

(2009) 09 DEL CK 0444

In the Delhi High Court

Case No : L.P.A. No. 2057 of 2006 and C.M. No. 14710 of 2006

Wholesome Bites P. Ltd.

APPELLANT

Vs

State Industrial Corpn. of Maharashtra Ltd.

RESPONDENT

Date of Decision : 10-09-2009

Acts Referred:

Civil Procedure Code, 1908 (CPC) — Order 21 Rule 72A, Order 21 Rule 72A(2), Order 21 Rule 72A(5), Order 21 Rule 72A(6), Order 21 Rule 74A
Companies Act, 1956 — Section 529
Constitution of India, 1950 — Article 226
Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Rules, 2004 — Rule 8
State Financial Corporations Act, 1951 — Section 29

Citation : (2009) ILR Delhi 296 Supp

Hon'ble Judges : Vikramajit Sen, J;V.K. Jain, J

Bench : Division Bench

Advocate : P.V. Kapur, Abhinit Das and Chetna Gulati, for the Appellant; Ashwani Mata and Chinmay Pradip Sharma, for the Respondent

Final Decision : Dismissed

Judgement

Vikramajit Sen, J.—By this Appeal the Order dated 22.8.2006 passed by the learned Writ Judge has been assailed before us. The Court had rejected the Appellant's challenge to the sale by auction of the assets of the Appellant Company. There are two elements which come into play wherever the legitimacy of a Court auction is under scrutiny. On the one hand the auction must be expeditiously executed. The reality is that more often than not parties within the trade are not interested in making a bid because of the endemic delays and obstacles that are encountered in jural sales. This runs counter to the expectation that the Company Judge should endeavour to revive the Company whose fortunes are flagging; that winding-up proceedings should not be fatal to the existence of the Company. If that is so, and the troubles of the Company facing liquidation are a result of inept management, it would be in the general interests, and especially of the work force, to locate a party desirous of

rejuvenating and continuing the business of the wounded industrial unit. Experience, however, indicates that persons participating in Company Court auctions are more often than not "scrap dealers" whose objective is to dismember the unit and sell its sundry assets for profit. This trend needs to be reversed, and this is possible only if the Court ensures a quick transfer of the Company. Very seldom do the promoters of a sick company have such intentions; on the contrary their efforts are to protract proceedings in order to retain control of the assets. Having said this much, it is equally imperative that the Company Court should be alive to the possibility of the assets being sold at unreal prices because of machinations of some elements. Financial institutions who are creditors of legal entities (incorporated companies) whose liability is limited, adequately cover their possible losses by insisting on personal guarantees of the Promoters/Directors. Therefore, Courts have had to walk the tightrope adeptly and cautiously. Precedents on the subject bear witness to jural efforts to bring about a balance between these competing interests.

2. The facts of the case, in brief, are that the Appellant had been sanctioned by way of a term loan a total sum of Rupees 365 lacs from the State Industrial Corporation of Maharashtra Limited ["SIDCOM" for brevity], out of which Rupees 350 lacs was borrowed. The Appellant was unable to liquidate the loan and the Respondent put the assets of the Company to auction, exercising powers u/s 29 of the State Financial Corporation Act, 1951 ("SFC Act" for short). This sale by the Respondent had been assailed before the Writ Court on the grounds that the Respondent had firstly not fixed a Reserve Price for the sale; secondly, it had not carried out wide and adequate publicity; thirdly, its advertisement was defective in that it was too small with inadequate coverage and lastly that details of the assets had not been mentioned along with the Reserve Price in the advertisement.

3. On behalf of the Appellant reliance has been placed by Mr. P.V. Kapur, learned Senior Counsel, on Union Bank of India Vs. Official Liquidator H.C. of Calcutta and Others, The penultimate paragraph contains a direction to the Official Liquidator to resell the property after obtaining a fresh Valuation Report from reliable experts, copy whereof was to be given to the secured creditors. The Supreme Court further directed that the Notice should be duly advertised in newspapers circulating in commercial cities, including Delhi, Mumbai and Chennai; and that the Notice should contain the Reserve Price. These directions were passed in the context of Section 529 of the Companies Act, 1956. It is of significance to note that the SFC Act had not been invoked and, therefore, Section 29 thereof did not feature in the considerations. Section 29 empowers a financial corporation, such as the Respondent, to take-over the management or possession or both of indebted and defaulting industrial concerns and transfer by way of lease or sale the property pledged, mortgaged, hypothecated or assigned to the financial corporation. The directions of their Lordships mentioned above will, therefore, not be applicable in their full rigour.

4. Reliance has next been placed on Divya Manufacturing Company (P) Ltd. Vs. Union Bank of India and Others, which was a case under the Companies Act and not under the SFC Act. The Apex Court ordered a fresh sale in the "peculiar circumstances of the case" because the auction that had been held was confined to new bidders only.

5. Allahabad Bank etc. etc. Vs. Bengal Paper Mills Co. Ltd. and Others, has been relied upon for the reason that the sale was held to be improper since the Reserve Price for the sale had not been fixed and that the sale had been advertised only in three newspapers, two of which were local newspapers. What should not be lost sight of is the fact that the Allahabad Bank was the creditor and had not been privy to the auction. Furthermore, the offer of the highest bidder was in variance with the terms and conditions of the sale. The other important distinction is that the case was decided in the context of the Companies Act. We have, however, to consider and apply the provisions of the SFC Act. In the case in hand, the Respondent/Creditor is in favour of sustaining the sale, even though the sale proceeds are not commensurate with the outstandings to be received by the Respondent from the Appellant. Therefore, the fact that the Valuation Report was seen as suspect would in that case not be of any avail to the Appellant.

6. In D.S. Chohan and Anr. v. State Bank of Patiala, (1997) 10 SCC 65 in its Order the Supreme Court had observed that it is mandatory in an auction of mortgaged property in execution of a decree under Order XXI Rule 72A(2) of the Code of Civil Procedure, 1908 ("CPC" for short) that a Reserve Price should have been fixed. Hence, the sale of immovable property was ordered to be started de novo. Section 29 of the SFC Act was not attracted and hence was not considered. We would, however, like to highlight that the provisions of Rule 72A are intended to have very salutary effect. What it ordains is that the mortgagee of immovable property can participate in an auction only with the leave of the Court. It preserves protection to the interests of the mortgagor inasmuch as it prescribes the conditions which must be complied with before the Court can grant permission. These are that the Court must fix a Reserve Price as regards the mortgagee which will not be less than the amount then due for principal, interest and the costs in respect of the mortgage. At the threshold of this Judgment our endeavour had been to focus on the fact that liability is not limited even in respect of dues of incorporated companies because personal guarantees of the Promoters/Directors are asked for in the normal course of loan transactions. Theoretically, this enables the creditors of a company to be nonchalant in recovering the best price for sale of the assets, since rights to proceed under the personal guarantees remain unaffected. Rule 72A(2) removes this possible mischief since it provides that the Reserve Price will not be less than the total dues.

7. Rani Aloka Dudhuria v. Goutam Dudhuria JT 2009(3) SC 629 contains comments similar to the precedents analysed above but in the context of the

Partition Act.

8. Mr. P.V. Kapur, learned Senior Counsel appearing for the Appellant, has also laid great store on the decision in *Bakemans Industries Pvt. Ltd. Vs. New Cawnpore Flour Mills and Others*, and, in particular, to the following paragraphs:

64. If the jurisdiction of a Company Judge is limited, any substantial deviation and departure therefrom would result in unfairness. When an order is passed in total disregard of the mandatory provisions of law, the order itself would be without jurisdiction. In this case, however, even otherwise a fair procedure was not adopted. We, however, very much appreciate the anxiety on the part of the Court to see that otherwise just dues of SICOM be realized. Conduct of a party plays an important role in the matter of grant of a relief. However, only because the conduct of a party was not fair, the same, by itself, cannot be a ground to adopt a procedure which is unjust or unfair, particularly, when by reason thereof, not only the Company itself but also other creditors are seriously prejudiced. We fail to see any reason as to why the hearing of the case was to be preponed. Why even a day's time could not have been granted when a prayer for adjournment was made. The jurisdiction of the Company Court is vast and wide. It can mould its reliefs. It may exercise one jurisdiction or the other. It may grant a variety of reliefs to the parties before it. The parties before the Company Judge are not only the Company or the creditors who had initiated the proceedings but also others who have something to do therewith. Even in a given case a larger public interest may have to be kept in mind. The court may direct winding up. It may prepare a scheme for its restructuring.

65. We, therefore, are of the opinion that the Company Judge was not correct in its view and passed the impugned judgments only having regard to the wrongful conduct on the part of the appellant in obtaining an award from the conciliation tribunal or failure to bring a better offer from another bidder. What should not be ignored, however, are the observations that the proceedings u/s 29 of the SFC Act prevail over winding up proceedings before a Company Judge and that proceedings in *Bakemans* were under the Companies Act and not in terms of Section 29 of the SFC Act. It cannot be over-emphasised that in the case in hand the Respondent/State Financial Corporation has exercised powers u/s 29 of the SFC Act, unlike in *Bakemans* where the Respondent Company had waived its rights and had submitted to the jurisdiction of the Company Judge. The Court was of the view that the auction sale had been held in an undue haste. It disapproved the conduct on the part of *BAKEMANS* in obtaining an Award from the Conciliation Tribunal. Furthermore, their Lordships noted that all creditors had not been duly notified. It was in that factual matrix that the Court had ordered a fresh auction.

9. In *Gajraj Jain Vs. State of Bihar and Others*, the Apex Court opined that the first charge-holder must obtain the best possible price, which means fair market value; it should not be seen to protect its own interests at the expense of the subsequent charge-holders; wherever the debtor seeks to enforce its rights u/s

29 of the SFC Act it should ensure that the sale is sufficient, not only for meeting its own dues alone, but also for distributing the surplus sale proceeds amongst other creditors. The State Corporation concerned had accepted down-payment of its own dues and for the outstandings of the Central Bank had procured a promise to pay in the future, which their Lordships found not to be sufficient. In addition, it had been observed that in the absence of a Valuation Report and a Reserve Price an auction sale by invoking Section 29 of the SFC Act was reduced to a mere pretence. Furthermore, the State Corporations were obliged to call for matching offers from the Directors/Guarantors which has been done in the present case but has failed to elicit any response. The decision in *S.J.S. Business Enterprises (P) Ltd. Vs. State of Bihar and Others*, as well as *Haryana Financial Corporation and Another Vs. Jagdamba Oil Mills and Another*, and *Chairman and Managing Director, SIPCOT, and Madras and others Vs. Contromix Pvt. Ltd. by its Director (Finance) Seetharaman, Madras and another*, were reiterated and applied by the Court. The decision was vitally influenced by *Express Newspapers Pvt. Ltd. and Others Vs. Union of India (UOI) and Others*, inasmuch as their Lordships were of the view that the concerned Financial Corporation had misused its authority and power in breach of law by taking into account extraneous matters and ignoring relevant matters.

10. Rule 8 of the Security Interest (Enforcement) Rules, 2002 ("SIE Rules" for short) can be seen as attempting to achieve a purpose similar to Order XXI Rule 74A of the CPC and accordingly militates against the arguments advanced by learned Senior Counsel for the Respondent. Where possession of a secured asset has been taken-over after issuing requisite notice, an immediate responsibility is cast on the custodian to preserve and protect the secured assets and insure them till they are sold or otherwise disposed of. Sub-Rule (5) obliges the authorised officer to obtain a valuation of the property from an approved valuer and in consultation with the secured creditor to fix the Reserve Price of the property. Pursuant thereto, the sale can be effected by four methods. Firstly, by obtaining quotations from persons dealing with similar secured assets or otherwise interested in buying such assets; secondly by inviting tenders from the public; thirdly by holding public auctions and fourthly and lastly by private treaty. At all stages notice to the borrower is an essential and unwavering requirement. The proviso to Sub-rule (6) envisages that in the event of the sale of secured assets through the tender process or by holding public auctions a public notice in two leading newspapers, of which one should be in vernacular language, having sufficient circulation in the locality must be carried out. The Notice must include, not only the description of the immovable property and details of the secured debt, but also the Reserve Price, below which the property may not be sold. The essentials spelt-out in *Gajraj Jain* have, for good reasons, been written into the SIE Rules.

11. Mr. Mata, learned Senior Counsel for the Respondent, has submitted that the amounts due to the Respondent as on 7.2.2003 were to the tune of Rupees 4,86,82,159/- together with interest thereon at 17 per cent per annum with

effect from 1.12.2002 which aggregates approximately Rupees 6.5 crores. The Appellant had been taken-over on 20.6.2006 and the date of auction had been fixed for 3.8.2006. Eleven Bids were rejected and out of the remaining six legally valid Bids the highest had been accepted. This Bid was, in fact, higher than the price projected in the Valuation Reports. On 10.8.2006 the Appellant was granted an opportunity to bring a better offer. A Valuation Report had been duly obtained which assessed the valuation of the plot at Rupees 289 lacs. In stark contrast thereto, the Appellant had assessed the realisable value of the land at Rupees 85 lacs, building at Rupees 65.71 lacs, plant and machinery at Rupees 47.65 lacs and miscellaneous fixed assets at Rupees 0.15 lacs aggregating only Rupees 198.51 lacs. Mr. Mata, learned Senior Counsel for the Respondent, accordingly argues that the auction sale at Rupees 3,65,30,000/- cannot possibly be seen as an inadequate consideration. It is further contended by Mr. Mata that the requirement of fixation of a Reserve Price is envisaged under Order XXI Rule 72A(2) of the CPC and under the Companies Act and not u/s 29 of the SFC Act, which argument is not correct in view of Rule 8 of the SIE Rules.

12. Furthermore, there appears to be no plausible answer to the dicta and the exposition of law laid down in *Gajraj Jain*. The argument of Mr. Mata that wherever the Reserve Price is fixed it has the effect of depressing prices is attractive but would not be sustainable on the basis of the empirical experience. In these circumstances, it would be difficult to sustain the impugned Judgment, even though we have no reason to suspect fairness and genuineness of the auction, as highlighted by Mr. Mata.

13. There is, however, another dimension to the litigation. The Writ Petition came to be filed by the Appellant herein on 21.8.2006 and was dismissed on 22.8.2006. The Appeal was filed on 3.11.2006 with an application for condonation of delay of 27 days. In our view, there is a fatal omission which has occurred on the part of Petitioner/Respondent inasmuch as the auction purchaser has not been impleaded as a party. The Writ Petition had been filed one day prior to the confirmation of the offer as a sequel of which, uncontrovertibly, possession has been handed over to the purchaser. Even if we were to ignore the non-impleadment of the purchaser before the Writ Court because of the dismissal of the Writ in limine, since the purchaser is a necessary party, steps should have been taken for its impleadment before us. We cannot be persuaded to set aside an auction which has been fully implemented, in the absence of the most vitally effected party, namely, the purchaser who has been put in possession. Added to this is our satisfaction that efforts to obtain the best price, which may closely correspond to the prevailing market price, had been carried out. In this regard, we cannot be oblivious of the fact that the Respondent had notified the Appellant of the highest offer in order to give them an opportunity of presenting a yet higher offer. Mr. Kapur contends that the Supreme Court has enunciated that the Promoters/Directors of the debtor company are not obligated to locate a higher offer, which runs counter to the opinion of the Supreme Court in *Gajraj Jain*. What we have before us, therefore, is the punctilious failure to comply with the

procedural safeguards of the law on the one hand, and the setting aside of a sale behind the back of the successful bidder who is already in possession on the other. We are unable to persuade ourselves that the former outweighs the latter. These contentions, we find, are relevant to any Court which is exercising extraordinary powers contained in Article 226 of the Constitution of India.

14. It is in these circumstances that we dismiss the Appeal, as well as the Application, leaving the parties to bear their respective costs.