
(2007) 03 RAJ CK 0002
In the Rajasthan High Court

In Re: Lords Chloro Alkali Ltd. (formerly known as Modi Alkalies and Chemicals Ltd.)

Date of Decision : 15-03-2007

Acts Referred:

Companies Act, 1956 — Section 391

Citation : (2009) 148 CompCas 873

Hon'ble Judges : Shiv Kumar Sharma, J

Bench : Single Bench

Final Decision : Allowed

Judgement

Shiv Kumar Sharma, J.—The petitioner, Lords Chloro Alkali Ltd. (formerly known as Modi Alkalies and Chemicals Ltd.) filed this petition under Sections 391 and 394 of the Companies Act, 1956 (hereinafter shall be referred to as "the Act of 1956"), for sanction of scheme of arrangement so as to be binding on all the secured creditors of the petitioner, i.e., respondents herein.

2. The petitioner-company was incorporated on March 1, 1979, in the State of Punjab originally under the name and style of Modi Alkalies and Chemicals Ltd. Subsequently in the year 1979 itself, the registered office of the petitioner was shifted to Industrial Area, Alwar (Rajasthan). The name of the petitioner-company was subsequently changed to Lords Chloro Alkalies Ltd. on February 1, 2003.

3. The petitioner-company had availed of financial assistance from the IDBI, IFCI, PNB, ICICI, SBI, Indian Bank, Syndicate Bank, IIBI, UTI and RIICO. It was stated in the petition that the company had operated successfully till for almost fifteen years. Thereafter, it had incurred financial losses and as a result of which its net worth had fully eroded. Upon erosion of its net worth as on June 30, 1999, the petitioner-company filed a reference, which was rejected by the Board for Industrial and Financial Reconstruction. Upon further erosion of its net worth as on June 30, 2000, the company had accordingly filed another reference with the BIFR. The BIFR vide its order dated January 15, 2002, had declared the petitioner-company as a sick industrial company in terms of Section 3(1)(o) of

the Sick Industrial Companies (Special Provisions) Act, 1985 ("SICA") on the basis of its reference for the financial year ending on June 30, 2000. It was stated in the petition that while the petitioner-company was in the process of entering into negotiation with its secured creditors, for settlement in their dues the BIFR, vide an ex parte order dated June 2, 2004, formed prima facie opinion to wind up the petitioner-company u/s 20(1) of the SICA and accordingly directed issuance of show cause notice for winding up of the petitioner-company. The petitioner-company filed an appeal before the Appellate Authority for Industrial and Financial Reconstruction. In the interregnum the dues of PNB, SBI were settled at 26.5 per cent, of the principal by effecting payment to the tune of Rs. 61.75 lakhs and Rs. 55 lakhs, respectively, in full and final settlement of their dues. The IDBI assigned its debts to D and DARC, and ICICI had assigned its debts to Sopan Securities (P.) Ltd. The Indian Bank had also assigned its debt to D and DARC while Syndicate Bank had assigned its debt to First Alert Fire Systems (P.) Ltd. It has been stated in the petition that all the assignees are also prepared to settle their dues at 26.5 per cent, of the principal. The AAIFR, vide its order dated December 20, 2005, allowed the appeal and set aside the order dated June 2, 2004 and remanded back the matter to the BIFR, where the matter is currently pending. It is stated in the petition that the petitioner-company is interested in settling the liabilities of its secured creditors. The IFCI, Sopan Securities (P.) Ltd. and D and DARC, who compositely constitute 86.94 per cent, of the total secured creditors, vide their letters dated March 10, 2006, July 26, 2006, and June 26, 2006, expressed their willingness for the settlement of their dues at 26.5 per cent, of the principal amount towards the full and final settlement of their dues. The board of directors of the petitioner-company, vide board's resolution dated July 31, 2006, approved the scheme of arrangement and the payments to be made thereunder. The scheme of arrangement has been annexed as annexure A to the petition.

4. The petitioner-company filed Company Application No. 43 of 2006 for convening meeting of its secured creditors. This Court vide its order dated August 18, 2006, directed to convene meeting of the secured creditors on September 9, 2006, but the said meeting could not be conducted as on account of delay in calling the meeting. The petitioner-company filed application and on the application this Court further directed to call the meeting of the secured creditors, vide order dated September 1, 2006 and the meeting was directed to be convened on September 30, 2006. In the absence of Shri Suresh Pareek, chairman appointed by the court the meeting was adjourned and was notified to be held on October 7, 2006. In the meeting held on October 7, 2006, the scheme was supported and approved by D and DARC, SSPL and CCPL who jointly constitute more than 86.94 per cent, of the total secured creditors, while RIICO and UTI opposed the scheme and submitted their objections whereas IIBI had not attended the meeting. The petitioner-company submitted that more than 93.22 per cent, of the secured creditors present and voting agreed to the scheme of arrangement. The petitioner-company averred that more than three-fourth of

the total secured creditors agreed for sanctioning scheme of arrangement.

5. The petitioner-company filed the above petition and this Court on December 1, 2006, directed to publish the notice of this petition to the Regional Director, Northern Region, Ministry of Company Affairs, NOIDA. Subsequently, by the order of this Court dated December 8, 2006, the notice was directed to be published in daily newspaper Dainik Bhaskar (Jaipur-Hindi edition) and daily newspaper The Hindustan Times (New Delhi-English edition). The petitioner-company filed the copies of the publication published in the said newspapers.

6. The official liquidator attached to this Court filed affidavit of the Regional Director, on January 4, 2007. In the affidavit it has been averred that except IIBI all other secured creditors attended the meeting held on October 7, 2006. The RIICO submitted letter dated September 29, 2006, objecting that the scheme of arrangement at 26.5 per cent, of the outstanding principal is not agreeable to them. The UTI also raised objection that they are taking a hit not only on interest dues but also the principal amount given to the petitioner-company. The other four secured creditors, i.e., D and DARC (IDBI), D and DARC (IB), SSPL (ICICI), and Circus Chemicals (P.) Ltd. (IFCI) agreed to the scheme of arrangement proposed by the petitioner-company. In the affidavit regarding report in paragraphs 4(A), 4(B) and 5 in relation to balance-sheet as at March 31, 2005 and March 31, 2006, the auditors stated as under:

(i) The accounts for the year have been prepared on a going concern basis even though the company has been declared as a sick company by the BIFR. However, the financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and to amounts and classification of liabilities. In view of the above, we are unable to express our opinion on the appropriateness of going concern assumption in the preparation of financial statements.

(ii) Balance of current assets including inoperative bank accounts, sundry debtors, recoverable loans and advances, secured loans and current liabilities including sundry creditors are subject to confirmation and adjustments necessary upon reconciliation thereof. The effect of the adjustments arising from reconciliation/confirmation and possible loss that may arise on account of non-recovery or partial recovery of current assets including sundry-debtors, and recoverable advances is not ascertainable.

(iii) The company has investments in unquoted shares of two companies amounting to Rs. 302.35 lakhs (previous year Rs. 373.35 lakhs). These are shown at cost and no provision has been made regarding possible diminution in the value of these shares.

(iv) Advances received in earlier years towards sale of non-factory land owned by the company remain unadjusted pending completion of necessary formalities.

(v) The company is taking steps to comply with the provisions of Section 113 and

other applicable provisions of the Companies Act, 1956.

(vi) The company has not transferred an amount of Rs. 11.64 lakhs to the "Investor Education and Protection Fund" as required. This is contravention of the provisions of Section 205C of the Companies Act.

(vii) As informed to us by the management, the recoverable amount of the assets are more than the carrying amount of assets, hence, the company has not carried out any adjustments in the book value of its fixed assets as required under AS-28, for impairment of assets, issued by ICAI. This being a technical matter, we are unable to express our opinion regarding the value at which the above fixed assets are being carried in the accounts for the year and realisable value of the same.

(viii) The company has not complied with the mandatory Accounting Standards (revenue recognition issued by the ICAI) as the company is recognising revenue consistently on cash basis in few cases as stated in Accounting Policy No. A.2(ii) of Schedule "O".

(ix) As per past practice the company has not provided for electricity authorities demand of Rs. 1,316.70 lakhs, electricity duty demand of Rs. 27.71 lakhs, entry tax demand of Rs. 26.14 lakhs, Income Tax authorities demand of Rs. 976 lakhs, excise duty demand of Rs. 619.13 lakhs. Special Directorate of Enforcement demand of Rs. 150 lakhs, interest liability of Rs. 431.40 lakhs on deposits from dealers/group companies, provident fund authorities demand of Rs. 186.80 lakhs and staff dues for ,prior years of Rs. 457.53 lakhs.

(x) Had the observations made above in paragraph (ix) been considered, the loss for year would have been Rs. 5,123.63 lakhs as against reported figure of Rs. 4,731.61 lakhs and accumulated loss would have been Rs. 35,287.63 lakhs as against the reported figure of Rs. 30,499.65 lakhs.

In the affidavit it has been averred that the above adverse remarks of the auditor has direct bearing on the financial position of the company.

7. Countering to the affidavit of the Regional Director an affidavit has been filed by P.K. Goyal, chief financial officer of the petitioner-company stating that the petitioner-company, a financially unviable entity, is making efforts for turning around during the last couple of years as is evident from the fact that the company has achieved a sales turnover of Rs. 52 crores for the year ended March 31, 2006, as against a sale turnover of Rs. 19.17 crores in the year ended on March 31, 2005. It is stated that despite the increase in sale value the petitioner-company is incurring losses due to heavy interest burden and that is the reason for entering into an arrangement with the secured creditors and the secured creditors representing more than 86 per cent, of its value have already approved the scheme of arrangement in the meeting held on October 7, 2006. In relation to requirement for making provisions for impairment of assets arises only when the value of the assets will be less than the recoverable value. Since

the current management has already formed an opinion that the amount that will be recovered from the assets of the company will be more than the value of assets, there is no need for making any provision for impairments of assets. Regarding electricity dues, entry tax, etc., in the affidavit, it is submitted that the petitioner-company was a sick industrial company and they were bound to be non-fulfilment of certain obligations. The company will clear all the liabilities specified in accordance with the scheme of rehabilitation sanctioned by the BIFR.

8. The RIICO, one of the secured creditors, filed application under Sections 391 and 394 of the Act read with Rules 9, 67 to 87 of the Companies (Court) Rules, 1959, for reconsideration and modification of scheme of arrangement proposed by the petitioner-company. The RIICO submitted that the scheme is not acceptable to them as the petitioner-company had put the RIICO in separate class of creditors for repayment of its dues. The petitioner-company vide letter dated February 15, 2006, proposed to pay the principal amount due Rs. 81 lakhs in three years time, out of which 10 per cent, of the principal amount was agreed to be paid immediately on the acceptance on the part of RIICO and balance 90 per cent, of the amount was proposed to be paid in six half yearly interest free instalments in three years time. In the hearing held on November 30, 2006, before the BIFR the petitioner-company's advocate stated that the dues of IIBI, RIICO and UTI would be settled separately. It was stated that in these circumstances it would not be proper to include the applicant-RIICO's due in the scheme proposed in the meeting dated October 7, 2006, under the orders of this court.

9. The petitioner-company filed reply to the application in the form of affidavit and stated that, vide letter dated February 15, 2006, the petitioner-company made a proposal to settle the principal dues of RIICO in three years time. As RIICO did not accept the proposal, the petitioner-company which was in a financially distressed condition, whose more than 75 per cent, of the secured creditors had agreed to settle their principal dues at the rate of 26.5 per cent, submitted the scheme of arrangement before this Court which was duly supported by more than 75 per cent, of the secured creditors present and voting in the meeting held on October 7, 2006, as per the directions of this court. The BIFR, while sanctioning the scheme for revival of the petitioner vide its order dated November 30, 2006, observed as under:

13. The Bench observed that 86.94 per cent, of the total secured creditors by value were agreeable to the provisions of the DRS and had agreed for settlement at 26.50 per cent, of their principal outstanding dues. This left IIBI, RIICO and UTI who constituted only 13.06 per cent, of the outstanding principal dues. Although the company had made the same offer to them also the settlement was not yet finalised. As such they could not be allowed to hold up sanction of the scheme and their dues will be settled by the company/promoters separately, in line with the directions of AAIFR. The Bench noted the LCAL had filed a scheme of arrangement u/s 391 of the Companies Act, 1956 with the Jaipur Bench of the

High Court for settlement of dues of secured creditors/assignees and the remaining 3 secured creditors, viz., IIBI, UTI and RIICO on identical terms by payment of 26.5 per cent, of outstanding principal.

10. Furthermore in the scheme sanctioned by the BIFR, for the settlement of dues of RIICO, IIBI and UTI under the heading "Reliefs and Concessions" it has been provided as under:

4. Settlement of dues on similar terms, viz., 26.5 per cent, of outstanding principal are under negotiation with IIB Ltd. UTI and RIICO. As such, their dues will be settled by the company/strategic investors separately by way of scheme filed before the Jaipur Bench of the High Court u/s 391 of the Companies Act, 1956.

11. The petitioner-company averred that before the AAIFR, the term "dealt with separately" implied that their dues shall not be governed by the scheme to be drawn by the BIFR but to be dealt with outside that scheme, i.e., scheme of arrangement which was separate and distinct from the scheme sanctioned by the BIFR, wherein the BIFR had allowed the petitioner to settle the dues of all its secured creditors including RIICO as per the scheme of arrangement filed before this court. The petitioner-company averred that it is wrong and incorrect that they had put RIICO in a separate class of creditors for repayment of its dues separately. Actually, the dues of RIICO are proposed to be settled at the same pedestal as the other secured creditors through the scheme of arrangement and not as per the scheme drawn by the BIFR and, thus, it cannot harp upon the fact that its dues are to be dealt with separately as being alleged in the application.

12. RIICO filed rejoinder to the reply filed by the petitioner-company. In the rejoinder it was averred that the proposal for mode of repayment made by the petitioner-company vide letter dated February 15, 2006, was under negotiation and the RIICO believing the same to be in good faith did not initiate the recovery proceedings but it was a mechanism developed by the petitioner-company with mala fide intentions. The other creditors in the matter namely IDBI, ICICI, IFCI and Indian Bank have assigned their dues to the companies/institutions, who were present in meeting dated October 7, 2006. Dhir and Dhir Reconstruction and Securitisation Co. Ltd., one of the assignee, is the second shareholder of the company holding 9.24 per cent, of the total share capital. The other higher shareholder is Modipon Ltd., who has 10.54 per cent, of the total shares. In the event of settlement as per the scheme the beneficiaries would be the shareholders mainly Modipon Ltd. and Dhir and Dhir Assets Reconstruction and Securitisation Co. Ltd. The arrangement proposed was based on the valuation report of ICICI Bank provided to RIICO by the company in November 2002, which shows the value of the assets as Rs. 17.18 crores. The company has a huge chunk of industrial as well as residential land, whose value has been assigned only Rs. 66.46 lakhs. The valuation report does not assign any value to residential land on account of dispute. As against the same on the basis of RIICO's industrial rates the present value of the same works to around Rs.

1,890.91 lakhs. The value of land on RIICO's rate for industrial land if added to the valuation of buildings and plant and machinery done by the valuer the total valuation would be more than Rs. 3,542.88 lakhs as against the settlement of Rs. 1,027.70 lakhs. The majority of the secured creditors have not acted bona fide as a result the minority of the creditors including the RIICO is sought to be overridden in an unreasonable and unjust manner, causing heavy losses to public money and serious detriment to RIICO. The dues of RIICO, UTI and IIBI are liable to be settled separately inasmuch as the scheme of arrangement in question does not confirm the standard of reasonableness and the same does not deserve approval by this court. The petitioner-company tried to misconstrue the term dealt with separately in utter disregard to the facts of the case. Lastly, prayer was made to take the rejoinder on record and for allowing the application of the RIICO.

13. I have heard learned Counsel for the parties and weighed the material on record.

14. In *Miheer H. Mafatlal Vs. Mafatlal Industries Ltd.*, , the following broad contours of the jurisdiction of the company court have been laid down for sanctioning the scheme:

(i) The sanctioning court has to see to it that all the requisite statutory procedure for supporting such a scheme has been complied with and that the requisite meetings as contemplated by Section 391(1)(a) have been held.

(ii) The scheme put up for sanction of the court is backed up by the requisite majority vote as required by Section 391, Sub-section (2).

(iii) The meetings concerned of the creditors or members or any class of them had the relevant-material to enable the voters to arrive at an informed decision for approving the scheme in question. That the majority decision of the concerned class is just and fair to the class as a whole so as to legitimately bind even the dissenting members of that class.

(iv) All necessary material indicated by Section 393(1)(a) is placed before the voters at the meetings concerned as contemplated by Section 391, Sub-section (1).

(v) All the requisite material contemplated by the proviso of Sub-section (2) of Section 391 of the Act is placed before the court by the applicant concerned seeking sanction for such a scheme and the court gets satisfied about the same.

(vi) The proposed scheme of compromise and arrangement is not found to be violative of any provision of law and is not unconscionable, nor contrary to public policy. For ascertaining the real purpose underlying the scheme with a view to be satisfied on this aspect, the court, if necessary, can pierce the veil of apparent corporate purpose underlying the scheme and can judiciously X-ray the same.

(vii) The company court has also to satisfy itself that the members or class of

members or creditors or class of creditors, as the case may be, were acting bona fide and in good faith and were not coercing the minority in order to promote any interest adverse to that of the latter compromising the same class whom they purported to represent.

(viii) The scheme as a whole is also found to be just, fair and reasonable from the point of view of prudent men of business taking a commercial decision beneficial to the class represented by them for whom the scheme is meant.

(ix) Once the aforesaid broad parameters about the requirements of a scheme for getting sanction of the court are found to have been met, the court will have no further jurisdiction to sit in appeal over the commercial wisdom of the majority of the class of persons who with their open eyes have given their approval to the scheme even if in the view of the court there would be a better scheme for the company and its members or creditors for whom the scheme is framed. The court cannot refuse to sanction such a scheme on that ground as it would otherwise amount to the court exercising appellate jurisdiction over the scheme rather than its supervisory jurisdiction. It is the commercial wisdom of the parties to the scheme who have taken an informed decision about the usefulness and propriety of the scheme by supporting it by the requisite majority vote that has to be kept in view by the court. The court has neither the expertise nor the jurisdiction to delve deep into the commercial wisdom exercised by the creditors and members of the company who have ratified the scheme by the requisite majority. Consequently, the company court's jurisdiction to that extent is peripheral and supervisory and not appellate. The court acts like an umpire in a game of cricket who has to see that both the teams play their game according to the rules and do not overstep the limits. But subject to that how best the game to be played is left to players and not to the umpire. The supervisory jurisdiction of the company court can also be culled out from the provisions of Section 392. Of course, this section deals with post-sanction supervision. But the said provision itself clearly earmarks the field in which the sanction of the court operates. The supervisor cannot ever be treated as the author or a policy-maker. Consequently, the propriety and the merits of the compromise or arrangement have to be judged by the parties who as *sui juris* with their open eyes and fully informed about the pros and cons of the scheme arrive at their own reasoned judgment and agree to be bound by such compromise or arrangement.

15. In *Hindustan Lever and Another Vs. State of Maharashtra and Another*, the apex court indicated that the jurisdiction of the company court while sanctioning the scheme is supervisory only. While exercising its power in sanctioning the scheme of amalgamation the court is to satisfy itself that the provisions of statute have been complied with, that the class was fairly represented by those who attended the meeting, that the statutory majority was acting bona fide and not in an oppressive manner and that the arrangement is such as which a prudent, intelligent or honest man or a member of the class concerned and acting in respect of the interest might reasonably take. While examining as to

whether the majority was acting bona fide, the court would satisfy itself to the effect that the affairs of the company were not being conducted in a manner prejudicial to the interest of its members or to public interest. The basic principle underlying such a situation is none other than the broad and general principle inherent in any compromise or settlement entered into between the parties, the same being that it should not be unfair, contrary to public policy and unconscionable or against the law, once these things are satisfied, the scheme has to be sanctioned as per the compromise arrived at between the parties. The court would have no further jurisdiction to sit in appeal over the commercial wisdom of the class of persons who with their eyes open give their approval even if, in the view of the court a better scheme could have been framed.

16. Bearing the above principles in mind I proceed to weigh the scheme as well as the objections raised by the Regional Director in his affidavit regarding auditors report, application filed by the RIICO, reply to the application filed by the petitioner-company and the rejoinder to the reply filed by RIICO. As laid down by the apex court, while exercising its power in sanctioning the scheme of arrangement the court is to satisfy itself that the provisions of statute have been complied with, the class was fairly represented by those who attended the meeting, the statutory majority was acting bona fide and not in an oppressive manner and the arrangement is such as which a prudent, intelligent or honest man or a member of the class concerned and acting in respect of the interest might reasonably take. While examining as to whether the majority was acting bona fide, the court would satisfy itself to the effect that the affairs of the company were not being conducted in a manner prejudicial to the interest of its members or to public interest. The basic principle underlying such a situation is none other than the broad and general principle inherent in any compromise or settlement entered into between the parties, the same being that it should not be unfair, contrary to public policy and unconscionable or against the law, once these things are satisfied the scheme has to be sanctioned as per the compromise arrived at between the parties. In the instant matter where the secured creditors voted in their meeting in favour of the scheme of arrangement it is not for this Court to sit in appeal over the commercial wisdom of the majority of the class of persons who with their open eyes have given their approval to the scheme.

17. Having closely scrutinised the scheme of arrangement, I find that it is not unjust and unfair to the secured creditors. The scheme appears to be reasonable, according to law and in the interest of the secured creditors.

18. For these reasons the petition stands allowed and the scheme of arrangement is sanctioned in terms of prayer Clause (a). Costs of Rs. 2,500 (two thousand five hundred) to the official liquidator to be paid by the petitioner within two weeks from today. The copy of the order be sent to the Registrar of Companies as per the Rules. The application filed by RIICO for reconsideration and modification of the scheme shall consequently stand rejected.