
(2014) 09 AP CK 0131

In the Andhra Pradesh High Court

Case No : Company Appeal No. 6 of 2014 in Company Petition Nos. 26 and 65 of 1987

LVSR Farms Private Limited

APPELLANT

Vs

The Official Liquidator

RESPONDENT

Date of Decision : 16-09-2014

Acts Referred:

Companies Act, 1956 — Section 235, 237, 529, 529(1)(c), 529A
Provincial Insolvency Act, 1920 — Section 28, 28(6), 35, 44(2), 47
Workmens Compensation Act, 1923 — Section 14

Citation : (2014) 187 CompCas 400

Hon'ble Judges : C.V. Nagarjuna Reddy, J

Bench : Single Bench

Advocate : L.V.V. Iyer, Advocate and B. Chandrasen Reddy, Advocate for the Appellant; M. Anil Kumar, Counsel, Advocate for the Respondent

Judgement

C.V. Nagarjuna Reddy, J.

A. Introduction:

1. A short, but important question arises in this Company Appeal. The question is whether a secured creditor is entitled to contractual rate of interest for the post winding-up period if surplus amount is available before such amount is distributed among the unsecured creditors?

B. The background facts:

2. The facts lie in a narrow compass. M/s. Vidyut Steels Limited (hereinafter referred to as "the company in liquidation") was ordered to be wound up by this Court by order dated 22-4-1988 in C.P. Nos. 26 and 65 of 1987. The Official Liquidator attached to this Court was appointed as the Liquidator of the company in liquidation. By order dated 7-4-2010 in C.A. No. 240 of 2010, this Court has permitted the Official Liquidator to invite claims from all the creditors. In pursuance of the publication made by the Official Liquidator in newspapers, the

appellant herein has filed its claim on 25-10-2010 for a sum of Rs. 24,42,42,138-84 ps. before the Official Liquidator in its capacity as the assignee of security interests of four secured creditors, viz., IDBI, IFCI, ICICI and LIC. As there was delay in filing its claim, the appellant has filed C.A. No. 1346 of 2010 before this Court for condonation of delay. By order dated 23-11-2010, this Court has condoned the delay.

3. Upon considering the claim putforth by the appellant as the assignee of the four secured creditors referred to above, the Official Liquidator has admitted the appellant's claim only to an extent of Rs. 2,66,73,817/-. While adjudicating the claim, the Official Liquidator has allowed the principal amount as claimed by the assignee along with contractual rate of interest upto the date of winding up of the company while disallowing the claim for interest at the contractual rate for the post winding up period. The appellant filed this appeal to the extent of the Official Liquidator disallowing the claim for interest at the contractual rate for the said period.

4. The appellant claimed that on the principal amount it is entitled to interest @ 9.50% which is the contractual rate of interest for the post winding up period also. That the contracts of the secured creditors provide for interest @ 9.50% is not in dispute. However, in his report, the Official Liquidator stated that he has adjudicated the claims of the secured, preferential and unsecured creditors at Rs. 4,81,65,026/- as against a sum of Rs. 22,34,55,625-72 ps. which is lying to the credit of the company in liquidation. While referring to Rule 179 of the Companies (Court) Rules 1959 (for short "the Rules"), the Official Liquidator stated in his report that though surplus funds are available, in view of the said Rule placing a limit on payment of interest @ 4% per annum from the date of winding up order, he is disabled from paying the contractual rate of interest which is higher than 4% per annum and that if this Court directs him to pay interest at the contractual rate, he has no objection to pay such interest to all the creditors of the company in liquidation.

5. I have heard Sri L.V.V. Iyer, learned Counsel for the appellant and Sri M. Anil Kumar, learned Counsel for the Official Liquidator.

C. Legal Environment

Relevant provisions under the Companies Act:

6. Part VII, Chapter V of the Companies Act, 1956 (for short "the Act") deals with Proof and ranking of claims. Section 529 of the Act made insolvency rules applicable in winding up of insolvent companies. Section 529-A of the Act which contains a non-obstante clause provides that the workmen's dues and debts due to secured creditors as mentioned in sub-clause (b) of sub-section (1) thereof shall be paid in priority to all other debts. Sub-section (2) thereof ordains that the debts payable as mentioned in sub-clauses (a) and (b) of sub-section (1) shall be paid in full, unless the assets are insufficient to meet them in which case they shall abate in equal proportions. Section 530 provides for giving priority in

respect of certain debts over other debts. As these provisions play a pivotal role in the disposal of this Company Appeal, it is necessary to reproduce them herein below:

Section 529 - Application of insolvency rules in winding up of insolvent companies:

(1) 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.

(2) All persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company, may come in under the winding up, and make such claims against the company as they respectively are entitled to make by virtue of this section:

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 realization by the secured creditor .

Explanation.-For the purposes of this proviso, the portion of expenses incurred by the liquidator for the preservation of a security which the secured creditor shall be liable to pay shall be the whole of the expenses less an amount which bears to such expenses the same proportion as the workmen's portion in relation to the security bears to the value of the security.

(3) For the purposes of this section, section 529A and section 530,-

(a) "workmen", in relation to a company, means the employees of the company, being workmen within the meaning of the Industrial Disputes Act, 1947 (14 of 1947);

(b) "workmen's dues", in relation to a company, means the aggregate of the following sums due from the company to its workmen, namely:-"

(i) all wages or salary including wages payable for time or piece work and salary earned wholly or in part by way of commission of any workman, in respect of services rendered to the company and any compensation payable to any workman under any of the provisions of the Industrial Disputes Act, 1947 (14 of 1947);

(ii) all accrued holiday remuneration becoming payable to any workman, or in the case of his death to any other person in his right, on the termination of his employment before, or by the effect of, the winding up order or resolution;

(iii) unless the company is being wound up voluntarily merely for the purposes of reconstruction or of amalgamation with another company, or unless the company has, at the commencement of the winding up, under such a contract with insurers as is mentioned in section 14 of the Workmen's Compensation Act, 1923 (8 of 1923) rights capable of being transferred to and vested in the workman, all amounts due in respect of any compensation or liability for compensation under the said Act in respect of the death or disablement of any workman of the company;

(iv) all sums due to any workman from a provident fund, a pension fund, a gratuity fund or any other fund for the welfare of the workmen, maintained by the company;

(c) "workmen's portion", in relation to the security of any secured creditor of a company, means the amount which bears to the value of the security the same proportion as the amount of the workmen's dues bears to the aggregate of-

(i) the amount of workmen's dues; and

(ii) the amounts of the debts due to the secured creditors.

Illustration:

The value of the security of a secured creditor of a company is Rs. 1,00,000. The total amount of the workmen's dues is Rs. 1,00,000. The amount of the debts due from the company to its secured creditors is Rs. 3,00,000. The aggregate of the amount of workmen's dues and of the amounts of debts due to secured creditors is Rs. 4,00,000. The workmen's portion of the security is therefore, one-fourth of the value of the security, that is Rs. 25,000.

Section 529A: Overriding preferential payment

(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 debts.

(2) The debts payable under clause (a) and clause (b) of subsection (1) shall be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions.

Section 530 :

(1) In a winding up [subject to the provisions of section 529A, there shall be paid] in priority to all other debts-

(a) all revenues taxes, cesses and rates due from the company to the Central or a State Government or to a local authority at the relevant date as defined in clause (c) of sub-section (8), and having become due and payable within the twelve months next before that date;

(b) all wages or salary (including wages payable for time or piece work and salary earned wholly or in part by way of commission) of any employee, in respect of services rendered to the company and due for a period not exceeding four months within the twelve months next before the relevant date subject to the limit specified in sub-section (2);

(c) all accrued holiday remuneration becoming payable to any employee, or in the case of his death to any other person in his right, on the termination of his employment before, or by the effect of, the winding up order or resolution;

(d) unless the company is being wound up voluntarily merely for the purposes of reconstruction or of amalgamation with another company, all amounts due, in respect of contributions payable during the twelve months next before the relevant date, by the company as the employer of any persons, under the Employees' State Insurance Act, 1948 (34 of 1948), or any other law for the time being in force;

(e) unless the company is being wound up voluntarily merely for the purposes of reconstruction or of amalgamation with another company, or unless the company has, at the commencement of the winding up, under such a contract with insurers as is mentioned in section 14 of the Workmen's Compensation Act, 1923 (8 of 1923), rights capable of being transferred to and vested in the workman, all amounts due in respect of any compensation or liability for compensation under the said Act in respect of the death or disablement of any employee of the company;

(f) all sums due to any employee from a provident fund, a pension fund, a

gratuity fund or any other fund for the welfare of the employees maintained by the company; and

(g) the expenses of any investigation held in pursuance of section 235 or 237, in so far as they are payable by the company.

(2) The sum to which priority is to be given under clause (b) of sub-section (1), shall not, in the case of any one claimant, exceed such sum as may be notified by the Central Government in the Official Gazette.

(3) Where any compensation under the Workmen's Compensation Act, 1923 (8 of 1923), is a weekly payment, the amount due in respect thereof shall, for the purposes of clause (e) of sub-section (1), be taken to be the amount of the lump sum for which the weekly payment could, if redeemable, be redeemed if the employer made an application for that purpose under the said Act.

(4) Where any payment has been made to any employee of a company,-

(i) on account of wages or salary; or

(ii) to him, or in the case of his death, to any other person in his right, on account of accrued holiday remuneration,

out of money advanced by some person for that purpose, the person by whom the money was advanced shall, in a winding up, have a right of priority in respect of the money so advanced and paid, up to the amount by which the sum in respect of which the employee or other person in his right would have been entitled to priority in the winding up has been diminished by reason of the payment having been made.

(5) The foregoing debts shall-

(a) rank equally among themselves and be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions; and

(b) so far as the assets of the company available for payment of general creditors are insufficient to meet them, have priority over the claims of holders of debentures under any floating charge created by the company, and be paid accordingly out of any property comprised in or subject to that charge.

(6) Subject to the retention of such sums as may be necessary for the costs and expenses of the winding up, the foregoing debts shall be discharged forthwith so far as the assets are sufficient to meet them, and in the case of the debts to which priority is given by clause (d) of sub-section (1), formal proof thereof shall not be required except in so far as may be otherwise prescribed.

(7) In the event of a landlord or other person distaining or having distrained on any goods or effects of the company within three months next before the date of a winding up order, the debts to which priority is given by this section shall be a first charge on the goods or effect so distrained on, or the proceeds of the sale

thereof:

Provided that, in respect of any money paid under any such charge, the landlord or other person shall have the same rights of priority as the person to whom the payment is made.

(8) For the purposes of this section-

(a) any remuneration in respect of a period of holiday or of absence from work through sickness or other good cause shall be deemed to be wages in respect of services rendered to the company during that period;

(b) the expression "accrued holiday remuneration" includes, in relation to any person, all sums which, by virtue either of his contract of employment or of any enactment (including any order made or direction given under any enactment), are payable on account of the remuneration which would, in the ordinary course, have become payable to him in respect of a period of holiday, had his employment with the company continued until he became entitled to be allowed the holiday;

(bb) the expression "employees" does not include a workman; and]

(c) the expression "the relevant date" means-

(i) in the case of a company ordered to be wound up compulsorily, the date of the appointment (or first appointment) of a provisional liquidator, or if no such appointment was made, the date of the winding up order, unless in either case the company had commenced to be wound up voluntarily before that date; and

(ii) in any case where sub-clause (i) does not apply, the date of the passing of the resolution for the voluntary winding up of the company.

(9) This section shall not apply in the case of a winding up where the date referred to in sub-section (5) of section 230 of the Indian Companies Act, 1913 (7 of 1913), occurred before the commencement of this Act, and in such a case, the provisions relating to preferential payments which would have applied if this Act had not been passed, shall be deemed to remain in full force."

7. Rules 156 and 179 of the Rules provide for payment of interest. While Rule 156 pertains to pre-winding up period, Rule 179 relates to post-winding up period. The said Rules read as under:

"Rule 156 : Interest : On any debt or certain sum payable at a certain time or otherwise, whereon interest is not reserved or agreed for, and which is overdue at the date of the winding-up order, or the resolution as the case may be, the creditor may prove for interest at a rate not exceeding four per cent per annum up to that date from the time when the debt or sum was payable, if the debt or sum is payable by virtue of a written instrument at a certain time, and if payable otherwise, then from the time when a demand in writing has been made, giving notice that interest will be claimed from the date of demand until the time of

payment.

Rule 179 : Payment of subsequent interest : In the event of there being a surplus after payment in full of all the claims admitted to proof, creditors whose proofs have been admitted shall be paid interest from the date of the winding up order or of the resolution as the case may be, upto the date of the declaration of the final dividend, at a rate not exceeding 4 per cent per annum, on the admitted amount of the claim, after adjusting against the said amount the dividends declared as on the date of the declaration of each dividend."

In fact, in the present case, Rule 179 of the Rules constituted the basis for the Official Liquidator to deny the contractual rate of interest for post winding up period.

Relevant provisions under the Insolvency Act;

8. Section 28 of the Insolvency Act deals with the effect of an order of adjudication and speaks of vesting of the property of the insolvent in the court or in the receiver. The said provision reads as under :

Sections 28 : Effect of an order of adjudication:

(1) On the making of an order of adjudication, the insolvent shall aid to the utmost of his power in the realisation of his property and the distribution of the proceeds among his creditors.

(2) On the making of an order of adjudication, the whole of the property of the insolvent shall vest in the Court or in a receiver as hereinafter provided, and shall become divisible among the creditors, and thereafter, "except as provided by this Act, no creditor to whom the insolvent is indebted in respect of any debt provable under this Act shall during the pendency of the insolvency proceedings have any remedy against the property of the insolvent in respect of the debt, or commence any suit or other legal proceeding, except with the leave of the Court and on such terms as the Court may impose.

(3) For the purposes of sub-section (2), all goods being at the date of the presentation of the petition on which the order is made, in the possession, order or disposition of the insolvent in his trade or business, by the consent and permission of the true owner, under such circumstances that he is the reputed owner thereof, shall be deemed to be the property of the insolvent.

(4) All property which is acquired by or devolves on the insolvent after the date of an order of adjudication and before his discharge shall forthwith vest in the Court or receiver, and the provisions of sub-section (2) shall apply in respect thereof.

(5) The property of the insolvent for the purposes of this section shall not include any property (not being books of account) which is exempted by the Code of Civil Procedure, 1908 (5 of 1908), or by any other enactment for the time being in force from liability to attachment and sale in execution of a decree.

(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.

(7) An order of adjudication shall relate back to, and take effect from the date of the presentation of the petition on which it is made.

Section 47 of the Insolvency Act dealing with Secured creditors reads as under:

Secured creditors:

(1) Where a secured creditor realises his security, he may prove for the balance due to him, after deducting the net amount realised.

(2) Where a secured creditor relinquishes his security for the general benefit of the creditors, he may prove for his whole debt.

(3) Where a secured creditor does not either realise or relinquish his security, he shall, before being entitled to have his debt entered in the schedule, state in his proof the particulars of his security, and the value at which he assesses it, and shall be entitled to receive a dividend only in respect of the balance due to him after deducting the value so assessed.

(4) Where a security is so valued, the Court may at any time before realisation redeem it on payment to the creditor of the assessed value.

(5) Where a creditor, after having valued his security, subsequently realises it, the net amount realised shall be substituted for the amount of any valuation previously made by the creditor, and shall be treated in all respects as an amended valuation made by the creditor.

(6) Where a secured creditor does not comply with the provisions of this section, he shall be excluded from all shares in any dividend.

9. Section 48 of the Insolvency Act deals with interest. The said provision reads as under:

Interest: (1) On any debt or sum certain whereon interest is not reserved or agreed for, and which is overdue when the debtor is adjudged an insolvent, and which is provable under this Act, the creditor may pray for interest at a rate not exceeding six per centum per annum -

(a) if the debt or sum is payable by virtue of a written instrument at a certain time, from the time when such debt or sum was payable to the date of such adjudication; or

(b) if the debt or sum is payable otherwise, from the time when a demand in writing has been made giving the debtor notice that interest will be claimed from the date of the demand until the time of payment to the date of such adjudication.

(2) Where a debt which has been proved under this Act includes interest or any pecuniary consideration in lieu of interest, the interest or consideration shall, for the purposes of dividend, be calculated at a rate not exceeding six per centum per annum, without prejudice to the right of a creditor to receive out of the debtor's estate any higher rate of interest to which he may be entitled after all the debts proved have been paid in full.

Section 61 of the Insolvency Act deals with priority of debts. This provision reads as under :

Priority of debts:

(1) In the distribution of the property of the insolvent, there shall be paid in priority to all other debts -

(a) all debts due to the Government or to any local authority; and

(b) all salary or wages, not exceeding twenty rupees in all, of any clerk, servant or labourer in respect of services rendered to the insolvent during four months before the date of the presentation of the petition.

(2) The debts specified in sub-section (1) shall rank equally between themselves, and shall be paid in full, unless the property of the insolvent is insufficient to meet them, in which case they shall abate in equal proportions between themselves.

(3) Subject to the retention of such sums as may be necessary for the expenses of administration or otherwise, the debts specified in sub-section (1) shall be discharged forthwith in so far as the property of the insolvent is sufficient to meet them.

(4) In the case of partners, the partnership property shall be applicable in the first instance in payment of the partnership debts, and the separate property of each partner shall be applicable in the first instance in payment of his separate debts. Where there is a surplus of the separate property of the partners, it shall be dealt with as part of the partnership property; and where there is a surplus of the partnership property, it shall be dealt with as part of the respective separate property in proportion to the rights and interests of each partner in the partnership property.

(5) Subject to the provisions of this Act, all debts entered in the schedule shall be paid rateably according to the amounts of such debts respectively and without any preference.

(6) Where there is any surplus after payment of the foregoing debts, it shall be applied in payment of interest from the date on which the debtor is adjudged an insolvent at the rate of six per centum per annum on all debts entered in the schedule.

Under Section 67 of the Insolvency Act, the insolvent is entitled to surplus after

payment in full of his creditors with interest as provided under the said Act.

D. Analysis:

10. Let me now analyse the above noted statutory provisions. Subsection (1) of Section 529 of the Act adumbrated by incorporation Insolvency Rules in relation to winding up of a company qua the debts provable, the valuation of annuities and future and contingent liabilities and the respective rights of secured and unsecured creditors. Section 529 was first amended incorporating what now appears to be the second proviso by the Companies (Amendment) Act 1960. This proviso is not of much significance as it pertains to payment of expenses incurred by liquidator for preservation of security. However, by the Companies (Amendment) Act 1985 (Act 35 of 1985), Section 529-A has been introduced which provided for overriding preferential payments to workmen's dues and debts due to secured creditors. In tune with the said provision, the first proviso was added to Section 529 of the Act. As could be seen from the statement of objects and reasons of Act 35 of 1985, these changes were brought out for protecting the workmen's interests in case of winding up of an insolvent company. The main object behind these amendments is mainly to ensure recovery of workmen's dues by treating them on par with the dues of the secured creditors. Under the proviso introduced to Section 529 by the said Amendment Act, the secured creditors' dues are made subject to *pari passu* charge in favour of the workmen to the extent of the workmen's portion of dues and where a secured creditor, instead of relinquishing his security and proving his debt, opts to realise the security, under clause (a) of the said proviso, the liquidator shall represent the workmen and enforce the statutory charge over the workmen's dues; under clause (b), the amount realised by enforcement of charge by the secured creditor shall be applied rateably for discharge of workmen's dues; and under clause (c), where the debt of the secured creditor could not be realised in full by sale of the charged property of the company in liquidation, the balance amount due to such secured creditor or the amount of workmen's portion in his security, whichever is less, shall rank *pari passu* with the workmen's dues for the purposes of Section 529-A. Sub-section (2) of Section 529 of the Act envisages that in case where the secured creditor could not realise all his dues by enforcing the security, i.e., where the security was not enough to recover all the dues of the secured creditor, all other creditors would be entitled to prove for and receive dividend out of the assets of the company by making their claims. Sub-section (3) of Section 529 defined "workmen", "workmen's dues" and "workmen's portion". This provision also contains an illustration as to how to workout the workmen's dues vis-à-vis the security of a secured creditor.

11. Under sub-section (1) of Section 529-A of the Act, workmen's dues and the debts due to the secured creditors which could not be realised through enforcement of security and whichever is less as per clause (c) of the proviso to sub-section (1) of Section 529 of the Act, apart from being treated as *pari passu*

with each other, shall be paid in priority to all other debts. Sub-section (2) of Section 529-A of the Act is very significant. It provides that the workmen's dues and the debts due to secured creditors shall be paid in full, unless the assets are insufficient to meet them, in which case, they shall abate in equal proportions. Under Section 530 of the Act, certain debts due to Central or State Governments, local authority etc., are treated as preferential payments, however, subject to the provisions of Section 529-A of the Act.

12. A careful analysis of Sections 529, 529-A and 530 of the Act would reveal that these provisions constitute a self-contained scheme. Indeed, the significance of sub-section (1) of Section 529 which made the provisions of the Insolvency Act applicable to the winding up proceedings is reduced substantially with the incorporation of these provisions. This is because, in these provisions, the spirit of the provisions of the Insolvency Act is imbibed in the matter of distribution of the proceeds realised by the sale of the assets of the company in liquidation qua the secured debts and workmen's dues. The need for secured creditor to invoke the provisions of the Insolvency Act would arise if the debt of the secured creditor is not fully covered by the security he holds. Under these provisions, the dues of the secured creditor and the dues of the workmen of the company in liquidation are made to stand on par with each other. As per sub-section (2) of Section 529-A, the debts payable to these categories shall be paid in full. The phrase "paid in full" undoubtedly presupposes that in case of secured creditors, the debts must include principal and interest payable under the contract and in case of workmen, wages payable to them under the contract of employment, or the statutory provisions in force, as the case may be. Thus, unless the assets of the company in liquidation are insufficient to meet the dues payable to these two categories, they shall be paid in full. In case the amount realised by sale of the charged property is insufficient to satisfy the debts of the secured creditors and the workmen's dues, such balance amounts, not exceeding workmen's portion in the secured debtor's security shall be treated as priority debts under sub-section (1) of Section 529-A and in such case, these debts shall be paid before considering the claims of other creditors. It is only after making payment of these debts in full, if any further amounts remain, that the creditors included under Section 530 shall have preference for payment. If any further amount still remains, the unsecured creditors who include the secured creditors are entitled to, to the extent of the portions of their unsecured debt, payment of dividends subject to proof of their debt by applying the provisions of the Insolvency Act.

13. Coming to the provisions of the Insolvency Act, Section 28 vests the whole of the property of the insolvent in the Court or in a receiver, as the case may be, consequent on adjudication of the debtor as an insolvent. It also bars a debtor whose debt is provable under the Insolvency Act to avail any remedy against the property of the insolvent during the pendency of the insolvency proceedings. However, subsection (6) exempts secured creditors from the said bar 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 Section 28 is not in existence. Section 47 of

the Insolvency Act deals with "secured creditor". It envisages three contingencies in relation to the security of a secured creditor. First, where the secured creditor realises his security and his proving for the balance debt due to him after deducting the net amount realised; second, where the secured creditor relinquishes his security for the general benefit of the creditors and his proving his whole debt; and third, where the secured creditor does not either realise or relinquish his security. Under the first contingency, the need for a secured creditor to prove his debt arises only in case of debt which remains balance after realising his security. Under the second contingency, the secured creditor needs to prove his entire debt in case of his relinquishing his security for the general benefit of the creditors. Under the third contingency, without either realising or relinquishing his security, the secured creditor may approach the court or the receiver, as the case may be, by furnishing proof of particulars of his security and the value on which he assesses his security. Under this contingency, it is only the balance amount in excess of the value of the security that will be included in the Schedule. The provisions of Section 48 of the Insolvency Act, which deal with interest, have to be understood in the light of Section 28 and Section 47 thereof, in respect of which interest is not reserved or agreed for. Under the said provision, if the debt or sum is payable by virtue of a written instrument at a certain time, interest is payable from the time when such debt or sum was payable to the date of such adjudication. If the debt or sum is payable otherwise, from the time when a demand in writing has been made giving the debtor notice that interest will be claimed from the date of demand until the time of payment to the date of such adjudication. In either case, the maximum interest prescribed is 6% per annum.

14. Rule 179 of the Rules placed a ceiling on payment of interest @ 4% per annum. There is an apparent conflict between Section 48 of the Insolvency Act and Rule 179 of the Rules as regards the rate of interest. We are, however, not concerned with this aspect in this case because neither of these provisions has any relevance to the case on hand, in that, both the provisions apply in respect of debts which are provable/proved under the Insolvency Act. The provisions of the Section 47 of the Insolvency Act make it clear beyond any cavil of doubt that the value of the secured asset, unless the secured creditor relinquishes his security, does not fall within the category of debts to be proved. Even in cases of third contingency referred to above, namely, where the secured creditor does not either realise or relinquish his security, it is only the balance of the amount due to him in excess of the value of the security that will form part of the provable debt and be entered in the Schedule. This necessarily means that by mere submission of his proof of debt before the court or receiver in cases of debt under the Insolvency Act and before the liquidator in case of winding up of a company under the Companies Act, it cannot be said that a secured creditor has submitted himself to the jurisdiction of the court or receiver or the liquidator, as the case may be. In so far as his security value is concerned, he is still deemed to stand outside the insolvency/winding up proceedings to the extent of his

security interest. The debt to that extent is not a provable debt. It is only the amount remaining as balance after recovering the debt covered by the security that becomes a provable debt, which falls under the provisions of Section 48 of the Insolvency Act or under Rule 179 of the Rules. My view of this stands fully fortified by the Judgment in a strikingly similar case to the one on hand in K.V. Lakshminarayana Sastry Vs. Vijaya Commercial Bank Ltd. and Others, , wherein, Kumarayya, J., made a lucid exposition of the whole concept. It must be mentioned that when the said Judgment was rendered amendments to Section 529 and Section 529-A of the Act were not incorporated. It must also be mentioned that the Judgment has not noticed Rule 179 of the Rules which was presumably in existence when the Judgment was rendered. With these caveats, let me narrate the facts of the said case briefly :

15. One Vijaya Bank Limited was under liquidation by the order of this Court. One Mullapudi Thimmaraju, a secured creditor (for convenience "the secured creditor"), has filed his claim before the Official Liquidator, and so have the other creditors. The other creditors have disputed the legality and validity of "floating charge" claimed by the secured creditor and consequently his status as a secured creditor. The Official Liquidator moved this Court for an order to adjudicate upon the claim of the said secured creditor. Viswanatha Sastri, J., upheld the claim of the secured creditor for Rs. 2 lakhs and held that out of the sum of Rs. 2 lakhs claimed by him, he is entitled to a charge only to the extent of Rs. 46,000/- with subsequent interest @ 5% per annum and that in relation to the balance sum of Rs. 1,53,000/-, he would rank only as an unsecured creditor. Subsequently, the Official Liquidator has adjudicated the claims. As there was a serious dispute as to the entitlement of the secured creditor for interest at the contractual rate post winding up period, the Official Liquidator has applied for directions of this Court. In the light of those facts, the learned Judge framed the following question:

"The only question for determination is whether a secured creditor is entitled to interest subsequent to the date of order of winding up of the Bank, which is January 19, 1954".

16. Though Section 529 of the Act making the provisions of the Insolvency Act applicable to winding up proceedings existed when this Court has decided the case in Lakshminarayana Sastry (1-supra), the learned Judge has fallen back upon the provisions of Section 229 of the Indian Companies Act, 1913 (Act VII of 1913) which in its content, if not in form, are similar to sub-section (1) of Section 529 of the Act. The learned Judge held that on the clear language of the said Section, the provisions of Insolvency Act were applicable. On an analysis of the provisions of Section 28 and Section 47 of the Insolvency Act, the learned Judge allowed the claim of interest at the contractual rate. The ratio of the said Judgment can be summarised as under :

(i) Sub-section (6) is an exception to sub-section (2) of Section 28 of the Insolvency Act and therefore the secured creditor stands outside the bankruptcy (insolvency proceedings).

(ii) So long as the secured creditor does not choose to come in by adopting one of the courses in Section 47 of the Insolvency Act, he stands outside the Insolvency Act; till then he can neither claim any benefit nor suffer from any disadvantage under the Insolvency Act.

(iii) He will neither be entitled to any share in the dividend under Section 47(6) nor he will be subjected to the baneful effect of Section 44(2).

(iv) A secured creditor's rights under the contract are safe so long as the security is sufficient to meet his full demand.

(v) If there is any deficiency, unless he comes in and proves his claim for the balance, he may not get anything.

(vi) The secured creditor hardly comes in under bankruptcy when the security is sufficient to pay his claim in full.

(vii) Whether or not the secured creditor has exercised his option to come in depends upon the question whether or not his case falls within any of the first three sub-clauses of Section 47 i.e., (i) he may realise the security and then prove for the balance; (ii) he may relinquish his security and prove for the whole debt and (iii) if he does not adopt any of the two above courses, he may state in his proof the particulars of the security and the value on which he assesses it and prove for the balance after deducting the assessed value.

(viii) By accepting some payment from the Official Liquidator in part payment of his security, the secured creditor cannot be deemed to have forfeited his right as a secured creditor to rely on his security for payment of the balance. He will yet remain outside the insolvency as contemplated by Section 28(6).

(ix) Under Section 47, a secured creditor may prove for the deficiency after realisation of security or relinquish the whole of the security and prove for the entire debt as any unsecured creditor or value the security and prove for the balance. In the last mentioned case, the security so valued will be governed by the provisions of sub-sections (4) and (5) of Section 47 of the Insolvency Act.

(x) Unless the secured creditor steps into the insolvency proceedings seeking to prove a part or whole of his debt, whether due under principal or interest, or both, he will not be governed by the provisions of the Insolvency Act like any unsecured creditor.

(xi) If security is insufficient to meet his full demand, the respondent must be content with the amount realised to the extent of the value of his security.

(xii) Section 48 must be construed along with Sections 35, 61 and 67 and so construed where surplus is available the debt is payable "in full" which means principal and also interest at contractual rate.

E. Summation of legal position;

17. On the analysis of the provisions of the Companies Act and the Insolvency

Act, the law can be summed up as under:

18. A secured creditor is unaffected by the winding up proceedings to the extent of his security interest unless he has relinquished his security and chosen to prove his debt like any other unsecured creditors; that mere participation before the Official Liquidator by making a claim does not amount to relinquishment of his security interest and his coming under the winding up proceedings; so long as he has not relinquished his security interest, he is still deemed to be standing outside the winding up proceedings to recover his security interest; If the amount realised from the sale of security is sufficient to satisfy his debt subject to the payment of workmen's dues, he is entitled to payment of debt in full, which includes interest at contractual rate even for post winding up period and, however, if the amounts realised by the sale of assets of the company in liquidation are not sufficient to satisfy the secured debt (subject to the provisions of Sections 529 and 529-A of the Act) he will stand on par with the unsecured creditors for realising his balance principal amount or interest as the case may be. Rules 156 and 179 placing ceiling of 4% interest apply to the claims relating to unsecured debts which require to be proved by the creditors, secured or otherwise.

19. This view of mine also derives support from the Judgment of Ramesh Ranganathan.J in M/s. Crips Laboratories Ltd. (In liquidation) Company Application No. 14578 of 2007, dt. 2-5-2008. In that case, the company in liquidation availed a loan of Rs. 160 lakhs from State Bank of India (SBI) against mortgage of immovable properties comprising land and buildings. The charge was registered with the Registrar of Companies. The company in liquidation failed to repay the debt due to the SBI. The SBI filed O.A. before the Debt Recovery Tribunal, Visakhapatnam for recovery of Rs. 1,69,10,978-62 ps. and for interest thereon at 15% per annum compounded quarterly from the date of application till realisation by sale of immovable properties of the company in liquidation. Industrial Development Bank of India (IDBI) also filed another application before the Debt Recovery Tribunal, Hyderabad against the company in liquidation and also other guarantors. The SBI was impleaded as defendant No. 6. The Debt Recovery Tribunal, Hyderabad allowed the application filed by the IDBI subject to the rights of the SBI. At this stage, the Official Liquidator filed an application before this Court seeking its permission to declare 100% dividend to the secured/preferential creditors and 86.50% dividend to the unsecured creditors of the company in liquidation whose claims have been adjudicated. The Official Liquidator has allowed the claim of the SBI at the contractual rate of interest only upto the date of winding up of the company in liquidation. The SBI pleaded before the Court that it is entitled to receive a sum of Rs. 1,66,84,572-19 ps. at the contractual rate of interest for the post winding up period and that the Official Liquidator has committed an error in not admitting the said claim. It is in this background that this Court allowed the claim of the SBI. Upon analysing the provisions of the Act, the Rules and the Insolvency Act, the learned Judge, placing reliance "on the Judgments in Canara Bank Vs. Official Liquidator, and

State Bank of Patiala Vs. Northland Sugar Complex Ltd., held as under :

"... It is thus evident that a secured creditor, if he intends to claim any amount in addition to the value of the security, is required to first assess the value of the security and to state the value of the security in his proof. The secured creditor is entitled to receive dividend only in respect of the balance due to him after deducting the value of the security as assessed by him. Where the security is insufficient to meet the debt of a secured creditor, Section 47(3) of the Provincial Insolvency Act, 1920, enables him to claim for the balance. Where, however, the security is insufficient to meet the dues of the secured creditor, they would be entitled , under Section 47 of the Provincial Insolvency Act, 1920 to make a claim only for the balance due after application of the sale proceeds of the security in its entirety for repayment of their debt. Section 48 relates to interest where the debt has been proved. As noted above, a secured creditor is entitled to submit proof of his debt only in cases where the security is insufficient to meet their dues in full. Where a secured creditor submits proof of any amount due to them, after adjusting the value of the security, they would then, under Section 48, be entitled to prove for interest at a rate not exceeding 6% per annum. Payment of interest at 6% per annum would arise only where the security, on its realisation, is insufficient to repay the dues of the secured creditor in full i.e., principal plus the contracted rate of interest from the due date till the date of repayment (Canara Bank v. Official Liquidator). The claim of the secured creditors for repayment of their debt is on the strength of their security and they are entitled to realise the interest due to them, in terms of the agreement, from the proceeds realised on the sale of the secured assets. However, such realisation would be subject to the dues of the workmen (SBP v. Northland Sugar Complex). Section 48, which prescribes the rate of interest at 6% per annum, cannot be understood to mean that even where the sale proceeds of the security are more than sufficient to repay the secured creditor's debt in its entirety i.e., principal plus interest at the contracted rate i.e., 15% per annum from the date the debt fell due till the date of repayment, even then S.B.I. would be entitled to claim interest only at 6% per annum under Section 48 of the Provincial Insolvency Act, 1920 or 4% per annum under Rule 179 of the Company (Court) Rules, 1959 from the date of winding up, that too only in case a surplus is available after repaying the principal due to all creditors, both secured and unsecured. It is evident, from a conjoint reading of Section 529(1)(c) of the Companies Act and Sections 47(3) and 48 of the Provincial Insolvency Act, 1920, that in cases where a sum is available, on the sale of the security of which the secured creditor is a charge holder, even after the principal with interest at the contracted rate is paid from the date the debt fell due till the date of winding up, it shall be utilised for payment of the interest due to the secured creditor at the contracted rate from the date of winding up till the date of sale of the assets, subject of course to repayment of the dues of the workmen which rank pari passu with the debt of the secured creditor. It is only if some amount is still available, after such payment, can it be utilised for repayment of the dues of the

secured creditors and, thereafter, if a surplus is still available it may be utilised for payment of interest to the unsecured creditors in accordance with Section 48 of the Provincial Insolvency Act, 1920 or Rule 179 of the Companies Court Rules, 1959, as the case may be. It is only if the sum realised on the sale of the security is insufficient to repay the debt of the secured creditor, consisting of the principal with interest from the due date till the date of sale of the assets, would the secured creditor, after the sum realised on the sale of the security is utilised in its entirety for repayment of their debt, and proportionately towards the workmen's dues, be entitled to claim/prove, along with the other unsecured creditors, for the balance. In such a situation the secured creditor would be treated on par with an unsecured creditor for the balance due to them and, in case of availability of surplus, be entitled for interest, subsequent to the order of winding up, at 6% per annum or 4% per annum, as the case may be."

Sri M. Anil Kumar, learned Counsel for the Official Liquidator, placed reliance on the Judgment of the same learned Judge in A.P. State Financial Corpn. Vs. Magna Hard Tempt Ltd. (In Liquidation), and submitted that the opinion of the learned Judge in this Judgment is in conflict with his Judgment in Crips Laboratories Ltd. (2-supra). To appreciate this submission, the facts in Magna Hard Tempt Ltd. (5-supra) need to be noted. In brief, the facts are that the A.P. State Financial Corporation (APSFC) advanced loan to Magna Hard Tempt Ltd. on mortgage of land and buildings belonging to it. The APSFC and A.P. Industrial Development Corporation (APIDC) held the first charge over the properties of the company in liquidation. With the permission of this Court, the APSFC sold the mortgaged properties and deposited Rs. 50 lakhs realised representing the sale proceeds in a Nationalised Bank (Andhra Bank) on the directions issued by this Court to the effect that the deposit will be subject to further orders of the Court relating to distribution of sale proceeds between the secured creditors and the workmen's dues. The APSFC has filed an application for permission to them to appropriate the sum of Rs. 50 lakhs deposited by them in the Andhra Bank by holding that they are not aware of the dues of the workmen and that the Official Liquidator has not determined the workmen's dues, if any. It was contended on behalf of the APSFC that it was entitled to be paid interest on their outstanding dues at 16% per annum which is the contractual rate of interest for the post winding up period and that Rule 156 (sic: 179) of the Rules, 1959 which restrict payment of interest subsequent to the order of winding-up to 4% per annum is ultra vires the provisions of the Indian Contract Act and liable to be ignored. These contentions were repelled by the learned Judge, who, inter alia, held, at para-12 as under :

"... Therefore, when the assets of the company are sold and the proceeds realised, the debts by way of workmen's dues, and that of the secured creditors, have to be paid in full if the assets are sufficient to meet them, and if they are not sufficient, in equal proportions. Once a winding-up proceeding has commenced, and the Liquidator is put in charge of the assets of the company being wound up, the distribution of the proceeds of the sale of the assets, held at

the instance of the financial institutions coming under the Recovery of Debts Act or of financial corporations coming under the SFC Act, can only be with the association of the Official Liquidator and under the supervision of the Company Court. The right of a financial institution stands restricted by the requirement of the Official Liquidator being associated with it, giving the Company Court the right to ensure that the distribution of the assets in terms of Section 529A of the Companies Act takes place. The right to sell under the SFC Act, or under the Recovery of Debts Act, by a creditor coming within those Acts, and standing outside the winding-up, is different from the distribution of the proceeds on the sale of the security. The distribution, in a case where the debtor is a company in the process of being wound-up, can only be in terms of Section 529A read with Section 529 of the Companies Act. The Liquidator represents the entire body of creditors and also holds a right on behalf of the workers to have a distribution *pari passu* with the secured creditors. Distribution of the sale proceeds under the direction of the Company Court, is the Official Liquidator's responsibility *Rajasthan Financial Corporation and Another Vs. The Official Liquidator and Another*, .

The learned Judge has taken judicial notice of the fact that more often than not, the amounts received by Official Liquidator, on the sale of the assets of the company in liquidation, are insufficient to meet the entire dues of the secured creditors and the workmen, necessitating the amount available being paid to them *pari passu*; that if the total dues payable to a secured creditor increases, then the proportionate amount available for repayment of the dues of the workmen decreases; and that acceptance of the contention of the APSFC would mean that while the secured creditor would be repaid the principal and the contracted rate of interest till the date of realisation, repayment of the dues of the workmen would be restricted only to the principal and they (the secured creditors) would be entitled for interest on their dues, thereby defeating the very purpose of introduction of Section 529-A to treat the workmen's dues on par with the dues of the secured creditors. The Court further held that as the dues payable to the workmen are computed only till the date of order of winding up and the Companies (Court) Rules 1959 disentitles them from claiming interest on such dues except in accordance with Rule 156, permitting the secured creditor to claim interest at the contracted rate till the date of realisation of its dues, would render the very provision under Section 529-A illusory. The learned Judge, while declining the relief claimed by the APSFC for payment of contractual rate of interest for the post winding up period, has, directed the APSFC to set apart the workmen's dues determined by the Official Liquidator at Rs. 8,07,035/-from out of the sum of Rs. 50 lakhs.

20. From the facts narrated in the above Judgment, though it was not specifically stated that "the amounts realised from the sale of the assets of the company in liquidation were not sufficient to satisfy the secured creditors and also the workmen's dues", from the observations of the court that "...more often than not, the amounts received by Official Liquidator, on the sale of the assets of the

company in liquidation, is insufficient to meet the entire dues of the secured creditors and the workmen, necessitating the amount available being paid to them *pari passu*", it is presumable that that was a case where the sale proceeds were not sufficient to discharge the secured debts and also the workmen's dues. Sri L.V.V. Iyer, learned Counsel for the appellant, sought to distinguish this Judgment from Crips Laboratories Ltd. (2-supra) on this basis. Sri M. Anil Kumar, has fairly conceded that in Magna Hard Tempt Ltd. (5-supra) the amount realised from the sale of assets of the company in liquidation were insufficient to satisfy the dues of the secured creditors and workmen in full. Therefore, as a necessary corollary, the amounts have to be apportioned between the secured creditors and the workmen who hold *pari passu* charge along with the secured creditors. From what is noted above, I have no hesitation to hold that the facts in Magna Hard Tempt Ltd. (5-supra) bear no similarity with the facts in Crips Laboratories Ltd. (2-supra) and therefore the question of the learned Judge expressing conflicting views does not arise. While Magna Hard Tempt Ltd. (5-supra) pertains to insufficient sale proceeds and distribution of the same among the secured creditors and the workmen who held *pari passu* charge, Crips Laboratories Ltd. (2-supra) is a case where despite availability of surplus funds, the secured creditor was denied the contractual rate of interest for the post winding up period.

21. While the claim for payment of interest at the contractual rate for the post winding up period is supported by the statutory provisions discussed above, even in equity also a secured creditor is entitled to claim interest at the contractual rate where the amounts realised from the sale of assets are sufficient to discharge the debt of the secured creditors and the workmen's dues. It is not merely iniquitous but also wholly illogical that a secured creditor is denied the contractual rate of interest, for, many of the secured creditors are public institutions which lend tax payers' money. Denial of interest at contractual rate to these public institutions, which are instrumental in establishment of companies, seriously affects public interest as they will not be in a position to plough back the substantial monies disbursed by way of loans into their capital, resulting in crippling of their activities. In the long run, these financial institutions may become a great burden to the State as further State funds need to be pumped in to nurture them.

F. Conclusion:

22. On the analysis as above, I hold that the provisions of Section 48 of the Insolvency Act and Rules 156 and 179 of the Companies (Court) Rules, 1959 do not apply to the secured creditors who did not relinquish their security interest in cases where the amounts realised by sale of the assets under charge are sufficient to discharge the workmen's dues and debts due to the secured creditors i.e., principal along with contractual rate of interest even for the post winding up period till the date of realisation of the debt.

G. Result:

23. From the report of the Official Liquidator, it is quite evident that the amount claimed by the appellant at the contractual rate of interest is less than the surplus amount available with him even after allowing all the admissible claims of the workmen and other creditors. Therefore, the Official Liquidator is directed to pay to the appellant interest at the contractual rate i.e., 9.50 % per annum, on the principal amount adjudicated by him from 22-4-1988 i.e., the date on which the company was ordered to be wound up till date within one month from the date of receipt of this order.

24. The Company Appeal is accordingly allowed.