

(1999) 04 AP CK 0002

Andhra Pradesh High Court

Case No: Company Referred Case No"s. 6 of 1997, 1, 2, 4, 5, 6, 7, 9, 12, 14, 15, 18 and 19 of 1998 and C.A. No"s. 466 and 554 of 1998 in C.P. No"s. 39 of 1993 and 69 of 1994

Board for Industrial and
Financial Reconstruction

APPELLANT

Vs

Adivasi Paper Mills Ltd. and
Others, Bell Remedies Ltd. and
Others, Annapurna Cements Ltd.
and Others, Universal Wires Ltd.
and Others, Delhi Tubes Ltd. and
Others, Sree Krishna Oil
Complex Ltd. and Others,
Mercury Resins and Polymers (P.)
Ltd. and Others, Andhra Pradesh
Lightings Ltd. and Others, Hiflon
India Ltd. and Others, Vaishu
Engineering Industries Ltd. and
Others, Suman Metallurgical and
Chemical Product Ltd. and
Others, Sri Katruggadda
Electronics Ltd. and Others and
Annavaram Spinning Mills Ltd.
and Others
 A.P. State
Financial Corporation Vs T.G.L.
Quick Foods Ltd.
 Official
Liquidator Vs State Bank of India
Ltd. and Another

RESPONDENT

Date of Decision: April 15, 1999

Acts Referred:

- Companies Act, 1956 - Section 529, 529(1), 529(2), 529A, 537
- Provincial Insolvency Act, 1920 - Section 28, 28(6)
- State Financial Corporations Act, 1951 - Section 29, 30, 32E, 32E(2), 42B

Citation: AIR 2000 AP 179 : (2000) 1 CompLJ 209

Hon'ble Judges: B.S. Raikote, J

Bench: Single Bench

Advocate: Ajay Reddy T., Badrinath P., Bala Rami P., Gopalakrishna D., Gopala Krishna Murthy K., Gurumurthi P., Kodandaram C., Krishna Murty A., Krishna Murthy V.V., Kumar E.S., Lohita Y.N., Madan Mohan Rao E., Mallikharjuna Rao K., Markandayulu P.V., Md. Ubedulla, Mohan Rao, Mohan Reddy C.V., Narahari M., Narender Reddy M., Niranjan Reddy S., Narasimha Rao A.V.D., Prabhakar Sripada, Pradeep Kumar C., Prasad P.R., Rajagopala Reddy V., Rajiv Reddy C.V., Rama Krishna P.V., Rama Krishna Rao A.H., Rama Raju P.V., Ravi S., Ravindra Babu M., Sambasiva Pratap E., Sarveswara Murthy S.P.V., Srinivasa Murthy K., Suresh P., Trivikrama Rao C., Venkateswara Rao K.V., Vijayanandan Reddy R.Y., Viswanatham V.K. and Viswanatha Reddy B. and Government Pleader for Industries, for the Appellant;

Judgement

B.S. Raikote, J.

In all these cases, the official liquidator is claiming proportionate expenses from the other creditors like financial institutions, and in some cases, such report praying for such contribution of expenses are pending and in some cases, there is already a direction to the financial institutions to pay their share of expenses and in some cases, such financial institutions have filed applications to recall the earlier order directing them to contribute towards the expenses. In view of these circumstances, the learned counsel appearing for the other secured creditors who were permitted to stand outside the winding up, are contending that they are not liable to pay or contribute towards the expenses to be incurred by the official liquidator for paper publication, etc. It is their case that the official liquidator can claim such expenses from the Central Government. But the case of the official liquidator in all these cases is that such other creditors are liable to share the expenses proportionately in view of the proviso to Sub-section (2) of Section 529 of the Companies Act, 1956. On the other hand, the counsel for other secured creditors contended that when they have opted to stand outside the liquidation, they are not liable to share any expenses. The counsel appearing for the Andhra Pradesh State Financial Corporation contended that under the State Financial Corporations Act, 1951, the financial corporation as the secured creditor has to follow its own procedure under the Financial Corporations Act, and, therefore, Section 529 or 529A of the Companies Act, would not apply and as such the financial corporation has no liability to contribute towards the expenses claimed by the official liquidator. He also submitted that the provisions of Section 28(6) of the Provincial Insolvency Act, 1920, are made applicable by virtue of Section 529A of the Companies Act and as such, the corporation as a secured creditor can independently proceed to realise its debts, on the basis of security in its possession, and the company court cannot insist for payment of the contribution of the expenses. In view of these contentions urged on both sides, the point that now requires to be decided by me is, whether the other secured creditors including the State Financial Corporation, standing outside the

winding up proceedings, are liable to contribute towards the expenses incurred by the official liquidator.

2. In order to appreciate the controversy between the parties, I have taken notice of certain provisions of the Companies Act in relation to the State Financial Corporations Act, 1951, and also Section 28(6) of the Provincial Insolvency Act, 1920.

3. By virtue of Section 456(2) of the Companies Act, all the properties and effects of the company under winding up, shall be deemed to be in the custody of the court as from the date of the order for the winding up of the company. Section 446 of the Companies Act mandates that when once the winding up order is made by appointing the official liquidator, "no suit or other legal proceedings shall be commenced, or if pending at the date of the winding up order, shall be proceeded with, against the company, except by leave of the court and subject to such terms as the court may impose". Under Clause (2) of the said section, such suit or proceedings, the company court may itself dispose of. From this position of law, it is clear that once a winding up order is passed, no suit or proceedings shall be instituted or shall go on without the leave of the court and u/s 447 of the Companies Act, it is further provided that an order for winding up a company shall operate in favour of all the creditors and all the contributories of the company as if it had been made on the joint petition of the creditors and of a contributories. u/s 448, for the purpose of this Act, so far as it relates to the winding up of the company by the court, there shall be attached to each High Court an official liquidator appointed by the Central Government, who shall also be a liquidator of the company as per Sections 449 and 450 of the Companies Act. As per Section 451, such liquidator appointed, shall conduct the proceedings in winding up of the company and perform such duties in reference thereto as the company court may impose. Such official liquidator appointed, has the power to institute or defend any suit or other legal proceedings or to carry on the business of the company under liquidation to sell the immovable and movable property and actionable claims of the company, by public auction or private contract, with power to transfer the whole thereof to any person or body corporate, or to sell the same in parcels, and to raise on the security of the assets of the company any money requisite, and he has all such other things as may be necessary for winding up the affairs of the company and even to distribute its assets in terms of Section 457 of the Companies Act. u/s 468 of the Companies Act, the court may require any contributory or any trustee, receiver, banker, agent or officers of the company to pay, deliver, surrender or transfer to the official liquidator any money, property or books and papers in their custody, under the control of the official liquidator. As per Section 537(1)(b) of the Companies Act, if there is any sale of the property of the company, without the leave of the company court, such sale would be void. From this it follows that once a winding up order is passed, no suit or proceedings of the creditors against the company shall go on without the permission of the court, nor there shall be any sale of the property belonging to such company under liquidator, without the permission of the court

and such winding up proceedings would be for the benefit of all the creditors. u/s 529A of the Companies Act, it is further provided as under :

"529A. Overriding preferential payments.-(1) Notwithstanding anything contained in any other provision of this Act or any other law for the time being in force, in the winding up of a company.--

(a) workmen's dues ; and

(b) debts due to secured creditors to the extent such debts rank under Clause

(c) of the proviso to Sub-section (1) of Section 529 pari passu with such dues, shall be paid in priority to all other dues.

4. From this section, as amended by the Companies (Amendment) Act, 1985, for the workmen's dues, the workmen is made pari passu creditor along with other secured creditors. Under the proviso to Section 529(1), of the Companies Act, it is further made clear that the security of every secured creditor shall be deemed to be subject to a pari passu charge in favour of the workmen to the extent of workmen's portion in such security. From these provisions it is clear that once the winding up order is passed, the workmen also become pari passu creditors along with other secured creditors and such workmen's charge shall be a charge on the security of every secured creditor to the extent of such workmen's portion therein. If that is so, any security at the hands of any secured creditor is answerable to the dues of the workmen. From this it logically follows that whenever a secured creditor is granted leave to stand outside the liquidation proceedings, can realise his debts from the security along with the dues of the workmen, since the workmen as pari passu has priority on such security. Therefore, such creditor cannot say that he would proceed with the realisation of his debt independently of the other creditors. In other words, the security in the hand of such creditor is also answerable to the charges of other co-creditors. In other words, such security in the hand of such creditor, who has opted to stand outside the liquidation proceedings is also security for the benefit of other secured creditors. It is only having regard to these factors, it is provided by the Companies Act that such creditor shall not proceed to realise his debt from such security without the leave of the court, since winding up proceedings is for the benefit of all the creditors. Therefore, for the preservation of such security, which is for the benefit of all the co-creditors, all such creditors shall necessarily share the expenses for such preservation of security, as contemplated by proviso to Section 529(2) of the Companies Act. It is an established principle of law that the burden and the benefit go together. If a secured creditor relinquishes his security, he would not be liable to share the expenses for preserving such security, since he would not be claiming the benefit of such security. Hence, as long as such secured creditor does not relinquish his security, he shall be liable to pay his portion of the expenses, incurred by the official liquidator, for the preservation of the security before its realisation by the secured creditors. The position of the State Financial Corporation

as one of the secured creditors would not be different from other creditors so far as the provisions of the Companies Act are concerned. In the decision in A. P. S. Financial Corporation v. Electrothermic Pvt. Ltd. 1996 86 Comp Cas 402 ; 1996 2 ALD 213, the Division Bench of this court held that the State Financial Corporation while exercising its right u/s 29 of the Financial Corporations Act, 1951, can exercise such statutory right to sell the property with the rights of pari passu charge holders in whose favour statutory charge is created by the provisions of Section 529(1) of the Companies Act. The Division Bench of this court has pointed out that the State Financial Corporation shall necessarily stand in the queue of the secured creditors pari passu with the claim of other secured creditors like State Bank of Hyderabad, etc. In this view of the matter, the contention of learned counsel appearing for the State Financial Corporation that as the financial corporation opted to stand outside the winding up proceedings with the permission of the court, the corporation can realise its debts u/s 29 of the State Financial Corporations Act, independently of the provisions of the Companies Act, cannot be upheld. A Division Bench of the Karnataka High Court in the decision in Karnataka State Industrial Investment and Development Corporation Limited Vs. M/s. Shivmoni Steel Tubes Limited and Others, made this position further clear by observing as under (page 14) :

"The proviso to Sub-section (1) of Section 529 as also Section 529A of the Act, having created pari passu charge in favour of the workmen, the same would affect the right of the appellant, Karnataka State Industrial Investment and Development Corporation, to sell the security directly by itself by invoking Section 29 of the State Financial Corporations Act, The appellant is required to join the official liquidator in the sale, and the property cannot be sold ignoring the pari passu charge holder,"

5. So far as the sharing of the expenses is concerned, a Division Bench of this court in Andhra Pradesh State Financial Corporation Vs. Official Liquidator, has further pointed out as under :

"As far as the third condition is concerned it calls upon the financial corporation to obtain the permission of the court before finalising the tenders. For this purpose it is necessary to take note of the fact that the proviso to Sub-section (2) of Section 529 of the Companies Act, which was incorporated by the Amendment Act (65 of 1960) lays down that if a secured creditor instead of relinquishing his security and proving for his debt proceeds to realise his security, he shall be liable to pay his portion of the expenses incurred by the liquidator for the preservation of security before its realisation by the secured creditor."

6. The Division Bench has further pointed out in that judgment that even though the official liquidator may not be in custody of the property secured, in view of Section 529(2) of the Companies Act such secured creditor may be saddled with the liability. If instead of relinquishing his security and proving for his debt, the secured creditor proceeds to realise his security, he has to reimburse the expenditure incurred by the official liquidator. According to this judgment, the liability to make contribution

towards the expenses would not have arisen, but for the proviso to Section 529(2) of the Companies Act, creating liability in such secured creditor also. In the said judgment, the Division Bench has further pointed out that for the purpose of enforcing the pari passu charge in favour of the workmen, the official liquidator should apply for rateable apportionment of the amount in the hands of such secured creditor on behalf of the workmen. Having regard to this principle enunciated by the Division Bench of this court, it follows that the company court may direct the other secured creditors, whether it is a financial corporation or any other creditor, to contribute his share of expenses in the expenses incurred by the official liquidator in preserving and maintaining the security. Such preservation and maintenance of security so far as he is concerned, is for the benefit of the workmen, who are pari passu secured creditors, having equal rights with other co-creditors, since "pari passu" itself means "with equal step equally without preference" as per Jowitt's Dictionary of Law. The official liquidator may have to incur other incidental expenses like paper publication communicating orders to the other persons affected by the winding up proceedings and all such expenses are ultimately meant to preserve and maintain the security for the benefit of the workmen, who are pari passu secured creditors. Therefore, the official liquidator is entitled to contribution from other co-secured creditors, for the expenses incurred by him proportionately. Another learned single judge of this court in *Business Machines (I) P. Ltd. v. Bank of India* 1998 91 Comp Cas 434, has also held that the company court can direct such secured creditors standing outside the winding up proceedings, but without relinquishing their security, to pay their proportionate share in the expenses incurred by the official liquidator. In all these cases on hand I find that it is not the case of any secured creditor, including the State Financial Corporation that they have given up or relinquished their interest in the security and if they have not relinquished their interest in the security, they are bound to make contributions towards the expenses incurred in preserving and maintaining such security. To the same effect also is the law declared by the High Court of Punjab and Haryana in the decision in *Punjab United Forge Ltd. v. Punjab Financial Corporation* 1993 76 Comp Cas 660.

7. However, counsel appearing for the State Financial Corporation by relying upon the judgment of the Supreme Court in *Industrial Credit and Investment Corporation of India Ltd. v. Srinivas Agencies* 1996 86 Comp Cas 255, contended that the corporation as the secured creditor standing outside the company proceedings can proceed to realise its security without the leave of the court, if the financial corporation had initiated action before the winding up order is passed against the company. From a reading of the said judgment, I find that counsel appearing on both sides in that case, did not dispute the principle of law laid down by the Supreme Court in *M.K. Ranganathan v. Government of Madras* 1955 25 Comp Cas 344. There is a difference between the provisions of the Indian Companies Act, 1913, and the provisions of the Companies Act, 1956. From a reading of the entire

judgment, I find that the Hon'ble Supreme Court was not considering the effect of Section 529A of the Companies Act, as amended in the year 1985. Moreover, the Division Bench of this court has already considered the principle laid down by the Supreme Court in *M. K. Ranganathan v. Government of Madras* 1955 25 Comp Cas 344 and held that the State Financial Corporation, though permitted to stand outside the liquidation proceedings, has to stand in the queue along with the other secured creditors. In view of these circumstances, in my humble opinion, the said judgment of the Hon'ble Supreme Court cannot assist the case of the financial corporation, to avoid the contribution of its share in the expenses to be borne by the official liquidator. If the financial corporation is also one of the secured creditors in the queue, it is also in the same queue even to share the contribution towards the expenses incurred by the official liquidator and because of Section 29 of the State Financial Corporations Act, 1951, the position of the financial corporation as a co-secured creditor would not be affected. Moreover, by virtue of Section 32E(2) of the State Financial Corporations Act, the Companies Act, 1956 is made applicable to the management of any industrial concern when it is taken over by the financial corporation. From this it follows that the power of the corporation to realise its debts under Sections 29 and 30 of the State Financial Corporations Act, would be subject to the provisions of the Companies Act, This conclusion is irresistible, because Section 46B of the State Financial Corporations Act specifically provides that save as provided in this Act, the provisions of this Act shall be in addition to and not in derogation of any other law for the time being applicable to the industrial concerns, there is no provision in the State Financial Corporations Act similar to Section 529A of the Companies Act. Therefore, Section 529A of the Companies Act would be applicable in addition to whatever is provided in the State Financial Corporations Act. Thus Section 32E of the State Financial Corporations Act would be subject to Section 46B of the State Financial Corporations Act. As pointed by the High Court of Delhi in the decision in *Disco Electronics Ltd. (In Liquidation)*, In the matter of: M/s. Disco Electronics Ltd., (In Liquidation), such a harmonious construction would lead to a conclusion that there is absolutely no inconsistency between Sections 29 and 30 of the State Financial Corporations Act and the provisions of the Companies Act. To the same effect also is the judgment of the High Court of Bombay in Maharashtra State Financial Corporation, Bombay Vs. Ballarpur Industries Limited, v. The Official Liquidator, High Court Bombay and Liquidator of M/s. Atrois Chemicals Private Limited,. Moreover, in the instant case, the State Financial Corporation is proceeding to realise its debts from the security, only with the permission of this court, subject to the conditions and stipulations the company court may impose. Therefore, there can also be a further direction to the State Financial Corporation to contribute its share towards the expenses incurred by the official liquidator in maintaining and preserving the security.

8. Learned counsel appearing for the State Financial Corporation further contended that in view of Section 529A of the Companies Act, Section 28(6) of the Provincial

Insolvency Act, 1920, is made applicable and if that is so, nothing shall affect the power of any secured creditor to realise or otherwise to deal with his security in the same manner as he would have been entitled to realise or deal with it, if Section 28 of the Provincial Insolvency Act had not been enacted. From a reading of Section 28 (1) and (2) of the said Act, I find that on the making of an order of adjudication, the property of the insolvent becomes divisible among the creditors and Sub-section (6) of Section 28 further provides as under :

"(6) Nothing in this section shall affect the power of any secured creditor to realise or otherwise deal with his security, in the same manner as he would have been entitled to realise or deal with it if this section had not been passed."

9. From a reading of the entire Section 28 of the Provincial Insolvency Act along with Section 529 of the Companies Act, I find that Section 28 of the Insolvency Act, though made applicable u/s 529, is made subject to the pari passu charge of the workers under the proviso to Section 529(1) of the Companies Act. The proviso to Sub-section (2) of Section 529 of the Companies Act, further provides as under :

"Provided that if a secured creditor instead of relinquishing his security and proving for his debt proceeds to realise his security, he shall be liable to pay (his portion of) the expenses incurred by the liquidator (including a provisional liquidator, if any) for the preservation of the security before its realisation by the secured creditor."

10. From this proviso, it follows that notwithstanding Section 28(6) of the Provincial Insolvency Act, the rights of the financial corporation as a secured creditor are subject to the pari passu charge in favour of the workmen, and the corporation also shall be liable to pay its portion of the expenses for preservation of the security as long as it does not relinquish his security. Viewed from any angle, in my opinion, the irresistible conclusion would be that all the secured creditors, including the State Financial Corporation as the secured creditor, are bound to contribute towards the expenses incurred by the official liquidator.

11. In view of this position of law, that I have ascertained, it follows that the official liquidator is entitled to the contribution from all the secured creditors, towards the expenses incurred by him. In this view of the matter, I direct that in the cases in which the other secured creditors, including the State Financial Corporation have not paid their contributions, they shall pay their contributions towards the expenses incurred by the official liquidator and in the cases where there is already a direction of the court to the secured creditors to pay certain amounts towards the expenses incurred by the official liquidator, such direction does not call for any modification.

12. Accordingly, the issue arising in all the referred company cases and company applications is hereby answered in terms of the above order. No costs.