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# Article

## Disputing a dispute under Insolvency and Bankruptcy Code, 2016

By **Arun Mohanty**

Debt recovery in India has been a challenge with creditors and debtors disputing rights and obligations in legal wrangles under various provisions under applicable laws making the process time consuming and costly.

The Insolvency and Bankruptcy Code, 2016 ("IBC" or "Code") was enacted on May 28, 2016 with an aim to *inter alia* address and resolve these issues in addition to providing for the mechanism for resolution of insolvency and bankruptcy matters in India. The laws in India prior to enactment of the Code were spread across several enactments with winding up being under the jurisdictions of the High Courts of India under the Companies Act, 1956. The Ministry of Corporate Affairs ("MCA") has now notified provisions related to winding up of a company under the Companies Act, 2013[1] and the Companies (Transfer of Pending Proceedings) Rules, 2014[2], by virtue of which all pending proceedings[3] in relation to winding up of a company pending before the High Courts shall be transferred to the relevant bench of the National Company Law Tribunal ("NCLT").

IBC being a new legislation is undergoing judicial tests which shall hopefully render its provisions robust and effective. Various benches of NCLT have pronounced conflicting orders giving rise to inconsistency in interpretation of IBC provisions. One issue at the core of remedies available to a debtor under the IBC is the term 'dispute' under the IBC. The term has been the point of focus and interpretation of various orders of the NCLT in context of IBC.

For understanding the interpretation of the term 'dispute', it would be ideal to study the recent developments in light of the Order passed by National Company Law Appellate Tribunal ("NCLAT") in the *Kirusa* case.

### *Kirusa Software Private Limited v. Mobilox Innovations Private Limited*

In *Kirusa Software Private Limited v. Mobilox Innovations Private Limited*, the applicant operational creditor filed a petition under Section 9 of IBC claiming its outstanding dues and requesting NCLT, Mumbai to initiate corporate insolvency resolution process against the corporate debtor.

To satisfy requirements under Sections 8 and 9 of IBC, the operational creditor issued a demand notice on the corporate debtor. *Per* Section 8 of IBC, a corporate debtor may resist initiation of corporate insolvency process by either repaying the outstanding operational debt or bringing into notice the existence of a dispute in relation to such outstanding amount.

The corporate debtor responded to the demand notice by issuing a notice of dispute against the outstanding amount. NCLT, Mumbai adjudicated that the creditor was in receipt of and had admitted to the existence of a dispute in respect of the outstanding amount payable to the operational creditor and therefore, dismissed the petition.

The operational creditor appealed against NCLT's order in the NCLAT. NCLAT determined that it is pertinent to examine the meaning of 'dispute' and 'existence of dispute' in light of Section 9 of IBC.

Section 5(6) of IBC defines 'dispute' as:

*"…….(6) 'dispute' includes a suit or arbitration*

[1] MCA Notification dated December 7, 2016
[2] MCA Notification dated December 7, 2016
[3] as on December 15, 2016

*proceedings relating to:*

*(a) the existence of the amount of debt;*

*(b) the quality of goods or service; and*

*(c) the breach of a representation and warranty;……"*

The question was reduced to examination of what constitutes a 'dispute'. Further, NCLAT sought to determine whether it is necessary for a suit or arbitration proceeding to have been initiated to demonstrate existence of a dispute.

In the instant case, NCLAT was of the view that the definition of the term 'dispute' is inclusive and not exhaustive. The term 'dispute' has to be given a wider meaning provided it is relatable to the existence of the amount of debt, quality of goods or service, or breach of representation or warranty.

NCLAT further held that it is necessary to determine the circumstances in which the dispute has been raised by the corporate debtor. A genuine notice issued by the corporate debtor to the operational creditor shall suffice demonstration of a dispute. The judgment states that a "dispute" under Section 8 and 9 of the IBC would mean any proceeding initiated or pending before any consumer courts, tribunal, labour court, mediation or conciliation, including an action taken by a corporate debtor under any Act or law such as replying to a notice under Section 80 of the Code of Civil Procedure, 1908, or an action under Section 59 of the Sale of Goods Act, 1930 or an action regarding the quality of goods provided by an Operational Creditor. The dispute should be a genuine dispute and not one that was raised with *malafides* to stall the insolvency resolution process. While even in the pre-IBC era, the courts did not entertain disputes or winding up petitions pending before any authority, courts or tribunals, the IBC provides a legitimate possibility to request for a winding up of a company even if it is not insolvent (unable to pay its debts).

## *Conflicting interpretations of the term 'Dispute':*

Various benches of NCLT have had contradictory views on interpretation of the term 'dispute'. The Delhi bench of NCLT, in the matter of *One Coat Plaster, Shivam Construction Company v. Ambience Private Limited* held that the term 'dispute' needs to have a broad and inclusive definition. The Delhi bench further held that it is not mandatory on part of the debtor to have initiated a suit or arbitration proceeding prior to the receipt of demand notice to assert the existence of a dispute. Mere response to the demand notice showcasing existence of a *bona fide* dispute shall suffice. The NCLAT affirmed these views in the *Kirusa* case.

In the *Kirusa* case, the order stated that if the legislative intent was to determine a dispute by showing a record of a pending suit or arbitration proceedings, the term 'dispute' would have been defined in such restrictive manner in the Code.

The Mumbai bench of NCLT in the matter of *DF Deutsche Forfait AG and Another v. Uttam Galva Steel Limited* held that the 'existence of a dispute' means that a suit or arbitration proceedings must be pending before an operational creditor serves a demand notice. Raising a dispute in reply to the demand notice does not amount to notice of an existing dispute. Similarly, filing a suit or initiating arbitration proceedings subsequent to receipt of demand notice shall not amount to an existing dispute.

## *Conclusion:*

Such conflicting orders have their own ramifications. While it is prudent to analyze the circumstances in which a dispute has arisen, there are no set parameters to verify if a thwarted dispute is kosher.

To avoid frivolous disputes being raised in response to a demand notice, NCLAT, in the *Kirusa* case held that merely raising an illusory dispute in response to a demand notice shall not be used as a tool to reject an application if the

Adjudicating Authority believes that there is a debt and default on the part of the corporate debtor. It is pertinent to note that the Adjudicating Authority is empowered and required to verify the *bona fides* of a dispute if the application for initiation of corporate insolvency resolution process is filed by a financial creditor. However, such is not the situation in the event the dispute relates to an operational creditor. In such a scenario, the onus to prove the existence of a *bona fide* dispute shifts from the operational creditor to the corporate debtor.

The NCLAT order mandates analyzing circumstances while deciding upon the existence of a *bona fide* dispute. It may not be possible to scrutinize every dispute on subjective criteria. While IBC survives its testing times, it would have been efficient if NCLAT had laid down clear principles of determining a dispute. Determination of disputes on subjective criteria may give rise to interpretational inconsistencies.

A look back at an order passed under the Companies Act, 1956 in relation to winding up of a company – In *K. Appa Rao v. Sarkar Chemicals Private Limited*[4], the Andhra Pradesh High Court held that where a company has *prima facie* sustainable defence or a *bona fide* dispute of its obligations to discharge the alleged debts or liabilities, the court may not entertain proceedings for winding up, much less order winding up.

Such conflicting orders have implications on both operational creditors and corporate debtors. The corporate debtors should, if there exists any dispute in relation to the amount of debt or the quality of goods and services or breach of representation and warranty, raise a notice of dispute against the operational creditors in a proactive manner. On the contrary, operational creditors have an upper hand since raising a dispute or initiating a suit in response to a demand notice may not hold water of its *bona fides*, during adjudication. Parties should also consider the issue while drafting their dispute resolution clauses where they agree to a settlement period prior to raising formal process such as arbitration or a court process. This is significant in view of the possibility of operational creditors with malafide intent seeking to pursue a process under the IBC in the wake of a legitimate dispute by the debtor, who perhaps has not initiated a formal dispute process before any authority while the settlement discussions are ongoing. While eventually this would be considered by the NCLT, it may cause undue hardships to justified debtors especially in view of several conflicting judgments.

With the current stance, we are sure to witness a lot of debate on the determination of *bona fides* of a dispute. It would be interesting to await further interpretation of the term 'dispute' and await judicial orders laying down strict guiding principles on this issue.

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## Notifications and Circulars

**Exemptions to Private Companies:** The Ministry of Corporate Affairs (MCA) by its Notification dated June 5, 2015 (Principal Notification), had notified number of exemptions available to private companies with regards to compliance requirements under the 2013 Act. In addition to the relaxations previously granted under the Principal Notification, the MCA has by

4 1995 84 CompCas 670 AP

a recent Notification dated June 13, 2017 (G.S.R. 583(E)), provided further relaxations by amending the Principal Notification. Such relaxations and modifications can only be availed by a private company if it has not defaulted in filing its financial statements and annual returns *per* compliance requirements under Sections 137 and 92 of the 2013 Act.

The amending notification provides for the following amendments:

*Financial Statement*: According to revised provisions, the financial statement with respect to one-person company, small company, dormant company and a private company (if such private company is a start-up) may not include the cash flow statement. Previously, the 2013 Act limited such relaxation to one-person companies, small companies and dormant companies.

*Acceptance of Deposits*: Section 73 of the 2013 Act lays down conditions and requirements that are to be fulfilled by a company before accepting deposits from its members. The Notification provides for exemption from such conditions to the following categories of private companies:

(a) To a private company, which is a start-up, for 5 (five) years from the date of its incorporation; or

(b) To a private company which accepts from its members monies not exceeding one hundred per cent of aggregate of the paid up share capital, free reserves and securities premium account; or

(c) To a private company that fulfills all the conditions below:

1. It is not an associate or a subsidiary company of any other company;
2. Its borrowings from banks, financial institutions or any body corporate is less than twice of its paid up share capital or fifty crore rupees, whichever is lower; and
3. It has not committed default in the repayment of such borrowings subsisting at the time of accepting deposits.

*Annual Return*: The Principal Notification provided that in relation to one-person companies and small companies, the Company Secretary or in his absence, the Director of the company shall sign the annual returns. The new notification further extends this relaxation to private companies which are start-ups. It also provides that small companies shall be required to disclose only the aggregate amount of remuneration drawn by the Directors instead of the previous requirement of disclosing the remuneration of all Directors and Key Managerial Personnel.

*Auditor's Report*: Auditor's reporting requirements under Section 143 of the 2013 Act requires an auditor to report on the adequacy of the company's system for internal financial controls and its operating effectiveness. The amended relaxations now provide that a private company which is a one-person company or a small company shall not be liable to comply with this requirement. This requirement shall also not be applicable to a private company which has a turnover of less than fifty crores rupees (as per latest audited financial statement) or has aggregate borrowings from any bank, financial institution or any body corporate at any point of time during the financial year, less than twenty five crore rupees.

*Board Meetings*: According to the Principal Notification a one-person company, small company or a dormant company is deemed to have complied with provisions relating to board meetings, if at least one meeting of Board of Directors has been conducted in each half of the financial year and the gap between the two meetings is not less than ninety days. This relaxation has now been further extended to a private company, which is a start-up.

*Quorum for meetings of Board*: The 2013 Act states that for the purposes of quorum for meetings of the Board of Directors, if the number of interested directors exceeds or is equal to two-thirds of the total strength of the Board of Directors, the number of directors who are not interested directors and present at the meeting should be at least two. The amending notification provides that interested directors may also be counted for the purpose of quorum in such meetings after they have disclosed their interest pursuant to Section 184 of the 2013 Act.

**Foreign Investment Promotion Board Abolished:** The Ministry of Finance, through an Office Memorandum dated June 5, 2017 (F.No. 01/01/FC/2017-FIPB), has outlined the proposal approved by the Central Government for abolition of the Foreign Investment Promotion Board (FIPB). The FIPB was a 25-year-old inter-ministerial body, responsible for vetting Foreign Direct Investment (FDI) applications in India in sectors that required prior Government approval. The abolition aims at facilitating 'ease of doing business' in India. It is envisaged that subsequent to the abolition, the work of granting Government approval for foreign investment under the FDI Policy and Foreign Exchange Management Act, 1999, shall be entrusted to the concerned administrative ministries or departments for the 11 (eleven) notified sectors/activities requiring Government approval. The concerned administrative ministry / department will be required to obtain the approval of the Minister-in-charge / Cabinet Committee on Economic Affairs on the applications *per* FDI Policy. Investment proposals that raise security concerns, that is, proposals from 'Countries of Concern' will be processed by the Ministry of Home Affairs.

FDI proposals by Non-Resident Indians (NRIs) or Export Oriented Units (EOUs) requiring approval of the Government will be dealt with by the Department of Industrial Policy and Promotion (DIPP), that will continue to be the administrative Ministry for this purpose. The DIPP will also handle applications relating to issue of equity shares under the Government route for import of capital goods, machinery or equipment, as well as applications relating to issue of equity shares for pre-operative / pre-incorporation expenses. DIPP has been entrusted with the responsibility of identifying the administrative ministry or department in respect of applications where there is a doubt regarding the administrative ministry concerned.

Further, it is envisioned that ordinarily FDI applications, including the applications from NRI, EOU, food processing, single brand retail trading and multi brand retail trading will be decided in 60 (sixty) days. In situations wherein the application is proposed to be rejected by the competent authority or where approval is proposed subject to additional conditions not provided in the FDI Policy, the concurrence of DIPP would be mandatory.

The concerned administrative ministry / department would be responsible for monitoring the compliance of conditions under the FDI approvals, including past FDI applications approved by FIPB. To ensure accountability of a concerned ministry / department, the Memorandum provides for a joint quarterly review meeting to be undertaken by a committee co-chaired by Secretary, Department of Economic Affairs, and Secretary, DIPP which shall focus on pending FDI proposals. The Secretary of the concerned department / ministry may be asked to attend such meeting, as required.

The concerned administrative ministry / department would be responsible for handling any litigations / liabilities / claims that may arise.

Files in possession of the FIPB Secretariat, as well as pending RTI applications and appeals, shall be transferred to the concerned ministry / department.

The Government has also launched a new online Foreign Investment Facilitation Portal for foreign investment proposals, which will be responsible for processing FDI proposals in a time bound manner thereby creating a conducive atmosphere for investment inflow in the country. The SOP for processing FDI proposals has also been released in this regard. It is felt that with the allocation of approval of FDI proposals to concerned ministries / departments, the pendency of FDI proposals with Government is expected to reduce since the facilitation of FDI proposal from FIPB for the concerned ministry's approval and review will no longer be required.

**Insolvency and Bankruptcy Board of India (Inspection and Investigation) Regulations, 2017 notified:** The Insolvency and Bankruptcy Board of India (IBBI) has notified the Insolvency and Bankruptcy Board of India (Inspection and Investigation) Regulations, 2017 on 12th June, 2017. The Regulations stipulate a procedure for inspection by the IBBI of records of various service providers (insolvency professional agencies, insolvency professionals, insolvency professional entities and information utilities) for ensuring compliance with the Insolvency and Bankruptcy Code ('Code'). To initiate inspection, the IBBI is required to serve a 10 (ten) day notice to the service provider who is proposed to be inspected. The Regulations also provide that an Inspection Authority and an Investigating Authority, consisting of officers from IBBI, shall be constituted to conduct inspection and investigation.

An interim inspection report may be submitted by the Inspecting Authority to IBBI, and if the said report suggests that there is a gross violation of the Code on the part of the service provider, then IBBI shall refer the matter to the Disciplinary Committee (a committee constituted by IBBI, consisting of whole time members of IBBI) for appropriate action, which may then pass an interim order against the defaulting service provider, which order shall expire in 90 (ninety) days. A final inspection report shall then be prepared by the Inspecting Authority and submitted to IBBI.

Similar powers have been given to IBBI, in relation to investigation of service providers, by the Investigating Authority constituted by IBBI. Once IBBI is in receipt of the reports given by the Inspecting Authority and the Investigation Authority, if IBBI is satisfied that *prima facie,* a case can be taken against the service provider, then IBBI shall issue a show cause notice to the defaulting service provider and refer the same, along with relevant records and written submissions, if any, made by such service provider, to the Disciplinary Committee. The Disciplinary Committee shall then dispose of the case in 180 days from the issue date of the show cause notice, by passing an order against the defaulting service provider, which *inter-alia* may stipulate suspension or cancellation of registration of the defaulting service provider. Normally, an order passed by the Disciplinary Committee shall be effective only after 30 (thirty) days have elapsed from the date of issue of such order.

Furthermore, the Regulations also provide that when a direction is issued to any person for disgorgement of amount under Section 220 (4) of the Code, as soon as after such an amount has been realised by IBBI, a public announcement shall be made inviting claims from people seeking restitution from the disgorged amount. IBBI, upon scrutiny of the said claims shall prepare a list of valid claims, and disburse proportionate amounts to the claimants within 30 (thirty) days from the date of making the said list.

**Insolvency and Bankruptcy Board of India (Fast Track Insolvency Resolution Process for Corporate Persons) Regulations, 2017 notified:** Chapter IV (i.e. Section 55 to Section 58) of the Insolvency and Bankruptcy Code ('Code') dealing with the fast track corporate insolvency resolution process, has come into force with effect from June 14, 2017 *vide* Notification S.O.1910(E) dated June 14, 2017 issued by the Ministry of Corporate Affairs. The Ministry of Corporate Affairs, by Notification S.O.1911(E) dated June 14, 2017, has also notified the categories of debtors in respect of which an application for fast track corporate insolvency resolution process may be made:

(a) a small company; or

(b) a Start-up (other than a partnership firm) as defined by the Ministry of Commerce and Industry; or

(c) an unlisted company with total assets (as reported in financial statement of immediately preceding financial year) not exceeding Rs.1 Crore.

Simultaneously, the Insolvency and Bankruptcy Board of India (IBBI) has on June 14, 2017 notified the Regulations governing the fast track corporate insolvency resolution process. The Regulations envision a maximum 90-day period (commencing from date of admission of an application for initiating the fast track process) for the insolvency resolution process to be completed. However, if the committee of creditors established under the Code is of the opinion that the insolvency resolution process cannot be completed within the stipulated 90-day period, the committee is empowered to instruct the resolution professional to make an application to the Adjudicating Authority (i.e. National Company Law Tribunal) for seeking an extension. As per Section 56 of the Code, the NCLT may extend the duration of the insolvency resolution process beyond the said 90-day period as it deems fit, provided such extension does not exceed 45 days.

# Ratio Decidendi

## Mismanagement by a Director leads to removal from directorship in a Company

*Facts:*

The Petitioner was a promoter and Director of the Respondent 1 (The Company), incorporated on 15.12.2003, along with his father (Respondent 2) and brother (Respondent 3). The Company structure was such that each Director managed and administered separate construction projects within his scope and was functioning as a separate individual cost/profit centre. The Company received money into a Master Account, which was then transferred to three separate sub-accounts from time to time for the purpose of carrying out projects falling within the scope of individual Directors. Though the three sub-accounts were also in the name of the Company, each Director independently administered his sub-account vis-à-vis projects within his scope.

The Company had an overdraft facility with South Indian Bank Ltd. (Respondent 4; The Bank) which was renewed periodically. The monies drawn from the Overdraft A/c were transferred to sub-accounts and the sub-accounts would transfer realization to the Master Account to repay such overdraft. The Directors were required to prepare various reports regarding the projects under their centers with details about the work-in-progress, financial statements, etc.

The dispute arose when Respondent 3 tried to secure the release of personal properties charged with the Bank, without the consent or knowledge of the Petitioner, when huge outstanding amounts lay pending with Respondent No. 3's project/cost centres, and resultant arrears to the bankers in discharging overdraft liability, to which the Petitioner objected through a letter dated 5.8.2010. As on 31.03.2012, Respondent No. 3 had overdrawn his sub-account upto Rs. 16.48 crores. Further, Respondent 2, along with Respondent 3 began to sideline the Petitioner from Board and shareholder meetings.

*Decision:*

The Petitioner contended that he cannot be made liable for the losses incurred/shortfall arising due to mismanagement of funds by Respondent 3 who had overdrawn his sub-account upto Rs.16.48 crores, and that Respondent 3 was responsible and liable for the losses suffered by the Company. With respect to the contention that Respondents 2 and 3 were not fit to be managing the affairs of the Respondent Company and therefore should be removed from the Board of Directors, it was held that Respondent 3 had indeed caused losses to the Company, constituting mismanagement of the Company and Respondent 2 had failed to implement corrective measures. The Petitioner on the other hand, had handled all his projects diligently.

Therefore, Respondent 3 was removed from his Directorship of the Company and the Petitioner was appointed as the Director-cum-Managing Director. Respondent 2 was directed to assist and support the newly appointed Managing Director. With regard to the contention that Respondent No. 3 ought to indemnify the Company and the Petitioner against default in payment to the creditors, it was held that the overdrawn amount of Rs. 16.48 Crores along with interest was liable to be paid only by Respondent 3 as such money was overdrawn by him through his sub-account of the Company. [*Rojer Mathew P* v. *P.T. Mathai Construction Company Pvt. Ltd.* – Order dated 7th June, 2017, NCLT (Chennai) Division Bench]

**New legislative provision affecting substantive rights is prospective unless made retrospective either expressly or by necessary intendment**

Providing clarity on the situation wherein repeal of an enactment is followed by a fresh legislation and how this might impact the substantive or vested rights of parties in a litigation, National Company Law Tribunal (NCLT) has held that generally, a new legislative provision will be prospective in nature if it affects the substantive or vested rights of the parties, unless made retrospective either expressly or by necessary intendment. However, if a new legislation is procedural in nature, then it is presumed to operate retrospectively.

*Facts:*

The matter arose out of non-payment of Petitioner's salary dues, for rendering services to the Respondent. The Petitioner filed an application under Section 433 (b), (c), (e) and (f) read with Section 434 of the Companies Act, 1956 in the High Court of Delhi, praying that the Respondent company be wound up.

Upon issuance of Companies (Transfer of Pending Proceedings) Rules, 2016 (Transfer Rules), the petition was transferred to NCLT on March 2, 2017 *per* Rule 5[4] of Transfer Rules read

[4] Rule 5 (1), Companies (Transfer of Pending Proceedings) Rules, 2016 read with Rule 2, Companies (Transfer of Pending Proceedings) Amendment Rules, 2017:
*"**5. Transfer of pending proceedings of Winding up on the ground of inability to pay debts**.—(1) All petitions relating to winding up under clause (e) of section 433 of the Act on the ground of inability to pay its debts pending before a High Court, and where the petition has not been served on the respondent as required under rule 26 of the Companies*

with Rule 2 of Companies (Transfer of Pending Proceedings) Amendment Rules, 2017 (Transfer Amendment Rules). As per Rule 5(1) of the Transfer Rules, Company petitions filed under Section 433(e) of Companies Act, 1956, are to be transferred to NCLT, provided notice of the petition had not been served on the respondent. The proviso to Rule 5(1) mandates a petitioner to submit complete information necessary for admission of the petition to NCLT (including details of the proposed insolvency professional), within a 60-day period from the date of the notification which expired on 07.02.2017, failing which the petition would abate. However, this 60-day period was subsequently increased to 6 months vide the Transfer Amendment Rules dated 28.02.2017. In accordance with the Transfer Rules and Transfer Amendment Rules, the Petitioner filed an application on April 10, 2017 praying that the application be considered as an application under Section 9 of the Insolvency and Bankruptcy Code, 2016 (IBC). However, the petition did not name any insolvency professional.

*Contentions:*

**Contentions of Petitioner:** Provisions of Section 433 of Companies Act, 1956 will continue to be applicable in the instant case. Neither the provisions of Companies Act, 2013 (2013 Act) nor IBC would be applicable since the substantive rights of the Petitioner that had arisen on filing the petition before High Court of Delhi (in July 2016), could not be altered or modified by any subsequent legislative amendments .

Alternatively, the Petitioner contended that even if the provisions of IBC were applicable, the Petitioner would still be covered within the ambit of an 'operational creditor' under Section 5 (20)[5] read with Section 5 (21)[6] and Section 8 & 9 of IBC. Further, notice of demand previously issued by Petitioner under Section 433 of the erstwhile Companies Act, 1956 must be deemed as a notice of demand issued under Section 8 (1) of IBC, since the notice substantively satisfies all requirements of Section 8 (1) of IBC. Therefore, the Petitioner was not required to serve a fresh notice of demand upon the Respondent to initiate insolvency proceedings.

**Contentions of Respondent:** In the instant case, the petitioner was required to have filed a compliance affidavit within the 60-day period, i.e. before 07.02.2017. As the Petitioner's application purporting to show compliance of the IBC had been filed in April 2017, the Respondent argued that the petition had abated since such requirement under proviso to Rule 5 (1) of Transfer Rules had not been satisfied by the Petitioner. Once the petition had abated, the subsequent notification issued on 28.02.2017, increasing the above-mentioned time period from 60 days to 6 months, cannot infuse a new life into the abated petition.

The petition was grossly defective and incomplete. *Per* Section 9 (1) of IBC, the Petitioner had failed to send any demand notice to the Respondent company. Delivery of demand

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*(Court) Rules, 1959 shall be transferred to the Bench of the Tribunal established under sub-section (4) of section 419 of the Act, exercising territorial jurisdiction and such petitions shall be treated as applications under sections 7, 8 or 9 of the Code, as the case may be, and dealt with in accordance with Part II of the Code:*

*Provided that the petitioner shall submit all information, other than information forming part of the records transferred in accordance with Rule 7, required for admission of the petition under sections 7, 8 or 9 of the Code, as the case may be, including details of the proposed insolvency professional to the Tribunal within* ***sixty days*** *from date of this notification, failing which the petition shall abate."; read with*

*"**2.** In the Companies (Transfer of Pending Proceedings) Rules, 2016, in rule 5, in sub-rule (1) in the proviso for the words "sixty days" the words "**six months**" shall be substituted."*

[5] Section 5 (20), Insolvency and Bankruptcy Code, 2016:

*"**5 (20).** "operational creditor" means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred"*

[6] Section 5 (21), Insolvency and Bankruptcy Code, 2016:

*"**5 (21).** "operational debt" means a claim in respect of provision of goods or services including employment or a debt in respect of the repayment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority"*

notice under Section 8[7] of IBC is a condition precedent to filing of an application under Section 9 of IBC for initiating the insolvency resolution process. The Petitioner had issued a notice dated May 7, 2016 to the Respondent under Section 271 of the 2013 Act. However, Section 271 was not in force at the time, and only came into effect from December 15, 2016. Additionally, the notice issued by Petitioner cannot be considered as a demand notice issued under Section 8 of IBC as the effect of both notices was different. Thus, in the absence of a demand notice, the Petitioner cannot approach NCLT for initiating insolvency resolution proceedings. The Petitioner had not complied with conditions laid down in Section 9 (3) (c) of IBC which provides that a certificate from the financial institution maintaining its accounts be furnished. The Petitioner had also not furnished an affidavit stating that no notice has been given by the operational creditor regarding existence of a dispute relating to the operational debt.[8]

### *Issue:*

Whether provisions of Section 433 of the erstwhile Companies Act, 1956 continue to apply or provisions of IBC would be applicable.

### *Observations:*

NCLT observed that provisions concerning winding up of a company due to its inability to pay debts as incorporated under Section 271 (2) of the 2013 Act or in Section 433 (e) of the Companies Act, 1956, have been substituted by provisions of IBC which allow a financial creditor or operational creditor to approach NCLT either under Section 7, 8 or 9 of IBC.

NCLT noted that a new legislation cannot be presumed to apply retrospectively if it affects substantive or vested rights of parties, unless it is expressly provided or becomes apparent by the words of provision. However, if a new legislation is procedural in nature, it is presumed to operate retrospectively.

While rejecting the Petitioner's contentions, NCLT held that there is no substantive or vested right with the Petitioner to seek winding up of the Respondent company till the time the process of winding up has been initiated. The Petitioner had not acquired any substantive/vested right to seek winding up of the Respondent company, by merely filing a petition. *Per* Transfer Rules, cases wherein notice was served were to be retained by the respective High Courts whereas in cases where notices were not served were to be transferred to NCLT. Further, the nature of the remedy continues to be available to the Petitioner under IBC which may eventually result into liquidation of the Respondent company. The omission of Section 433 (e) of Companies Act, 1956 had not taken away any substantive or vested right of the Petitioner. Rather, with the IBC coming into force, such rights have been 're-regulated'.

### *Judgment:*

NCLT dismissed the application filed by Petitioner since the application fell short of numerous compliances provided under IBC, thereby failing to satisfy the criteria laid down under Section 9 of the IBC for triggering insolvency resolution process.

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[7] Section 8 (1), Insolvency and Bankruptcy Code, 2016:
*"**8 (1). Insolvency resolution by operational creditor**: An operational creditor may, on the occurrence of a default, deliver a demand notice of unpaid operational debtor copy of an invoice demanding payment of the amount involved in the default to the corporate debtor in such form and manner as may be prescribed."*

[8] Section 9 (3), Insolvency and Bankruptcy Code, 2016:
*"**9 (3). Application for initiation of corporate insolvency resolution process by operational creditor:** The operational creditor shall, along with the application furnish— (a) a copy of the invoice demanding payment or demand notice delivered by the operational creditor to the corporate debtor; (b) an affidavit to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt; (c) a copy of the certificate from the financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor; and (d) such other information as may be specified."*

*Analysis:*

NCLT has provided clarity in respect of transfer of pending applications under the Transfer Rules read with Transfer Amendment Rules. NCLT has expressly held that the requirements laid down under Sections 8 and 9 of IBC for initiating corporate insolvency resolution process must be strictly followed to ensure that the process for liquidating a company is not detrimental to the interests of the company. [*Prem Sarup Narula* v. *Bycell Telecommunications (I) Private Limited* - C.P No. 7902016, Order dated 12-5-2017, NCLT, New Delhi]

## Amalgamation when form for Board resolution, and annual returns not filed

*Facts:*

The matter arose due to objections raised by the Regional Director in response to the petition filed by the Petitioners in relation to the amalgamation scheme. The Regional Director contended that: (i) the Transferee Company was in contravention of the 2013 Act[9] as it failed to file Form MGT-14 for the Board resolution pertaining to approval of the proposed Scheme with the Regional Director within prescribed timelines; (ii) Transferor Company No. 1 failed to file their annual returns and balance sheet for the financial year 2015-2016, being in contravention of the 2013 Act[10]; (iii) Transferor Company No. 2 failed to register as a Non-Banking Financial Institution (NBFC), given that the objectives stated in its Memorandum of Association were similar to the activities carried out by an NBFC**;** and (iv) the Transferee Company failed to register as an NBFC when its financial assets constituted more than fifty per cent of its total assets.

The Petitioners contended that filing of the above-mentioned Form MGT-14 with the Regional Director is a procedural requirement for intimating the Registrar of Companies (RoC). They argued that non-compliance of the abovementioned contentions should not cost the stakeholders, and that the process of filing the same had also commenced.

Further, the Petitioners contended that neither the Transferor Company No. 2 nor the Transferee Company were NBFCs and relied on the interpretation of the term '*financial assets*' as defined by the Reserve Bank of India (RBI) *vide* its notification with respect to *"Non Recurring Fixed Deposits with Banks as Financial Assets".* As per this Notification, 'investments in fixed deposits' cannot be treated as financial assets and therefore, receipt of interest income on fixed deposits with banks cannot be treated as income from financial assets as these are not covered under the activities mentioned in the definition of financial institution[11]. The Petitioners also showed proof of having filed annual returns and balance sheet for the financial year 2015-2016.

*Observations:*

NCLT, in view of the approval to the proposed Scheme accorded by the members and creditors of the Petitioners, along with the report received from the Official Liquidator showing no objection by any interested parties, approved the proposed Scheme. NCLT further acknowledged that as the Petitioner did not qualify as an NBFC and was not required to have registered as an NBFC with the RBI, the question of obtaining prior written permission from RBI with respect to the proposed Scheme did not arise.

NCLT observed that, the Petitioners shall remain bound to comply with the statutory requirements in accordance with law even after the Scheme has been sanctioned. Any contravention of the law, would attract action against the concerned persons, directors and officials of the Petitioners.

[9] Section 117(1) read along with section 179 (3) of the Act

[10] Section 129 read along with Section 134 and Section 137 of the Act

[11] Notification No. RBI DNBS (PD) CC. NO. 259/03.02.59/2011-12 dated 15.03.2012

*Judgment:*

NCLT granted sanction to the Scheme. However, it was clarified that such an order must not be construed as an order granting exemption in any manner, from payment of stamp duty, taxes or other charges, if any, and payment in accordance with law or in respect to any permission / compliance with any other requirement which may be specifically required under any law.

*Analysis:*

In this ruling, NCLT confirmed that as long as petitioners have not conducted the business in a manner prejudicial to the interest of its members, creditors or the public and have not violated provisions of the Companies Act, 1956/2013, Foreign Exchange Management Act, 1999, Securities and Exchange Board of India Act, 1992, Reserve Bank of India Act, 1934 etc., as applicable, their petition seeking approval of a scheme of amalgamation will be allowed. [*Superlite Auto Private Limited*, In Re, C.P No. 1101 of 2016, C.A (M) No. 110 of 2016 – Order dated 11-5-2017, NCLT, New Delhi]

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