Form No. J.(2)

IN THE HIGH COURT AT CALCUTTA
Civil Appellate Jurisdiction
Original Side

Present:

The Hon'ble Justice Ashim Kumar Banerjee

And

The Hon'ble Justice Shukla Kabir (Sinha)

A.P.O. No. 469 of 2012
A.P.O. No. 470 of 2012
C.P. NO. 493 of 2011

KOTAK MAHINDRA BANK LTD.
Vs.
EASTERN SPINING MILLS & INDUSTRIES LTD.

For the Appellant	**: Mr. Anindya Kumar Mitra, Senior Advocate** **Mr. Debangshu Basak, Advocate** **Mr. Deep Nath Roy Chowdhury, Advocate** **Mr. Sourav Mukherjee, Advocate**
For the Respondent	**: Mr. S.N. Mookherjee, Senior Advocate** **Mr. Ratnanko Banerjee, Advocate** **Mr. Subhankar Nag, Advocate**
Heard on	: January 15, 16,18 and 22, 2013.
Judgment on	: February 13, 2013.

ASHIM KUMAR BANERJEE.J:

Short question would involve in these appeals as to whether a secured creditor was within its right to maintain a petition for winding up without giving up its security and without pleading that the security they had, would be insufficient to satisfy their claim.

Eastern Spinning Mills and Industries Ltd., a company incorporated under the provisions of the Companies Act, 1956 availed credit facilities from State Bank of India against securities being mortgaged to the bank that would include land assets, plant, machineries and all other fixed assets belonging to the company. One would not dispute if someone would say, the assets that were kept as security, if sold to pay off the bank dues, would amount to complete closure of the business of the company as without land, building, machineries and other fixtures the company would be left hardly with anything to run its day-to-day affairs.

The Company could not pay off the dues of the bank. The bank assigned their claim and/or the right as a secured creditor to M/s Kotak Mahindra Bank Ltd. who stepped into the shoes of the State

Bank of India. Kotak Mahindra Bank initiated recovery proceedings by taking measures under the SARFAESI Act (Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002). They however could not take physical possession of the assets giving rise to protracted litigations that may not be relevant for the present purpose. Fact would remain, they are yet to take possession of the assets. However, Official Liquidator could make an inventory of the assets after great effort.

The Company became sick. Its networth became negative that compelled them to make a reference to the Board of Industrial and Financial Reconstruction (BIFR) under the Sick industrial Companies Act, 1987. BIFR accepted the reference and declared the company, a sick company within the meaning of Section 3(1)(o) of the said Act of 1987. However, at the instance of the Kotak Mahindra, the reference stood resolved without a logical conclusion in view of the provisions of the SARFAESI Act that would not permit the reference to continue once the secured creditor took steps for sale of the assets to realize their dues. Kotak also gave notice to the company under Section 434 of the Companies Act 1956 *inter alia* praying for winding up of the

company in case the company would not meet their dues. The learned Single Judge initially asked the Official Liquidator to make inventory. Official Liquidator did so after a great deal of obstruction referred to above. However, the learned Judge ultimately dismissed the winding up petition by holding it not maintainable in law. The principal reason for dismissal would appear from two paragraphs of the judgment and order that are quoted below:

"It is, thus, the inevitable conclusion from the discussion herein that a secured creditor of a company which has not established the inefficacy or the inadequacy of the security held by it may maintain a petition for winding up the company but such petition, if founded solely on the legal fiction under Section 434(1)(a) of the Act, will not qualify either to be admitted or for any order of winding up to be passed thereon.

Since the petitioning creditor here has neither averred nor otherwise established that the security that it enjoys is inefficacious or inadequate to meet its claim against the company, the petition cannot be admitted. In any event, even if the petitioning creditor had crossed that hurdle and had established that a debt was due which was unmatched by any efficacious security, its conduct in advertising the

statutory notice prior to instituting this petition is a good ground for exercising the limited discretion available to the company court to refuse to admit a creditor's petition even if the debt were unimpeachably established."

Being aggrieved, Kotak filed two appeals, one for dismissal of the winding up and the other for not entertaining the application for provisional liquidator. We heard both the appeals on the abovementioned dates and wish to dispose of by this common judgment pronounced herein.

Mr. Debangshu Basak, learned counsel appearing for the appellant placed the appeal. According to him, as per the balance-sheet the liability towards the secured creditor as on September 30, 2004 was Rs.19 crores as admitted by the company appearing at page-174 of the paper book whereas the amount became Rs.21 crores as on September 30, 2003. Mr. Basak would also contend, the company in the said balance-sheet did not take into account the overdue interest that had accrued in the meantime. He also placed the relevant correspondence including the statutory notice of demand. According

to him, the notice was never replied to. However, the company sought to rely upon a copy of the reply said to have been served upon the company appearing at page-292 of the paper book.

Taking it over from Mr. Basak, the learned Advocate General also appearing for the appellant contended, the company's refusal to pay would itself amount to neglect to pay attracting the jurisdiction of the winding up Court. The learned Advocate General would contend, learned Judge fell in grave error in observing, the creditor was obliged to prove insufficiency of the assets to maintain a petition for winding up. He placed Sections 433, 434 and 439 of the said Act of 1956. According to him, on a combined reading of the said three sections the right of a creditor to maintain a petition for winding up could not be questioned in the absence of a *bona fide* dispute being raised by the company. He referred to paragraph-9 of the affidavit-in-opposition appearing at page-275 of the paper book to say, the company admitted their liability towards the State Bank of India that stood assigned in favour of Kotak. The company was itself a sick company as its networth became negative that would clearly prove the commercial insolvency. According to the learned Advocate

General, the company could not make its networth positive to come out of the mischief of the said Act of 1987. The provisions of SARFAESI Act would be responsible for dropping of the BIFR proceeding. According to him, there was no law that would debar a secured creditor from filing a winding up petition. There would be no law obliging the secured creditor to prove that the secured assets would be insufficient to meet the claim. Once the creditor could prove his status as a creditor having a claim of more than Rs.500/- the winding up petition would be maintainable. It could be resisted by the company by raising a *bona fide* dispute that the present company utterly failed. He cited the decision in the case of **V.V. Krishna Iyer Song Vs. New Era Manufacturing Co. Ltd.** reported in **35 Company Cases page-410** to support his proposition, the balance-sheet would itself prove the commercial insolvency of the company that would maintain the winding up petition. He cited the Madras decision in the case of **Sree Shanmugar Mills Ltd. By Managing Agents Sri Alagai Ltd –Vs S.K. Dharmaraja Nadar & Anr.** reported in **ALL India Reporter 1970 Madras page-203** to support his contention that value of the fixed assets was not at all relevant to maintain a winding up petition. The petition could never be resisted

by the company without a *bona fide* dispute being raised as observed by the Apex Court in the case of **M/s. Madhusudan Gordhandas & Co. Vs. Madhu Woollen Industries Pvt. Ltd.** reported in **1971 Volume-III Supreme Court Cases page-632**.

According to the learned Advocate General, different High Courts including the Calcutta High Court, Madras High Court and Bombay High Court consistently upheld the right of a secured creditor to maintain a winding up petition. He relied on the following decisions on this issue :

1. **All India Reporter 1971 Calcutta page-78 (Calcutta Safe Deposit Co. Ltd. –Vs- Ranjit Mathuradas Sampat)**
2. **174 Company Cases Volume-58 page-22 (Rajiv Tandon & Ors. Vs. Dena Bank & Anr.)**
3. **58 Company Cases page-174 (Bharat Overseas Bank Ltd. Vs. Shree Arcee Steels P. Ltd.)**
4. **All India Reporter 1955 Madras page-582 (Karnatak Vegetable Oils and Refineries Ltd. Vs. Madras Industrial Investment Corporation Ltd.)**

According to him, to maintain a winding up petition by a secured creditor, the security need not be given up as held by the Karnataka High Court in the case of **Hegde & Golay Limited Vs. State Bank of India** reported in **ILR 1987 Karnataka page-2673** and by our Court in the case of **Confin Homes Ltd. Vs. Lloyds Steel Industries** reported in **106 Company Cases page-52**.

Per contra, Mr. Subhankar Nag, learned counsel appearing for the company raised the issue of parallel proceeding. According to Mr. Nag, the secured creditor could opt for winding up proceeding once they would give up their right to proceed with the other proceedings under the SARFAESI Act.

He also referred to the proceeding before the Debt Recovery Tribunal that was initiated by State Bank of India and continued by Kotak upon substitution being made in their favour. He referred to Section 13(13) of the SARFAESI Act to show, that once the secured creditor gave notice for taking possession that would itself put them in symbolic possession having an injunction against the debtor from initiation of any proceeding to forestall such attempt. In the instant

case, Kotak not only took steps to continue with the proceeding before the Debt Recovery Tribunal but also took steps under the SARFAESI Act. The winding up petition was thus rightly not admitted.

Taking it over from Mr. Nag, Mr. Ratnanko Banerjee, learned counsel also appearing for the company contended, winding up being a discretionary remedy the learned Company Judge must take into account all aspects surrounding the said proceeding. According to him, the petition for winding up was nothing but a *mala fide* attempt to malign the company. He referred to the advertisement published in the newspaper. He referred to the pleadings where the appellant claimed, despite receipt of notice the company did not reply to the notice of demand. Hence, there was no occasion for the appellant to publish the statutory notice of demand in the newspaper. He referred to Section 434 (1)(a) and Section 433 (e) and (f) to contend, the claim must be an admitted one that would require a winding up petition to be admitted. He also referred to the parallel proceedings and contended, the same was contrary to each other. It was nothing but an attempt to put pressure upon the company to accede to the

unreasonable demand of the respondent. According to him, the claim was a disputed one. He was however unable to highlight the dispute on merits. He would contend, winding up petition was not maintainable by a secured creditor. In this regard he cited the Apex Court decision in the case of **National Conduits (P) Ltd. Vs. S.S. Arora** reported in **1968 Volume-I Supreme Court Cases page-430**. He lastly contended, once the appellant initiated proceeding under SARFAESI Act to realize its own dues the winding up petition being a representative action would no longer be maintainable at its instance.

Further taking it over from Mr. Banerjee, Mr. S.N. Mookherjee, learned senior counsel also appearing for the respondent placed reliance on the decision in the case of **V.V. Krishna Iyer** (supra) cited by the learned Advocate General. According to him, since the appellant did not have any interest in the company, it was not entitled to maintain the petition. He referred to decision in the case of **Davco Products Ltd. Vs. Rameswarlal Sadhani & Ors.** reported in **ALL India Reporter 1954 Calcutta page-195**.

Distinguishing the decision in the case of **Shanmugar Mills Ltd** (supra) cited by the learned Advocate General, he referred to paragraph-3 of the report to say, land, machinery and other assets should be taken note of as security. According to him, the Madras High Court decision would be contrary to the decision in the case of **V.V. Krishna Iyer** (supra).

According to Mr. Mookherjee, the appellants must restrict themselves on the issue raised before the Single Bench. They maintained their winding up petition before the learned Single Judge only on the issue of deemed insolvency relying on the notice issued under Section 434 (1)(a). Hence, they would not be entitled to urge the issue of the commercial insolvency at the appellate stage. In this regard he referred to Section 114 of the Evidence Act. He also relied upon the decision in the case of **State of Maharashtra Vs. Ramdas Shrinivas Nayak and Anr.** reported in **ALL India Reporter 1982 Supreme Court page-1249** to support his contention, the points not urged before the learned Single Judge could not be raised at the appellate stage. He referred to the pleadings to show, no pleadings as to insolvency were made. He referred to two Calcutta High Court

decisions in the case of In Re: **Bengal Flying Club Limited** reported in **Volume-71 Calcutta Weekly Notes page-38** and in the case of **Mica Export Promotion Council Vs. Joneja** reported in **Volume-72 Calcutta Weekly Notes page-117**.

Distinguishing the decision in the case of **Madhu Woolen Mills Pvt. Ltd.** (supra) Mr. Mookherjee contended, the decision was rendered at the post admission stage whereas the case in hand was otherwise. He distinguished the other five decisions as follows :

1. **All India Reporter 1971 Calcutta page-78 (Calcutta Safe Deposit Co. Ltd. Vs. Ranjit mathuradas Sampat)**
2. **58 Company Cases 1985 page-174 (Bharat Overseas Bank Ltd. Vs. Shree Arcee Steels P. Ltd.)**
3. **1987 ILR Karnakata page-2673 (Hedge & Golay Limited Vs. State Bank of India)**
4. **All India Reporter 1955 Madras page-582 (Karnatak Vegetable Oils and Refineries Ltd. Vs. Madras Industrial Investment Corporation Ltd. and Anr.)**

5. **106 Company Cases page-52 (Confin Homes Ltd. Vs. Lloyds Steel Industries).**

He contended, the learned Judge dealt with all these cases and rightly held that those would have no application in the present case. He would rely upon the observation made by His Lordship on the said decisions. He also distinguished the decision in the case of **Rajiv Tandon** (supra) to say, the said decision would be of no assistance to the appellant. He lastly cited the decision in the case of **State Trading Corporation of India Ltd. Vs. Punjab Tanneries Ltd.** reported in **Volume-66 1989 Company Cases page-634** and in the case of **Manipal Finance Corporation Ltd. Vs. CRC Carrier Ltd.** reported in **107 Company Cases page-288** and in the case of In Re: **Cambrian Mining Company** reported in **1881 Weekly Notes page-125** to support his contentions.

Mr. Mookherjee summed up his argument by contending as follows :

(i) In view of the provisions of Section 13(1) and 13(4) of the SARFAESI Act, the winding up petition would not be maintainable.

(ii) The right of a secured creditor under the SARFAESI Act was inconsistent with others connected with the company. Hence, the winding up at the instance of a secured creditor would run contrary to the SARFAESI proceeding and as such would not be maintainable.

(iii) The appellant based their petition for winding up on a notice of demand issued under Section 434(1) (a) and not beyond. Hence, the learned Judge was right in not admitting the same after observing, the appellant failed to prove insufficiency of security.

(iv) Reliance on the balance-sheet as an annexure in absence of appropriate pleading would not help the creditor to take the plea of commercial insolvency.

(v) Admission of winding up is a discretionary remedy. The learned Judge, considering all aspects including the *mala fide* conduct of the appellant who came in unclean hand, very rightly rejected the winding up petition that would deserve no interference by this Court.

While giving reply, the learned Advocate General contended, the plea of parallel proceeding was never argued before His Lordship. Even in the cross-objection, this plea was not taken. Hence, the submission

made on that score must be rejected. The learned Judge accepted the status of the creditor. The learned Judge also accepted the plea of assignment. His Lordship also recorded the inability of the appellant to take possession by reason of resistance put up by the company. Having held so, His Lordship should not have declined to admit the winding up petition. The learned Advocate General relied on the report of the Official Liquidator that would show, the total area mentioned in the appropriate deed of conveyance would not match the physical verification. The land was found short by the Official Liquidator. He also referred to the order of the Court of appeal that dismissed an attempt to challenge the order for inventory dated September 19, 2011.

Commenting on the argument raised by the company on the statutory notice of demand the learned Advocate General referred to paragraphs 19, 20, 21, 22, 26, 27, 30 and 31 of the petition for winding up to show, the appellant averred commercial insolvency of the company that was not dealt with in the affidavit-in-opposition. According to him, the extract of the judgment and the order impugned quoted (supra) was contrary to the earlier findings of His

Lordship as contained in the internal page-9 of the judgment. On the issue of advertisement the learned Advocate General would contend, notice was initially given at the registered office of the company by Registered Post with Acknowledgment Due. The Acknowledgement Due Card did not come back compelling the appellant to publish the said notice. The extract of the notice was published. Hence, the plea of *mala fide* conduct would be of no consequence. He also referred to the pleadings to show that no reply was ever received by the appellant. Distinguishing the decision in the case of **National Conduits (P) Ltd.(supra)** he contended, the appellant published the statutory notice of demand and not the notice of petition for winding up. Hence, this decision was of no assistance to the appellant.

The Advocate General further contended, the appellant did urge the plea of commercial insolvency before His Lordship. He referred to the Apex court decision in the case of **State of Maharashtra-Vs- Ramdas Shrinivas Nayak and another (Supra)** in this regard. He referred to the judgement and the order impugned to say, the plea of commercial insolvency was duly taken as would be appearing from the judgement and order impugned. In this regard he referred to page 403 and 430

of paper book. He also referred to page 427 wherein the learned judge considered decision in the case of **Bukhtiarpur, Bihar Light Railway Company Limited** reported in **All India Reporter 1954 Calcutta page 499.**

Distinguishing the decision in the case of **Bengal Flying Club (supra)** the learned Advocate General contended, the facts would differ in the said case where substratum of the company was gone whereas such plea was never taken in this case. Distinguishing the decision in the case of **Mica Export Promotion Council (Supra)** he contended, the plea taken therein was never pleaded nor argued whereas in the present case such averment was made. Hence this decision would be of no assistance. In the case of **Manipal Finance Corporation (Supra)** claim was disputed. The Court termed the debt as "doubtful". In the present case learned judge never expressed any doubt with regard to the claim of the appellant. In the case of **Cambarian Mining Company (Supra)**, the court exercised discretion, no law was decided. In the case of **State Trading Corporation (Supra)**, it was not clear whether the decision was rendered before or after admission of the winding up petition.

He lastly contended, once the learned Judge considered the plea of commercial insolvency, His Lordship should not have dismissed the same only on the ground of deemed insolvency in terms of section 434 (1) (a).

Learned judge heard analogous matters where the common issue of section 434 (1) (a) was involved. In the present case, the petition was maintainable not only on the statutory notice but also on inability to pay. The learned Advocate General also demonstrated the pleading in this regard. Hence even if the notice of demand was not sufficient to maintain the winding up petition the plea of commercial insolvency would fill in the gap or short comings, if any.

In the SARFAESI Act they would be in deemed symbolic possession of asset once they invoked the provisions of said Act by serving the notice of demand. They could not take physical position because of the resistance that would be apparent from the record. We are not aware of any law that would debar the creditor from applying for winding up although they have taken resource to other civil action to realise their dues. The creditor has to show they would have a debt

more than Rs 500/- that the company failed or neglected to pay or otherwise unable to pay the debts because of its precarious financial condition that would make it just and equitable to pass an order of winding up. Neglect to pay is a fiction that would depend upon the notice to be served under section 434 (1) (a) that would permit the creditor to claim deemed insolvency as a fiction. However, that would not take away the creditor's right to claim, the company is also commercially insolvent or otherwise unable to pay its debt. If we give a close look to section 433 (e) and (f) we would find, the company may be wound up if it is unable to pay its debt and the court is of the opinion, it is just and equitable that it should be wound up. These two provisions could be invoked by the creditor as we find from section 439. Section 439 (1) (b) would permit any creditor to maintain the winding up petition. Sub section (2) would also include a secured creditor as a creditor within the meaning of sub section (1)(b). Section 434 (1) (a) would give right to a creditor by assignment or otherwise having a claim more than Rs. 500/- to serve the notice of remand and if the demand is not satisfied he would be entitled to claim deemed insolvency as per sub section (2). From the analysis as above, we would find as follows:-

i) A creditor could maintain the winding up petition.

ii) A secured creditor is also creditor to maintain winding up petition.

iii) A creditor should have the claim for Rs. 500 and above.

iv) He would serve the notice of demand, that demand, if unattended and /or unsatisfied, would permit the creditor to claim deemed insolvency

v) The creditor would maintain the winding up petition on the ground of inability to pay.

vi) He would have to prove, it is otherwise just and equitable that the company should be wound up.

In the present case, the appellant was a secured creditor. It had the claim for Rs. 500 and above. The creditor also pleaded, the company was insolvent and unable to pay its debts. The appellant also claimed, it was just and equitable that the company should be wound up. The above pleas could only be resisted by the company once they would raise the bona fide dispute meaning there by, if the creditor has an admitted claim it must be paid, in default that could only be resisted by raising a bona fide dispute. In the present case, creditor

could prove that it had a claim. The learned judge observed that there was little dispute that too, with regard to interest, the relevant observation as appearing in page 463 is as follows:

*"It is **beyond dispute** that the original creditor had granted substantial credit facilities to the company. Despite the company's proclamation to the contrary, it is evident that the petitioner is a creditor of the company, as the amount due and owing from the company to the original creditor and the securities furnished by the company to the original creditor have all been assigned to the petitioner."*

From the pleading, it would hardly appear that the company could dispute, far to speak of *bona fide*, that could resist a winding up petition. The learned Judge did not advert to the said issue.

His Lordship mainly considered the issue of deemed insolvency as per the notice. The learned judge, observed, in our view erroneously, *"since the present assessment is as to whether this petition made by a secured creditor, relying exclusively on section 434 (1) (a) of the Act for the court to presume the inability of the company to pay its debts,*

should be admitted for being advertised in the absence of the petitioning creditor having asserted or established the inefficacy or the inadequacy of the securities that it enjoys."

His Lordship was of the view, in view the provisions of section 434 (1) (a) creditor could maintain the petition upon service of notice of demand and the company's inability to pay or secure or compound to the reasonable satisfaction of the creditor. His Lordship was of the view, to claim deemed insolvency the creditor would have to show, securities were insufficient. Even if we accept the said view, the petition could not be held to be not maintainable due to mere absence of such fiction. In our view, His Lordship erred in holding, the petitioner maintained the petition exclusively under this provision. There were enough material to hold, the company was commercially insolvent. We asked Mr. Mookherjee in vain, how he would propose to clear off the dues. He was unable to give any suitable reply. The entire fixed assets were mortgaged. The company did not have sufficient funds to pay off the dues. The balance sheet would clearly demonstrate such insolvency. Even if we hold, their fixed assets were sufficient enough to pay off the dues, that could

only be possible upon sale of those assets and the company would hardly have anything left to carry out day to day business. The learned Judge possibly overlooked this aspect.

A creditor who has unpaid dues could only be reasonably satisfied if company has means to pay. When the creditor serves the notice upon the company asking them to pay off the dues the company has option either to pay off or dispute the same. Even if the company has means to pay and does not pay without any reasonable cause it would be liable to be wound up. However, this question may not be relevant here as the record shows, the company was in involved circumstances due to its precarious financial condition. In our view, His Lordship should have admitted the winding up petition and directed advertisement of notice making the said proceeding a representative action.

Emphasis was placed on the advertisement of notice of demand. The petitioning creditor claimed, they did not receive back the acknowledgement due card. It would have been proper, if the appellant would enquire from the postal authorities about the fate of such undelivered packet, or the acknowledgement due card. They

took no step in this regard. However, this ground alone would not be sufficient to deny admission of petition. This irregularity could not be presumed as *mala fide* as erroneously held by his Lordship.

If we go by His Lordship's views per se on section 434 (1) (a) we might agree with the ultimate result. However, the right of a creditor, secured or unsecured, to maintain the winding up petition would lie both under section 434 (1) (a) as well as 433 (e) and (f). Mr. Mookherjee contended, it was not argued. The learned judge however mentioned about the other aspect particularly the issue of commercial insolvency and such recording, unless confronted before His Lordship, must be taken as sacrosanct.

We thus conclude, the petition by a creditor would be maintainable on both counts. Once the creditor established his right to claim the amount more than Rs 500/- the onus would shift on the company to rebut such claim by raising bona fide dispute. Once the bona fide dispute is raised it would weaken the chance to have admission of the winding up petition, otherwise admission is an obvious consequence.

Even if we accept the view of His Lordship on the interpretation of section 434 (1) (a) we would not be in a position to agree with the ultimate finding as we find enough material to hold, the petition was maintainable in terms of sections 433 (e) and (f) read with sections 439 (1) (b) and 439 (2).

The appeal thus succeeds and is allowed. The judgement and order of His Lordship to the extent it declined to admit the winding up petition, is set aside. Winding up petition is remanded back to His Lordship for necessary direction with regard to admission and advertisement.

The APO 469 and 470 of 2012 is thus disposed of without any order as to costs.

Urgent certified copy of this judgment, if applied for, be given to the parties on their usual undertaking.

Shukla Kabir (Sinha), J:

I agree.

[ASHIM KUMAR BANERJEE,J.]

[SHUKLA KABIR (SINHA),J.]