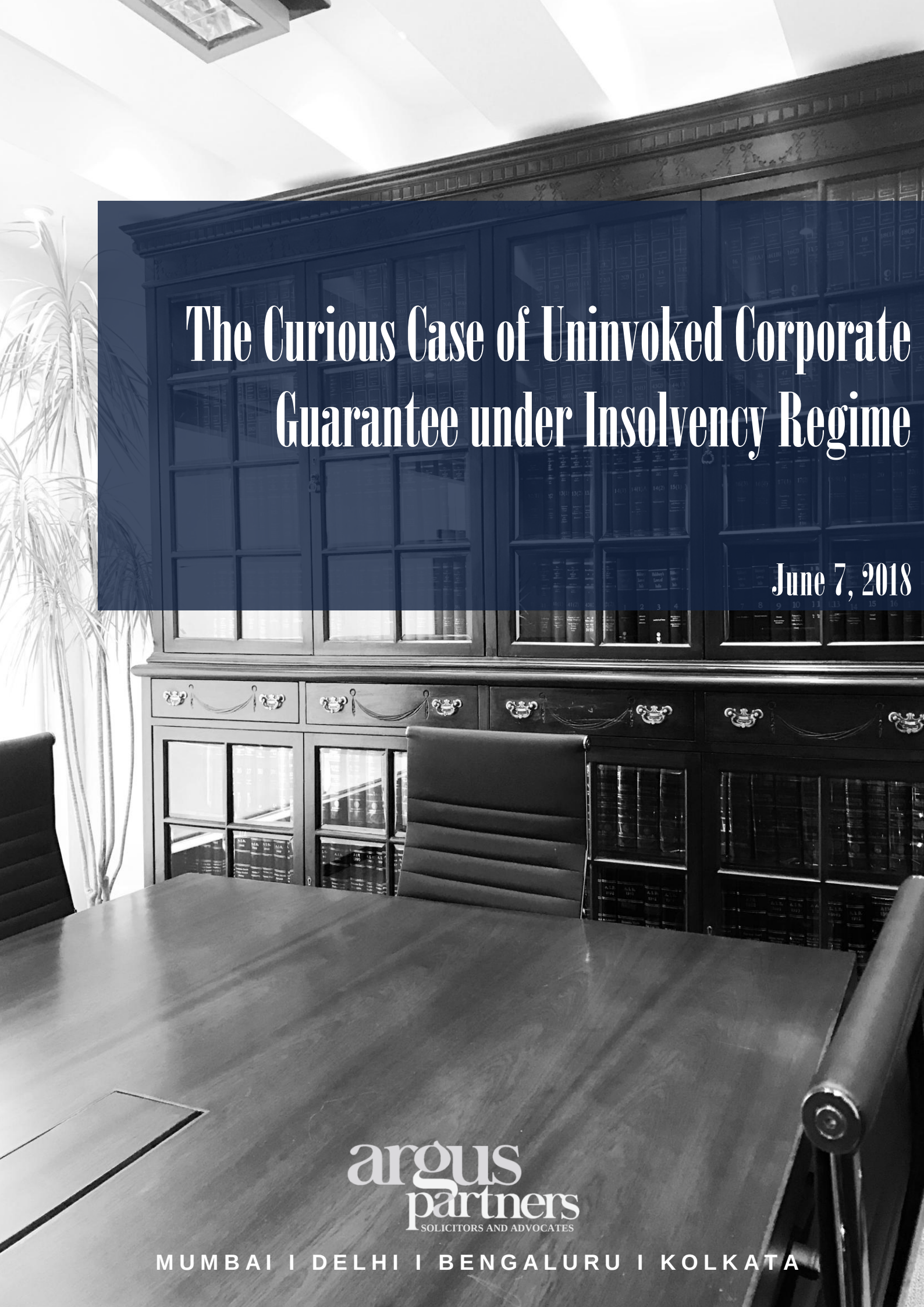

The Curious Case of Uninvoked Corporate Guarantee under Insolvency Regime

June 7, 2018

argus partners
SOLICITORS AND ADVOCATES

MUMBAI I DELHI I BENGALURU I KOLKATA

1. INTRODUCTION

1.1 Under the Insolvency and Bankruptcy Code, 2016 ('**the Code**'), upon admission of application for initiation of corporate insolvency resolution process ("**CIRP**") in relation to a corporate debtor, the interim resolution professional or the resolution professional is required to verify every claim, as on the insolvency commencement date, for the purpose of admission or rejection of any such claim. One of the issues, which has confounded the resolution professionals alike, is whether a claim is maintainable basis the corporate guarantee issued by the corporate debtor undergoing CIRP, which had not been invoked as on the insolvency commencement date. Whilst there have been few decisions rendered by different benches of the National Company Law Tribunal ('**NCLT**') on the aforesaid issue, it would be wrong to assume that the issue has been finally resolved, with different benches having expressed different opinions and National Company Law Tribunal ('**NCLAT**') having not conclusively addressed the issue.

1.2 The purpose of this paper is to critically analyse the issue of maintainability of a claim based on the status of a corporate guarantee remaining uninvoked as on the insolvency commencement date. During the course of its journey, the paper intends to review the decisions rendered by the different benches of NCLT on the issue, explore the rationale behind insolvency legislations and ascertain the extent of claim which may be admitted, in the event claim is maintainable basis such invoked corporate guarantee.

2. STORY SO FAR- DECISIONS OF NCLT

2.1 In one of the first decisions rendered on the issue, in the case of Axis Bank Limited v. Edu Smart Services Private Limited[1], the Principal Bench of NCLT dealt with the issue whether a creditor is entitled to make a claim by invoking a corporate guarantee given by a corporate debtor after the commencement of CIRP under the Code against such corporate debtor. The Bench referred to the provisions of regulation 13(1) of the Insolvency and Bankruptcy Board of India (Insolvency Resolutions Process for Corporate Persons) Regulations ("**CIRP Regulations**")[2] which provides that the Resolution Professional ("**RP**") is required to verify every claim as on the insolvency commencement date, i.e. the date of admission of the insolvency application by the NCLT and observed as follows:

> *"It is thus evident that in order to qualify as a 'debt' firstly provisions of the corporate guarantee must be satisfied by raising a demand which is expressed by invoking the corporate insolvency commencement date. In the present case, the CIRP commenced on 27.06.2017 and the corporate guarantee was admittedly invoked on 21.07.17, which is much after the insolvency commencement date. Therefore, we find that the Resolution Professional would not be in a position to verify the claim as it will not be reflected in the Books of Accounts which were supposed to be updated as on 27.06.2017. In the absence of any record to verify the claim, it will be impossible for Resolution Professional to accept any such claim which has become a debt after 27.06.2017." (emphasis supplied)*

[1] *Axis Bank Limited v. Edu Smart Services Private Limited, CP (IB)-102(PB)/2017*, order dated October 27, 2017 by NCLT Principal Bench

[2] **Regulation 13: Verification of Claims**: (1) The interim resolution professional or the resolution professional, *as the case may be, shall verify every claim, as on the insolvency commencement date*, within seven days from the last date of the receipt of the claims, and thereupon maintain a list of creditors containing names of creditors along with the amount claimed by them, the amount of their claims admitted and the security interest, if any, in respect of such claims, and update it

2.2 To substantiate its argument, the NCLT also referred to the definitions of 'claim'[3] and 'debt'[4] under the Code and observed as under:

> *"The emphasis appears to be on the expression 'payment and the debt, claim and the debt which is due from any person and includes financial debt and operational debt. Going by the aforesaid provisions, debt has not become due from the Corporate Debtor on the insolvency commencement date, i.e., 27.06.17. It became due only when the corporate guarantee was invoked by the Axis Bank Ltd.- the Corporate Debtor-applicant on 21.07.2017." (emphasis supplied)*

2.3 Finally, the NCLT made a reference to moratorium provisions contained in Section 14(1)(c) of the Code[5], and observed as follows:

> *"A perusal of the aforesaid provision makes it abundantly clear that there would be moratorium prohibiting any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property. It appears to us that invocation of corporate guarantee against the Corporate Debtor-respondent would result in enforcing security interest and it would thus be in violation of the moratorium provision of Section 14(1)(c) of the Code." (emphasis supplied)*

2.4 The aforesaid decision was relied upon by the NCLT Kolkata in Bank of Baroda v. Binani Cements Limited[6] and by the NCLT Allahabad in Export-Import Bank of India v. JEKPL Private Limited[7], for the proposition that, corporate guarantee which has not been invoked before the commencement of insolvency process, cannot be considered as debt if it was invoked after the commencement of insolvency process and "moratorium" was issued.

2.5 Notably, appeal against all the aforesaid three orders were preferred before NCLAT, and in all the three cases, NCLAT had directed the resolution professional to consider the claim of the claimant[8], with specific direction issued to the resolution professional of the Binani Cement, to reconsider the claim of the appellant uninfluenced by the order, if any, passed by the Adjudicating Authority, Principal Bench, New Delhi[9]. It may also be noted, as per the newspaper reports[10], the Mumbai bench of NCLT may have taken a view contrary to the aforesaid decisions, though a detailed reasoned order on the same is awaited.

---

[3] **3(6) "claim**" means—

(*a) a right to payment, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured or unsecured;*

(b) right to remedy for breach of contract under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured

[4] **3(11) "debt"** means *a liability or obligation in respect of a claim which is due from any person and includes a financial debt and operational debt;"*

[5] "**14(1)**(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 and Enforcement of Security Interest Act, 2002 (54 of 2002);"*

[6] *Bank of Baroda v. Binani Cements Limited, CP (IB) No. 359/KB/2017, order dated November 17, 2017 by NCLT Kolkata.*

[7] *Export-Import Bank of India v. JEKPL Private Limited, CA No. 159/2017, order dated November 27, 2017 by NCLT Allahabad.*

[8] See, *Axis Bank Ltd. v. Edu Smart Services Pvt Ltd* [Company Appeal (AT)(Ins) No.302 of 2017, order dated December 6, 2017] and *Export Import Bank of India v. Resolution Professional, JEKPL Pvt. Ltd*. [Company Appeal (AT) (Insolvency) No. 304 of 2017, order dated December 8, 2017]

[9] See, order dated December 18, 2017, rendered in the case of *IDBI Bank v. Vijaykumar V. Iyer* [Company Appeal (AT) (Insolvency) 313 of 2017]

[10] See, http://www.business-standard.com/article/companies/nclt-allows-new-claims-of-rs-8-bn-against-monnet-ispat-energy-118040400727_1.html (last accessed on June 6, 2018)

2.6 As is apparent from the aforesaid discussion, the issue is far from settled and would continue to elicit divergent opinions from the tribunal and the professionals alike. Before, however, we embark on our effort to analyse the decisions rendered in the aforesaid cases, it would be imperative to understand what an insolvency legislation, like the Code, intends to achieve and the relevance of a specific cut-off date for determination of liability.

3. INSOLVENCY LEGISLATION AND CUT-OFF DATE- OBJECTIVE AND SIGNIFICANCE

3.1 Way back in 1931, the Supreme Court of the United States in the matter of Maynard, Varney, Smith et al and Rutherford v Elliott[11] ("**Maynard**") had noted the purpose behind a bankruptcy proceeding as follows:

> *"Possible doubts as to the meaning of the section should be resolved in the light of the purpose of the Act 'to convert the assets of the bankrupt into cash for distribution among creditors, and then to relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.' Williams v. U.S. Fidelity Co., supra, page 554 of 236 U. S., 35 S. Ct. 289, 290; Central Trust Co. v. Chicago Auditorium, supra, page 591 of 240 U. S., 36 S. Ct. 412. (emphasis supplied)*

3.2 The aforesaid sentiment was echoed by Supreme Court in United Kingdom, in the case of In re Nortel GmbH (in administration)[12] where the following was observed:

> *"92. The Report of the Review Committee on Insolvency Law and Practice ("the Cork Report", 1982, Cmnd 8558), para 1289, described it as a "basic principle of the law of insolvency" that "every debt or liability capable of being expressed in money terms should be eligible for proof" so that "the insolvency administration" should deal comprehensively with, and in one way or another discharge, all such debts and liabilities".*

And, by Supreme Court of South Australia in the matter of Gray v Oz North Food & Liquor Wholesalers (NT) P/L[13] ("**Gray**") which observed as follows:

> *"18. The modern law of bankruptcy serves three purposes. The first is to ensure that the assets of the bankrupt are distributed rateably amongst creditors. The second is to ensure that one creditor does not obtain an undue advantage over others. The third is to bring about the discharge of the debtor from future liability for the debtor's existing debts so that the debtor may start afresh.[14]" (emphasis supplied)*

3.3 In so far as the relevance of specifying a specific date for determination of the claims admissible (in the context of CIRP, such date being the insolvency commencement date), the rationale was explained by Outer House of Scotland, in the case of Thomas M Burton, liquidator of The Ben Line Steamers Ltd[15], ("Thomas"), as follows:

---

[11] 283 U.S. 273(1931)

[12] *In re Nortel GmbH (in administration)* [2013] UKSC 52

[13] *Gray v Oz North Food & Liquor Wholesalers (NT) P/L* [2016] SA SC 165. Overruled subsequently in Oz North Food & Liquor Wholesalers (Nt) P/L v. Gray [2017] SASCFC 1, but basis the facts.

[14] *Storey v Lane* (1981) 147 CLR 549 at 556 – 557; *Re McMaster; ex parte McMaster* (1991) 33 FCR 70 at 72 – 73; *Australian Gypsum Industries Pty Ltd v Dalesun Holdings Pty Ltd* [2015] WASCA 95 at [211], (2015) 297 FLR 1 at 44.

[15] *Thomas M Burton, liquidator of The Ben Line Steamers Ltd* [2011 S.L.T. 535, order dated December 24, 2010]

> *"[21] …….. Winding up has been described as "a process of collective enforcement of debts for the benefit of the general body of creditors": Re Lines Bros Ltd, at [1983] 1 Ch., p.20 per Brightman LJ. The debts that may be enforced in that process are those outstanding as at the date of winding up. In the words of Selwyn LJ in Re Humber Ironworks and Shipbuilding Co, (1868–69) L.R. 4 Ch. App., at pp.646–647 : "I think the tree must lie as it falls; that it must be ascertained what are the debts as they exist at the date of the winding up, and that all dividends in the case of an insolvent estate must be declared in respect of the debts so ascertained." The debts so ascertained rank pari passu, subject obviously to the special statutory rights of preferential creditors; that is the fundamental principle of equality among creditors. The critical point is that any personal obligation of the insolvent company, if it is to be enforceable in the winding up process, must be in existence as at the date of winding up". (emphasis supplied)*

3.4 Reference may also be made to the following observation of the Chancery Court in the matter of Lomas v. Burlington Loan Management Ltd ("Lomas")[16]:

> *"202. It is a principle of insolvency law that the realisation of assets and the distribution of the proceeds among creditors are treated as notionally taking place simultaneously on the date of the commencement of the liquidation or administration: see MS Fashions Ltd v Bank of Credit and Commerce International SA at page 432G per Hoffmann LJ (sitting at first instance). In Re Dynamics Corporation of America [1976] 1 WLR 757, Oliver J said at page 774G-H:*
>
> > *"What the court is seeking to do in a winding up is to ascertain the liabilities of the company at a particular date and to distribute the available assets as at that date pro rata according to the amounts of those liabilities. In practice the process cannot be immediate, but notionally I think it is, and, as it seems to me, it has to be treated as if it were, although subsequent events can be taken into account in quantifying what the liabilities were at the relevant date. In the context of a liquidation, therefore, the relevant date for the ascertainment of the amount of liability is the notional date of discharge of that liability, and, despite what was said by Lord Wilberforce and Lord Cross by way of illustration, that date must, in my judgment, be the same for all creditors and it must be "the date of payment" for the purposes of any judgment which has been entered for the sterling equivalent at the date of payment of a sum expressed in foreign currency."*
>
> *203. At the same time, the courts apply the principle in order to give effect to the underlying purpose of a fair distribution between creditors pari passu and not as a rigid rule. It does not go so far as to entitle a person who was a creditor at the date of administration but had ceased to be so before the date of a dividend to participate in the dividend: see Wight v Eckhardt Marine GmbH at [29] per Lord Hoffmann." (emphasis supplied)*

3.5 Now that we have noted the objective behind insolvency legislations like the Code, and the rationale behind identification of a specific cut-off date for determination of the admissible claims, let us examine, if contingent claims, which have not crystallised as on the relevant cut-off date, is capable of being admitted.

---

[16] *Lomas v. Burlington Loan Management Ltd* [2015] EWHC 2269 (Ch) (31 July 2015).

4. ADMISSIBILITY OF CONTINGENT CLAIMS

4.1 A compelling argument was made by the United States Supreme Court in the Maynard[17] judgment for inclusion of contingent claims and liabilities, as follows:

> *"Although the omission of any reference to contingent claims in section 63 of the present act has led to some confusion and uncertainty in the decisions, it is now settled that claims founded upon contract, which at the time of the bankruptcy are fixed in amount or susceptible of liquidation, may be proved under subdivision (a)(4) of that section, 11 USCA § 103(a)(4), although not absolutely owing when the petition is filed. Williams v. U.S. Fidelity Co., 236 U.S. 549, 35 S. Ct. 289, 59 L. Ed. 713; Central Trust Co. v. Chicago Auditorium, MANU/USSC/0163/1916 : 240 U.S. 581, 36 S. Ct. 412, 60 L. Ed. 811, L. R. A. 1917B, 580. The sole question now presented is whether the liability of an endorser is of that class.*
>
> .....
>
> *"Possible doubts as to the meaning of the section should be resolved in the light of the purpose of the Act 'to convert the assets of the bankrupt into cash for distribution among creditors, and then to relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.' Williams v. U.S. Fidelity Co., supra, page 554 of 236 U. S., 35 S. Ct. 289, 290; Central Trust Co. v. Chicago Auditorium, supra, page 591 of 240 U. S., 36 S. Ct. 412. If this purpose be given its appropriate weight, a meaning cannot be attributed to the plain words of subdivision (a)(4), which would so restrict them as to preclude proof of claim upon the liability of an endorser of commercial paper, and result in its survival of the bankrupt's discharge as an obligation enforceable against him. That some contingent claims are deemed not provable does not militate against this conclusion. The contingency of the bankrupt's obligation may be such as to render any claim upon it incapable of proof. It may be one beyond the control of the creditor, and dependent upon an event so fortuitous as to make it uncertain whether liability will ever attach. In re Merrill & Baker (C. C. A.) 186 F. 312.*
>
> *Such a claim could not be proved under the Act of 1841 although in terms permitting proof of contingent claims. Riggin v. Magwire, 15 Wall. 549, 21 L. Ed. 232. Or, the contingency may be such as to make any valuation of the claim impossible, even though liability has attached. Of this latter class was the claim upon the bankrupt's contract to pay his divorced wife a specified amount annually so long as she should remain unmarried, proof of which was for that reason rejected in Dunbar v. Dunbar, supra; see Atkins v. Wilcox (C. C. A.) 105 F. 595, 53 L. R. A. 118.*
>
> *But the liability of an endorser is of neither class. Its amount is certain; and the contingency of notice of dishonor to the endorser is within the control of the creditor, so as to place his claim, so far as its certainty of accrual and its susceptibility of liquidation are concerned, upon the same footing as the contract of indemnity which was held provable in Williams v. U.S. Fidelity Co., supra, although the claimant had done nothing at the time of the bankruptcy to satisfy the liability for which the indemnity was given. See also Central Trust Co. v. Chicago Auditorium, supra, pages 593, 594 of 240 U. S., 36 S. Ct. 412.*

[17] *Maynard, Varney, Smith et al and Rutherford v Elliott* 283 U.S. 273(1931)

> *The claim against the endorser of paper not matured at the time of the bankruptcy thus stands on the same plane as contracts of suretyship or guarantee of payment of a debt not due until after the bankruptcy. See In re Lyons Bee Sug ar Refining Co., supra; Collier on Bankruptcy, supra; Remington on Bankruptcy, supra. Even though not due until after the year allowed for proof of claims, if proved in time, such a claim may be liquidated as are other unmatured claims. In re Buzzini, supra, page 830 of 183 F. As the claim is provable, and as notice of dishonor after the petition is filed is necessary only to charge the endorser, in the event he does not secure his discharge, the claimant need not give notice of dishonor in order to share in the estate. See Colman Co. v. Withoft, supra, page 253 of 195 F." (emphasis supplied)*

4.2 Keeping in mind the objective of insolvency legislation, the rationale behind inclusion of all potential claims was also noted by Supreme Court in United Kingdom, in the case of In re Nortel GmbH (in administration)[18], as follows:

> *93. The notion that all possible liabilities within reason should be provable helps achieve equal justice to all creditors and potential creditors in any insolvency, and, in bankruptcy proceedings, helps ensure that the former bankrupt can in due course start afresh. Indeed, that seems to have been the approach of the courts in the 19th century before the somewhat aberrant decisions referred to in para 88 above. Thus, in Ex p Llynvi Coal and Iron Co; In re Hide (1871) LR 7 Ch App 28, 32, James LJ described one of the main aims of the bankruptcy regime as to enable the bankrupt to be "a freed man – freed not only from debts, but from contracts, liabilities, engagements and contingencies of every kind". If that was true in 1871, it is all the more true following the passing of the 1986 and 2002 Acts, and as illustrated by the amendment to rule 13.12(2) effected following the decision in In re T & N Ltd [2006] 1 WLR 1728, so as to extend the rights of potential tort claimants to prove." (emphasis supplied)*

4.3 The rationale behind admissibility of contingent claims was also explained in the case of Thomas[19], as follows:

> *"[22] The obligations that are ranked in this way include future and contingent obligations. This principle was stated by LP Inglis in Mitchell v Scott, at (1881) 8 R., p.879 : "[F]uture and contingent creditors are just as much entitled to a ranking as present creditors, in a different way no doubt, and subject to different rules, but they are all entitled to claim in a sequestration. This does not depend on statute, but on the common law — on the fundamental rules of equity which underlie our whole system. If future creditors, i.e. , those whose date of payment have not yet come, and contingent creditors, i.e. , those whose debts are not yet payable and may never become payable, were not entitled to claim in the sequestration, their debts would be gone for ever, because the bankrupt's discharge would finally put an end to them. The statute therefore allows future and contingent creditors to claim just as much and no more than justice requires. Future debtors are allowed to rank subject only to a deduction of interest for the period between the date of sequestration and of the payment of their debt. In the case of contingent creditors, a sum is set apart to meet their claim, should the condition upon which it depends become purified."* (emphasis supplied).

[18] *In re Nortel GmbH (in administration)* [2013] UKSC 52

[19] *Thomas M Burton, liquidator of The Ben Line Steamers Ltd* [2011 S.L.T. 535, order dated December 24, 2010]

4.4 Specifically, in the context of contingent liability in the nature of guarantee liability, an exhaustive discussion can be found in the Gray[20] decision, where the following was noted:

> "*19. A convenient starting point for the consideration of whether the claim made against the appellant pursuant to the guarantee agreement is a liability that would have been provable in bankruptcy is the rule in Hardy v Fothergill.*[21] *The rule enunciated by Lord Halsbury was considered in Thiess Infraco (Swanston) Pty Ltd v Smith*[22] *where Finkelstein J said:*
>
> > *"Since 1869 it has never been doubted that if at the date of bankruptcy the bankrupt was bound by an executory contract the creditor could prove as a contingent creditor for any losses that he might suffer from a past or future breach of that contract. This accords with the evident purpose of bankruptcy which is to permit all creditors to share in the distribution of the assets of the bankrupt and to leave the debtor thereafter free from the liability of previous obligations. As Lord Halsbury observed in Hardy v Fothergill (1888) LR 13 AC 351, 355: "[T]he legislature has been engaged in the effort to exhaust every conceivable possibility of liability under which a bankrupt might be, to make it provable in bankruptcy against his estate and relieve the bankrupt for the future from any liability in respect thereof." It would be most unfortunate if persons entitled to the performance of executory agreements on the parts of bankrupts were excluded from participation from bankrupt estates and the bankrupts themselves as a necessary corollary were left still subject to action for non-performance in the future although without the property or credit often necessary to enable them to perform those obligations. The categories of claims which are admissible should be as wide as possible so that the financial affairs of the bankrupt are dealt with comprehensively "* (emphasis supplied)
>
> *20. In In Re Northern Counties of England Fire Insurance Co; Macfarlane's Claim*[23] *Sir George Jessel MR said:*[24]
>
> > "I should think the law in bankruptcy as to contingent liabilities was pretty plain, and that any liability contingent at the date of the adjudication which ripens into a debt during the bankruptcy is provable."
>
> ……..
>
> 28. For a debt to be provable there must be a legally enforceable obligation upon which the debt is founded, being an obligation incurred before the date of bankruptcy. The above authorities support the proposition that a post-bankruptcy demand made pursuant to a contract of guarantee, pre-existing the guarantor's bankruptcy, for payment of a debt incurred pursuant to the principal contract subsequent to the date of bankruptcy is a contingent debt or liability provable in the guarantor's bankruptcy. This would be a legally enforceable obligation incurred before the date of bankruptcy.

[20] *Gray v Oz North Food & Liquor Wholesalers (NT) P/L* [2016] SA SC 165. Overruled subsequently in Oz North Food & Liquor Wholesalers (Nt) P/L v. Gray [2017] SASCFC 1, but basis the facts.

[21] (1888) 13 AC 351.

[22] [2004] FCA 1155, (2004) 209 ALR 694.

[23] (1880) 17 Ch D 337.

[24] (1880) 17 Ch D 337 at 340.

> *29. In my view, this construction accords with both the text and purpose of s 82. Section 82 is a rehabilitative provision. It effects the third of the three purposes of the Bankruptcy Act. It is intended to give the debtor a fresh start. It should be given a wide, liberal construction consistent with the language of the section. That was the approach taken by the Full Federal Court in Official Trustee in Bankruptcy v C S & G J Handby Pty Ltd[25] where in a joint judgment Morling, Beaumont and Burchett JJ said:[26]*
>
> > *"Section 82(1) and its precursors have been generously construed. In Re Hide; Ex Parte Llynvi Coal and Iron Co; Re Hide James LJ said (of s 31 of the Bankruptcy Act 1869 (UK)):*
> >
> > > *"Every possible demand, every possible claim, every possible liability, except for personal torts, is to be the subject of proof in bankruptcy, and to be ascertained either by the Court itself or with the aid of a jury. The broad purview of this Act is, that the bankrupt is to be a freed man – freed not only from debts, but from contracts, liabilities, engagements, and contingencies of every kind. On the other hand, all the persons from whose claims, and from liability to whom he is so freed are to come in with the other creditors and share in the distribution of the assets."*
> > > (Emphasis supplied)

4.5 Finally, reference may be made to the UNCITRAL Legislative Guide to Insolvency Law[27], where the following was recommended:

> *"171. The insolvency law should specify that claims that may be submitted include all rights to payment that arise from acts or omissions of the debtor prior to commencement of the insolvency proceedings, whether mature or not, whether liquidated or unliquidated, whether fixed or contingent. The law should identify claims that will not be affected by the insolvency proceedings."* (emphasis supplied)

5. NCLT DECISIONS- A CRITIQUE

5.1 In the preceding paragraphs, we have reviewed the authorities supporting admissibility of contingent claims in an insolvency proceeding. Let us now review the provisions of the Code and CIRP Regulation to ascertain whether the provisions of the Code allow for admission of contingent liability.

5.2 As the issue pertains to admissibility of a claim, reference may be made to very definition of "claim" under section 3(6) of the Code, which includes claims which are unmatured or otherwise contingent and need not have crystallised into a "debt". The definition of claim as under the Code is reproduced hereunder –

> "3(6)" ***claim*** *" means –*
>
> > *"(a) a right to payment, whether or not such right is reduced to judgment, fixed, disputed, undisputed, legal, equitable, secured or unsecured;*

---

25 (1989) 21 FCR 19.

26 (1989) 21 FCR 19 at 24.

27 UNITED NATIONS PUBLICATION SALES NO. E.05.V.10 ISBN 92-1-133736-4, available at < https://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf > (last accessed on June 6, 2018)

(b) right to remedy for breach of contract under any law for the time being in force, if such breach gives rise to a right to payment, whether or not such right is reduced to judgment, fixed, matured, unmatured, disputed, undisputed, secured or unsecured;"

(emphasis supplied)

5.3 That even contingent claims are also capable of being admitted, is also evident from Regulation 14 of the CIRP Regulations, which itself provides for claims which are not "precise" and stipulate that the resolution professional is required to make best estimate of such a claim and can also revise such an estimate. Regulation 14 of the CIRP Regulation is reproduced hereunder –

"14. Determination of amount of claim.

(1) Where the amount claimed by a creditor is not precise due to any contingency or other reason, the interim resolution professional or the resolution professional, as the case may be, shall make the best estimate of the amount of the claim based on the information available with him.

(2) The interim resolution professional or resolution professional as the case may be, shall revise the amounts of claims admitted, including the estimates of claims made under sub-regulation (1), as soon as may be practicable, when he comes across additional information warranting such revision" (emphasis supplied)

5.4 From the above provisions it is clear that under the scheme of the Code and relevant regulations, a "claim" is not necessarily a fixed amount but rather is a right to payment which may be subject to estimation, revision and may become determinate at any point after filing the claim.

5.5 Now that, from our review of the provisions of the Code and CIRP Regulation, we do not see any restriction on the admissibility of a contingent claim, let us analyse the decisions of the Principal Bench in the Axis Bank Limited v. Edu Smart Services Private Limited[28].

5.6 As would be apparent from the excerpts of the decision extracted herein above, one of the primary grounds on which the admission of uninvoked corporate guarantee was rejected was premised on Section 14(1)(c) of the Code[29], which prohibited enforcement of any security interest created by the corporate debtor in respect of its property. It is submitted that, the same may be an erroneous application of law, as subsequent invoking of corporate guarantee cannot be considered as enforcement of security interest which is prohibited during the moratorium. At best, it is a notional invocation of claim for the purpose of ascertainment of value of the claim and in our view, is not different from a financial creditor submitting its claim basis a fund-based liability which has not been recalled or accelerated as on the date of insolvency commencement date, whether due to initiation of CIRP by an operational creditor or another financial lender.

5.7 In so far as the other ground relied upon by the Bench, citing the absence of any record to verify the claim in the Books of Accounts, we were not able to verify from the MCA website whether the factum of corporate guarantee was reflected in the annual report for the relevant

[28] *Axis Bank Limited v. Edu Smart Services Private Limited, CP (IB)-102(PB)/2017*, order dated October 27, 2017 by NCLT Principal Bench

[29] "**14(1)(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 and Enforcement of Security Interest Act, 2002 (54 of 2002);*"

period (presumably, because the CIRP was commenced before the finalization of the accounts), at least in the case of Binani Cements, the factum of corporate guarantee was specifically disclosed[30] and thus, could not have been rejected on the basis of absence of record.

5.8 In view of the aforesaid discussion, it may be argued that, even a corporate guarantee, which was not invoked as on the insolvency commencement date, being in the nature of contingent liability, would be capable of being admitted as a claim.

6. FINAL THOUGHTS

6.1 As has been noted, there seems to be divergence in views amongst the different benches of NCLT, with the majority view seeming to be a result of misapplication of the statutory provisions, in so far as they refuse to admit an uninvoked corporate guarantee as a claim (whether or not invoked subsequently), by failing to appreciate the object behind the Code as well as by overlooking the specific provisions of the Code. For the sake of certainty, we hope that the appellate authority may take a conclusive view and set the confusions to rest.

This thought paper has been prepared by Arka Majumdar, Partner.

[30] See, Note No. 33 of Standalone Financial Statements for The Year Ended 31st March, 2017, available at < http://www.binanicement.in/wp-content/uploads/Binani-Cement-Annual-Report-FY-2016-17.pdf> (last accessed on June 6, 2018)

DISCLAIMER

This document is merely for informational purposes. This document should not be construed as a legal opinion. No person should rely on the contents of this document without first obtaining advice from a qualified professional person. This document is contributed on the understanding that the Firm, its employees and consultants are not responsible for the results of any actions taken on the basis of information in this document, or for any error in or omission from this document. Further, the Firm, its employees and consultants, expressly disclaim all and any liability and responsibility to any person who reads this document in respect of anything, and of the consequences of anything, done or omitted to be done by such person in reliance, whether wholly or partially, upon the whole or any part of the content of this document. Without limiting the generality of the above, no author, consultant or the Firm shall have any responsibility for any act or omission of any other author, consultant or the Firm. This document does not and is not intended to constitute solicitation, invitation, advertisement or inducement of any sort whatsoever from us or any of our members to solicit any work, in any manner, whether directly or indirectly.

You can send us your comments at:

argusknowledgecentre@argus-p.com

www.argus-p.com

Mumbai I Delhi I Bengaluru I Kolkata