

# Role of NCLT under the Insolvency and Bankruptcy Code, 2016

**By:**

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The Code recognizes National Company Law Tribunal (**the NCLT**) constituted under Section 408 of the Companies Act, 2013 as Adjudicating Authority for the purpose of insolvency resolution and liquidation for corporate persons.

The Code also recognizes Debt Recovery Tribunal (**the DRT**) constituted under subsection (1) of Section 3 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 as Adjudicating Authority for the purpose of insolvency resolution and bankruptcy of partnership firms and individuals.

# **Jurisdiction of NCLT**

Situs of the registered office of the corporate entity is the deciding criteria for insolvency resolution and liquidation of corporate persons, corporate debtors and personal guarantors thereof. Application for initiating insolvency resolution process or liquidation of corporate debtor shall be filed before the NCLT having jurisdiction over the place where registered office of the corporate entity is situated.

Similarly, voluntary liquidation application of corporate person shall be filed before the NCLT having jurisdiction over the place where registered office of the corporate entity is situated.

Though, DRT is recognized as adjudicating authority for partnership firms and individuals, but, where an individual is personal guarantor of a corporate debtor and a corporate insolvency resolution process or liquidation proceedings of such corporate debtor is pending before a NCLT, an application relating to the insolvency resolution or bankruptcy of personal guarantor of such corporate debtor shall also be filed before such NCLT.

In dealing with the application relating to the insolvency resolution or bankruptcy of personal guarantor of corporate debtor the NCLT shall be vested with the powers of DRT dealing with the insolvency resolution or bankruptcy of individual.

## **Admission of IRP Application**

An Insolvency Resolution Process can be initiated by-

- a) Financial creditor or
- b) Operational Creditor or
- c) Corporate itself.

Under Section 7 - Financial creditor can, either alone or jointly with others, file an application before NCLT for initiating IRP when default has occurred.

Default includes a default in respect of a financial debt owned not only to the applicant financial creditor but to any other financial creditor of the corporate debtor.

Section 5(8) of Code defines “Financial Debt” means a debt along with interest, if any, which is disbursed against the consideration and include:-

- a) Money borrowed against payment of interest;
- b) Any amount raised by acceptance under any acceptance credit facility or its de-materialized equivalent.
- c) Any amount raised pursuant to any note purchase facility

- d) Issue of bonds, notes, debentures, loan stock or any similar Instruments;
- e) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other amounting standards as may be prescribed;

- f) receivables sold or discounted other than any receivables sold on non-recourse basis;
- g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only on the market value of such transaction shall be taken into account;

- h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution;
- i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clause (a) to (h) of this clause;

The following are some of the instances of Financial Debt:

**A)** The amount is admitted under an agreement - (Lease Agreement - Hewlett Packard India Ltd Vs. BPL Net Co Ltd 2002 (2) Comp LJ 271 (Karnataka). NCC Finance Ltd vs. TMT India Ltd 2000 (3) Comp LJ 230 (AP).

B) the amount is acknowledged under money receipt; Indian Oil Corpn Ltd Vs. NEPC India Ltd 2003 (114) Company Cases Madras.

C) Amount is admitted under bills of exchange, promissory notes, Tolani Shipping Co Ltd Vs. Saw Pipes Ltd 1999(97) Company Cases 394.

D) Inter-corporate deposits. Hi-Tech Gears Ltd v. Yogi Pharmacy Ltd 1998 (5) Comp LJ 400 All.

E) Failure to pay amount of redemption amount of debentures. Ranjana Kumar Vs. Indian Dyestuff Industries Ltd Vs. 2002 (46) CLA 151 (Bom).

## **Condition Precedent for Filing Petition :**

Though Code does not specifically says so but from the scheme of the Code, it is apparent that the petition under Section 7 and 8 of the Code shall not be maintainable if there is a slightest dispute or doubt about the payability of the amount claimed either by (i)Financial Creditor or by (ii)Operational Creditor.

The above provisions has been held in the case law **Annapurna Infrastructure Pvt. Ltd and Ors. Vs. Soril Infra Resources Ltd. MANU/NC/0190/2017** where the petition is rejected since the amount claimed was in dispute due to a counter claim.

**(A) Amount claimed should not be time-barred**

Indian Turpentine & Resin Co Ltd Vs. Pioneer  
Consolidated Co of India Ltd 1988 (64) Company  
Cases 169

**(B) The amount should not be in dispute:**

- I) Madhusudar Gordhandas & Co Vs. Madhu Woollen  
Industries (P) Ltd 1972 (42) Company Cases 125 : AIR  
1971 SC 2600.
- II) Sir Shadilal Enterprises Vs. Coop Co Ltd  
2001(103) Company Cases 863 (All).

## **(C) Claim for short delivery or non delivery**

Vineet Udyog Ltd Vs. Roayale Manor Hotel  
1999 (20) SCL 298 (Guj).

Section 5(6) of Code defines “Disputes” include a “Suit” or “Arbitration Proceedings” relating to :-

- i) Existence of the amount of debt;
- ii) The quality of goods or services; or
- iii) The breach of representation or warranty;

The above definition is clearly interpreted in the case laws-

1. Capital Partners vs. Reliance Defence and Engineering Ltd. MANU/NC/0451/2017
2. Macquarie Bank Limited vs. Uttam Galva Mettalics Limited MANU/NC/0460/2017
3. Himalay Dassani vs. Isolux Corsan India Engineering & Construction Pvt. Ltd. MANU/NC/0363/2017

“When the word "dispute" means pendency of suit or arbitration, then "dispute in existence" in section 8 means suit or arbitration proceedings pending since before the receipt of notice under section 8, on this logic, the receipt of notice of dispute under section 9 (5)(ii)(d) will obviously become a notice of dispute reflecting pendency of suit or arbitration proceedings in respect to the debt claim since before receipt of notice under section 8 of the code.”

Under Section 7 of Code, Financial Creditor shall make an application in Form No.6 along with the following documents:

- a)A record of default
- b)Evidence of default
- c)Other records
- d)Letters exchanged between the parties
- e)A Statement of Account showing the financial debt payment by the Corporate Debtor - preferably certified by CA or other practicing professional;

- f) Legal Notice sent by the Financial Creditor
- g) Reply, if any, received from the Corporate Debtor
- h) Board Resolution authorizing person who signed petition
- i) Evidence of Fees of Rs.25,000 – The DD in the name of The Pay & Accounts Officer, Ministry of Corporate Affairs;

j) Copy of Memorandum & Article of

Corporate Debtor;

k) Consent of Insolvency Resolution

Professional

l) Application for interim stay;

Legally speaking Section 7 does not postulate service of notice upon the Corporate Debtor. However, it is advisable for the financial creditor to serve a notice upon the corporate debtor setting out therein the

- (i) amount of loan or credit facilities availed provided
- (ii) how much amount has been repaid (iii) how much is the balance left (iv) accrued interest thereon
- (v) any other admissible amount (vi) aggregate amount payable by the corporate debtor;

## **SECTION-8 PETITION BY OPERATIONAL CREDITOR**

The Section 8(1) says if there is a default in payment of debt, the creditor shall have to give 10 days demand notice along with the copy of the invoice demanding the payment of invoice. It is mandatory that along with the notice, copies of invoice must be sent to the operational debtor otherwise notice shall be held defective and the petition is liable to be dismissed.

The above provision is stated in the case law- **Prem Swarup Narula vs. Bycell Telecommunications (I) Pvt. Ltd. MANU/NC/0330/2017** as “It is thus evident that in the absence of demand notice under Section 8 (1) of the Code, the petitioner could not have approached this Tribunal for initiation of insolvency resolution process against the respondent company. In the present case, there are many other defects pointed out by the learned counsel for the respondent. Therefore, we find that the present application is incomplete as the same is liable to be dismissed.”

The corporate debtor shall have to point out, within the period of 10 days, (a) existence of dispute and shall produce the evidence of any suit which is pending or any arbitration proceedings or alternatively, the corporate debtor may produce the proof of payment.

The Section 9 of the Code says that after the expiry of ten days and where the payment has not been received by the Operational Creditor, the operational creditor may file a petition before the NCLT. The petition shall be accompanied by the following documents:

- a)Invoice showing supply of goods/service
- b)Statement of Account
- c)Correspondence exchanged between the parties
- d)Consent of Insolvency Resolution Professional

- e) An Affidavit swearing that no notice was given by the corporate debtor relating to dispute
- f) Copy of 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. The NCLT has dismissed number of petitions where the certificate has not been enclosed from the banker about the non-receipt of payment in respect of which the petition has been filed; and

The above point has been held in the following case laws-

1. In Re: Smart Timing Steel Ltd. [LSI-1676-NCLAT-2017-(NDEL)] held that NCLAT holds that filing of certificate copy from Financial Institution maintaining Operational Creditor's accounts is mandatory and rejects the application for failing to furnish the same.
2. Achenbach Buschhutten GmbH & Co. KG vs. Acrotech Limited MANU/NC/0431/2017
3. In Re: Dr. Jain Video on Wheels Limited and Ors. MANU/NC/0431/2017

g)Board Resolution authorizing person who signed petition

h)Evidence of Fees of Rs.2,500 – The DD in the name of The Pay & Accounts Officer, Ministry of Corporate Affairs;

i)Copy of Memorandum & Article of Corporate Debtor;

j)Application for interim stay;

However, it is not mandatory to suggest the name of Insolvency Resolution Professional. If no name is given then Adjudicating Authority shall seek name of such IRP from the Board and then appoint such person as IRP. Therefore, it is recommended that whenever any Operational Creditor is filing a petition, he must always recommend the name of IRP in the petition itself so that IRP is their own person.

## **SECTION 7(4) - SCRUTINY OF DEBT**

The NCLT under Section 7(4) shall, within 14 days from the receipt of an application, ascertain the existence of default from the records of information utility or on the basis of other evidence furnished by the financial creditor.

## **SECTION 7(5) – ADMISSION OF PETITION BY NCLT**

Where NCLT is satisfied that default has occurred and application is complete in all respect and no disciplinary proceedings are pending against the proposed Interim Resolution Professional -

(a) Invariably the NCLT is also requiring a certificate from IRP saying that he is not attached or connected to the Petitioner Company. Therefore, a separate certificate may be obtained and annexed along with the petition.

But, where NCLT is satisfied that no default has occurred or application is incomplete or any disciplinary proceedings are pending against the resolution professional, it may, by order, reject the application. NCLT shall before rejecting application give notice to the applicant to rectify the default in his application within seven days of receipt of such notice from NCLT. It is mandatory on the part of the Petitioner Company to remove the defects within a period of seven days failing which, on many occasions, the Company Petition has been dismissed.

## **SECTION 10 - PETITION BY CORPORATE DEBTOR ITSELF.**

The Corporate Debtor of its own may also file a petition of for initiating corporate insolvency resolution process with the Adjudicating Authority as stated in section 10(1) of the Code:

“Where a corporate debtor has committed a default, a corporate applicant thereof may file an application for initiating corporate insolvency resolution process with the Adjudicating Authority.”

As stated in the case law:

**1. In Re: P&S Jewelers LSI-1697-NCLT-2017(MUM)**

NCLT Mumbai admits Corporate Applicant, P & S Jewelers, Corporate Debtor and Petitioner application u/s. 10 of the Insolvency and Bankruptcy Code, 2016 for initiating insolvency proceeding under the Code holding Petitioner was registered as sick industrial company with BIFR.

**2. In Re: LML Limited, MANU/NC/0501/2017**

**3. In Re: Dunn Foods Private Limited, MANU/NC/0385/2017**

**4. In Re: SRS Modern Sales Limited, MANU/NC/0256/2017**

**5. In Re: Sky Blue Papers (P.) Ltd., MANU/NC/0490/2017**

The petition was filed in the above cases by the corporate debtor as corporate applicant for the insolvency resolution process and was rightly admitted by the NCLT.

## **SECTION 13 - DECLARATION OF MORATORIUM**

Section 13 says that whenever any petition is filed either by (i) Financial Creditor; or (ii) Operational Creditor; or (iii) Corporate Debtor, the NCLT may, after admission of petition, shall declare a moratorium for the purpose of Section 14. In other words, it is mandatory for the NCLT to declare moratorium in terms of Section 14.

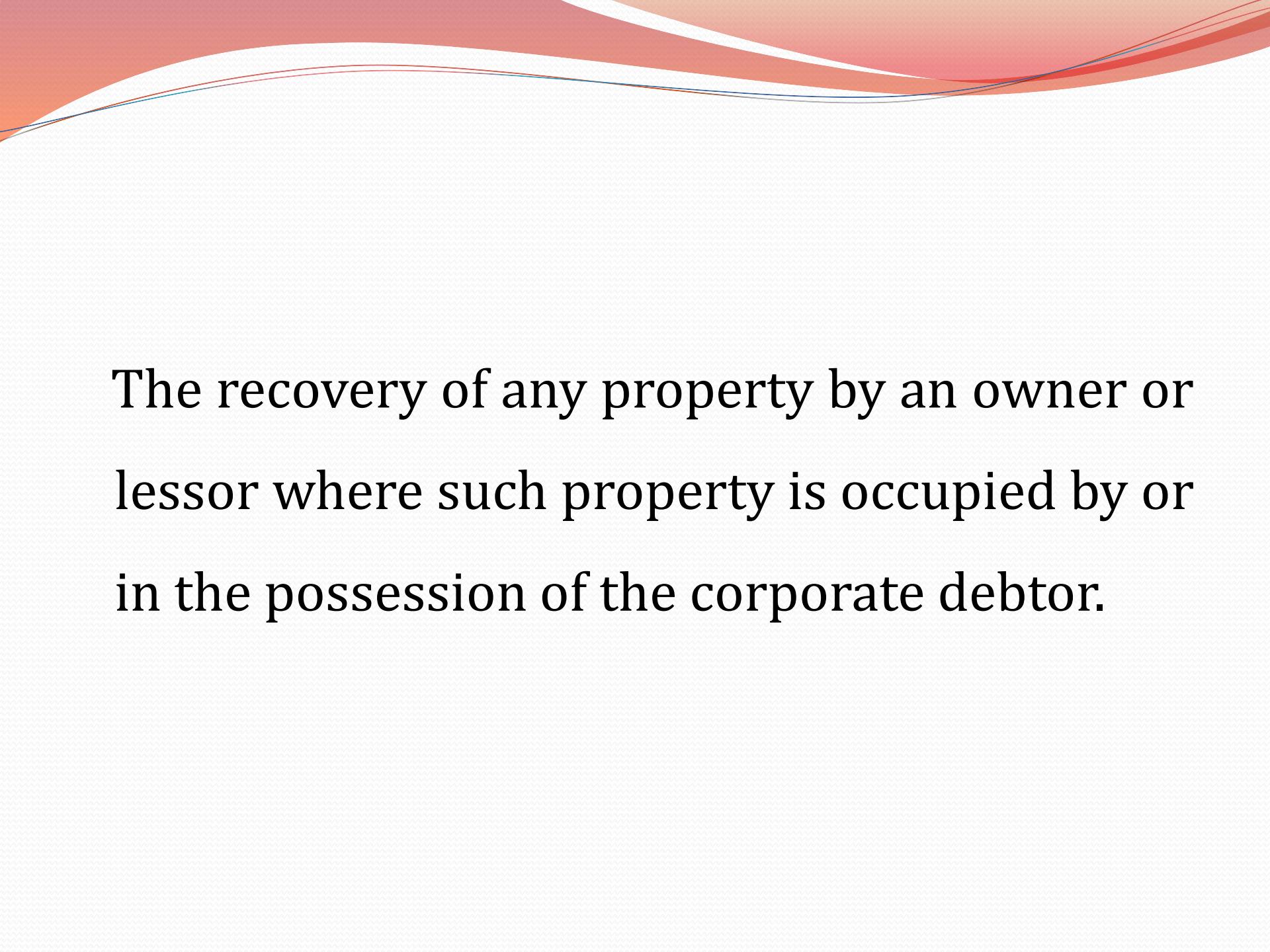
## **SECTION 14 - SCOPE OF MORATORIUM**

The NCLT under Section 14, shall prohibit all the following:

The institution of suits or continuation of pending suits or proceedings against the corporate debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;

Transferring, encumbering, alienating or disposing of by the corporate debtor any of its assets or any legal right or beneficial interest therein;

Any action to foreclose recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;



The recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

## **Power to Extend Time Limit**

The Section 12 of the Code has set default maximum time of 180 days for completing insolvency resolution process in normal case and 90 days in fast tracked insolvency resolution process under Section 56. The resolution professional if instructed by committee of creditors shall file application before NCLT for extension of time beyond 180 days, or 90 days, as the case may be.

The NCLT, on being satisfied that subject matter of the case is such that it cannot be completed within default maximum time, may, by order, grant one time extension beyond prescribed default maximum time. One time extension in case of normal process cannot exceed 90 days and in case of fast tracked process cannot exceed 45 days. The NCLT, in both cases, is empowered to grant extension of time only once.

## **Approval of Resolution Plan**

When the NCLT is satisfied that resolution plan approved by committee of creditors meets requirement of the Code, it shall, by order, approve the plan. An approved plan is binding on debtors and its employees, members, creditors, guarantors and other stakeholders in the resolution plan.

However, where the NCLT is satisfied that resolution plan does not meet requirement of the Code, it may, by order, reject the plan. On approval of resolution plan, the IRP is closed. When IRP is closed, the moratorium ceases to have effect, resolution professional is relieved of his duties and all documents related to IRP are consigned to the Board.

## **Power to Initiate Liquidation Process**

The NCLT has power to order liquidation if resolution plan has been rejected as it fails to meet the requirements of the Code; or maximum time allowed for resolution process has expired without any resolution plan being agreed upon; or during the IRP but before confirmation of resolution plan committee of creditors through resolution professional intimates adjudicating authority to about its decision to liquidate the corporate debtor; or when the corporate debtor, or any person connected with corporate debtor, contravenes the approved resolution plan.

Where IRP fails and liquidation proceedings have started the resolution professional continues to act as liquidators, but, new liquidator is appointed in case IRP has failed because it did not meet requirement of law or there is a complaint against resolution professional.

## **Dissolution Order**

When the business operations of the corporate person have been completely wound up and its assets have been completely liquidated, the liquidator shall make an application to the NCLT for dissolution of corporate person. On such application being filed, the NCLT shall order that corporate person shall be dissolved from the date of the order. The order of NCLT has effect of dissolving the corporate person from the date of order.

Order of dissolution is required to be forwarded within seven days (fourteen days in case of voluntary liquidation) from the date of order to the authority with which the corporate debtor (corporate in case of voluntary liquidation) is registered.

## Avoidance of Preferential Transactions

When liquidator or resolution professional, as the case be, is of the opinion that a corporate debtor during the period specified under the Code has transferred any property or an interest thereof of the debtor to specified persons on account of antecedent debt or liability in a manner putting specified person in a beneficial position than it would have been in the event of a distribution of assets in liquidation(**preferential transaction**), he shall apply to NCLT for avoidance of such transactions.

When an application for avoidance of preferential transaction is made, the NCLT may, *inter alia* by an order require that property transferred be vested in the corporate debtor; or release or discharge security interest created by the corporate debtor; or require payment by any person of sum in respect of benefit received by him from such transaction; or restore the position of guarantor whose debts were released or discharged; or direct providing security or charge on any property for discharge of any debt under order.

The period specified in respect of transactions with related parties is two years preceding the insolvency commencement date and one year preceding the insolvency commencement date in other transactions.

## **Avoidance of Undervalued Transactions**

When a corporate debtor, except in the course of ordinary business, makes a gift or transfers one or more assets for insignificant consideration (**the undervalued transaction**), the resolution professional or liquidator, as the case may be, shall, or failing them a creditor, member or partner of corporate debtor, as the case may be, may make an application to NCLT to declare such transaction void and reverse their effect.

The NCLT, on being satisfied about undervalued transaction and failure of the resolution professional or liquidator to file application, shall pass order (i) for restoring the position as it existed before transaction and reversing the effect thereof; and (ii) requiring the Board to initiate disciplinary proceedings against the resolution professional or the liquidator, as the case may be.

An order reversing effect may require any property transferred as part of the transactions, to be vested in the corporate debtor; or release or discharge any security interest granted by the corporate debtor; or require the payment of such consideration for the transaction as may be determined by the independent expert; or require beneficiary to pay such sum, to the liquidator or the resolution professional as the case may be, as the NCLT may direct.

# **Avoidance of Extortionate Credit Transactions**

The term extortionate transaction means a transaction wherein one party was made to pay unfairly high rate of interest or subjected to unfair credit term. The Code provides for avoidance of extortionate transactions related to financial or operational debt during the period within two years preceding insolvency commencement date. The application for avoidance of extortionate credit transaction may be made by the resolution professional or the liquidator, as the case may be, to the NCLT.

The NCLT on examining the application and being satisfied that terms of the credit transactions required exorbitant payment to be made by debtor, it shall, by order (i) restore the position as it existed before the transaction; (ii) set aside whole or part of debt created; (iii) modify terms of the transaction; (iv) require any person, who was party to transaction, to repay any amount received by such person; or (v) require to relinquish the security interest that was created as part of extortionate transaction.

## **Power in Case of Malicious and Fraudulent Proceedings**

The NCLT has been empowered under the Code to deal with cases of fraudulent and malicious initiation of proceedings to ensure proceedings are brought only for the purpose of resolution of insolvency, or liquidation, as the case may be and not for malicious or fraudulent purpose. Where any person initiates fraudulent or malicious liquidation proceeding or insolvency resolution process the NCLT may impose upon such person a penalty which may not be less than rupees one lakh, but which may extend to rupees one crore.

Also where any person initiates voluntary liquidation proceeding with intent to defraud any person, the NCLT may impose upon such person a penalty which may not be less than rupees one lakh, but which may extend to rupees one crore.

# **Power in Case of Fraudulent or Wrongful Trading**

When it is detected during the corporate insolvency resolution process or a liquidation process that the business of corporate debtor has been carried on with the intent to defraud creditors of corporate debtors or for any fraudulent purpose, the NCLT on an application may (i) pass an order that any persons who were party to such business transactions shall be liable to make such contribution to the assets of the corporate debtors as it may deem fit; (ii) by an order, under specified conditions, direct that a director or partner of corporate debtor, as the case may be, shall be liable to make such contribution to the assets of the corporate debtor as it may deem fit.



THANK YOU