



Banking business and Assumption of Contractual Obligations – An analysis

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While transacting banks knowingly and unknowingly enter into various contracts some are written and formal some other are informal and unwritten. Some common contractual relationships assumed by the banks are **Debtors – Creditor, Creditor – Debtor, Bailor – Bailee, Guarantor – beneficiary, Pledgor – Pledgee and Principal and Agent**. These relationships need to be understood with specific reference to their consequence on us. Some of these relationships are common in the eye of law and provisions which are applicable to general contract are applicable to these contractual relations while some other are of a special nature and in the eye of law these relationships have been casted certain rights and obligations. A detailed discussion on special nature relationships is as follows :-

Guarantor – Beneficiary :- This is the most expressed contractual relationship of special nature where contractual relationship is entered by way of express written contract. Bank enters this relationship at both ends i.e. sometimes bank act as surety and sometimes as credit. Knowledge of rights and obligations are result of this contractual arrangement. For a valid guarantee all the parties must be capable of entering into contract. In case principal debtor is affected by the incapacity then surety will be regarded as principal debtor. Hence no guarantee should be issued for person having incapacity i.e. minor, un sound mind, insolvent etc. A contract of guarantee is not a contract of *uberrimae* – i.e. one requiring full disclosure of all material facts to the surety. When a person guaranteed the bank account and Principal Debtors drew account defrauding Surety and Bank. Even if transaction was suspicious to bank it did not discharge surety [National Provincial Bank of England Vs Glanusk (1913) 3 K.B. 335]. Person who provide guarantee (Surety) has various rights against person on whose behalf guarantee is given (Principal Debtor) and towards person to whom guarantee is given (Creditor) – Surety can set off the liability from the counter claim of the principal debtor towards creditor [Bechevaise v Lewis (1872) L.R. 7 C.P. 372]. This can be further understood from example – when a Principal Debtor sent some stock in fulfillment of his part obligation to the creditor, On payment in full surety will receive the value of that goods from the creditor and not the principal debtor. *Right of Subrogation* - Where a guaranteed debt has become due and surety has paid all equities that he is liable for, he is

invested with all the rights which the creditor had against the principal debtor (Section 140). Where a guaranteed debt has become due and surety has paid all equities that he is liable for he shall have right to be indemnified towards principal debtor. Contract of guarantee is a contract between Principal Debtor, Surety and Creditor and consensus of all these three is needed for it (section 133 & 135). If principal debtor is released from the liability surety is also relieved for his responsibility (Section 134). Surety is also relieved if creditor loses the security which was given to him at the inception of the guarantee (Section 141)

Bailor –Bailee :-

When The customer, who deposits the things in the box for safe custody (Lockers) with the bank which contractual relationship arises ?

In the Indian context, it is a general legal standing that unless and until there exists a formal agreement, granting an exclusive and actual possession of the contents of the safe deposit case, no transfer of possession will be assumed to have taken place. Hence, there is a presumption against the existence of a relationship of bailment between a customer of the safe deposit boxes and the service provider and the responsibility to prove the existence of a duty to safeguard the contents of the safe deposit box by the virtue of a contract of bailment, falls upon the customer. In case of hiring a safe deposit box, the goods are in no manner, entrusted to the bank. The delivery of the goods is done to the premises of the bank (by utilizing the vault or the box within the premise) and not to the bank itself. This legal relationship is analogous to the relationship between a landlord and a tenant. A landlord cannot be said to have a control over the personal property of the tenant, but merely provides the tenant with a place to store their property. Therefore, even though the landlord might be obligated to exercise ordinary care to protect the premises of the rented property, the landlord cannot be expected to extend this care to protecting the personal property of the tenant. Similarly, banks are required to exercise ordinary care to protect their premises, but they cannot be expected to protect the contents of every safe deposit box, unless the bank has been given actual and exclusive possession, leading to an existence of an agreement of bailment between the two. In this respect leading case is *Atul Mehra Vs Bank of Maharashtra* In this case Atul Mehra had hired locker on 15th January 1986 at bank of Maharashtra. He deposited jewellery in the box. The strong room in which the locker was located was broken in and the contents thereof were stolen by miscreants. On 9th January 1989 an FIR for the same was filed. It was alleged strong room was made only of plywood where it ought to have been made of iron and concrete. The court in this case, reaffirmed the reliance of the previous courts on *Mohinder Singh Nanda v Bank of Maharashtra*, and laid down the proposition that a relationship of bailment cannot arise without the bailee knowing and controlling the goods exclusively. There existed no contract between the appellant and the respondent, informing and giving control to the bank, over the contents of the safe deposit box. Since the bank was totally unaware of the quality, quantity and the value of the jewellery kept in the safe deposit box, the bank cannot be said to have been given "entrustment" or "control" of the contents of the box, and therefore there was no transfer of possession. Hence, a case of bailment wouldn't arise by a mere hiring of a safe deposit box, unless and until the bank has exclusive knowledge and possession of the contents of the box. Reserve Bank of India (RBI) have said that banks would not be liable to compensate you if the contents of your lockers are stolen or damaged due to a natural calamity. However Supreme Court have reiterated that banks cannot wash off their hands towards their customer for the operation of lockers, Apex court have directed RBI to lay down regulations for locker facility management.

In the American context, however, the legal status on this issue favours the customers and there is a presupposition in the favour of the existence of a contract of bailment between the customer and the bank.

Hence we can conclude that in Indian Context provision of lockers for safe custody is an agreement for service and not a contract of bailment.

Contract of Pledge :- An example of pledge is Gold loan where gold is pledged as security.

The bailment of goods as security for payment of a debt or performance of a promise is called pledge. The person delivering the goods is called 'Pledger' or 'Pawner' and the person to whom they are delivered are called 'Pledgee' or 'Pawnee'. (Sec 172) The fundamental difference between pledge and bailment is –Pledge is a bailment of goods as a security and in bailment goods are delivered for some purpose e.g. delivery of cloth to the tailor for stitching. Rights of Pawnee – He may retain the pledged goods until dues (Principal + Interest + Expenses) are paid by pawner. When the pawnor has obtained possession of the goods pledged by him under a voidable contract (i.e. by fraud, undue influence and coercion etc.) but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title of the goods provided he acts in good faith (Sec 178A). If pawner makes a default pawnee can (Sec 176):- (a). May file a suit against the pawner upon the debt and may retain the goods as collateral security , (b). He may sell the goods pledged after giving the pawner a reasonable notice of the sale. (c). He can recover the deficiency arising on sale .

Law Relating to Lien :-

'Lien' means the right of a person to retain possession of some goods belonging to another until some debt or claim of the person in possession is satisfied. It appertains to the person who has possession of the goods which belong to another, entitling him to retain them until the debt due to him has been paid. In order to create a lien the possession must be (a). Rightful, (b), not for a particular purpose and (c). continuous.

Particular Lien is available to the person whom goods are delivered for only against those goods on which some skill or labour have been expended by him. In that case he can retain those goods until all claims in respect of those goods are satisfied. General Lien is a right to retain the property of another for a general balance of the account.

Extinguishment of Lien :- A lien is extinguished or lost by (a) abandonment, (b) Payment or tender of the amount due or (c). Loss or surrender of possession of goods.