

M/s. Karnataka Ball Bearing Corporation Ltd. Vs M/s. Dolphin Fisheries and Trading Pvt. Ltd. and others

Court: Karnataka High Court

Date of Decision: March 10, 1995

Acts Referred: Companies Act, 1956 " Section 446 (2), 446 (2) (b)

Constitution of India, 1950 " Article 141

Sick Industrial Companies (Special Provisions) Act, 1985 " Section 15, 15 (1), 19

Citation: AIR 1995 Kar 330 : (1995) 83 CompCas 544 : (1995) ILR (Kar) 784 : (1995) 3 KarLJ 577

Hon'ble Judges: S.A. Hakeem, Acting C.J.; H.N. Narayan, J

Bench: Division Bench

Advocate: Sri. Udaya Holla, for the Appellant; C.K. Narayana Rao, Sri. S.M. Chandrasekhar, Sri. G.S. Bhat and Sri. S. Krishnaiah, for the Respondent

Judgement

@JUDGMENTTAG-ORDER

Mr. S. A. Hakeem Ag., C.J.

This appeal is directed against the winding up order dated 7-1-1994 passed by the learned Company Judge

in Company Petition No. 10 of 1988.

2. In order to appreciate the question of law arising in this case, it is appropriate to briefly refer to undisputed facts and the chronological events

leading to passing of the impugned order.

3. The appellant is a public limited Company incorporated under the provisions of the Companies Act 1956, having its Registered Office as well as

Factory at Mysore. The 1st respondent herein claiming to be a creditor, filed a petition for winding up of the Company on the ground under

Sections 433(e) and 434(1)(a) and (c) of the Companies Act seeking winding up of the Company for non-payment of certain amounts due to it.

The said petition was admitted on 12-2- 1988. While the said petition was pending, the Company having become a sick industrial unit made a

reference before the Board for Industrial and Financial Reconstruction (hereinafter referred to as "BIFR") u/s 15(1) of the Sick Industrial

Companies- (Special Provision) Act, 1985 (hereinafter referred to as "the Act"). The Company Petition was being adjourned from time to time

until 16-6-1989 when it was adjourned sine die in view of the pendency of the reference before the BIFR. It transpires that the BIFR prepared a

scheme for implementation. During the pendency of the said proceedings, a proposal was made for one time settlement on payment of certain sums

of money. This proposal failed as the Company was not in a position to raise the necessary funds. Thereupon, the BIFR issued a show cause

notice as to why the Company should not be directed to be wound up. This notice was challenged before the Appellate Authority for Industrial

and Financial Reconstruction (hereinafter referred to as "AAIFR"). By its order dated 20-7-1993, the AAIFR dismissed the appeal, inter alia,

with the following observations:--

No useful purpose would be served by entertaining the appeal at this stage particularly, when ample opportunities are available, to the appellant to

submit proposals before the BIFR, as indicated in the impugned order. Such opportunities being available, it is not required of this authority to

proceed with this matter further at this stage.

As far as the representatives of the workers" are concerned, it was pointed out to them that they are at liberty to urge all their contentions and

proposals before the BIFR when this matter is next taken up by it.

4. Strangely, a copy of the aforesaid order was forwarded by the AAIFR to this Court although the same was not an order or a final opinion of the

AAIFR u/s 20 of the Act for winding up of the Company. The petition was thereupon taken up for hearing and the impugned winding up order

was passed. In the course of the order, referring to the proceedings before the BIFR and the dismissal of the appeal by the AAIFR, the learned

Company Judge has observed that ""since the conditions made were not adhered to, the proceedings before it were dismissed. This obviously

shows that the respondent-Company is not financially in sound condition and is commercially bankrupt"". The instant appeal was preferred against

the said order and an order of stay of the winding up proceedings was granted by the Division Bench on 10-2-1994.

5. It is only subsequent to the impugned order that a final order was passed by the BIFR on 1-3-1994 rendering its opinion u/s 20 of the Act that it

is just and equitable that the Company should be wound up. The said opinion was forwarded to this Court. The order of the BIFR is challenged in

appeal (Appeal No. 71 of 1994) before the AAIFR which was admitted on 30-9-1994. The said appeal is pending consideration.

6. The main contention of Sri Udaya Holla, learned Counsel for the appellant, is that having regard to the mandatory provisions of Section 22 of

the Act, no proceedings for the winding up of the Company shall lie or" be proceeded further during the pendency of the reference made u/s 15 of

the Act until it is finally disposed of u/s 20, or when an appeal u/s 25 is pending. That admittedly the impugned winding up order came to be

passed even before the BIFR rendered its final opinion u/s 20(1) of the Act and which order being challenged in the statutory appeal u/s 25 of the

Act is pending before the AAIFR. In the circumstances, the learned Company Judge could not at all have proceeded further with the winding up

proceedings much less passing the impugned order directing winding up of the Company. Sri Sirsi, learned Counsel appearing for intervening

applicant and Sri S.K.V. Chalapathy, learned Counsel appearing for one of the creditors, have urged that in the facts and circumstances of the

case the statutory bar u/s 22 of the Act against a proceeding or passing an order of winding up by the Court, was not attracted.

7. The scope and ambit of Section 22 of the Act having come up for consideration before the Supreme Court in The Gram Panchayat and another

Vs. Shree Vallabh Glass Works Ltd. and others, the Supreme Court has held thus:-

Section 22(1) provides that in case the enquiry u/s 16 is pending or any scheme referred to under S. 17 is under preparation or consideration by

the Board or any appeal under S. 25 is pending then certain proceedings against the sick industrial company are to be suspended or presumed to

be suspended. The nature of the proceedings which are automatically suspended are: (1) winding up of the industrial company; (2) Proceedings for

execution, distress or the like against the properties of sick industrial company and (3) Proceedings for the appointment of Receiver. The

proceedings in respect of these matters could, however, be continued against the sick industrial company with the consent or approval of the

Board or of the Appellate Authority as the case may be.

8. It is further clarified that it is open for the creditors to approach the BIFR for permission to proceed against the Company for recovery of their

dues by whatever name it is called. The Board at its discretion may accord its approval for proceeding against the Company. If such approval is

not granted, the remedy is not extinguished. It is only postponed. The period of such postponement has to be excluded for the purpose of

limitation. As rightly urged by Sri Udaya Holla, the secured creditors/interveners who opted out of the winding up proceedings and who did not file

any affidavits either supporting or opposing the winding up proceedings, have no locus standi to intervene and oppose this appeal by the Company.

It appears to be well settled that a secured creditor of a company in winding up opting to stand outside the winding up has to obtain a decree

against the company after making the Official Liquidator a party to the suit and enforce the decree against the Official Liquidator. Enforcement of

the security cannot be effected by preferring a claim under Section 446(2)(b) of the Companies Act, unless the secured creditor also stands within

winding up proceedings.

9. In "Maharashtra Tubes v. S.I.I.C. of Maharashtra" 1993 (78) Com Cas 803 Bom : AIR 1993 SCW 991, the Supreme Court has considered

the overriding effect of the provisions of Section 22 vis-a-vis Section 29 of the State Financial Corporations Act, 1951. The question that arose for

consideration was whether in a case where an industrial concern makes any default in repayment of any loan or advance or any instalment

therefore or otherwise fails to reedits obligations under the terms of any agreement with a Financial Corporation, the latter can take recourse to

Sections 29 and/or 31 of the State Financial Corporations Act, 1951, notwithstanding the bar of Section 22 of the Act.

10. Referring to the relevant provisions of the Act of 1951 and the Act of 1985, it is held that if the Corporation is permitted to resort to the

provision of Section 29 of the 1951 Act, while proceedings under Sections 15 to 19 of the 1985 Act are pending, it will render the entire process

nugatory. Therefore, where an inquiry is pending u/s 16/17 of the Act or an appeal is pending u/s 25 of the Act, there should be cessation of the

coercive activities of the type mentioned in Section 22(1) of the Act to permit the BIFR to consider what remedial measures it should take with

respect to the sick industrial company. In this context, it is slated thus:--

On the other hand the 1985 Act was enacted, as its preamble manifests, with a view to timely detection of sick or potentially sick companies

owning industrial undertakings, the identification of the nature of sickness through experts in the relevant fields with a view to devising suitable

remedial measures through appropriate schemes and their expeditious implementation. Here the emphasis is to prevent sickness and in cases of

sick undertakings to prepare schemes for their rehabilitation by providing financial assistance by way of loans, advances or guarantees or by

providing reliefs, concessions or sacrifices from Central or State Governments, scheduled banks, etc. The basic idea is to revive the sick units, if

necessary, by extending further financial assistance after a thorough examination of the units by experts and it is only when the unit is found to be

no more capable of rehabilitation, that the option of winding up may be resorted to. It is for that reason that Section 22(1) provides that during the

pendency of (i) an inquiry u/s 16, or (ii) preparation or consideration of a scheme u/s 17, or (iii) an appeal u/s 25, no proceedings for winding up of

the concerned industrial company or for execution distress or the like shall lie or be proceeded with in relation to the properties of that concern

unless the BIFR/appellate authority has consented thereto. The underlying idea is that every such action should be frozen unless expressly

permitted by the specified authority until the investigation for the revival of the industrial undertaking is finally determine. It is thus crystal clear that

the main thrust of this special legislation is on revival or rehabilitation of the sick industrial undertaking and it is only when it is realised that the same

is not feasible that the option of winding up of the unit can be resorted to.

It is further held (at page 818) thus:--

..... Section 22(1), shorn of the irrelevant part, provides that where an appeal u/s 25 relating to an industrial company is pending, then,

notwithstanding anything contained in any other law, no proceedings for the winding up of the industrial company or for execution, distress or the

like against any of the properties of the industrial company or for appointment of a receiver in respect thereof shall he or be proceeded with further,

except with the consent of the BIFR, or as the case may be, the appellate authority. The purpose and object of this provision is clearly to await the

outcome of the reference made to the BIFR for the revival and rehabilitation of the sick Industrial company. The words ""or the like"" which follow

the words ""execution"" and ""distress"" are clearly intended to convey that the properties of the sick industrial company shall not be made the subject-

matter of coercive action of similar quality and characteristic till the BIFR finally disposes of the reference made u/s 15 of the said enactment. The

Legislature has advisedly used an omnibus expression ""the like"" as it could not have conceived of all possible coercive measures that may be taken

against a sick undertaking

(Underlining ours)

xxxx xxxx xxxx xxxx xxxx

..... If the corporation is permitted to resort to the provision of Section 29 of the 1951 Act, while proceedings under Sections 15 to 19 of the

1955 Act are pending it will render the entire process nugatory. In such a situation the law merely expects the corporation and for that matter any

other creditor to obtain the consent of the BIFR or, as the case may be, the appellate authority to proceed against the industrial concern. The law

has not left them without a remedy. We are, therefore, of the opinion that the word "proceedings" in Section 22(1) cannot be given a narrow or

restricted meaning to limit the same to legal proceedings. Such a narrow meaning would run counter to the scheme of the law and frustrate the very

object and purpose of Section 22(1) of the 1985 Act,

11. In view of the Scheme and Object of the Act which has been discussed at length by the Apex Court in the above case, it is urged by Sri

Udaya Holla that while construing a welfare legislation like the Act, a liberal construction should be placed to their provisions so that the purpose of

the legislation may be allowed to be achieved rather than frustrated or stultified. This view also finds support in M/s. International Ore and

Fertilizers (India) Pvt. Ltd. Vs. Employees' State Insurance Corporation,

12. In the above case 1988 78 Comp Cas 803 SC) the Supreme Court has cited with approval the decision of the Gujarat High Court in Testeels

Ltd. Vs. Radhaben Ranchhodlal Charitable Trust, on the question whether a winding up proceeding already commenced against an industrial

company ought to be dismissed or stayed during the pendency of the reference u/s 15 of the 1985 Act the High Court had held that the words ""be

proceeded with further"" in Section 22 cannot be interpreted to mean that the proceedings should be kept in abeyance but the various provisions of

the enactment must be construed to put an end to both the contemplated and pending winding up proceedings. It had further held that if the

winding up proceedings are kept pending it may be difficult to effectively administer the schemes u/s 18 or grant financial assistance u/s 19 of the

1985 Act. It is stated that the various provisions of the Act which have been enacted to safeguard the economy of the Nation and to protect the

viable sick companies, definitely puts an end both to the contemplated winding up proceedings and the pending winding up proceedings. It is

further stated in the said decision that the legislation in order to revive and rehabilitate the sick industry has come forward with specific provisions.

The financial assistance envisaged u/s 19 cannot be forthcoming if the winding up proceeding is not disposed of. Various other schemes envisaged

u/s 18 cannot be effectively administered by having the winding up proceedings alive without the same being dismissed. Ultimately, it is stated that

the continuance of a pending proceeding for winding up, if allowed by the Court in exercise of its discretion, would clearly conflict with the the

paramount object for which Section 16(4) of the Act is enacted. Hence, the provisions of Section 22 have to be broadly construed keeping in

mind the scheme of the law so that the ultimate objective is achieved and not defeated. Similar view was taken by the Allahabad High Court in

Industrial Finance Corporation of India and Another Vs. Maharashtra Steel Ltd. and Others,

13. In Maharashtra Tubes" case (supra), the Supreme Court has observed that these two cases reinforce the view that the provision of Section

22(1) of the Act should receive a broad construction that the expression ""proceedings"" in Section 22(1) need not be limited to ""legal proceedings

as understood in the narrow sense notwithstanding the use of that, expression in the marginal note. It is further pertinent to note the observations of

the Supreme Court while rejecting the view that where the creditors of a sick industrial concern happen to be banks or State Financial

Corporations different considerations would come into play. It was observed thus:--

It must be realised that in the modern industrial environment large industries are generally financed by banks and statutory corporations created

specially for that purpose and if they are permitted to resort to independent action in total disregard of the pending inquiry under Sections 15 to 19

of the Act, the entire exercise under the said provisions would be rendered nugatory by the time the BIFR is able to evolve a scheme of revival or

rehabilitation of the sick industrial concern by the simple device of the Financial Corporation resorting to Section 29 of the 1951 Act. We are,

therefore, of the opinion that where an inquiry is pending u/s 16/17 or an appeal is pending u/s 25 of the 1985 Act, there should be cessation of the

coercive activities of the type mentioned in Section 22(1) to permit the BIFR to consider what remedial measure it should take with respect to the

sick industrial company. The expression ""proceedings"" in Section 2(1), therefore, cannot be confined to legal proceedings understood in the

narrow sense of proceedings in a court of law or a legal Tribunal for attachment and sale of the debtor's property.

14. Sri Chalapathy, learned Counsel for one of the intervening applicants, sought to reply upon the ruling in Sudarsan Chits (I) Ltd. Vs. O.

Sukumaran Pillai and Others, in upport of his proposition that once the Liquidator is appointed, notwithstanding the stay granted in appeal, the

winding up order remains effective. In that case, the order of winding up and appointment of Liquidator was challenged before the Appellate

Bench of the Kerala High Court. When the matters came up for hearing, the appeals were disposed of after approving the scheme of compromise

and arrangement u/s 391 of the Companies Act directing that the winding up order shall be held in abeyance on certain undertakings to be filed by

the Company before the Court. On failure to abide by the conditions in the judgment, the winding up order passed by the Company Judge would

stand confirmed. In the circumstances of the case, it was held that if the winding up order was subsisting, the Court which made that order or the

Court which kept it in abeyance will have jurisdiction to give necessary directions to the provisional Liquidator to take recourse to Section 446(2)

of the Companies Act. The fact situation in the instant case is distinguishable and as such the said ruling is of no assistance to the intervening

applicants.

15. As stated earlier, in the instant case, the BIFR had directed stay of further proceedings under the Act and as on the date when the impugned

winding up order was made the Board was yet to take a final decision on the material on record to decide whether it was not practicable for the

Company to make its network positive and consequently to recommend winding up thereon. The Board having approved and recommended

winding up of the Company, an appeal u/s 25 of the Act was entertained before the Appellate Authority which is still pending. Hence, in the view

taken by the Supreme Court in The Gram Panchayat and another Vs. Shree Vallabh Glass Works Ltd. and others, (supra), the winding up

proceedings against the Company stood ""suspended or presumed to be suspended"" within the purview of Section 32(1) of the Act.

16. The other two decisions cited by Sri Chalapathy are State of U.P. and Another Vs. Synthetics and Chemicals Ltd. and Another, and

Municipal Corporation of Delhi Vs. Gurnam Kaur, These are pertaining to the binding nature of the precedents under Article 141 of the

Constitution in which it is observed that per incuriam and subsilento decisions and orders made with consent of parties etc., are not of binding

nature. There cannot be any dispute regarding the principle stated therein. However, we do not see any assistance to the contentions urged in the

instant case.

17. Ballabhadas Mathurdas Lakhani and Others Vs. Municipal Committee, Malkapur, was cited in the context of the contention that the effect of

the pendency of the reference and the provisions of Section 22 of the Act was not argued or brought to the notice of the Company Judge and

hence the said question was not open for consideration. There is no merit in this contention since sufficient material regarding this aspect was

already on record.

18. Sri Sarkar for M/s. Khaithan & Co., appearing for ICICI, sought to rely upon the decisions in Bengal Lamps Limited Vs. Furmanite Nicco

Limited, In the earlier case, the court has opined that mere registration of a reference under S. 15 of the Act does not amount to an inquiry pending

u/s 16 since the Board can refuse to hold an inquiry if it finds the reference to be frivolous. The fact situation in that case was that an application u/s

15 was filed during the pendency of an appeal against the admission of a winding up petition by the Company Court. In the next case, it is held that

under sub-section (2) of Section 20 of the Act, the High Court has no option but to pass an order of winding up on the basis of the opinion of the

Board. The fact situation in the instant case is clearly distinguishable and hence the said decisions are of no assistance to the intervening creditor.

However, it is further observed that it is not the endeavour of the Court to examine the correctness or otherwise of the decision of BIFR as an

appeal u/s 25 is pending against the same. The AAIFR would dispose of that appeal as early as possible on merits.

19. In *Sponge Iron India Ltd. v. Neelima Steels Ltd.*" 1990 (68) Comp Cas 201 learned single Judge of the Andhra Pradesh High Court, has held

that the registration of a " reference in relation to a company by the BIFR is prima facie proof that the inquiry before the Board u/s 16 of the Act is

pending and the Board has to take further steps for taking one of alternative measures under Sections 17 to 20 of the Act. Once it is shown that a

reference is registered under the Act, Section 22 of the Act becomes applicable and proceedings for winding up the company cannot continue.

However, the creditors can intervene and seek relief at the stage of inquiry before determination of the question of applicability of Section 3(o) of

the Act to the Company, if they dispute it and have material to show that the industrial sickness is a device to defeat the claims. But this is a matter

which can be examined and decided only by the Board.

20. In view of the above discussion, it is difficult to sustain the order of winding up as the same has undoubtedly been made during the pendency of

the reference which becomes final only by the order of the Board u/s 20 or by the final order made by the AAIFR in an appeal u/s 25 of the Act

which is now pending.

21. In the result, this appeal is allowed. The order of winding up passed by the learned Company Judge dt. 7-1-1994 is set aside. The matter is

remitted to the Company Court to await final decision of the Appellate Authority for Industrial and Financial Reconstruction in the Company"s

appeal pending before it.

22. Before parting with this appeal, the only other question that remains for consideration is whether the appellant is entitled to get back possession

of Company. In this connection, it is fairly conceded by Sri Udaya Holla that unsealing of the factory may be done and possession may be

delivered to the Company subject to any reasonable conditions. In view of this concession, we make the following order:--

(1) The Official Liquidator shall unseal and deliver possession of the factory to the appellant, subject to its undertaking, to be filed within one week,

that it shall not alienate the assets and properties of the Company until final disposal of the proceedings before ""the AAIFR and the proceedings

before this Court;

(2) That the management shall take one of the nominees of the Financial Institutions involved in this case as a Director in the Board of Management

of the Company to watch and have a say in the day to day management of the Company;

(3) It is open for the AAIFR to pass any orders or directions in modification of the above conditions or otherwise as it may deem necessary for

proper functioning of the Company or the factory;

(4) A further affidavit and commitment by any of the financiers (who have already expressed their willingness to assist the Company) by committing

funds at least to the extent of Rs. 1.5 Crores within Ten days on such terms and conditions that may be agreed upon between the Board of

Management and such financiers;

(5) Any of the parties are at liberty to move the AAIFR for any further directions.

The AAIFR is directed to dispose of the appeal before it expeditiously and in any event within four months from the date of receipt of this

judgment.

In view of the above judgment, I. As-II V & IX stand disposed of.

23. Soon after pronouncement of the judgment, an oral application is made on behalf of the ICICI to stay the operation of this judgment for a

period of 4 weeks. In the circumstances, neither it is just nor expedient to stay the operation of the judgment. The request is rejected.

24. Appeal allowed.