

INTERNATIONAL COACH BUILDERS LTD.

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v.

KARNATAKA STATE FINANCIAL CORPN.

MARCH 5, 2003

[RUMA PAL AND B.N.SRIKRISHNA, JJ.]

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State Financial Corporation Act, 1951/ Companies Act, 1956—Sections 29 and 46B/Sections 433, 529 and 529A—Right of State Financial Corporation under Section 29 to sell and resell—Exercise of—Without reference to Company Court—When winding up order made against the debtor-Company—Held, State Financial Corporation cannot exercise its power to sell and resell the security without reference of the Court in case of Company in a winding up, in view of pari passu charge of the workmen created by the proviso to Section 529 of Companies Act—The right can be exercised only with the consent of the Official Liquidator representing workmen for their pari passu charge—Sections 529 and 529A of Companies Act would override and control the provisions of Sections 29 and 46B of Financial Corporation Act—Transfer of Property Act, 1882—Mortgage.

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Winding up petitions were filed against certain companies by the creditors. The companies had borrowed money from State Financial Corporations. As security, the companies had mortgaged their property with the respective Corporations. The Corporations took mortgaged assets of the Companies in exercise of their power under Section 29 of the State Financial Corporation Act, 1951 (SFC Act). Companies were ordered to be wound up by the Company Court and Official Liquidators were appointed. The Corporation filed petitions before Company Court/High Court seeking permission to stand outside winding up proceedings and work out their remedies under Section 29 of SFC Act. Thus the question that arose for consideration before the High Courts was whether the rights of the State Financial Corporation under Section 29 of SFC Act to sell and resell the security could be exercised without reference to the Company Court when a winding up order is made against a Company? Conflicting views were given by different High Courts. In appeal to this Court State Financial Corporations contended that they are secured creditors and as such were entitled to exercise their rights under mortgage as also statutory rights conferred under Section 29 of SFC Act without reference of Court. Hence the Corporation could sell

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A the mortgaged and charged properties without reference to any Court.

Disposing of the appeals, the Court

B HELD: 1. The right unilaterally exercisable under section 29 of State Financial Corporation Act, 1951 (SFC Act) is available against a debtor, if a company, only so long as there is no order of winding up. The State Financial Corporations (SFCs) cannot unilaterally act to realize the mortgaged properties without the consent of the official liquidator representing workmen for the pari passu charge in their favour under the proviso to section 529 of the Companies Act, 1956. If the official liquidator does not consent, the SFCs have to move the Company court for appropriate directions to the official liquidator who is the pari passu charge holder on behalf of the workmen. In any event, the official liquidator cannot act without seeking directions from the Company Court and under its supervision. [652-A-C]

D 2. As a result of the proviso added in Section 529 of Companies Act, the security of every secured creditor is deemed to be subject to a 'pari passu' charge in favour of the workmen to the extent of the workmen's dues (called 'workmen's portion, as defined in sub-section (3)(c) therein. Where the secured creditor, instead of relinquishing its mortgage and proving his debt, opts to stand outside the winding up proceedings and realize his security, the Official Liquidator shall be entitled to represent the workmen and enforce such charge and that any amount realized by enforcement of such charge shall be applied ratably by the Official Liquidator for the discharge of workmen's dues. It is true that even the amended proviso does not give the Liquidator an independent right of enforcing the charge by selling the security against which such charge is created. Nonetheless, it creates a 'pari passu' charge in favour of the workmen to the extent of their dues and makes the Liquidator representative of the workmen to enforce such a charge. By reason of Clause (c) of the newly added proviso, so much of the debt due to the secured creditor opting to realize security as could not be realized because of the specially created rights in favour of the workmen, or the amount of the workmen's portion in the security, whichever is less, shall rank pari passu with the workmen's dues under Section 529A of Companies Act. Section 529A provides for overriding preferential payments of workmen's dues and unrealized portion of the secured creditors dues, as provided in clause (c) of the proviso to Section 529. [644-D-H]

H *M.K. Ranganathan and Anr. v. Government of Madras and Ors., AIR (1955) SC 604, distinguished.*

Maharashtra State Financial Corporation v. Ballarpur Industries Limited, AIR (1993) Bombay 392, referred to. A

3. There is no conflict between the provisions of the Companies Act as amended in 1985 and the provisions of the SFC Act, 1951. The provisions of the SFC Act were merely intended to give an expeditious remedy to the SFCs without having to go through the procedure of enforcing the mortgage under the Transfer of Properties Act, 1882. In fact, even under Section 69 of the Transfer of Property Act, under certain circumstances, a mortgagee has the power to sell the mortgaged property in default of payment of mortgaged money without intervention of the court. Under the general law, the SFCs would have to file a suit for realizing their security unless they qualified under Section 69 of the Transfer of Property Act. This meant considerable delay and holding up of the public monies due to the SFCs. In public interest, therefore, special provisions were made by Sections 29, 30, 31 and 32 enabling the SFCs to take possession of the mortgaged asset and sell them without having to move a court of law. The provisions of Section 29 to 32 and the rights flowing thereon are exercisable under ordinary circumstances. However, when the debtor is a Company in winding up, the right of the SFCs is affected by the provisions of the Companies Act, 1956. Assuming that there is conflict, the amendments made in Section 529 and 529A would override and control the rights under Section 29 of the SFC Act. Though the Companies Act may be general law, the provisions introduced therein in 1985 were intended to confer special rights on the workers and, *pro tanto*, must be treated as special law made by Parliament. Since the amendments to the Companies Act were made by a later Act of 1985, they would override the provisions of Section 29 of SFC Act, 1951. [645-A-F] B C D E

A.P. State Financial Corporation v. Official Liquidator, [2000] 7 SCC 291, relied on. F

Jowitt's Dictionary, Vol. II, 1959 Edition 1294 and *Black's Law Dictionary*, 6th Edition, 115, referred to.

4. The right of the *pari passu* charge holders would run equally, temporally and potently, with the rights of the secured creditors. The Official Liquidator, as the representative of the workmen, to enforce such *pari passu* charge would have the right of representing the workmen equally with the rights of the secured creditors. [646-C-D] G

5. Though the charge by itself may not amount to mortgage, all the H

- A provisions which apply to a simple mortgage, so far as may be, apply to a charge. Thus, the Official Liquidator, as the representative of the workmen's *pari passu* charge, would be in the position of a co-mortgagee. Though Section 29 hitherto enabled the SFC as a mortgagee to exercise its right thereunder by taking possession of the property and selling it in satisfaction of its debt,
- B the situation has now changed. Because of the aforesaid statutory intervention, the SFC must necessarily contend with a *pari passu* charge holder who has equal rights. Where there are co-mortgagees, one co-mortgagee cannot sell without consent of the co-mortgagee or institute any proceedings for sale of mortgaged property without joining the other co-mortgagees either as plaintiffs or as defendants. The SFC's right under Section 29 of freely realizing
- C its security gets trammelled. If it has to take on a *pari passu* charge holder, the realization of the security can thereafter only be done either by satisfaction of the *pari passu* charge or by a suit in which the *pari passu* charge holder would be a party defendant. Though when the SFC Act was enacted in 1951 it was intended that SFC could act unilaterally, the amendments made to the Companies Act in 1985 have introduced a *pari passu* charge holder as a co-
- D helmsman of the ship of the SFC, who can neither be ignored nor overridden. In other words, the existence of the *pari passu* charge holder being represented by the Official Liquidator would necessarily bring in supervision of the Company Court as the Official Liquidator cannot act without directions from and supervision of the Company Court. The statutory right to sell the property
- E under Section 29 of the Act has now to be exercised in tandem with the rights of *pari passu* charge in favour of the workmen created by the proviso to Section 529 of the Companies Act. [646-F-H]

Sunitibala Debi v. Dharae Sundari Debi, AIR (1919) PC 24, referred to.

- F 6. Every creditor is interested in realizing the security only for his benefit and to the extent necessary for recovery of his outstandings. Prior to 1985 it might have been possible for a secured creditor under Section 529 of the Companies Act, 1956, or its predecessor, Section 232 of the Companies Act, 1913 to opt to stand outside the winding up and realize the security by bringing
- G it to sale. This was possible because the secured creditor had unrestricted right of standing outside the winding up and proceeding against the property mortgaged to him. [648-G-H]

M.K. Ranganathan and Anr. v. Government of Madras and Ors., AIR (1955) SC 604, relied on.

- H 7. No doubt section 29 of the SFC Act was intended to place the SFCs

on a better footing. This better footing is available only so long as the debtor is not a company or is a going company. The moment a winding up order is made in respect of a debtor company, the provisions of section 529 and 529A come into play and whatever superior rights had been ensured to SFCs under the provisions of the SFC Act are now subjected to and operate only in conjunction with the special rights given to the workmen, who as *pari passu* charge-holders are represented by the official liquidator. [649-D-E]

8. If the non-obstante clause in section 529A and section 46B conflicts with the non-obstante clause in section 529A, then the amendments to the Companies Act made in 1985 must prevail over the non-obstante clause in section 46B of the SFC Act which was inserted in the year 1956. [650-D]

A.P. State Financial Corporation v. Official Liquidator, [2000] 7 SCC 291-relied on.

Andhra Pradesh State Financial Corporation v. Electrothermic (P) Ltd., and Anr. (1986) Co. Cases 402; *Official Liquidator, Ravindra Pharmaceutical (P) Ltd. v. Haryana Financial Corporation Company* Cases Vol. 98 p. 683, referred to.

9. The reasoning of the Gujarat High Court that in case the secured creditor does not opt to realize the security, the liquidator, by dint of the proviso to section 529, does not become a charge holder in the estate of the company so as to exercise the right of a simple mortgagee as envisaged under section 100 of the Transfer of Property Act, appears to be non-sequitur. If a secured creditor does not opt to stand outside the winding up but relinquishes his security and proves his debt in the winding up, then there is no doubt that the official liquidator will come into custody of all the assets of the company in liquidation and the distribution of the assets would have to proceed in accordance with the provisions of section 529 A of the Companies Act, in which case the secured creditor stands in line as an unsecured creditor. It is only when the SFC as a secured creditor opts to stand outside the winding up and seeks to realize its security that conflict, if any, can arise. The fact that the liquidator or the workmen do not have a right independently to enforce the charge, unless the creditor decides to stand outside the winding up, does not make any difference to the situation. [650-H; 651-A-C]

10. As a result of the amendments made by the Act of 1985 in the Companies Act, 1956, the SFCs as secured creditors, must seek leave of the Company Court for the limited purpose of ensuring that the *pari passu* charge

A in favour of the workmen is safeguarded by imposition of suitable conditions under the supervision of the Company Court. If this amounts to impeding their hitherto unimpeded rights, so be it. Such is the Parliamentary intendment. This impediment is of a limited nature for the specific purpose of protecting the *pari passu* charge of the workmen's dues and subject thereto, **B** SFCs can continue to exercise their statutory rights as secured creditors without being reduced to the status of unsecured creditors required to prove their debts in insolvency and standing in line with other unsecured creditors. [651-F-G]

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 4702 of 1994.

C From the Judgment and Order dated 17.6.1983 of the Karnataka High Court in C.P. No. 188 of 1993.

WITH

C.A. Nos. 4703/94, 6303, 6491/95, 12928/96 and 2007 of 1997.

D R.P. Bhatt, Dilip Goswami, Revathy Raghavan, Arvind Biswal, Gopala Krishnan, S. Prasad, S. Ravindra Bhat, Naveen R. Nath, Lalit Mohini Bhat, Ms. Hetu Arora, Dyan Prakash, Nikhil Nayyar, Trideep Pais, Gautam Narayan, B. Smita Rao, Shrish Kumar Misra, Anis Kumar Gupta, Sunil Dogra, Ms. Sayali Phatak Rakesh K. Sharma, M.N. Shroff, S.N. Bhat, P.P. Singh, (NP), **E** Ms. H. Wahi, (NP) for the appearing parties.

The Judgment of the Court was delivered by

F **SRIKRISHNA, J.** These appeals arising under different factual background raise the same question of law and can, therefore, conveniently be disposed of by a common judgment.

Facts

Civil Appeal Nos. 4702 and 4703 of 1994

G On 23rd May, 1988 a winding up petition was filed under Section 433 of the Companies Act, 1956 seeking to wind up the company known as International Coach Builders Ltd. Another petition by another creditor was also filed on 2.11.88. On 10.11.89, during the pendency of the above petitions before the High Court of Karnataka, the respondent, a Corporation established under the State Financial Corporation Act, 1951 (SFC Act), which was the **H** second charge holder on the assets of the said company, took possession of

the mortgaged assets of the said company in purported exercise of its power under Section 29 of the SFC Act. On 30.11.1990 the High Court of Karnataka in Company Petition No. 131 of 1988 made an order of winding up of International Coach Builders Ltd. and appointed the Official Liquidator as the Liquidator to take charge of the assets of the said company. On 30.11.90 the respondent-Corporation accepted a bid of Rs. 85 lakhs made by Raheja Development Corporation for sale of the mortgaged assets of the said company, although, to its knowledge, the assets charged were totally valued at an estimated value of Rs.97 lakhs. Neither the Official Liquidator, nor the Company Court, was in any way involved with the negotiations held by the respondent-Corporation with the prospective purchaser. On 4.3.1991 the respondent filed an application under Section 446 (2) (b) read with Section 537 of the Companies Act, 1956 before the High Court of Karnataka praying for leave to stand outside the winding up proceedings and realize its securities by selling the assets mortgaged to it. As per the resolution passed in its Board meeting held on 30.11.1990, it was resolved to accept the bid of *M/s Raheja Development Corporation*. On 8.10.1991 the Company Court allowed the application of the respondent-Corporation for standing outside the liquidation proceeding to work out its remedies under Section 29 of the SFC Act subject to an undertaking to discharge the workmen's dues. The Official Liquidator appealed against the order of the Company Judge praying that the sale of the assets of the company under liquidation should only be done by the Official Liquidator under the supervision of the Company Court. The appeal of the Official liquidator (OSA No. 26/91) was dismissed by a Division Bench of the High Court of Karnataka. An application for review, Review, Application No. 118/93, was also dismissed by the High Court of Karnataka. The Official Liquidator filed two Special Leave Petitions before this Court challenging the order of the Division Bench dated 23rd January, 1992 dismissing the appeal OSA No.26/91, and the order dated 17th June, 1993 dismissing the Review Application No. 118/93. These are respectively Civil Appeal Nos. 4702 & 4703 of 1994.

When the Special Leave Petitions came up for admission this Court made the following order.

“Special Leave Petition granted.

Meanwhile, it appears appropriate that the Respondent KSFC should sell the properties acting jointly with the Official Liquidator under the supervision and in accordance with the direction of the Learned Company Judge of the High Court and sale proceeds be deposited in

A the Court and then distributed in accordance with the direction of the Learned Company Judge.”

Civil Appeal No. 12928 of 1996

B As a sequel to the above order, *M/s Raheja Development Corporation* moved an application before the Company Judge, High Court of Karnataka, for a direction to the Official Liquidator to concur in the sale effected by Karnataka State Finance Corporation (KSFC) in its favour. The Company Judge disposed of the application holding that, in view of the order passed by this Court, the application did not survive. *M/s Raheja Development Corporation* made an unsuccessful attempt to intervene in Civil Appeal C No.4702/94 by seeking relief therein, but its applications I.A. Nos. 4,5,6 & 7 were dismissed. *M/s Raheja Development Corporation* appealed against the order of the Company Judge raising similar contentions as urged by the KSFC. The Division Bench dismissed the appeal by taking the same view as the Company Judge. The appellant is before this Court.

D **Civil Appeal No. 6491 of 1995**

A company known as *M/s. Prasad Bakers Pvt. Ltd.* borrowed money from the appellant—a State Financial Corporation established in Uttar Pradesh. The repayment of the borrowed money was secured by mortgage of the factory premises and hypothecation of plant and machineries of the said E *M/s. Prasad Bakers Pvt. Ltd.* (the second respondent in the appeal). The second respondent defaulted in repayment of the loan and the appellant called in the money by a notice dated 30th June 1997. On 18.9.1987 the appellant, in purporting to exercise its power under Section 29 of SFC Act, took possession of the mortgaged assets. In the meanwhile, the first respondent, a F creditor of the second respondent, had filed a petition under Section 433 (e) of the Companies Act on which the High Court of Allahabad made an order dated 1.2.1994 for winding up of the second respondent company. The appellant-Corporation appeared before the Company Judge and contended that it was a secured creditor having first charge over the mortgaged property and, despite commencement of the winding up proceeding, entitled to exercise G its powers under Section 29 of the SFC Act to put to sale the mortgaged assets without leave of the Company Court. The learned Company Judge rejected the submission made on behalf of the appellant-Corporation and directed winding up of the company. An appeal carried to the Division Bench was summarily dismissed. Hence, the appeal by the Corporation.

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Civil Appeal No. 2007 of 1997

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The respondent company obtained large amounts of loans/advances from the appellant Karnataka State Finance Corporation (KSFC). The loans were secured by mortgages and charges on the assets of the respondent company. The company having defaulted in repayment of the loans according to the schedule, the KSFC issued a notice and took over the mortgaged and charged assets under Section 29 of the SFC Act. In the meanwhile, at the instance of a creditor of the respondent company the company was ordered to be wound up. The KSFC made an application to the Company Judge under Section 537 of the Companies Act, 1956 for permission to stand outside the winding up proceedings and realize its security. The learned Company Judge dismissed the petition of the respondent. An appeal to the Division Bench also failed. The KSFC is in appeal and raises the same contentions with regard to its rights under Section 29 of the SFC Act.

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Civil Appeal No. 6303 of 1995

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A company known as Himalaya Tools (India) Pvt. Ltd. had borrowed money from the Gujarat State Financial Corporation. The said company was ordered to be wound up on 25.1.1988 by the Company Court. On 9.5.1988, in purported exercise of rights under Section 29 of the SFC Act, the Gujarat State Financial Corporation (GSFC) took possession of the charged assets of the said company. The Official Liquidator of the said company took out a judge's summons seeking a direction to GSFC forthwith to hand over possession of the asset of the company in liquidation. In the meanwhile, the GSFC took steps to transfer of the properties of the company liquidation, again purportedly under Section 29 of the SFC Act. On 20.12.1989 the GSFC handed over possession of the premises of the company in liquidation to M/s Mahuvawala Trading Company for a consideration of Rs. 8,99,726.52. At no point of time was permission of the Company Court taken, nor was the sale approved by the Company Court. The Company Court on being moved did not find the sale to be wanting in *bona fides* and declined to set aside the sale, but directed GSFC to deposit the consideration received in court taking the view that the powers under Section 29 could not be unilaterally exercised without concurrence of the Company Court. GSFC carried the matter in appeal to the Division Bench which allowed the appeal holding that GSFC as a secured creditor could opt to realise the securities by standing outside the winding up proceeding and neither the liquidator, nor the Company Court, could interfere with the rights of GSFC as a secured creditor once it opted

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A to remain outside the winding up proceedings. The Official Liquidator is in appeal.

The common question agitated in all these appeals is: whether the rights of the State Financial Corporation under Section 29 of SFC Act to sell and realise the security could be exercised without reference to the Company

B Court when a winding up order is made against the company.

Conflicting views have been taken by different High Courts on this issue. Hence, the need for this Court to settle the law.

C Relevant Statutory Provisions

Before we address ourselves to the question of law argued, it is necessary to refer to some of the relevant statutory provisions. The State Financial Corporation Act, 1951 was brought on the statute book to grant special privileges to State Financial Corporations established thereunder in the matter of enforcement of their claims against borrowers and to enable speedier recovery of public monies. The relevant provisions of the SFC Act are Sections 29 and 31 which read as under:

E “Section 29 - (1) Where any industrial concern, which is under a liability to the Financial Corporation under an agreement, makes any default in repayment of any loan or advance or any instalment thereof [or in meeting its obligations in relation to any guarantee given by the Corporation] or otherwise fails to comply with the terms of its agreement with the Financial Corporation, the Financial Corporation shall have the [right to take over the management or possession or both of the industrial concerns] as well as the [right to transfer by way of lease or sale] and realize the property pledged, mortgaged, F hypothecated or assigned to the Financial Corporation.

G (2) Any transfer of property made by the Financial Corporation, in exercise of its powers [***] under sub-section (1), shall vest in the transferee all rights in or to the property transferred [as if the transfer] had been made by the owner of the property.

H (3) The Financial Corporation shall have the same rights and powers with respect to goods manufactured or produced wholly or partly from goods forming part of the security held by it as it had with respect to the original goods.

(4) [Where any action has been taken against an industrial concern] under the provisions of subsection (1), all costs, [charges and expenses which in the opinion of the Financial Corporation have been properly incurred] by it [as incidental thereto] shall be recoverable from the industrial concern and the money which is received by it [***] shall, in the absence of any contract to the contrary, be held by it in trust to be applied firstly, in payment of such costs, charges and expenses and, secondly, in discharge of the debt due to the Financial Corporation and the residue of the money so received shall be paid to the person entitled thereto.]

(5) [Where the Financial Corporation has taken any action against an industrial concern] under the provisions of sub-section (1), the Financial Corporation shall be deemed to be the owner of such concern, for the purpose of suits by or against the concern, and shall sue and be sued in the name of [the concern].

“Section 31 - (1) Where an industrial concern, in breach of any agreement, makes any default in repayment of any loan or advance or any instalment thereof [or in meeting its obligations in relation to any guarantee given by the Corporation] or otherwise fails to comply with the terms of its agreement with the Financial Corporation or where the Financial Corporation requires an industrial concern to make immediate repayment of any loan or advance under Section 30 the industrial concern fails to make such repayment, [then, without prejudice to the provisions of section 29 of this Act and of section 69 of the Transfer of Property Act, 1882 (4 of 1882)] any officer of the Financial Corporation, generally or specially authorized by the Board in this behalf, may apply to the district judge within the limits of whose jurisdiction the industrial concern carries on the whole or a substantial part of its business for one or more of the following reliefs namely:-

- (a) for an order for the sale of the property pledged, mortgaged, hypothecated or assigned to the [Financial Corporation] as security for the loan or advance; or
- (aa) or enforcing the liability of any surety; or]
- (b) for transferring the management of the industrial concern to the Financial Corporation; or
- (c) for an interim injunction restraining the industrial concern from

A transferring or removing its machinery or plant or equipment from the premises of the industrial concern without the permission of the Board, where such removal is apprehended.

(2) An application under sub-section (1) shall state the nature and extent of the liability of the industrial concern to the Financial Corporation, the ground on which it is made and such other particulars as may be prescribed.

B Section 32 empowers the Corporation to move the District Judge for appropriate ad interim and interim orders in aid of action under Section 31. Section 46B gives an overriding effect to the provisions of the Act and reads as under:

C “Section 46B - The provision of this Act and of any rule or orders made thereunder shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in the memorandum or articles of associations of an industrial concern or in any other instrument having effect by virtue of any law other than this Act, but save as aforesaid, the provisions of this Act shall be in addition to, and not in derogation of, any other law for the time being applicable to an industrial concern.]

D Section 46B was inserted by Act 56 of 1956 with effect from 1.10.1956.

E The relevant provisions of the Companies Act, 1956 which need to be noticed are: Section 529 and 529A which read as under:

“Section 529 - (1) In the winding up of an insolvent company, the same rules shall prevail and be observed with regard to-

F (a) debts provable;

(b) the valuation of annuities and future and contingent liabilities; and

(c) the respective rights of secured and unsecured creditors;

G 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 if every secured creditor shall be deemed to be subject to a *pari passu* charge in favour of the workmen to the extent of the workmen's portion therein, and, where a secured creditor, instead of relinquishing his security and proving his debt, opts to

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realize his security:-

- (a) the liquidator shall be entitled to represent the workmen and enforce such charge;
- (b) any amount realized by the liquidator by way of enforcement of such charges shall be applied ratably for the discharge of workmen's dues; and
- (c) so much of the debt due to such secured creditor as could not be realized 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 purpose of section 529.]”

“Section 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.”

The Contentions

It is contended on behalf of the SFCs that they are secured creditors and as such entitled to exercise their rights under the mortgage as also the statutory rights conferred on them by Section 29 of SFC Act without interference of courts. Hence, it is urged that the SFCs can sell the mortgaged and charged properties without reference to any court, much less the Company Court. Reliance is placed on the judgment of this Court in *M.K. Ranganathan and Anr. v. Government of Madras and Ors.*, AIR (1955) SC 604. That was a case arising under Section 232 of the Companies Act, 1913. This Court was required to consider the meaning of the provision “any sale held without leave of the Court of any of the properties” used in Section 232 (1) of the Companies Act, 1913 which rendered such sales void. It was held that these words refer only to sales held through the intervention of the Court and not to sales effected by the secured creditor outside the winding up without intervention of the Court. This Court pointed out that the law in England, and under the provisions of the Companies Act in India, was the same, namely, that the secured creditor had the right of realizing his security by standing outside the winding up, in which case he was not required to seek intervention

A of the Court.

The decision in *Ranganathan* (supra) held the field for considerable period, both under the Companies Act, 1913 and the Companies Act, 1956. However, by amending Act 35 of 1985, amendments were carried out in section 529 and a new Section 529A was enacted. These developments in our view, brought about a qualitative change in the legal situation. It is important to notice that *M.K. Ranganathan* (supra) was decided under the Companies Act, 1913 which did not have any provision corresponding to the proviso to Section 529 or Section 529A of the Companies Act 1956. Obviously therefore, *Ranganathan* could not have considered the impact of these amendments on the provisions of section 232 of the Companies Act, 1913 (corresponding to Section 537 of the Companies Act. 1956).

The Division Bench of the Bombay High Court has considered in detail the change in the legal situation brought about by these new legal provision in *Maharashtra State Financial Corporation v. Ballarpur Industries Limited*, AIR (1993) Bombay 392.

As a result of the proviso added in Section 529, the security of every secured creditor is deemed to be subject to a '*pari passu*' charge in favour of the workmen to the extent of the workmen's dues (called 'workmen's portion, as defined in sub-section (3)(c) therein. It is further provided that, where the secured creditor, instead of relinquishing its mortgage and proving his debt, opts to stand outside the winding up proceedings and realise his security, the Official Liquidator shall be entitled to represent the workman and enforce such charge and that any amount realised by enforcement of such charge shall be applied ratably by the Official Liquidator for the discharge of workmen's dues. It is true that even the amended proviso does not give the Liquidator an independent right of enforcing the charge by selling the security against which such charge is created. Nonetheless, it creates a '*pari passu*' charge in favour of the workmen to the extent of their dues and makes the Liquidator the representative of the workmen to enforce such a charge. By reason of Clause (c) of the newly added proviso, so much of the debt due to the secured creditor opting to realise security as could not be realize because of the specially created rights in favour of the workmen or the amount of the workmen's portion in the security, whichever is less, shall rank '*pari passu*' with the workmen's dues under Section 529A. Section 529A provides for overriding preferential payments of workmen's dues and unrealised portion of the secured creditors dues, as provided in clause (c) of

the proviso to Section 529.

Counsel for the SFCs contended that there is a conflict between the provisions of Section 529 read with Section 529A of the Companies Act on the one hand and Section 29 of the SFC Act on the other. It is urged that the provisions of the Companies Act being general law must yield to the provisions of the SFC Act which is special law. In the first place, we see no such conflict between the provisions of the Companies Act as amended in 1985 and the provisions of the SFC Act, 1951. In our view, the provisions of the SFC Act were merely intended to give an expeditious remedy to the SFCs without having to go through the procedure of enforcing the mortgage under the Transfer of Properties Act, 1882. In fact, even under Section 69 of the Transfer of Property Act, under certain circumstances a mortgagee has the power to sell the mortgaged property in default of payment of mortgaged money without intervention of the court. Under the general law, the SFCs would have to file a suit for realising their security unless they qualified under section 69 of the Transfer of Property Act. This meant considerable delay and holding up of the public monies due to the SFCs. In public interest, therefore, special provisions were made by Section 29, 30, 31 and 32 enabling the SFCs to take possession of the mortgaged assets and sell them without having to move a court of law. The provisions of Section 29 to 32 and the rights flowing thereon are exercisable under ordinary circumstances. However, when the debtor is a Company in winding up, the rights of the SFCs are affected by the provisions of the Companies Act, 1956. Looked at from this point of view, therefore, there is no conflict between the provisions of the SFC Act and the Companies Act. Assuming that there is conflict, then the judgment of this Court in *A.P. State Financial Corporation v. Official Liquidator*, [2000] 7 SCC 291 clearly holds that the amendments made in Section 529 and 529A would override and control the rights under Section 29 of the SFC Act. Though the Companies Act may be general law, the provisions introduced therein in 1985, were intended to confer special rights on the workers and *pro tanto* must be treated as special law made by Parliament. Since the amendments to the Companies Act were made by a later Act of 1985, they would override the provisions of section 29 of SFC Act, 1951. We are unable to accept the contention that the view taken in *A.P. State Financial Corporation* (supra) needs reconsideration. Far from it, we are in agreement with the view expressed therein.

The decision of the Bombay High Court in *Maharashtra State Financial Corporation* case (supra) gives weighty reasons as to why when the company

- A is under winding up the SFC to which the assets of the company are charged cannot proceed to realise the security without intervention of the Company Court. We have already noticed that as a result of the amendment to Section 529 a *pari passu* charge to the extent of the workmen's portion is created on the security of every secured creditor when he opts to realize a security by standing outside winding up. 'Pari Passu' means "with equal steps, equally, without preference" (Jowitt's Dictionary, Vol. II, 1959 Edition 1294). Black's Law Dictionary, 6th Edition, 115 defines it as 'By an equal progress... used especially of creditors who, in marshalling assets, are entitled to receive out of the same fund without any precedence over each other.' It is also defined as "With equal steps, that is to say, proceeding side by side at the same place" (Prem's Judicial Dictionary, Volume III, 1964 Edition, page 1217)
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The rights of the *pari passu* charge holders would run equally, temporally and potentially, with the rights of the secured creditors. The Official Liquidator, as the representative of the workmen, to enforce such *pari passu* charge would have the right of representing the workmen equally with the rights of the secured creditors. Charge is defined under Section 100 of the Transfer of Properties Act thus:

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- "Section 100-Where immovable property of one person is by act of parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property; and all the provisions hereinbefore contained [which apply to a simple mortgage shall, so far as may be, apply to such charge.]
- E

- Though the charge by itself may not amount to mortgage, all the provisions which apply to a simple mortgage, so far as may be, apply to a charge. Thus, the Official Liquidator, as the representative of the workmen's *pari passu* charge, would be in the position of a co-mortgagee. Though Section 29 hitherto enabled the SFC as a mortgagee to exercise its right thereunder by taking possession of the property and selling it in satisfaction of its debt, the situation has now changed. Because of the aforesaid statutory intervention, the SFC must necessarily contend with a *pari passu* charge holder who has equal rights. It is well established law that where there are co-mortgagees, one co-mortgagee cannot sell without consent of the comortgagee or institute any proceedings for sale of mortgaged property without joining the other co-mortgagees either as plaintiffs or as defendants. The SFC's right under Section 29 of freely realising its security gets trammelled if it has to take on a *pari passu* charge holder. The realisation of the security
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can thereafter only be done either by satisfaction of the *pari passu* charge or by a suit in which the *pari passu* charge holder would be a party defendant. Though when the SFC Act was enacted in 1951 it was intended that SAF could act unilaterally, the amendments made to the Companies Act in 1985 have introduced a *pari passu* charge holder as a co-helmsman of the ship of the SFC, who can neither be ignored nor overridden. In other words, the existence of the *pari passu* charge holder being represented by the Official Liquidator would necessarily bring in supervision of the Company Court as the Official Liquidator cannot act without directions from and supervision of the Company Court. This is precisely the reason why the judgment of this Court in *A.P. State Financial Corporation* (supra) holds that the statutory right of the SFCs to sell the property under Section 29 of the SFC Act is now subject to the provisions of Section 529 and Section 529 A of the Companies Act. The statutory right to sell the property under Section 29 of the Act has now to be exercised in tandem with the rights of *pari passu* charge in favour of the workmen created by the proviso to Section 529 of the Companies Act. This Court observed in *A.P. State Financial Corporation* (Supra):

“The Act of 1951 is a special Act for grant of financial assistance to industrial concerns with a view to boost up industrialization and also recovery of such financial assistance if it becomes bad and similarly the Companies Act deals with companies including winding up of such companies. The proviso to sub-section (1) of Section 529 and Section 529-A being a subsequent enactment, the non obstante clause in Section 529-A prevails over Section 29 of the Act of 1951 in view of the settled position of law. We are, therefore, of the opinion that the above proviso to sub-section (1) of Section 529 and Section 529-A will control Section 29 of the Act of 1951. In other words the statutory right to sell the property under Section 29 of the Act of 1951 has to be exercised with the rights of *pari passu* charge to the workmen created by the proviso to Section 529 of the Companies Act. Under the proviso to sub-section (1) of Section 529, the liquidator shall be entitled to represent the workmen and force (sic enforce) the above *pari passu* charge. Therefore, the Company Court was fully justified in imposing the above conditions to enable the Official Liquidator to discharge his function properly under the supervision of the Company Court as the new Section 529-A of the Companies Act confers upon a Company Court the duty to ensure that the workmen’s dues are paid in priority to all other debts in accordance with the provisions of the above section. The legislature has amended the

A Companies Act in 1985 with a social purpose viz. to protect dues of the workmen. If conditions are not imposed to protect the right of the workmen there is every possibility that the secured creditor may frustrate the above *pari passu* right of the workmen.”

B Since the Official Liquidator is in the position of a comortgagee, the SFCs cannot act independently or by ignoring him for enforcing their security. It is established law that, in case of co-mortgagees, all of them should join in the suit for enforcing the security, but if some of them refuse to join, they have to be included as defendants, not merely as perma parties, but as necessary parties inasmuch as the mortgage right vests in them along with the plaintiffs mortgages. (See in this connection the judgment of the Privy Council in *Sunitibala Debi v. Dharae Sundri Debi*, AIR (1919) PC 24). The same principle would be substantially true and applicable in the case of a mortgagee and a *pari passu* charge-holder over the same security for realising the security. The realization of the security can only be done by both the charge-holders joining and realising the security simultaneously. If a sale takes place, it can only be simultaneously for recovery of the claim of all *pari passu* charge holders and sale proceeds are required to be divided proportionately in the same proportion as their dues.

E In support of their respective contentions, parties have referred to and relied upon judgments of different High Courts. The view taken by the Bombay High Court commands itself to us. The Division Bench of the said High Court pointed out that, like a secured creditor, the official liquidator as a *pari passu* charge holder cannot independently bring the security to sale ignoring the secured creditor. He must, therefore, either obtain concurrence of the secured creditor for sale and take the Court’s sanction, or he can apply for sanction of the Court after notice to the secured creditor. In either event, the Court while granting sanction may impose appropriate conditions and give directions regarding the conduct of the sale, the fixing of the reserve bid, acceptance of the bid, confirmation of sale and distribution of sale proceeds.

G We cannot be unmindful of the fact that every creditor is interested in realizing the security only for his benefit and to the extent necessary for recovery of his outstandings. Prior to 1985 it might have been possible for a secured creditor under section 529 of the Companies Act, 1956, or its predecessor, section 232 of the Companies Act, 1913 as interpreted by this Court in *M.K. Ranganathan* case (*supra*), to opt to stand outside the winding up and realise the security by bringing it to sale. This was possible because

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the secured creditor had unrestricted right of standing outside the winding up and proceeding against the property mortgaged to him. Or, to put it in the words *Lord Wrenbury in Food Controller v. Cork*, (1923) AC 647 A, [as quoted in para 15 of *M.K. Ranganathan* case (supra)]:

“The phrase ‘outside the winding up’ is an intelligible phrase if used, as it often is, with reference to a secured creditor, say a mortgagee. The mortgagee of a company in liquidation is in a position to say “the mortgaged property is to the extent of the mortgage my property. It is immaterial to me whether my mortgage is in winding up or not. I remain outside the ‘winding up’ and shall enforce my rights as mortgagee”. This is to be contrasted with the case in which such a creditor prefers to assert his right, not as a mortgagee, but as a creditor. He may say ‘I will prove in respect of my debt’. If so, he comes into the winding up.”

Of course, even in such a situation, if the same property was mortgaged to more than one secured creditor, they had to either come to an agreement, or in the event of disagreement, there had to be a suit in which dissenting mortgagee had to be sued as a necessary party defendant. No doubt section 29 of the SFC Act was intended to place the SFCs on a better footing. But, in our view, this better footing is available only so long as the debtor is not a company or is a going company. The moment a winding up order is made in respect of a debtor company, the provisions of section 529 and 529A come into play and whatever superior rights had been ensured to SFCs under the provisions of the SFC Act are now subjected to and operate only in conjunction with the special rights given to the workmen, who as *pari passu* chargeholders are represented by the official liquidator. We are, therefore, of the view that the unhindered right hitherto available to the SFCs to realise their security, without recourse to the Court, no longer holds true as the right vested in the official liquidator is a statutory impediment to such exercise and has to be reckoned with. And since the official liquidator can do nothing without the leave or concurrence of the Court, all necessary applications must, therefore, come to the Company Court.

We do not really see a conflict between Section 29 of the SFC Act and the Companies Act at all, since the rights under Section 29 were not intended to operate in the situation of winding up of a company. Even assuming to the contrary, if a conflict arises, then we respectfully reiterate the view taken by the Division bench of this court in *A.P. State Financial Corporation* case (supra). This Court pointed out therein that section 29 of the SFC ACT

A cannot override the provisions of section 29(1) and 529A of the Companies Act, 1956, inasmuch as the SFCs cannot exercise the right under section 29 ignoring a *pari passu* charge of the workmen. It was observed in the judgment:

B “The proviso to sub-section (1) of Section 529 and Section 529-A being a subsequent enactment, the non obstante clause in section 529-A prevails over Section 29 of the Act of 1951 in view of the settled position of law. We are therefore, of the opinion that the above proviso to sub-section (1) of the Section 529 and Section 529-A will control Section 29 of the Act of 1951. In other words the statutory rights to sell the property under Section 29 of the Act of 1951 has to be exercised with the rights of *pari passu* charge to the workmen created by the proviso to Section 529 of the Companies Act. Under the proviso to sub-section (1) of Section 529, the liquidator shall be entitled to represent the workmen and force (sic enforce) the above *pari passu* charge.”

D This very contention based on the non-obstante clause in Section 46B of the SFC Act was rejected by pointing out that if the non-obstante clause in section 529A and section 46B of the SFC Act which was inserted in the year 1956. Far from taking a different view of the matter, we too are of the same view as has been taken in the judgment of this Court in *A.P. State Financial Corporation case* (supra).

E Similar view was taken by a Division Bench of the A.P. High Court in *Andhra Pradesh State Financial Corporation v. Electrothermic (P) Ltd. and Anr.*, (1986) Co. Cases 402 and a learned single Judge of the Punjab High Court in *Official Liquidator, Ravindra Pharmaceutical (P) Ltd. v. Haryana Financial Corporation*, (Company cases Vol. 98 p. 683).

F The Division Bench of the Gujarat High Court in C.A. No. 6303 of 1995 has, however, struck a discordant note. The Division Bench was impressed by the fact that in *M.K. Ranganathan* this Court had emphasised the right of a secured creditor to realize his security by standing outside the winding up of a company. It also emphasised that the proviso to section 529 of the Companies Act operates only where a secured creditor, instead of relinquishing his security and proving his debt, proceeds to realise his security. In the words of the Gujarat High Court “But the fact remains, it has yet been left at the option of the secured creditor to realise the security without proving his debt in the winding up proceedings.” This seems to be the linchpin of the reasoning.

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In our view, the reasoning of the Gujarat High Court that in case A
secured creditor does not opt to realise the security, the liquidator, by dint of
the proviso to section 529, does not become a charge holder in the estate of
the company so as to exercise the right of a simple mortgagee as envisaged
under section 100 of the Transfer of Property Act, appears to be non-sequitur,
secured creditor does not opt to stand outside the winding up but relinquishes B
his security and proves his debt in the winding up, then there is no doubt that
the official liquidator will come into custody of all the assets of the company
in liquidation and the distribution of the assets would have to proceed in
accordance with the provisions of section 529A of the Companies Act, in
which case the secured creditor stands in line as an unsecured creditor. It is
only when the SFC as a secured creditor opts stand outside the winding up C
and seeks to realise its security that the conflict, if any, can arise. We have
already indicated as to who must yield in such a clash of the titans. The fact
that the liquidator or the workmen do not have a right independently to
enforce the charge, unless the creditor decides to stand outside the winding
up, does not make any difference to the situation, in our view. It is not the D
contention of the SFCs that they do not desire to exercise the option available
to them of standing outside the winding up. In fact, it is their contention that
as mortgages they have a right to stand outside the winding up and are not
subject to the supervisory jurisdiction of the Company Court. They also
contend that, unlike other mortgagees, they have a special right by reason of
sections 29 of the SFC Act of taking possession of the assets and realising E
them by sale, transfer and so on. We are, therefore, unable to accept the
reasoning of the Gujarat High Court as correct.

Finally, counsel for the SFCs urge that the view we are to take would
obliterate the difference between a creditor opting to stay outside up and one F
who opts to prove his debts in winding up. We are unable to accept it. As
a result of the amendments made by the Act of 1985 in the Companies Act,
1956, the SFCs as secured creditors, must seek leave of the Company Court
for the limited purpose of ensuring that the *pari passu* charge in favour of
the workmen is safeguarded by imposition of suitable conditions under the
supervision of the Company Court. If this amount to impeding their hitherto G
unimpeded rights, so be it. Such is the Parliamentary intendment, according
to us. This impediment is of a limited nature for the specific purpose of
protecting the *pari passu* charge of the workmen's dues and subject thereto,
SFCs can continue to exercise their statutory rights as secured creditors without
being reduced to the status of unsecured creditors required to prove their
debts in insolvency and stand in line with other unsecured creditors. Neither H

A is the apprehension expressed justified, nor the contention sound.

We, therefore, hold as under :

1. The right unilaterally exercisable under section 29 of the SFC Act is available against a debtor, if a company, only so long as there is no order of winding up ;
2. The SFCs cannot unilaterally act to realise the mortgaged properties without the consent of the official liquidator representing workmen for the *pari passu* charge in their favour under the proviso to section 529 of the Companies Act, 1956.
3. If the official liquidator does not consent, the SFCs have to move the Company Court for appropriate directions to the official liquidator who is the *pari passu* charge holder on behalf of the workmen. In any event, the official liquidator cannot act without seeking directions from the Company Court and under its supervision.

In the result, Civil Appeal No. 4702/1994 and Civil appeal No. 4703/1994 are allowed and the Karnataka State Finance Corporation is directed to move the Company Court to seek appropriate directions in the matter. The judgment of the Division Bench as well as the single Judge permitting the SFC to sell the assets of M/s Raheja Development Corporation without the leave of the Company Court are set aside, with liberty to the KSFC to move the Company Court and seek appropriate directions in the matter of realization of its securities.

Civil Appeal No. 12928/1996 is dismissed.

Civil Appeal Nos. 6491/95 and 2007/97 are dismissed with the same liberty to the SFC to move the Company Court for further directions.

Civil Appeal No. 6303/1995 is allowed. The judgment of the Division Bench of the Gujarat High Court is set aside and the judgment of the Company Judge is upheld. The Gujarat State Finance Corporation has the same liberty for moving the learned Company Judge for appropriate directions for realisation of the sale proceeds of the assets.

All the aforesaid appeals are accordingly disposed of with no order as to costs.

K.K.T.

Appeals disposed of.