

ACUITY **LAW**

INSOLVENCY

LAW NEWSLETTER

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ABOUT ACUITY LAW

Acuity Law was founded in November 2011. Acuity Law comprises a team of young and energetic lawyers/ professionals led by Souvik Ganguly, Gautam Narayan and Deni Shah 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.

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 the Insolvency Law during the month of July 2021.

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

1) **DEMAND NOTICE ISSUED BY OPERATIONAL CREDITOR BASED ON INVOICES CAN BE ISSUED IN FORM-3 INSTEAD OF FORM-4.**

Matter: Tudor India Pvt. Ltd. v. Servotech Power Systems Ltd.

Order dated: 02 July 2021.

Summary:

Tudor India Pvt. Ltd (**Tudor**), an operational creditor of Servotech Power Systems Ltd. (**Servotech**), issued a Demand Notice in Form-3 to Servotech and thereafter filed an application for initiation of Corporate Insolvency Resolution Process (**CIRP**) against Servotech. The issue before the NCLT, New Delhi Bench, was whether the demand notice issued by Tudor to Servotech, which was in Form-3, was valid or not. The Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 provides two forms to an operational creditor for delivering a demand notice to a corporate debtor i.e., Form-3 or Form-4.

The NCLT noted that Form-3 requires filing a notice or invoice and has seven columns wherein detailed information is to be provided. On the other hand, Form-4 is a cover page of the invoice in which an operational creditor is not required to provide details. Form-3 covers instances where the debt arose against an invoice or other documents that prove the existence of the debt (ex. – for supply of goods). It also covers debts where an invoice was not generated, like the salary of an employee. It also informs the corporate debtor of its statutory right of replying to the operational creditor within ten days.

On this basis, the NCLT held that no prejudice could be caused to a party if a demand notice supported with invoices was delivered in Form-3. However, in the present case, the usage of Form-3 was held to be valid as it was annexed with an invoice.

2) **BANKERS CAN RELEASE THE FUND TO THE EXTENT OF FULL VALUE OF THE BANK GUARANTEE MINUS MARGIN MONEY PROVIDED BY THE CORPORATE DEBTOR TO THE BANKER.**

Matter: C & C Construction Ltd. v. Power Grid Corporation of India Ltd.

Order dated: 19 July 2021.

Summary:

The resolution professional of C & C Construction Ltd. (**Corporate Debtor**) filed an appeal before the NCLAT being aggrieved by the order of the NCLT, Principal Bench, as it vacated an ad-interim injunction which it had previously granted against encashment of bank guarantee issued on behalf of Corporate Debtor to its various customers.

The NCLAT set aside the NCLT's order and held that the bank guarantee issued by bankers are also the responsibility of the bankers and that the monies will go out of the fund of the banks and not directly from the fund of the Corporate Debtor. However, keeping in mind the provisions of the Insolvency & Bankruptcy Code, 2016 (**Code**) on moratorium, if any such bank guarantee is liquidated, it can be restricted to the full value of the guarantee minus margin money provided by the Corporate Debtor to the banker for taking that bank guarantee. Accordingly, NCLT held that banks can release the fund to the extent of full value of the bank guarantee minus margin money provided by the Corporate Debtor to the banker.

3) **TERM LOAN AGREEMENT BEING INADEQUATELY STAMPED CANNOT BE A GROUND FOR NOT ADMITTING THE CORPORATE DEBTOR INTO CIRP IF THERE EXISTS OTHER DOCUMENTS TO PROVE DEBT AND DEFAULT.**

Matter: Ashique Ponnamparambath v. The Federal Bank Ltd.

Order dated: 19 July 2021.

Summary:

The suspended director of the corporate debtor, M/s. Platino Classic Motors (**Corporate Debtor**), had challenged the order of the NCLT, Kochi Bench, admitting the Corporate Debtor into CIRP on the basis of an application filed by a financial creditor. The ground for challenge was that the 'Term Loan Agreement' under which the entire loan transaction was based was an inadequately stamped document and is therefore not admissible in evidence.

The NCLAT held that the objections raised were unsustainable. This is because the financial creditor had not only relied upon the Term Loan Agreement but also on the demand promissory note, hypothecation letter regarding depositing of title deed, a certified copy of the bank statement, and many other documents and therefore the debt and default were proved beyond doubt. Accordingly, the appeal was dismissed by the NCLAT.

4) **INTEREST IS NOT A MANDATORY CONDITION FOR A DEBT TO BE CONSIDERED AS A 'FINANCIAL DEBT' UNDER THE CODE.**

Matter: Orator Marketing Pvt. Ltd. v. Samtex Desinz Pvt. Ltd.

Order dated: 26 July 2021

Summary:

The issue before the SC was whether a person giving a term loan to a Corporate Person, free of interest, is a financial creditor, and would qualify to initiate CIRP under the Code. The NCLT, New Delhi Bench and NCLAT had both held that since the loan was interest free, the same could not be termed as a 'financial debt.'

SC relied on the definition of 'financial debt' under the Code which is defined as "a debt along with interest, if any, which is disbursed against the consideration of the time value of money and includes money borrowed against the payment of interest." SC held that the NCLT, New Delhi Bench and the NCLAT had overlooked the words "if any". SC also observed that both NCLAT and NCLT, New Dei Bench had failed to notice that the definition of 'financial debt' under the Code also includes "any amount raised under any other transaction, having the commercial effect of borrowing." The SC explained that a 'financial debt' would mean outstanding principal due in respect of a loan and would also include interest, if any. However, if no interest were payable on the loan, only the outstanding principal amount would qualify as a 'financial debt' under the Code.

Therefore, SC held that the definition of 'financial debt' under the Code does not expressly exclude an interest free loan and 'financial debt' would have to be construed to include interest free loans advanced to finance the business operations of a corporate body.

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