

(1995) 09 PAT CK 0027

In the Patna High Court

Case No : Company Petition No. 2 of 1991

In Re: Bihar Woollen Fabrics Ltd. (In Liquidation)

Date of Decision : 22-09-1995

Acts Referred:

Companies Act, 1956 — Section 446, 446(1), 446(2), 446(3), 529
State Financial Corporations Act, 1951 — Section 29

Citation : (1998) 93 CompCas 334

Hon'ble Judges : S.N. Jha, J

Bench : Single Bench

Judgement

S.N. Jha, J.—Section 446 of the Companies Act, 1956 (in short, "the Act"), provides that after a winding-up order with respect to a company has been made or the official liquidator has been appointed as provisional liquidator, no suit or other legal proceeding shall be commenced, or if pending at the date of 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. In view of that provision, Canara Bank, the Bihar State Credit Investment Corporation Limited (in short, BISCICO) and the ex-managing director of the company have filed applications seeking, in the case of Canara Bank and the ex-managing director, leave to prosecute suits (Title Suits Nos. 104 and 106 of 1991, before the Subordinate Judge, Patna), and in the case of BISCICO, leave to file the suit for recovery of the money against the company. This order will dispose of the said applications.

2. Both the Canara Bank and the BISCICO are secured creditors. It is well settled that the secured creditors stand outside the liquidation proceeding and can realise their respective security without leave of the court but if they file the suit or take up other legal proceeding for realisation of the security, by reason of Section 446(1) of the Act, they are bound to obtain leave of the winding-up court. The BISCICO has further pressed into service the provisions of Section 29 of the State Financial Corporations Act, 1951 (in short, "the SFC Act"), to make out a case of pre-eminence. Section 29 of the SFC Act lays down that where any industrial concern, which is under liability to the financial corporation under an

agreement, makes any default in repayment of loan or advance, etc., the financial corporation is entitled to take over the management of the industrial concern including the right to transfer by way of lease or sale and realise the property pledged, mortgaged, hypothecated or assigned to the financial corporation. The BISCICO is said to be a "financial institution" within the meaning of Section 46 of the SFC Act to which the provisions of the SFC Act have been made applicable by the Central Government by notification, and thus entitled to put the assets of the defaulting company to sale and secure its liability from the sale proceeds. The point for consideration is whether having regard to the provisions of Section 446 of the Companies Act, a financial institution can be permitted to take recourse to the provisions of Section 29 of the SFC Act without taking leave of the company court. The other point for consideration is whether leave is to be granted to the secured creditors as a matter of course.

3. Section 537 of the Companies Act provides that where any company is being wound up by or subject to the supervision of the court, any attachment, distress or execution put in force, against the estate or effects of the company, or any sale of the properties or effects of the company held after the commencement of the winding-up proceeding, without leave of the court, shall be void, except a proceeding for recovery of any tax or impost or any dues payable to the Government. In view of the said provision there cannot be any doubt that the provisions of Section 29 of the SFC Act have to be read as subject to the provisions of the Companies Act. Besides, the provisions of Section 446 as also Sections 529 and 529A give enough indication that a secured creditor cannot be given a free choice in the matter of sale of the assets of the company and its appropriation.

4. Sub-section (2) of Section 446 provides that the winding-up court shall, notwithstanding anything contained in any other law for the time being in force, have jurisdiction to entertain or dispose of, inter alia, "any question of priorities or any other question whatsoever." Sub-section (2) of Section 446 was introduced by Act 65 of 1960. By this sub-section, the company court was entrusted with the power to entertain and dispose of the matters more particularly mentioned in Sub-clauses (a), (b), (c) and (d). Under Sub-clause (b), the court can dispose of any claim made by or against the company. Under Sub-clause (d), the court can also decide "any question of priorities or any other question whatsoever, whether of law or fact, which may relate to or arise in course of the winding-up of the company." While considering the scope of the said provision in the case of *Sudarsan Chits (3) Ltd. v. G. Sukumaran Pillai* AIR 1984 SC 1529 ; [1985] 58 Comp Cas 633 the Supreme Court, after noticing the historical evolution of the provision, observed :

"To avoid this eventuality and to keep all incidental proceedings in winding-up before the court which is winding up the company, its jurisdiction was enlarged to entertain a petition, amongst others, for recovering the claims of the company. In the absence of a provision like Section 446(2) under the repealed

Indian Companies Act, 1913, the official liquidator in order to realise and recover the claims and subsisting debts owed to the company had the unenviable fate of filing suits. These suits, as is not unknown, dragged on through the trial court and courts of appeal resulting not only in multiplicity of proceedings but in holding up the progress of the winding-up proceedings. To save the company which is ordered to be wound up from this prolix and expensive litigation and to accelerate the disposal of winding-up proceedings, Parliament devised a cheap and summary remedy by conferring jurisdiction on the court winding up the company to entertain petitions in respect of claims for and against the company. This was the object behind enacting Section 446(2) and, therefore, it must receive such construction at the hands of the court as would advance the object and at any rate not thwart it."

5. Section 529 provides that in the winding up of an insolvent company the same rules shall prevail and be observed with regard to-

(a) debts provable ;

(b) the valuation of annuities and future and contingent liabilities ; and

(c) the respective rights of secured and unsecured creditors as are in force for the time being under the law of insolvency with respect to the estates of persons adjudged insolvent :

Provided 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 the workmen's portion therein, and, where a secured creditor, instead of relinquishing his security and proving his debt, opts to realise his security,--(a) the liquidator shall be entitled to represent the workmen and enforce such charge ; (b) any amount realised by the liquidator by way of enforcement of such charge shall be applied rateably for the discharge of workmen's dues ; and (c) so much of the debt due to such secured creditor as could not be realised by him by virtue of the foregoing provisions of this proviso or the amount of the workmen's portion in his security, whichever is less, shall rank pari passu with the workmen's dues for the purposes of Section 529A. All persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company, as may come in under the winding-up, and make such claims against the company as they respectively are entitled to make by virtue of the said provision. Where a secured creditor instead of relinquishing his security and proving for his debt proceeds to realise the security, he shall be liable to pay the expenses incurred by the liquidator for the preservation of the security before its realisation by the secured creditor.

6. Section 529A which came on the statute book by Act 35 of 1985 lays down that notwithstanding anything contained in any other provision of the Companies Act or any other law for the time being in force in the winding-up of the company, workmen's dues and 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 and in full unless the assets are insufficient to meet them in which case they shall abate in equal proportions.

7. The total effect of all these provisions is that the entire property and assets of the company which has been ordered to be wound-up, immediately come under the custody of the company court and become custodia legis. The position of the official liquidator is like a receiver appointed by the court for the purpose of acquiring and retaining the property of the company and acting subject to and in accordance with the directions, from time to time, given by the company court.

8. Thus, while a secured creditor may choose to stand outside the winding-up proceedings, the jurisdiction of the company court to deal with such creditors and the properties is not taken away. Sub-section (2) of Section 446 recognises the jurisdiction of the company court to entertain and dispose of any claim made by or against the company and to determine any question of priorities or "any other question whatsoever which may relate to or arise in course of the winding-up". The expression "standing outside the winding-up" merely means that the secured creditor is given option to realise the security either by private sale if it has power to do so, or through a court sale if there is any dispute regarding the nature of the security or the value of the security, or u/s 29 of the SFC Act. But that does not mean that the company's assets in liquidation pursuant to the order of the company court are taken out of the purview of the jurisdiction of the company court. u/s 529A, the workmen's dues and the debts due to the secured creditors to the extent of Section 529(1)(c) have to be worked out in the light of the illustrations given u/s 529 and that can be done only by the company court in exercise of the power u/s 446(2) (b) and (d) of the Act.

9. I would, accordingly, reject the plea advanced on behalf of the BISCICO for leave to effect sale of the assets of the company u/s 29 of the SFC Act.

10. During the course of hearing my attention was drawn to an interim order passed by the Supreme Court in SLP (Civil) No. 18199 of 1993, with SLP (Civil) No. 7338 of 1994, arising out of the judgment of the Karnataka High Court upholding the action of the Karnataka State Financial Corporation in regard to the sale of the property of the company, The interim order runs as follows :

"Meanwhile it appears appropriate that the respondent-Karnataka State Financial Corporation should sell the property acting jointly with the official liquidator under supervision and in accordance with the direction of the learned company judge of the High Court and the sale proceeds be deposited in the court and then distributed in accordance with the directions of the learned company judge."

11. The above order is no doubt an interim order. It, however, gives some indication of the fact that the power of the financial institution in the matter of sale of the assets of the company, which is being wound up, u/s 29 of the SFC Act should be exercised subject to the jurisdiction of the company court and the provisions of the Companies Act.

12. Coming to the petition filed by Canara Bank it would appear that its right to sell the assets of the company, either by private sale or court sale, and realise its security from the sale proceeds rests on the agreement. There is no statutory provision like Section 29 of the SFC Act conferring upon it any additional right in the matter of sale. In that sense it stands on a lesser footing compared to the BISCICO or other like financial institution. Its claim cannot, therefore, stand on any higher legal pedestal. The observations made hereinabove that while the secured creditor has got an option to realise the security outside the liquidation proceedings, such rights are to be exercised subject to the jurisdiction of the company court and the provisions of the Companies Act where the liquidation proceeding with respect to the company has commenced, would apply with equal force if not more in its case as well. On behalf of the Canara Bank, however, reliance was placed on a judgment of this court in the case of United Bank of India v. Official Liquidator, Maksudpur Refrigeration Industries (P.) Ltd. [1986] 59 Comp Cas 770 wherein it has been held that if a secured creditor chooses to file a suit or has already filed a suit before the winding-up order is passed, he is no doubt required to obtain leave of the company court but the same should be granted as a matter of course unless there are special grounds for its refusal.

13. In view of the clear provisions of Sub-section (1) of Section 446 there is no dispute at the Bar that the suits cannot proceed except by leave of this court. The only question for consideration then is whether in the case of secured creditors leave should be granted as a matter of course. Having regard to the aforementioned provisions of Section 446(2), Section 529 and Section 529A, which do not appear to have been noticed by the learned judges, I find it difficult to subscribe to the view taken by this court in the aforementioned case. Granting leave "as a matter of course" would make the provisions of Section 529 (as amended) and Section 529A superfluous and the scheme unworkable. It would also result in multiplicity of proceedings causing avoidable financial burden on the company which would not be in its interest. The order which commends itself more to me is the one contemplated by Sub-section (3) of Section 446 regarding transfer of the proceeding.

14. I would accordingly refuse leave to BISCICO to either file a suit or take recourse to Section 29 of the SFC Act on its own, but direct that suits already pending, namely, Title Suit No. 104 of 1991, and Title Suit No. 106 of 1991, by the Canara Bank and ex-managing director, in the court of the Subordinate Judge at Patna, be transferred to be disposed of by this court in the present proceedings. I order accordingly.

15. The petitions in question at flags "20", "21", "13" and "33" are, accordingly, disposed of.