SUPREME COURT OF INDIA

Industrial Credit and Investment Corporation of India Ltd.

Vs.

Srinivas Agencies

C.A.Nos.5082-85 of 1989

(A.M.Ahmadii, C.J. and B.L.Hansaria J.)

22.02.1996

JUDGMENT

B.L. HANSARIA, J.

1. The extent of right of secured creditors-to realise their debts from the assets of a company which is under winding-up or has been wound up, by approaching for a other than the company court, is required to be spelt out in these appeals. We have also been called upon to decide as to when a pending suit or proceeding relating to realisation of the debts by such a creditor should be transferred to itself by a company court seized with the winding-up proceeding.

2. The foundational premise of the aforesaid points is that it is a settled position by now that a secured creditor stands outside the winding-up proceeding and under the law he can proceed to realise his security without the leave of the winding-up court, if by the time he initiated the action the company has not been wound up. The view has been holding field ever since a three-Judge bench decision of this Court in M.K. Ranganathan v. Government of Madras: [1955]2SCR374 . As this legal position has not been assailed by any of the parties, we need not advert to the reasons which led this Court in Ranganathan's case to hold as above. Despite this being the legal position, there were some provisions in the Indian Companies Act, 1913, which enactment preceded the present Companies Act, 1956 (hereinafter the 'Act') in which also a parallel provision find place, which put some restrictions on the aforesaid power.

3. It would be profitable to note these provisions of the Act at the threshold itself. These are Sections 446 529(1) and (2) 529A and 537, reading as below:

446. (1) When a winding up order has been made or the Official Liquidator has been appointed as provisional liquidator, no suit or other legal proceeding shall be commenced, or if pending at the date of the winding up order, shall be proceeded with, against the company, except by leave of the Court and subject to such terms as the Court may impose.

(2) The Court which is winding up the company shall, notwithstanding anything contained in any other law for the time being in force, have jurisdiction to entertain, or dispose of-

(a) any suit or proceeding by or against the company;

(b) any claim made by or against the company (including claims by or against any of its branches in India);

(c) any application made under Section 391 by or in respect of the company;

(d) any question of priorities or any other question whatsoever, whether of law or fact, which may relate to or arise in course of the winding up of the company;

whether such suit or proceeding has been instituted, or is instituted, or such claim or question has arisen or arises or such application has been made or is made before or after the order for the winding up of the company, or before or after; the commencement of the Companies (Amendment) Act, 1960.

(3) Any suit or proceeding by or against the company which is pending in any Court other than that in which the winding up of the company is proceeding may, notwithstanding anything contained in any other law for the time being in force, be transferred to and disposed of by that Court.

(4) Nothing in Sub-section (1) or Subsection (3) shall apply to any proceeding pending in appeal before the Supreme Court or a High Court. 529. (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 pan 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 portion as the workmen's portion in relation to the security bears to the value of the security.

(3) xxx xxx xxx

529A. (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 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.

537. (1) Where any company is being wound up by or subject to the supervision of the Court-

(a) any attachment, distress or execution put in force, without leave of the Court, against the estate or effects of the company, after the commencement of the winding up; or

(b) any sale held, without leave of the Court, of any of the properties or effects of the company after such commencement;

shall be void.

(2) Nothing in this section applies to any proceedings for the recovery of any tax or impost or any dues payable to the Government.

4. A combined reading of the aforesaid provisions leads to the following results :

(i) A winding-up court has jurisdiction, inter alia, to entertain or dispose of any suit or proceeding by or against the company, even if such suit or proceeding had been instituted before an order for winding-up had been made. This apart, the winding-up court has jurisdiction to transfer such a suit or proceeding to itself and dispose of the same. These follow from Sub-sections (2) and (3) of Section 446.

(ii) When a winding-up order has been made or the official liquidator has been appointed as provisional liquidator, no suit or other legal proceeding, even if pending at the date of the winding-up order, can proceed against the company, except by leaves of the Company Court vide Sub-section (1) of Section 446. (iii) Any sale held, even without the leave of the winding-up court pursuant to order of a civil court on it being approached by a secured creditor to realise its debt will not ipso facto be void, in view of the holding in Ranganathan's case that Section 537, dealing with voidness of sale, operates when the sale is pursuant to attachment of company court. This, however, would be the position where a company has not been wound up, but is in the process of being wound up.

5. None of the parties has assailed the aforesaid propositions of law as well. The real bone of contention is as to when (i) leave of the winding-up court should be granted to a secured creditor to proceed with the suit after an order of winding-up has been made; and (ii) when should a winding-up court transfer to itself any suit or proceeding by or against the company during the pendency of the winding-up proceeding.

6. The aforesaid questions arise because a secured creditor who has initiated a suit or proceeding in a civil court is interested in realisation of his debt only, whereas the company court looks after the interest of all the creditors; so too,' the workmen dues, which rank pari passu with debts due to secured creditors. This is brought home not only by Section 529A, which was inserted by the Companies (Amendment) Act, 1985, t but also by the proviso to Sub-section (1) of Section 529 inserted by the same Amendment Act. The winding-up court does these acts through a liquidator, who has been given wide powers by Section 457 of the Act. As against this, a receiver appointed by a civil court on being approached by secured creditor would basically look after the interest of that creditor, whose interest may in many cases be in conflict with that of liquidator, as was acknowledged in re Karamelli & Barnett, Limited 1917 (1) CH 203, We feel ho difficulty in stating that in case of such conflict, the interest of liquidator has to receive precedence over that of the receiver inasmuch as the former looks after the interest of a large segment of creditors alongwith that of workmen, whereas the latter confines his concern to the interest of the secured creditor on whose approach the receiver had been appointed. This view cannot also be, and has indeed not been , contested by the learned Counsel appearing for the appellants.

7. The real controversy is as to when a winding-up court should get transferred to itself a pending proceeding initiated by secured creditor; and when a winding-up court should grant leave to the secured creditor to pursue his remedy in the civil court, despite winding-up order having been passed. Shri Salve brought to our notice, on the first aspect of the controversy, a decision of two-Judge bench decision of this Court in Central Bank of India v. Elmot Engineering Company: [1994]3SCR766 . It was held therein that the aim of Section 446 is to safeguard the assets of the company against wasteful or expensive litigation as for as matters which could be expeditiously and cheaply decided by the company court. It was also observed that while granting leave under this section the court always takes into consideration whether the company is likely to be exposed to unnecessary litigation and cost.

8. In this context, it would be apposite and useful to note what was stated by a three-Judge bench in Sudarsan Chits (I) Ltd. v. O. Sukumaran Pillai: [1985]1SCR511 , which has traced the historical evolution as well as the present setting of Section 446(2). A need for such a provision was felt because Section 171 of the predecessor Act had only provided for stay of suits and proceedings pending at the commencement of winding-up proceeding, alongwith the embargo against the commencement of any suit or other legal proceedings against the company except by the leave of

the court. That provision, with little modification, was re-enacted in Sub-section (1) of Section 446. There was thus no specific provision conferring jurisdiction to the court winding-up the company analogous to the one conferred by Sub-section (2), which was introduced to enlarge the jurisdiction of the winding-up court so as to facilitate the disposal of winding-up proceedings. This Sub-section, as originally enacted, did not meet with the requirement fully, with the result that the Committee appointed for examining comprehensive amendment to the Companies Act recommended that "a suit by or against a company in winding-up should notwithstanding any provision in law for the time being be instituted in the court in which the winding-up proceedings are pending". The Committee made this recommendation having noticed that on winding-up order being made and the official liquidator being appointed, he has to take into his custody company property as required by Section 456. Then, Section 457 confers power on the liquidator to sell the properties of the company and to realise the assets. The Committee felt that at the stage when winding-up order is made, the company may as well have subsisting claims and to realise these claims the liquidator will have to file suits. TO avoid this eventuality and to keep all incidental proceedings in winding-up before the court, its jurisdiction was required to be enlarged to entertain petition, amongst others, for recovering the claims of the company. To give effect to this recommendation, Sub-section (2) was suitably amended to bring it to its present form by the Companies (Amendment) Act, 1960. The amendment obviated the need filing of suits by the liquidator (which are prolix and expensive) to realise and recover the claims and subsisting debts owned to the company; and instead, provided a cheap and summary remedy by conferring the required jurisdiction on the company court.

9. Shri Salve's entire submission had been that a working principle may be got evolved which would, on the one hand, protect the substantive right of a secured creditor, specially in view of large sums of money being advanced of later of such creditors and, on the other hand, not jeopardise the interest of other secured creditors. According to the learned Counsel, these twin objects can be achieved if the company court were to grant leave wherever required as a rule, subject to reasonable conditions. This would preserve the integrity of the substantive right of the secured creditor. The terms to be imposed which should facilitate, rather than obstruct, the realisation of security. Further, wherever a receiver has been appointed prior to the commencement of the winding-up proceedings, he should be permitted to continue in general run of cases. As to the suits to be filed after the winding-up proceeding has commenced, the learned Counsel urged that such permission should normally he granted by the winding-up court. On this being done, when the question of appointment of receiver would arise, the civil court would do so if a case for same were to be made out after hearing the liquidator, who would be a defendant in the suit. As regards transfer of the pending suit by the company court, the submission was that convenience may not be the guiding factor; the preservation of integrity of the substantive right of the creditor should be the main consideration.

10. To buttress his submissions, Shri Salve has referred us to the Recovery of Debts to Banks and Financial Institutions Act, 1993, which was recently enacted because of the considerable difficulty being experienced by financial institutions in recovering loans and enforcement securities charged with them. Earlier, recovery procedure used to block a significant portion of their funds in unproductive assets, the value of which deteriorates with the passage of time. An urgent need was, therefore, felt for successful implementation of the financial sector reforms, to work out a suitable mechanism through which dues to these institutions could be realised without delay. To achieve this purpose, the aforesaid Act visualises establishment of the Debts Recovery Tribunals by the Central Government, with its own procedure which is speedy in nature. Section 18 of this Act has barred jurisdiction of other courts, except the writ power of the higher courts, in relation to the matters specified in Section 17 the same being recovery of debts due to such institutions.

11. Shri Subba Rao, who appeared for official liquidator in many cases, however, urged that it is the liquidator who can look after the interests of all the secured creditors, and so, his actions should be allowed to prevail over that of the receiver. He submitted that Section 529 of the Act contains many provisions to duly protect the interest of secured creditors. Shri Grover, appearing for some of the respondents, brought to our notice that part of Sub-section (1) of Section 446 which mentions about the grant of leave on "such terms as the Court may impose", which provision, according to learned Counsel, means that the terms have to be reasonable. The underlying idea of this contention is that there cannot be any uniform working principle, and the question whether leave should be granted, if so, on what terms and whether transfer should at all be ordered would depend on the facts and circumstances of each case.

12. We have duly applied out mind to the rival contentions. It is no doubt correct that the interest of the secured creditor, who has taken recourse to an independent proceeding to realise his debt has to be protected; but it is apparent this cannot be done at the cost of other secured creditors. To preserve the integrity of one secured creditor, another secured creditor cannot be discredited - his integrity has to be of equal concern. It may, however, be that in a particular case the secured creditor who has approached the civil court happens to be one who has lent huge amount, or be one who is the main secured creditor. In such a situation, on approach being made by such creditor, we have no doubt that company court would duly take note of this fact and should like to grant leave required by Sub-section (1) of Section 446; and by the same token refuse to transfer the proceeding to his court. This is not to say that in all cases where the proceedings have been initiated by the main secured creditor, the company court would grant leave. Much would depend on the circumstances of each case. But, if the position be that the secured creditor who had approached the civil court is one amongst many similar creditors, it may be that the company court feels that to take care of the interest of other secured creditors, either the relief of leave does not deserve to be granted or that the proceeding is required to be transferred to it for disposal. It may be pointed out that Sections 529 and 529A of the Act do contain provisions in so far as the priority of secured creditor's claim is concerned. Of course, the company court would not transfer the proceeding to it merely because of its convenience ignoring the difficulties which may have to be faced by the secured creditor, who may be at a place far away from the seat of the company court. The need to protect the company from unnecessary litigation and cost have, however, to be borne in mind by the company court.

13. We are, therefore, of the view that the approach to be adopted in this regard by the company court does not deserve to be put in a straight jacket formula. The discretion to be exercised in this regard has to depend on the facts and circumstances of each case. While exercising this power we have no doubt that the company court would also bear in mind the rationale behind the enactment of Recovery of Debts Due to the Banks and Financial Institutions Act, 1993, to which reference has been made above. We make the same observation regarding the terms which a company court should like to impose while granting leave. It need not be stated that the terms to be imposed have to be reasonable, which would, of course, vary from case to case. According to us, such an approach, would maintain the integrity of that secured creditor who had approached the civil court or desires to do so, and would take care of the interest of other secured creditors as well which the company court is duty bound to do. The company court shall also apprise itself about the fact whether dues of workmen are outstanding: if so, extent of the same. It would be seen whether after the assets of the company are allowed to be used to satisfy the debt of the secured creditor, it would be possible to satisfy the workmen's dues pan passu.

14. The appeals and transfer cases stand disposed of with these observations, leaving the company court to pass appropriate orders in the concerned matters in the light of what has been stated by us. No order as to cost.