

Winding Up of Industrial Company

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Introduction to SICA

Background of SICA

During the eighties with the pervasive Industrial Sickness around the nation, the Government of India to overcome this determined problem enacted a special and distant legislation specifically for these sick industry, “the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA)” (hereinafter the Act) with the provisions which were essential to be taken in relation of sick industrial companies which were -formative, corrective, precautionary, ameliorative, and remedial in nature. The provisions were exclusively framed for the sick industrial company.

“Sick industrial company” means an industrial company (being a company registered for not less than five years) which has at the end of any financial year accumulated losses equal to or exceeding its entire net worth.”¹

“It is explanatory in itself from the above definition that an industrial company, which at the end of any financial year, has, accumulated losses equal to or exceeding the entire net worth of the company would be termed as a sick industrial company.”

The stance of the Act was – *“securing the timely detection of sick and potential sick companies owning industrial undertakings, the speedy determination by a body of experts of the preventive, ameliorative, remedial and other measure which need to be taken with respect to such companies and the expeditious enforcement of the measures so determined and for matters connected therewith or incidental thereto”²*. The Act been enacted with a stated purpose that is -*“reviving ‘sick’ companies by referring them to the Board for Industrial and Financial Reconstruction (BIFR) constituted under the Act.”*

The objective were very vivid ,if executed in the best possible way they would have been resulted in economical benefits thereby giving the “sick company” new horizons after their revival and thus helping the sick industry to execute and prosper after their rehabilitation .

The Act was in public interest with the twin objective of

- “securing the timely detection of sick and potentially sick companies”
- “speedy determination and enforcement of remedial measures”³

But it was unfortunate, that the Act was been used adversely and was rather misused than been executed properly, by the company in order to escape from paying off the debts.

Failure of the SICA, 1985 –

¹ Section 3(1)(o) of the Act .

² Brief Introduction of BIFR and its functioning, available at <http://bifr.nic.in/introduction.htm> last visited 3/13/14

³ Purnima Mishra, The Provisions of SICA & Companies Act. Available at - http://www.icaiejournal.org/Journal/792_2004_3.pdf last visited 3/11/2014

- 1) “BIFR as was set up under SICA started to function from 1987 thereby to deal with the revival and rehabilitation of sick Industrial companies, but in definite performance the intact procedure became very dawdling, slow and sore for all the authentic stakeholders and this prolonged process, under the BIFR, with the absence of judicious commencement of proceedings and pitiable enforcement mechanism the entire objective notion behind the Act was badly defeated.
- 2) Secondly, for defaulting borrowers who wanted to escape from the gateway of repayment BIFR became a rescue point, which was a safe haven and they took shelter under the BIFR with an intention to get statutory protection from the creditors who were wanting and had their legal right and interest to recover their dues.”⁴ Companies perceived SICA as an official exit route, which not only saved them from the harsh legal proceedings but also gave access to various relief and concessions from the financial institutions.

*“It was found that that more than being interested in reviving the sick industrial undertakings, Companies was keener to get the shelter of the overriding provisions of the SICA as a shield against the legitimate dues of the creditors and other stakeholders.”*⁵

These difficulties under the Act resulted in an unfavorable and adverse economic impact as the intent of revival and rehabilitation under the Act could not be fulfilled and in most of the cases the creditors got knotted in the procedural of SICA.

As some companies started to perceived SICA as an official exit route, thereby resulting into losses to creditors and increased NPA’s in the banking sector SICA, 1985, the Act was repealed by sick industrial companies (special provisions) Repeal Act, 2003.

*“The new Act has made an attempt to remove the bottlenecks and curb the practice of turning an operationally fit company into a sick unit”.*⁶

Essential Features of SICA

The meaning concept and role of BIFR

It is provided with in the ambit and jurisdiction of the Act, that a, Board and Appellate Authority for Industrial and Financial Reconstruction shall be constituted under Section 4 of the Act.⁷

The Board of experts named BIFR was set up in January, 1987 and functional with effect from 15th May 1987. The Appellate Authority for Industrial and Financial Reconstruction (AAIFR) was constituted in April 1987. Government companies were brought under the purview of SICA in 1991 when extensive changes were made in the Act including, inter-alia, changes in the criteria for determining industrial sickness.⁸

⁴ Pavan Kumar Vijay, Revival & Rehabilitation of Sick Companies – A Paradigm Shift, available at http://cpadvocates.in/Dynamicimages/260_1_843634656122018437500.pdf last visited 3/12/14.

⁵ Pavan Kumar Vijay, Revival & Rehabilitation of Sick Companies – A Paradigm Shift, available at http://cpadvocates.in/Dynamicimages/260_1_843634656122018437500.pdf last visited 3/12/14.

⁶ Purnima Mishra, The Provisions of SICA & Companies Act. Available at - http://www.icaiejournal.org/Journal/792_2004_3.pdf last visited 3/11/2014

⁷ Section 4 (1) with effect from such date as the Central Government may, by notification, appoint, there shall be established a Board to be known as the "Board for Industrial and Financial Reconstruction" to exercise the jurisdiction and powers and discharge the functions and duties conferred or imposed on the Board by or under this Act.

⁸. Brief Introduction of BIFR and its functioning, available at <http://bifr.nic.in/introduction.htm> last visited 3/13/14

Reference to the Board. (Section 15)

It is been made obligatory for the Board of Directors of the sick company that they should file a reference under Section 15 of SICA on corrosion of entire net worth of the company of the preceding financial year . When the reference is been filed, the BIFR is then empowered to initiate an enquiry to examine the sickness status of the company.

“When an industrial company becomes sick, a duty is cast upon the Board of Directors of that company under Section 15(1) to, that the Board within sixty days from the date of finalization of the duly audited accounts of the company for the financial year as at the end of which the company has become sick industrial company, make a reference to BIFR for determination of the measures which are to be adopted in respect of the said company.”

Under the section 15(2) a reference to BIFR can be made either by the Board of Directors of the company itself or by the Central Government, RBI etc.

“As per the provisions Section 15(2), the Central Government or the Reserve Bank or a State Government or a public financial institution or a State level institution or a scheduled bank may, without prejudice to the requirement of the Board of Directors of an industrial company which has become sick to make a reference to the BIFR within Section 15(1), can also make a reference in respect of a company in respect of which there are sufficient reasons to believe that it has become a sick industrial company”.

Further Section 16 is also significant and, its provisions can be implicated as follows –

“A plain meaning of Section 16(1) implies that the BIFR is been instituted to seek into the inquiries which determine the Sickness of the industrial company i.e. whether the company is sick or not. In its sub clauses it provides that what shall be the criteria to determine that the inquiry shall be held,- “it can be either on a receipt of reference been made under Section 15, or upon any information been received with respect to such company it can be done even on its own motion having any such knowledge as to the financial condition of the company.”

Section 16 (2) empowers the Board that –an operating agency can enquire into and make a report with respect to such matter as may be specified in the order, and act provides the provision for completion of the inquiry within 60 days of the commencement of the inquiry under Sec 16 clause 3 .

Section 17 empowers the Board to make suitable order on the completion of inquiry for the sickness of the company.

“This section provides that after the sickness of the company is been determined the Board shall after making the due considerations shall make an order that whether it is feasible for the company to make its net worth exceed the accumulated losses within a reasonable time [17(1)], for this purpose the Board shall order restrictions or conditions. [17(2)]”

That if Board is of the view that it is not practically possible for the company to exceeds it accumulated losses within reasonable time and for public interest it is necessary it is important to adopt some measures, the company shall soon order any operating agency to prepare schemes as provided under Section 18 so as to minimize the economical losses of the creditors, which can be

- Financial reconstruction
- Proper management.
- The amalgamation of the sick company with a solvent company ,
- The sale or lease of a part or whole of any industrial undertaking of the sick industrial company,
- Any other appropriate measures.

Rehabilitation and revival of the Sick Industrial Company –

SICA provides for obtaining their consent to the draft scheme where the Scheme provides for financial assistance by way of loans and advances, guarantees or relief and concessions or calls upon them to make sacrifices in relation to financial assistance already granted by such entities [sections 19(1) and (2)]. Once the process under sub-section (2) of section 19 is over, the scheme becomes binding on all concerned.

The provision of the rehabilitation is been provided under Section 19 of the Act , which basically provides that – “the scheme may provide financial assistance , from the state or central government or any financial institute operative under the government if such an initiative aids in preventive, ameliorative, remedial scheme for the sick industrial company .

This scheme shall be financial only after it has been circulated and due consent has been provided by the person giving the financial assistance, within 60 days of the circulation.[section 19(2)]

Winding up - (Sec 20)

The salient features of Section 20 of SICA are as follows:⁹

1. “When the due inquiry under is been made as per Section 16 and after the due consideration been made to the concerned parties, it is been found by the BIFR that the sick industrial company is not likely capable of making accumulated losses exceed the net worth in a reasonable time and it is not likely to become viable in future and as such it is just and equitable to wind up the company, BIFR may record and forward its opinion to the concerned High Court.
2. Then the High court may order the winding up of the company as per the companies act.
3. The High Court may appoint any officer as the liquidator having all the powers of, the official liquidator under the Companies Act, 1956.
4. The High Court is bound to order the winding up of the company on the basis of the opinion of BIFR.
5. Once BIFR forwards its opinion to the connected High Court, the role of BIFR comes to an end in respect of the said sick industrial company.
6. The BIFR has the power to direct the sale of assets of the sick industrial company in such manner as it may deem fit.”

The Supreme Court in *V R Ramaraju v. Union of India & others*

In relation to Section 20(2) of SICA held that the High Court in deciding the question of winding up of the company has to take into account the opinion of BIFR forwarded to it and is not to abdicate its own function of determining the question of winding up.¹⁰

Adding clarity to the end of jurisdiction of BIFR and beginning of jurisdiction of High Court, the

Division bench of the Karnataka High Court in *BPL Limited, Bangalore v. Inter Modal Transport Technology Systems (Karnataka) Limited, Bangalore (in liquidation) & others*

⁹ Seen GENERALLY KPC Rao., Revival / Close Down Of Sick Companies Through Sick Industrial Companies Act. 1985 (Sica) Rout, Perils and Pitfalls available at <http://businessandmanagementarticlesofkpcrao.blogspot.in/2013/04/revival-close-down-of-sick-companies.html>

¹⁰ KPC Rao., Revival / Close Down Of Sick Companies Through Sick Industrial Companies Act. 1985 (Sica) Rout, Perils and Pitfalls available at <http://businessandmanagementarticlesofkpcrao.blogspot.in/2013/04/revival-close-down-of-sick-companies.html>

It was held-“ that the scheme of SICA as contained in Sections 22, 22A, 20 and 32 of that makes it clear that from the date of commencement of an inquiry in regard to any reference received under Section 15, till passing of an order of winding up by the High Court under Section 20(2) of SICA, BIFR retains absolute control over the affairs of the company and can either prevent any sale or permit any sale and the sick industrial company is entirely governed by the provisions of SICA. On the other hand, hand, once an order of winding up is made by the High Court under Section 20(2) of SICA, acting on the opinion of BIFR under Section 20(1), the control and jurisdiction over the company, its affairs and assets passes over to the High Court and BIFR, ceases to have any power to pass any orders or give any directions.” The division bench further held that the company court does not sit in appeal over the orders of BIFR nor exercise power under Articles 226 and 227 of the Constitution. The apex court held that the sale of assets of a company by a secured creditor as per directions of BIFR, prior to the date of winding up order, is not void for want of leave of the court and there is no question of obtaining any leave or permission of this court.”

Sick Company Under Company Act 2013.

Sick (industrial) Company revival & rehabilitation related legal provisions in India have been made at par with developed countries under chapter XIX of The Companies Act 2013 section 253 to 269, the new company act has more advanced ruling on this aspect.

The company law's provisions have even changed the definition of the Sick industrial company, The new Company Act instead of the previous “net worth erosion”, has used the to inability to pay dues to creditors within 30 days of the demand itself would prove that the company has become a sick company.

The new provisions are incorporated in such a way as to overcome the fault and difficulties which existed in the setup, it provides for more harsh and rigorous liability to the directors which comprises in itself an imprisonment of 7 year and or fine up to Rs 10 lacks , the time management has also become prudent , and all the activates at each stage has to be done and managed timely ,ranging from determining the company as a sick company or sanction of revival of company or to wind up sick company all activities have to be completed within the stipulated time frame .

The Sick Company Revival and Rehabilitation legal provisions under chapter XIX are as follows:

Determination of Sickness of Company. (253)

The Act has given the Secured creditors the right to apply to the Tribunal an application to determine the Sickness of the company; no such provision prevailed under the Company Act 1956, or the SICA Act. Section 253 (1) “secured Creditors having 50% share in the outstanding debts of the company whose claim are unpaid even after 30 days from the notice can apply to the tribunal in the prescribed manner along with the relevant evidence for such default, non-repayment or failure to offer security or compound it, for a determination that the company be declared as a sick company. The creditors may also apply for stay of the proceeding, for winding up of the company, or execution, distress or the like against any property and assets of the company, or for appointment of a receiver in respect of any property and assets of the company, or for enforcement of any security against the company.

The tribunal may pass an order which shall be operative for 120 days.

The provision also empowers the Central Government, or the Reserve Bank of Indian, or the State Government, or a public financial institution, or a state level institution, or a schedule bank to file

reference before the Tribunal provided that they have sufficient reasons to believe that the company became a sick industrial company.

Further the time period is also been prescribed under the Act, the tribunal shall, within a period of sixty days of the receipt of any application, determine whether a company is a sick company or not.

The Section also incorporates in itself the provisions of repayments of the debts which is the most important aspect of entire philosophy of the insolvency laws, this has been left upon the tribunal to decide then whether the company may make repayment of its debt within a reasonable time or not, and when it is been decided that the company shall repay the debt the tribunal in writing shall prescribe the time period.

Once a company is determined as a sick company by the Tribunal under 253, any secured creditor of the company or the company itself may make an application to the Tribunal for determination of measures for revival and rehabilitation of the company, the application been so made shall be accompanied by financial statement, prescribed scheme and fees and a draft scheme of revival and rehabilitation. This application shall be made to, the tribunal within 60 days from the determination of the sickness of the company.

Application for Revival and Rehabilitation (Section 254):

As the tribunal determines the sickness of the company, an application by the secured creditors can be made for the Revival and Rehabilitation of the company.

The reference shall subsist if the secured creditors representing three – fourths in value of the amount outstanding against financial assistance disbursed to the borrower have taken measures to recover their secured debt under sub – section (4) of Section 13 of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002.

No reference shall be made if the secured creditors representing three – fourths in value of the amount outstanding against financial assistance disbursed to the borrower have taken measure to recover their secured debt under sub – section (4) of Section 13 of the SARFAESI Act.

No such application shall be made without consent of the securitization or reconstruction company, where the financial assets of the sick company had been acquired by such Securitization Company or Reconstruction Company under sub – section (1) of the Section 5 of (SARFAESI) ¹¹

A special an exclusive fund for the purpose is also been maintained under the act under Section 269.

Appointment of administrator. (Sec 256)

For the execution of the work in proper manner an interim administrator is been appointed under section 254, by the Tribunal, and a date is also been fixed for the hearing. The tribunal shall furthermore issue such other directions to the interim administrator it Tribunal may deem fit to initiate to protect and preserve the assets of the sick company it has to be taken into consideration by the interim administrator whether it is or not possible to revive and rehabilitate the sick company, and shall assert the measures to be taken for this purpose within 60 days of the application.

This interim administrator shall under section 257 appoint a Committee of creditors with not more than 7 members giving representation to each class of creditors..

¹¹ Seen generally - SICK COMPANIES (Companies Act, 2013) available at <http://aishmghrana.me/2014/02/04/sick-companies-companies-act-2013/> last seen 12/3/2014 .

Winding up of the Sick company (265)

If the scheme of sanction is not approved by the creditors, the administrator shall “submit an report to the Tribunal within 15 days, and thus an order of winding up of the company shall be passed by the tribunal .the proceeding shall be similar to those as provided under chapter XX of the Act.”

Comparison between SICA and company Act provision .

The provisions relating to the revival and rehabilitation of sick companies has been underwent commendable changes under the company act 2013, more apt worth laws are been framed and enacted which tunes in with the global laws on bankruptcy. The new laws modified and thus they suit more with the revival and rehabilitation of the Sick Company.

The comparative provisions of the SICA, 1985 and Chapter XIX of Companies Act 2013 relating to revival and rehabilitation of sick companies are presented in the following table.¹²

S.No	Basis	SICA provisions	Companies Act 2013
1	Reference	Section 15 provides that – Reference can be made either by Board of Directors, or Central/State Government, Reserve Bank of India, public financial institution, State level institution or a Schedule Bank.	Section 253 clause 1 provides – “Reference can be made by the secured creditors of the company representing 50%of its outstanding amount of debt; the company has failed to pay within 30 days of the notice of payment.
2	Tribunal /appellant tribunal	BIFR/AAIFR	.NCLAT/NCLT.
3	Definition	Any industrial company being registered for 5 yrs, which at the end of the financial year has more accumulated losses exceeding the net worth is a sick company.	There is no per se definition been provided under the Act , the tribunal has to declare the status of sickness of the company within 60 days of the application been made ,
4	Potentially Sick Industrial company	Section 23 provides that if the accumulated losses of the industrial company at the end of the financial year has resulted in erosion of 50 % or more of its peak net worth during immediately preceding 4 financial year such company shall be a sick company ,	No such provisions are there.
5	Interim administrator	No provision for the appointment. An operating agency was appointed	The provisional of appointment is been incorporated in the Act and is

¹² Seen generally , Pavan Kumar Vijay, Revival & Rehabilitation of Sick Companies – A Paradigm Shift, available at http://cpadvocates.in/Dynamicimages/260_1_843634656122018437500.pdf last visited 3/12/14. Seen also Satwinder singh Revival and Rehabilitation -Legislative Changes & Challenges, available at <http://www.icsi.edu/portals/70/328092013.pdf> last seen 3/12/2014 ,

			been given powers even to take over the management.
6	Committee of creditors	No such committee was established under the act .	Such an committee is been appointed by the interim administrator which shall comprise of 7 members representing the each class of creditors.
7	Measures to be adopted for the revival of the sick company	No provision corresponding to section 254(3) were there.	Section 254 (3) are - As the company has been determined as a sick company after the reference is been made , an application within period of 60 days to the tribunal for the determination Of the measures to be taken for the revival and rehabilitation shall be taken.
8	paramount effects of SURFACI	Section 15 of the Act corresponds to the principles of the Act	Similar under company act its section 253.
9	Takeover of the industrial company	No such provision	Any solvent company can take over the sick industrial company .u/s 261 (2)(d)
10	Punishment and penalties	Whosoever violates the provisions of the Act , makes or gives false evidences to the authority – Shall be punishable with imprisonment of 3 yrs which may be coupled with fine	Whosoever violates the provisions of the chapter XIX , makes or gives false evidences to the authority or attempts to tamper with records . Shall be punishable with fine of Rs 10 lacks and imprisonment of 7 yrs.

Conclusion

In no way a sick company can continue, Board or the tribunal has to make changes as per the position of the company. The schemes can be adopted by the operating agency or the sick company can go for revival or rehabilitation, and when there is no scope for these alternatives to prosper the sick company is finally winded up.

The law and procedures for handling of insolvency remain outdated and not at all in tune with the changing needs of the economy but Winding up of industrial company has underwent certain changing with the enforcement of the Company Act 2013, the provisions which have been incorporated attempts to overcome the problems which prevailed under the SICA, the new provisions are more defined and enhanced so as to work in furtherance of revival and rehabilitation of the sick company.

The provisions like power to the creditors for making a reference, or appointing an interim administrator or the takeover of the sick company by another solvent company, which are beneficial in the revival of

the sick company are now incorporated in the Company Act, which will be a catalyst in creating a law-friendly image of India at an Global Platform in order to retain the investors, creditors and faith of all stakeholders of the corporate sector.

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