[2001] 45 CLA (Mag.) 83

Better late than never – Sick Industrial Companies (Special Provisions) Repeal Bill, 2001

AYAZ BILAWALA*

In the article below Shri Bilawala points out how "Sick Industrial Companies (Special Provisions) Act, 1985" was rendered ineffective by its section 22 and expresses the view that the proposal in the Companies (Amendment) Bill, 2001 to ask a new National Company Law Tribunal to deal with sick companies may not serve its purpose unless and until those who have been responsible for the sickness of the companies are also subjected to deterrent punishment. ❖❖EFW❖❖

Background

1. In the Finance Act, 2001, the Finance Minister, Mr. Yashwant Sinha proclaimed that the Sick Industrial Companies (Special Provisions) Act, 1985 ('the Act') would be repealed. Looking to the provisions of the Act, and bearing in mind the fact that the stress on the liberalisation of economic policies commenced from 1991 in our nation, it is indeed surprising that it has taken such a long time for the Central Government to discover the advantage of repealing the Act. The object of the Act was undoubtedly laudable but it failed to provide for appropriate measures against the persons responsible, where it was found that sickness was caused by factors other than circumstances beyond the control of the management. More often sickness was really caused by the dubious and manipulative acts of the persons responsible. This is a stark reality which after all had to be addressed.

1.1 *Bygone era of protectionism* - The Act belonged to an era of 'protectionism' which sought to keep alive the 'sick industrial companies' by injecting public funds, and by providing various concessions to the sick companies so as to make them viable in an attempt to save the public funds. But various steps, including amendments in the Act, over the last fifteen years have not altered the situation satisfactorily to either check industrial sickness or to find timely solutions for restructuring of the corporate sector. Nobody ever enquired why a particular industry had become sick, and whether sickness was wilfully induced or whether it was on account of factors beyond the control of management.

1.2 *Some deficiencies of the Act* – Many deficiencies were by and by noted in the operation of the Act which, inter alia, include the following :

- Slow pace of BIFR intervention
- Excessive protection of sick industries under section 22 of the Act providing for automatic stay of all proceedings
- Delays in winding up of sick companies, etc.

* *Advocate & Solicitor*

Misuse of the Act

2. In course of time, the Apex Court as well as High Courts and Tribunals in the country also came across cases where unfair advantage was sought to be taken of the provisions of section 22 of the Act by certain industrial companies feigning sickness. In the case of *Real Value Appliance* v. *Canara Bank* [1998] 29 CLA 434 (SC) the appellant, *i.e.*, Real Value Appliance had approached the Board for Industrial and Financial Reconstruction ('BIFR'), and filed a reference before the Board, but the aforesaid fact was not disclosed to the Bombay High Court, where the appellant was facing a recovery suit and liquidation proceedings. The appellant was repeatedly seeking adjournments before the Bombay High Court, while, on the other hand, it has approached the BIFR and filed a reference seeking to be declared a sick company. The appellant in its application before BIFR had, however, disclosed the pending proceedings against it before the Bombay High Court. The Supreme Court, after looking into the provisions of sections 15 and 22 of the said Act, held that a reference under section 15, and the registration of the case by the BIFR under the Act cannot be said to have become bad because of any conduct of the company before the High Court. Accordingly, the appellant was given protection and shelter under section 22. Taking advantage of the aforesaid decision, many companies by feigning took shelter under the Act and managed to prolong the proceedings pending against them before civil courts and the company courts to enjoy undeserved legal protection.

Problems of companies coming before BIFR/AAIFR only to wriggle out of commitments

3. The BIFR and the Appellate Authority for Industrial and Financial Reconstruction ('AAIFR') did pass appropriate orders against the industrial companies which had, inter alia, filed a reference under section 15 only with the oblique purpose of wriggling out of their commitments made before the High Court/civil court. The said authorities held that where a reference is made by companies by fraudulently manipulating and/or falsifying the accounts or for the oblique purpose of thwarting the due process of law, the application may *ispso facto* be rejected. The AAIFR in the case of *Madalsa International Ltd.* v. *BIFR* [1999] 35 CLA 279 allowed the holders of consent decrees to proceed with the execution of the decrees. Further, relying upon its earlier decision in the case of *Tejoomal Karbonless Papers Ltd.* v. *BIFR* [1998] 5 Comp LJ 603 and after considering the statements and objects of the Act, it held that if a reference is made by fraudulent manipulation or falsification of accounts or for thwarting the due process of law, the same can be straightaway rejected. Accordingly, the AAIFR rejected the case of the company.

3.1 *Consent decree is not coercion* - The Division Bench of Madhya Pradesh High Court in the case of *Redia Distilleries Ltd.* v. *AAIFR* reported in [2000] 38 CLA 56 also held that section 22 is not attracted where execution of consent decree is sought, as the same does not partake of the nature of coercive proceedings as contemplated under the Act.

3.2 *Supreme Court to rescue of creditors* – The Supreme Court came to the rescue of creditors and passed orders keeping in mind the effect of the provisions of section 22 of the Act. In the case of *Deputy Commercial Tax Officer* v. *Coromandal Pharmaceutical Ltd.* [1999] 25 CLA 10, the Apex Court held that statutory dues like stales tax, etc., which the sick industrial company is able to collect after the date of the sanctioned scheme legitimately belonged to the Revenue and cannot be and could not have been intended to be covered within the meaning of section 22. The Apex Court further held that a construction which is unfair, unreasonable and against the spirit of the statute should be avoided.

Courts had to repeatedly interpret section 22

4. The courts have been required to interpret section 22 on a number of occasions, particularly as various companies have misused and abused the provisions to take undue advantage and shelter under the Act. The BIFR in Case No. 53 of 2000 in the matter of *Rushabh Precision Bearings Ltd.* by its order dated 9th April, 2000 had one more occasion to deal with the company in default which had attempted to obtain shelter under the Act by fraudulent manipulation and falsification of accounts. In the instant case, the company, Rushabh Precision Bearings Ltd. had prepared two audited balance sheets on the same date by its auditors. One was filed with the BIFR demonstrating the company as 'sick' and the other was filed with its bankers, *viz.*, Union Bank of India showing a rosy and viable picture of management sustaining the business in an attempt to obtain further advances, and to defraud the public undertakings. The BIFR, while going through the papers, observed that the company had not come with clean hands before the Board and summarily rejected the application as not maintainable, and dismissed the reference filed by the company. In another Case No. 35 of 1999 in the matter of *N K Industries Ltd.*, BIFR by its order dated 23rd May, 2000 also rejected the application for reference as being not maintainable as the company had suppressed material facts from the BIFR. Thus, the courts and the BIFR have protected the public funds while interpreting section 22.

The Act no longer in tune with current economic policies

5. The Hon'ble Justice Shri B P Jeevan Reddy (as he then was) in the case of *Coromandal Pharmaceuticals Ltd.* (*supra*) observed how out of tune the Act had become with the economic policies being pursued in our country. The learned Judge observed that the Supreme Court had come across cases where unfair advantage was sought to be taken of the provisions of section 22 by certain unscrupulous companies and observed that the Act was not meant to breed dishonesty nor could it be so operated as to encourage unfair practices. The learned Judge further observed that where it is no longer advisable to keep alive inefficient and uneconomic industries by injecting public funds or in the name of safeguarding the employment of the workers, the said companies should be wound up. Keeping in mind the difficulties faced in the operation of the Act, the learned Judge urged the Government to bring about changes in

the Act which were needed with the advance of time.

Belated decision to repeal the Act

6. The Government has, however, taken more than four years after the above decision to come out with the Sick Industrial Companies (Special Provision) Repeal Bill, 2001 (hereinafter referred to as 'the Bill') to finally repeal the Act. However, the task of rehabilitating sick units is proposed to be entrusted to the National Company Law Tribunal to be constituted by amending the Companies Act, 1956 on the basis of the recommendations of Justice Eradi Committee. The Bill envisages the dissolution of the BIFR and the AAIFR. All proceedings pending before the BIFR and the AAIFR prior to their dissolution shall also stand abated.

The Companies (Amendment) Bill, 2001

7. Separate action is being initiated by the Department of Company Affairs to introduce the Companies (Amendment) Bill, 2001 for giving effect to the recommendation of the Justice Eradi Committee. The salient features of the Companies (Amendment) Bill, 2001 are as follows :

• A National Company Law Tribunal will be set up. The powers and jurisdiction presently being exercised by various bodies, *viz.*, Company Law Board or BIFR or AAIFR or High Courts will now be consolidated and vested in the Tribunal. Thus, multiplicity of litiga-tion before various courts or quasi-judicial bodies or forums regarding revival or rehabilitation or merger or amalgamation or winding up will be avoided as all these matters will be heard and decided by the proposed National Company Law Tribunal.

• All the parties will be bound by the Tribunal's orders and in case of non-availability of a workable proposal for revival or rehabilitation, etc., the Tribunal can decide the matter on merits including introduction of its own scheme.

• The Tribunal shall work through Benches. There shall be ten special Benches which will deal with the matters relating to revival or reconstruction or rehabilitation or winding up of companies.

• This will reduce the entire process, which is presently taking several years in winding up of the companies, to about two years or so.

• Stripping of assets of sick companies will be avoided.

• Since individual affidavits will be filed with the National Company Law Tribunal which will have powers of contempt of court, there will be an in-built seriousness in the new legislation.

Conclusion

8. The new provisions may not, however, be very effective unless steps are taken to ensure that stringent measures are initiated to fix the civil and criminal liability of those who had been responsible for the sickness and other problems of the companies which have so far been under BIFR's umbrella. Such action may, among other things also deter others from resorting to similar maladministration/malpractices.