, the same could be subsequently withdrawn or amended. An arbitral tribunal, upon an objection under Section 16 (objection to jurisdiction) of the Act, can always decide whether any of the claims made by the claimants are within its jurisdiction to adjudicate upon. Accordingly, the court in the present case proceeded to hold that the facts satisfy the principles for grant of the reliefs and passed orders in favour of the Petitioner.

ANALYSIS

The judgment provides valuable guidance in context of lender disputes, where lenders normally obtain multiple securities such as guarantee, pledge of shares and including a mortgage of property.

The judgment is also critical from the perspective of the real estate sector as lending activities in the real estate sector would almost always be backed by a mortgage of the property. Further, the real estate sector has grown at a tremendous pace in the past few years, and especially since it was opened to foreign investment in 2005. However, with the dampening of the world economy and the regulatory ambiguity surrounding normal modes of exit, foreign investors have adopted a more cautious approach, which has slowly led to a predilection towards mezzanine and pure debt financing structures as opposed to pure equity investments. The regulatory measures recently taken such as opening up and liberalization of the QFI route and increase in the corporate debt limits available for foreign investment has revealed the regulatory acceptance and interest in attracting foreign investment via the debt route. Buoyed by the regulatory support the sector has continued to attract foreign investments which normally are in form of collateralized debt and one of the most important collateral is the mortgage of the immovable property.

Accordingly, an important takeaway from the present judgment comes in relation to the various debt transactions. The present judgment indicates that in such scenarios lenders may first invoke arbitration to obtain an adjudication on the pending debts and the amounts owed. Thus providing an expeditious option as compared to a through and through court mechanism. Further, the ruling highlights the importance of a section 9 relief in securing the claims as in all scenarios the mortgage security may not be a sufficient security.

- Ashish Kabra, Prateek Bagaria and Vyapak Desai

You can direct your queries or comments to the authors

¹ Arb P No. 1321/2012, Judgment delivered on February 21, 2013

² Section 9 - Interim measures etc. by Court: A party may, before, or during arbitral proceedings or at any time after the making of the arbitral award but before it is enforced in accordance with section 36, apply to a court-

(i) for the appointment of a guardian for a minor or person of unsound mind for the purposes of arbitral proceedings; or

(ii) for an interim measure of protection in respect of any of the following matters, namely:-

(a) the preservation, interim custody or sale of any goods which are the subject-matter of the arbitration agreement;

(b) securing the amount in dispute in the arbitration;

(c) the detention, preservation or inspection of any property or thing which is the subject-matter of the dispute in arbitration, or as to which any question may arise therein and authorising for any of the aforesaid purposes any person to enter upon any land or building in the possession of any part) or authorising any samples to be taken or any observation to be made, or experiment to be tried, which may be necessary or expedient for the purpose of obtaining full information or evidence;

(d) interim injunction or the appointment of a receiver;

(e) such other interim measure of protection as may appear to the Court to be just and convenient, and the Court shall have the same power for making orders as it has for the purpose of, and in relation to, any proceedings before it.

³ (2011) 5 SCC 532

⁴ 14. Suit for sale necessary for bringing mortgaged property to sale.- (1) Where a mortgagee has obtained a decree for the payment of money in satisfaction of a claim arising under the mortgage, he shall not be entitled to bring the mortgaged property to sale otherwise than by instituting a suit for sale in enforcement of the mortgage, and he may institute such suit notwithstanding anything contained in Order II, rule 2.

(2) Nothing in sub-rule (1) shall apply to any territories to which the Transfer of Property Act, 1882 (4 of 1882), has not been extended.

⁵ 2. Suit to include the whole claim.- (1) Every suit shall include the whole of the claim which the plaintiff is entitled to make in respect of the cause of action; but a plaintiff may relinquish any portion of his claim in order to bring the suit within the jurisdiction of any Court.

(2) Relinquishment of part of claim-Where a plaintiff omits to sue in respect of, or intentionally relinquishes, any portion of his claim, he shall not afterwards sue in respect of the portion so omitted or relinquished.

(3) Omission to sue for one of several reliefs-A person entitled to more than one relief in respect of the same cause of action may sue for all or any of such reliefs, but if he omits except with the leave of the court, to sue for all such reliefs, he shall not afterwards sue for any relief so omitted.

Explanation: For the purposes of this rule an obligation and a collateral security for its performance and successive claims arising under the same obligation shall be deemed respectively to constitute but one cause of action.

Illustration.- A lets a house to B at a yearly rent of Rs. 1,200. The rent for the whole of the years 1905, 1906 and 1907 is due and unpaid. A sues B in 1908 only for the rent due for 1906. A shall not afterwards sue B for the rent due for 1905 or 1907.

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