

ACUITY **LAW**

**INSOLVENCY
LAW NEWSLETTER**

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ABOUT ACUITY LAW

Acuity Law was founded in November 2011. Acuity Law comprises of a team of young and energetic lawyers/ professionals led by Souvik Ganguly, Gautam Narayan, Deni Shah and Renjith Nair who have deep and diverse experiences in their chosen areas of practice. We advise Indian and multinational companies, funds, banks and financial institutions, founders of companies, management teams, international law firms, domestic and international investment banks, financial advisors, and government agencies in various transactions in and outside India.

Acuity Law takes pride in rendering incisive legal advice taking into consideration commercial realities. Our areas of practice are divided into three departments. The Corporate practice is led by Souvik Ganguly, the Global Trade and Tax practice is led by Deni Shah and the Disputes practice is led by Gautam Narayan with assistance from Renjith Nair.

As part of the Corporate practice, Acuity Law advises on:

- Mergers and acquisitions;
- Distressed mergers and acquisitions;
- Insolvency Law;
- Private Equity and Venture Funding;
- Employment and labour laws;
- Commercial and trading arrangements; and
- Corporate Advisory

As part of the Global Trade and Tax practice, Acuity Law advises on:

- Cross-border tax planning and jurisdiction analysis
- Strategies for acquisitions, mergers, divestitures, diversification or consolidation of businesses
- Inbound and outbound investment structuring
- Endowment planning / wealth management strategies
- Global Trade & Customs laws, including foreign trade policy
- International supply chain optimization
- Goods & Services Tax and other Indirect taxes

As part of the Disputes practice, Acuity Law advises and represents clients on domestic and cross - border:

- Civil disputes;
- Criminal law matters; and
- Arbitration matters

Acuity Law actively follows legislative and policy developments in its chosen areas of practice and shares such developments with clients and friends on a regular basis.

If you want to know more about Acuity Law, please visit our website acuitylaw.co.in or write to us at al@acuitylaw.co.in.

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INTRODUCTION

This newsletter covers key updates about developments in insolvency law during the month of February 2022.

We have summarized the key judgments passed by the Supreme Court (**SC**), National Company Law Appellate Tribunal (**NCLAT**), National Company Law Tribunals (**NCLT**) and amendments to the Insolvency and Bankruptcy Code, 2016 (**Code**) proposed by the Government of India. Please see below the summary of the relevant regulatory developments.

1) **NCLT CAN ENTERTAIN PETITION RELATED TO PERSONAL GUARANTEES OF CORPORATE DEBTOR, EVEN IF THE CORPORATE DEBTOR WAS ADMITTED INTO CORPORATE INSOLVENCY RESOLUTION PROCESS AND RESOLUTION PLAN IS APPROVED**

Matter: State Bank of India v. Savita Gowda

Order date: 20 January 2022

Summary:

Corporate insolvency resolution process (**CIRP**) was initiated against Sharon Bio-Medicine Ltd. (**Sharon Bio-Med**) and a resolution plan was approved by the NCLT. In the meanwhile, State Bank of India (**SBI**) filed an insolvency application against Ms. Savita Gowda (**Guarantor**), the personal guarantor of Sharon Bio-Med and the erstwhile promotor of Sharon Bio-Med. As a resolution plan for Sharon Bio-Med was already approved by the NCLT, though still pending implementation, the Guarantor sought dismissal of the petition filed by SBI for initiating insolvency process against her. The question before the NCLT was whether the petition filed for initiation of insolvency process of the Guarantor was maintainable in view of the fact that the resolution plan against Sharon Bio-Med was approved.

The NCLT held that the since CIRP of Sharon Bio-Med had commenced and the resolution plan was approved by the present Bench of the NCLT, so the jurisdiction to entertain the petition against the Guarantor is also vested in the present Bench. Once Sharon Bio-Med was admitted into CIRP and a resolution plan was approved, the NCLT Bench would have the territorial jurisdiction to hear any applications filed for insolvency of the personal guarantor. Accordingly, insolvency proceedings were initiated against the Guarantor.

2) **FINANCIAL CREDITORS REALISING SECURITY INTEREST ALSO ENTITLED TO DOCUMENTS AND INFORMATION ON PAR WITH OTHER STAKEHOLDERS**

Matter: Bennet Property Holdings Company Ltd. v. The Liquidator, Biodiversity Conservation (India) Pvt. Ltd.

Order dated: 02 February 2022

Summary:

Biodiversity Conservation (India) Pvt. Ltd. was undergoing liquidation process as per the Code. Bennet Property Holdings Company Ltd. (**Bennet Property**) submitted its claim to the liquidator which was admitted. The liquidator issued directions to Bennet Property to remit its share of the liquidation costs.

Bennet Property contended that the liquidator treated it as a secured financial creditor under the Code. Accordingly, under the Code, (i) a secured financial creditor is only required to pay liquidation costs from the date of admission of its claim during liquidation and not the entire CIRP costs and (ii) the liquidation cost is required to be paid in proportion to the amount recovered and not in proportion to the admitted claim. Further, Bennet Property requested the liquidator to share information/ documents. However, the liquidator refused to share the same.

The liquidator contended that the provisions of the Code relied on by Bennet Property are not applicable. Therefore, it is liable to pay costs as determined by the liquidator. Further, regarding the request for information/documents, it was contended that since Bennet Property chose to realise its security interest, it is not entitled to the information/documents.

The NCLT observed that averments of Bennet Property are not supported by any provision of the Code or a precedent with respect to requirement of (i) liquidation costs being paid only from the date of admission of claims or (ii) liquidation costs being paid in proportion to the amount recovered. With respect to the information/document requests, the NCLT noted that even though Bennet Property has chosen to realise its security interest outside the liquidation process, it is entitled to the same information/document as any other stakeholder. Therefore, the NCLT directed the liquidator to furnish information/documents on par with any other stakeholder.

3) OPERATIONAL CREDITOR UNDER THE CODE INCLUDES PURCHASER OF GOODS AND SERVICES

Matter: Consolidated Construction Consortium Ltd. v. Hitro Energy Solutions Pvt. Ltd.

Order date: 04 February 2022

Summary:

In the present matter, Consolidated Construction Consortium Ltd (**CCCL**) was awarded a contract by Chennai Metro Rail Ltd (**CMRL**) for light fittings. In turn, CCCL placed certain purchase orders with a proprietary concern (**Proprietary Concern**) for supply of the light fittings. CMRL, on behalf of CCCL, paid a certain sum, by way of a cheque to the Proprietary Concern as an advance on its order with CCCL. CMRL later cancelled the project with CCCL and this was also informed to the Proprietary Concern. Consequently, CMRL instructed CCCL (who in turn called upon the Proprietary Concern) to return the amount encashed by the Proprietary Concern. As, the Proprietary Concern failed to remit the amount it received from CMRL, CCCL refunded the amount to CMRL and demanded the refund from the Proprietary Concern.

In the meantime, one Hitro Energy Solution Private Limited (**Hitro**) was incorporated to take over the business of the Proprietary Concern. CCCL sent a demand notice to Hitro under the Code seeking refund payable by the Proprietary Concern. However, Hitro denied any outstanding to CCCL. CCCL filed an application initiating CIRP against Hitro in NCLT which was admitted. The order of the NCLT was reversed by the NCLAT. One of the grounds for reversing the decision was that CCCL was a 'purchaser', and thus did not come under the definition of 'operational creditor' under the Code since it did not supply any goods or services to the Proprietary Concern. The said order of the NCLAT was appealed before the SC.

One of the issues before the SC was whether CCCL is an 'operational creditor' under the Code even though it was a 'purchaser'. The SC observed that the debt arises from purchase orders between CCCL and the Proprietary Concern, which is the underlying contract, regardless of whether CMRL may have made the payment on behalf of CCCL. Therefore, the SC opined that the ultimate dispute is between CCCL and the erstwhile Proprietary Concern, and the debt arises from the underlying contract. The SC further observed the following (i) under the definition of 'operational debt', the operative requirement is that the claim must bear some nexus with a provision of goods or services, without specifying who is to be the supplier or receiver; (ii) an operational creditor can issue a notice in relation to an operational debt either through a demand notice 'or' an invoice. Therefore, the presence of an invoice for having 'supplied' goods or services is not essential since a demand notice can also be issued on the basis of other documents which prove the existence of the debt. Accordingly, the SC held that CCCL is an operational creditor under the Code, since an 'operational debt' will include a debt arising from a contract in relation to the supply of goods or services from the corporate debtor. Therefore, the SC held that a debt arising out of advance payment made to a corporate debtor for supply of goods or services would also be considered as an operational debt. Accordingly, the appeal was allowed and the NCLT's judgment was upheld.

4) GOVERNMENT AMENDS THE NORMS FOR THE RESOLUTION PROCESS FOR CORPORATE PERSON

Notification dated: 09 February 2022

Summary:

On 09 February 2022, the Government of India notified the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) (Amendment) Regulations, 2022 amending the norms for the resolution process for corporate person. The amendment now allows the Resolution Professional to place proposals made by members before the Committee of Creditors (**CoC**) representing at least 33% (thirty-three percent) of the voting rights. Further, a new regulation has been added which mandates preservations of electronic copies of all records relating to the insolvency process for a minimum period of eight years and physical copies for three years from the date of completion of the insolvency process by the resolution professional.

5) **AN ARBITRATION CLAUSE IN THE CONTRACT DOES NOT BAR A CREDITOR FROM MAKING AN APPLICATION TO INITIATE CIRP OF ITS CORPORATE DEBTOR**

Matter: Hasan Shafiq v. CT – Technologies Aps and Anr.

Order dated: 14 February 2022

Summary:

In the present case, B.Y. Agro and Infra Ltd. (**B.Y. Agro**) entered into an agreement with CT-Technologies Aps (**CT-Tech**) for purchasing certain products. The agreement contained an arbitration clause that all disputes between the parties shall be referred for settlement to the court of Arbitration of Switzerland. On account of failure of B.Y. Agro to make payments to CT-Tech towards goods supplied, CT-Tech filed an application before the NCLT for initiating CIRP of B.Y. Agro, and B.Y. Agro was admitted into CIRP by the NCLT. B.Y. Agro challenged the NCLT's order before the NCLAT on the ground that the NCLT ought to have referred the matter to arbitration to the court of Switzerland as per the arbitration clause in the agreement.

NCLAT held that the Code has been given an overriding effect over inconsistent provisions of other laws, including any instrument having effect by virtue of such law. Using this reasoning, the NCLAT held that if an application under the Arbitration and Conciliation Act, 1996 is filed before the NCLT for referring the matter to arbitration, the NCLT shall first proceed to find out whether any default is there. If the NCLT is satisfied that there is a default, it will initiate CIRP of the corporate debtor and reject the prayer for arbitration. As in the present case the debt and default were admitted by B.Y. Agro, the NCLAT held that the NCLT had correctly initiated CIRP of B.Y. Agro. As NCLAT found no error in NCLT's order, the appeal was dismissed.

6) **WITHDRAWAL OF CIRP AGAINST THE PRINCIPAL BORROWER NOT A BAR FOR THE LENDER IN INITIATING FRESH CIRP OF THE GUARANTOR**

Matter: Rajnish Gupta v. Union Bank of India & Anr.

Order dated: 22 February 2022

Summary:

In the present case, DMC Infrastructure Pvt. Ltd. (**DMC Infra**) had provided guarantee to secure loan facilities sanctioned to J. B. Gold Pvt. Ltd. and Roshni Jewellers Pvt. Ltd. (collectively referred as "**Borrowers**"). On account of failure of the Borrowers to repay the loan, CIRP was initiated against them and also a petition was filed against DMC Infra seeking initiation of its CIRP. Subsequently, CIRP of the Borrowers was withdrawn with approval of the CoC. DMC Infra sought discharge of the petition filed against it as the process initiated against the Borrowers was withdrawn. The NCLT did not grant such relief and CIRP of DMC Infra was initiated. The order of the NCLT was challenged before the NCLAT.

The issue before NCLAT was whether an action can be initiated by the financial creditors against a corporate person concerning guarantee offered by it in respect of a loan given to the principal borrower, where the action taken against such principal borrower itself has been withdrawn. NCLAT observed that it is a well settled proposition in Law that the lender is not bound to exhaust its remedy against the principal borrower before suing the guarantor for payment of outstanding sum (unless otherwise agreed to in the guarantee deed). In the present case, the NCLAT was of the view that DMC Infra had failed to establish that the contract of guarantee contains any such stipulation contrary to its liability as a guarantor being coextensive with that of the Borrowers. NCLAT further noted that CIRP against the Borrowers was withdrawn as they did not possess a single asset and therefore CIRP would have only resulted in additional cost. Therefore, NCLAT held that mere withdrawal of CIRP against the principal borrower will not be a bar for the lender in initiating fresh CIRP against the guarantor.

7) **NO INSOLVENCY CAN BE INITIATED UNDER THE CODE AGAINST PERSONAL GUARANTOR OF NBFC, UNTIL IT FALLS WITHIN THE THRESHOLD OF HAVING ASSET SIZE INR FIVE BILLION**

Matter: Shapoorji Pallonji Finance Pvt. Ltd. v. Rekha Singh

Order date: 22 February 2022

Summary:

Shapoorji Pallonji Finance Pvt. Ltd. (**Shapoorji**) filed a petition seeking initiation of insolvency process against Mr. Siddharth Singh and Mr. Ajay Singh, being the personal guarantor (**Guarantors**). The Guarantors had provided personal guarantees for the repayment of the term loan advanced by Shapoorji to Jumbo Finvest (India) Ltd. (**Jumbo**), a Non-Banking Financial Company (**NBFC**). Applications were filed by the Guarantors seeking dismissal of the petition filed against them.

One of the issues before the NCLT was whether insolvency process can be initiated against the personal guarantors of NBFCs before initiation of CIRP against such NBFC.

The NCLT noted that as per the present framework of the Code, only NBFCs with asset size of INR Five Billion or more, as per last audited balance sheet, can be taken up for CIRP under the Code. In the present case, Jumbo had assets below the INR Five Billion threshold and therefore it did not fall within the purview of the Code and is not a "Corporate Debtor" under the Code. Since NCLT only has jurisdiction to initiate insolvency process of personal guarantors of "Corporate Debtors", and as in the present case Jumbo was not a 'Corporate Debtor', it was held that insolvency process cannot be initiated against the Guarantors by NCLT under the provisions of the Code.

8) NCLT CAN ISSUE A NON-BAILABLE WARRANT FOR ENFORCING ATTENDANCE OF A PERSON

Matter: Vikram Puri and Anr. v. Universal Buildwell Pvt. Ltd. and Anr.

Order dated: 28 February 2022

Summary:

In the present case, CIRP was initiated against Universal Buildwell Pvt. Ltd. (**Universal**) and a resolution professional was appointed. The two directors of Universal refused to co-operate with the resolution professional and refused to provide documents related to Universal. This led to the resolution professional filing an application before the NCLT seeking suspension of the directors. Despite an order having been passed by the NCLT and issuance of summons and bailable warrants, the directors failed to appear before the NCLT Registrar for submission of documents. Eventually, the NCLT issued non-bailable warrants of arrests against them. The order of the NCLT refusing to cancel the non-bailable warrants of arrest, on grounds that the directors had failed to comply with the order to appear before the Registrar, was challenged before the NCLAT.

The issue before the NCLAT was whether the NCLT has any jurisdiction to issue non-bailable warrant against any person or party. NCLAT observed that as per the NCLAT Rules and the Code of Civil Procedure, 1908, the NCLT at its discretion, can issue at any time a warrant either with or without bail for arrest of such person who without any lawful excuse, failed to attend or to produce the document in compliance with summons. NCLAT observed that in the present case, despite multiple opportunities, the directors of Universal had refused to appear before the Registrar and had refused to submit documents. Further, the reasons provided by the directors for such non-appearance was not acceptable. Therefore, NCLAT found no error with the NCLT's order refusing to cancel the non-bailable warrants. Accordingly, the appeal was dismissed.

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