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REVIVAL OF A COMPANY UNDER LIQUIDATION

- UNDER THE COMPANIES ACT

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SOLICITORS AND ADVOCATES

MUMBAI I DELHI I BENGALURU I KOLKATA I AHMEDABAD

Introduction

Prior to the advent of the Insolvency and Bankruptcy Code, 2016 ("**IBC**"), financial distress caused on account of rising non-performing assets ("**NPA's**"), stressed assets and prolonged litigation plagued the banking sector in India. The Reserve Bank of India ("**RBI**") attempted to bring the defaulting companies out of difficulties through various reforms. However, the Sick Industrial Companies Act ("**SICA**"), the Companies Act, 1956 ("**Companies Act**") and other revival schemes which were provided by RBI proved to be futile.

A large part of such distress was attributable to the lack of a rational insolvency law relating to companies and the tedious mechanism of winding up of companies under the Companies Act. The inability to pay debts, led many creditors to file winding up petitions under the Companies Act, which would, on many occasions result in the winding up of the borrower companies. In such situations, the remedies available for creditors were, if secured, to either enforce their securities by standing outside winding up process and proceed under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 ("**SARFAESI Act**"), or give up their securities and participate in the winding up proceedings just like any other unsecured creditors by standing in queue with a hope to receive their dues upon the liquidation of the company's assets.

Although it was always preferable for banks and other financial institution to attempt a revival or a restructuring of a distressed borrower company rather than having the same wound up, which essentially spelled the (civil) death of the company, the scope to do the same was extremely limited.

SICA, which was an attempt at allowing restructuring and revival of such distressed companies, also failed to meet its objectives. Rather the borrowers used it to their advantage and legal proceedings came to be suspended. Keeping this in mind, long needed reforms relating to the revival/restructuring and if necessary, winding up of companies were introduced into law by way of IBC. SICA was repealed and the provisions relating to winding up of companies on the ground of inability to pay debts were also amended/deleted from the Companies Act, 2013.[1]

Thereafter under a notification dated December 7, 2016 issued by the Central Government, all petitions relating to winding up under the Companies Act before the High Court, which were not served upon the borrower, stood transferred to the National Company Law Tribunal ("**NCLT**").[2] This notification essentially created two classes of petitions, one set of petitions which were retained in the High Court and other set of petitions were transferred to the NCLT.[3]

On account of this, as SICA stood repealed, it was apprehended by the banks and financial institutions whose petitions were retained in the High Court that they could neither opt for the speedy and much favourably provisions under the IBC nor any remedies for revival or restructuring of the borrower companies under SICA. For many such banks and financial institutions, the revival of the borrower company could have been a more financially prudent option than to (i) seek liquidation of the company (ii) sale of the secured assets at distressed values or (iii) winding up of the company.

Some of these apprehensions have been now been settled by judgments of various High Courts as well as the Supreme Court. The judgments have dealt with issues where the winding up petitions are retained by the High Court; however, IBC proceedings could still be initiated against

[1] Central Government issued a notification no S.O. 3453(E) dated November 15, 2016 under Section 1(3) of IBC bringing into effect Section 255 of the IBC. The provisions related to winding up and continued to be governed by old Companies Act of 1956.
[2] Notification GSR 1119(E) dated December 7, 2016.
[3] *West Hills Realty* v. *Neelkamal Realtors Tower Private Limited*, 2017 (3) Mh.L.J.

such borrower companies. This provided an avenue for the creditors of such borrower companies to invoke all the benefits of the IBC, including an attempt at reviving or restructuring the borrower company.

However, there did not seem to be a remedy to the creditors of borrower companies against which the petitions were not only retained by the High Courts, but where a winding up order was already passed and an Official Liquidator had already been appointed.

The present paper seeks to analyse the options available to such banks and financial institutions, whose borrowers are already undergoing winding up under the Companies Act, to attempt a revival of the borrower company instead of having its assets liquidated.

Jotun India Private Limited v PSL Limited Company ("Jotun India") [4]

Numerous cases were filed across High Courts in the country which related to companies against whom winding up petitions remained before the High Court and did not get transferred to NCLT. One such case before the Hon'ble Bombay High Court is *Jotun India Private Limited* ("**Jotun**") v. *PSL Limited Company* ("**PSL**") filed on July 26, 2018.

The brief facts of which are as follows:

i. A winding up petition was filed by Jotun before the Bombay High Court on March 10, 2015 against PSL claiming an outstanding amount of Rs. 7.25 crores together with interest.
ii. PSL made a reference to the Board of Industrial and Financial Reconstruction ("**BIFR**") under SICA for restructuring themselves.
iii. Thereafter, the IBC was brought into force on May 28, 2016 and on December 1, 2016 and the SICA came to be repealed. Under the provisions of Section 4(b) of SICA, a company whose reference was pending before the BIFR as on December 1, 2016 was entitled to file an application under Section 10[5] of the IBC on or before May 31, 2017 (within a period of 180 days).
iv. On March 9, 2017, the company petition filed by Jotun came to be admitted by the company judge.
v. In accordance with the provisions of Section 4(b) of SICA, PSL filed an application before the NCLT, Ahmedabad Bench on May 29, 2017 under Section 10 of the IBC, within days as prescribed by SICA.
vi. On July 18, 2017, the application under Section 10 was taken up for hearing by NCLT, Ahmedabad Bench and reserved for orders. Jotun filed a company application before the Bombay High Court on the same day requesting for an appointment of a provisional liquidator, in accordance with the admission order dated March 9, 2017.
vii. On July 19, 2017, the company judge on hearing the company application filed by Jotun, restrained the NCLT Ahmedabad Bench from continuing with the Section 10 application. PSL then filed an application before the Bombay High Court to recall the order.

The Bombay High Court while deciding the matter, essentially observed that there is a definite purpose behind the legislature creating two classes of petitions, one set of petitions which are retained in the High Court and other petitions pending before the NCLT. The legislature did not intend to transfer all the petitions to NCLT. The court further recorded that the purpose of IBC and the NCLT hearing petitions is primarily to revive the company by having a resolution method. Whereas, in the winding up petition pending before the

[4] 2018 SCC Online Bom 1952.
[5] Section 10 of IBC: Initiation of Corporate Insolvency Resolution Process by Corporate Debtor.

company court, ultimate approach is to windup the company. NCLT is a separate and distinct forum and not a subordinate to the High Court.

The Bombay High Court eventually decided that the company court while dealing with winding up petitions which were not transferred to the NCLT, have no jurisdiction to injunct and stay the proceedings before the NCLT in respect of revival or resolution issue. In case the NCLT fails to revive or successfully implement the resolution plan, then the company court dealing with the winding up petitions (which were not transferred to NCLT) would deal with the petition in accordance to law.[6]

However, the position in Jotun India (*supra*) was that the winding up petition was pending hearing and final disposal before the Bombay High Court and the company had not been ordered to be wound up.

1. Whether the decision in Jotun India *(supra)* extended to cover companies against which final order of winding up is passed?

The answer is in the negative. In the case of Jotun India *(supra)* it was held that pendency of a petition before the High Court by itself would not in any manner trigger the applicability of the IBC and does not give a right to the creditor to invoke the proceedings under IBC. Jotun India *(supra)* did not consider a situation where a company had already been wound up in a non-transferred petition.

Upon a company being ordered to be wound up under the Companies Act the Official Liquidator is appointed as the liquidator of the company and all properties and assets of the company vests in the custody of the Company Court in accordance with the Act. These assets and properties are essentially then to be liquidated and the sale proceeds thereof are to be distributed in accordance with the provisions of the Companies Act.

If the decision in Jotun India *(supra)* is applicable to companies which are already ordered to be wound up under the Companies Act in a non-transferred petition, then it may lead to a confusing scenario as provisions under IBC are substantially different from the Companies Act. The objective of IBC is to attempt a restructure and revive the company as opposed to the provisions of the Companies Act.

The said view is also approved by other judgments of Supreme Court as well as various High Courts, which are discussed herein below.

***1.1. Jaipur Metals and Electricals Employee Organisation* v. *Jaipur Metals and Electricals Limited*, (2019) 2 SCC 227 ("Jaipur Metals")**

The Supreme Court in its judgment dated December 12, 2018 considered the question whether the Rajasthan High Court was right in refusing to transfer a winding up proceeding pending before it to the NCLT, but where no final order of winding up was passed.

[6] Paragraph No. 45 of Jotun India – **"***In view of the afore-stated reasoning and case laws cited, we are of the considered opinion that the Company Court while dealing with the winding up petitions (saved petition) shall have no jurisdiction to stay the proceedings before the NCLT in respect of revival or resolution issue. We may further state that in the forum under IBC, 2016 i.e. the NCLT fails to revive or successfully implement the resolution plan, then the Company Judge seized with the winding up petitions(saved petition) would deal with petition in accordance with law. We are of the view that allowing both the forums i.e. Company Court and NCLT to go ahead with the liquidation proceedings/ winding up proceedings simultaneously would not serve any purpose, There is a likelihood of creating of confusion and complexity. To harmonize this situation, we observe that the company Judge, in saved petitions, would exercise jurisdiction in case revival efforts by NCLT fails***"***.*

The facts of the matter in brief are as follows:

The borrower company had become a non-performing asset and the net worth had turned negative. A reference was accordingly made to BIFR under the SICA. The BIFR was *prima facie* of the opinion that the company ought to be wound up. This opinion was forwarded to the High Court. The High Court accordingly registered the case as a company petition. In the meantime, one of the worker's union filed a writ petition. The High Court in the writ petition directed the Official Liquidator to be provisionally attached to that court and join the evaluation of the value of assets lying in the factory premises of the company so that the dues of the workmen could be paid. In the meantime, an application under Section 7 of the IBC was filed before NCLT. Considering the fact that the debt was admitted by the company and no liquidation order had been passed in the winding up proceeding, the NCLT admitted the application and a moratorium was declared under Section 14 of the IBC. An Interim Resolution Professional ("**IRP**") came to be appointed. The High Court thereafter passed an order and set aside the order of the NCLT stating that it had been passed without jurisdiction.

This order of the Rajasthan High Court was set aside by the Supreme Court, which was of the opinion that the NCLT proceeding is an independent proceeding which has nothing to do with the transfer of pending winding-up proceedings before the High Court. The Supreme Court held that *"It was open for the creditor at any time before a "winding-up order is passed" to apply under Section 7 of the IBC. This is clear from a reading of Section 7 together with Section 238[7] of the IBC."*

1.2. Forech India v. *Edelweiss Asset Reconstructions Company Limited*, Civil Appeal No. 818 of 2018 ("Forech India")

In yet another judgment of the Supreme Court in Forech India, dated January 22, 2019,the question before the court was whether an application by a financial creditor under Section 7 of the IBC would be maintainable when a winding up petition is pending before the High Court. In this case as well, there was no final order of winding up passed.

The facts of the matter in brief are as follows:

A winding up petition was filed before the High Court on January 20, 2014. Notice on that petition was served. The financial creditor moved the NCLT under Section 7 of the IBC in 2017. In May to June, 2017 the said petition was admitted by the NCLT. Against the said order, an appeal was filed by the appellant before National Company Law Appellate Tribunal ("**NCLAT**"). It was held by NCLAT that since there was no winding up order passed by the High Court, the financial creditor's petition would be maintainable. As a result, the appeal was dismissed. This order of NCLAT was impugned in the Supreme Court. The relevant submission of the appellant was that the winding up proceedings before the High Court should continue and not proceedings filed by the other creditors under the IBC.

It has been held by the Supreme Court that an application before the NCLT is an independent proceeding which must be decided in accordance with the provisions of IBC unhampered by any winding up petition that may be pending.

[7] Section 238 of IBC: Provisions of this Code to override other laws -The provisions of this Code shall have effect, notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by virtue of any such law.

The Supreme Court approved the decision of the Bombay High Court in Jotun India (*supra*) and reiterated its earlier decision in Jaipur Metals (*supra*).

1.3. Sicom Limited v. *Hanung Toys and Textile Limited*, 2019 SCC Online Del 10399 ("Sicom Limited")

On September 30, 2019, the Delhi High Court considered two issues (i) whether in exercise of the powers under the provisions of Section 434 of the Companies Act, the High Court can transfer proceedings to NCLT even when an Official Liquidator has been appointed and (ii) whether an application under Section 7 or Section 9 of the IBC can be initiated before NCLT once the Official Liquidator is appointed.

The facts of the matter in brief are as follows:

The Delhi High Court deals with three separate applications for transfer of petitions from High Court to NCLT, in which the common factor was that the winding up petitions were admitted by the High Court and an Official Liquidator had been appointed. Three banks i.e. Punjab National Bank ("**PNB**"), State Bank of India and Dena Bank were the secured creditors of the borrower companies who filed applications under Section 7 of the IBC in the NCLT.

The NCLT heard the applications filed by the three banks and passed contradictory orders. In the first application filed by PNB, the NCLT admitted the Section 7 petition and appointed an IRP. This order was subsequently stayed by NCLAT. The second application was dismissed by the NCLT on the ground that an Official Liquidator has already been appointed by the company court. Similarly, the third application was also dismissed by the NCLT because a provisional liquidator was appointed by the company court.

The Delhi High Court, while deciding the applications to transfer the petitions from High Court to NCLT, analysed the decisions of the Supreme Court in Jaipur Metals (*supra*), where the Supreme Court had held that it was open to a financial creditor at any time before a winding up order is passed to apply under Section 7 of the IBC. The Delhi High Court also analysed the decisions of the Supreme Court in Forech India (*supra*) which reiterated the view of the Supreme Court in Jaipur Metals (*supra*) and also approved the view of the Bombay High Court in Jotun India (*supra*).

The Delhi High Court eventually held that, where an Official Liquidator is not appointed as the liquidator, the company court would transfer the petitions to NCLT. However, once an Official Liquidator is appointed by the company court in retained petitions, the process of liquidation commences. Then no purpose would be served by handing over the company under liquidation to another liquidator who would also perform a similar function all over again. This would set the entire effort of the Official Liquidator at naught which would not have been intended. Hence, once the court has appointed the Official Liquidator as the liquidator, normally such petition would not be transferred to NCLT.

Additionally, the Delhi High Court also held that once an Official Liquidator is appointed as a Provisional Liquidator, normally the whole exercise would still be at an initial stage and in these circumstances, normally, the court would transfer the matter to NCLT. This would also give an opportunity to try and revive the company by the IRP.

On a separate note, one of the company petitions forming the subject matter of the decision in Sicom Limited (*supra*), was company petition no. 518 of 2013 filed against M/s. Hanung Toys and Textiles Limited. Since PNB was seeking transfer of the winding up petition to the NCLT, after the winding up order was passed by the Delhi High Court, and an Official Liquidator was appointed who had taken symbolic possession of the borrowing companies' properties, the Delhi High Court rejected PNB's application. However, it appears that this order of the Delhi High Court has been dismissed by the NCLAT *vide* its order dated November 25, 2019 in *Ashok Kumar Bansal* v. *Punjab National Bank*,[8] by holding that the petition filed before the NCLT was maintainable in accordance with the view of the Supreme Court in Forech India (*supra*). The decision of the Delhi High Court is not referred to or discussed in the NCLAT order. The appeal filed against this decision of the NCLAT is pending before the Supreme Court. However, in our humble view, the view taken by the NCLAT does not seem to be a sound decision. As discussed above, from a perusal of the scheme of the Companies Act and the IBC, as well as the decisions discussed above, once an order of winding up is passed by the company court in the retained petitions, an application under IBC would not be maintainable.

Therefore, banks and financial institutions being creditors of companies already been ordered to be wound up cannot invoke the provisions of IBC. The banks and financial institutions may have to opt for other remedies under the Companies Act itself if they intend to seek a restructuring or revival of the borrowing company.

Remedy for banks and financial institutions in cases where a winding up petition is admitted.

One remedy which may be available to banks and financial institutions is stay of winding up before the company court under Section 466 of the Companies Act. The decision of the Supreme Court in *Meghal Homes (P.) Ltd.* v. *Shree Niwas Girni K.K. Samiti*,[9] which was subsequently followed by Bombay High Court in *Forbes & Company* v. *Official Liquidator*,[10] and the Gauhati High Court in *Jahnu Barua* v. *Aideopukhuri Tea Estate*,[11] held that the company court assumes complete charge of the company once winding up order has been made. Stay of winding up proceedings is provided for in Section 466 of the Companies Act, 1956. Section 466(1) states that the court may at any time after making a winding up order on an application made either by the Official Liquidator or of any creditor of the borrower company, and on proof to the satisfaction of the court that all proceedings in relation to winding up ought to be stayed, make an order staying such winding up either for a limited period or altogether on such terms and conditions as the court deems fit. There is no condition precedent prescribed for invocation of the power under Section 466 of the Companies Act. It lies in the discretion of the company court.

On such an application made under Section 466 before the Company Court to stay the winding up proceedings, the company court before granting any stay, considers the scheme for the revival or restructuring of the borrower company. The Supreme Court in Meghal Homes (*supra*) has also clarified that nothing stands in the way of a company court before the ultimate step is taken for winding up of the company or disposing the assets, to accept a scheme or proposal for revival of a company. The court has to see the *bona fides* of the scheme and ensure that the scheme is not a ruse to dispose off the assets of the company in liquidation and satisfies the elements of public interest and commercial viability.

[8] Company Appeal (AT) (Insolvency) No. 465 of 2019.
[9] (2007) 7 SCC 753.
[10] Company Application No. 243 of 2011.
[11] (2017) 3 Gauhati Law Reports 442.

Conclusion

Creditors of a company, which is finally been ordered to be wound up and where the Official Liquidator has taken possession of the company's assets, cannot take the benefit of the provisions of IBC.

Further, the plain language of Section 466 of the Companies Act states that "creditors" can file or apply under the provisions of Section 466 for stay of winding up. This can be done by proposing a scheme of revival of a company, if creditors are of the opinion that revival is better than winding up of the company. Restructuring and revival of a company, which is capable of being revived, can be an option available to such creditors, even if the scope of Section 466 of the Companies Act may not include everything that can probably form part of a resolution plan under the IBC.

Therefore, banks seeking restructuring or revival of a company already ordered to be wound up under the Companies Act may have the opportunity to seek restructuring or revival of company even though the benefits of the IBC may not be available to them. Banks may consider working together with all other creditors and propose a scheme under Section 466 of the Companies Act, which may be similar to a resolution plan under the provisions of IBC.

Even though it is not be a preferable remedy, it is an option available to such creditors, who cannot invoke the provisions of IBC.

This paper has been written by Ranjit Shetty (Senior Partner) and Priyanka Shetty (Senior Associate).

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