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U.P. FINANCIAL CORPORATION AND ORS.

v.

M/S NAINI OXYGEN AND ACETYLENE GAS LTD. AND ANR.

NOVEMBER 22, 1994

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[KULDIP SINGH AND P.B. SAWANT, JJ.]

U.P. State Financial Corporation Act, 1951: Section 29—Default in repayment of loan instalments—Corporation justified in taking over the industrial establishment—In matters commercial the Courts should not risk their judgments for the judgments of the statutory bodies.

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The appellant - State Financial Corporation was established under the State Financial Corporation Act, 1951. On 10.12.1975 it sanctioned a term loan of Rs. 30 lakhs to the first respondent - Company payable in 17 half-yearly instalments by 22.8.1986. The Memorandum of Agreement executed between the appellant and respondent provided for recall of the entire balance of the loan in the event of default on the part of the respondent in paying two instalments of the loan and further to recover the balance of loan as arrears of land revenue.

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The respondent, however, made persistent defaults in repayment of the loan instalments with the result that the recovery certificate was issued against it under section 3 of the U.P. Public Moneys (Recovery of Dues) Act. Thereafter on 30th November, 1981, the respondent filed Company Petition under Sections 397 and 398 of the Companies Act in the High Court seeking removal of certain persons on grave charges of manipulation of accounts, re-allotment of forfeited shares etc.

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On 30.5.86 the appellant issued to the respondent notice under Section 29 of the Act for recovery of Rs. 90,31,102.13. On 13.6.86 the appellant took over the industrial establishment under Section 29 of the Act. The respondent filed a writ petition in the High Court challenging the take over. The High Court allowed the petition and directed the appellant to hand-over the industrial unit to the respondent.

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On 5.3.1987, this Court granted special leave and stayed the operation of the High Court's order and asked the Industrial Reconstruction Bank of India (IRBI) to submit its report as to the viability of the respondent - Company. On 29.1.1988, the IRBI made a

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report stating therein *inter alia* that after reschedulement and further A
infusion of about Rs. 1 crore, the unit will be "marginally viable".

On behalf of the appellant a question was raised whether it was
obliged to invest a further sum of Rs. 1 crore in the establishment and
whether even after such investment the unit would be viable or whether B
it should realise its loan from the sale of the assets of the respondent -
Company.

Allowing the appeal, this Court

HELD : 1. The fact that the appellant is an independent C
autonomous statutory body having its own constitution and rules to
abide by, and functions and obligations to discharge, cannot be lost
sight of. As such, in the discharge of its function, it is free to act
according to its own right. The views it forms and the decisions it
makes are on the basis of the information in its possession and the
advice it receives and according to its own perspective and calculations. D
Unless its action is mala fide, even a wrong decision taken by it is not
open to challenge. It is not for the courts or a third party to substitute
its decision, however more prudent, commercial or business like it may
be, for the decision of the appellant. Hence, whatever the wisdom (or
the lack of it) of the conduct of the appellant, the same cannot be
assailed for making the appellant liable. (664 B, C) E

2. It cannot further be forgotten that in the present case, the
Company had made persistent defaults in repayment of the loan-
instalments with the result that recovery certificate had to be issued
against it under Section 3 of the U.P. Public Moneys (Recovery of Dues)
Act. The then management had mismanaged the Company and a F
Company Petition had to be filed seeking its removal on grave charges
of manipulation of accounts, re-allotment of forfeited shares, etc. The
non-discharge of the liabilities of the Company was on account of the
said fraudulent practices of the management. By 30th May, 1986, the
dues of the Company mounted to Rs. 90, 31, 102.13 with the result that
on 13th June, 1986, the Corporation had to take over its industrial G
establishment under Section 29 of the Act. The report of the IRBI
which was given at the instance of this Court on 29th January, 1988
had stated that the industrial unit could be made only marginally
viable provided another Rs. one crore were invested in it and the loan
instalments were rescheduled. In the circumstances, if the Corporation H

A thought that the revival of the unit even after giving all concessions and reliefs as per the package deal was problematic and the Corporation will stand to lose whatever little it could retrieve towards its dues, the Corporation could hardly be blamed for the same. (664 D to H)

B 3. This is not a matter where the High Court should have stepped in and substituted its judgment for the judgment of the appellant which should be deemed to know its interests better whatever the sympathies the Court had for the prosperity of the Company. In matters commercial, the courts should not risk their judgments for the judgments of the bodies to whom that task is assigned. (665 A)

C 4. If the situation was bad on the date of the impugned judgment, it has become worse today. Between 1988 when the IRBI gave its report and this day, the situation has worsened with the further deterioration of the machinery and the spiralling of the liabilities. To grant any indulgence to the respondent at this stage will be akin to flogging a dead horse. The appellant will now be free to proceed according to law. (665 B, C)

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 568 of 1987.

From the Judgment and Order dated 13.1.87/15.1.87 of the Allahabad High Court in W.P. No. 16691 of 1986.

E R.K. Jain, Prashant Kumar and Satish Vig, for the Appellants.

Shanti Bhushan, Prashant Bhushan, Shanti Swarup Sharma, A.K. Sil and R.K. Sharma for the Respondents.

The Judgment of the Court was delivered by

F SAWANT, J. The case of the appellant-State Financial Corporation [for short the "Corporation"] is that it was established under the State Financial Corporation Act, 1951 [hereinafter referred to as the "Act"]. On 10th December, 1975, it sanctioned a term loan of Rs. 30 lakhs to the 1st respondent - Company [for short the "Company"] payable in 17 half-yearly instalments by the 22nd of August, 1986. The Memorandum of Agreement executed between the Corporation and the Company and the Deeds of Mortgage and Hypothecation executed by the Company in favour of the Corporation, *inter alia* provided for recall of the entire balance of the loan in the event of default on the part of the Company in paying two instalments of the loan and further to recover the balance of loan as arrears of land revenue. Accordingly, the Corporation disbursed Rs. 18 lakhs to the

Company in 1977 and Rs. 10 lakhs in 1978. In 1979, the Acetylene Gas plant of the Company was commissioned. In 1980, the Corporation disbursed the balance of Rs. 2 lakhs to the company thus making the total payment of loan of Rs. 30 lakhs. In July 1981, the Oxygen Gas plant of the Company was also commissioned. A

2. The Company, however, made persistent defaults in repayment of the loan instalments with the result that the recovery certificate was issued against it under Section 3 of the U.P. Public Moneys [Recovery of Dues] Act. The Company challenged the said recovery proceedings before the High Court in W.P. No. 15648 of 1981 which, however, was withdrawn by it later. Thereafter on 30th November, 1981, the Company filed Company Petition No. 23 of 1981 under Sections 397 and 398 of the Companies Act in the High Court seeking removal of persons then in management on grave charges of manipulation of accounts, re-allotment of forfeited shares etc. B C

On 25th March, 1982, the State Government issued Office Memorandum enunciating a scheme for rehabilitation of sick units and setting up, *inter alia* a State Level Inter-institutional Committee with power to approve loan upto Rs. 30 lakhs. On 9th January, 1984, there was a compromise in Company Petition No. 23 of 1981 whereunder the then management of the Company started running the plants. On 30th November, 1984, the Joint Director of Industries declared the Company to be a sick unit. On 5th October, 1985, the State Level Inter-Institutional Committee suggested a Rehabilitation Package which envisaged reschedulement of payment by the Company, arrangement of finances by the Company, appointment of two Directors nominated by the Corporation and execution of personal guarantee by the Directors. D E

On 19th October 1985, the Corporation wrote a letter to the Company stipulating the said conditions of the package. On 28th November, 1985 the terms of the Rehabilitation Package were acknowledged by the Company. On 5th December, 1985, the Board of Directors of the Corporation approved the Rehabilitation Package. The Company, however, did not take any steps to implement the Rehabilitation Package. F G

On 30th May, 1986, the Corporation issued to the Company notice under Section 29 of the Act for recovery of Rs. 90,31,102.13 which was made up on the principal amount of Rs. 30 lakhs, interest amount of Rs. 59,40,514.13 upto 31st March, 1986 and expenses of Rs. 90,588.00. The Company gave a reply to the notice on 5th June, 1986. H

- A On 13th June, 1986, the Corporation took over the industrial establishment under Section 29 of the Act. On 11th August, 1986, the Corporation pointed out to the Company that none of the conditions of the Rehabilitation Package was complied with. On 1st October, 1986, the Company filed W.P. No. 16691 of 1986 in the High Court. On 16th December, 1986, the Corporation declined to further liberalise the package.
- B On 13th/15th January, 1987, the High Court allowed the writ petition and directed the Corporation to hand over the possession of the industrial unit to the Company without any adjustment. On 5th March, 1987, this Court granted special leave and stayed the operation of the High Court's order and asked the Industrial Reconstruction Bank of India [IRBI] to submit its report as to the viability of the Company. On 29th January, 1988, the IRBI made a report stating therein *inter alia* that after reschedulement and further infusion of about Rs. 1 crore, the unit will be "marginally viable."

- On these facts, the question raised by the Corporation in this appeal is whether the Corporation is obliged to invest a further sum of Rs. 1 crore in the establishment and whether even after such investment the unit will be viable or whether the Corporation should realise its loan from the sale of the assets of the Company.
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3. As against the aforesaid case of the Corporation, the contention of the Company is that pursuant to the loan sanctioned by the Corporation, the Company imported two heavy-duty compressors from the U.S.A. and commissioned the Acetylene and Oxygen plants in 1979 and 1980 respectively. On account of the mismanagement of the majority group then dominating the management of the company, the present management which consisted of a minority of share-holders, had to institute proceedings in the High Court under Sections 397 and 398 of the Companies Act, and in February 1984 the High Court under a compromise order got the shares of the then management transferred to the present management at the face value of Rs. 10 per share. The equity capital invested by the present management viz., D.P. Agrawal Group, therefore, became of the order of Rs. 18 lakhs. Thereafter, the present management took various steps to revive the Company which had become sick and brought the plants into running condition after overhauling them at a considerable cost. For the purpose the present management gave loans of about Rs. 30 lakhs to the Company. On this investment, the total investment of the present management group became of the order of about Rs. 50 lakhs.
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4. On 30th November, 1984, the unit was declared sick by the Inter-institutional Committee consisting of various State Government agencies
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including the Corporation. This Committee was formed under the Government Order dated 25th March, 1982. By the said G.O. the Committee had been given full powers to take all steps to revive sick units in the State which were found viable and which could be restored to health. The Committee had also the power to wind up such units as were found not viable. A

5. On 5th October, 1985, the State-level Inter-institutional Committee which was presided over by the Commissioner, Allahabad Division, suggested the Rehabilitation Package. On the same day, viz., 5th October, 1985 the Board of the Corporation met and noted that the new management of the Company had brought about Rs. 8.30 lakhs during 1984-85 and 1985-86 and approved of the Rehabilitation Package suggested by the Committee. On 19th October, 1985, the Corporation also issued to the Company a formal letter communicating that the request for rehabilitation of the unit had been considered and the reliefs and concessions set out in the said letter had been granted. The concessions included rescheduling of the payment of the principal amount of the loan of Rs. 30 lakhs so as to require the said repayment from 22nd August, 1987 to 22nd August, 1993. The concessions also included the grant of interest-free funding on simple interest which was made repayable from February 1987 to February, 1996. The penal and compound interests were waived. The result of the grant of these concessions was that the repayment of the amount due to the Corporation was only to commence in 1987 and not before. B
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6. On 23rd December, 1985, the Commissioner and Director of Industries, U.P. wrote to the Reserve Bank to place the matter relating to the Company before the State Level Inter-institutional Committee for their final decision and asked the Reserve Bank to request all departments including the Corporation to stay their recovery proceedings till the final decision was taken on the rehabilitation. On 6th January, 1986, the Reserve Bank requested the Corporation to stay the recovery proceedings. F

In spite of this and in spite of the fact that the matter concerning the rehabilitation of the unit was pending consideration before the State Level Inter-institutional Committee and the Corporation itself had granted deferment of the repayment of the loan to 1987 to be completed in 1996, the Corporation issued another recovery notice of 9th January, 1986. However, on 18th January, 1986, the Head Office of the Corporation advised its Allahabad branch to stay the recovery proceedings. On 2nd May, 1986, a meeting of the State Level Inter-institutional Committee convened by the Reserve Bank, was held and the representative of the G
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- A Corporation informed the Committee that the Corporation had stayed the recovery proceedings against the Company in consultation with the Canara Bank a proposal for rehabilitation of the Company had been forwarded to the IRBI. The Committee decided that the Reserve Bank will call a joint meeting of all the agencies to take a decision in the matter. However, the Corporation once again issued a recovery notice on 30th May, 1986. The
- B Company replied to the said notice on 5th June, 1986 stating that on account of the deferment of the repayment scheduled by the Corporation itself, dues for which the notice was issued were not payable before 1987 and further the whole matter of rehabilitation was pending to be finalised.

7. Both the Acetylene and Oxygen plants, in the meanwhile, were
- C working to full capacity, the same being 24 hour continuous process plants. However, on 13th June, 1986, the Corporation got the factory sealed and the workers were forcibly evicted from the factory. This arbitrary action of the Corporation was criticised by all Government agencies and officers in [written] letter which are on record. They are : IRBI's letter dated 30th June, 1986, Canara Bank's letters dated 14th, 16th and 17th June, 1986;
- D letter dated 28th June, 1986 of the Commissioner, Rehabilitation Division and the letter dated 30th June, 1986 of the Additional Director of Industries. The Corporation, however, did not consider the advice given by these institutions and instead wrote to the Company's customers asking them not to pay the dues of the Company's bills and not to return the Company's
- E empty cylinders [about 1000 of the value of about Rs. 20 lakhs]. The said cylinders are now not traceable with the lapse of time.

8. On 11th August, 1986, the Director of Industries again wrote to the Reserve Bank requesting it to take up the matter of rehabilitation before the State Level Inter-institutional Committee. On the same day, the Corporation
- F wrote to the Company agreeing to give to the Company the possession of the unit stating that the IRBI shall prepare a total rehabilitation proposal within three months and the Corporation will follow the said proposal. The letter further stated that the present Directors of the Company should give personal guarantee for the repayment of the liabilities of the Corporation. On 21st August, 1986, the Company accepted the terms stipulated by the
- G Corporation in its said letter and also confirmed that the Directors will give personal guarantee for such amounts as were decided upon by the IRBI. On the same day, i.e. 21st August, 1986 the Reserve Bank wrote to the Director of Industries that in the meeting of the State Level Inter-institutional Committee held on 2nd May, 1986, an assurance was given by the representative of the Corporation that the recovery proceedings against the
- H Company had been stayed, and, therefore, a decision was taken to call

another meeting for the rehabilitation of the unit. Since, however, the Corporation had taken physical possession of the unit, no further action could be taken pursuant to that decision. The Reserve Bank in that letter also desired that the matter be taken up with the State Government so that the Government could intervene to stay the actions of the Corporation. By his letters of 29th August, 1986, the Director of Industries advised the Corporation to withdraw its action and allow the unit to run.

9. It was in these circumstances that the Company was forced to file the writ petition in the High Court on 1st August, 1986. The High Court had, by its impugned judgment, found that the action of the Corporation was very arbitrary and had directed it to restore the possession to the Company forthwith. It had also directed the IRBI to prepare rehabilitation package within four months of the restoration of the possession.

10. At the time the Corporation sealed the unit viz., on 30th June, 1986, according to the Company, the value of its assets was about Rs. 96 lakhs. This valuation had been done at the instance of the Corporation by a registered valuer in the later part of 1985. Under the Rehabilitation Package proposed by the Corporation, the Company was liable to pay to it the principal amount of Rs. 30 lakhs and interest on it in deferred instalments from 1987 to 1993 and without any further interest on the said interest amount in easy instalments from 1987 to 1996. In addition, the liabilities of the Canara Bank had already been quantified at Rs. 12.5 lakhs and the Bank had also to recover the said liabilities in easy instalments. Thus, as against the assets of the Company worth Rs. 96 lakhs, the total liabilities of the Company to the Corporation and the Canara Bank together were between Rs. 75 to 80 lakhs and these liabilities were also to be discharged in easy instalments upto 1996. Hence it is the case of the Company that the impugned judgment of the High Court was perfectly justified.

11. However, the Corporation obtained the stay of the said judgment from this Court which has continued from 1987 to this day. The result has been that the plants have continued to remain closed and the interest has continued to accumulate on the dues of the Corporation and the Canara Bank. The plants have, in the meanwhile become almost a junk, and the cylinders worth Rs. 20 lakhs are not traceable. Today, the total value of the assets including land and buildings has come down to Rs. 42 lakhs from Rs. 96 lakhs in 1986. It is, therefore, the contention of the Company before us that the Corporation's appeal should be dismissed and the Company should be restored to the same position in which it had been on the date the stay order was obtained in this appeal. It is contended that if the stay order had

- A. not been obtained by the Corporation, the Company would have got the possession of the plants in January 1987 in good condition and its liabilities would have been only between Rs. 75 to 80 lakhs. The Company further prays that the interest which has accrued on the dues of the Corporation should be waived and that on the dues of the Canara Bank should be borne by the Corporation. It is further contended by the Company that as per the
- B order of this Court passed on 5th March, 1987, the IRBI has submitted its report on 5th February, 1988 according to which the unit was found viable. In this connection, the following passages from the said report are relied upon by the Company.

- C “Resolved that the proposal contained in memorandum of IRBI No. 8793/88 dated 1.12.88 for sanction of Rupee term loan not exceeding Rs. 190 lakhs (Rupees one hundred and ninety lakhs only) to Naini Oxygen and Acetylene Gas limited (NOAG) towards the cost of proposed modernisation-cum-rehabilitation scheme on the terms and conditions contained in Appendix of the memorandum,
- D besides normal terms and conditions applicable to such loan from IRBI, be and is hereby approved.”

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- E “In the light of IRBI having submitted a report on the viability aspect of NOAG as elaborated earlier, the Hon’ble Supreme Court has directed IRBI to consider the report and intimate its decision to this court. UPFC sometime in August, 1986 had communicated earlier to the Company its intention, *inter-alia*, to follow the rehabilitation proposal approved by IRBI. In the discussion with Canara Bank it
- F appeared that the Bank was favourably inclined to support rehabilitation proposal approved by IRBI. Meanwhile, market study undertaken by M/s Development Consultant Pvt. Ltd., reflects a favourable market condition for the proposed product mix of NOAG.”

- G The Report had provided for a package of reliefs and concessions relating to the Corporation and the Canara Bank. Apart from the waiver of penal and compound interests which had also been agreed to by the Corporation and refunding of the simple interest which had also been agreed to by the Corporation, the package proposed in the report, “interest holiday” during the period of the closure of the factory, i.e., from the date
- H of the take-over of the factory to the date of the reopening of the same.

In this connection, the Company also pointed out that the IRBI was prepared to give a term loan of Rs. 1.9 crores for making the unit profitable and no additional finance was required either from the Corporation or the Canara Bank. The Company had thereupon made an application to this Court for permitting it to repair the machinery under the supervision of the Corporation pending the disposal of the appeal. However, the Corporation through its counsel had undertaken to carry out the said repairs itself, and this was recorded by this Court in its order of 27th April, 1988. In spite of the undertaking to carry out the repairs, the Corporation did not do so with the result the Company was compelled to file an application for contempt being CMP No. 2715 of 1989. That Contempt Petition is still pending. The Company would, therefore, also be entitled to be compensated for the losses caused to it on account of the non-fulfilment of the undertaking given by the Corporation to the Court.

12. No doubt, there is nothing on record to explain certain events, viz., [i] when on 19th October, 1985 the Corporation had issued to the Company a formal letter communicating to it its acceptance of the rehabilitation package and grant of reliefs and concessions set out therein, what impelled the Corporation to issue recovery notice on 9th January, 1986 which was later on stayed by the Corporation itself on 18th January, 1986; [ii] if on 2nd May, 1986, the Corporation had informed the State-level Inter-institutional Committee that it had stayed the recovery proceedings, what impelled the Corporation once again to issue the recovery notice on 13th May, 1986; [iii] if the Corporation itself had agreed by its letter on 19th October, 1985 to reschedule the payment of loan from 1987 to 1996, what impelled it to issue the said recovery notice on 13th May, 1986 when admittedly as per the Corporation's offer, the payment of loan and interest from the Company was not due and when the entire matter of the rehabilitation of the Company was under active consideration; [iv] what impelled the Corporation on 13th June, 1986 to seal the unit and write to the customers not to pay the bills and not to return the cylinders to the Company; [v] when on 11th August, 1986, the Corporation had written to the Company agreeing to give it back the possession of the unit and to follow the rehabilitation proposal that would be prepared by the IRBI on the condition that the Directors of the Company would give personal guarantee for the payment of the liabilities and the Company had accepted the terms by its letter of 21st August, 1986 and when the Director of Industries had advised the Corporation on 12th August, 1986 to withdraw the recovery notice, why had the Corporation not handed over the possession of the unit to the Company; [vi] why had the Corporation not taken steps to repair the machines, in spite of the undertaking given to this

- A Court and [vii] why had the Corporation not accepted the report of the IRBI submitted on 5th February, 1988 to this Court when the IRBI was prepared to invest term loan of Rs. 1.9 crores for making the unit marginally viable?

B 13. However, we cannot lose sight of the fact that the Corporation is an independent autonomous statutory body having its own constitution and rules to abide by, and functions and obligations to discharge. As such, in the discharge of its functions, it is free to act according to its own light. The views it forms and the decisions it takes are on the basis of the information in its possession and the advice it receives and according to its own perspective and calculations. Unless its action is mala fide, even a wrong
C decision taken by it is not open to challenge. It is not for the courts or a third party to substitute its decision, however more prudent, commercial or business like it may be, for the decision of the Corporation. Hence, whatever the wisdom [or the lack of it] of the conduct of the Corporation, the same cannot be assailed for making the Corporation liable.

D 14. It cannot further be forgotten that in the present case, the Company had made persistent defaults in repayment of the loan-instalments with the result that recovery certificate had to be issued against it under Section 3 of the U.P. Public Moneys [Recovery of Dues] Act. The then management had mismanaged the Company and a Company Petition had to be filed seeking
E its removal on grave charges of manipulation of accounts, re-allotment of forfeited shares, etc. The non-discharge of the liabilities of the Company was on account of the said fraudulent practices of the management. By 30th May, 1986, the dues of the Company mounted to Rs. 90,31,102.13 with the result that on 13th June, 1986, the Corporation had to take over its industrial establishment under Section 29 of the Act. The report of the IRBI
F which was given at the instance of this Court on 29th January, 1988 had stated that the industrial unit could be made only marginally viable provided another Rs. one crore were invested in it and the loan instalments were rescheduled. Between 1981 when the industrial establishment was closed down and 1988 when the IRBI report was submitted, the machinery of the establishment was lying idle and was almost rusty with the result that
G by 1988, the value of the machinery had gone down considerably, while its liabilities had gone up still further. In the circumstances, if the Corporation thought that the revival of the unit even after giving all concessions and reliefs as per the package deal was problematic and the Corporation will stand to lose whatever little it could retrieve towards its dues, the
H Corporation could hardly be blamed for the same.

15. We are, therefore, of the view that this is not a matter where the High Court should have stepped in and substituted its judgment for the judgment of the Corporation which should be deemed to know its interests better whatever the sympathies the Court had for the prosperity of the Company. In matters commercial, the courts should not risk their judgments for the judgments of the bodies to whom that task is assigned. A

If the situation was bad on the date of the impugned judgment, it has become worse today. Between 1988 when the IRBI gave its report and this day, the situation has worsened with the further deterioration of the machinery and the spiralling of the liabilities. To grant any indulgence to the Company at this stage will be akin to flogging a dead horse. In the circumstances, we, allow the appeal and set aside the impugned judgment of the High Court. The Corporation will now be free to proceed according to law. B C

V.S.S.

Appeal allowed.