

-* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% *Judgment Reserved on : January 20, 2016*

Judgment Delivered on : January 29, 2016

+ **W.P.(C) 7876/2015**

M/S. ISPAT PROFILES INDIA LIMITEDPetitioner
Represented by: Ms.Manisha Dheer, Advocate with
Ms.Varsha Banerjee, Advocate
versus

APPELLATE AUTHORITY FOR
INDUSTRIAL AND FINANCIAL
RECONSTRUCTION & ORS.Respondents

Represented by: Mr.Arvind Kumar, Advocate with
Ms.Henna George, Mr.Karan
Khanna and Ms.Asmita Kumar,
Advocates for R-2
Mr.Arun Aggarwal, Advocate with
Mr.Taranjeet Singh, Advocate for
R-5
Mr.Sanjay Bhatt, Advocate with
Ms.Vidhushi Shubham, Advocate
for R-6
Mr.A.V.Rangam, Advocate for
R-7
Ms.Rama Ahluwalia, Advocate for
R-8
Mr.Rajiv Kapur, Advocate for
R-11
Mr.Shreyans Singhvi, Advocate
with Ms.Ekta Mehta and
Mr.Umrao Singh Rawat,
Advocates for R-12
Ms.Chetna Bhall, Advocate for
R-13

CORAM:

HON'BLE MR. JUSTICE PRADEEP NANDRAJOG

HON'BLE MS. JUSTICE MUKTA GUPTA

PRADEEP NANDRAJOG, J.

1. Way back in the year 1989 the petitioner commenced commercial production of steel products at its plant located in District Pune in the State of Maharashtra. It availed credit facilities from various banks and financial institutions such as IFCI, Indian Bank, State Bank of Bikaner and Jaipur, Dena Bank, State Bank of India, State of Bank of Hyderabad and ICICI Bank. Being a new unit, as per the policy of the State of Maharashtra, the petitioner was given a credit facility of collecting sales tax from the buyers of the product manufactured by the petitioner and paying the same to the State Government with a moratorium of ten years i.e. ten years sales tax collected could be paid in installments after ten years of commencement of the sale.

2. The net worth of the petitioner turned negative in the year 2000, and on September 30, 2001 the petitioner filed a reference under Sick Industrial Companies (Special Provisions) Act, 1985 before the Board for Industrial and Financial Reconstruction (BIFR). It was registered as Case No.50/2002. BIFR dismissed the reference as belated on June 17, 2003, which order was set aside by the Appellate Authority for Industrial and Financial Reconstruction (AAIFR) on November 08, 2005 and Case No.50/2002 was revived. On March 30, 2006 BIFR declared the petitioner a sick company and appointed IFCI as the operating agency to prepare a revival scheme, which in turn appointed M/s.M.N.Dastur & Co. as a consultant to submit a report regarding revival of the petitioner. M/s.Bhatwadekar & Co. were appointed as a valuer to submit a valuation report regarding assets of the petitioner. Consortium meeting of the bank was held on October, 2006, when in principal decision was taken to proceed for a onetime settlement requiring petitioner to submit a better onetime settlement proposal. Between June to September, 2007 the secured lenders considered a rehabilitation package offered by the

petitioner containing offer as to how it would like the debts to be restructured and paid. Matter thereafter lingered on. Interim orders passed by BIFR were repeatedly challenged before AAIFR resulting in proceedings lingering on till when BIFR passed an order on November 04, 2003 issuing a show cause to the petitioner as to why it should not be wound up under Section 20 of Sick Industrial Companies (Special Provisions) Act, 1985. As per the show cause notice the petitioner, its promoters and even outsiders were given an opportunity to submit a proposal for revival of the petitioner. There is haziness in the facts hereinafter and it is not clear whether the petitioner submitted any proposal afresh for revival of itself or any of its promoter gave a proposal for the revival of the petitioner. Order dated January 23, 2014 was thereafter passed by BIFR ordering winding up of the petitioner.

3. In ordering winding up of the petitioner, BIFR recorded the journey chartered before it after Case No.50/2002 was registered and that secured creditors did not accept the proposal submitted by the petitioner for a onetime settlement, nor did the petitioner submit a comprehensive report justifying its revival. It was recorded that it would be just equitable and in public interest to wind up the petitioner.

4. Challenge to the order dated January 23, 2014 failed before AAIFR when Appeal No.86/2014 was dismissed vide impugned order dated May 20, 2015.

5. AAIFR has noted that no serious attempt was made by the petitioner to either settle the disputes with secured creditors nor was a creditworthy report submitted for revival of the petitioner and that the liabilities has crossed ₹616 crores as per the audited balance sheet dated December 31, 2008. AAIFR has noted that apart from secured creditors and unsecured creditors use of State Electricity Board, Workers and Sales

Tax Department had accumulated. The Appellate Tribunal has noted that the claim of having settled the dues of IFCI and ICICI was a ruse because these dues had been assigned to two sister companies and thus in the balance sheets of the petitioner the liabilities remained. AAIFR has thereafter noted amounts due to the various creditors.

6. Admitting its liability as per the audited balance sheet referred to by AAIFR and conceding that thereafter, due to interest accumulating, the debts have arisen, argument of learned counsel for the petitioner was that a techno economic viability report submitted in July, 2003 by ANT Steel Engineers (Asia) Pvt. Ltd. has not been considered by AAIFR.

7. The report is at pages 223 to 281 of the writ record.

8. We have perused the report and would succinctly bring out that as per it the reasons for sickness were initial teething problem leading to quality control issues. The petitioner had to upgrade its equipment in the year 1994. Continuous recession in the market of steel products. So heavy was the recession that even basic cost of production could not be recovered. Increase in the cost of raw materials and especially power. Inadequate working capital facilities. As per the report there was a spurt in demand of steel items and the company could shift to manufacture Carbon, Alloy and Special Steel to take advantage of the Electric Arc Furnace and Laddle Furnace installed by the petitioner company because the Carbon, Alloy and Special Steel items could be sold at a premium. The report projects that these finished products could be consumed by the automobile sector which was growing. The report thereafter projects the demand of steel till the year 2019-20 and highlights a very rosy picture of how the petitioner could be revived. As per the report if ₹150 crores could be injected into the petitioner and the secured creditors agreed to waive off some past dues the company could be revived.

9. Dealing with revival report submitted to BIFR and AAIFR, since this Bench is coming across matters concerning whether BIFR and AAIFR correctly appraised the rehabilitation schemes, we need to transgress a little and speak about the rehabilitation reports. We find each one of them to be painting a rosy picture, without delving into the basic issues which must be highlighted in a report justifying revival of a sick unit. We thus propose to pen a few words on the subject.

10. Sickness in a unit does not occur overnight. The causes of sickness in a unit are manifolds, but generally:

(i). Fall in production. The causes which lead to decline in production are poor condition of machinery, low labour productivity, power shortage, lack of production planning and efficient control etc.

(ii). Poor cash management which includes diversion of funds to other areas, poor collection procedures, high inventory, increase in unproductive expenditure.

(iii). Increase in cost of production which is due to increased cost of raw materials, overhead costs, inefficiency in production, heavy borrowing with high burden of interest, lack of planning etc.

(iv). Liquidity constraint is the major cause of sickness in most companies. Inadequate or late sanction of working capital assistance by banks is a major cause of sickness. This leads to technical insolvency, i.e., a unit is not able to pay its debts on time, when it is due because of lack of funds.

(v). There is absence of financial sense. Operating expenses required to support production activity on hand is very high. Statutory and other liabilities make demands on revenues generated and so there is nothing left for the production process.

(vi). Over investment at the initial stages and the failure to appreciate technical complexities and build provisions to overcome these inevitably create working capital problems. The tendency to stretch resources too thin is also very common.

11. Therefore, any scheme for rehabilitation must state the specific problem area(s) requiring remedial action and must indicate a clear road map for implementing the future course of action.

12. To find the problem areas and the strength of the company, information has to be dug out. Balance sheets and income statements taken at face value hide interesting facts (Hartel, Robert. *Basics of Financial Management* Wm.C.Brown Publishers, College Division, 1986). These relevant facts have to be ascertained by making further elementary calculations. For example, the ratio of sales to inventory - the figure of inventory as such does not mean much. But if it is related to sales it can be more meaningful and more in-depth knowledge can be gained.

13. A company's assets and liabilities, revenues and expenses have limited value if stated at a particular time and in isolation. Evaluation is not possible unless compared with something. Ratios convert financial statements into a form which can be compared. For example, two balance sheets as such may be difficult to compare, but if one calculates ratios of each balance sheet, then the ratios can be compared. Thus, ratio analysis provides more complete information in greater depth and in a form which is easier to compare.

14. For a sick unit, revival whereof is contemplated, because the financial health of the unit has already put the unit on a ventilator, the oxygen for revival is adequate. The oxygen to which we have referred to is obviously the cash inflow. Therefore, it has to be ensured that the

scheme for revival reflects cash forecasts which is realistic, comprehensive, comprehensible and appropriate. Realistic, in the sense, that it should represent a sensible estimate of what the market will take, what the business will produce and what profit/return this will bring. Comprehensive, in the sense, that it should include assessments of the future levels of all those variables which are involved in the company's performance. By comprehensive we mean, in terms which all managers, producers, sellers, buyers and accountants can understand. Appropriate, in the sense, that the forecasts should be expressed in units which each manager recognizes and can use within his own sphere of activity.

15. It is recognized that various factors have to be taken into account while forecasting cash flows. The forecast period being the most important. Thus, the cash flows forecast has to be for a specified period. The selection of the period would depend upon the purpose of forecasting. Forecasts may be prepared to control daily cash disbursements or to compare annual changes in cash level. The time factor plays a significant role in choosing the forecast period. The three types of forecast periods are: (a) Capital period, (b) Budget period; and (c) Immediate period.

16. Capital period refers to a planning period beyond one year. This would not have a direct impact on daily cash receipts and payments. This is concerned with estimating the resources required for the next year to meet established goals. Budget periods are either quarterly or monthly cash related forecasts which are incorporated into the annual budget. The purpose behind this is to allocate funds and provide a control over the inflow and outflow of cash. Immediate period refers to daily or weekly forecasts of cash receipts and disbursements. The results are more immediate and action oriented. The actual can be compared with the

estimated figures simultaneously and immediate corrective action can be taken. There are different elements in a cash forecast. The term element is used to identify the parts or components that comprise a cash forecast. These elements are quantifiable and are directly related to the forecast result. If one of the elements contains a significant error in its estimation, it will be directly reflected in the forecast result. Decisions taken are related to the futurity of these elements. This deals with the time factor of elements. For example, maturity dates of securities, or the requirements of ready cash at a particular time needs to be synchronized. Matching and regulating the timing of inflows and outflows are very important. Each element has some degree of certainty and uncertainty which in turn affect the number of variables that require forecasting. Some of the elements of cash forecasting are deposits lying with the company. They need to be classified depending upon the period for availability purposes. Their maturity period needs to be known. Disbursements also have to be broken into time, i.e. when each payment has to be made or after what period. Cash has to be arranged for these payments. Inflows and outflows have to be synchronized. Maturing investments is another source of cash which can be matched with the timing of heavy capital expenditure. They have a high degree of certainty and are controllable.

17. A Scheme must focus on liquidity management.

18. Liquidity management has a broader perspective than cash management. Liquidity means the ability to generate cash to meet all cash demands, cash may be needed for operations, or for contingency or for an opportunity or for development purposes. Liquidity management permeates total operations of the firm including its sales, expenditures, investment and financing activities as it focuses at the total cash flows of

the firm arising from its total operations. Assets that can be converted into cash quickly contribute to the liquidity position. Liquidity does not only mean to generate cash from within but it also depends upon the borrowing capacity, that is, the ability to borrow cash when needed. Liquidity is not required only to pay debts but also to replace assets when they become obsolete or their value has been written off, or take advantage of favourable market situations. Low profits and wrong utilization of funds will lead to a disadvantageous liquidity position. Sufficient liquidity is a protection against default or payments due. At the same time it provides flexibility to the organization to take advantage of any new markets or opportunities. It focuses on the total cash flows arising from the total operations of the firm. It includes the processes of cash flow forecasting, budgeting, monitoring and control.

19. The scheme for revival has just not looked into, in any case does not give any clue, on an analysis of the balance sheets of the company there is no ratio analysis which is warranted by the jurisprudence concerning sickness and revival of companies. It is useless to highlight in a report that the installed production capacity is X and that estimated price at which the product could be sold is Y. The money generated would be XY and the cost of production including overhead expenses would be Z, which is less than XY.

20. The whole report is based on the assumption that the requirement of steel would rise in this country. The basis on which the assumption has been drawn is the growth in the automobile sector.

21. With respect to the assumption, we would only note the report released by the State Bank of India pertaining to manufacturing activity in the country dipping to a one year low in January of this year. The yearly SBI Composite Index in the country dipped to a one year low in

January suggesting moderation in growth. The composite index fell below the 50 marks to 47.3 in January – the lowest level in the past one year, indicating economic activity in recession; certainly not going forward. As per the report steel and textiles are some of the sectors that are *clear headwinds and thus need to be addressed head-on*. The plight of the steel industry could be highlighted with reference to the report which brings out that in Mandi Gobindgarh, in the State of Punjab, a major centre for iron and steel forging units, so severe is the recession that about 150 units have closed down in the last two years. As per the report the steel sector is *not looking good as of now* and there is no ray of hope in the near future.

22. This itself belies the rosy picture projected in the revival report submitted justifying putting the petitioner on a course of rehabilitation.

23. Hoping that in future BIFR and AAIFR would insist that the operating agencies file rehabilitation reports keeping in view the jurisprudence on the subject enunciated by us in paragraphs 10 to 18 above, we dismiss the writ petition for the reason the accumulated debts of the petitioner as of today have crossed at least ₹800 crores. The scheme for revival does not inspire any confidence.

24. No costs.

(PRADEEP NANDRAJOG)
JUDGE

(MUKTA GUPTA)
JUDGE

JANUARY 29, 2016
mamta