

IN THE HIGH COURT OF JUDICATURE AT MADRAS

Judgment reserved on	26.09.2019
Judgment pronounced on	16.10.2019

CORAM

THE HONOURABLE Mr. JUSTICE **SENTHILKUMAR RAMAMOORTHY**

O.P. No.421 of 2009

The Official Liquidator
High Court,
Madras,
Chennai - 600 104.

... Petitioner

Vs.

1.M/s. Infrastructure Leasing and Financial Services Ltd.,
Wescare Towers, III Floor,
No.16, Cenotaph Road,
Teynampet,
Chennai - 600 018.

... 1st Respondent/Respondent

2.Hon'ble Mr Justice A.S.Venkatachalamoorthy
The Arbitrator,
V-87, 5th Avenue,
Anna Nagar,
Chennai-600 040.

... 2nd Respondent

Prayer:- Original Petition is filed under Section 34 of the Arbitration and Conciliation Act, 1996 to set aside the Award dated 05.12.2007 passed by the Arbitral Tribunal.

For Petitioner : Mr.S.R. Sundar
Counsel for
The Official Liquidator
High Court Madras

For Respondents : Mr.K.Manoj Menon and
Mr.O.S Karthikeyan
for R-1

ORDER

The respondent before the Arbitral Tribunal is the Petitioner before this Court. By Arbitral Award dated 05.12.2007(the Award), all the claims made by the first Respondent/claimant in the arbitration were allowed and the said Award is challenged by filing the present petition.

2.The dispute between the parties arises out of a Term Finance Agreement dated 09.01.2006 (the Loan Agreement), Ex.C-4, relating to the sanction of financial facilities by the first Respondent to the Petitioner. Prior to that, it appears that the Asian Development Bank, Manila, had sanctioned a loan for a sum of US\$ 15 million to the first Respondent as per agreement dated 16.01.1995. Pursuant to the Loan Agreement, the first Respondent extended a term loan facility for a sum of US\$ 3.3 million to the Petitioner, which was required to be repaid in 10 equated half yearly instalments commencing from 30 May 1997 and ending on 30

November 2001. As security for the said financial facility, the movable capital equipment, plant and machinery of the Petitioner were exclusively hypothecated to the first Respondent in terms of a Deed of Hypothecation dated 09.01.1996 (the Original Hypothecation Deed), Ex.C-6. The assets that were hypothecated were described both generically and specifically in the schedule to the Original Hypothecation Deed. The charge over the aforementioned assets was duly registered with the Registrar of Companies, Coimbatore, by filing Forms 8 and 13, as required under section 125 of the Companies Act 1956 (CA 1956), Ex.C-7. In view of the inability of the Petitioner to repay the said term loan, a Supplementary Agreement was executed on 10.09.1996 (the First Supplementary Agreement, Ex.C-11, whereby the terms of repayment were revised. Around this juncture, a Deed of Hypothecation dated 25.09.1996 (the Modified Hypothecation Deed), Ex.C-14, was executed and the schedule thereto sets out the details of assets that were hypothecated both in generic and specific terms (the Hypothecated Assets). Once again, the modification of the charge over the assets was registered by filing Forms 8 and 13 (Ex.C-10) before the relevant Registrar of Companies. The record discloses that a Second Supplementary Agreement was executed on 10.07.1998, Ex. C-11, but in view of the continual default in repayment by the Petitioner, a notice of termination dated 28.09.2001 was issued whereby the financial facility was recalled and the Petitioner was called

upon to repay the sum of about Rs. 16.19 Crore. Upon failure by the Petitioner to make repayment as demanded, the first Respondent invoked the arbitration clause in the Letter of Offer dated 07.07.1995 (Ex. C-3) by letter dated 24.12.2001(Ex.C-19).

3.In view of the financial crisis faced by the Petitioner, a reference was made to the Board for Industrial and Financial Reconstruction (BIFR) but the attempted rehabilitation was unsuccessful. Eventually, by order dated 28.4.2004, in C.P. No.107 of 2001, the Petitioner was ordered to be wound up by this court. In the said proceedings, by order dated 7.2.2006, this Court appointed a sole arbitrator to decide the dispute between the parties. In the said arbitration proceeding, the first Respondent filed a statement of claim, wherein it made the following claims: (i) a sum of Rs.36,21,92,610 in US dollar equivalent as on 10.5.2006; (ii) interest on the principal sum of Rs.11,68,15,845 in US dollar equivalent at 18% per annum from the date of claim statement until the date of realisation; (iii) to direct the attachment and sale of the hypothecated machinery; and (iv) for costs. In order to substantiate its claim, the first Respondent adduced evidence through its witness, Mr.Gautham (CW-1), and exhibited 30 documents, which were given exhibit numbers C-1 to C-29A. The Petitioner herein did not lead either documentary or oral evidence. Upon consideration of the pleadings, evidence and the oral arguments, the

Arbitral Tribunal directed the Petitioner herein to pay the first Respondent the following: (i) a sum of Rs.36,21,92,610; (ii) interest on Rs.11,68,15,845, i.e. the principal amount at 12% per annum from 11.05.2006 till the date of realisation; (iii) the Petitioner's share of arbitrator's fees of Rs.1,55,000 with interest thereon at 12% per annum from 01.12.2007 till the date of realisation; and (iv) Rs.5 lakhs as costs. The said Award is under challenge in this proceeding.

4.I heard Mr.S.R.Sundar, the learned counsel appearing on behalf of the Official Liquidator, and Mr.Manoj Menon, the learned counsel appearing on behalf of the first Respondent. Mr.S.R.Sundar commenced his arguments by pointing out that the first Respondent had filed an application under Section 31 (6) of the Arbitration and Conciliation Act, 1996 (the Arbitration Act) wherein the Arbitral Tribunal was requested to pronounce an award for payment of the admitted sum of Rs.22,29,30,300/-. This application was rejected by order dated 08.01.2007 of the Arbitral Tribunal. By referring to the said order, he submitted that the claims made by the first Respondent should also have been rejected because the Official Liquidator was not in a position to verify the said claims and the only information that was available with the Official Liquidator was from the Statement of Affairs filed by the ex-directors, which reflected that a sum of Rs.22,29,30,300/- was due and

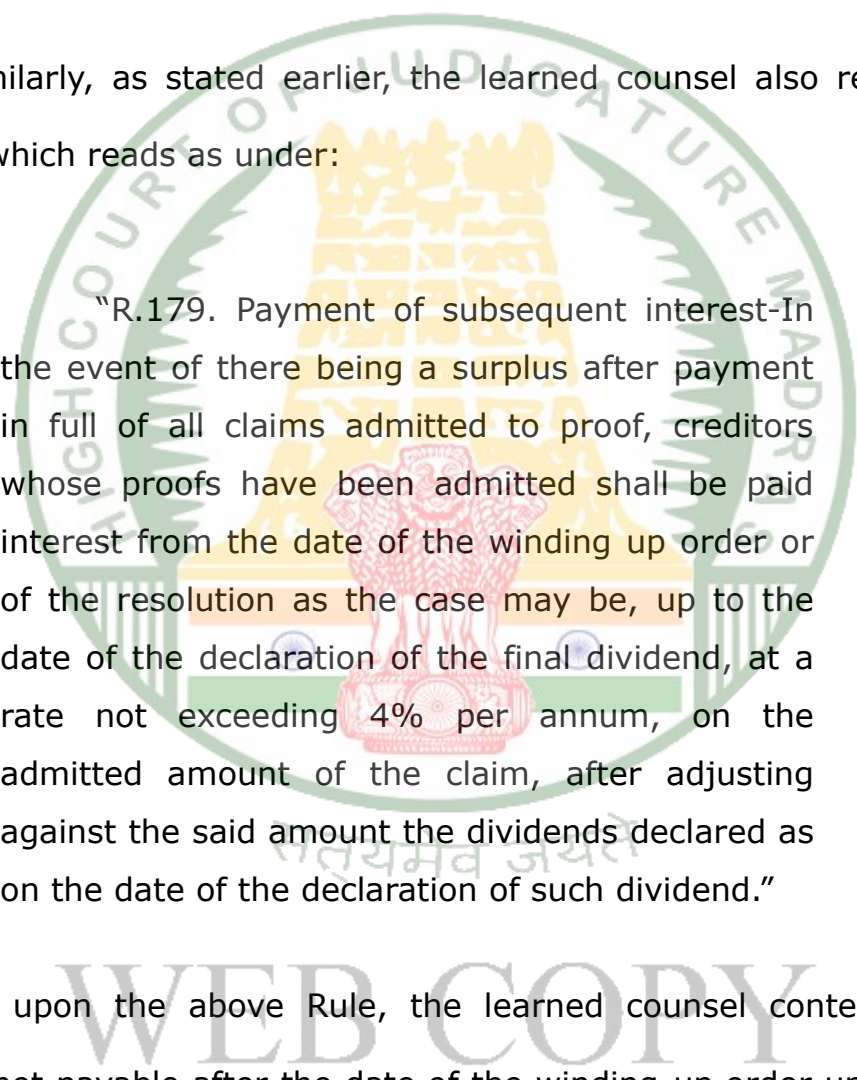
payable by the Petitioner to the first Respondent, but could not be verified and admitted by the Official Liquidator.

5.The learned counsel, thereafter, contended that the Arbitral Tribunal violated public policy by awarding interest at 12% per annum on the principal sum up to the date of realisation. In this regard, the learned counsel referred to Rule 156 and Rule 179 of the Companies Court Rules, 1959 (the Rules). According to the learned counsel, Rule 156 governs the payment of interest by a company in liquidation up to the date of the order of winding up whereas Rule 179 governs the payment of interest for the period commencing from the date of the order of winding up. Rule 156 reads as under:

"R.156. Interest.-On any debt or certain sum payable at a certain time or otherwise, whereon interest is not reserved or agreed for, and which is overdue at the date of the winding up order, or the resolution as the case may be, the creditor may prove for interest at a rate not exceeding 4% per annum up to that date from the time when the debt or sum was payable, if the debt or sum is payable by virtue of a written instrument at a certain time, and if payable otherwise, then from the time when demand in writing has been made, giving notice that interest will be claimed from the date of demand until the time of payment."

By referring to the above Rule, the learned counsel contended that not more than 4% interest per annum should have been granted by the Arbitral Tribunal up to 28.04.2004 and that the Award is liable to be set aside in this regard.

6. Similarly, as stated earlier, the learned counsel also relied upon Rule 179, which reads as under:



"R.179. Payment of subsequent interest-In the event of there being a surplus after payment in full of all claims admitted to proof, creditors whose proofs have been admitted shall be paid interest from the date of the winding up order or of the resolution as the case may be, up to the date of the declaration of the final dividend, at a rate not exceeding 4% per annum, on the admitted amount of the claim, after adjusting against the said amount the dividends declared as on the date of the declaration of such dividend."

By relying upon the above Rule, the learned counsel contended that interest is not payable after the date of the winding-up order unless there is a surplus and, even in such event, at a rate not exceeding 4% per annum. Once again, according to the learned counsel for the Petitioner, the award of interest at 12% per annum from the date of the order of

winding up up to the date of realisation is in contravention of Rule 179 and therefore, the Award is liable to be set aside in this regard.

7. In order to substantiate the above submissions, the learned counsel referred to and relied upon the judgments, which are set out below along with context and principle:

(a) **The Federal Bank v. Official Liquidator 2003 (1) ILR 572(the Federal Bank case)**, wherein, at paragraph 8, the Division Bench of the Kerala High Court set out the principles that apply with regard to the rights of a secured creditor in the context of a company in liquidation. In specific, it was held therein as follows:

"8 (vi). Secured creditor who stood outside the winding up proceedings and obtained decree can enforce the decree as against the assets and the ceiling with regard to payment of interest under Rule 179 would not apply in the case of those secured creditors and they are entitled to get interest as decreed by the civil court. In a case where there is no surplus after payment in full of all the claims admitted of proof, the creditors who stood outside the winding up proceedings as well as the secured creditors who fall under section 529 A would be treated alike to the extent of granting interest at the rate of 4% under Rule 179 of the Companies (Court) Rules. In a case where there is surplus amount after

satisfying the decree of secured creditors, including secured creditors who stood outside the winding up as well as those who covered under section 529 A read with Rule 179, secured creditors who obtained decree with interest at a rate more than 4% would be entitled to realise the said interest from the surplus amount. In such an event, even though there is surplus amount secured creditors covered under section 529 A are not entitled to demand in excess of 4%.

9.If we apply the aforementioned principle we may indicate leave was granted without any condition imposed under section 446 of the Companies Act. Further, if there being surplus amount after paying off all the claims admitted to proof and that the secured creditors covered by section 529-A could be satisfied fully with interest at the rate of 4%, the Official Liquidator is bound to honour the decree of the civil court. Contributories and other shareholders would be entitled to only rest of the amount after the decree is being satisfied fully."

(b) Haryana Financial Corporation vs. PNB Auto Ancillary (India) Ltd (in liquidation) (1994) 81 Comp.cas 588 (Delhi), wherein, at paragraphs 19 and 20, the Delhi High Court held that the claims of the secured creditor are payable up to the date of the order of

winding up and that the payment of interest for the subsequent period would be governed by Rule 179 of the Rules.

(c) **IDBI Ltd v. The Official Liquidator of Maharashtra Explosives Limited 2011 113 (4) Bom. LR 2213**, wherein, at paragraphs 21 and 24, the Nagpur Bench of the Bombay High Court held that the Official Liquidator is competent to restrict the claims of secured creditors by applying Rules 156 and 179 of the Rules.

(d) **AP State Financial Corporation v. Magna Hard Tempt Limited (in liquidation) (2008) 146 Comp.cas 254 (AP)**, wherein, at paragraph 15, the Andhra Pradesh High Court held that the liability of the company in liquidation to a secured creditor in respect of payment of principal and the contractual rate of interest can only be to the date of the order of winding up and not thereafter.

(e) **KFC v. The Official Liquidator, High Court of Kerala, ILR 1993 (1) 197**, wherein, the Kerala High Court held, at paragraph 10, that a secured creditor is entitled to get the claim admitted regarding interest only up to the date of winding up and that the payment of interest after that date will be governed by Rule 179 of the Rules.

(f) **S. Anthony Raj vs. A. Shanmugam (1994) 80 Company Cases 531 (Mad)(the Anthony Raj case)**, wherein, in the context of a claim by workmen, a Division Bench of this Court held that Rule 156

applies to such a claim and that interest should be granted at a rate not exceeding 4% per annum.

8.By relying upon the aforesaid decisions, the learned counsel for the Official Liquidator submitted that the Award is liable to be set aside in respect of the grant of interest at 12% from 11.05.2006 till the date of realisation. He also pointed out that the Official Liquidator had paid a sum of Rs. 53,11,845 to the first Respondent herein.

9.In response, the learned counsel for the first Respondent contended that the first Respondent is a secured creditor of the company in liquidation. Accordingly, he submitted that leave was granted to the first Respondent to prosecute its claim by standing outside the winding up. Consequently, he submitted that neither Rule 156 nor Rule 179 is applicable. Instead, he contended that the first Respondent's entitlement to interest is on the basis of the contract between the Petitioner and the first Respondent. Upon consideration of the relevant evidence, including the contract documents and the provision relating to interest as contained therein, he pointed out that the learned Arbitrator had granted interest at the contractual rate up to the date of the claim statement. With regard to the period subsequent thereto, he submitted that the learned Arbitrator had granted interest at the rate of 12% per annum, which is lower than the contractual rate.

10.He also pointed out that the learned counsel for the Official Liquidator had not made out any ground to interfere with the Award of the Arbitral Tribunal. In specific, he submitted that the learned Arbitrator considered the pleadings, documentary and oral evidence and the arguments of both sides and upon a reasonable appraisal of the evidence and by applying the terms of the contract, the Award was pronounced. As such, he submitted that no case is made out for interference with the Award either in respect of the principal amount or interest.

11.The records were examined and the oral submissions of both sides were considered carefully. The main focus of the arguments of the learned counsel for the Official Liquidator was on the grant of interest at the rate of 12% per annum by the Arbitral Tribunal. As stated above, the contention of the learned counsel for the Official Liquidator was that interest is payable at a rate not exceeding 4% per annum up to the date of winding up order as per Rule 156. In order to test this contention, it is necessary to closely examine Rule 156. Upon examining Rule 156, it is clear that it applies if "interest is not reserved or agreed for". By implication, it does not apply if interest is agreed upon in the contract out of which the debt arises. In this case, it is the admitted position that the debt arises out of the extension of financial facilities to the Petitioner by the first Respondent and that the relevant loan agreements specify a rate

of interest and a rate of penal interest. Therefore, Rule 156 is clearly inapplicable. Moreover, Rule 156 also refers to the right of a creditor to "prove for interest at a rate not exceeding 4% per annum up to that date from the time when the debt or sum was payable". This clearly indicates that even in cases where a rate of interest is not specified in the contract in question, Rule 156 only applies to creditors who participate in the winding up and submit their claims for adjudication by the Official Liquidator. Therefore, the contention of the learned counsel for the Official Liquidator with regard to the applicability of Rule 156 up to the date of the winding up order is rejected.

12. This brings us to the next contention relating to the applicability of Rule 179 from the date of the order of winding up. Once again, it is necessary to examine Rule 179 closely so as to decide this issue. Rule 179 states, inter alia, that "in the event of there being a surplus after payment in full of all the claims admitted to proof, creditors whose proofs have been admitted shall be paid interest from the date of the winding up order or of the resolution as the case may be, up to the date of the declaration of the final dividend, at a rate not exceeding 4% per annum, on the admitted amount of the claim...." This Rule also makes it clear that it is applicable to creditors whose proofs have been admitted. In other words, there is a clear indication that it only applies to creditors who participate

in the winding up by submitting Form 66 for adjudication by the Official Liquidator.

13. In this regard, even the Division Bench judgment of the Kerala High Court in the **Federal Bank case**, which was referred to and relied upon by the learned counsel for the Official Liquidator, makes it clear that Rule 179 does not apply to secured creditors who stand outside the winding up proceedings and enforce the decree against secured assets, whereas it provides that a decree can otherwise be enforced in respect of interest only in accordance with Rule 179. The judgment of the Division Bench of this Court in the **Anthony Raj case** is also distinguishable inasmuch as it deals with a claim by workmen and, therefore, it is not a case where a contractual rate of interest is specified. In that factual context, the Division Bench held that Rule 156 is applicable. I am unable to concur with the conclusions of the other High Courts, in the judgments cited by the learned counsel for the Official Liquidator, with regard to the applicability of Rules 156 and 179 to secured creditors who stand outside the winding up. As stated earlier, the text of the said Rules provide unambiguous evidence of the intention to apply the said Rules only where contractual interest is not specified, in the case of Rule 156, and with regard to both Rules 156 and 179, only where the creditor concerned, whether secured or unsecured, submits a claim for adjudication by the

Official Liquidator. Thus, the contention of the learned counsel for the Official Liquidator to the effect that interest should not have been awarded at a rate exceeding 4% per annum for the period subsequent to the date of the winding up order is also untenable. Consequently, both the grounds of challenge to the Award are rejected.

14. However, it is to be noted that the Hypothecated Assets of the Petitioner were brought to sale by the Official Liquidator and not by the first Respondent; nevertheless, the first Respondent asserted its right to enforce its security for purposes of realising its dues and certainly did not relinquish the security. The charge, including the modified charge, was also duly registered with the Registrar of Companies and is, therefore, enforceable against the Official Liquidator. Therefore, the first Respondent is in the position of a secured creditor who stood outside the winding up but permitted the Official Liquidator to sell the identified assets subject to the charge. The principles, in this regard, are set out in the judgment of the Hon'ble Supreme Court in **Jitendra Nath Singh v. Official Liquidator (2013) 1 SCC 462**. As such, the first Respondent is entitled to recover the amounts awarded only from the sale proceeds of the Hypothecated Assets, as described in the schedule to the Modified Hypothecation Deed read with the relevant Forms 8 and 13, after also ensuring that permissible expenses of the Official Liquidator in relation to

the Hypothecated Assets and the amounts due as per the pari passu charge of the workmen in respect of the workmen's portion of the said security are paid from such sale proceeds. However, if the sale proceeds of these assets are insufficient to realise the amount awarded, whether in respect of principal or interest, the claims of the first Respondent would be required to be decided in accordance with Section 529, 529-A and other applicable provisions of the Companies Act and, in such event, Rule 179 would apply. The relevant facts and documents with regard to the sale price of the Hypothecated Assets, the "workmen's dues", the "workmen's portion" in the Hypothecated Assets, etc. are unavailable. These aspects would be required to be considered while dealing with execution proceedings relating to the Award and no definitive conclusions can be recorded herein.

15. In fine, the Petition to set aside the Arbitral Award is dismissed subject to the observations made herein.

Speaking order
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Internet : Yes
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SENTHILKUMAR RAMAMOORTHY.J.,

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**Pre-Delivery Order
in
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