DEVELOPMENTS IN INSOLVENCY LAWS

IN JANUARY 2019

ACUITY LAW

ABOUT ACUITY LAW

Acuity Law was founded in November 2011. Acuity Law comprises of a team of young and energetic lawyers led by Souvik Ganguly and Gautam Narayan, who have deep and diverse experiences in their chosen areas of practice. We have advised 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 two departments.

The Corporate practice is led by Souvik Ganguly 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 Disputes practice, Acuity Law under the leadership of Gautam Narayan 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 www.acuitylaw.co.in or write to us at al@acuitylaw.co.in.

INTRODUCTION

This newsletter covers developments with respect to the Insolvency and Bankruptcy Code, 2016 during the month of January 2019. We have covered orders passed by the National Company Law Appellate Tribunal and various benches of the National Company Law Tribunal. Please see below the summary of the relevant orders.

ABBREVIATIONS

Adjudicating Authority	AA
Committee of Creditors	CoC
Corporate Insolvency Resolution Process	CIRP
Insolvency and Bankruptcy Code, 2016	Code
Insolvency and Bankruptcy Board of India	IBBI
Interim Resolution Professional	IRP
National Company Law Tribunal	NCLT
National Company Law Appellate Tribunal	NCLAT
Resolution Professional	RP
The Sick Industrial Companies Act, 1985	SICA
Tax Deducted at Source	TDS

1. IT IS NOT NECESSARY TO INITIATE CIRP AGAINST THE PRINCIPAL BORROWER BEFORE INITIATING CIRP AGAINST THE CORPORATE GUARANTOR

Matter: Ferro Alloys Corporation Limited vs. Rural Electrification Corporation Limited

Order dated: 08 January 2019

Summary:

In this matter, Rural Electrification Corporation Limited ("**Financial Creditor**") sanctioned a loan to FACOR Power Limited ("**Principal Borrower**"), under various loan agreements and accordingly disbursed an amount aggregating to INR 5,109,700,000 on various dates. In order to secure the loan facility extended by the Financial Creditor to the Principal Borrower, a corporate guarantee agreement was executed between the Financial Creditor, the Principal Borrower and Ferro Alloys Corporation Limited ("**Corporate Guarantor**"). The case of the Financial Creditor was that the Principal Borrower defaulted in repaying dues and the account of the Principal Borrower was classified as Non-Performing Asset ("**NPA**"). In view of the defaults committed in the repaying the loan, as per the terms and conditions of the loan agreements, the Financial Creditor recalled the facilities and demanded the entire amount of loan, interest and all other amounts due in respect thereof. Despite the said demand, no payment was made to the Financial Creditor. The Principal Borrower had admitted its liability in the audited balance-sheet for F.Y. 2015-16. The Corporate Guarantor in its audited balance-sheet for the F.Y. 2015-16 had also acknowledged the said debt. On account of the default in making payment of the debt amount by the Principal Borrower, the Financial Creditor invoked the corporate guarantee and thereby called upon the Corporate Guarantor to pay forthwith the amount due and payable by the Principal Borrower along with future interest within a period of 21 days.

The Financial Creditor pleaded that the said corporate guarantee is an unconditional, continuing and irrevocable guarantee. As per the terms of the guarantee, the obligation of Corporate Guarantor is separate, independent and is that of primary obligor and not merely as surety, on a full indemnity basis to indemnify the Financial Creditor. The corporate guarantee provided by the Corporate Guarantor is joint and several and co-extensive with that of the Principal Debtor and can be invoked even without exhausting the remedies against the Principal Debtor. The NCLT, Kolkata Bench taking into consideration the fact inter alia held that there is a 'debt' and 'default' and the application being complete, admitted the same.

Being aggrieved by the said order, an appeal was filed by the Corporate Guarantor. The question for determination in this appeal was whether the application filed under Code is maintainable against a corporate guarantor without initiating CIRP against the principal borrower.

The NCLAT held that CIRP under the Code can be initiated against the guarantor who is a 'corporate person' and who by operation of law ipso facto becomes a 'corporate debtor' by satisfying the ingredients as required for a 'corporate person' under the Code. The NCLAT further held that it is not necessary to initiate CIRP against the principal borrower before initiating CIRP against the corporate guarantors and accordingly disposed of the appeal.

2. TWO APPLICATIONS CANNOT BE FILED BY THE SAME FINANCIAL CREDITOR FOR THE SAME SET OF CLAIM AND DEFAULT AGAINST DIFFERENT CORPORATE DEBTORS (i.e. EITHER A PRINCIPAL BORROWER OR CORPORATE GUARANTOR(S))

Matter: Dr. Vishnu Kumar Agarwal vs. Piramal Enterprises Limited

Order dated: 08 January 2019

Summary:

In this matter, a 'Deed of Agreement' was entered into by 'All India Society for Advance Education and Research' (hereinafter referred to as "Principal Borrower") with M/s. Piramal Enterprises Limited ("**Financial Creditor**") for grant of INR 380,000,000 which was guaranteed by two corporate guarantors viz. Sunrise Naturopathy and Resorts Private Limited ("**Corporate Guarantor No.1**") and Sunsystem Institute of Information Technology Private Limited ("**Corporate Guarantor No.2**").

Subsequently, the Financial Creditor issued a separate demand notice to Corporate Guarantor No.1 and Corporate Guarantor No.2 on 24 October 2017 and 26 October 2017, respectively, thereby calling upon them to repay the outstanding amount of INR 402,876,461. Thereafter, the Financial Creditor filed an application under the Code for initiation of CIRP against Corporate Guarantor No.1 and Corporate Guarantor No.2. The NCLT, Principal Bench, New Delhi ("**NCLT**") vide orders dated 31 May 2018 and 24 May 2018 admitted the applications and initiated CIRP against Corporate Guarantor No.1 and Corporate Guarantor No.2, respectively.

In the aforesaid background, Dr. Vishnu Kumar Agarwal, shareholder ("**Appellant**") filed an appeal before the NCLAT questioning the maintainability of the CIRP initiated against Corporate Guarantor No.1 and Corporate Guarantor No.2 which were based on same set of claim, default and record.

The issues before the NCLAT were (a) whether CIRP can be initiated against a corporate guarantor, if the principal borrower is not a 'Corporate Debtor' or a 'Corporate Person' and (b) whether CIRP can be initiated against two corporate guarantors simultaneously for the same set of debt and default.

The NCLAT inter alia held that, it is not necessary to initiate CIRP against a principal borrower before initiating CIRP against a corporate guarantor. Further, without initiating any CIRP against the principal borrower, it is always open to a financial creditor to initiate CIRP against a corporate guarantor, as a creditor is also the financial creditor qua corporate guarantor. Also, the Code does not bar filling two applications simultaneously against a principal borrower as well as the corporate guarantor or against both the corporate guarantors. However, once an application is filed by a financial creditor against one of the corporate debtor (i.e. either the principal borrower or corporate guarantor) and the same has been admitted, a second application by the same financial creditor for same set of claim and default cannot be admitted against the other corporate debtor (i.e. the corporate guarantor or the principal borrower). In view of the above, the NCLAT upheld the initiation of CIRP only against Corporate Guarantor No.2 and held that the application filed against Corporate Guarantor No.1 is not maintainable, as the application filed against Corporate Guarantor No.2 got admitted prior to Corporate Guarantor No.1.

3. A FINANCIAL CREDITOR SHOULD FILE ITS CLAIM BEFORE RP OR BRING HIS GRIEVANCE TO THE NOTICE OF AA OR THE MEMBER OF COC BEFORE THE APPROVAL OF THE RESOLUTION PLAN BY THE COC

Matter: Kotak Mahindra Prime Limited vs. Rave Scans Private Limited & others

Order dated: 08 January 2019

Summary:

In this matter, Kotak Mahindra Prime Limited ("**Appellant**") filed an appeal before the NCLAT against the approval of the resolution plan for Rave Scans Private Limited ("**Corporate Debtor**"), for non-inclusion of itself in the CoC of the Corporate Debtor, as a financial creditor. However, it is pertinent to note that, the Appellant not only failed to file any claim before the RP of the Corporate Debtor but also failed to bring its grievance to the notice of the NCLT, Principal Bench ("**NCLT**") or the CoC within time and before approval of the resolution plan by the CoC and the NCLT.

The NCLAT observed that the Appellant had failed to explain the delay and laches on its part in making its claim pursuant to publication of advertisement or to move before the NCLT against its demand. In view of the above, the NCLAT held that, it is not open for the Appellant at this stage to move an appeal before the NCLAT.

4. ELEMENT OF INTEREST, RECORDING IN THE BOOKS OF ACCOUNTS AND DEDUCTION OF TDS ARE KEY FACTORS IN DETERMINING THE EXISTENCE OF FINANCIAL DEBT

Matter: Vijay Rochlani vs. Shantai Exim Limited

Order dated: 14 January 2019

Summary:

In the present matter, Mr. Vijay Rochlani ("**Applicant**"), being the financial creditor, filed an application before the NCLT, Mumbai Bench ("**NCLT**") against Shantai Exim Limited ("**Respondent**"), on the ground that the Respondent failed to pay the total outstanding debt of INR 5,000,000 with interest as on 11 October 2017.

The main issue before the NCLT was whether the impugned amount falls under the definition of financial debt or not, since the Respondent claimed that the impugned amount was retained by them as an escrow amount for the alimony of their sister who is seeking a divorce from the Applicant. On the other hand, the Applicant claimed that the impugned amount was a short-term loan given to the Respondent.

The NCLT perused the definition of 'financial debt' as prescribed under the Code and observed that it has a component of 'Interest', in other words it has a component of "Time Value of Money". In view of the above, the NCLT admitted the said application holding the impugned amount as a 'Financial Debt' for the following reasons:

a) The transfer of money had the element of payment of interest;
b) The Respondent had recorded the impugned amount in its books of accounts as 'Short Terms Borrowings', thus showing a financial liability; and
c) TDS was deducted by the Respondent as and when interest was paid by the Applicant.

5. NO CREDITOR / LENDER CAN RECOVER THEIR DEBTS, INCLUDING ENCASHMENT OF POST-DATED CHEQUES, DURING THE PENDENCY OF THE CIRP AND THE MORATORIUM PERIOD

Matter: Mr. Satish Kumar Gupta vs. L&T Infrastructure Finance Company Limited

Order dated: 28 January 2019

Summary:

In the present matter, Mr. Satish Kumar Gupta ("**Applicant**") i.e. the RP of M/s. Essar Steel India Limited ("**Corporate Debtor**") filed an application before the NCLT, Ahmedabad Bench ("**NCLT**") against L&T Infrastructure Finance Company Limited ("**Respondent**"). As per the Applicant, during the pendency of the CIRP of the Corporate Debtor, the Respondent undertook the process of encashing certain cheques, including post-dated cheques, which were issued by the erstwhile management of the Corporate Debtor. In view of the above, the Applicant sought the following directions from the NCLT to be passed against the Respondent, a) to return the amount of the post-dated cheques that were encashed; and b) to restrict the Respondent from encashing the remaining post-dated cheques.

The Respondent inter alia argued that the provisions of the Code, with respect to moratorium, does not restrict it for encashing cheques, which was issued in favour of the creditor for the purpose of discharging a legally valid enforceable debt.

The NCLT granted the reliefs / directions sought by the Applicant and *inter alia* held that it is not open to any kind of creditors / lenders to make recovery of such debt during the pendency of CIRP and moratorium period. The NCLT further held that presenting such post-dated cheques for its encashment amounts to violation of moratorium period and is contrary to the provisions of the CIRP.

6. ALL MATERIAL FACTS NEED TO BE DISCLOSED IN AN INSOLVENCY APPLICATION

Matter: Amar Remedies Limited

Order dated: 29 January 2019

Summary:

Amar Remedies Limited ("**Corporate Applicant**"), filed an application under the Code before the NCLT, Mumbai Bench ("**NCLT**") to initiate CIRP against itself.

At the time of submission of the resolution plan to the NCLT for its approval, it was brought to the attention of the NCLT by one of the Corporate Applicant's financial creditor that the Bombay High Court ("**HC**") had passed a liquidation order against the Corporate Applicant. This fact was suppressed by the Corporate Applicant in the said application made before the NCLT.

The explanation set out by the Corporate Applicant was that one of its creditors had filed a winding up application in the HC, which got admitted. Subsequently, the Corporate Applicant sought reference to the Board for Industrial and Financial Reconstruction under SICA which was rejected. Pursuant to the said rejection an appeal was filed before the Appellate Authority for Industrial and Financial Reconstruction ("**AAIFR**"). Noting the pendency of the proceedings in AAIFR, the HC adjourned the liquidation proceedings sine die. On account of the introduction of the Code since SICA got repealed, the Corporate Applicant filed an application under the Code before the NCLT. The NCLT observed that the HC had in the meanwhile, taking notice of the abatement of appeal in AAIFR, passed liquidation order against the Corporate Applicant.

The question before the NCLT was whether the Corporate Applicant was bound to disclose the liquidation order passed against it by the HC. For this purpose, the NCLT referred to the provisions of the Code that barred an application for CIRP to be filed against a company against whom a liquidation order has been passed.

The NCLT found that the Corporate Applicant's conduct amounted to offence under the provisions of the Code as the Corporate Applicant had suppressed material facts in its application for CIRP. Further, the NCLT directed Registrar of Companies, Mumbai to lodge prosecution. Accordingly, the application was rejected with costs of INR 1,000,000.

7. AN INSOLVENCY PROFESSIONAL IS REQUIRED TO DISCHARGE HIS STATUTORY RESPONSIBILITIES AS IRP AND RP TO MANAGE THE CORPORATE DEBTORS AS A GOING CONCERN

Matter: Mr. Sandeep Kumar Kejriwal

Forum: Disciplinary Committee ("**DC**"), IBBI

Order dated: 28 January 2019

Summary:

In this matter, Mr. Sandeep Kumar Kejriwal ("**Defendant**") was appointed as the IRP vide order dated 29 August 2017, for undertaking CIRP of Upadan Commodities Private Limited ("**Corporate Debtor No.1**"). The Defendant was also appointed as the IRP vide order dated 08 September 2017 for undertaking CIRP of Maa Tara Industrial Complex Private Limited ("**Corporate Debtor No.2**").

A show cause notice was issued to the Defendant for the following important contraventions on his part in conducting the CIRP of Corporate Debtor No.1 and Corporate Debtor No.2:

a) The progress report was not submitted to the AA in time;
b) The public announcement was not made in time;
c) The registered valuers were not appointed;
d) The information memorandum was not prepared and circulated;
e) Resolution plan was invited only from the sole member of the CoC without providing information memorandum;
f) The meetings of the CoC were conducted without adequate notice; and
g) Corporate Debtor No.1 and Corporate Debtor No.2 were not run as a going concern.

The DC observed that Corporate Debtor No.1 and Corporate Debtor No.2 belong to the same group and were under the same management and the CIRP's were triggered by the same operational creditor.

The explanation given by the Defendant for such contravention was:

a) funds were not available to make public announcement;
b) there was no co-operation from Corporate Debtor No.1 and Corporate Debtor No.2;
c) he was unwell from 04 September 2017 to 22 October 2017.

The DC found no merit in the submissions made by the Defendant and observed that the Defendant did not discharge any of his statutory responsibilities as IRP or RP to manage the operations of Corporate Debtor No.1 and Corporate Debtor No.2 as a going concern as laid down under the Code. The DC further observed that there were two mitigating factors in favour of the Defendant one being the Defendant was unwell during the relevant period and the other being that Corporate Debtor No.1 and Corporate Debtor No.2 were not going concerns to start with. Accordingly, the DC imposed a monetary penalty equal to 100% of the total fee payable to the Defendant as IRP and RP of Corporate Debtor No.1 and Corporate Debtor No.2. Further, the DC also directed the Defendant to undergo the pre-registration educational course specified under the Insolvency and Bankruptcy Board of India (Insolvency Professionals) Regulation, 2016 from the Defendants Insolvency Professional Agency in order to improve the Defendants understanding of the Code and its relevant regulations before taking up any assignment under the Code.

8. THE IBBI (INSOLVENCY RESOLUTION PROCESS FOR CORPORATE PERSONS) (AMENDMENT) REGULATIONS, 2019

IBBI amended the IBBI (Insolvency Resolution Process for Corporate Persons) Regulations, 2016 vide the IBBI (Insolvency Resolution Process for Corporate Persons) (Amendment) Regulations, 2019 ("**Amended Regulations**") on 24 January 2019.

The Amended Regulations mandates that the request for resolution plans shall require the resolution applicant, in case its resolution plan is approved by the CoC, to provide a performance security.

Further, the RP is required to attach the evidence of receipt of performance security while submitting the resolution plan to the AA for approval. Such performance security shall be forfeited if the resolution applicant of such plan, after its approval by the AA, fails to implement or contributes to the failure of implementation of the plan.

The Amended Regulations also requires the resolution plan to include a statement as to whether the resolution applicant or any of its related parties has ever failed to implement or have contributed to the failure of implementation of any resolution plan approved by the AA under the Code.