Insolvency and Bankruptcy Code:
Analysis of a Selected Few Orders – Part II

October 4, 2017

Introduction

The introduction of the Insolvency and Bankruptcy Code, 2016 ("**Code**") overhauled the insolvency and liquidation processes in India and led to the creation of a new ecosystem for resolving distressed assets. The Code, once notified in its entirety will cover insolvency cases of individuals and partnership firms as well.

Given that these are still early days of implementation of the Code, the jurisprudence under the Code is still evolving and there is not much by way of judicial precedents to guide the Adjudicating Authority i.e. the National Company Law Tribunal ("**NCLT**"), the corporate debtors and the creditors alike.

This paper is the second in a series of papers analysing certain judgments passed under the Code. Our last paper, dated August 3, 2017, dealt with issues pertaining to the meaning of 'operational debt', grounds for refusal to admit an insolvency application etc.

This paper attempts to analyse certain recent decisions pertaining to the scope of discretion of the NCLT in admitting an insolvency application, applicability of the Limitation Act, 1963 ("**Limitation Act**") to proceedings under the Code, moratorium on proceedings against guarantors and the meaning of 'existence of a dispute' in connection with filing of an insolvency application by an operational creditor.

Discretion in admitting an insolvency application

Section 7 of the Code, which deals with the procedure for filing and admission of an insolvency application by a financial creditor, provides that where the NCLT is satisfied that a default has occurred, the application is complete, and there is no disciplinary proceeding pending against the proposed resolution professional, it *may* admit such application.

In contrast to this, sections 9 and 10 of the Code, which deal with the procedure for filing and admission of an insolvency application by an operational creditor and a corporate applicant respectively, provide that the NCLT *shall* admit an application if the specified requirements are met.

The relevant extracts of sections 7(5), 9(5) and 10(4) are reproduced hereinbelow for ease of reference:

> *"7(5) Where the Adjudicating Authority is satisfied that—*
> *(a) a default has occurred and the application under sub-section (2) is complete, and there is no disciplinary proceedings pending against the proposed resolution professional, it **may**, by order, admit such application; or*
> *(b) default has not occurred or the application under sub-section (2) is incomplete or any disciplinary proceeding is pending against the proposed*

*resolution professional, it **may**, by order, reject such application: […]*" (emphasis supplied)

"*9(5) The Adjudicating Authority **shall**, within fourteen days of the receipt of the application under sub-section (2), by an order—*

(i) admit the application and communicate such decision to the operational creditor and the corporate debtor if,—

(a) the application made under sub-section (2) is complete;

(b) there is no repayment of the unpaid operational debt;

(c) the invoice or notice for payment to the corporate debtor has been delivered by the operational creditor;

(d) no notice of dispute has been received by the operational creditor or there is no record of dispute in the information utility; and

(e) there is no disciplinary proceeding pending against any resolution professional proposed under sub-section (4), if any." (emphasis supplied)

"*10(4) The Adjudicating Authority **shall**, within a period of fourteen days of the receipt of the application, by an order—*

(a) admit the application, if it is complete; or

(b) reject the application, if it is incomplete: […]" (emphasis supplied)

On a plain reading of the aforesaid provisions, it may be argued that in case of an application by a financial creditor, the NCLT may exercise its discretion in admitting the application even when it is determined that a default has occurred and all the other conditions are fulfilled. However, where an operational creditor or a corporate applicant has filed an application, the NCLT has to mandatorily admit the application if all the specified requirements are met.

This issue came before the Ahmedabad Bench of the NCLT in the case of *State Bank of India* v. *Essar Steels Limited*[1], where an application for initiation of corporate insolvency resolution process against Essar Steels Limited ("**Essar**") was made by State Bank of India ("**SBI**") and Standard Chartered Bank ("**SCB**"). Essar was one of the twelve accounts identified by the Reserve Bank of India ("**RBI**") in its press release dated June 13, 2017 ("**Press Release**") for initiation of proceedings before the NCLT under the Code. Essar had challenged the constitutional validity of the Press Release before the Gujarat High Court[2], where the Gujarat High Court, *inter alia*, upheld the constitutional validity of the Press Release and held that the banks could proceed against Essar before the NCLT.

One of the contentions which was raised by SCB before the NCLT was that the expression 'may' used in section 7(5) should be read as 'shall' in the context of initiation of the insolvency resolution process. On the other hand, it was argued on behalf of Essar that the legislature has deliberately used the expression 'may' in section 7(5) in juxtaposition to sections 9(5) and 10(4) where the word 'shall' is used. It was further argued that the intention of the

[1] *State Bank of India* v. *Essar Steel Limited*, C.P. No. (I.B) 39/7/NCLT/AHM/2017, order dated August 2, 2017 by NCLT Ahmedabad.

[2] *Essar Steel India Limited* v. *Reserve Bank of India*, Special Civil Application No. 12434 Of 2017, order dated July 17, 2017 by the Gujarat High Court.

legislature is to give discretion to the NCLT when an application is filed by a financial creditor whereas in case the application is filed by an operational creditor or a corporate applicant, subject to fulfillment of other conditions, the NCLT must admit the application.

The NCLT observed that in order to give appropriate meaning to the words 'may' and 'shall', the intent of the legislation and the surrounding circumstances must be taken into account. The NCLT referred to the aforesaid judgment of the Gujarat High Court, where it was held that the admission of an insolvency application filed by a financial creditor is not a routine order and the NCLT has to apply its mind to all the factual details before passing the order.

The NCLT held that the order of admission of an application for initiation of corporate insolvency resolution process is a judicial order which should be in accordance with the provisions of the Code and principles of natural justice and should take into consideration the consequences of the order. Therefore, the NCLT has discretion in admitting or rejecting the application and this discretionary power has to be exercised in a judicious manner.

However, the Supreme Court ("**SC**") in *Innoventive Industries Ltd.* v. *ICICI Bank*[3] has observed that under section 7(5) all that needs to be shown is that a default has occurred and the moment the NCLT is satisfied that a default has occurred, the application of the financial creditor must be admitted unless it is incomplete.

The true scope of judicial discretion under sections 7, 9 and 10 would hinge on the interpretation of the expressions 'shall' and 'may'. In a catena of judgments on the interpretation of the words 'may' and 'shall', courts have interpreted the words 'may' as 'shall' in certain circumstances and 'shall' as 'may' in others.

In *Smt. Bachahan Devi* v. *Nagar Nigam, Gorakhpur*[4], the SC has held that mere use of word 'may' or 'shall' is not conclusive. In this regard, it may be pertinent to refer to the following observations of the SC:

> *"The question whether a particular provision of a statute is directory or mandatory cannot be resolved by laying down any general rule of universal application. Such controversy has to be decided by ascertaining the intention of the Legislature and not by looking at the language in which the provision is clothed. And for finding out the legislative intent, the Court must examine the scheme of the Act, purpose and object underlying the provision, consequences likely to ensue or inconvenience likely to result if the provision is read one way or the other and many more considerations relevant to the issue.*
>
> *[…]*
> *Obviously where the legislature uses two words may and shall in two different parts of the same provision prima facie it would appear that the legislature manifested its intent on to make one part directory and another mandatory. But that by itself is not*

[3] *Innoventive Industries Ltd.* v. *ICICI Bank*, Civil Appeal Nos. 8337-8338 of 2017, order dated August 30, 2017 by the Supreme Court.

[4] *Smt. Bachahan Devi* v. *Nagar Nigam, Gorakhpur*, AIR 2008 SC 1282.

> *decisive. The power of court to find out whether the provision is directory or mandatory remains unimpaired.*" (emphasis supplied)

In view of the aforesaid decision of the SC it may be argued that even though the word used in section 7 is 'may' as opposed to the word 'shall' in sections 9 and 10 of the Code, it is still open to interpretation whether these provisions are directory or mandatory.

At this juncture it is germane to refer to the Notes on Clauses annexed to the bill in respect of the Code ("**Bill**"). In the aforesaid notes, while discussing section 7 of the Code, it has been stated that once the Adjudicating Authority is satisfied as to the existence of the default and has ensured that the application is complete and no disciplinary proceedings are pending against the proposed resolution professional, the Adjudicating Authority *shall admit* the application. The Adjudicating Authority is not required to look into any other criteria for admission of the application.

Further, it may be pertinent to note the following observations of the Bankruptcy Law Reforms Committee[5]:

> *"When a firm (referred to as the corporate debtor in the draft law) defaults, the question arises about what is to be done. Many possibilities can be envisioned. One possibility is to take the firm into liquidation. Another possibility is to negotiate a debt restructuring, where the creditors accept a reduction of debt on an NPV basis, and hope that the negotiated value exceeds the liquidation value. Another possibility is to sell the firm as a going concern and use the proceeds to pay creditors. Many hybrid structures of these broad categories can be envisioned.*
>
> *The Committee believes that there is only one correct forum for evaluating such possibilities, and making a decision: a creditors committee, where all financial creditors have votes in proportion to the magnitude of debt that they hold. In the past, laws in India have brought arms of the government (legislature, executive or judiciary) into this question. This has been strictly avoided by the Committee. The appropriate disposition of a defaulting firm is a business decision, and only the creditors should make it.*
>
> […]
>
> *1. The law must explicitly state that the viability of the enterprise is a matter of business, and that matters of business can only be negotiated between creditors and debtor. While viability is assessed as a negotiation between creditors and debtor, the final decision has to be an agreement among creditors who are the financiers willing to bear the loss in the insolvency.*

[5] The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design, November 2015, p. 12 and 29.

2. *The legislature and the courts must control the process of resolution, but not be burdened to make business decisions*." (emphasis supplied)

In view of the above, it may be mentioned that the Notes on Clauses annexed to the Bill indicate that the intention of the legislature was that an insolvency application filed by a financial creditor must be admitted once the existence of the default is determined and the other requirements prescribed in the Code are met.

Further, as mentioned in the Report of the Bankruptcy Law Reforms Committee, once a default is determined, the evaluation of the mode and manner of resolution being a business decision should be made by the creditors.[6] Since the Code was enacted to address the shortcomings of the prior enactments on the subject, conferring an unguided discretionary power upon the NCLT may not be consistent with the objective sought to be achieved. Whilst the NCLT would need to satisfy itself of the occurrence of a default, once it is determined that a default has occurred the NCLT must admit the application. In order to satisfy itself of the occurrence of a default, the NCLT may take into consideration the entire facts and circumstances and be guided by the principles of natural justice[7].

Limitation

In *Neelkanth Township and Construction* v. *Urban Infrastructure Trustees Limited*[8], the National Company Law Appellate Tribunal ("**NCLAT**") dealt with the issue of applicability of the Limitation Act to the Code. In this case, the appellant (Neelkanth Township and Construction) had preferred an appeal against the order passed by the NCLT admitting an application for initiation of insolvency resolution process against the appellant under section 7 of the Code. The appellant, *inter alia*, contended that the claim of the respondent (financial creditor) was time barred as the debenture certificates issued to the Respondent were due for redemption in the years 2011, 2012, and 2013.

The NCLAT held that there is nothing on record to show that the Limitation Act is applicable to the Code. Further, it was observed that the Code is not an enactment for the recovery of money claims and that it relates to initiation of the insolvency resolution process. Accordingly, if there is any debt which includes interest and there is a default of such debt, the claim for such debt cannot be said to be barred by limitation. However, on an appeal against the aforesaid order of the NCLAT, the SC while dismissing the appeal observed that **the question of applicability of the Limitation Act to the Code is still open.**[9]

[6] The Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design, November 2015, p. 29.
[7] *Sree Metaliks Limited* v. *Union of India*, W.P. 7144 (W) OF 2017, order dated April 7, 2017 by the Calcutta High Court.
[8] *Neelkanth Township and Construction* v. *Urban Infrastructure Trustees Limited*, C.A. (AT) (Insolvency) No. 44 of 2017, order dated August 11, 2017 by the NCLAT.
[9] *Neelkanth Township and Construction* v. *Urban Infrastructure Trustees Limited*, Civil Appeal No. 10711 of 2017, order dated August 23, 2017 by the Supreme Court.

Contrary to this, the Principal Bench of the NCLT in three cases (*M/s. Deem Roll Tech Limited* v. *M/s. R.L. Steel & Energy Ltd.*[10], *Prowess International Private Limited* v. *Action Ispat and Power Private Limited*[11] and *Sanjay Bagrodia* v. *Sathyam Green Power Pvt. Ltd.*[12]) has held that the Limitation Act is applicable to proceedings under the Code.

In the *Deem Roll* case, the NCLT noted that section 255 of the Code provides that the Companies Act, 2013 ("**Companies Act**") will be amended in the manner specified in the Eleventh Schedule of the Code. Whilst the Eleventh Schedule specifies various amendments to be made to the Companies Act, section 433 is not sought to be amended. Section 433 of the Companies Act states:

> *"The provisions of the Limitation Act, 1963 (36 of 1963) shall, as far as may be, apply to proceedings or appeals before the Tribunal or the Appellate Tribunal, as the case may be."*

Accordingly, the NCLT held that since there is no specific bar on application of the Limitation Act to proceedings under the Code and given that section 433 makes the Limitation Act applicable to the NCLT, it would be applicable.

In the *Prowess International* case, the NCLT considered the definitions of 'debt' and 'default' under the Code and observed that a default occurs when a debt becomes *due and payable*. It was held that a debt which is not recoverable for any valid reason, including by reason of being barred by limitation, ceases to be an amount due and payable.

In the *Sanjay Bagrodia* case, the NCLT also referred to section 60(6) of the Code, which reads as follows:

> *"(6) Notwithstanding anything contained in the Limitation Act, 1963 or in any other law for the time being in force, in computing the period of limitation specified for any suit or application by or against a corporate debtor for which an order of moratorium has been made under this Part, the period during which* such moratorium is in place shall be excluded." (emphasis supplied)

The NCLT observed that the aforesaid provision shows that for computing the period of limitation specified for any suit or application by or against the corporate debtor, the moratorium period is to be excluded. It was held that from a plain reading of section 60(6) of the Code it is clear that a claim made before the NCLT must be within the period of limitation as prescribed by the Limitation Act.

It may be noted that in the Bill which was introduced in the Lok Sabha, section 60(6) was applicable only to any suit or application *in the name or on behalf of* a corporate debtor. One of the suggestions made was that section 60(6) should also apply in

[10] *M/s. Deem Roll Tech Limited* v. *M/s. R.L. Steel & Energy Ltd.*, C.A. No. (I.B.)24/(PB)/2017, order dated March 31, 2017 by NCLT Principal Bench.
[11] *Prowess International Private Limited* v. *Action Ispat and Power Private Limited*, C.A. No. (I.B)18(PB)/2017, order dated March 15, 2017 by NCLT Principal Bench

[12] *Sanjay Bagrodia* v. *Sathyam Green Power Pvt. Ltd.*, C.P. No. (IB)108(PB)/2017, order dated May 25, 2017 by NCLT Principal Bench.

respect of suits against the company by the creditors which are also subject to stay under the moratorium provisions. The Joint Committee to which the Bill was referred agreed to the aforesaid suggestion and recommended modifications to section 60(6) to that effect.[13]

However, it may be noted that section 179(3) of the Code (applicable to insolvency applications in respect of individuals and partnership firms) which is *pari materia* with section 60(6) of the Code, provides for exclusion of the moratorium period for computing the limitation period only in case of suits or applications *filed by* the debtor *and not against* the debtor (as is the case under section 60(6) of the Code). In view of the above, reliance solely on section 60(6) to assess the intention of the legislature on the applicability of the Limitation Act to the Code may not be a failsafe argument.

Having said that, we will now proceed to analyse various judicial precedents which have dealt with the issue of applicability of the Limitation Act to tribunals and quasi-judicial bodies. The SC, in a catena of decisions, has held that the Limitation Act is only applicable to suits, appeals and applications filed in a court and not to matters before a quasi-judicial body,[14] however, the application of the Limitation Act can be extended in cases where the relevant special statute provides for a specific provision extending the application of the Limitation Act to such quasi-judicial body[15].

In *Bharat Bank Ltd* v. *Employees of Bharat Bank Ltd.*[16] the SC discussed the distinction between a court and a quasi-judicial body. In this case, the SC referred to the following observations in the case of *Cooper* v. *Wilson*:

> *"A true judicial decision presupposes an existing dispute between two or more parties, and then involves four requisites :- (1) The presentation necessarily orally) of their case by the parties to the dispute; (2) if the dispute between them is a question of fact, the ascertainment of the fact by means of evidence adduced by the parties to the dispute and often with the assistance of argument by or on behalf of the parties on the evidence; (3) if the dispute between them is a question of law, the submission of legal argument by the parties, and (4) a decision which disposes of the whole matter by a finding upon the facts in dispute and application of the law of the land to the facts so found, including where required a ruling upon any disputed question of law. A quasi-judicial decision equally presupposes an existing dispute between two or more parties and involves (1) and (2), but does not necessarily involve (3) and never involves (4). The place of (4) is in fact taken by administrative action, the character of which is determined by the Minister's free choice."* (emphasis supplied)

[13] Report of the Joint Committee on the Insolvency and Bankruptcy Code, 2015, available at http://ibbi.gov.in/16_Joint_Committee_on_Insolvency_and_Bankruptcy_Code_2015_1.pdf, ¶ 29.

[14] *M.P. Steel Corporation* v. *Commissioner of Central Excise*, (2015) 7 SCC 58.

[15] *Sakuru* v. *Tanaji*, AIR 1985 SC 1279.

[16] *Bharat Bank Ltd* v. *Employees of Bharat Bank Ltd*, 1950 SCR 459.

The SC has on a number of occasions reiterated the view that though all courts are tribunals not all tribunals are courts. A tribunal may be categorised as a court if it has all the trappings of a court.[17]

Whilst in this paper we shall not be analysing whether the NCLT is a court or a quasi-judicial body, it would be pertinent to note that the NCLT while deciding the cases under the Code does determine contested questions of law and disposes of the cases after application of the law to the facts in question. However, we will now proceed to examine whether irrespective of the determination whether the NCLT is a court or a quasi-judicial body, the provisions of the Limitation Act would apply to proceedings before it under the Code.

In this context, we may refer to section 408 of the Companies Act which provides as follows:

> *"408. Constitution of National Company Law Tribunal.— The Central Government shall, by notification, constitute, with effect from such date as may be specified therein, a Tribunal to be known as the National Company Law Tribunal consisting of a President and such number of Judicial and Technical members, as the Central Government may deem necessary, to be appointed by it by notification, to exercise and discharge such powers and functions as are, or may be, conferred on it by or under this Act or any other law for the time being in force."*

Section 408 of the Companies Act, which deals with the constitution of the NCLT, clearly envisages exercise of powers and functions by the NCLT under laws other than the Companies Act. Further, section 433 of the Companies Act extends the application of the Limitation Act to all proceedings *before the NCLT*. Section 433 nowhere provides that the application of the Limitation Act is extended only to proceedings under the Companies Act before the NCLT.[18] On a combined reading of section 408 and section 433, it may be argued that the Limitation Act will apply to all proceedings before the NCLT not only where such proceedings are under the Companies Act but also proceedings under other laws where the NCLT is required to exercise/ discharge any powers/ functions.

It is to be noted that the NCLAT in *J.K. Jute Mills Company Limited* v. *Surendra Trading Company*[19] while dealing with the issue of whether the timelines mentioned in the Code for admitting or rejecting a petition or initiation of insolvency resolution process are mandatory or not, observed that under sections 7, 9 and 10 of the Code the 'Adjudicating Authority' is empowered to pass orders and not the NCLT. It is only by the virtue of section 5(1) that NCLT is the 'Adjudicating Authority' for the purposes of the Code. Thus, the NCLAT held that the mandate under section 420 (which deals with the orders) of the Companies Act cannot be transposed under the Code by reading 'Orders of Tribunal', as 'Orders of

[17] *S.D. Joshi* v. *High Court of Judicature at Bombay*, Writ Petition (Civil) No. 598 of 2008, order dated November 11, 2010 by the Supreme Court.

[18] *State Bank of India, Colombo* v. *Western Refrigeration Pvt. Ltd.*, C.P. (LB) No. 17/7/NCLT/AHM/2017, order dated May 26, 2017 by NCLT Ahmedabad.

[19] *J.K. Jute Mills Company Limited* v. *Surendra Trading Company*, C.A. (AT) No. 09 of 2017, order dated May 1, 2017 by the NCLAT.

Adjudicating Authority'. In this regard it may be mentioned that the argument with respect to the provisions of section 408 of the Companies Act, which stipulates that the NCLT is established to discharge such powers and functions as are or may be, conferred on it by or under the Companies Act or any other law for the time being in force, was not brought to the notice of the NCLAT and therefore, it may be argued that the judgment in the *J.K. Jute Mills* case on this issue would be *per incuriam*.

The intent of the legislature is also manifested in section 60(6) of the Code which provides that for calculating the limitation period specified for any suit or application by or against the corporate debtor, the moratorium period is to be excluded.

In light of the above discussion, in our view an insolvency application filed before the NCLT should be within the limitation period prescribed by the Limitation Act.

Moratorium for guarantors/ promoters

In *Schweitzer Systemtek* v. *Phoenix ARC Limited*[20], it was argued before the Mumbai bench of the NCLT that once a moratorium is declared on the admission of an insolvency application against a corporate debtor, there would be a prohibition on the taking over of possession of personal properties of the promoters mortgaged in favour of the lenders of the corporate debtor.

The NCLT held that the moratorium under section 14 of the Code prohibits any action to recover or enforce any security interest created by the corporate debtor in respect of *its* property. Accordingly, the personal properties of the promoters of the corporate debtor, which have been provided as security to the lenders, will not be subject to the moratorium.

This issue also came before the NCLT in the case of *Alpha & Omega Diagnostics (India) Ltd* v. *Asset Reconstruction of India & Ors.*[21], where the NCLT has taken the same view as in the *Schweitzer* case. This decision was challenged before the NCLAT[22], wherein the NCLAT decided not to interfere with the order of the NCLT while dismissing the appeal.

In the case of *Sanjeev Shriya* v. *State Bank of India*[23] this issue came up for discussion before the Allahabad High Court. The lenders had approached the Debt Recovery Tribunal ("**DRT**") under the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 ("**RDDBFI Act**") against Lohia Machines Limited ("**LML**"). Whilst the proceedings before the DRT were pending, LML approached the NCLT under section 10 of the Code for initiation of the insolvency resolution process. The NCLT admitted the application filed by LML and issued the moratorium order under section 14 of the Code. Pursuant to this, the DRT stayed the proceedings against LML but

[20] *Schweitzer Systemtek* v. *Phoenix ARC Limited,* T.C.P. No. 1059/I&BP/NCLT/MB/MAH/2017, order dated July 3, 2017 by NCLT, Mumbai.
[21] *Alpha & Omega Diagnostics (India) Ltd v. Asset Reconstruction of India & Ors.*, T.C.P. No. 1117/I&BP/NCLT/MB/MAH/2017, order dated July 10, 2017 by NCLT, Mumbai.
[22] *Alpha & Omega Diagnostics (India) Ltd.* v. *Asset Reconstruction Company of India Ltd. & Ors.,* Company Appeal(AT) (Insol) No. 116 of 2017, order dated July 31, 2017 by the NCLAT.
[23] *Sanjeev Shriya* v. *State Bank of India,* Writ C. No. 30285 of 2017, order dated September 6, 2017 by the Allahabad High Court.

continued the proceedings against the appellants since they were the personal guarantors for the loan provided by the lenders to LML. The appellants therefore approached the High Court to obtain a stay on the proceedings against the appellants before the DRT.

The High Court stayed the proceedings before the DRT against the guarantors. The High Court observed that the provisions of the Code prevail over the provisions of the RDDBFI Act and, therefore, once the application is admitted by the NCLT and an order of moratorium is passed under section 14 of the Code, the proceedings against the guarantors before the DRT have to be stayed. The High Court was of the view that proceedings against the guarantors cannot be continued unless the liability of LML as well as that of the guarantors is determined and crystalised. Accordingly, the proceedings before the DRT were stayed till the finalisation of the corporate insolvency resolution process or till the NCLT approves the resolution plan or passes an order for liquidation of the corporate debtor.

In this context the interpretation of section 14 of the Code becomes the moot point. It is a well-established principle of statutory interpretation that where the language of the provision is explicit, the language of the statute must prevail.[24] The other rules of interpretation must be resorted to only if the plain words of the statute are ambiguous or lead to no intelligible results or if read literally would nullify the very object of the statute.[25] The courts cannot legislate under the garb of interpretation[26].

In *Delhi Financial Corporation* v. *Rajiv Anand*[27] while dealing with the interpretation of section 32G of the State Financial Corporations Act, 1951("**SFC Act**"), the SC held that even assuming there is a defect or omission in the words used by the legislature, the courts cannot correct or make up the deficiency. The courts cannot add words to a statute or read words into it which are not there, especially when a literal reading thereof produces an intelligible result. In this case it was held that section 32G of the SFC Act would apply whenever any amount is due to a financial corporation irrespective of the fact whether the amount is due to a state financial corporation from an industrial concern or from a surety. The SC stipulated that it must be presumed that the legislature made no mistake when it chose to the omit the words 'from the industrial concern' in section 32G.

Reference may be made to the language of section 14 of the Code, whereby a moratorium is required to be declared by the NCLT prohibiting the following:

> *"(a) 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;*
> *[…]*
> *(c) 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*

[24] *Kailash Nath Agarwal* v. *Pradeshiya Industrial and Investment Corporation,* (2003) 4 SCC 305.
[25] *B. Premanand* v. *Mohan Koikal,* (2011) 1 SCC (LS) 676.
[26] *Jinia Keotin* v. *K.S. Manjhi,* 2003 (1) SCC 730.
[27] *Delhi Financial Corporation* v. *Rajiv Anand*, 2004 (11) SCC 625.

and Enforcement of Security Interest Act, 2002;" (emphasis supplied)

The language used in section 14 clearly demonstrates that the moratorium is on institution of suits/ proceedings *against the corporate debtor* and action to recover security interest created *by the corporate debtor*. There appears to be no ambiguity in the plain words used in section 14 which cover proceedings/ actions only against the corporate debtor.

In this regard, it may be noted that under section 22 of the Sick Industrial Companies (Special Provisions) Act, 1985 ("**SICA**"), it was specifically provided that there would be a moratorium on proceedings for enforcement of the guarantees in respect of any loans or advance granted to the industrial company, where an inquiry was pending or a rehabilitation scheme was under preparation.

Section 22 of SICA was amended in 1994 to specifically provide that no suit for recovery of money can be initiated against the guarantor in respect of the loans advanced to the industrial company. It may be mentioned that the Parliament, while drafting the Code, must be taken to be aware of the amendments made to SICA to specifically include a moratorium for guarantors. Therefore, the absence of any such provision in the Code, which specifically extends the moratorium to the guarantors, would indicate that the Parliament deliberately did not extend the moratorium to the guarantors.

On the contrary, section 60(3) of the Code provides that an insolvency resolution process or bankruptcy proceeding of a personal guarantor of the corporate debtor pending in any court or tribunal will stand transferred to the NCLT dealing with the insolvency resolution process or liquidation proceeding of such corporate debtor. This clearly envisages parallel proceedings being initiated and continued against the corporate debtor and the personal guarantor.

The object of the Code is to consolidate the laws relating to insolvency resolution and provide for a speedy and efficient resolution so as to maximize the value of the assets of the debtor. As long as the liabilities of the guarantors are not determined before the committee of creditors, initiating/ continuing parallel suit/ proceedings against the guarantors during the moratorium period may not be a constructive exercise. The institution of moratorium ensures that multiple proceedings are not taking place simultaneously and helps obviate the possibility of potentially conflicting outcomes in related proceedings which would otherwise frustrate the object of the insolvency resolution process, thus, ensuring that the resolution process is a collective one. Though the decision of the Allahabad High Court is in congruence with the spirit of the Code, however, on a strictly legal analysis it may *ipso facto* amount to judicial overreach given the precise and plain nature of the language used in section 14 of the Code. Judicial restraint should be exercised in reading words into a statute which may otherwise amount to judicial legislation. This anomaly can only be rectified by way of a suitable amendment to the Code to give effect to the spirit of the Code.

Dispute over a dispute

The interpretation of the term 'dispute' and the meaning of the expression 'existence of dispute' has been one of the most contentious issues under the Code. The NCLT has delivered various conflicting decisions while trying to define the contours of 'dispute'. In both *One Coat* Plaster v. *Ambience Private Limited*[28] and *Phillips India Limited* v. *Goodwill Hospital and Research Centre Limited*[29], the Principal Bench of the NCLT held that the definition of dispute under section 5(6) of the Code is not an exhaustive definition but an illustrative one. Thus, 'dispute' was given a broad and inclusive meaning. The reasoning of the NCLT in both the cases was that the use of the word 'includes' (in the definition of dispute), which immediately succeeds the word dispute enlarges the meaning of the term 'dispute' beyond the wordings of section 5(6).

In complete contrast to this, the term 'dispute' was given a very restrictive meaning in the *Essar Project India* v. *MCL Global Street Private Limited*[30], where the NCLT held that if the dispute raised by the corporate debtor was not raised before any court of law till the receipt of the demand notice from the operational creditor, then such dispute cannot be treated as a dispute in existence under the Code on the receipt of the demand notice. A similar view was taken in the case of *Deutsche Forfait* v. *Uttam Galva Steel*[31] where it was held that a dispute would exist under the Code if the issues are in dispute before a court or arbitral tribunal prior to the date of receipt of a demand notice and that merely contesting the amount in question did not constitute a 'dispute' within the meaning of the Code.

This issue has been finally settled by the SC in the case of *Mobilox Innovations Private Limited* v. *Kirusa Software Private Limited.*[32]

The SC traced the genesis of the Code to the UN Resolutions which elucidated the legislative guide on insolvency law. The legislative guide acts as a blueprint for member nations seeking to formulate insolvency laws for themselves. The SC also duly noticed the interim report of the Banking Law Reforms Committee which had discussed in detail the *Madhusudan Gordhandas* v. *Madhu Woollen Industries Pvt. Ltd*.[33] In this case it was had held that when a petition is presented for winding up under the Companies Act, 1956, on the grounds that the company is unable to pay is debts, the petition can only be dismissed if the debt is 'bona fide' disputed. A bona fide dispute is said to exist when the defense of the debtor is genuine, substantial and is likely to succeed on a point of law.

At this juncture it may be pertinent to refer to section 8(2)(a) of the Code which reads as follows:

[28] *One Coast Plaster* v. *Ambience Private Limited,* C.A. No. (I.B.) 07/PB/2017, order dated March 1, 2017 by NCLT Principal Bench.
[29] *Philips India Limited* v. *Goodwill Hospital and Research Centre Limited,* C.A. No. (I.B.) 03/PB/2017, order dated March 2, 2017 by NCLT Principal Bench.
[30] *Essar Projects India Limited* v. *MCL Global Street Private Limited,* C.P. No. 20/I & BP/NCLT/MAH/2017, order dated March 6, 2017 by NCLT Mumbai.
[31] *Deutsche Forfait* v. *Uttam Galva Steel*, C.P. No. 45/I&BP/NCLT/MAH/2017, order dated April 10, 2017 by NCLT Mumbai.
[32] *Mobilox Innovations Private Limited* v. *Kirusa Software Private Limited,* Civil Appeal No. 9405 of 2017, order dated September 21, 2017 by the Supreme Court.
[33] *Madhusudan Gordhandas* v. *Madhu Woollen Industries Pvt. Ltd.,* (1972) 2 SCR 201.

> *"(a) existence of a dispute, if any, and record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute;"* (emphasis supplied)

The SC then juxtaposed the provisions of the Bill and the Code. It observed that in the definition of dispute, the term used in the Bill was 'means' as opposed to 'includes' in the Code and the words 'bona fide' prefixing the phrase 'suit or arbitration proceedings' though present in the Bill were excluded in the Code. This indicates that the definition of dispute under section 5(6) is an inclusive one.

Further, it was observed that the Notes on Clauses annexed to the Bill only mention the requirement of the corporate debtor informing the operational creditor of the existence of the dispute in case of filing of an insolvency application by an operational creditor and there is no mention of the requirement to provide the record of pendency of the suit or arbitration proceeding. Thus, under the Code it is important that the dispute must be in existence before the receipt of the demand notice from the operational creditor.

The SC read the word 'and' in the aforesaid section as 'or'. The SC considered the fact that the use of 'and' gave rise to an anomalous situation which the legislature would not have intended since a dispute would then include only a pending suit or arbitration. Such an interpretation would even exclude a situation where a dispute arises amongst the parties a few days before the application is made to the NCLT and there is no time to approach either an arbitral tribunal or a court.

The SC further observed that the Code has made a distinction between operational debts and financial debts. One of objects of the Code qua the operational debts (such as trade debts, salary or wage claims) is to ensure that such debts which are usually smaller in sum than the financial debts do not result in premature initiation of insolvency resolution process against the corporate debtor. Further operational debts are usually recurring in nature and may not be accurately reflected in the records of the information utilities. It is for these reasons that the requirement of serving a demand notice and the threshold for establishing the existence of a dispute has been set out in the Code.

The SC thereafter determined the contours of the word 'dispute'. It analysed various decisions under insolvency laws by the courts of Australia and the United Kingdom to ascertain the role of adjudicating authority when adjudging the plea of a corporate debtor that a dispute under the Code exists.

It was observed that the notice of dispute to an operational creditor must bring to the notice of the operational creditor the 'existence' of a dispute or the fact that a suit or arbitration proceeding relating to the dispute is pending between the parties. The SC held that the NCLT needs to see that the corporate debtor is making a plausible contention which would require further investigation and that the dispute so brought to the notice is "not a patently feeble legal argument or an assertion of fact unsupported by evidence" and that at this stage the court need not go into the merits of the dispute or see if the defence is likely to succeed. All that the court should see is that for a dispute to exist the dispute must truly exist in fact and the grounds for alleging the existence of a dispute should be real and not spurious, hypothetical, illusory or misconceived.

The decision of the SC is a welcome step in bringing clarity to the meaning and scope of the expressions 'dispute' and 'existence of a dispute'. It will now be interesting to see how the NCLT applies the tests propounded by the SC to determine the existence of a dispute.

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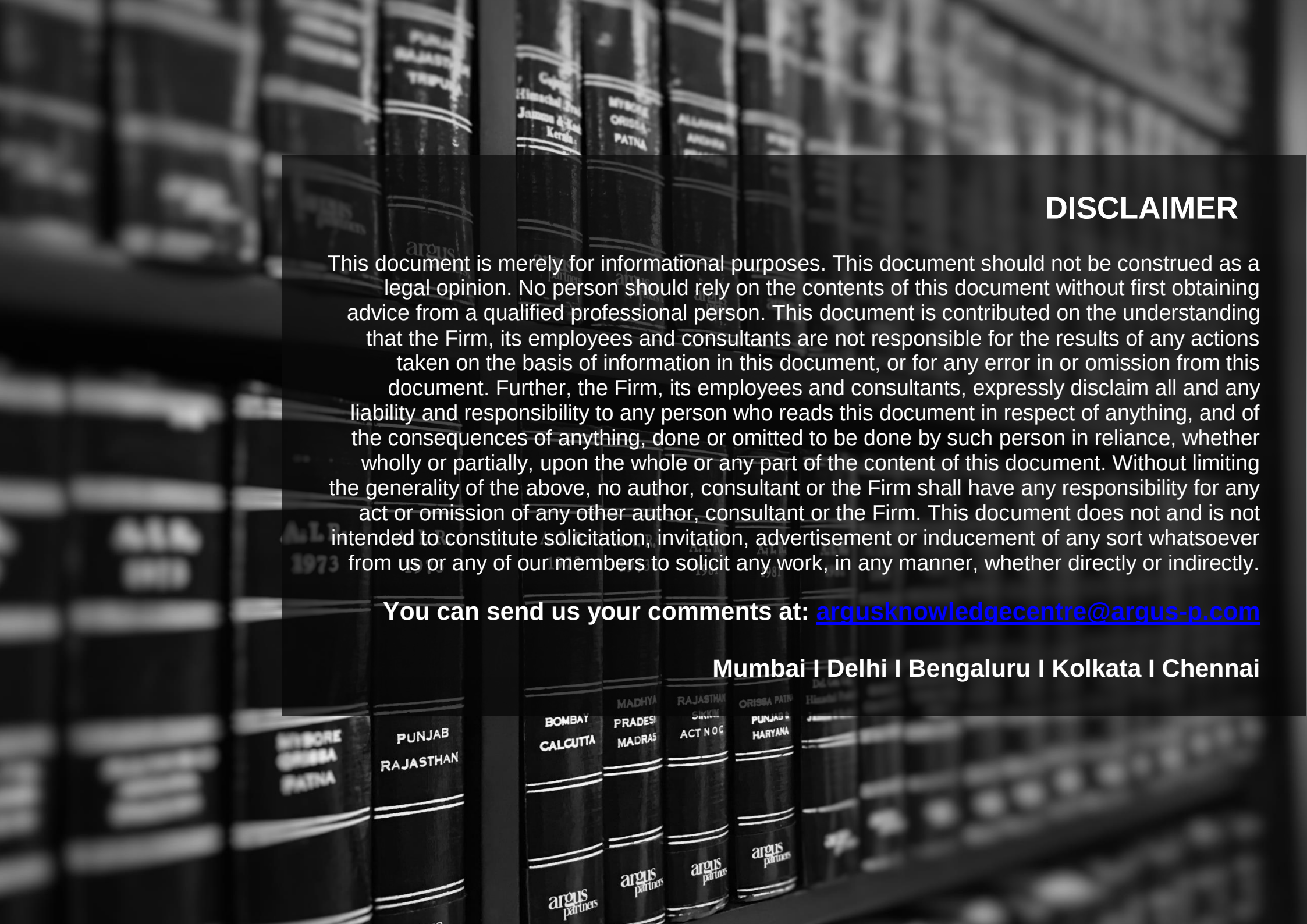

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