CASE UPDATES

National Company Law Appellate Tribunal (NCLAT)
M/s. Innoventive Industries Ltd. (Appellant/Corporate Debtor)
Vs.
ICICI Bank & Anr. (Respondents/Financial Creditor)
Date of Order: 15-05-2017

Section 60 read with sections 7,8 & 9 of the Insolvency and Bankruptcy Code, 2016 read with Rule 4(3) of the Insolvency and Bankruptcy (Application to Adjudication Authority) Rules, 2016 read with Section 424 of the Companies Act, 2013 and Section 4 of the Maharashtra Relief Undertaking (Special Provisions) Act, 1958 – Adjudicating Authority for Corporate Persons

FACTS:

Pursuant to default in payment of dues the financial creditor filed an application under section 7 of the IB Code. The corporate debtor filed an interim Application stating that the Industry, Energy and Labour Department of Maharashtra has passed a relief under the provision of the Maharashtra Relief Undertaking (Special Provisions) Act, 1958 (Bombay Act XCVI of 1958) (hereinafter referred to as MRU Act 1958) suspending the liabilities of the Corporate Debtor and remedies against the debtor for one year from 22.7.2016 and therefore the financial Creditor could not have invoked this relief till 21st July, 2017.

The Adjudicating Authority/Tribunal held that IB Code has come into existence subsequent to MRU Act 1958 and therefore, Non-Obstante clause in section 238 of IBC prevails upon any other law for the time being in force, hence it could not be said that Notification given under MRU Act will become a bar to passing order u/s. 7 of the IB Code. Moreover, the objective under MRU Act, is to prevent unemployment of the existing employees of an industry which is recognized as relief undertaking, but by passing an order u/s. 7 it will not cause any obstruction to their employment until next 180 days, even if the company goes into liquidation, then also the rights of the employees are protected to the extent mentioned under IB Code. The Application filed by the Corporate Debtor was therefore dismissed. The Tribunal also dismissed the plea of the corporate debtor that notice has not been served on the ground that this plea pales into insignificance because this Bench has already heard the Corporate Debtor's application which was already been dismissed. The Adjudicating Authority/Tribunal on perusal of the documents filed by the financial creditor found that the application under section 7(2) is complete and therefore admitted the same declaring moratorium. Aggrieved with the order of the Tribunal the appellant/corporate debtor filed this appeal.

The questions involved in this appeal are:

(i) Whether a notice is required to be given to the Corporate Debtor for initiation of Corporate Insolvency Resolution Process under IB Code and if so, at what stage and for what purpose?

(ii) Whether MRU Act 1958 shall prevail over IB Code. In other words, whether a Corporate Debtor who is enjoying the benefit of MRU Act, can be subjected to IB Code? and

(iii) Whether in a case where Joint Lender Forum (JLF) have reached agreement and granted permission to the Corporate Debtor prior consent of JLF is required by financial creditor, before filing of an application under Section 7 of the IB Code?

DECISION:

1st issue:

After considering various decisions of the Supreme Court it was observed that "useless formality" is another exception to the ratio of natural justice. Where on the admitted or undisputed facts only one conclusion is possible and under the law only one penalty is permissible, the Court may not insist on the observance of the principles of natural justice because it would be futile to order its observance. Therefore, where the result would not be different, and it is demonstrable beyond doubt, order of compliance with the principles of natural justice will not be justified.

Further from the decisions of Hon'ble Supreme Court, the exception on the Principle of Rules of natural justice can be summarised as follows:-

(i) Exclusion in case of emergency,

(ii) Express statutory exclusion

(iii) Where discloser would be prejudicial to public interests

(iv) Where prompt action is needed,

(v) Where it is impracticable to hold hearing or appeal,

(vi) Exclusion in case of purely administrative matters.

(vii) Where no right of person is infringed,

(viii) The procedural defect would have made no difference to the outcome.

(ix) Exclusion on the ground of 'no fault' decision maker etc.

(x) Where on the admitted or undisputed fact only one conclusion is possible - it will be useless formality.

There is no specific provision under the I&B Code, 2016 to provide hearing to corporate debtor in a petition under Section 7 or 9 of the I&B Code, 2016. I&B Code, 2016 empowers 'adjudicating authority' to pass orders under Section 7, 9 and 10 of the Code, 2016 and not the National Company Law Tribunal. It is by virtue of the definition under sub-Section (1) of Section 5 read with section 60 of the I&B Code, 2016, the National Company Law Tribunal plays role of an "adjudicating authority".

As amended Section 424 of the Companies Act, 2013 is applicable to the proceeding under the I&B Code, 2016, it is mandatory for the adjudicating authority to follow the Principles of rules of natural justice while passing an order under I&B Code, 2016. Further, as Section 424 mandates the 'Tribunal' and Appellate Tribunal, to dispose of cases or/appeal before it subject to other provisions of the Companies Act, 2013 or IB Code 2016 such as, Section 420 of the Companies Act, 2013 was applicable and to be followed by the Adjudicating Authority. Thus it is clear that sub-Rule (3) of Rule 4 of I&B (Application to Adjudicating Authority) Rules, 2016, mandates the applicant to dispatch forthwith, a copy of the application "filed with the Adjudicating Authority". Thereby a post filing notice required to be issued and not as notice before filing of an application. The purpose for the same being to put corporate debtor to adequate impound notice so that the Corporate Debtor may bring to the notice of Adjudicating Officer "mitigating factor/records before the application is accepted even before formal notice is received."

The insolvency resolution process under Section 7 or Section 9 of I&B Code, 2016 have serious civil consequences not only on the corporate debtor - company but also on its directors and shareholders in view of the fact that once the application under Sections 7 or 9 of the I&B Code, 2016 is admitted it is followed by appointment of an 'interim resolution professional' to manage the affairs of the corporate debtor, instant removal of the board of directors and moratorium for a period of 180 days. For the said reason also the Adjudicating Authority is bound to issue limited notice to the corporate debtor before admitting a case under section 7 and 9 of the 'I & B Code', 2016.

The Adjudicating Authority is bound to issue a limited notice to the corporate debtor before admitting a case for ascertainment of existence of default based on material submitted by the corporate debtor and to find out whether the application is complete and or there is any other defect required to be removed. Adherence to Principles of natural justice would not mean that in every situation the adjudicating authority is required to afford reasonable opportunity of hearing to the corporate debtor before passing its order.

The Adjudicating Authority post ascertaining and being satisfied that such a default has occurred may admit the application of the financial creditor. In other words, the statute mandates the Adjudicating Authority to ascertain and record satisfaction as to the occurrence of default before admitting the application. Mere claim by the financial creditor that the default has occurred is not sufficient. The same is subject to the Adjudicating Authority's summary adjudication, though limited to 'ascertainment' and 'satisfaction'.

It is evident from Section 9 of the I & B Code that the Adjudicating Authority has to, within fourteen days of the receipt of the application under sub-section (2), either admit or reject the application. Section 9 has two-fold situations insofar as notice of dispute is concerned. As per sub-section (5)(i) of Section 9, the Adjudicating Authority can admit the application in case no notice raising the dispute is received by the operational creditor (as verified by the operational creditor on affidavit) and there is no record of a dispute is with the information utility. On the other hand, sub-section (5)(ii) of Section 9 mandates the Adjudicating Authority to reject the application if the operational creditor has received notice of dispute from the corporate debtor. Section 9 thus makes it distinct from Section 7. While in Section 7, occurrence of default has to be ascertained and satisfaction recorded by the Adjudicating Authority, there no similar provision under Section 9. Under Section 7 neither notice of demand nor a notice of dispute is relevant whereas under Sections 8 and 9 notice of demand and notice of dispute become relevant both for the purposes of admission as well as for the rejection.

While ascertaining, the 'Adjudicating Authority' comes to a conclusion whether there is an existence of default for the purpose of section 7 or there is a dispute raised by the corporate debtor and all other purpose whether an application is complete or incomplete, it is not only necessary to hear the Financial Creditor/Operational Creditor but also the Corporate Debtor.

The different decisions of the Hon'ble Supreme Court and exception of principles of natural justice as summarised in the preceding paragraphs is not applicable to the insolvency resolution process as it is not a case of emergency declared or prejudicial to public interest or that there is a statutory exclusion of rules of natural justice or it is impracticable to hold hearing. It is not the case that no right of any person has been affected, as immediately on appointment of an Interim Resolution Professional, the Board of directors stand superseded. There are other persons who are also affected due to order of moratorium. Therefore, the 'adjudicating authority' is duty bound to give a notice to the corporate debtor before admission of a petition under Section 7 or Section 9.

In the present case though no notice was given to the Appellant before admission of the case but it was found that the Appellant intervened before the admission of the case and all the objections raised by appellant has been noticed, discussed and considered by the 'adjudicating authority' while passing the impugned order dated 17th January 2017. Thereby, merely on the ground that the Appellant was not given any notice before admission of the case cannot render the impugned order illegal as the Appellant has already been heard. If the impugned order is set aside and the case is remitted back to the adjudicating authority, it would be 'useless formality' and would be futile to order its observance as the result would not be different. Therefore, order to follow the principles of natural justice in the present case does not arise.

However, in some of the cases initiation of Insolvency Resolution Process may have adverse consequences on the welfare of the Company. Therefore, it will be imperative for the "adjudicating authority" to adopt a cautious approach in admitting Insolvency Application by ensuring adherence to the principle of natural justice.

2nd Issue:

The Schedule to the MRU Act specifies only certain acts to which the restriction applies. Accordingly, the application of the MRU Act can only be extended to such acts as specified in the schedule and no other legislation. The legislations referred to in the 'schedule' to the MRU Act are employment welfare related which is in consonance with the objects and purposed of the MRU Act i.e. 'employment and unemployment'. The protection under the MRU Act, therefore, cannot be extended to other legislations especially to union legislation which is subsequent to the MRU Act and related to insolvency resolution i.e. I&B Code, 2016. Section 4 of the MRU Act, including Section 4 (iv), therefore, is limited in scope to the acts listed in the schedule thereto.

The MRU Act operates in a different field from the I&B Code, 2016. MRU Act is an Act to make temporary provisions for industrial relations and other matters to enable the State Government to conduct or to provide a loan, guarantee or financial assistance for the conduct of certain industrial undertakings 'as a measure of preventing unemployment or of unemployment relief.'

On the other hand the I&B Code, 2016 is an Act enacted to consolidate and amend the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximization of value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interest of all the stakeholders including alteration in the order of priority of payments of Government dues. The I&B Code, 2016, which is later act of greater specificity, seeks to balance the interests of all stake holders.

Section 238 of the I&B Code, 2016 is non-obstante clause which overrides the operation of the MRU Act. As per Section 238 of the I&B Code, 2016 the provisions of the Code are to be given effect to notwithstanding anything contrary contained any other law or any instrument having effect under such law.

In view of the aforesaid objects of the two enactments it is apparent that the two enactments operate in entirely different fields. This is further made clear by the fact that the MRU Act is enacted under Entry 23 of List III while the Code has been enacted under Entry 9 of the List III. The MRU Act has received Presidential assent under Article 254(2) of the Constitution of India, which is only required for statutes enacted by the State Government in exercise of its legislative competence under the Concurrent List.

In light of the aforementioned non-obstante provision (which is a subsequent Union Law), the provisions of the I&B Code, 2016 shall prevail over the provisions of the MRU Act and any instrument issued under the MRU Act including the Notification.

Following the law laid down by Hon'ble Supreme Court in Yogender Kumar Jaiswal Vs. State of Bihar, (2016) 3 SCC 183 and Madras Petrochem Limited and Another Vs. Board for Industrial and Financial Reconstruction and Others," (2016) 4 SCC 1 it was held that there is no repugnancy between I&B Code, 2016 and the MRU Act as they both operate in different fields. The Parliament has expressly stated that the provisions of the I&B Code, 2016 (which is a later enactment to the MRU Act) shall have effect notwithstanding the provisions of any other law for the time being in force. This stipulation does not mean that the provisions of MRU Act or for that matter any other law are repugnant to the provisions of the Code.

In view above, it was held that the Appellant was not entitled to derive any advantage from MRU Act, 1958 to stall the insolvency resolution process under Section 7 of the I&B Code.

3rd Issue:

The Tribunal has noticed that there is a failure on the part of appellant to pay debts. The Financial Creditor has attached different records in support of default of payment. Apart from that it is not supposed to go beyond the question to see whether there is a failure on fulfilment of obligation by the financial creditor under one or other agreement, including the Master Restructuring Agreement. In that view of the matter, the Appellant cannot derive any advantage of the Master Restructuring Agreement dated 8th September, 2014.

For initiation of corporate resolution process by financial creditor under sub-section (4) of Section 7 of the Code, the 'adjudicating authority' on receipt of application under sub-section (2) is required to ascertain existence of default from the records of Information Utility or on the basis of other evidence furnished by the financial creditor under sub-section (3). Under sub-section 5 of Section 7, the 'adjudicating authority' is required to satisfy:-

(a) Whether a default has occurred;

(b) Whether an application is complete; and

(c) Whether any disciplinary proceeding is against the proposed Insolvency Resolution Professional.

Once it is satisfied that it is required to admit the case but in case the application is incomplete application, the financial creditor is to be granted seven days' time to complete the application. However, in a case where there is no default or defects cannot be rectified, or the record enclosed is misleading, the application has to be rejected.

Beyond the aforesaid practice, the 'adjudicating authority' is not required to look into any other factor, including the question whether permission or consent has been obtained from one or other authority, including the JLF. Therefore, the contention of the petition that the Respondent has not obtained permission or consent of JLF to the present proceeding which will adversely affect loan of other members cannot be accepted and fit to be rejected.

In the aforesaid circumstances the 'adjudicating authority' having satisfied on all counts, including default and that the application is complete and that there is no disciplinary proceeding pending against the Insolvency Resolution Professional, no interference is called for against the impugned judgment.

CASE REVIEW:

Order dated 17th January, 2017 and Order dated 23rd January, 2017 passed by National Company Law Tribunal, Mumbai Bench, Mumbai in ICICI Bank Ltd. Vs. M/s. Innoventive Industries Ltd. (C.P. No. 1/I&BP/NCLT/MB/MAH/2016), Upheld.

National Company Law Appellate Tribunal (NCLAT)
M/s. Starlog Enterprises Ltd. (Appellant/Corporate Debtor)
Vs.
ICICI Bank Ltd. (Respondent/Financial Creditor)
Date of Order: 24-05-2017

Section 61 read with Sections 7, 9 & 75 of the Insolvency and Bankruptcy Code, 2016 – Appeals and Appellate Authority

FACTS:

Financial Creditor/Applicant having failed to realise the outstanding dues filed an application under section 7 of the Code before the Adjudicating Authority/NCLT. The applicant filed proof for service of notice to the corporate debtor. The NCLT satisfied that there was a default on the part of corporate debtor and passed an ex parte order admitting the application filed under section 7 of the Code declaring moratorium.

The corporate debtor/appellant filed an appeal against the order of NCLT on the following grounds:

1. In absence of notice given to the Appellant before admitting the case under Section 7 of the Code, the impugned order is violative of rules of natural justice.
2. The application under Section 7 by the Financial Creditor is incomplete, misleading and being not bona fide was fit to be rejected.
3. The impact of the appointment of Insolvency Resolution Professional on the business and management of the appellant was that in view of the mismanagement the appellant has incurred financial losses as one of its contracts was terminated and also suffered loss of several valuable human resources.

DECISION:

It is clear that before admitting an application under Section 9 of the Code it is mandatory duty of the 'adjudicating authority' to issue notice. In the present case admittedly no notice was issued by the 'adjudicating authority' to the corporate debtor, before admitting the application filed under Section 9 of the Code. For the said reason the judgement order cannot be upheld having passed in violation of principle of natural justice.

Showing an incorrect claim, moving the application in a hasty manner and obtaining an ex-parte order from the 'adjudicating authority' which admitted such an incorrect claim, the Financial Creditor cannot disprove its mala fide intention by stating that the claim submitted is correct amount. The I&B Code does not provide for any such mechanism where post-admission, the applicant financial creditor can modify their claim amount.

In some of the cases, an insolvency resolution process can and may have adverse consequences on the welfare of the company. This makes it imperative for the 'adjudicating authority' to adopt a cautious approach in admitting insolvency applications and also ensuring adherence to the principles of natural justice.

For the reasons aforesaid, the appellate Tribunal set aside the ex-parte impugned order passed by NCLT.

In effect the appointment of Interim Resolution Professional, order declaring moratorium, freezing of account and all other order passed by 'adjudicating authority' pursuant to impugned order and action taken by the Interim Resolution Professional, including the advertisement published in the newspaper calling for applications are declared illegal. The 'adjudicating authority' is directed to close the proceeding. The appellant company is released from the rigour of law and allow the appellant company to function independently through its Board of Directors from immediate effect.

The Tribunal imposed a penalty of Rs. 50,000/- on Respondent/Financial Creditor.

CASE REVIEW:

Order dated 17th February, 2017 passed by NCLT, Mumbai Bench, in ICICI Bank Ltd. Vs. M/s. Starlog Enterprises Ltd. (C.P. No.12/I&B/NCLT/MAH/2017), set aside.

Hope you find this Update helpful.
Suggestions if any, may be mailed to ipa@icai.in