Patna High Court
In Re: Chotanagpur Banking ... vs Unknown on 21 August, 1958
Equivalent citations: AIR 1959 Pat 288
Author: K Sahai
Bench: K Sahai
ORDER K. Sahai, J.

1. The question which arises for consideration in this case is whether this Court should order the winding up of a Bank named Chotanagpur Banking Association Ltd. (hereinafter to be referred to as the Bank) or direct that the scheme of composition put up by the Bank under Section 391 of the Companies Act, 1956, be considered by the creditors and share-holders of the Bank at meetings to be held for the purpose.

2. The Bank filed an application in this Court on 6-1-1958, praying for an order of moratorium under Section 37 of the Banking Companies Act (X of 1949), It was not accompanied with a report from the Reserve Bank as required by Sub-section (2) of the section. Acting under the proviso to that sub-section, however, I granted moratorium and called for a report from the Reserve Bank on the affairs of this Bank. By my order dated 14-1-1958, I appointed a Special Officer to take over charge of the assets of the Bank.

In accordance with my order, the Reserve "Bank submitted a report dated the 14th March, stating that there was no reasonable chance of the Bank paying its debts within the period of six months beyond which the order of moratorium could not last. On the 17th March, the Bank filed an application proposing a scheme under Section 391 of the Companies Act, 1956, and praying for an order that the scheme be considered by the creditors and shareholders at meetings to be held in accordance with the directions of this Court.

The Chotanagpur Banking Depositors' Association (hereinafter called the Depositors' Association) filed an application on the 17th April, praying that an order for the winding up of the Bank be passed. The order of moratorium was rescinded in view of the Reserve Bank's report on the 22nd April. On the same date, a number of depositors, who are represented by Mr. S. C. Ghose, filed an application, supporting the scheme proposed by the Bank and suggesting some modifications in it.

The Special Officer could not remain in charge of the Bank as the order of moratorium had been rescinded. With the agreement of all the parties who appeared before me on 13-5-1958, therefore, I appointed the Official Liquidator attached to this Court as the Provisional Liquidator of the Bank on that date, and directed that he should take charge of all its assets and affairs. He is accordingly in charge.

3. I may mention that one Sri Abdul Hai Khan filed an application dated the 13th May, praying for an order for him to be added as a petitioner along with the Depositors' Association in the application dated the 17th April. By my order dated 6-8-1958, I have rejected that application.

4. Before proceeding to discuss the points which arise for decision, I consider it necessary to ascertain the financial position of the Bank. In its original application of 6-1-1958, the Bank stated that it stopped payment from the 3rd January, and that it was temporarily unable to meet its obligations. Although the Reserve Bank was primarily concerned with the question whether the Bank would be able to meet its obligations within the maximum period for which moratorium could be granted, it has, in its report dated the 14th March, given a clear picture of the Bank's assets and liabilities. It has balanced the assets and liabilities of the Bank in Appendix I, and has discussed in its report the items mentioned in that Appendix. It has also attached several other Appendices.

5. (After discussion of the evidence His Lordship proceeded): On a consideration and analysis of the Reserve Bank's report with the Appendices, I am quite satisfied that the assets of the Bank do not exceed the sum of Rs. 91,45,000. They are, therefore, short of the liabilities by Rs. 21,35,000.

6. The first point which Mr. Das has argued is that the application filed by the Depositors' Association for winding up dated 17-4-1958, is not legally entertainable because the Association is not a legal entity. Section 439 of the Companies Act 1956 (hereinafter referred to as the new Act) gives a list of those who can apply for the winding up of a company. No attempt has been made on behalf of the Depositors' Association to show that it is a legal entity or that it is one of the parties in the list given in that section. It must, therefore, be held that its application is not maintainable.

7. Mr. Das has next argued that this is a fit case in which this Court should exercise its power under Section 391 of the new Act and order a meeting of depositors and shareholders to be held For consideration of the scheme of composition proposed by the Bank. He has submitted that the procedure has been laid down in Section 391 of the new Act, which is equivalent to Section 153 of the Indian Companies Act, 1913 (hereinafter referred to as the old Act), and Section 45 of the Banking Companies Act, 1949. The provisions of those sections, when read together, show that the procedure in such cases is as follows:

1. Firstly, the Court has to consider whether the scheme is fit to go to creditors or share-holders or both for consideration and then, in exercise of its discretion, to order meetings of those persons to be called, held and conducted in accordance with its directions.

2. If the requisite majority under Sub-section (2) of Section 391 does not approve of the shcheme, the matter is at an end. If, on the other hand, the lequisite majority approves of it, the petitioner for sanction of the scheme, if the company concerned is a banking company, must obtain a certificate from the Reserve Bank in writing to the effect that the scheme is not incapable of being worked and is not detrimental to the interests of the depositors under Sub-section (1) of Section 45 of the Banking Companies Act before the scheme is put up before the Court for its sanction. If the Reserve Bank does not issue a certificate as required, the Court will be powerless to confirm the scheme,

3. When the scheme relating to a Banking company is put up along with the Reserve Bank's certificate for sanction before the Court, it may direct the Reserve Bank to make certain enquiries under Sub-section (2) of Section 45. On receipt of the report if such enquiries are ordered, or without any report if enquiries are ordered, the Court has to consider the scheme, and, if it thinks

proper, it may sanction it. In deciding the question of sanction, the Court will attach due weight to the opinion of, the majority but will not be bound by it. After sanction, the scheme will be binding on the company, its creditors, share-holders and others who are concerned.

8. I am satisfied that the procedure as I have detailed it above and the order of the different stages are correct. This is supported by the views expressed in Bengal Bank Ltd. v. Suresh Chakravarty, 55 Cal WN 206: (AIR 1952 Cal 133), a decision in which the procedure was discussed.

9. Appearing on behalf of some depositors and share-holders, Mr, Lalnarayan Sinha has contended that this Court is bound, under Section 38 of the Banking Companies Act, to order the winding up of the Bank, and it is not open to it to entertain the scheme proposed by the Bank. He has also argued that, even if is open to this Court to sanction the scheme in the circumstances of this case, the scheme is quite worthless, and it will be a sheer waste of time to send it for consideration to the creditors and share-holders.

On the other hand, Mr. Das has argued that it is legally open to this Court to confirm the scheme as proposed, and that the proper course to adopt at this stage would be to send it for consideration to the creditors and share-holders. Mr. S. C. Ghose has argued a different point. His contention is that the Court cannot order the winding up of the Bank in the absence of a legally entertainable application for the purpose. Neither of them has advanced any argument on the interpretation and scope of sub-ss. (1) and (3) of Section 38 of the Banking Companies Act.

10. It is necessary first to consider the true scope of Sub-section 0) of Section 38 of the Banking Companies Act. That sub-section reads:

"Without prejudice to the provisions contained in Section 162 or Section 271 of the Indian Companies Act, 1913 (VII of 1913), and without prejudice to its powers under Section 37, the High Court shall order the winding up of a banking company if it is un-able to pay its debts and the High Court shall also order the winding up of a banking company if the Reserve Bank applies in this behalf to the High Court."

Section 162 of the old Act is equivalent to Section 433 of the new Act. I am not concerned in this case with Section 583 of the new Act which is equivalent to Section 271 of the old Act. Section 37 of the Banking Companies Act gives power to the High Court to grant moratorium for a fixed period of time which cannot extend beyond six months.

11. Section 433 of the new Act lays down six circumstances in which the Court may order a company to be wound up. One of those circumstances as given in Clause (e) is that "the company is unable to pay its debts." It is to be noticed that this section gives a discretion to the Court to order or. not to order winding up of a company not only in the other circumstances mentioned in the section but also in the case of inability of the company concerned to pay its debts.

12. The language used in Section 38(1) apparently makes it mandatory for the Court to order the winding up of a banking company in two cases:

(1) if the banking company is unable to pay its debts; or (2) if the Reserve Bank applies for winding up. Sub-section (2) of the section lays down the circumstances in which the Reserve Bank may make an application. This does not arise for consideration as the Reserve Bank has not filed any application. Sub-section (3) lays down when a banking company is to be deemed to be unable to pay its debts.

13. The question which has now to be considered is whether the opening words "Without prejudice to the provisions contained in Section 162" in Section 38(1) leave undisturbed the discretion vested in the Court by Section 433 of the new Act to order winding up of a banking company in any of the circumstances mentioned in that section. The word used in Section 38(1) is 'shall,' and I have no doubt that its provisions are mandatory.

The effect or the opening words of this section, which I have just quoted, is that no restriction is placed upon the discretion of the Court to order or not to order winding up in the circumstances other than that contained in Clause (e) of Section 433 because Section 38(1) is confined only to that clause. There is an obvious inconsistency between the powers of the Court as conferred by Section 433 and those conferred by Section 38(1) of the Banking Companies Act in a case where the Bank concerned is unable to pay its debts.

Section 616 of the new Act lays down, among other things, that the provisions of that Act "shall apply (b) to banking companies, except in so far as the said provisions are inconsistent with the provisions of the Banking Companies Act, 1949 (X of! 1949)." This does not leave any room for doubt that a provision of he Banking Companies] Act is to prevail in the case of a banking company, where there is an inconsistency between a provision made in it and a provision made in the Companies Act.

In my judgment, therefore, the discretion given to the Court under Section 433 of the new Act is taken away by Section 38(11 of the Banking Companies Act where a banking company is found to be unable to pay its debts, and, in that case, it becomes obligatory for the Court to order the winding up of that company.

14. Section 38(1) came up for consideration before a Bench of the Calcutta High Court in Dwarkadas v. Dharam Chand, AIR 1954 Cal 583. Chakarvartti, C.J. with whom Sarkar, T. concurred, has, while referring to Section 38(1), observed:

"There can be no doubt that the section is most clumsily drafted and does no credit to the draftsman. The only reasonable and sensible meaning that can be spelt out of it is that the opening words preserve the discretion of the Court only in cases specified in Clauses (i) to (iv) and Clause (vi) of Section 162, but so far as Clause (v) is concerned, namely, a case where a company is unable to pay its debts, the provisions of Section 38(1), Banking Companies Act must prevail in the case of a banking company".

15. That case was decided before the new Act came into force, and, as I have said above, Section 616(b) of that Act leads one to the same conclusion. There is no inconsistency between the two Acts

in so far as Clauses (a) to (d) and (f) of Section 433 of the new Act equivalent to Clauses (i) to (iv) and (vi) of Section 162 of the old Act are concerned, and hence, the discretion given to the Court in respect of the circumstances mentioned in those clauses is preserved by the opening words of Section 38(1) of the Banking Companies Act.

16. Unfortunately, the case of Vastulal Pareek v. Moolchand has not been fully reported; but a gist of the principles laid down in that case has been given in AIR 1955 NUC (Raj) 4680 (V. 42). It appears that the Bench in that case also took the view that, under Section 38, Banking Companies Act, the Court is bound to order the winding up of a banking company if it is unablle to pay its debts unless the Court takes action under Section 37 of the same Act.

17. The next question which I propose to consider is whether, in the circumstances of this case, the Bank can be held to be unable to pay its debts. For an answer to this question, it is necessary to construe and consider the scope of Sub-section (3) of Section 38 of the Banking Companies Act which runs:--

"(3) Without prejudice to the provisions contained in Section 163 of the Indian Companies Act, 1913 (VII of 1913), a banking company shall be deemed to be unablle to pay its debts if it has refused to meet any lawful demand for payment made at any of its offices or branches within two working days, if such demand is made at a place where there is an office, branch or agency of the Reserve Bank, or within five working days, if such demand is made elsewhere, and if the Reserve Bank certifies in writing that the banking company is unable to pay its debts".

Section 163 of the old Act is equivalent to Section 434 of the new Act. The opening words of subsection (1) of Section 38, which I have already quoted, leave unaffected the provisions of Section 433, and the opening words of Sub-section (3) show that the sub-section does not affect the provisions of Section 434.

Hence, the first impression which I formed was that the legislature intended that, for the purpose of Clause (e) of Section 433, a company would be deemed to be unable) to pay its debts in the circumstances referred to in Section 434, and that, for the purposes of Sub-section (1) of Section 38, a banking company would be deemed to be unable to pay its debts in the circumstances mentioned in subsection (3) of that section. On fuller consideration, however, I have come to the conclusion that my impression was wrong.

There are several reasons which support this conclusion. Firstly, there is nothing in Sub-section (1) of Section 88 to suggest that the expression "unable to pay its debts" as used in this sub-section limited to the circumstances covered by Sub-section (3), nor is there anything in Sub-section (3) to suggest that it is only in the circumstances given in that section that a banking company can be held to be unable to pay its debts.

18. Secondly, reference may be made to Section 2 of the Banking Companies Act which reads:-

"2. The provisions of this Act shall be in addition to, and not, save as hereinafter expressly provided, in derogation of, the Indian Companies Act, 1913 (VII of 1913), and any other law for the time being in force".

Hence, the circumstances mentioned in section 38(3) as Heading to the conclusion that a banking company is unable to pay its debts must be held to be in addition to and not in derogation of the circumstances given in Section 434 as leading to the same conclusion.

19. Thirdly, I may refer only to one of the circumstances mentioned in Section 434. The relevant circumstance is contained in Sub-section (l)(c) which may be quoted:-

"(1) A company shall be deemed to be unable to pay its debts-

(c) if it is proved to the satisfaction of the court that the company is unable to pay its debts, and, in determining whether a company is unable to pay its debts the court shall take into account the contingent and prospective liabilities of the company."

It seems to me to be manifest that, under Section 434 (1) (c) a company must be held to be unable to pay its debts if its liabilities exceed its assets. In such a case, this company is permanently unable to pay its debts. This circumstance is not included in Sub-section (3) of Section 38. The only circumstances which are given in that Sub-section are (1) that the banking company is unable to pay its debts in certain cases for two days and in certain other cases for five days and (2) that the Reserve Bank certifies in writing that the banking company is unable to pay its debts.

These circumstances do not necessarily imply permanent inability on the part of the Bank to pay its debts. It will be extremely unreasonable to hold that the court is bound to order the winding up of a banking company when it is temporarily unable to pay its debts within the meaning of Section 38(3) and the Reserve Bank issues the required certificates but the court is not bound to order its winding up if it is permanently unable to pay its debts.

20. For the reasons given above, I am satisfied that Section 38 (1) is applicable when the Banking company is unable to pay its debt either within the meaning of Section 434 of the new Act or within the meaning of Section 38(3) of the Banking Companies Act. This view is fully supported by the decision in the case of AIR 1954 Cal 583, (supra).

21. The use of the words "without prejudice to its powers under Section 37" in Section 38(1) shows that the High Court must take one of two actions if it finds that a Banking Company is unable to pay its debts. It can grant moratorium, if it is of opinion that the inability of the Bank concerned to pay its debts is temporary and if the other conditions of Section 37 are complied with. Such an order of moratorium can only continue up to the maximum period of six months. If the High Court is of opinion that the Bank's inability is not temporary, or if the Reserve Bank's report shows that moratorium will not serve any useful purpose, it has no option but to carry out the mandate given in Section 38(1) and to pass an order for winding up.

22. I have already analysed the financial position of the Bank as it is apparent from the Reserve Bank's report. I had granted moratorium under section 37 to the Bank; but, finding from the Reserve Bank's report that it would be unable to pay its debts within the period of six months, I had to cancel it. As I am fully satisfied that the liabilities of the Bank substantially exceed its asserts, I am bound to order its winding up.

23. I may also mention that there will be definite advantages if a winding up order is passed. As I have shown, more than half of the realisable assets of the Bank consist of secured and unsecured advances made to other persons. In the ordinary course, the Bank will have to undertake costly litigations in order to secure decrees against its debtors and it may take a very long time for it to realise the decretal amounts even alter decrees are passed. Under sections 45B, 45C and 45D and Sub-section (3) of Section 45T, the proceedings for realisation of the- debts due to the Bank will entail little expenses and will be much easier and quicker when the Bank is being wound up.

24. I have next to consider Mr. Ghose's argument that this court has no power to pass an order for winding up in the absence of an application. He has first referred to Section 439 of the new Act which lays down that an application for the winding up of a company shall be by a petition presented by the different parties enumerated in it. He has argued that where the legislature intended to give power to the court to act suo motu, it has expressly said so. In support of this argument, he has drawn my attention to Sub-section (2) of Section 45k of the Banking Companies Act which is as follows:-

"(2) If the High Court is satisfied that a compromise or arrangement sanctioned under Section 153 of the Indian Companies Act, 1913 (VII of 1913) cannot be worked satisfactorily with or without modifications, it may, either on its own motion or cm the application of any person interested in the affairs of the Banking Company, make an order winding up the banking company and such an order shall be deemed to be an order made under Section 162 of the Indian Companies Act, 1913".

Mr. Chose has further argued that a petition for winding up is necessary because the party which files the petition will satisfy the court that circumstances exist which necessitate the passing of an order of winding up, and that, in the absence of such a petition, there will be no one to satisfy the Court

25. In my opinion, there is no substance in the arguments of Mr. Ghose. It is true that there must be materials before the court on the basis of which it can be satisfied about the necessity of passing a winding up order. Ordinarily such materials can be furnished by a party who files a petition for winding up. In the present case, however, the Bank itself came up to this court for grant of moratorium with the result that, under the court order, the Reserve Bank made enquiries and submitted its report. As I have already said, the renort is useful and gives a clear picture of the Bank's financial position. That being so, there is adequate material in the present case which satisfies me that the Bank is unable to pay its debts.

26. There is clear indication in Section 37 of the Banking Company's Act itself that the Court's power is not confined to merely passing an order for continuation of moratorium or for rescinding it. With

reference to the order of moratorium, the proviso to Sub-section (2) of Section 37 lays down that on receipt of a report from the Reserve Bank the Court "may either rescind any order already passed or pass such further orders thereon as may be just and proper in the circumstances". This has to be read along with Sub-section (1) of Section 38 which makes it imperative for the court to pass an order for winding up of a Bank if it is unable to pay its debts. The two sections leave no room for doubt as to the action which the High Court has to take if the Reserve Bank's report satisfies it about the Bank's inability to pay its debts.

27. Section 433 of the new Act gives a discretionary power to the Court to order the winding up of a Company, and, as I have already held, Sub-section (1) of Section 38 of the Banking Companies Act imposes a duty upon the Court to order the winding up of the banking company if it is unable to pay its debts. While the court need not exercise its discretion under Section 433, without an application for winding up can it be reasonably argued that the court should not perform its duty or fulfil the obligation placed upon it under Section 38 (1) until one of the parties enumerated in Section 439 of the Act has been astute enough to file a petition for winding up? The only answer must be no.

I may also mention that no reference is made in Section 38 (1) to the necessity of an application when the banking company is found to be unable to pay its debts. Sub-section (2) of Section 45K does not lead to any contrary conclusion because that sub-section also gives merely a discretion to the Court to order the winding up of a banking company. The court can exercise this discretion on its own motion or on the application of an interested person. I may mention that Sub-section (2) of Section 392 of the new Act also vests the court with a similar discretion in regard to any company.

28. Several sections of the Banking Companies Act express the solicitude of the legislature for the depositors. I may refer to some of them, Section 40 lays down:--

"Notwithstanding anything to the contrary contained in Section 173 of the Indian Companies Act 1913 (VII of 1913) the High Court shall not make any order staying the proceedings in relation to the winding up of a banking company unless the High Court is satisfied that an arrangement has been made whereby the company can pay its depositors in full as their claims accrue".

The corresponding provision in the new Act is to be found in Section 466 which does not require satisfaction of the court that there is an arrangement whereby the company can pay its creditors in full. Section 43 lays down that every depositor "shall be deemed to have filed his claim for the amount shown in the books of the banking company as standing to his credit." When the banking company concerned is being wound up, Section 43-A puts the depositors in an advantageous position in regard to payment of some deposits. Under Subsection (1) of Section 45, the High Court is prohibited from sanctioning a compromise or arrangement unless it is certified by the Reserve Bank to be not detrimental to the interests of the depositors. It is, therefore, necessary for the court to be vigilant in safeguarding the interests of the depositors.

29. In my judgment, the legal position can be summarised thus. A winding up order cannot ordinarily be passed without a petition under Section 439 of the new Act. Such a petition is not necessary, however, in two cases (1) when the affairs of a Bank come to the notice of the court by

reason of an application for moratorium under Section 37 and the court is satisfied on materials before it that the Bank is unable to pay its debts and that moratorium cannot be granted or should not be continued : and (2) when a scheme has been sanctioned by the court and it feels satisfied that the scheme is not capable of being worked satisfactorily. In the former case, the court has no option but to order winding up, irrespective! of whether a petition under Section 439 is or is not filed. In the latter case, it may, in its discretion, take action only after a petition is filed.

30. In the present case, a practical consideration makes the necessity for passing a winding up order greater. As I will presently show, the proposed scheme is worthless. In the absence of a satisfactory scheme, there are only two alternatives which I can follow : (1) to order the Bank to be wound up; or (2) to order that the Bank be released from the court's control and put back under the very management which has brought it to its present difficult position. Surely, the interests of the depositors will be greatly jeopardised if the latter alternative is adopted.

31. The last point which requires consideration is whether it is open to this court to sanction the scheme proposed by the Bank, and, if so, whether the scheme is fit to be sent for consideration to the creditors and share-holders. There are some observations in the case of AIR 1954 Cal 583 (Supra) which appear to indicate that, in their Lordships' view, the learned single Judge who originally decided the case was right in holding that he was unable to entertain an application for a scheme. If I have understood the observations correctly, I must with great respect, express my dissent.

The Court can approve of a compromise or arrangement put up before it under Section 391 of the new Act either when the company in question is going concern or when it is under liquidation. Even though the court is bound, in a case covered by Section 38 (1) of the Banking Companies Act, to order wanding up of the Bank concerned, I am unable to find any provision of law which prevents the Court from taking into consideration a scheme which is proposed in such a case. I, therefore, hold that there is no legal bar to the entertainment of the Bank's application dated the 17th March.

32. I have, however, considered the merits of the proposed scheme, and I am of the view that it is quite worthless. It is based upon the assumption that the Bank's assets are greater than its liabilities--an assumption which is clearly wrong. A number of paragraphs have been devoted to the constitution of the Board of Directors and management of the Bank. It has been stated in paragraph 14 that the Bank shall carry on its business with the existing assets, and that it will also be entitled to carry on business with new assets including fresh deposits and additional working capitals. It seems to me that, the Bank's doors having remained closed for several months from the 3rd January, 1958, it is not at all likely that it will be able to attract fresh deposits or additional working capital.

It is highly improbable for any one to sink his good money in the Bank in view of its present condition. In any case, it has been said in paragraph 14 itself that the Bank will keep a separate account of its existing assets from the account of its new assets and that the two kinds of assets will not be mixed up. In paragraph 25, it has been stated that new deposits made subsequently to the date of sanction of the scheme shall not come under the scheme. Thus, no part of the new assets can go to the liquidation of the Bank's liabilities as they exist at present.

33. Although, it has been stated in paragraph 17 that certain percentage of the claims will be paid by the Bank to its depositors in each year so that they will be paid in full in seven years, neither Mr. Das nor Mr. Ghose was able to point out to me how the Bank would be able to add to its existing assets or the method in which it will derive sufficient income to enable it to pay the depositors and its other creditors in full or even substantially.

The modifications suggested by Mr, Ghose's clients in their application dated the 22nd April, relate only to the constitution of the Board of Directors and management. Though they have supported the scheme, they have indicated their apprehension by suggesting that a Special Officer should be appointed to manage the affairs of the Bank, and that he should be under the control of this court. They have said that full payment to the depositors should be made in five years instead 6! seven years; but they have not indicated how the Bank can find money to do so.

34. I am clearly of the opinion that the proposed scheme is quite unworkable. No useful purpose will be served by sending it for consideration to the creditors and share-holders because it will not at all be possible for me to sanction it even if they approve of it by the requisite majority.

35. In the circumstances mentioned above, I reject the scheme proposed by the Bank, and I hereby direct that the Bank be wound up.

36. The parties will bear their own costs.